The European Union and Russia

Report with Evidence

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FOREWORD—What this Report is about

The relationship between the European Union and Russia has been going through a difficult phase with disputes over energy supplies, foreign policy issues, and tension between Russia and individual Member States. The change of presidency in Russia provides an opportunity to take stock and to consider whether this deterioration can and should be reversed. Russian politicians emphasise the importance of the relationship. This report discusses how the relationship might be developed in practice, while avoiding the unrealistic expectations which bedevilled European policy towards Russia in the early years after the end of the Cold War.

We look at recent history: the traumatic events which followed the collapse of the Soviet Union, which help to explain Russia’s present domestic, economic, and foreign policies. We examine Russia’s claim to be a “European” country, but argue that this is of less practical importance than the fact that Russia is Europe’s largest and closest neighbour, and that the two are tied by extensive and very substantial shared interests.

We then examine the institutional arrangements which both side have built up for managing the relationship, and the agreements through which they implement their cooperation. Negotiations to replace the most substantial, the Partnership and Cooperation Agreement, are expected to begin this year, and in this context the subject of democracy and human rights will be a challenge.

We also examine Russia’s still growing interest in a range of international multilateral agreements (G8, WTO, OECD). We conclude that it is in the European Union’s interest to sustain and strengthen these links.

Russia is Europe’s largest single supplier of gas and a major supplier of oil. Some European Union Member States are heavily or wholly dependent on Russian gas. We examine the obvious political, economic and commercial problems that arise. Russians whom we met made clear that they are unwilling to accept some of the legal and other constraints which are contained in existing documents, such as the Transit Protocol of the Energy Charter Treaty, which Russia is unlikely to ratify. We believe that the problems faced in this area by the European Union can be mitigated if the European Union adopts the right common policies.

The European Union and Russia come into contact with one another not only over bilateral matters, but also over issues involving third countries. The European Union’s European Neighbourhood Policy is intended to expand links with neighbouring countries that are not members, and encourage them to bring their economic and political systems more closely into line with those of the EU’s members. The Policy covers countries in Eastern Europe and the Caucasus which were formerly in the Soviet Union and with which Russia still has many close ties. These ties give the Russians no right of veto over those countries’ policies, or over their aspirations for a closer relationship with the European Union including—for example for Ukraine—eventual membership. We believe that potential frictions can be better managed if the Union consults with Russia over all aspects of the European Neighbourhood Policy.

The Common Foreign and Security Policy (CFSP) involves the European Union in discussion with the Russians on a number of international issues. Meanwhile
there has been substantial cooperation in areas, such as Iran, where there is an identifiable common interest; less so where this is not the case, such as Kosovo. The two sides work together usefully on the Middle East, terrorism, non-proliferation, and other issues. We believe that the European Union should continue and strengthen its efforts to reach common ground with the Russians on such international issues without, of course, compromising the interests of the European Union or its members.

Many people in Europe hold that the European Union has the right and the duty to speak out against abuses of democratic values in today’s Russia. Some Russian interlocutors found these interventions unacceptable, and questioned the moral basis on which they were made. Some Russians believe however, that outside support, judiciously expressed, does make a positive difference. Our own view is that although the European Union has no choice but to deal with Russia as it currently is, the issue of values is of fundamental importance. The European Union must therefore speak out from time to time if the Russian government falls short of the standards it has formally accepted in a number of international agreements.
The European Union and Russia

CHAPTER 1: INTRODUCTION

1. The European Union’s relationship with Russia is highly topical, as Russia embarks on a new phase of the post-Soviet era under a new President, Mr Dmitri Medvedev. The relationship is high on the agenda of the European Union (EU) and likely to remain there. In this report we look at developments in Russia and in the European Union and examine whether the present European strategy for relations with Russia including the mandate for the negotiations on a new Partnership and Cooperation Agreement (PCA) is appropriate and whether enough is being done to determine relevant strategies.

2. The enlargement of the EU to include countries which were formerly part of the Warsaw Pact and of the Soviet Union itself requires a careful review and reassessment of the EU’s overall interests and relationship with Russia. This is despite the fact that the division between “old” and “new” Europe was never clear cut, and it is fading as the “new” Member States find themselves involved in a shifting pattern of tactical alliances in order to promote their national interests in Brussels. Without such a review of the relationship with Russia, the EU will continue to find itself ill-prepared in its dealings with its most important neighbour.

3. The European Union defines its relationship with Russia as a “strategic partnership”, one of eight such partnerships, the others being with the United States, Canada, Japan, South Korea, China, Brazil and India. The European Commission’s current strategy towards Russia is set out in its Country Strategy Paper for 2007–2013, of March 20071 which describes the strategy as a “robust and coherent approach”. The paper states that:

“[T]he main interests of the EU in Russia lie in fostering the political and economic stability of the Federation, in maintaining a stable supply of energy; in further cooperation in the fields of justice and home affairs, the environment and nuclear safety in order to combat ‘soft’ security threats; and in stepping up cooperation with Russia in the southern Caucasus and the western [Newly Independent States] for the geopolitical stability of the [Commonwealth of Independent States] region, including for the resolution of frozen conflicts. EU cooperation with Russia is conceived in terms of, and is designed to strengthen, a strategic partnership. The EU places emphasis on the promotion of democracy, the rule of law and good governance in general, as well as respect for human rights and fundamental freedoms.”

4. The institutional framework for EU-Russia relations is based on the PCA, which entered into force in 1997 for a ten year period. The Agreement, which we discuss in Chapter 3, defines the main objectives of EU-Russia cooperation, establishes the institutional framework for bilateral contacts, and calls for activities and dialogue in a number of areas. It is a “mixed” agreement covering matters falling under both EU/EC competence and Member State competence. The relationship was extended with the adoption

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of a new basis for long-term cooperation in 2003, structured around four themes or “Common Spaces”: a Common Economic Space; a Common Space of Freedom, Security and Justice; a Common Space on External Security; and a Common Space on Research, Education and Culture. We discuss these in Chapter 4. The PCA has now reached the end of its term, but its provisions pending the negotiation of a successor continue to apply. These negotiations have been held up due to concerns among some EU Member States, notably Poland and Lithuania.

5. In evidence to the Committee, Sir Mark Lyall Grant, Political Director, Foreign and Commonwealth Office (FCO) set out the British Government’s assessment of the relations. He thought the EU/Russia relationship was important for their common strategic economic and political interests. Russia and the EU were dependent on each other in the energy field and Russia needed EU direct investment particularly in the technology of the hydrocarbon sector. He saw a strong coincidence of interests in financial and international matters: “The City of London has become the centre of choice for Russian business in terms of capital … [with] a record number of initial public offerings by Russian companies” in London. The EU and Russia also needed to co-operate on wider political issues “Iran … Kosovo, the Middle East, Sudan, climate change, the global challenges in … counter-terrorism, … non-proliferation … drug-trafficking and organised crime,” all of which were common challenges (Q 1).

6. The original strategy of the European Union towards Russia was based on the assumption that Russia and Europe share “common values”, and that building closer economic and political relations with Russia are both desirable and possible in the short term. We look at whether this assumption reflects the reality of Russia and the EU today. There is no doubt that in key areas the EU and Russia need to work together, for example on energy: Russia is a major source of oil and gas supplies for a number of EU countries. Security of supply is an issue of considerable importance in the context of the EU-Russia energy relationship. At the same time the Russian energy industry has benefited from the investment and expertise of European companies. In Chapter 5 we discuss energy issues including the Energy Charter Treaty and its Transit Protocol and the important issues of the ownership and control of energy production and transport, and particularly the question of gas pipelines.

7. The relationship between Russia and the European Union is, however, going through a bad-tempered phase. There are disputes over energy supplies, and over foreign policy issues. There are some bilateral disputes, such as that over the British Council, which the Russians are pursuing with a counterproductive mixture of intransigence and self-righteousness. The Russians resent criticism by the European Union and its Member States over what the latter see as the decline of democracy and the growth of authoritarianism in Russian politics. The formal arrangements which should govern the relationship—a renewed PCA and the Energy Charter Treaty, which we discuss in Chapter 5—are stalled, in part because the Russians consider that their provisions are one-sided.

8. The challenge for the European Union is to devise common policies which enable it to deal with Russia as an equal in the promotion of common interests, but also to act effectively when it comes to defending its own interests and those of its Member States. It is a central theme of our Report
that the European Union has the greatest influence and negotiating leverage when it has coherent policies that are supported by the EU institutions and the Member States and speaks with one voice. Both the EU and Russia have an interest in working closely together to tackle issues of common concern.

9. One of our witnesses, Katinka Barysch, of the Centre for European Reform, summed it up thus: “It is time the EU gave up pretending that the relationship is something that it is not. The EU’s governments and institutions need to start an honest and forward-looking debate about their Russia policy. This debate should involve at least three issues: a clear definition of what the different EU members want and need from Russia; a sober assessment of how much influence the EU has over its biggest neighbour; and contingency plans in case things in Russia turn out better or worse than policy planners [expect].”

10. The rest of this Report is divided into seven Chapters:

   In Chapter 2: Russia Today, we discuss the European character of Russia; and look at the present state of Russia’s domestic politics, its economy, and its foreign relations.

   In Chapter 3: The Institutional Framework for EU-Russia Relations, we analyse the institutional and legal framework for conducting the relationship.

   In Chapter 4: Building Cooperation through the Four Common Spaces, we take a closer look at the four main policy areas of EU-Russia relations.

   In Chapter 5: Energy, we deal with European dependence on energy supplies from Russia and the politics surrounding it, the prospects for the Energy Charter Treaty and its Transit Protocol, and the nature of future EU energy policy towards Russia.

   In Chapter 6: The Common Neighbourhood and International Issues, we examine foreign and security policy issues.

   In Chapter 7: Managing the EU’s Strategy towards Russia, we take a look at how the European Union manages its relations with Russia overall, including the question of whether the EU can influence Russian policy on democracy and human rights.

   In Chapter 8: Summary of Conclusions and Recommendations, we set out our overall conclusions and recommendations.

11. This Report was prepared by the European Union Sub-Committee C whose members are listed in Appendix 1. The list of those from whom we took evidence, to whom we are grateful, is listed in Appendix 2. We are also grateful to our Specialist Adviser, Sir Rodric Braithwaite, former British Ambassador to Russia. The Sub-Committee visited Russia and the record of our discussions is in Appendix 4.

12. We make this report to the House for debate.

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2 Centre for European Reform pamphlet Three Questions that Europe must ask about Russia, CER briefing note, 16 May 2007.
CHAPTER 2: RUSSIA TODAY

13. Russian domestic policy has taken an illiberal direction which is unwelcome in the West and its foreign policy is increasingly assertive and pugnacious. There is unlikely to be much improvement, at least until Russian politics has settled down following the installation of the new President.

Russia: a European Country?

14. Whether Russia is European or not is a question which has exercised Russians and Russia-watchers for centuries. President Putin insisted in his annual Address to the Nation in 2005 that Russia had played her part in the development of European values and that “the ideals of freedom, human rights, justice and democracy have for many centuries been our society’s determining values.” The Russian Ambassador in London emphasised to us that “Partnership with the EU and leading European nations has always been and continues to be a sine qua non, a necessary prerequisite for a successful foreign policy of Russia” (Ambassador Fedotov Q 413). Officials whom we met in Moscow echoed this line. Alexander Grushko, the Russian Deputy Foreign Minister, told us that Europe was “our house” and Russia was part of Europe. Europe, he said, was more than the EU. Russia was not planning to join the EU or NATO: Russia was too big and had to consider its relations with other neighbours such as China. Russia’s settled policy was nevertheless to build a general strategic partnership with Europe: everything, he thought, but membership.3 Mikhail Margelov, Chairman of the Foreign Affairs Committee of the Federation Council, Russia, reminded us that hundreds of thousands of Russians now live and work in Europe, and that the economies of Russia and the European Union are inextricably entwined.4

BOX 1

Russia Population Statistics

| The population of Russia is some 142 million. Most Russian citizens live in the part of Russia which is geographically Europe: only one fifth live in Russia’s Asian territory to the East of the Urals. People are drifting steadily from Siberia to European Russia. Most of the Federation’s citizens—some 80%—are ethnically Russian. Another 4% are other Slavs—Ukrainians or Belorussians. Practising Muslims are estimated to make up 10–15% of the population of the Russian Federation although some make the figures substantially lower. The largest single ethnic group among these are the Tatars, who have their own region within the Federation, and make up 3.8% of the total population.5 |

15. The aspirations of the current EU strategy outlined in paragraph 3 above are laudable. They beg a central and much debated question: Is Russia a European country, whose political and economic systems, like those of the new Central European members, can be harmonised with those of its

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3 Meeting, Mr Alexander Grushko, Moscow, 12 December 2007, see Appendix 4
4 Meeting, Mr Mikhail Margelov, Moscow, 12 December 2007, see Appendix 4
5 The Foreign and Commonwealth Office figures are: 81.5% Russians, Tatars 3.8%, Ukrainians 3% (more than 100 nationalities in all). Source: FCO website at www.fco.gov.uk.
neighbours to the West through its own efforts and those of the European Union; or is it special, a country which will retain its own unchanging attitudes and values despite the similarities of its history and culture?

16. This paradox lies at the heart of the frustration and confusion which surrounds European policy towards Russia today. In the 1990s the EU failed to appreciate that Russia’s transition to the “European values” of democracy, the rule of law, good governance, and respect for human rights and fundamental freedoms—which she accepted in joining the Council of Europe and the OSCE⁶—would take generations, not decades. Faced with a more assertive and increasingly prosperous Russia, which is not willing to be patronised and expects to be treated as an equal, the EU’s more ambitious early aspirations look less easily attainable and European policy is in some disarray as a result.

17. Many of the Russians to whom we spoke took a very categorical line: Russia is inescapably a part of Europe by history, religion, and culture.⁷ Russia adopted Christianity before many of its European neighbours and the Russian contribution is an integral part of modern European culture. Ambassador Fedotov told us in London “Russia is Europe, from any possible point of view, be it geography, history, culture, economy, politics, ideologies … philosophy, human values, relationships, family ties, et cetera. Secondly, Europe without Russia is not Europe in all its inclusiveness, so any dream of creating a pan-European cooperation without Russia is a myth” (Q 412).

18. Ties at the level of the general population are also close. According to one source, there are now up to ten million people who speak Russian as their first language living inside Russia’s EU neighbours. Russia lies sixth among the European countries in terms of the number of its citizens who travel to other European countries, and the number is increasing.⁸

19. Some western observers argue that Russian attitudes to a whole range of issues in the field of civil society, human rights and the rule of law, show that Russia is not attached to “European” values. It is true that these values do not have secure roots in the Russian past, nor are they fully reflected in the present. Russia’s political regime has historically always been of an autocratic nature. However, the history of the European continent in the twentieth century shows that “European values” have proved fragile even in European countries where they seemed most deeply rooted.

20. Some, both inside and outside Russia, argue that Russia is not Europe but Asia, or “Eurasia”. Russia’s interests are in part defined by its Asian territories where lie many of its richest mineral deposits. Its southern frontier is the longest in the world, and borders on some of the world’s most unstable regions. Russia’s relationship with the great Asian powers, China, Japan, and India, and with other neighbours such as Iran and Korea, inevitably

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⁶ The commitments that Russia has entered into are set out in the Helsinki Final Act and the Charter of Paris for the OSCE and the Statute of the Council of Europe, as well as in a number of Conventions and secondary texts, including in particular the European Convention on Human Rights (ECHR).

⁷ For example Ambassador Likhachev, Meeting, Moscow, 12 December 2007, see Appendix 4.

⁸ Interview, Vyacheslav Nikonov (President of the Politika Foundation, Moscow) London, 14 January 2008. The figures for Russian speakers living in the EU are very approximate. Many of these are not ethnic Russians, but Ukrainians and other Russian speakers from the former Soviet Union. Four million Russian speakers are said to live in Germany, many of them ethnic Germans from Central Asia. The figures for tourism come from European Tourism Insights 2006, published by the European Travel Commission, www.etc-corporate.org/resources/uploads/ETI_2006_new_final_version.pdf.
distinguishes its foreign policy from its western neighbours. From the time of the Tartar yoke in the thirteenth century, Asian culture and history have had a powerful influence on the growth of the Russian state.

21. Recent figures seem to show that the Russians are far more pro-European than they were in 1998–9 at the time of Russia’s economic collapse and the Kosovo war. Other figures paint a different picture.\(^9\) Given the roller-coaster of the past two decades, it is perhaps not surprising that Russian opinion should be uncertain.

These considerations affect attitudes, and therefore policy-making, on both sides.

22. **Russia is a country of substantially European history and culture whose government and many of whose political elite regard it as a European country.** However, most Russians do not think in these terms because they regard themselves as Russians, first and foremost. Russia shares a border with the European Union, with which it is bound by numerous ties of practical interest. Consequently, the EU and Russia have a mutual interest in building a close relationship, and the need for a practical cooperation with Russia in areas such as border controls is greater than with, say, India or China.

23. **The EU should resist any attempts to isolate Russia, which would not be in the interests of the EU, but should rather pursue a policy of engagement at all levels and in all policy areas.** In practice what matters are the concrete measures for developing that cooperation between Russia and the European Union which both know is necessary. The EU should recognise that the illusions entertained in the 1990s about the speed of Russia’s transition to democracy have hampered the EU’s efforts to deal with a newly assertive Russia. The current difficulties in the relationship should not weaken the EU’s determination to build a long-term partnership with Russia, based on dialogue, trust and common interests.

### Recent Russian History

**The collapse of the Soviet Union**

24. The attitudes of Russians today to their domestic politics and to international affairs are profoundly affected by what has happened to their country in the last two decades.

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\(^9\) Figures from the Levada Center, an agency that carries out public opinion and market research, website: [http://www.levada.ru/interrelations3.html](http://www.levada.ru/interrelations3.html). One poll conducted by the Levada Center for the EU-Russia Centre in February 2007 shows that 71% of the Russian respondents did not consider themselves Europeans. Nearly half thought the European Union was a threat to Russia and its financial and industrial independence. One third perceived Europe as a neighbour and partner, though only 15% thought the perception was reciprocated by the Europeans. Nearly half thought that Russia could learn from European culture and democracy, but a third thought that European democracy did not suit Russia. (See “The Russians’ perception of European Values”, EU-Russia Centre study entitled: “Voices from Russia: Society, Democracy and Europe”, 15 February 2007, website: [http://www.levada.ru/press/2007021501.html](http://www.levada.ru/press/2007021501.html)). A study by Aberdeen University (based on polls conducted in 2005) says that, by a majority of more than two to one, Russians see the country’s future linked with other CIS states rather than with Western Europe. R Rose and N Munro (Centre for the Study of Public Policy, University of Aberdeen), *Do Russians see their future in Europe or the CIS?* Europe-Asia Studies, 60, 1, 49–66, 2008.
25. For nearly 40 years the Soviet Union was one of the two superpowers. The Soviet Union was victorious in the Second World War. Soviet scientists were at the forefront of knowledge. A Soviet citizen was the first man in space. The Soviet Union was feared and respected throughout the world, uniquely able to meet America as a military equal. These glittering successes masked poverty, an economic system incapable of modernising or sustaining itself, a political system that stifled initiative and, towards the end, a growing weariness with the burdens of empire.

26. In 1991, in a reversal without precedent in history, the Soviet people lost their political and economic systems, their cradle-to-grave welfare system, their empire, their ideology, and their position in the world without significant bloodshed and in a matter of months. The command economy was replaced, on the advice of Western advisers, by a market economy which was unsuited to Russia’s immediate needs and which resulted in poverty, hunger and chaos. Vladimir Mau, Director of the Working Centre for Economic Reforms of the Russian Government described it to us as a turbulent time. The oligarchs profited from the sell-off of the nation’s wealth. The West provided food aid, and lectured the Russians on the virtues of democracy and they were expected to be grateful. The Chairman of the Foreign Affairs Committee of the Federation Council, Mikhail Margelov, described the time following 1991 as one of humiliation.

27. For Russians of all classes the 1990s were a time of national and personal humiliation. For many of them, it was also a time of deep poverty. However unfairly, many Russians attribute their troubles to the attempt to impose on them a system which they now consider as unsuited to Russian conditions. They put the blame not only on the Russian politicians of the 1990s and their Western supporters, but on Western ideas of democracy.

The Putin era: stability, restrictions on freedom

28. In 2000 the new President, Vladimir Putin, promised stability and prosperity. He also promised democracy and the rule of law—when Russia was ready for it. He brought order out of political chaos, although at the cost of the second war in Chechnya, and presided over eight years of rapid economic growth, considerably helped by rising oil prices, and prosperity which is trickling downward even in the provinces. He curbed the oligarchs though in legally questionable ways. He partially restored Russia’s perception of its position in the world while not pursuing the interventionist policies of the Soviet Union in Africa, Latin America and south-east Asia.

29. Much of this has been achieved at the expense of clipping back the fragile shoots of democracy. This is seen in the curbed press, the weak parliament, the arbitrary courts, the corruption, the murders of journalists and political

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10 Meeting, Mr Vladimir Mau, Moscow, 12 December 2007, see Appendix 4.
11 Meeting, Mr Mikhail Margelov, Moscow, 12 December 2007, see Appendix 4.
12 Professor Phil Hanson, Centre for Russia and East European Studies at Birmingham University described two measures associated with the World Bank: the Ease of doing Business ranking, where Russia looked poor on an international perspective on a range of different indicators, including corruption; and the Business Environment and Enterprise Performance Survey (in association with the EBRD) which showed an increase in corruption between 2002 and 2005. This survey asked businesses what their experience was of paying bribes. Professor Hanson thought bribe frequency had gone up in the period when there had been an increase in state control. He saw this as an unpromising situation (Q 50).
activists, the intrigues which surround politics from the Kremlin downwards, the ubiquitous secret policemen, now often deeply involved in the more lucrative parts of the economy. Regional government has been recentralised: regional governors are no longer elected but are appointed directly by the Kremlin. Mr Jim Murphy, MP, Europe Minister, told us that “the democratic space in Russia continues to contract” (Q 394).

30. Katinka Barysch of the Centre for European Reform (CER) thought that Russia was not particularly democratic: “the striking thing about Putinism for me is that [President Putin] always insists on leaving the full institutions of democracy in place. He hollows them out but he has not touched the formal system of checks and balances” (Q 101). Referring to the recent Russian elections, she added: “I would be somewhat reluctant to call it an election, it is a changeover or handover of power” (Q 133). Following the Russian parliamentary elections of December 2007, the Duma would probably remain a “rubber-stamp parliament” (Q 134).

31. For Sir Roderic Lyne, formerly British Ambassador to Russia: “The general attitude to democracy in Russia is that democracy equals the 1990s, equals a complete nightmare, and if that is what you are offering the Russian population, they do not want that. They would like to have more law and order. They would like to have much less corruption. Corruption is very high on the list of complaints of the Russian populace, but they are much more comfortable with Putin and the sort of rule he has given them than with what happened in 1990s, and anyway they think that those leading democratic figures were all tainted and a lot of them were allied with big business and oligarchs. I think there is a very important distinction to be made between freedom and democracy. Essentially what Gorbachev and Yeltsin gave Russia was freedom. Although Gorbachev did institute what has probably been the fairest election in terms of voting that Russia has had in the 1989 elections to the Congress of People’s Deputies, democracy in Russia has never ever happened; it has no history. The country has not yet really started down the road to democracy” (Q 170).

32. Charles Grant (Centre for European Reform) said: “I think sovereign democracy for Putin means autonomy and it is defined in relation to the US. It is about Russia not having to do what the US wants it to do. There is a paranoia about the US that is very strong in the Russia ruling elite, and sovereign democracy is an answer to the problem they have about America dominating the world and CNN ruling the airwaves and so on” (Q 170).

33. The Foreign and Commonwealth Office (FCO) annual report on human rights for 2007 lists Russia as a major country of concern. It states that “the past 18 months have seen a shrinking of the democratic space in Russia, primarily through the recent non-governmental organisation (NGO) and anti-extremism laws and the restrictions imposed on political parties.” It cites concerns about allegations of electoral malpractice in relation to the December 2007 parliamentary elections, on which the EU Presidency published a statement on 4 December 2007 which referred to harassment of opposition parties and NGOs in the run-up to the election, and concluded, inter alia, that “procedures during the election did not meet international standards and commitments voluntarily assumed by Moscow”. The FCO report lists four other areas of concern:

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• restrictions on media freedom and increased risks to journalists’ safety;
• the rise in attacks on ethnic, racial and religious minorities;
• the increasing use of forced psychiatric treatment and detention; and
• the ongoing reports of extra-judicial killings, torture, abduction, and arbitrary detention in Chechnya and the North Caucasus.

34. Many Russians, in the centre as well as in the provinces, are doing what they can to sustain the democratic values which they believe are essential for the future well-being of their country. They are often harassed by the authorities, who find little difficulty in portraying them as stooges of the West.

35. The fate of what the Russian business paper Vedomosti enumerated as the 227,577 non-governmental organisations which have grown up in Russia since the last years of the Soviet Union, and especially the recent laws regulating their activities and requiring them to re-register with the authorities, has attracted much critical attention in the West. In practice most have re-registered successfully. About two thousand of them, however, deal with issues of politics, human rights, and democracy, and these are unpopular with the authorities, especially at election time. Most, including the ones receiving foreign funding, have survived, according to François Bellon, Head of the Moscow Delegation of the International Committee of the Red Cross. They are, however, regularly harassed, and in early February the European University of St Petersburg suspended its activities, ostensibly because it could not meet health and safety regulations, but it has been suggested that its EU-funded election monitoring project had fallen foul of the authorities. It has subsequently been reopened.

36. Nostalgia for national greatness does not mean a desire to return to the Soviet system, as Yevgeni Primakov, a former Prime Minister, assured us during our visit to Moscow. The state’s near monopoly of the media is not complete. Information circulates widely through foreign broadcasting and foreign travel. The number of Russians on the internet has grown from 8.7 million in 2002 to 25 million in 2007, about 28% of the population over 18. This is not a large figure by Western standards, but it is still growing fast. Russian internet users are not inhibited in expressing their views, either through self-censorship or, so far, by the Russian authorities who, unlike the Chinese, have made no serious attempt to interfere with them.

37. President Putin brought stability back to Russia. Associated with this has been an increasing trend to restrict the freedoms of political opponents and the media. Russia is not going back to the days of Stalin, or even to the days of Brezhnev. It is now more open than ever before. For many Russians the restrictions on political freedom have been a price worth paying. That is why Mr Putin was able to command popularity ratings of 60–70% for most of his two terms of office, and why a

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14 Vedomosti, 8 April 2008. This paper reported that of the 227,577 NGOs (Vedomosti’s figures) operating in Russia, 11,000 had been refused official registration in 2007. About one sixth had been checked so far and the Russian authorities had filed court appeals seeking the closure of some 8,274 since 2002. Many NGOs had closed of their own accord since strict new registration requirements were introduced in 2006.

15 Meeting, Mr François Bellon, Moscow, 11 December 2007, see Appendix 4.

16 Meeting, Mr Yevgeni Primakov, Moscow, 12 December 2007, see Appendix 4.

majority of Russians wanted him to remain at the head of affairs even though he was obliged under the Constitution to relinquish the Presidency after two terms.

38. **Russia’s failure to fulfil the high hopes of the early 1990s that Russia would become a democracy, working under the rule of law, and with human rights, a free media and civil society have led to disappointment in the West. The changes needed to transform an authoritarian continental empire need to go very deep, and are likely to take decades if not generations. The sense of disappointment is mutual. For many Russians the West’s moral standing has been severely diminished. They are disillusioned by their experience of the market economy and the Western model of democracy and see little reason to listen to western criticism or prescriptions.**

*The Political Prospect following the March 2008 Presidential elections*

39. Our visit to Moscow followed the elections to the Duma on 2 December 2007 in which Mr Putin’s United Russia party won a large majority with 64% of the vote. During our visit Mr Putin also announced that Mr Medvedev was his preferred successor as president, an outcome which was confirmed in the 2 March presidential election. Both elections were criticised by opponents of Mr Putin, and such outside observers as were not prevented from entering the country, as flawed. Mr Medvedev announced that he would appoint Mr Putin as Prime Minister once he became President. Mr Putin has since been elected as president of United Russia.

40. Mr Medvedev is an academic lawyer and administrator who has been close to Mr Putin throughout his career. He has been Chairman of the state gas monopoly Gazprom since 2002. Medvedev’s publicly expressed views have been reported as liberal and realistic. He said at Davos in 2007: “We realise the problems we are facing—excessive dependence on (natural resources), corruption, a declining population.”

18 He has also remarked that true democracy needs no adjectives, and on another occasion that “no non-democratic state has ever become truly prosperous for one simple reason: freedom is better than non-freedom.” However, Dimitri Suslov, Russian Higher School of Economics, warned us not to interpret Mr Medvedev’s success as a victory for liberalism.

41. In a recent interview with the Financial Times, Mr Medvedev stressed that it will be important for Russia to build on its economic success and to make sure that it translates into social programmes, with the aim of improving the lives of Russians. In particular, he pledged to modernise the healthcare and education systems, as well as housing conditions. In response to a question about what steps he would take to strengthen the rule of law in Russia, Mr Medvedev set out his three objectives: the assertion of the supremacy of the law in Russian society; embedding a culture of law-abidance in society; and making progress towards an active and effective court system, with independent and objective courts.

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19 Meeting, Mr Dmitri Suslov, Moscow, 11 December 2007, see Appendix 4.
42. The relationship between the President and the future Prime Minister following the March election will not necessarily be simple to establish. Under the Russian Constitution, as under the French, the president is responsible for foreign policy, defence, and security, and the prime minister is an executive. It is the President, not the Prime Minister, who represents the country at the highest level, including at the annual meetings of the G8. Both President Medvedev and Mr Putin have declared that they will work together, but such a system of operating in tandem is a new departure in Russian political life and may lead to some uncertainties in the EU’s dealings with the Russians.

43. Professor Anatol Lieven (King’s College, London) reflected in evidence to us in November 2007 on how Mr Putin might manage his future position relative to the next President and whether the President would escape from Putin’s control and decide to continue with a strong presidency. Professor Lieven speculated on the consequences of two possible roles which were open to Putin under the Medvedev presidency: the premiership, when power might migrate from state institution to state institution leading to uncertainty and delay in decision-making with increased corruption; or as head of United Russia which might emerge as a serious mass political party either run by local middle-class people in the Russian provinces, or as a vehicle for the top elite (Q 205). Since these comments were made President Medvedev has asked Mr Putin to be Prime Minister and Mr Putin has become Head of United Russia.

44. All indications are that the initial period of Mr Medvedev’s presidency will be characterised by a high degree of continuity with the policies of President Putin. Mr Putin, whom Mr Medvedev has appointed as Prime Minister, will continue to exercise substantial power and influence. The extent to which Mr Medvedev will follow up his recent statements, including those on strengthening the rule of law, with concrete action remains to be seen.

The Economic Situation in Russia

Russia’s Economic Recovery

45. Central to Russia’s new found self-confidence has been its remarkable economic performance from its nadir in 1998, when the Russian economy was by some measures no larger than that of a medium-sized Member State of the EU. World Bank figures for 2006\(^{21}\) indicate that Russian GDP was US$986.9 billion, whereas per capita income, at US$5780, was still well below the EU average. The economy which Russia inherited from the Soviet Union was weak. Systemic problems had already begun to appear by the early 1960s. The crude methods of forced industrialisation which had worked for Stalin were no longer adequate. Growth had slowed almost to a standstill. Production was still heavily skewed towards heavy industry and defence, at the expense of welfare and the consumer. The striking achievements of Soviet science reflected a well developed system of higher education and research. Their fruits, too, were directed to defence, and rarely penetrated into the civilian economy. Investment was hugely

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inefficient. Agriculture was still, as it had been throughout the Soviet period, a disaster.

46. President Khrushchev’s attempts at creating a market economy had little success and he was removed from office in 1964. By the end of the decade the impetus for reform had petered out. During the 1970s the Soviet leaders were able to ignore the pressure for change because of high oil prices; the country was able to afford to import the advanced technology, the machine tools, and the grain that the Soviet economy could not produce for itself. As the oil price began to fall in the 1980s, Mr Gorbachev was elected, in 1985, but failed to grasp the economic nettle, and was pushed aside in 1991. His successor, Mr Yeltsin, privatised much of industry; imposed strict, even brutal macro-economic disciplines; and opened the economy to foreign trade and foreign investment.

47. Unscrupulous private speculators, often linked to the Kremlin, acquired substantial sections of the economy at low prices and became immensely rich. For ordinary Russians the results were disastrous. Inflation rose to 3000% in the first year. Large numbers of ordinary people sank below the poverty line. As the result of a rouble kept artificially high, much domestic industry was put out of business by a flood of foreign imports. Corruption, crime, and capital flight all flourished. In 1998, partly as a result of the Asian economic crisis, the rouble collapsed and the country defaulted on its domestic debt of US$40 billion. The price of Russian oil rose from around $10 to above $20 a barrel. Local products substituted for imports. The Russian economy began to rise from the ashes.

48. Since then, sound macroeconomic management by the Putin government, and the rising price of oil, have been in great measure responsible for the continued growth of the economy. Professor Julian Cooper of Birmingham University commented that Putin had been a fortunate President, having overseen the growth of the economy by 6–7% a year during his entire presidency, though this figure would probably begin to slow down (Q 48).

49. During President Putin’s first term, he launched an initial programme of economic reform which was much praised in the West, including a radical tax reform, whose implementation was selective and slow. Laws which had already been prepared to allow for land sales, the liberalisation of the railway and electricity monopolies and a reform of the mortgage system were implemented slowly or not at all. Strategic sectors including gas and banking are dominated by State owned companies, including the gas company, Gazprom, the oil group Rosneft, the pipeline monopoly Transneft, and Russia’s largest retail bank, Sberbank.

50. We deal in Chapter 5 with the central role which energy plays in Russia’s domestic economy and the implications for the European Union.

51. Mr Putin’s centralisation of political control damaged business confidence. He cut the autonomy of provincial governors and reduced the power of the oligarchs, especially those who had displayed political ambitions. The media barons Gusinsky and Berezovsky left the country. The oil magnate Khodorkovsky, who had engaged in independent political activity displeasing to Mr Putin, was imprisoned after a ruthless and highly questionable set of court cases against him and his business associates. His company Yukos was bankrupted and most of its assets fell into the hands of the state-controlled
Rosneft. These actions were popular among ordinary Russians; however, they seriously damaged Russia’s reputation abroad as a country ruled by law, and helped to trigger a shift in Western attitudes towards Russia as a whole.

52. The current economic situation in the Russian Federation is strong. Russia’s foreign exchange reserves and current account balance of payments are strong, according to Professor Hanson (Q 61). Professor Cooper said Russia had foreign currency reserves of $425 billion and a stabilisation fund of another $140 billion. The Government’s foreign debt had been reduced substantially and was about 4% of GDP. He did not foresee any crisis in relation to the public finances or another banking crisis in Russia in the next 2–3 years although private sector and banking debt with the outside world could create some problems (Q 61).

53. There are some current and longer term weaknesses which the Russian leadership is seeking to address (see paragraphs 55–64 below). The government is developing a “Concept for Long-term Social and Economic Development of the Russian Federation to the year 2020”. The key idea of the “Concept” is to make Russia a global leader through transition to an innovation economy. This strategy is based on several major points: taking advantage of existing global opportunities; forming competitive high-tech sectors in the economy and further diversifying its structure; and developing human capital, democratic institutions and assurance of personal freedoms. It will be for the new President and his new Prime Minister to see if they can turn these ambitious plans into a reality. We were told by Vladimir Mau, Director of the Working Centre for Economic Reforms of Government in Moscow, that the trouble with cheap money, such as Russia now enjoyed, was that people saw no reason for painful reform. High oil prices were an impediment to economic development, and prevented structural and institutional reform.

54. The Russian government has not abandoned its consistently declared objective of modernising the Russian economy so that it can compete with the best. However, the pressure to take painful reform measures has diminished.

Problems for the Economy

55. Two major challenges affect the economy: population decline and the need for diversification, which we deal with below. In addition to structural weaknesses, the Russian economy is suffering from a number of more immediate problems: an appreciating rouble which is now once again beginning to make domestic production unprofitable, rising inflation and the possible knock-on effect of the economic slowdown in the West. Inflation for 2007 was 11.9%, slightly less than had been feared, but significantly more than the 7–8% originally predicted. It is also a reversal of the recent downward trend: 12% in 2003, 11.7% in 2004, 10.9% in 2005, 9% in 2006. Significantly from the political point of view, food prices went up 16% last year, and the cost of services went up by 13%. This has already had an impact on public opinion, and the authorities are having to take account of

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22 Evidence from Amsterdam & Peroff, Barristers/Solicitors to Mr Mikhail Borisovich Khodorkovsky (pp 151–154)

23 Meeting, Mr Vladimir Mau, Moscow, 12 December, see Appendix 4.
it,\textsuperscript{24} with some staple foodstuffs now having their prices fixed. One reason for food price inflation may be that agriculture also continues to be a weak sector in the economy. Sir Anthony Brenton, British Ambassador to Russia, commented that there was “one bit of the Russian economy which really does need to develop or redevelop … agriculture, the black earth; they have some of the richest farmland in Europe which is scandalously underused at the moment” (Q 231).

\textit{Demography—The challenge of population decline}

56. One important problem that Russia faces is continued demographic decline, which is likely to have both political and economic consequences. Professor Cooper told us that the UN’s latest forecast is that by 2050 Russian could have only 110 million people compared with 142 million now (QQ 48–53). Professor Lieven, however, estimated that the future population figure was more likely to be 130 or 125 million (QQ 181–189). A low birth rate and a high death rate (particularly among men from age 20 to 35–40 because of alcohol, smoking and a high level of industrial and road accidents) painted a worrying demographic future for Russia. The economic and security consequences were already beginning to appear with questions over whether Russia would be able to maintain the size of the armed forces. It was particularly seen in a serious shortage of skilled workers and managers. Ethnic Russians living abroad had mostly either returned already or lacked the financial incentive to return. On the other hand one obvious source of labour, China, was causing concern, with anxiety about possible large-scale Chinese and Far Eastern immigration into the sparsely populated Siberian and Far Eastern provinces. Professor Lieven thought that the long-term existential threat for Russia was Chinese and Muslim immigration.

57. In his May 2006 Address to the Nation, President Putin described the demographic crisis as “the main issue”. He presented a detailed plan for improved childcare benefits to encourage women to have more children. Vladimir Mau, was sceptical that a higher birth rate and greater immigration would provide the answer.\textsuperscript{25} Economic growth was indeed always associated with population growth. Like Professor Cooper, Vladimir Mau thought that most Russians who wished to immigrate from the former Soviet Union had already done so. Russia would be unlikely to attract skilled immigrants in the way that Australia had succeeded in doing. The Russian birth-rate was not significantly lower than the European norm. There were no successful precedents for Government attempts to stimulate the birth rate. What could be done was to limit the population decline by reducing the early death rate, especially among younger men.

58. The problem of demographic decline and its impact on the Russian economy, and security policy is likely to exercise Russian governments and to influence a whole range of their policies for the foreseeable future.

\textit{Economic Diversification—Slow Progress?}

59. Another problem for the Russian economy is the heavy dependence on the production and export of energy and raw materials, including such commodities as wood. United Company Rusal, an aluminium conglomerate,
is now the world’s largest producer, worth an estimated US$30 billion.\footnote{Takeovers recast fast-changing sector\footnote{Financial Times online version, 9 October 2007.} sector, Financial Times online version, 9 October 2007.} This is, in the medium and longer term, a weakness rather than a strength. Professor Cooper thought that the Russian leadership was increasingly realising that Russia should move up the value chain for minerals, materials and commodities as the best way to diversify, rather than exporting them in an unprocessed form or trying to jump into high-technology areas such as electronics and information technology where Russia is very backward by international standards (Q 64). We were told in Moscow, by Yegor Gaidar, the former Prime Minister, that a degree of diversification is in fact going ahead. Manufacturing, vehicle construction, telecommunications, agriculture, housing construction, retail trade, and financial services are all contributing to this additional growth.\footnote{Meeting, Mr Yegor Gaidar, Moscow, 11 December 2007, see Appendix 4.}

60. The process of diversification is happening in two broad ways. The first is at the “para-statals” level, including large concerns directly or indirectly controlled by the government. At least six new state companies were recently created in the defence, aircraft (the United Aircraft Corporation), shipbuilding, high-tech and construction sectors, with more proposed for other sectors of the economy. Exports of state-produced Russian arms—among the few competitive manufactures—have been stepped up, especially to India and China. By the end of 2007, state-owned banks accounted for 43% of total banking assets, while state-owned corporations together with regional and municipal governments now account for more than half of all Russia’s assets.

61. More generally, the Russian banking system is now one of the fastest growing in the world. From 2002 to 2006 the average annual growth in assets was 25–30%. Consumer credit was practically non-existent in Soviet days, and the experience of the 1990s made consumers very wary of entrusting their savings to banks; in the years immediately up to 2005 consumer credit doubled every year, and in 2006 it increased by 75%.

62. The Russians are also diversifying in another way. On 1 February 2008 Mr Medvedev in his Financial Times interview indicated the government’s support for Russian companies seeking to acquire assets abroad. This would “allow us to retool Russian enterprises with technology, boost their production culture, and grant them the opportunity to diversify investments and win new markets.”\footnote{Financial Times, 1 February 2008, page 1.} In other words, the Russians will acquire foreign know-how not by allowing foreign firms to control strategic assets at home, but by acquiring control of leading-edge companies abroad.

63. Western liberal economists might believe that this would lead to inefficiency and waste, but for the time being the Russians apparently believe that they can best achieve their economic objectives through a form of state capitalism. A fully-fledged liberal economic model is considered by them not necessarily right for a backward economy emerging from decades of state planning. Yevgeni Primakov, Chairman of the Chamber for Commerce and Industry, told us that there was a dilemma in the 1990s: Russia had had to choose between macroeconomic rectitude and a free market; or state involvement in the real economy. Now the dilemma was over. The macroeconomy was working and the state was now involved, both of which were necessary for
Russia, even though the market was still working inadequately. He agreed that Russia needed to move away from a commodity-based economy, a change which was beginning to happen: two-thirds of Russian GDP was created on the basis of the domestic market, not on the basis of commodity exports.  

64. Other things being equal, Professor Hanson’s measured conclusion on the Russian economy remains plausible: “On balance a slow-down over a few years to growth rates closer to 5% a year … is a quite persuasive scenario. It is less dramatic than either a collapse or an acceleration towards Chinese rates of growth … Western commentary has tended for years to over-dramatise Russian prospects, both up and down. The country itself has tended to muddle through, fulfilling neither our fondest hopes nor our darkest fears.”

The Climate for Business

65. There is a public perception in the West that doing business in Russia is very difficult and barely profitable because of the degree of state control of the economy, the bureaucracy, the lack of a reliable system of commercial law, and corruption at every level from the top down. The 2007 Report of the Association of European Businesses (AEB) in the Russian Federation, whose representatives we met in Moscow, did indeed identify a number of obstacles to doing business, but their overall view was positive:

“According to the 2006 survey by the Foreign Investors Advisory Council, the majority of foreign investors in Russia are planning to expand their activity in the country over the next three years; 94% plan to expand their business operations; while 91% plan to increase investments into Russia. The overwhelming majority of respondents to the survey believe that their businesses are developing successfully and were able to report a considerable increase in sales and profits over the past year.”

66. In 2007 foreign investment in Russia grew at an unprecedented rate. “Some $100 billion was invested in Russia from abroad over the last 12 months, an all-time record for any emerging market country and a milestone of great historical and psychological significance for Russian business.” Most of this foreign investment—70% in 2006—came from the European Union (only 3% came from the United States). After Cyprus (a special case: investment flows from Cyprus mostly represent returning Russian capital) the largest investor was Britain, with 12.7%.

67. A great deal of business activity takes place at a level which, in Professor Hanson’s words, is “below the political radar”, where the state interferes comparatively little (Q 48). This was confirmed by members of the AEB. They were positive about business prospects in Russia. Business was growing at a double digit rate: KPMG’s Russian business was the fastest

29 Meeting, Mr Yevgeni Primakov, Moscow, 12 December 2007, see Appendix 4.
33 Meeting, the Association for European Business (AEB), Moscow, 13 December 2007, see Appendix 4.
growing of anywhere in the world. The financial sector had recently been growing at 40%. Foreign banks such as Deutsche Bank and Société Générale were doing well. They had good relations with the Central Bank regulators, and room to manoeuvre within the Russian banking regulations. The system of commercial law was slowly improving: it was being pushed forward by the authorities and companies were increasingly defending themselves with success, even in cases involving the tax authorities. Corruption was a problem but not a major issue. The Russians were gradually adopting many of the principles set out in the European acquis communautaire, and from best practice elsewhere, though they were sensitive about anything that seemed “not Russian.”

68. Professor Lieven also commented that Western businessmen he had spoken to still believed that there would be opportunities in many fields in Russia in the years to come (Q 192). Sir Anthony Brenton added some provisos: “First of all, Russian bureaucracy is horrendous. The corruption constraints, which add huge additions to industrial costs, remain very high … But these are bright guys running these things at the top now and they are very internationally oriented and they are keen to make themselves internationally competitive and respectable and, as they do so, so Russia’s economy will grow stronger” (Q 227).

69. At the same time, Russian businesses are increasingly looking to operate abroad. According to Katinka Barysch, “Russian officials routinely complain about EU protectionism but the figures do not support them. Officially recorded outward investment from Russia reached $20 billion in 2006, and once unrecorded transfers are taken into account, the true figure could be twice that. Most of this has gone to Europe. Gazprom now has investments in 16 out of 27 EU countries. In three of the biggest EU markets—Italy, Germany and France—it already has direct access to end consumers. In the UK, Gazprom hopes to raise its market share to 10% by the end of the decade.”

Professor Lieven thought that the Russians were interested in Western investment in Russia and “in their investment in us, and our markets. It is not a Russian policy to disrupt or destroy that” (Q 204). (We deal with some of the potential problems to which these developments could give rise in Chapter 5, Energy). The value of IPOs (initial public offerings) launched on the London Stock Exchange by Russian companies rose from $4.8 billion in 2005 to $14.5 billion in 2006.

70. The Russian economy is currently growing, buoyed up by high energy prices, but the prospect for the medium and long term is uncertain. Many questions remain about potential weaknesses and the threats these hold for its future prospects. Among these are demographic decline, which has implications for both Russian economic and security policy; the failure so far to diversify away from reliance on natural resources; and the failure to press ahead with market reform. The EU should continue to support Russian reforms in the economic sphere, which should be of benefit to both Russian and EU firms.

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34 Meeting, the Association for European Business (AEB), Moscow, 13 December 2007, see Appendix 4.
35 Barysch K, op. cit.
71. The Russians are unlikely to change their views on the need for substantial state involvement in the economy in the near or medium term. They seem, however, to accept that large parts of the private sector should operate free from state control. Both of these aspects of Russian policy have implications for EU policy and they are important for European business, which has largely and enthusiastically invested in the private sector of the Russian economy, and is generally making large profits as a result. The EU should where possible encourage further Russian steps towards improving the climate for foreign investment to provide the best environment for continued investment by European businesses in Russia.
CHAPTER 3: THE INSTITUTIONAL FRAMEWORK FOR RUSSIA-EU RELATIONS

Background

72. There were no formal relations between the European Community and the Soviet Union for the first decades of the former’s existence. The Soviets regarded the European Community as a stalking horse for the Americans, the civilian arm of NATO. They might perhaps have been prepared to recognise the European Community, but only on the basis of reciprocal recognition of the Council for Mutual Economic Assistance (CMEA), which the Europeans regarded as no more than a lever of Soviet economic control over the countries of the Warsaw Pact.

73. The distance began to be narrowed when, with American agreement, the European Community took the lead in the negotiations over economic matters and human rights which led to the Helsinki Final Act of 1975. Later in the 1970s the Russians sent a team to Brussels to negotiate with the Commission about fisheries matters. Formal recognition finally followed in June 1988 when the EU and the CMEA issued a Joint Declaration, and in December 1988 the European Community concluded a comprehensive Trade and Cooperation Agreement with the Soviet Union.

74. Since then Russia and the European Union have dealt with one another on a steadily increasing range of matters. The nature of the relationship between Russia and the European Union has been changing as a result of the European Union’s enlargement to the border of Russia, and the greater self-confidence that Russia has acquired with its new prosperity and its role as a major supplier of energy products to Europe. Some Russians make it clear that their country is no longer willing to remain under the EU tutelage implied by the EU’s “Russian Strategy”, and by many of the “unequal” agreements negotiated between the EU and Russia in the 1990s when the Russians consider that they were negotiating from a position of weakness. 37

The Institutions involved in EU-Russia relations

75. The European Union is represented in Moscow by a substantial office of the Commission. Marc Franco, the Commission’s current Head of Mission, believes that his office is well staffed and is probably amongst the three most effective European missions in Moscow. 38

We were struck by the range of specialisms among the staff whom we met. The office concentrates on the implementation of programmes designed to promote the approximation of Russian and European legislation, better accounting standards and economic legislation, the training of judges, and citizens’ awareness of rights and duties (on which the Commission have produced a Russian language handbook for schools). There is also an active human rights programme (see chapters 4 and 7).

37 This was reflected in comments by Mr Dmitri Suslov, Meeting, 11 December 2007, Moscow, see Appendix 4

38 Meeting, Mr Marc Franco, Moscow, 11 December, see Appendix 4.
BOX 2

EU Institutions

The European Union’s policies are adopted and managed by the EU Institutions, including the Commission, the Council and the European Parliament. Their powers vary depending on policy areas. The Commission has significant competence in areas such as trade, the internal market including energy, competition policy, and technical and financial assistance to Russia. The Common Foreign and Security Policy\(^\text{39}\) is decided by the Council, assisted by the High Representative, Dr Javier Solana. Cooperation on policing, judicial matters, border controls, and visa matters at present takes place between the appropriate national agencies of the Member States as well as the Commission under the Third Pillar.

The Member States make their contribution to all these activities through their missions in Brussels, through officials in national capitals, and through Ministerial meetings of the Council, the European Council, and informal meetings of foreign ministers.

The Delegation of the European Commission to Russia has been working in Moscow as a diplomatic mission since February 1991.

76. The Commission’s projects are now based on the principle that the EU should not lecture the Russians. Consultants from the West are barely used, and the exchanges are more like consultations between professionals on both sides. The Commission is more willing than before to discontinue projects which the Russians are not interested in, and does not attempt to seek credit where this seems likely to be counter-productive.\(^\text{40}\)

77. Marc Franco told us that good progress was being made on the alignment of legislation. The Russian administration and courts have difficulty in enforcing legislation, which is why the Commission has programmes to assist in improving the legal machinery. Exchanges in the fields of research, technology, and education have accelerated in the past two to three years.

78. Mr Franco’s operations are somewhat hampered by the fact that the Russians prefer to conduct most of their EU business through their Mission in Brussels. He believes that his office will be able to function more effectively when the Lisbon Treaty comes into force. This would entail the addition of at most a couple of extra officials.

79. We agree with our witnesses in both the Council Secretariat in Brussels and the Commission Office in Moscow that the passage of the Lisbon Treaty should make it easier to co-ordinate and execute the Union’s policies towards Russia, and therefore make them more effective. A modest increase in numbers in the Moscow office would provide the additional skills needed. In addition, the mechanisms for cooperation between the Council Secretariat, the Commission, and the Member States missions in Brussels should be strengthened.\(^\text{41}\)

\(^{39}\) The CFSP is the so-called “second pillar”.

\(^{40}\) Meeting, the EU Commission Office, Moscow, 11 December, see Appendix 4.

\(^{41}\) We have dealt with this and other aspects on the Lisbon Treaty at length in our Report “The Treaty of Lisbon: An Impact Assessment”, HL Paper 62 of Session 2007–08.
The Russian Institutional Machinery for Relations with the EU

BOX 3

The Russian Institutions

In the first years of the formal relationship between Russia and the EU, Russian policy-making was hampered by a lack of knowledge in Moscow of the complexities of the European system, and of the best way of bringing external influence to bear on it. Over the last decade or so, this situation has changed. The Institute of Europe of the Academy of Science was set up in 1987, and conducts research on European Union affairs. The Moscow State Institute for International Affairs houses the European Studies Institute, set up jointly with the support of the European Commission. There are also a number of other bodies such as the “Russia in the United Europe” committee, which contribute to Russian knowledge about the European Union.

Policy-making towards the EU in Moscow was co-ordinated in the past by an inter-ministerial committee chaired by a Deputy Prime Minister. Mr Fradkov, the previous Russian ambassador to the EU, considered, however, after he became Prime Minister in 2004, that policy could more effectively be co-ordinated by the mission in Brussels. The inter-ministerial committee was therefore abolished, and the responsibility for co-ordination fell on the Ministry of Foreign Affairs. The Foreign Ministry insists on keeping a tight control over the business, and is less flexible than the technical ministries, such as the Ministry of Culture and the Ministry of Economics. However, the general line is given from the Kremlin, which also resolves logjams and bureaucratic disagreements.

80. In its early years, the Russian Mission in Brussels was small, and the staff were inexperienced. Today it is the largest Russian diplomatic mission abroad, the largest third country mission to the EU, and is substantially staffed, with something like one hundred and fifty staff, not only professional diplomats but also experts on specific matters such as agriculture, customs and internal affairs (Ambassador Fedotov, Q 418). It is currently led by an experienced ambassador, Mr Vladimir Chizhov, a former Deputy Foreign Minister, who succeeded Mr Fradkov in July 2005. Mr Chizhov has four Deputy Heads to cover the Four Common Spaces (See Chapter 4). Our witnesses in the Commission told us that the Russian Mission was very active at all levels.

81. Mr Robert Cooper of the Council secretariat said that in terms of the number of meetings held, Russia is probably number one, ahead even of the US mission, although the relationship with the Americans is less formal and more productive (Q 330).

The Partnership and Cooperation Agreement

82. The main formal basis of the EU-Russia relationship is the Partnership and Cooperation Agreement (PCA), a treaty signed by EU leaders and President Yeltsin at the Summit in Corfu in June 1994. The Agreement, in the European view, provides an overall political and legal framework for the EU-

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42 The parties to the Treaty are the European Community and its Member States on the one hand, and Russia on the other.
Russia relationship. It is legally binding, and it provides the basis for “deep economic integration” between the EU and Russia at an unspecified time in the future.

83. The PCA was negotiated at a time when Russia was struggling with the challenges of transition, and was more ready to sign up to the core principles and common values which were central to the present Agreement. Since then, as we have noted, the nature of the relationship between Russia and the EU has changed, not least because they now share a common border following enlargement of the EU to Finland in 1995 and the enlargement to Poland and the Baltic states in 2004.

**BOX 4**

**The Partnership and Cooperation Agreement** (PCA)

The PCA was negotiated in 1994 and came into force on 1 December 1997 for an initial duration of 10 years, and provided for automatic extension on an annual basis provided that neither of the partners withdrew or until a new agreement entered into force. The two parties were unable to start negotiations on a replacement agreement in 2007, in part due to a bilateral dispute between Russia and Poland (which has now been resolved) and more fundamentally because the Russians object to the normative provisions of the Agreement. The Agreement remains in place while a replacement agreement is being negotiated. The negotiations on a new PCA are expected to be launched later this year, assuming the EU Member States agree on a mandate.

The various sections of the Agreement cover, in great detail, general principles, a political dialogue, competition, trade, cooperation in financial, economic and legislative, cultural matters, and the prevention of illegal activities. The Agreement provides for Summit meetings twice a year as well as ministerial meetings. Officials from both sides meet regularly to discuss the highly technical matters dealt with under the “Four Common Spaces” or policy areas (see Chapter 4). The “Political Dialogue” is conducted by Ministers and officials from Moscow, the EU Institutions, and national capitals, including the Russian Ambassador to the EU.

84. Some of our witnesses played down the importance of agreeing a successor to the PCA. Katinka Barysch, Deputy Director of the Centre for European Reform told us that in the present period of uncertainty in EU-Russia relations, “We are in a period where … Russia does exhibit a certain amount of nationalist paranoia, so at the present point in time to sit down and start yet another grand debate about common values and where this relationship should ultimately end up might be bad timing. I think we should let things settle down a bit. We should build mutual trust and everyday cooperation wherever we can achieve it and then maybe at a later point in time come back to negotiating a big comprehensive agreement with joint objectives and more fixed institutional mechanisms … We have moved into all sorts of areas that were not foreseen by the PCA, so it has not held us back, we can roll it over, and we can continue that more pragmatic cooperation in the meantime” (Q 114).

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[^44]: In 2007 summits were held in May in Samara, chaired by Mr Putin; and in Mafra in Portugal, chaired by the Portuguese Presidency under Prime Minister, Jose Socrates.
85. Another view was put forward by Sir Roderic Lyne (former British Ambassador to Russia) who thought that the EU should not attempt to negotiate a grand, overarching new agreement on the lines of the PCA: “the PCA was posited on the idea that Russia was moving towards a situation in which we could say that we had common interests and shared values; and that simply is not the case at the moment ... I think a much more productive approach at this present stage is for us to negotiate on individual, separate issues ... some of which may lead to an agreement with them if we have a shared interest ...” (Q 152).

**British Government and EU officials’ attitudes to the PCA**

86. Jim Murphy MP, Europe Minister believed it was important that there was a successor to the PCA because it was “a creature of its time” and did not properly reflect concerns that have grown in importance since it was drafted, such as the threat of terrorism, climate change, migration, and judicial cooperation (QQ 393, 396, 404). Sir Mark Lyall Grant, Political Director, Foreign and Commonwealth Office (FCO), added that “it would be useful to have an updated Partnership and Cooperation Agreement … some of the developments over the last ten years do need to be factored into the new agreement, … including the fact that it would give it sharper dispute-resolution mechanisms, it would give it a more secure legal framework than the existing arrangement and have a greater emphasis on migration, on counter-terrorism and on energy than the original agreement had, which are all areas which have grown in importance over the last ten years” (Q 26).

87. EU officials we met in Brussels agreed that a new PCA would be desirable, but some thought it more necessary and urgent than others. Eneko Landaburu, Director-General for External Relations in the European Commission, commented that cooperation through the Four Common Spaces was going well despite some difficulties. However, he also stressed the urgency of launching negotiations on a new PCA: “as soon as possible because this will provide us and the Russians with an adequate framework which we need in order to have a real negotiation process, including the energy question” (Q 270).

88. Patrick Child, Chef de Cabinet of the Commissioner for External Relations stressed that “any institutional framework is as successful or as unsuccessful as the political environment in which it is expected to operate” (Q 348). He said that against that background, the existing PCA and the Four Common Spaces currently provide a good basis for the EU’s relations with Russia. However, he also felt that it would be useful to review relations with Russia: “the PCA is … very much a product of the time when it was negotiated”. The Commission Office in Moscow thought there was no pressing need for a new PCA, but eventually one would be needed to define the ultimate objective of EU-Russia collaboration, for example, the creation of a deep free-trade area.45

89. Robert Cooper of the Council Secretariat said that the EU could live without negotiating a new PCA. It would be desirable that this should happen in due course, but “this may not be the right moment for it” (Q 327). However, his colleague, David Johns, pointed out that the disadvantage of the Road Maps agreed under the Four Common Spaces, the current basis for cooperation,

45 Meeting, the EU Commission Office, Moscow, 11 December 2007, see Appendix 4.
was that they were not legally binding. The EU’s interest in a new PCA came from the need to have a legally binding framework within which EU-Russia cooperation could be intensified.

**Russian attitudes to the PCA**

90. Russian attitudes to the PCA are complex. Several of those whom we met in Moscow told us that the Russians did want a new agreement. Some Russians are unhappy that the process is essentially one-way: it involves Russia adopting European technical, legal, and regulatory standards, and there was little flow in the opposite direction. Vladimir Mau at the Working Centre for Economic Reforms of the Russian Government told us that Russian economists thought in the early years (2000 to 2003) that Russia should adopt the European Union’s *acquis communautaire* — the body of EU laws and legal principles, including ECJ case law. He guessed that probably only a third of those people thought the same today; even so, he said, Russian legislation is still in practice being approximated to European legislation. There were two important limitations on the process: law enforcement mechanisms in Russia were not capable of ensuring the practical application even of good laws; and the human capital available was inadequate. On the whole, however, Vladimir Mau thought that cooperation in the Four Spaces of the PCA was helpful in this context.

91. More disturbing for the Russians are the normative aspects of the PCA on democracy and human rights. Dmitri Suslov told us that there was disagreement within the Kremlin on whether the Russians accepted European norms or whether they insisted on equality. The second tendency was beginning to prevail. It was unlikely that the stalemate would be overcome unless EU policies were changed and there was an identification of genuine common aims in the areas of energy, democracy and the CIS. Although the Agreement is between equals based on mutual commitments, some of the actual language points in a rather different direction. Among the principles set out in the preamble to the Agreement are “the political and economic freedoms which constitute the very basis of the partnership”; and “the paramount importance of the rule of law and respect for human rights, … the establishment of a multiparty system with free and democratic elections and economic liberalisation.” The Agreement refers to the obligations which Russia (and the European Community) assumed in these fields under the Helsinki Final Act of 1975 and similar documents. And the provision for a political dialogue binds the Parties to “co-operate on matters pertaining to the observance of the principles of democracy and human rights, and hold consultations, if necessary, on matters related to their due implementation”.

92. The language of the PCA and the associated mechanisms for regular consultations on human rights seem to give the European Union something of a green light to comment on Russia’s domestic business (It also gives Russia a similar green light to comment on the domestic business of the

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46 Meetings, Mr Yevgeni Primakov, 12 December; Minister Alexander Grushko, 12 December; Mr Mikhail Margelov, 12 December, Moscow, see Appendix 4.

47 Meeting, Mr Vladimir Mau, Moscow, 12 December 2007, see Appendix 4

48 Meeting, Mr Dmitri Suslov, Moscow, 11 December 2008, see Appendix 4.
members of the EU). This is something which, the Russians are increasingly disinclined to accept (see also chapter 7).

93. The Russian Ambassador to the UK pointed out that the principals at the EU-Russia Summit in Sochi in 2006 agreed that the PCA would remain in force until it was replaced by a new agreement, thus ensuring that there was no legal vacuum. There was no hurry. What was needed was a “legally binding … politically heavyweight, forward looking framework document, aimed at facilitating a balanced development of the system of sector agreements … complemented by other agreements, whether it be non-proliferation, cooperation in fighting organised crime, counter-terrorism, immigration, asylum” (Q 419). Alexander Grushko, the Russian Deputy Foreign Minister, thought that it was quite sufficient to roll the PCA over from year to year.  

94. Vasily Likhachev, a former Russian Ambassador to the EU, remarked that the existing PCA was not such a bad document: the proposed free trade zone between Russia and the EU was the only one of the ten targets listed in Title III of the Agreement (Trade in Goods) which had not yet been achieved and that problem would be on its way to solution once Russia was in the WTO (see Chapter 4). Dmitri Suslov (Russian Higher School of Economics) told us that the best thing would be to forget about the idea of an all embracing treaty, and concentrate on agreements on sectoral matters, with a political declaration to cover the whole.

95. It is not clear to us how much interest the Russians will have in negotiating a new legally binding agreement similar to the current PCA with normative aspects on human rights. Although it will not be easy, we believe that negotiations on a replacement Partnership and Cooperation Agreement should be started in 2008. An attempt should be made to enshrine the principles of the Energy Charter Treaty and the Transit Protocol in the new agreement or as a Protocol to it (See Chapter 5). Meanwhile the present PCA should continue to be rolled over.

49 Meeting, Mr Alexander Grushko, Moscow, 12 December 2007, see Appendix 4.
50 Meeting, Ambassador Vasily Likhachev, Moscow, 12 December 2007, see Appendix 4.
51 Meeting, Mr Dmitri Suslov, Moscow, 11 December 2007, see Appendix 4.
CHAPTER 4: BUILDING CLOSER COOPERATION THROUGH THE COMMON SPACES

96. This chapter reviews some of the progress that has been made in the framework of the Common Spaces. In relation to the Common Economic Space, we discuss the prospect of Russia’s accession to the World Trade Organisation (WTO) and EU-Russia cooperation on climate change. We assess recent progress under the Common Space of Freedom, Security and Justice, such as on counter-terrorism, visa facilitation and Kaliningrad. We examine the Common Space on Research and Education, including Culture, and cover the issue of the recent Russian attacks on the British Council offices in St Petersburg and Ekaterinburg. Issues relating to the Common Space on External Security are dealt with in Chapter 6, and energy is the subject of Chapter 5. The commercial relationship, which is linked to the Common Economic Space, was covered in Chapter 2.

BOX 5

The Four Common Spaces

At their St Petersburg Summit in May 2003, the EU and Russia agreed to create four ‘common spaces’ for more detailed cooperation. These are an “Economic Space”, to work out measures of trade and economic cooperation; a “Space of Freedom, Security and Justice”, which has already made progress on outstanding visa issues and on measures to combat terrorism; a “Space on External Security”, to reinforce multilateral cooperation especially in the fight against terrorism, non-proliferation, crisis management, and civil protection, and to stabilise the regions around Russia; and a “Space on Research, Education and Culture” to support cooperation in research, academic and cultural exchanges, and language teaching, among other things.

In May 2005 the Summit in Moscow adopted so-called “Road Maps” which set out in great detail the work that needed to be done to make the “common spaces” a reality.

97. Katinka Barysch of the Centre for European Reform told us that the pragmatic and flexible nature of the Four Spaces were their main strength: “Some of what was initially envisaged in the Partnership and Cooperation Agreement as a structure of expert committees and then moving up the hierarchy until you reached a six-monthly EU/Russia summit is now defunct and some of that has become an area of contention. When it comes to ministerial meetings, for example, Russia has always been in favour of having some kind of EU/Russia Council there to meet all the Member States at the same time, whereas of course the European side insists on Russia meeting the Troika.” What we have done is we have been very flexible about this and under the four common spaces we have set up a new structure of expert


53 The Foreign Minister of the EU Member State holding the rotating presidency, the High Representative for CFSP and the Commissioner for External Relations.
groups. The Common Spaces idea leaves us ultimate flexibility with regards to the institutions” (Q 114).

98. In terms of financial support, as Russia becomes more prosperous the need for development-related technical assistance of the kind that the EU was providing under the Tacis Programme54 is rapidly diminishing. Under the new European Neighbourhood and Partnership Instrument (ENPI) the EU will be reducing quite substantially the overall financial volume devoted to the Russia programme (Q 344). Patrick Child, Chef de Cabinet of Commissioner for External Relations Ferrero-Waldner explained that the EU will be concentrating on three or four areas: “Firstly, education, people-to-people contact and scholarship programmes, and that sort of thing and, secondly, on the work we have been doing in Kaliningrad, supporting the economic and social integration of Kaliningrad into its new immediate neighbourhood. That has been a particular focus of the work of Mrs Ferrero-Waldner as Commissioner. We are also encouraged by the recent signs that the Russians themselves are ready to contribute to the Cross-border Cooperation Instrument which we have in place under the Neighbourhood Instrument and that, therefore, again, will be an important theme. Another area I would mention in the context of the Northern Dimension is our work on environment issues, particularly in the North of Russia and the Baltic Sea … We are also doing a number of things through our separate Human Rights Instrument in terms of supporting the rule of law, democracy and civil society in Russia, which I think is an increasingly important thing given the recent political developments” (Q 344).

**The Common Economic Space**

*Economic links*

99. The economies of Russia and the members of the European Union have become increasingly intertwined since the end of the Cold War (see boxes below). The overall aim of the Common Economic Space is the creation of an open and integrated market between the EU and Russia.55 More specifically, the aim is to:

- Increase opportunities for economic operators
- Promote trade and investment
- Facilitate the establishment and operation of companies on a reciprocal basis
- Strengthen cooperation in different sectors of the economy
- Reinforce overall economic cooperation and reforms
- Enhance the competitiveness of the EU and the Russian Federation

Cooperation between the two sides is supported by business-to-business dialogue conducted within the EU-Russia Industrialists' Round Table (IRT).

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54 Launched by the European Community in 1991, the Tacis Programme provides grant-financed technical assistance to 12 countries of Eastern Europe and Central Asia and mainly aims at enhancing the transition process in these countries.

100. To help implement the Common Economic Space, a “Road Map” agreed in 2005 sets out objectives and areas for cooperation in the short and medium term. Fourteen EU-Russia dialogues have been established covering most economic sectors as well as a number of regulatory dialogues which aim to promote gradual approximation of legislation. EU-Russia relations with regards to energy are dealt with in chapter 5.

BOX 6
The Russia and the EU: Close Trading Partners

Russia is the EU’s third most important trading partner, after the USA and China. It accounted for 6.2% of the EU’s exports in 2006, compared to 2.7% in 2000. Germany was by far the largest exporter to Russia in 2006, with 36% of the total, followed by the Netherlands and Italy. Britain came sixth (after France and Poland). Germany was also the largest importer, followed by the Netherlands and Italy. The main exports to Russia from the EU are machine tools, transport equipment, agricultural products and textiles.

The European Union’s imports from Russia amounted to 10.4% in 2006, compared to 6.4% in 2000. 52% of Russian exports—mostly in oil, gas, and raw materials—go to the European Union: imports of energy products from Russia rose from €36 billion in 2000 to €94 billion in 2006. The EU is, with more than 60% of the total, the largest foreign investor in Russia. In 2006 the EU exported services worth €13 billion to Russia, and imported services worth €10 billion.56

Russian accession to the WTO

101. The work in the Economic Space is, among other things, part of the preparation for the closer relationship between Russia and the EU which will flow from Russian membership of the World Trade Organisation (WTO); and it also helps to smooth the way towards an eventual EU-Russia free trade area.

102. Mr Putin remains committed to Russian membership of the WTO. The negotiations began in 1993, and are now largely completed. Bilateral disputes with Georgia and Poland—not directly connected with the substance of the negotiation—have delayed the process. Although in principle the European Union has already agreed to Russian entry, there remain objections by European Union countries over such trade issues as the Russian regime for timber exports to Finland.

103. The arguments which the advocates of Russia’s WTO membership inside and outside Russia put forward in favour of membership are that even its prospect has encouraged Russia to continue with market reform; that it would give Russian exporters better access to markets; that it would make it more difficult for importing countries to mount successful anti-dumping and other protectionist measures against imports from Russia.

104. However some Russian industrialists believe that opportunities in foreign markets would not compensate them for the increased competition they would face at home. Some of those we spoke to in Moscow believed that the

56 Commission document on EU-Russia Relations (at http://ec.europa.eu/external_relations/russia/intro/index.htm.)
obstacles being put in the way of Russia’s early entry were politically motivated. Sir Andrew Wood (former British Ambassador to Russia) also commented that the Russians had often seen WTO entry as a political matter with their exclusion being politically motivated (p 191). Vladimir Mau in Moscow said that the Russian debate was now thoroughly confused. Yegor Gaidar agreed that Russians were strongly divided and a number of senior people thought that membership would not be to Russia’s advantage. He warned that the issue could not be used by the European Union as a negotiating lever.57

105. Professor Lieven (King’s College, London) thought, by contrast, that the WTO was one area where the West had a real capacity to bring pressure to bear on Russia—not as strong as some in the West thought because, he agreed, “the Russians are more ambiguous on the subject than may initially appear.” Some Russian small businessmen were doubtful about WTO membership from their point of view: “but the Russian top leadership, being dedicated to Russian exports, really is interested in the WTO” (Q 191).

106. The European Union should actively promote the widest possible engagement of Russia in international and multilateral institutions; it should resist any attempt to remove Russia from the G8; it should call for the early entry of Russia into the WTO. Any remaining minor disputes can be dealt with under the WTO’s dispute resolution mechanisms after Russia has joined the WTO. The European Union should in due course promote Russia’s membership of the Organisation for Economic Cooperation and Development (OECD).

107. One area where the EU might engage the Russians with greater enthusiasm is climate change. Sir Anthony Brenton, British Ambassador to Russia, told us that an important aspect of EU-Russia relations and negotiations are on international action on climate change: “if the world is to have successful negotiations, … getting Russia on board will be a very important part of those negotiations.” He did not think either the UK or the EU had done this very well so far. The Russians were difficult on the subject; their scientists were not entirely convinced and in Russian business circles some thought that while they were doing so well from oil and gas a global regime which limited demand for oil and gas was probably not going to be a very good thing for Russia. Russia is a large, cold country and others thought that a rather warmer world would be good place from Russia’s point of view. Because the EU and Russia did not see eye to eye on the subject, there was a strong argument for the EU and the UK to engage seriously with Russia on the subject (Q 243).

*Climate Change*

108. Mr Jim Murphy MP, Minister for Europe, in his letter to the Committee of 15 April 2008 (p 137), confirmed that climate change would have an impact on the EU’s relations with Russia. He noted that it is essential that the EU-Russia dialogue on climate and energy “helps us understand and take account of each other’s interests”. The UK needs to work with Russia bilaterally and through the EU and other international organisations on securing an “equitable and ambitious” post-2012 agreement under the UN

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57 Meetings, Messrs Yegor Gaidar, Vladimir Mau and Yevgeni Primakov, Moscow, 12 December 2007, see Appendix 4.
Framework Convention on Climate Change (UNFCCC) process. He confirmed that the draft negotiating mandate for a successor to the PCA covers climate change, as well as conflict prevention and resolution; and security cooperation between the EU and Russia: “this could include conflicts caused, worsened or prolonged by the effects of climate change”.

109. **It is in the interests of the EU to engage the Russians on climate change to a greater degree than at present, despite the Russian reluctance to engage fully.**

**The Common Space of Freedom, Security and Justice**

110. Cooperation in the Space of Freedom, Security and Justice is good, as there is a strong common interest, and the Russian Minister of Justice, Vladimir Vasilyevich Ustinov, and Russian Minister of the Interior, General Rashid Nurgaliyev, as well as the key Presidential Adviser, Mr Viktor Ivanov, have all been involved. One of the recent fruits of this cooperation is the respective agreements on visa facilitation and re-admission which entered into force on 1 June 2007. The visa facilitation agreement provides for simplified procedures for issuing visas which will make it easier for citizens to travel between EU countries and Russia. The readmission agreement concerns the return of Russian, EU Member State and third country nationals illegally residing in the territories of the EU Member States or Russia. The Commission views the obligations set out in this agreement as “an important tool to prevent and tackle illegal immigration.”

Eneko Landaburu, Director-General for External Relations in the European Commission, said: “… the movement of people … is another big and important issue … Now we have a tool, an instrument, in order to co-operate and try to implement a policy on the mobility of people … We will need to improve the provisions of these agreements … Russia is pushing to have the free movement of people without visas.” The Commission were somewhat reluctant because they had to take into consideration a number of elements, including security (Q 270).

111. Fighting terrorism and organised crime is a priority of cooperation in the area of security. The Commission promotes compliance with international law through political dialogue and technical assistance, and exchanges of information and best practice take place at meetings between the EU Counter Terrorism Coordinator and the Russian Special Presidential Envoy as well as at expert level. Cooperation also covers the areas of money laundering, drugs, trafficking in human beings and corruption. Regarding law enforcement, the EUROPOL-Russia Cooperation Agreement of 2003 provides for the exchange of strategic information which helps in the fight against organised crime. The EU and Russia also cooperate on judicial matters. The EU supports judicial reform in Russia, notably in areas such as the training of judges and the modernisation of the court system. (See paragraph 75 above).

112. In 2005 Russia and the EU agreed to establish regular human rights consultations. These cover dialogue on human rights issues in Russia and the EU as well as EU-Russia cooperation on human rights within international forums. The EU has supported the development of democracy, the
protection of human rights and civil society in Russia, notably through the European Initiative for Democracy and Human Rights (EIDHR). The approach of the EU to these issues is discussed more fully in chapter 7.

113. Three specific questions have arisen which can be considered under the Second Common Space: Kaliningrad, ethnic Russians in the Baltic States and extraditions cases between the UK and Russia.

114. A post-Schengen agreement was negotiated on transit through Lithuania for Russians travelling to and from Kalinigrad (See Box 7 below). It came into force in July 2003 and met most of the needs of both parties. It showed that Russia and the EU could hammer out practical agreements when both sides had much to gain from success, and much to lose from failure. It also demonstrated to the Russians, somewhat perhaps to their surprise, that EU solidarity worked, and that they could no longer impose their will on their smaller neighbours if the competences and responsibilities of the European Union were involved. To that extent it was an encouraging and educational model for the future.\textsuperscript{60}

\begin{center}
\textbf{BOX 7}
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\textbf{Kaliningrad}

The region of Kaliningrad is a Russian exclave in the northern part of what used to be East Prussia. The region was assigned to the Soviet Union after 1945, and its German inhabitants who fled were replaced by Soviet citizens. As long as Lithuania was still part of the Soviet Union, civilian and military traffic from Russia to Kaliningrad passed through Lithuania without constraint.

After Lithuania became independent, visa-free transit of Russian citizens through Lithuania was regulated by bilateral agreement. In 2001, according to Russian figures, the number of crossings through Lithuania between Russia and Kaliningrad was 960,000 by train and 620,000 by car.\textsuperscript{61}

As part of its membership of the European Union Lithuania had to apply the Schengen provisions, which involve the abolition of border controls between Member States, and as a corollary to erect them against countries with which they had formerly had bilateral border arrangements. This meant that Russian citizens would in future require a visa to enter or pass through Lithuania. Apart from the practical problems, this became a matter of prestige for the Russians, who expressed much public outrage that they would now need the permission of a foreign state simply to travel to another part of their own country. For their part the Lithuanians feared that their interests would be compromised by the European Union in the interests of maintaining good relations with Russia.

115. The second case concerns human rights issues which the Russians raise with the EU. The Russians complain that the ethnic Russian populations of the Baltic States have been denied the full rights of citizens. There are good historical reasons why the presence of large Russian minorities are a very


sensitive matter for the Baltic peoples. The European Union can help to ensure that ethnic Russians living in the Baltic States are given equal treatment under both national and EU law. The EU can help to manage these understandable sensitivities.

116. The third question relates to extradition which currently affects the UK’s relations with Russia directly because of the cases of Boris Berezovsky and Andrei Lugovoi. Berezovsky is a wealthy Russian who fled to the UK in 2000 and has publicly stated his opposition to the Russian regime. The Russian government has sought his extradition from the UK, but the British Courts have on several occasions refused this request on the ground that he would not be guaranteed a fair trial in Russia.

117. The British authorities, for their part, have requested the extradition of a Russian citizen, Andrei Lugovoi, who is alleged to have assassinated Alexander Litvinenko in London. Alexander Litvinenko formerly served in the KGB and then as a Lieutenant-Colonel in the Federal Security Service (FSB) specialising in counter-terrorism and infiltrating organised crime. He was also Boris Berezovsky’s bodyguard for a time. Litvinenko was granted British citizenship in 2006. He met the Russians Andrei Lugovoi and Dimitry Kovtun in a London restaurant on 1 November 2006 and died on 23 November from poisoning with the radioactive agent Polonium-210.

118. The Russian authorities have refused to extradite Andrei Lugovoi on the basis of article 61 of the Russian Constitution, which bars the extradition of Russian citizens. This led to the UK taking a series of measures announced by the Foreign Secretary in the House of Commons on 16 July 2007, including the expulsion of four Russian diplomats and other measures, which were in turn followed by several Russian measures.

119. On 18 July, the EU presidency issued a statement expressing “disappointment at Russia’s failure to cooperate constructively with the UK authorities” and urging “urgent and constructive cooperation by the Russian Federation on this matter … which raises important questions of common interest to EU Member States”.

120. We welcome the solidarity that the EU has shown with the UK on the question of the extradition of Andrei Lugovoi.

121. In the last few years, progress has been made in several areas of EU-Russia cooperation on justice and home affairs issues. However, serious questions remain about the commitment of the Russian authorities to the rule of law and the independence of the judiciary, especially in politically sensitive cases. The EU should continue in its efforts to promote Council of Europe, OSCE and other relevant standards with regard to the rule of law, the independence of the judiciary, and judicial processes in Russia. These are standards which Russia has accepted and is committed to upholding.

The Fourth Common Space: Research and Education, including Culture

122. The EU and Russia have agreed as part of the Common Space on Research and Education, including Culture, to build stronger ties in this field. Russia is the most successful country in taking up the possibilities of research cooperation with the EU: there are currently 220 projects worth some €2.3 billion, to which the Russians have contributed. This reflects the work
currently going on in the framework of this Common Space. Michael Davenport of the Foreign and Commonwealth Office said that cultural exchanges and language teaching were very important areas for cooperation with Russia, though he pointed out that the teaching of Russian language, literature and culture in the UK has “collapsed” (QQ 32–34). This is a pity as, according to Professor Lieven (King’s College, London), the Russians are obsessed by the notion that Russian has to remain an international language. He thought there was a “reasonable chance” that the Russian language would remain “the biggest medium of exchange, discourse, business, culture, between the states of the former Soviet Union” (Q 201).

123. Sir Roderic Lyne, formerly British Ambassador to Russia, echoed Michael Davenport’s views with regards to the importance of education and cultural exchanges: “I think a lot of the EU’s effort in Russia should be put into areas relating to education, and I have always argued that in discussions with the EU, because I really do think that investing in the next generation in Russia is probably the most helpful thing we can do” (Q 143). A concurrent opinion was expressed by Charles Grant, Director of the Centre for European Reform: “I believe that the EU Erasmus Mundus programme does have links with Russian universities but I am quite sure that it should do much more […] I agree with [Sir Roderic Lyne] that the more contact we can establish with younger people the better” (Q 143).

124. However, the positive atmosphere on cultural issues generally has been marred by the dispute that arose between the UK and Russia, regarding the legal basis for the operations of the British Council in Russia. The position of the Russian government is that the activities of the British Council lack a proper legal basis although Ambassador Fedotov confirmed that the Russian government does not have any concerns about what the British Council is doing in Russia (Q 422). According to the British Government, the assertion about the lack of legal basis of the Council’s operation is simply untrue and they characterise Russia’s action against the British Council offices and staff in St Petersburg and Ekaterinburg as “illegal” (written evidence, Jim Murphy letter of 18 February 2008).

125. The issue is apparently being used as a negotiating chip by the Russian government, which has sought to link it to other issues, a move which the UK Government has strongly resisted (written evidence, Jim Murphy letter of 18 February 2008). On 21 December 2007 the EU declared its support for the British position by issuing a Declaration expressing its concern and urging the Russian authorities to “revisit their decision concerning the closing down of the office of the British Council …” Other bilateral cultural institutions of EU Member States have not been affected.

126. We deplore the attacks on the British Council and its staff and consider that they are not motivated by its activities, but are a part of a wider political strategy to pressurise the UK and the EU into giving ground on other, unrelated issues. Russia’s approach is unacceptable and violates several bilateral and multilateral agreements that Russia has ratified. It is moreover not consistent with a desire to make genuine progress under the Fourth Common Space. The Russian position that this is a purely bilateral matter between them and the

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UK is neither convincing nor sustainable. The EU should continue to support British efforts to find an early solution over the status of the British Council.

127. We welcome the efforts by the EU and Russia to further research cooperation under the Fourth Common Space. The European Union should continue actively to facilitate all forms of contact with the Russian people, including the provision of scholarships and exchanges and the further simplification of visa procedures for students. EU Member States, and in particular the UK, should encourage the teaching of the Russian language in its schools and universities.
CHAPTER 5: ENERGY

The Issues

128. One of the major issues linking the EU and Russia closely is that of energy, especially gas. Russia is a major producer of oil and gas and supplies a number of EU countries, while the Russian energy industry has benefited from the investment and expertise of European companies. As part of the institutional framework for EU-Russia relations, the EU has instituted an Energy Dialogue with Russia. The two commodities have to be considered separately, not least because of the differences in transportation. Crude oil reaches Europe from many sources, and by many routes: road, rail, sea, pipeline, or a combination of these. If one source of supply falls short, it can usually be made up from another. However gas reaches Europe primarily through fixed pipelines which represent a major investment and for which there are, in the short and even medium term, few alternatives. In a crisis, it is therefore hard for the consumer to diversify by finding new suppliers. It is of course equally hard for the producer to diversify by finding new consumers. This means that the question of pipeline routes is always highly political. It also means that there is a measure of mutual dependence between producer and consumer: both are locked into the pipeline system at any one time. This will hardly change until the proportion of liquefied natural gas (LNG) transported by sea increases. Currently LNG supply is limited and initial costs are high, but 20% of the UK’s imports of gas will be LNG in the next year with major new terminals at Milford Haven and one already in the Thames Estuary. While LNG is likely to continue to constitute a minority of the UK’s supplies, it will nonetheless be an important source of the UK’s gas imports.

BOX 8

Russia: A major Producer and Exporter of Energy Commodities

Russia is the world’s largest producer and exporter of natural gas, the second largest oil exporter and the third largest energy consumer. In 2005, according to the estimates of the World Bank, the oil and gas sector represented around 20% of Russia’s GDP, generated more than 60% of its export revenues (64% in 2007), and accounted for 30% of all foreign direct investment (FDI) in the country.

Russia has the world’s largest known natural gas reserves. The other known major gas reserves are all in the Middle East: Iran (15%); Qatar (14%); Saudi Arabia (4%); UAE (3%). By contrast the EU has little more than 1%. Russia has the eighth largest known oil reserves. The largest known reserves of oil are in Saudi Arabia, followed by Iran and UAE. Russia and Venezuela each have 6.6%. Russia has the world’s second largest known coal reserves.

Oil production in the Soviet Union peaked in 1988 at 12.5 million barrels a day. This figure was halved after the collapse of the Soviet Union. It began to rise again in 1999, following the privatisation of much of the industry, the massive devaluation of the rouble, and the rise in the oil price. Production from older fields will decline over the next decade, but the decline should be offset as new fields come into production and will be producing more than half of the country’s oil by 2020.

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64 See written evidence (p 137): letter from the Minister for Europe, Jim Murphy MP, to Lord Grenfell, 15 April 2008.

65 Helm D, The Russian dimension and Europe’s external energy policy, 3 September 2007, quoting BP Statistical review of World Energy.
130. Security of supply is a key issue for the EU, especially in the wake of disruptions in gas supplies from Russia on several occasions in the last two years. Dieter Helm, Professor of Energy Policy at the University of Oxford, told us that there had been some oil issues and the Russians had slowed the oil supply to Germany, causing some disruption, but basically “the exposure to Russian oil is somewhat limited—the big game is about gas” (Q 369).

131. A second key issue is the ownership and control of the means of production and transport. The European Commission’s proposals for liberalisation of the EU energy market (see paragraph 150 onwards) a key component of which is the “ unbundling”, or separation, of production and distribution assets, have provoked opposition from Russia because they conflict with Gazprom’s strategy (See Box 10 below) of controlling downstream assets in the EU. In this respect, the EU is keen to agree the principles of the Energy Charter Treaty and its Transit Protocol with Russia, possibly as part of a new PCA (see chapter 3). As the Commissioner for External Relations recently said: “there is great interest on both sides in negotiating arrangements that allow for an expansion of a Russian and EU presence in each other’s markets. This should be done inside the New [Partnership and Cooperation] Agreement, of which energy will be an important part”. 66

BOX 9

Development of EU Energy Policy

The European Commission began a debate on the future of European energy policy with the publication of its Green paper in March 2006. 67 The paper was produced at the behest of EU leaders at the Hampton Court summit during the UK presidency in autumn 2005. This paved the way for the Energy Package presented by the European Commission on 10 January 2007. 68 An EU summit on 9 March 2007 endorsed the package, agreeing a two year action plan to launch a common energy policy. 69 Meeting in March 2008, Member States agreed to adopt the package by the end of 2008. These augment parallel Commission plans to further liberalise European energy markets. 70

A second strategic European Energy review is scheduled for November 2008 with its recommendations to be endorsed in March 2009. A second action plan for 2010 and onwards is scheduled for endorsement in March 2010. These measures are aimed at continuing the progress towards the development of a single European energy policy.

The French Government have announced that energy security will be one of the priorities of their presidency in the second half of 2008.


70 On 19 September 2007 the EC tabled a liberalisation package to complete earlier attempts to liberalise EU electricity and gas markets. These build on Directives 2003/54/EC and 2003/55/EC. Agreement for liberalisation is scheduled for June 2008.
The EU’s dependence on Russian energy

Overall Europe’s dependence on energy supplies from Russia is substantial. The British Government believes that, once the EU creates a single market for gas, the figure for the dependence on Russian gas of EU countries as a whole would be 25% (Q 401), though the dependence of individual Member States on Russian gas varies considerably and for some the dependence is total. British dependence is very small or nil.71

The table below sets out the figures for 2005.72

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<th>EU Member States Gas Imports from Russia</th>
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<td>Other EU Member States (Cyprus, Denmark, Ireland, Luxembourg, Malta, Netherlands, Portugal, Spain, Sweden, UK)</td>
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<td>EU 27 overall average</td>
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71 The British Government informed us that it was difficult to measure for certain the exact volumes of Russian gas imported into the UK, but there were no direct gas imports from Russia. Indirect imports measured no more than 0.5% (footnote to Q 402).

72 Figures obtained from the European Commission services, DG Energy and Transport, and are provided for purposes of comparison as percentage levels for dependency vary with the source. The International Energy Agency and Eurostat give different percentages.
Russian Oil and Gas Production

Supply and Demand

133. Many economists inside and outside the Russian Federation point out that domestic as well as international demand for Russian oil and gas is growing. Formidable new consumers are now competing for energy, notably China and India, and there are questions about whether Russia can meet the demand. The Europe Minister, Jim Murphy, told us that the British government believes that “within five years with the level of current investment Russia will not be able to meet her domestic demand and international obligations” (Q 401). Professor Helm told us that reserves and resources were vast and that further in the future the Arctic reserves were likely to be very great and increasingly accessible by sea. Very important uncertainties existed about the pipelines to markets and the LNG (liquefied natural gas) facilities, the investment process and the price of oil and gas (Q 360).

134. Sir Andrew Wood (former British Ambassador to Russia) agreed about potential shortages: “Domestic energy demand is increasing at present at around 5% each year. Available data show that Russian oil and gas production has not and will not keep pace with that demand, as well as meeting increasing commitments to Western customers. Investment in new fields has lagged, and cannot now be brought into effective production in good time. Difficult and very expensive decisions will be needed to ensure that the resulting strains are not prolonged, and that competing priorities are satisfied; Russia already depends on Central Asian gas, and will do so increasingly. Despite strong pressures on these countries that may not be easy to secure, … non-Gazprom Russian gas will be needed too and [this] will be easier said than done. It would call for bankable understandings between the independents and Gazprom which would conflict with that company’s monopolistic practices (or an inefficient extension of Gazprom’s reach). Using independents’ gas would also call for heavy investment in processing; and in pipelines. Existing ones badly need attention, including the network linking Russia and Central Asia. Construction capacity constraints are likely to prove as real as financial limits” (p 191).

135. We were told in Moscow that TNK-BP were investing heavily in new “greenfield” projects and expected to see overall production increase again in 2009. However, these were very complex, remote and expensive oil fields to bring on line. They were ice covered for six months and in swampy areas for the remainder of the year. Even more difficult conditions would have to be overcome if much of the gas reserves were to be brought on stream.73

Ownership and control

136. One path which the Russian Government could take to reach its targets would be to allow foreign companies to bring in their capital and know-how. However, Professor Helm thought it was naïve to think that the Russians would beg the Western oil companies to come and help them out (Q 361). In the last few years the Russian Government has moved in the opposite direction, itself taking control of the means of production and transport. Many of the privatised companies have been taken over or forced to allow

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73 Meeting, Mr Shawn McCormick, TNK-BP, Moscow, 13 December 2007, see Appendix 4.
the state a controlling share. To some extent this has simply redefined the problem. The energy sector remains as political as ever, a golden source of patronage and riches for contending factions in the Russian administration, and a driving factor of politics in the second Putin term. The political elite, the governmental institutions and the large monopoly corporations in Russia have become intimately entwined.

137. Many economists inside Russia believe that the effective re-nationalisation of the country’s strategic energy resources is a serious weakness and a brake on future economic development. Others, most Russian politicians, and the public at large believe that natural resources constitute the country’s “crown jewels”, and that it is natural that they should remain under state control. Most ordinary Russians are happy to see the oligarchs brought to heel. Professor Helm thought that state-owned Gazprom (see Box 10 below) was close to pursuing the right rational strategy: to monopolise the domestic resources, owning the reserves and pipes; controlling as much of the downstream market as it can (buying pipes and other assets in Europe); pursuing a policy of divide and rule to get bilateral contracts with particular countries, especially Germany; and entering into politics with all the other sources of supply (Q 368). Gazprom had pursued a policy which was now common to virtually all resource rich countries around the world that “the state either directly or indirectly through the likes of Gazprom should own the oil and gas” (Q 361). From a Russian point of view, he thought, this was a rational thing to do.

BOX 10

Gazprom

90% of Russia’s gas produced by the State owned Gazprom, which also operates the network of gas pipelines. Gazprom is also Russia’s largest earner of hard currency, and it accounts for around 25% of the government’s tax revenues. Its operations have been encumbered by ageing fields, by insufficient export pipelines, and by the requirement to supply heat and power to the domestic market at government-regulated prices, regardless of profitability. Nevertheless, production has started at two new fields: Zapolyarnoye in 2001, one of the largest gas fields brought on stream in the world; and South Russkoye in 2007, also a major field. Gazprom itself foresees that its production will increase by 1–2% a year by 2008, but most of Russia’s new natural gas production over the next two decades is expected to come from independent gas companies.74 However, even these developments may prove insufficient to meet domestic and foreign demand for Russian gas.

138. The Russian government considers that contracts negotiated some years ago with Western oil companies at a time of Russian weakness gave foreign companies excessive control over individual oil and gas fields and it has moved to renegotiate them. Referring in general to Russian foreign policy and specifically to Central Asia, Professor Hanson spoke of Russian feelings of paranoia, of having been “messed around” in the 1990s when they were weak—and now they were strong (Q 73). The oil companies are now bearing the consequences and feel that contracts are being renegotiated under something close to duress: BP had to give up its original arrangements to

exploit the massive Kovykta gas field in Siberia, and Shell was forced to give up majority control of the Sakhalin-2 project.

139. This has been an unpleasant process, which has done nothing for the reputation of the Russian government abroad. It has been compounded by Russian methods: in March 2008 the Russian authorities searched the Moscow offices of TNK-BP and BP and seized files and computer servers. The company employees (none of them UK citizens) were questioned. At first sight these sorts of actions ought to discourage the foreign investment the Russian energy sector urgently needs, but this picture is over-simple. The foreign energy companies have reluctantly accepted the reduced role imposed on them: they cannot afford to be absent from the Russian market. One Western oil man recently commented to Yegor Gaidar (Russian Institute for the Study of the Economy in Transition) that the Russians were doing everything to push the oil companies out, but they were not doing enough.75

140. There is also some evidence of caution on the Russian side. The Russians may be determined to retain ultimate control, but they are also showing signs of some flexibility. In 2006 Gazprom broke off negotiations which would have given a consortium of foreign companies 49% of the shares in the Shtokman gas field in the Barents Sea, 550 kilometres north east of Murmansk, the largest discovered but undeveloped gas field in the world. Less than a year later, Gazprom announced that the French company Total would be allowed a 25% share in an operating company together with a stake held by Hydro Statoil of Norway. Other foreign companies might also be allowed a substantial stake, although Gazprom would retain overall control.

141. There are serious concerns about whether Russia can supply sufficient gas and oil to meet its current and foreseeable domestic demand and international commitments. In the face of this probable shortfall Russia will need greater efficiency and foreign capital. It is unlikely however that these needs will force the Russians to change their ways and there is little chance at present that foreign companies will be allowed by the Russians to acquire ownership of Russia’s strategic oil and gas resources. However, this has not deterred, and should not deter, European companies from seeking opportunities to invest in the country.

Energy Politics

142. Many Europeans fear that the European Union’s dependence on Russian supplies will leave it open to political and economic blackmail, although Sir Mark Lyall Grant, Political Director, Foreign and Commonwealth Office (FCO) told us that the relationship is one of mutual interdependence and that Russia has concerns about security of demand (Q 36). Desirable though it might be that the production and supply of energy, and the siting and building of oil and gas pipelines, should be determined purely by market considerations, they rarely are. There is no pipeline bringing Central Asian gas to market through the convenient route across Iran because of American political opposition. The pipeline from Baku to the Turkish port of Ceyhan on the Mediterranean was deliberately designed to bypass an existing route through Russia for reasons of security rather than economics.

75 Meeting, Mr Yegor Gaidar, Moscow 11 December 2007, see Appendix 4
143. Two recent incidents have reinforced European fears of Russian energy blackmail. Western European consumers were affected when the Russians temporarily cut off gas to Ukraine in January 2006. Pricing was the official Russian explanation, but political motives were suspected connected to Russia’s objection to the “Orange Revolution.” A “technical” breakdown has deprived a refinery in Lithuania of its supplies of Russian crude for four years. The Russians’ explanation was that the pipeline was cracked and leaking; the suspicion is that this too was retaliation because the Lithuanians sold the refinery to a Polish company, rather than to a rival Russian company. Problems with energy supply were one of the reasons for the delay in re-starting negotiations with the Russians on the PCA.

144. Whatever the political motivations, there is no doubt that Russian energy companies backed, and in the case of Gazprom and the larger oil companies owned by the Russian government, are making an ambitious bid to become major players on the world scene. A Gazprom spokesman recently said: “We made a decision to go global in terms of acquiring assets and developing strategy outside Russia.” At the beginning of January 2008 Gazprom announced a deal to invest up to $2 billion to explore and develop the gas fields of Nigeria, a deal which raises further concerns for the Europeans, for whom Nigerian supplies are one obvious alternative to Russian gas. In February 2008 Gazprom also signed a Protocol with Bolivia on prospecting and exploration of natural gas in Bolivia. During President Putin’s visit to Libya in April 2008, Gazprom signed a memorandum of cooperation with Libya’s National Oil company for a joint venture in the gas and oil sector. Gazprom has developed special relationships with large European companies, set up its own supply businesses in Europe, and bought into gas networks there (we touch on the political implications of Gazprom’s recent deal in Serbia in Chapter 6 below).

145. Professor Helm commented to us that Russia was working very hard at constructing its foreign relationships (Q 373). Russian diplomacy had been very heavily focused in the Caspian States [Azerbaijan, Iran, Kazakhstan and Turkmenistan, as suppliers] and in Hungary, Austria, Serbia, Bulgaria and Romania [as customers] (Q 374). Russia is also deliberately diversifying pipeline routes to increase its own room for commercial and perhaps political manoeuvre. The response of a number of European states, particularly those with high gas dependency on Russia, has been to agree bilateral deals with Russia which have at times caused concern to other Member States. Germany has agreed with Russia to build a pipeline (Northstream) under the Baltic Sea, thus bypassing Poland and Lithuania, with both of which Russia’s relations have recently been poor. Northstream, on which construction began in 2006, is designed to reduce the pivotal role of the Ukraine but it is disliked by a number of Baltic States because of the environmental danger it could pose. It caused particular concern in Warsaw because it would rob Poland of valuable transit payments, and could enable Russia to use gas as a political lever in Central Europe, without jeopardising relations with its biggest customer, Germany.

146. Russia has signed long term supply contracts with Central Asian states to send gas north through Russia. These have deliberately sought to undermine alternative (non-Russian) pipeline proposals to Europe such as the Nabucco

pipeline,\textsuperscript{77} which is planned to transport Central Asian gas from Turkey to Austria via Bulgaria, Romania and Hungary, as an alternative to the routes which currently pass through Russia. Another competitor for Nabucco is the so-called Southstream pipeline which Gazprom agreed in June 2007 to build with ENI of Italy. This will run from Russia to Italy bringing gas from Russia across the Black Sea to southern Europe. Bulgaria joined the project in January 2008 and Hungary signed a deal in February 2008 bringing Hungary into the project. In April 2008, the Greek government signed an agreement to host a section of Gazprom’s planned south stream natural gas export pipeline”.\textsuperscript{78} We deal with these questions later in Chapter 7.

147. The Nabucco project has so far received a somewhat hesitant backing from Member States. Some member governments argue that the route is not commercially viable. Others believe that the additional costs should be regarded as an insurance premium to ensure flexibility of supply The view of the British government is that decisions on such matters should be settled by the market: “If you move all of these questions to a more commercial footing, the cost of gas coming through them becomes clearer and the consumer ultimately is better informed to take a decision …” (Nick Latta, Head of Russia Section, FCO, Q 406). “… if we set up a business environment which allows the market to dictate pipeline directions and diversity of routes to market, that gets us to where we need to be” (Europe Minister, Jim Murphy, Q 408). Robert Cooper’s view (Council Secretariat) was that “… Russia is probably more dependent on selling energy to us than we are on buying energy from Russia. They have a very strong interest in being a predictable supplier, so I would say that one should pay an insurance premium, but probably not an absolutely excessive one” (Q 314). Professor Helm thought that the prospects for Nabucco were quite limited and quite a long way off (Q 376).

148. \textbf{In the current situation it is uncertain whether Russian policy is the action of a country simply pursuing its economic and commercial interests in an old-fashioned and mercantilist way, or whether Russia intends to use its energy exports as a political weapon to impose its will on neighbours and partners. Since a number of gas pipelines run through countries such as Ukraine whose bilateral relations with Russia can affect supplies to Western countries, the EU Member States should therefore take active and coherent measures, involving common funding where necessary, to diversify both sources of supply and transportation routes, including pipelines such as Nabucco, even where these are not obviously commercial (though recognising that Nabucco will not on its own solve the problems).}\textsuperscript{79}

149. \textbf{The market will sort out many problems for the supply of gas, as it did after the first two oil shocks. However, on its own the market will not rapidly produce the right results, and considerations of security of supply need to enter into the equation.}

\textsuperscript{77} Nabucco is owned by a consortium of companies.

\textsuperscript{78} Financial Times, 30 April 2008.

\textsuperscript{79} The EU Committee’s report on Renewable Energy Targets is due to be published in July.
Improving the EU’s security of supply and The Third Energy Liberalisation Package

150. One of the points which emerged clearly in the evidence we heard was that the EU could do more in its dealing with Russia to protect its gas supplies: by acting together as well as improving its internal market and creating gas and electricity grids. Professor Helm expressed the view that if Europe were to speak with one voice to Russia its influence would be much greater (Q 372). Sir Roderic Lyne said: “I would put this [the energy dossier] at the very, very top of the list of subjects on which Europe now needs a more effective and co-ordinated policy. I think that is viable but difficult; it needs a lot more work” (Q 148).

151. Professor Hanson of Birmingham University, spoke of the deals which Gazprom made with national gas companies in Member States: “those create powerful interests in those countries which work through the national political level to facilitate deals with Russia and that is something which runs completely contrary to what the Competition Directorate of the Commission is trying to do with energy unbundling. That is one example of an issue where, if the EU could act in a more unified way, it would be very helpful …” (Q 91). Professor Cooper (Birmingham University) thought that “whether we like it or not … individual European powers are going to carry on behaving in this way, carving out their own separate diplomacy with Moscow”. For the EU this was “going to remain an extremely difficult issue, possibly with no solution” (Q 92).

152. The weakness of EU energy policy towards Russia has been compounded not only by the willingness of member governments to make their own bilateral deals with the Russians, but also by their reluctance to integrate the EU’s domestic energy market in a way that would make it more flexible and more able to respond to constraints on supply from one source or the other. Robert Cooper of the Council Secretariat told us: “There are other ways in which one can improve one’s security, notably by having a better internal market in energy by having connectivity, so that if one country has an energy problem with Russia or somebody else, they have got alternative ways of getting electricity or gas ... I would predict that we will have [a much stronger energy policy in the EU] in a few years’ time” (Q 314).

153. In an attempt to address the weaknesses in the EU’s position, the Commission produced the Third Energy Liberalisation Package (See Box 11 below.) The Commission believes that its proposals are central to the liberalisation of the internal market and to the European Union’s overall energy security. The proposals are not directed against foreign investors, although these would of course have to obey the same rules as European companies. State energy companies which wished to invest in European transmission networks would have to decide for themselves whether they wished to reorganise to meet EU rules, just as the Russians expect European companies operating in Russia to abide by the rules as formulated by them. The EU’s existing competition rules have showed themselves to be effective against major American companies such as Microsoft, Hewlett Packard, and Apple.
BOX 11

The EU’s Third Energy Liberalisation Package

The Third Energy Liberalisation Package, published in September 2007, contained European Commission proposals for the reform of the EU electricity and gas regulatory frameworks intended to improve the competitiveness, transparency and flexibility of the European energy market by breaking down barriers to trade within the European Union itself.

One provision was that vertically integrated energy companies would have to separate their production and distribution operations (“unbundling”). This provision would apply also to foreign companies wishing to acquire a significant interest or control over an EU network, which would have to comply with the same unbundling requirements as EU companies. One consideration is that unbundling can be helpful, not just in increasing competition, but in detaching grids. If the grids can then cooperate on a European level it might be possible to help construct a European grid (Professor Helm Q 384).

154. The Commission’s original proposals were supported by the UK, Sweden, the Netherlands, and four other Member States. “The key in all of this”, we were told by Nick Latta, Head of Russian Section at the FCO, “is the completion of a genuine internal market for gas and energy within Europe” (Q 401). Since overall dependence of the European Union on Russian gas supplies is, he believed, about 25% a genuine internal market in energy in the European Union would greatly assist those Member States which are at present wholly dependent on Russian gas (see paragraph 132).

155. Professor Helm warned that, even without dependence on Russia gas, the UK was “terribly exposed” (Q 387). Having depleted its North Sea gas as fast as possible and with nuclear power not consistently available, its need to import gas had increased dramatically and it had no long-term contracts. Eventually, he thought, the UK would have to agree a common energy position with the French and Germans.

156. The Commission’s proposals were severely criticised by the governments of France, Germany and five others, as well as by European energy companies with integrated operations, such as France’s EDF and Germany’s E.ON,81 (though E.ON has since accepted a degree of unbundling). Both the Commission and the French and Germans have since indicated some willingness to move towards a compromise.

157. The Russian reaction has been negative. Russians believe that the Commission’s unbundling proposal is designed to discriminate against Russian companies such as Gazprom. Yevgeni Primakov, (Russian Chamber of Commerce and Industry) who in principle favours state regulation of strategic sections of the economy, said that Russian experts thought that the proposal would be contrary to the national treatment provisions of the PCA and the Energy Charter.82 Even Yegor Gaidar, (Russian Institute for the Study of the Economy in Transition) who by contrast favours market freedom, and believes that the Russians should not think they can dictate

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80 The EU Committee’s report on “The Single Market: Wallflower or Dancing partner”, HL Paper 36, 8 February 2008, discusses the EU’s unbundling policies.
82 Meeting, Mr Yevgeni Primakov, 12 December 2007, Moscow, see Appendix 4.
Europe’s energy policy, thought the Commission’s proposal for unbundling was important, promising, but dangerous: the EU needed in his view to consider its policies carefully. 83

158. A different view was expressed by Pekka Sutela, Head of the Bank of Finland Institute for Economies in Transition: “From the Russian point of view, the premise of granting similar positions to EU and third country companies should be welcomed, not seen as evidence of increased protectionism” (p 185). Some would argue that the negotiation of long-term contracts therefore means that it is difficult to find a concerted approach. Putting forward the contrary view, Charles Grant of the Centre for European Reform said: “there is nothing particularly wrong in themselves with long-term contracts; they are not necessarily incompatible with the Commission’s efforts to unbundle supply from distribution, therefore such contracts need not be banned or necessarily revisited” (Q 150).

159. For the EU as a whole secure and competitive energy supplies are a highly desirable objective. The EU should further formulate its own energy policy, using the Commission’s proposals on energy liberalisation as its basis. There are ways in which security can and should be improved, notably by having a better internal market in energy, with grid inter-connections and storage, so that if one country has an energy problem with Russia or another country, there are alternative sources for electricity or gas.

160. The creation of genuinely competitive energy markets within Europe and the creation of Europe-wide energy grids should be a primary objective of EU policy. Even those countries (including the UK) that do not import significant quantities of Russian gas directly are vulnerable if supplies to their continental partners are interrupted; or if there is a prolonged period of cold weather. Exposure to a volatile spot market, without adequate storage facilities, and without long term contracts, mean that they could find themselves with soaring energy prices and gas supplies severely curtailed. Alternative supplies from Norway, even where they are available in sufficient quantity, will not be price competitive. Germany may be reluctant to surrender the competitive advantage it receives from its well developed gas and electrical systems and long term contracts, or France its relative security arising from the scale of its nuclear industry, but agreement between the UK, France and Germany will be a pre-requisite for a genuinely effective market combined with grids and storage systems.

161. Implementing the Commission proposals on the Third Energy Liberalisation Package will not be easy, given the diversity of view among Member States. The collective negotiating strength of the Member States is at present seriously undermined by the willingness of each of them to go its own way. A degree of structured cohesion is necessary if EU energy policy towards Russia is to be effective.

83 Meeting, Mr Yegor Gaidar, 11 December 2007, Moscow, see Appendix 4.
A European Energy Policy towards Russia?

The Energy Charter Treaty and the Transit Protocol

162. The belief that the Russians would adopt and apply liberal rules in their energy sector underlies the two main instruments available to the EU for managing its energy relationship with Russia: the Energy Charter Treaty and its Transit Protocol. Patrick Child (Head of Cabinet of the External Relations Commissioner) told us that the European Union has a “fairly clear understanding” of what it would like from Russia as a partner in energy: “reliable supplies which are not influenced by political considerations, but are based on sound and reliable commercial relationships”; and for European firms to have the same opportunities to get involved in Russian markets as foreign firms have in European markets (Q 358).

**BOX 12**

Energy Charter Treaty and Transit Protocol

The Energy Charter Treaty (ECT) dates back to a European initiative of the early 1990s, when energy appeared to be an obvious area for mutually beneficial cooperation between East and West. An “Energy Charter” was signed in 1991 between a number of countries including Russia. This was “a concise expression of the principles that should underpin international energy cooperation, based on a shared interest in secure energy supply and sustainable economic development.”

A Treaty was then negotiated, based on these principles, and expanded beyond Europe to include other states with a significant interest in energy matters. The Treaty was signed in December 1994, and entered into force in April 1998 after being ratified by 51 states in Europe, America, and Asia, and by the European Union. It has not yet been ratified by Russia or Belarus (though both apply it provisionally) or by Iceland, Norway and Australia.

The ECT, like the Partnership and Cooperation Agreement, is intended as a legally binding multilateral agreement designed “to strengthen the rule of law on energy issues, by creating a level playing field of rules to be observed by all participating governments, thus minimising the risks associated with energy-related investments and trade”. It focuses on five broad areas: protection of foreign investments; free trade in energy materials, products and equipment; freedom of transit through pipelines and grids; dispute resolution; energy efficiency and environmental protection.

The “Energy Charter Conference”, which consists of all signatories, meets regularly to monitor progress (in Istanbul in December 2007, the Conference discussed energy security in the Black and Caspian Seas). There is a small independent Secretariat based in Brussels. Experts meet to discuss technical matters such as energy market restructuring, regional energy markets, and regional gas markets.

Negotiations on a detailed Transit Protocol began in 2000 but have so far not been completed. The aim of the Protocol is “to develop a regime of commonly-accepted operative principles covering transit flows of energy resources, both hydrocarbons and electricity, crossing at least two national boundaries, designed to ensure the security and non-interruption of transit.”

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85 The Treaty is more comprehensive than the International Energy Agency, set up in 1974 at the time of the first oil shock, which does not include Russia and other countries of the former Soviet Union.
163. Attempts to design an effective policy to manage and reduce Europe’s dependence on Russian energy have, however, been undermined in part by a failure to assess Russian objectives realistically, and to accept that they differ substantially from those of the EU. The EU—driven by a combination of free market principle, commercial self-interest, and wishful thinking—has proceeded on the basis that the Russians would open their markets and their pipelines, in part because they needed Western know-how and capital. However, for the time being at least the Russian determination to maintain a firm control over their energy sector (see above) means that they have no interest in ratifying the Energy Charter Treaty and the Transit Protocol, which they believe are intended to weaken that control. The Russian Ambassador in London maintained that the Treaty was being implemented, but on a temporary basis (Q 426), but Professor Helm thought that Europeans should not have illusions that Russia would suddenly say “Let’s liberalise our market and give third party access”, selling the oil and gas to anyone. In his view this was an illusion which had cost the Europeans several years in putting a strategy together and it would have very serious consequences in the next decade (Q 368).

164. The view of the British Government is nevertheless that “the Charter is the only multilateral agreement in play” (Q 400). Russian concerns about the Charter Treaty and the Transit Protocol have not been clearly articulated which, say the British, makes it hard to envisage what mutually acceptable changes might be introduced. The scope of the Treaty goes, in any case, much wider than the EU and Russia: it embraces other countries formerly in the Soviet Union, Japan, and North America. The British view is therefore that “the best way forward is to remain with the Charter, willingly renegotiated if necessary, but only in principle entering into renegotiation if there is something worthwhile on the other side” (Q 400).

165. This approach does not explain why the Russians should offer “something worthwhile” to secure even an improved version of a Treaty they do not like. Indeed Patrick Child (Head of Cabinet of the Commissioner for External Relations) said to us that he did not know whether the Charter was the right vehicle to achieve the European Union’s objectives, because of the negative political baggage it had acquired on the Russian side (Q 358). Professor Helm thought it was hopeless to use political and diplomatic capital on the idea that the Russians could be persuaded to admit third party access to their gas network. The Europeans were wasting a great deal of time and effort to no net benefit (Q 383).

166. Negotiations on the Transit Protocol (Box 12 above) are currently hanging fire. The Russians consider that the Protocol discriminates against their interests and gives unfair advantages to the European Union. They object particularly to the provision for third party access to their pipelines, which remain a state monopoly under Transneft. They claim that allowing foreigners to buy into the Russian pipeline network, as demanded by the European Union, “would create huge risks for the Russian exporters working on the basis of long-term contracts. Losses on such risks could amount to many hundreds of millions of dollars.” The Russian position is therefore that “We are ready to ratify it if the transit negotiations see a successful
completion to the mutual satisfaction of the parties." The Russian Ambassador in London told us that Russia was interested in a lasting instrument that would effectively regulate transit, particularly since 95% of Russian gas and 40% of oil are supplied to trade markets by means of transit through other countries (Q 426). The Russian State Duma had decided some time ago that the Treaty could be ratified only when Russian proposals for the Transit Protocol and the Energy Charter were taken into account, and Mr Putin confirmed this during the EU-Russia Summit in Helsinki in 2006.

167. **We doubt whether the ECT and the Transit Protocol are the right vehicles to achieve the EU’s objectives because of Russian objections. There seems little point in expending further political capital on trying to persuade the Russians to ratify the Energy Charter Treaty and the Transit Protocol as they stand: they are not going to do so.**

168. **If negotiations get under way later this year for a new PCA the EU should be prepared to explore with Russia whether that instrument could provide a legally binding framework for incorporating energy provisions such as those contained in the ECT.**

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89 According to Mr Fedotov, the concerns include recognition in the Protocol of “the traditional supplier’s priority right to conclude a new transit contract, right of first refusal, and tariffs on long-term contracts, cost plus a reasonable income formula, and the transit protocol’s scope of obligation.”
CHAPTER 6: THE COMMON NEIGHBOURHOOD AND INTERNATIONAL SECURITY ISSUES

169. In recent years, and especially since the 2004 and 2007 enlargements, the EU has increasingly sought to develop its relations with the countries of the former Soviet Union: Ukraine, Moldova and Belarus in the west; Georgia, Azerbaijan and Armenia in the Caucasus; and the former Soviet republics of Central Asia. Russia sees these countries as being her “Near Abroad” and in her sphere of influence, and has sought to maintain privileged relations with them, both bilaterally and through organisations such as the Commonwealth of Independent States (CIS) and the Shanghai Cooperation Organisation (SCO). This has created significant tensions between the EU and Russia, which we explore below under the theme of the “common neighbourhood”. International security matters, including Iran, Kosovo and the Middle East Peace Process, are also regularly discussed between the EU and Russia, notably as part of the Common Space on External Security. Although the two sides do not always agree, their exchanges have generally been constructive. The second part of this chapter looks at these issues in more detail.

170. Before examining these issues we discuss Russia’s view of the world and in particular its attitudes to NATO and the EU.

EU-Russia Relations—The Wider Context

Russia’s World View

171. President Putin followed President Gorbachev in withdrawing from the last outposts of an overextended empire: he closed military bases in Cuba and Vietnam and withdrew peacekeepers from the Balkans. His priorities were Russia’s own hinterland, the “Near Abroad”; the relationship with neighbouring powers—Europe, India, China; and perhaps above all, the relationship with the United States. He was determined that Russia’s voice should be heard on matters in which it has a close interest, such as Iran; and on matters of less obvious direct importance, such as Kosovo. However, President Putin’s ambitions to reassert Russia as a world player did not mean that he was reviving the failed attempt by the Soviet Union to project imperial power across the globe. In a recent interview with the Financial Times, Mr Medvedev, then President-elect, stressed that Russia will continue to pursue a “well-balanced foreign policy, aiming to defend its own interests in a non-confrontational way, so that Russia’s positions will contribute towards strengthening world security”.

Russia’s Attitudes to NATO and the EU

172. Many Russians believe that they were humiliated and exploited by a triumphalist West after the end of the Cold War, and that both Presidents Gorbachev and Yeltsin failed to defend Russian interests. All that changed, they think, with President Putin, who put their country back on the map. That, together with the generally rising living standards, perhaps more than anything else accounts for his popularity. As the former Ambassador to

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Russia, Sir Andrew Wood put it: “many Russians feel themselves to have been cheated by the West ... Moscow gave up its international power and got nothing in return. That argument feeds on a tradition of xenophobia mingled with self-pity, now compensated for by the idea that ‘Russia is back’. President Putin is not the first to say that the weak are always beaten. The corollary is the conviction that Russia needs to show strength and surround herself with dependable, even controllable, allies.” (p 191)

173. Inevitably, the EU is often subsumed with the Americans under the heading of “the West” which the Russians feel have let them down and exploited their weakness. Many Russians date their disillusionment with the West from the 1999 air campaign against Serbia (a traditional Russian ally) which they saw as an illegal act of military aggression against a small country by the world’s most powerful military alliance. They did not and do not accept the justification put forward by the West that the war was a necessary response to a Serbian campaign of genocide against the Kosovars. They believe moreover that Russia did not receive the rewards it had earned from its rapid support of American actions in Afghanistan—including their acquiescence in American military operations through Central Asia—after the destruction of the Twin Towers in New York (see also paragraph 207). Their disillusionment was strengthened by the Western invasion of Iraq, which they opposed and which was illegal in their view.

174. Above all, however, the Russians feel betrayed by the West over its abandonment of the assurances they were given in early 1990 that NATO would not be enlarged.91 The announcement by the US in 2007 that agreement had been reached in principle to station a radar system in the Czech Republic and anti-missile missiles in Poland was seen by the Russians as the final straw.92 As a result, President Putin announced Russia’s intention to suspend their observance of the Conventional Forces in Europe (CFE) Treaty.

175. Charles Grant, Director of the Centre for European Reform, told us: “The Russian opposition to missile defence ... seems to me to be genuine rather than feigned. It is not just a tactic; I think they are genuinely upset by it. I have heard American diplomats say that in the 1990s we promised the Russians that we would never put any ‘something’ into the new members of NATO ... Some people say [advanced] military systems, some people say military bases, some people say significant American forces, but there was some verbal promise made to the Russians in the 1990s, and the Russians think that America has reneged on it” (Q 161).

176. According to Sir Anthony Brenton, British Ambassador to Russia, the EU should remember that Russia went through a period which they regard as a “national humiliation”. He argued that: “one of their main aims ... is to recreate a strong stable, successful Russia. That is what an awful lot of Russia’s foreign policy activity has been about. They are particularly concerned to maintain and to reinforce their influence in what they regard as their immediate neighbourhood in the near abroad, in places like Georgia,

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91 The Russians were given oral assurances by the Americans and the Germans as well as the British. Nothing was put in writing—something now regretted by Mr Primakov, later Yeltsin’s foreign minister, whom we met during our Moscow visit. The record of Prime Minister John Major’s exchange with the Soviet Defence Minister on 5 March 1990 has since been published by the Russian Foreign Ministry.

92 Presidents Bush and Putin recently discussed missile defence at the NATO summit in Bucharest and at their subsequent meeting at Sochi, April 2008, but without making a breakthrough.
Ukraine and so on. In regard to their relations with the West, they retain a lot of the suspicions and concerns which are hangovers from the time when the West was in confrontation with Russia during the Cold War. They deeply dislike NATO, they deeply dislike what they see as Western attempts to encircle them and to weaken them in various ways. It is for that reason that they are very hostile in particular to the US plans to site ballistic missiles in Poland and in the Czech Republic” (Q 216).

177. In terms of the relationship between Russia and the EU on the one hand, and between Russia and the United States on the other, Sir Mark Lyall Grant, Political Director, FCO told us that Russia did not see the EU and NATO as one block: on the contrary, it makes a clear distinction between the EU and NATO because of the membership of the United States in one but not the other (Q 23). He pointed out that: “[Russia] would like to use the European Union more as a forum for discussion of security and disarmament issues perhaps than the NATO-Russia Council, which again they find quite a difficult environment. They … feel a bit sort of ganged up on in that context. Also, they are perhaps jealous of the United States’ relationship with the European Union, which they feel is a sort of smoother relationship and one where less disagreements surface in the EU-US relationship than do in the EU-Russian relationship” (Q 22).

178. If Russia is less hostile to the EU than to NATO, she has nonetheless found handling relations with the EU difficult. The Russian preference is to deal with the EU as a single body or, at least, with big states on a basis of equality, rather than with small, unimportant (in their eyes) states. The Russians have wrestled with the concept of equality between states within the EU when it comes to the EU’s decision—and policy-making. They resent the fact that new Member States such as Poland, the Czech Republic and the Baltic States can have what they perceive as a disproportionate influence on the EU’s decisions and can hamper or dictate the EU’s policies towards Russia for what the Russians view as historical reasons.

179. Professor Lieven (King’s College, London) summed up the Russian view of the EU. The Russians “would really like … a super-French version of Europe in which Europe is essentially a great power allied with Russia against America. The sensible ones now realise that they are never going to get that. Their nightmare … ultimately is of a Polish Europe, a Europe … where policy towards Russia is made in Warsaw and Riga, and not in Berlin, Paris or even London, and in which the EU does become a kind of battering ram against their influence and interests, especially in the former Soviet Union … they would like there to be one telephone number that they can ring in Europe and they would like when they ring … to get an answer that they like. If they think there is a reasonable chance of that, then they think the more united Europe is the better. If they think that the answer is going to be in Polish and is an answer that they do not like, then … they want Europe to be as divided as possible … they would say they do not have a coherent policy towards the EU because the EU is not a coherent force, so they cannot have” (Q 204). “They were hoping … after the Iraq war that the EU would emerge under French and German leadership as a real counterbalance to America, which has not happened” (Q 175).

180. Patrick Child, Chef de Cabinet of the European Commissioner for External Relations, thought that: “It is certainly true that some of the more acute discussions we have had recently over, for example, the Polish meat issue or,
indeed, the Estonian War Memorial, are part of a broader sense of unease in Russian political circles about what the process of EU enlargement means for what they have traditionally considered to be part of their immediate zone of influence … It also explains why it is so difficult for us to engage in the sort of discussions which I would like to see with Russia on some of the frozen conflicts and issues that arise in the context of our common neighbourhood and in the implementation of the European Neighbourhood Policy in some of the countries of Eastern Europe” (Q 353).

181. Patrick Child considered that in the past eight years: “the Russian response to enlargement, and a desire to be more deeply involved and consulted in the enlargement process and decisions, has been a big feature of EU-Russia relations” (Q 353). As Katinka Barysch of the Centre for European Reform put it to us: “Despite the somewhat disdainful rhetoric that is sometimes coming out of Moscow, I think that most Russians are fully aware that the potential for partnership [with the European Union] is greater than with most other countries” (Q 118). However, as Dmitri Simes recently said, it is naive to assume that Europe can “secure Russia’s cooperation in areas important to [Europe] while maintaining complete freedom to ignore Russia’s priorities.”

182. The official Russian view of the international developments of the last two decades is very different from the West’s. Russians draw the conclusion that Russia’s interests do not necessarily coincide with those of the West. They believe that it is up to them to defend their interests, as they understand them, by the best means at their disposal. Most Russians no longer accept that Western countries represent a valid model to follow, both in terms of Russia’s domestic affairs and in terms of its foreign policy.

183. The Russia-United States relationship has always been a key determinant of EU-Russia relations. The attitude of the new US administration will be extremely important and the EU will need strong and direct dialogue with the new administration on Russia.

184. The EU should also listen more carefully to what the Russians say. The EU’s policy-making will be less effective and it will be unlikely to develop its policies towards Russia successfully if it does not understand their views and bear them in mind. That does not of course mean that the EU should not challenge Russian policies and actions if it thinks it necessary.

The Common Neighbourhood

185. The break-up of the Soviet Union and the expansion of the EU had profound implications for the European Union as well as for Russia. Not only have former members of the Soviet empire joined the EU, but the expanded borders of the European Union and of NATO have brought them ever closer to Russia. Russia’s interests now intersect those of the European Union in the countries of Central and Eastern Europe. Nine of these were either republics in the former Soviet Union or members of the Warsaw Pact, and have now become members of the European Union and of NATO. The Ukraine and Georgia aspire to join both the EU and NATO, and Moldova

the EU. The European Union has also asserted a strategic interest—political as well as economic—in the former Soviet republics in Central Asia. The United States have done the same: even before 9/11 and the arrival of US troops in the area they were explicitly “fostering the independence of the States and their ties to the West; breaking Russia’s monopoly over oil and gas transport routes; and promoting Western energy security through diversified suppliers.”

186. For the Russians these countries—especially the former members of the Soviet Union—are the “Near Abroad”, with which they have been closely involved for centuries. With regard to political developments in countries of the former Soviet Union which are now not part of Russia, Sir Mark Lyall Grant told us that Russian and EU interests varied “enormously” (Q 44). The Russians consider that exercising their influence and control over their “Near Abroad” is as natural as the Monroe Doctrine tradition in the foreign policy of the United States, according to which Latin America is the United States’ “backyard”.

187. This attitude is of course unacceptable to the newly independent countries, and to third parties which consider that, however legitimate Russia’s interest may be, it can no longer be exclusive. There are sensitivities on both sides. Russia’s neighbours are quick to react to Russian bullying or a failure of solidarity on the part of the European Union and its Member States, and Russia is always on the lookout for outside attempts to interfere in what it regards as its legitimate interests in countries and regions which were formerly part of the Soviet Union.

188. Referring to the EU’s policies with regards to the common neighbourhood, Sir Roderic Lyne said: “I think it is extremely important that we also think of NATO in this context. One of the most active questions within the broad East/West dispute over this neighbourhood is whether or not countries like Georgia and the Ukraine are going to enter NATO. I do not think you can divorce that from the question of the EU’s relationship with the Russian Federation and the other post-Soviet States. The Russians certainly look at these two things as part and parcel of the same problem from their point of view, which is one of Western encroachment into what they have traditionally regarded as part of their zone of influence, and indeed in the case of Ukraine as part of the Russian heartland. Only the other day Putin was reminding the Russian public that 17 million people whom he classified as Russians lived in Ukraine … This is extremely delicate territory and I can see no way in which we are going to reach an accommodation easily with the Russians over this because, as history shows, when empires break up … it takes a very, very long time for emotions to subside. We have got to frame policies here that respect the rights of those countries, that defend our legitimate interests in them and their rights very robustly, but which at the same time do not lend themselves to misrepresentation in Russia in a way that will make the situation in Europe more dangerous or that will allow new dividing lines to spring up” (Q 139).

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EU policies and actions

189. The EU conducts its foreign policy relationships with Russia through the mechanisms of the Common Foreign and Security Policy and the instrument associated with the Neighbourhood Policy (Box No 13 below).

**BOX 13**

**The European Neighbourhood Policy and the Northern Dimension**

In 2003–04 the EU devised a policy designed to encourage countries in the former Soviet Union, the Middle East and North Africa to become more stable, democratic and prosperous. The partners would get financial aid and better market access provided they undertook economic and political reforms set out in agreed action plans. It is membership neutral with regards to a country eventually becoming a member of the European Union (see House of Lords report “The Further Enlargement of the EU”, 53rd report of session 2005–06, HL Paper 273).

The European Neighbourhood Policy was originally intended to include the Russians, but they objected that it was inappropriate to include them in a programme directed primarily at small countries, many not even in Europe. The European Union therefore adopted a different approach towards Russia, based on financial cooperation, and priorities jointly identified. The Commission committed €17 million for these purposes for 2007, and is targeting between €30 and €40 million for 2008. The money will go on support for the Common Spaces, plus specific support for programmes aimed at the Northern Dimension and at Kaliningrad (see Chapter 4). The Commission is planning a feasibility study for a network of EU study centres in Russian universities. Russia would also like to agree a framework agreement with the EU covering Russian financial assistance for projects in the educational field in EU Member States (Q 279).

The “Northern Dimension”, originally a Finnish initiative, first got under way in 1997. In November 2005 Ministers from the relevant EU countries—those around the Baltic—agreed on an action plan for the further development of the Northern Dimension to include Russia. The new Northern Dimension was adopted at a Summit held on 24 November 2006 in Helsinki, which issued a Political Declaration and a Policy Framework Document.

The Northern Dimension brings together the European Union, Iceland, Norway and Russia. It co-operates with the existing Regional Councils (Barents Euro-Atlantic Council, Council of the Baltic Sea States, the Nordic Council of Ministers, and the Arctic Council). The USA and Canada are observers. The Northern Dimension deals with matters set out in the four EU-Russia Common Spaces, adapted to the particular problems of the region, such as reduction of the risk of nuclear and other pollution, maritime safety, protection of the marine environment in the Baltic and Barents Seas, biodiversity, forests, fish stocks and protection of the Arctic ecosystems. The partners meet at foreign minister level every two years. Senior officials meet in the intervening years. Observers and other attend by invitation. A Steering Group meets at least three times a year.

190. The quality and effectiveness of the European Union’s dealings with the Russians on foreign policy issues varies with the subject. A number of these issues—in Abkhazia and South Ossetia, in Nagorny Karabakh and in Transnistria—are known as “frozen conflicts”: where violence is at a low
level, but solutions are mostly not in sight. There are also differences between the Russians and the European Union over Ukraine, the Caucasus, Central Asia, and currently above all Kosovo. We discuss the context as well as some concrete cases below.

191. Gunnar Wiegand, Head of the Russia Unit and Acting Director of Eastern Europe, Southern Caucasus and Central Asia at the European Commission said: “We are convinced that we could work very closely with Russia in finding solutions to the problems of the so-called “frozen conflicts”, which unfortunately are not always completely frozen. We would like to work more strongly with the Russian Federation on this. We have, perhaps, the most constructive dialogue with Russia on the situation in Transnistria and the least detailed discussion in terms of finding solutions for the situation in Georgia, and Nagorny Karabakh is somewhere in between” (Q 290).

Belarus and Ukraine

192. Ukraine and Belarus form, with Russia, the heartland of the Eastern Slavs. Their peoples have been as often united as they have been divided by history. Although, ever since Yeltsin’s early years, there has been regular talk of forming a Union between Belarus and Russia, the project has got nowhere for political, economic and personal reasons. The Commission has repeated its readiness to engage with Belarus, and to negotiate a PCA provided Belarus adheres to the necessary economic and political standards. So far Belarus has made no practical response.

193. Ukraine looms much larger than Belarus in the Russian mind. Even Russians who accept Ukraine’s independence intellectually find it hard to adjust to it emotionally. Many still regard the separation as unnatural, and believe that in the fullness of time the two countries will be reunited. Personal, economic and cultural links remain strong. Mr Putin has said that 17 million people whom he classified as Russians live in the Ukraine, about a third of the population: a figure which Sir Rodric Lyne thought was broadly accurate (Q 139). The Putin government also feared that the “Orange” revolution in the Ukraine could be the prelude to a similar upheaval in Russia itself. The Russians would be much disturbed if Ukraine were to join the EU, still more if it were to join NATO. There have been suggestions that Russia could take “retaliatory steps” if Ukraine joined NATO.95

194. The Ukrainians themselves are divided about how best to balance their relationship with Russia and their aspirations to become members of NATO and the European Union. President Yushchenko has spoken in favour of Ukraine’s full membership of both organisations on many occasions. Polls indicate that around half the public support membership of the European Union, though the number may be declining. About a quarter support membership of NATO. However, opposition has grown: 20% are against EU membership and nearly half against membership of NATO.96 This doubtless

96 “In accordance with the Democratic Initiative Foundation (DIF) … in 2005 the public opinion was still quite supportive of Ukraine’s membership in the EU. Forty-four percent of the respondents were for the EU accession, 28% were against and 28% would abstain from partaking in the referendum. The results of the opinion poll of the National Institute for Strategic Studies (NISS) are less optimistic: ‘the support for Ukraine’s membership in the EU decreased from 55% in 2001, to 47% in 2005, and 43% in 2006’.”
reflects both the uncertainty in the EU about the pace and extent of further enlargement, and the attachment which the ethnic Russians of Eastern and to some extent Central Ukraine feel to traditional links with Russia.

195. The issue of Ukrainian and Georgian membership of NATO was a crucial aspect of discussions among NATO leaders, and between NATO leaders and President Putin, at the April 2008 NATO summit in Bucharest. Ukraine has been a member of the North Atlantic Cooperation Council since 1992, and is an active participant in NATO’s Partnership for Peace programmes but NATO members held back at the Bucharest summit from inviting Ukraine and Georgia to join a Membership Action Plan, despite keeping the door open for eventual membership. This led some commentators to suggest that Russia had re-established a “sphere of interest” where countries were no longer allowed to pursue their own goals without Moscow accepting them. The Russians are also able to exercise their influence through economic levers. (See Chapter 5 on Energy).

196. Ukraine’s first Partnership and Cooperation Agreement with the European Union came into force in 1998, and a new Agreement is now under negotiation. This looks forward to an EU-Ukraine Free Trade Area, negotiations on which will start when Ukraine has joined the World Trade Organisation (WTO). The EU and Ukraine agreed on the terms for Ukrainian accession to the WTO in January 2008, paving the way for membership this year. The EU and the Ukraine have also agreed a Partnership Action Plan under the EU’s European Neighbourhood Policy (ENP). Patrick Child of the European Commission said: “Few days go past without Ukraine saying they would like to be a member of the European Union. The European Union’s position on that is clear and well established that the focus of the relationship today is the European Neighbourhood Policy” (Q 355).

197. Sir Anthony Brenton, British Ambassador to Russia, said: “I am a very firm advocate of the EU moving as fast and as clearly as it can to getting a very close relationship with Ukraine—not because that disadvantages Russia particularly. Indeed, President Putin is on record as having said he would not oppose Ukrainian membership of the EU—but because the surest way of giving Ukraine the economic boost and the self-confidence to get over its own internal difficulties and to stabilise the democratic system, which is still developing there, is precisely to draw it into the EU embrace in exactly the same way as we did with Estonia, Latvia, Lithuania, the Czech Republic and so on” (Q 229).

**Moldova**

198. Moldova is not a Slav country, and it is not contiguous with Russia, but its breakaway province Transnistria, which emerged from a brief civil war in 1992, is dominated by ethnic Russians. For domestic political reasons the Russian Government cannot afford to be seen to abandon its brethren. There are still over a thousand Russian troops in Transnistria: the Russians claim they are there as peacekeepers, the Moldovans claim they are there illegally.

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199. The European Union has a Partnership and Cooperation Agreement with Moldova, and an appropriate Action Plan. In December 2005 it set up a Border Assistance Mission to help Moldova and Ukraine police their common border.98

_The South Caucasus (Azerbaijan, Armenia, Georgia)_

200. Russia has a very long connection with the South Caucasus, going back to the tenth century in the case of the area now known as Azerbaijan. It currently has good relations with Armenia and reasonable relations with Azerbaijan.

201. With Georgia on the other hand, Russian relations are bad, stemming from the continued presence of Russian troops after the Soviet collapse and Russian meddling in Georgia’s rebellious regions of Abkhazia and South Ossetia. The Russians resented US support for the “Rose Revolution” which brought the American-educated Saakashvili to power, the (very small) American military presence, and the increasingly close relationship between Georgia and NATO, which they see as having no historical justification (see also paragraph 185).

202. Russia—or at least elements of the Russian security services—have exploited these internal conflicts in order to put pressure on the Georgian government. Russia has not yet gone so far as to support the formal secession of Abkhazia and South Ossetia: it fears the precedent that would be created for its own turbulent provinces in the North Caucasus. It has also brought the potential for Abkhazian secession into its arguments against to Kosovo’s declaration of independence.

203. Relations between the European Union and Georgia are regulated by a Partnership and Cooperation Agreement which came into force in July 1999. The EU has allocated €120 million under a five-year Action Plan, and other sums are made available to Georgia under separate programmes. The EU has contributed more than €500 million towards rehabilitation and confidence building in Abkhazia and South Ossetia.99

204. The common neighbourhood in the Russian “near abroad” is an area in which both the Russians and the EU have close geopolitical interests. It is therefore a particularly sensitive area and should be treated as such by both parties.

205. We believe the EU should consult in depth with the Russians over all aspects of the European Neighbourhood Policy with regard to countries which were formerly part of the territory of the USSR, but should not give them a right of veto over EU policy.

_Central Asia_

206. Mr Putin has patiently and with some success worked to strengthen Russia’s political position in Central Asia and has built up his relationships with Central Asian leaders. For a variety of reasons the latter still look towards Russia, though they also exploit their new opportunities of playing the

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Russians off profitably against the Chinese, the Americans, and the Europeans.

207. Mr Putin, after his immediate expression of support for the United States over the destruction of the Twin Towers on 9/11, backed the establishment of US bases in the area, and arranged for the provision of intelligence and logistical support for the Americans to prosecute the war in Afghanistan (see also paragraph 173). At the time he was criticised at home for selling out, and Russians still feel that the Americans have never given them adequate recognition for their support. European interest in the area has been less of an irritant, though the Russians do not much like it.

208. The European Union’s policy towards Central Asia is set out in the Commission’s 2002 Strategy Paper for Central Asia. To implement the aid and other objectives of the Strategy, € 944.4 million has been provided over the past 10 years.\(^\text{100}\) There are Partnership and Cooperation Agreements in force with Kazakhstan, Kyrgyzstan, and Uzbekistan. Another has been signed with Turkmenistan, and there is a Trade and Cooperation Agreement with Tajikistan. The head office of the Commission’s Regional Delegation—which covers the Republic of Kazakhstan, the Kyrgyz Republic and the Republic of Tajikistan—is based in Astana, the capital of Kazakhstan. The Delegation is supported by smaller offices in Bishkek, Kyrgyzstan and Dushanbe, Tajikistan. There is a Commission Delegation in Astana, the capital of Kazakhstan, with sub offices in Bishkek (Kyrgyzstan) and Dushanbe (Tajikistan), and a “Europa House” in Tashkent (Uzbekistan). These activities have not led to difficulties with the Russians.

209. At its meeting of 21–22 June 2007, the European Council adopted an EU strategy for a new partnership with Central Asia (Kazakhstan, the Kyrgyz Republic, Tajikistan, Turkmenistan and Uzbekistan).\(^\text{101}\) The strategy identifies the EU’s strategic interests in the region, as regards both bilateral and regional cooperation, and suggests avenues for a partnership in areas such as: youth and education; human rights, the rule of law, governance and democratisation; economic development, trade and investment; energy and transport links; environmental sustainability and water; and combating common threats and challenges.

210. The Central Asian countries have become more important for the European Union in recent years, notably as suppliers and potential suppliers of gas and oil, (See Chapter 5) but also due to their strategic position in relation to Afghanistan, China, India and Pakistan. The EU has also expressed concern about human rights violations, notably in Uzbekistan, and the lack of progress towards democracy. This has brought the EU into conflict with Russia, which is keen to keep these countries under its leadership and does not share the EU’s concerns about their authoritarian regimes.

211. However, Sir Anthony Brenton, British Ambassador to Russia, emphasised the importance of the EU standing firm in its view on governance in the Central Asian countries: “With regard to Uzbekistan, for example, where there was an appalling massacre a couple of years ago, I think it is important for the prospects of development there that we be very clear on maintaining our democratic values” (Q 229).

\(^{100}\) http://ec.europa.eu/external_relations/ceeca/rsp2.

\(^{101}\) The EU and Central Asia: Strategy for a New Partnership (doc. 10113/07).
212. While Russia may see the EU merely as an unwelcome newcomer and rival in Central Asia, the EU should take account of Russia’s interests and concerns in the formulation of its policies towards the Central Asian countries. Beyond this the EU should seek to engage the Russians in a constructive dialogue about the mutual relationship with the Central Asian countries, and persuade Russia that democracy and prosperity in these countries—which are likely to be strengthened by their relationship with the EU—are also in Russia’s interest.

**International Issues**

213. The EU and Russia have shared interests in working together on a number of international issues. The Russian Ambassador in London stressed that both the EU and Russia were in favour of collective efforts to cope with international crises and to reinforce multilateral institutions such as the UN, to counter the proliferation of WMD and their means of delivery, and to develop effective international institutions to meet global challenges. In addition: Russia is in dialogue with the EU institutions, as well as with individual Member States on “outstanding international issues like the Middle East, Iran and the European agenda” (Q 431).

214. Issues where cooperation with the Russians is extensive and where common ground can be found include counter-terrorism and Iran where Russia has supported the EU-led talks over its nuclear programme and—together with the EU, the US and the UN—is a member of the Middle East Quartet. On a practical level, Russia has proposed providing military assets, especially helicopters, to assist the EU with crisis management. However, the views of the two sides are not always identical in these fields and diverge sharply with regards to Kosovo. We discuss these issues more fully in this section.

215. Ambassador Fedotov’s views contrast with scepticism on the part of some Russians about the workings of the EU’s Common Foreign and Security Policy (CFSP). Mr Sergei Karaganov, an influential Russian political scientist, has written:

“...There are serious grounds for thinking that the European project is in systemic crisis ... The EU cannot lay claim to an independent and lead role because its military capacity is undeveloped and because it is unable to formulate a single foreign policy or even a common point of view. The attempts to create a common European foreign and defence policy are, so far, not only ineffective but often counterproductive as well.”

**Iran’s nuclear programme**

216. The negotiations over Iran are perhaps the most striking example of the CFSP machinery at work with the Russians. The European Commission does not have any formal relations with Iran and there is no Delegation of the European Commission in Tehran. The Iranian embassy in Brussels is accredited to the European Community. The European Union is Iran’s main trading partner. The EU set up a “comprehensive dialogue” with Iran

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in 1998, followed by working groups on transport, trade, and human rights. These promising developments were halted after the Iranian elections of 2004, whose conduct was criticised by the European Union.

217. However, in 2003 Britain, France and Germany, supported by the European Union’s High Representative, Javier Solana, moved to revitalise stalled negotiations with Iran over its nuclear programme by offering Iran substantial economic incentives to comply with its international commitments under the Non-Proliferation Treaty of 1968 and the Safeguards Agreement. Subsequent talks with the Iranians involving, in various configurations, the three European countries, Javier Solana and his staff from the EU Council Secretariat, the Russians, and the International Atomic Energy Agency, supported by the Americans, have still not produced a satisfactory agreement with Iran to stop its programme of potentially weapons-related uranium enrichment.

218. The Russians are the main suppliers of technology and fuel for the Iranians’ nuclear power plant at Bushehr which is fully safeguarded against diversion to weapons production. Dr Solana’s staff have had a fair amount of contact with Russian officials over the issue and have found them sensible and very knowledgeable. They believe that the Russians are in some ways better able than Western countries to read the Iranians because of their intense relationship on nuclear affairs. Robert Cooper, of Dr Solana’s secretariat, also believes that the Russians are appropriately tough with the Iranians in private (Q 302). The Russians have gone along with Western proposals for sanctions with little enthusiasm, but believe that in the end there will have to be a negotiated solution, because the Iranians will not be coerced.

219. Sir Mark Lyall Grant, Political Director at the Foreign and Commonwealth Office, said: “Russia has always been an extremely co-operative member of the 3+3, and continues to be so, there has never been any question of a different sense of priorities or objectives. Russia does not want to see Iran develop nuclear weapons, nor do we, and that underpins the whole approach to the Russian nuclear issue, so that is a very close relationship” (Q 46). A similar view was expressed by Sir Roderic Lyne: “I think that President Putin has seen this as an area where he has diplomatic leverage because Russia has a relationship with Iran, America does not and the European Union does not have much of one. Russia does not want a nuclear-armed Iran ... I think what they are trying to do on Iran is to show that at times they can be helpful, at times they can be less helpful, and that therefore it is very much in the Western interest to deal with them in a way that encourages them to be more helpful. This is classic diplomatic leverage” (Q 162).

The Balkans: Kosovo and Serbia

220. As an increasing number of countries in South East Europe become members of the European Union or aspire to join, the Russians have seen their traditional role there diminish drastically. In the case of Serbia, the connection is reinforced by a sentimental attachment to what they see as a traditional brotherhood with the Serbs. This dates back to Russian support for Serbia, which contributed to the outbreak of the First World War and millions of Russians dead, their shared Orthodox faith, and Moscow’s ultimately unsuccessful attempts to broker an agreement with Serbia in 1999.

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104 The UK, France and Germany, on the EU side, plus the United States, China and Russia.
221. In historical reality, the Russians have regularly left the Serbs in the lurch, the last time in 1999 when their intervention was a major factor in getting Milosevic to capitulate. However, the irrational emotions of brotherhood, combined with a degree of calculation, do colour policy-making in Moscow.

BOX 14

The EU and Kosovo

The EU has been heavily involved in Kosovo since the province came under UN administration (UNMIK) at the end of the war in 1999, under UN Security Council Resolution 1244. It is by far the largest single donor: Kosovo had received more than €1.6 billion from the European Union by 2005. The European Union has a representative office there, and some 17,000 soldiers from the EU serve as members of the NATO-led Kosovo Force (KFOR). Under a compromise plan for a period of supervised independence for Kosovo, devised by the Finnish President, Martti Ahtisaari, UNMIK would hand over its responsibilities and many of its powers to an EU mission. NATO forces will remain in Kosovo as the main international security presence. The EU is deploying a new rule-of-law mission to Kosovo, known as EU-LEX Kosovo, consisting of 1,800 policemen, judges and other civilian experts, including customs officers.

222. Negotiations for a final status for Kosovo stalled. The Kosovar majority insisted on full independence; the Serbs insisted that Kosovo should formally remain an autonomous part of Serbia; and the Russians blocked any agreement in the UN on the final status of Kosovo which was not approved by the Serbs. The Serbs were undoubtedly encouraged in their intransigence by the Russian threat of a veto in the UN Security Council against any action Serbia did not accept. The Russians believe that the Kosovars were encouraged in their intransigence by the assurances they were given that the United States and others would support the move towards unilateral independence (Ambassador Fedotov Q 435).

223. On 17 February 2008 Kosovo unilaterally declared itself independent, having held off while the Serbian presidential campaign was being fought out. While the EU unanimously decided to deploy a 1,800-man mission to Kosovo to help stabilise the situation after the declaration of independence, it split on the question of recognition. By the end of April 2008, eighteen Member States of the EU, including the UK, France and Germany, had recognised the new country alongside the United States; Spain, Romania, Greece and Cyprus are among the nine who had not yet done so because of their own concerns about minorities. The EU has signed a Stabilisation and Association Agreement with Serbia.

224. The Russians offer three arguments for their opposition to Kosovan independence. To accept the right of Kosovo to secede would be illegal, since it is still formally part of Serbia. It would be the first time since World War II that frontiers in Europe have been changed without the agreement of both sides. Secession would create a dangerous precedent for Chechnya—and indeed for Abkhazia, South Ossetia, and Transnistria, whose defections from Georgia and Moldova are opposed by the West. Kosovo’s independence could have two further dangerous consequences: it could lead to the expulsion or worse of the few remaining Serbs who still live there; and

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it could give a fillip to the move for a Greater Albania, which in the worst case could destabilise the Balkans yet again, and possibly suck in both Turkey and Greece.

225. The Russian position is not entirely convincing. There is also, of course, an element of Russian self-interest. Russia has been building up its position in Serbia’s last remaining toehold in the area. Gazprom has signed an agreement for 51% of the Serbian gas network: the gas will travel through the Russian Southstream pipeline, the competitor to the European Union’s supported Nabucco.

226. Russia’s steadfast backing for Serbia, including in the UN Security Council, contributed to Serbia’s intransigence over the final status of Kosovo. This was one of the factors leading to the failure of the Serbs and Kosovars to reach an agreement through the UN-brokered process in 2007. The EU should recognise that Russia has expressed concerns about separatist movements in Russia and in countries near Russia. The EU should seek to persuade Russia to moderate its position and to encourage the Serbian authorities to show greater flexibility on the status of Kosovo.

227. The Russians may regard the lack of unity between EU Member States on the question of recognition of Kosovo as some justification for their position, despite the decision to proceed with the EU mission to Kosovo. The sooner this disunity is ended or is reduced, therefore, the better.

Cooperation on other Issues

228. Russia and the EU are both members of the Quartet on the Middle East Peace Process (see our report “The EU and the Middle East Peace Process”, 26th report of session 2006–07). Sir Mark Lyall Grant, Political Director, Foreign and Commonwealth Office (FCO) said: “I have not sensed that in its own bilateral activities in the Middle East Russia has caused any particular difficulties. Russian objectives in the Middle East are not very dissimilar from ours and I think this is a good area for cooperation” (Q 46). According to Sir Roderic Lyne, formerly British Ambassador to Russia, another area where cooperation has been good is over North Korea and Afghanistan (Q 162).

229. One challenge which the European Commission has been addressing in the field of external security is that of nuclear safety. Gunnar Wiegand of the European Commission told us that in this area since the early 1990s all the funds available to the Community have been spent on the former Soviet Union, with the lion’s share going to Russia and Ukraine, linked to Chernobyl. He commented that the Commission had gradually moved away from upgrading nuclear power stations to higher safety standards, including technical assistance and the provision of hardware, to its current focus on regulatory, supervisory and training assistance (Q 292): “We have a new instrument for this purpose, which is called the Instrument for Nuclear Safety. This provides us with a substantial sum over seven years of €572 million where we will also be able to go to different countries in the future.” Gunnar Wiegand added that: “Russia is quite a good partner in working with us on nuclear safety improvement. We are also working with other instruments and there is now the new Stability Instrument which provides for funding also on non-proliferation …”
230. A practical example of cooperation is the provision by Russia of heavy lift helicopters for the European peacekeeping mission in Chad. Ambassador Fedotov, told us this was under discussion (QQ 431, 433). The British Government have subsequently confirmed\textsuperscript{106} that Russia has been in contact with the EU Council Secretariat regarding this proposal, and HMG has welcomed in principle a continued and increased Russian support for EU, NATO and UN and other international operations, including through the contribution of helicopters, ground forces and other capabilities.

231. The Russians can be co-operative where there is an identifiable common objective: to some extent this is true in Iran where the negotiations are perhaps the most striking example of the CFSP machinery at work with the Russians. There has also been good cooperation with the Russians over anti-terrorism, and this needs to continue in the future. In general, however, the Russians have not been much impressed by the CFSP. Over Kosovo the best that can be hoped for is an agreement to disagree which does not spill over into other areas.

\textsuperscript{106} See written evidence (p 137): letter from the Minister for Europe, Jim Murphy MP, to Lord Grenfell, 9 March 2008.
CHAPTER 7: MANAGING THE EU’S STRATEGY TOWARDS RUSSIA

232. Managing the EU’s relations with Russia is a difficult and complex enterprise. Building a common EU approach requires the involvement of both the Member States and the European institutions. In Chapter 6 we have discussed some of the reasons for Russia’s current attitudes towards the West and in particular the EU. There are divergent views among the Member States about both the substance of EU policy towards Russia, and the most effective way to exert the EU’s influence. Similarly, there are often different views among and within the EU institutions. Russian policy-makers find the EU institutions complex, but are adept at dealing bilaterally with individual Member States in order to prevent the EU presenting a united front. Furthermore, they have a distinctive and intimidating negotiating style.

233. Russia’s increasing assertiveness and prosperity means that the challenges faced by the EU in managing its relations with Russia have become more pressing and more complex. These challenges include the formulation of coherent policies, maintaining solidarity, elaborating an effective method of influencing Russia, and choosing its negotiating strategy, all of which we look at below.

Common Values: Human Rights and Democracy

234. Two of the areas on which the EU seeks to influence Russia are democracy and human rights. We have already discussed in Chapter 2 the increasing restrictions on democratic freedoms in Russia, and in Chapter 3, some of the implications of this for the negotiation of a new PCA.

235. The EU agreed a Common Strategy on Russia in 1999 (which has now expired), which made reference to common values and the forging of closer relations with Russia, but it was short on specifics of how to achieve these goals. This Committee published a report on “EU Russia relations” in 2003\(^{107}\) in which it concluded that “most of the changes advocated with respect to Russia itself, though immediately desirable, are unlikely to be fulfilled in anything closer than the medium term ... the transformation of Russia will ultimately be completed primarily from within, from below as much as from above, and through a change in outlook as well as of institutions. The EU does, however, have a measure of responsibility.”

236. The EU has made some progress since then. In March 2005 the EU launched regular six-monthly human rights consultations with Russia (see paragraph 112). The EU delegation usually meets representatives of Russian non-governmental organisations (NGOs) in the margin. At these meetings the European delegation regularly expresses its concern about the situation in Russia. In October 2007, they raised issues about the forthcoming parliamentary elections; freedom of the press; Russia’s NGOs and civil society following the coming into force of the law regulating the activities of NGOs and the law on combating extremist activities; the rule of law; and the situation in the North Caucasus.

\(^{107}\) The European Union Committee report, “EU Russia relations”, 2003 (3rd report of session 2002–03 HL Paper 29), Extracts taken from paragraphs 93 and 94.
237. Some evidence to the Committee suggested that the EU’s message advocating both democratisation and a market economy had not been effective. Sabine Fischer, researcher at the German Institute, for international and security affairs,\textsuperscript{108} the SWP, pointed out that “one central goal of the PCA is to promote democracy and [a] market economy in Russia. A critical glance at the progress of the Russian transformation and the EU’s technical support shows, however, that in the case of Russia the EU’s conditionality policy has been able to contribute little to democratisation and liberalisation”.

238. Lars-Gunnar Wigemark of the European Commission thought that one problem lay with the clarity of the message: “when we convey this concept or mantra of common values to the Russians, I do not think it is always clear what we are talking about” (Q 296). “… the very basis for our relationship on strategic partnership dealings with Russia is common values and I think we, within the European Union, know what those common values are, and specifically we are often thinking of the Copenhagen criteria as the basis for membership of the European Union”. Lars-Gunnar Wigemark thought that the EU should be more specific in very concrete terms about what was meant by common values, “otherwise it will turn into a discussion of cultural values, which I think we are seeing coming more and more from the Russian side.”

239. Many in Europe hold that the EU should speak out in public against the weaknesses and abuses of democratic procedures in Russia today. The arguments for public criticism are that the European Union must be seen to stand up for what it considers right; that the EU’s public opinion demands it; and that Russian behaviour will be influenced for the better. A further consideration is that Russians who want the political and economic system in their country to become more democratic and liberal believe that public support from Europe will help their cause and perhaps protect them against the pressure of the state. However, the Russian government and its supporters have been known to use European support for Russian NGOs under pressure as evidence that they are pawns of the West. Therefore supporters of this argument believe that Europeans should keep faith with those who welcome support, but should also listen to them on the most effective ways of assisting.

240. There have been times in the past, even in the Brezhnev period, when outside pressure has changed Russian policy. One example is the steady campaign in favour of Jewish refuseniks during the 1970s and 1980s, which produced a trickle, and under Gorbachev a flow, of Jewish emigration. The human rights provisions (“Basket III”) of the Helsinki Final Act in 1975, to which the Brezhnev government agreed, gave great encouragement to those inside Russia who were fighting for a more liberal regime, and contributed significantly towards Gorbachev’s campaign of democratisation. President Putin himself has shown from time to time that he does care about his public image. He modified the behaviour of the Russian police in response to Chancellor Merkel’s criticism of the handling of demonstrators at the EU-Russia Summit in Samara in May 2007, but these have mostly been tactical moves. Other campaigns, such as those in support of the jailed businessman, Mikhail Khodorkovsky or against the way in which the war in Chechnya has

been prosecuted, have had no noticeable effect on the behaviour of the Russian government.

241. One notable example when the EU and the West more generally had to balance public criticism with understanding concerns Chechnya and the North Caucasus. This has been the biggest issue between Russia and the European Union for more than a decade. Chechnya and the other republics of the North Caucasus are an integral part of the Russian Federation and recognised as such by western governments. Western opinion has been appalled by the brutal means adopted by both Mr Yeltsin and Mr Putin in quelling the fighting by Chechen separatists. Very many Chechens and ethnic Russians have died, many have disappeared, and many have been forced into exile. Some Western governments accepted the Russian argument that they were fighting the wider war against terrorism: since the wars in Chechnya began under Yeltsin in 1994, the Russians have been the victims of one major terrorist atrocity after another—each on a scale experienced in Europe only by the Spaniards with the Madrid bomb in 2004. Nor have the Russians been alone in setting human rights aside in the name of anti-terrorism.

242. The devastation in Chechnya is beginning to be repaired under an authoritarian local regime. There have been no general hostilities for two years, and since 2004 no humanitarian crisis as defined by the International Committee of the Red Cross (ICRC). According to François Bellon, the ICRC Representative in Moscow, there has been a sharp decrease in the number of arrests by the security forces, and there is now a more orderly process of trial and conviction or release. However, thousands of civilians and eight hundred members of the security services who disappeared during the conflict have still not been traced. Most of the numerous ethnic Russians who used to live in Chechnya have now left, probably for good. Chechens who fled their homes are slowly returning to their devastated country.109

243. The EU responded to this difficult situation with a mixture of criticism (public and private) and humanitarian aid. Russian policy was criticised in many public statements by the Commission, by Ministers, and by the European Parliament. Since the start of the crisis in 1999, the European Union has given €200 million in aid to the North Caucasus, making it the leading donor in the region. In 2006, the Commission contributed €26 million in relief funding for victims of the Chechen conflict.110

244. The Russians, and President Putin personally, took very great umbrage at the European criticism which had little effect on Russian behaviour. Professor Hanson (Birmingham University) thought that the tradition in Russia was to see things in terms of interest. “If we have been lecturing them about Chechnya in the past or whatever it might have been, it has always been seen as a ploy to achieve something else and … not taken at face value if it is about democracy and human rights …” (Q 94)

245. Gunnar Wiegand, Head of the Russia Section in the European Commission, insisted that both sides should listen to the other on human rights issues as part of a dialogue: “When we talk about democracy, freedom, human rights and common values, what is important in the new way of interacting with

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109 Meeting, Mr François Bellon, Moscow, Moscow, 11 December 2007, see Appendix 4.
Russia is that we do not discuss these things, … with us being the lecturers. We should not forget that the majority of our Member States—and this I can say as a German—are countries which have come out of authoritarianism themselves, be it from left or right, and many are very young democracies. Many of our countries have undergone similar processes as in Russia and have known similar challenges and there are different ways and means to achieve the same standards in the end. What is important in this process is that we accept also when Russia raises critical points with us. Not everything is perfect in EU Member States, and there is one regular item which always comes up and this is minority rights. I can tell you that we are in close contact with a number of Member States to clarify exactly what is happening in this area. We have to be careful there that it is not a one-way dialogue but a two-way street” (Q 297).

**Russian Membership of the Council of Europe and the OSCE**

246. Russia’s membership of two significant pan-European institutions—the Council of Europe and the Organisation for Security and Cooperation in Europe—is one area where the EU can engage with the Russians on human rights, since both are based on “European” values and impose certain obligations on their members.

**BOX 15**

**The European Court of Human Rights of the Council of Europe**

The European Court of Human Rights of the Council of Europe, located in Strasbourg, hears complaints against any Member State of the Council of Europe. Proceedings can be brought by any person, non-governmental organisation, group of individuals, or another Member State of the Council of Europe. The Court’s judgments are binding: they must be implemented by Member States which are found to be in violation of their Convention obligations, under the supervision of the Committee of Ministers. However, while the Committee of Ministers may put political pressure on Member States to comply with a Court ruling, there are no formal sanctions available to ensure that Member States implement the Court’s decisions.

247. The EU supports the work of the Council of Europe, which, together with the OSCE, is the pre-eminent pan-European body responsible for upholding human rights in its Member States. In 2006 Russian citizens filed some 12,000 complaints, a fifth of all cases sent to the European Court of Human Rights (see Box 15) that year. Many concerned abuses by the security forces in Chechnya. In 2006 the Court ruled in favour of the Russian applicant in 80 out of 102 cases. In February 2006 the Parliamentary Assembly of the Council of Europe (PACE) published a report singling out Russia and

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111 All the Member States of the EU and Russia are members of the Council of Europe.
112 All the EU Member States are represented on the Committee of Ministers.
113 Under article 8 of the Council of Europe Statute, it is open to Member States to suspend a Member State’s rights of representation or eject it from the Council of Europe in the event of a serious breach of the rule of law or the obligation to ensure that human rights and fundamental freedoms are respected. In most cases, failure to implement a Court judgment would not meet this threshold.
Turkey as the two Member States least co-operative with the Court. Both President Putin and Foreign Minister Sergei Lavrov have accused the Court of handing down “political” rulings against Russia. However, defiance of the Court, or withdrawal from the Council of Europe, would have a severely negative effect on Russia’s reputation. Both therefore seem unlikely.

248. President Putin was always ready to facilitate the visits to Chechnya of Alvaro Gil Robles, the former Commissioner for Civil Rights of the Council in Europe, and to receive him at length in private. Successive Presidents of the European Council have taken advantage of EU-Russia Summit meetings to make similar private representations. Here too, though, the impact on Russian behaviour has unfortunately seldom been significant. And the Russian reaction has often been to counter with accusations about European failures to observe the norms of democracy and human rights, particularly, so they claim, in the Baltic States.

249. Sir Anthony Brenton, British Ambassador to Russia, pointed out that the Russian Constitution commits the Russians to a democratic way of government and: “They are committed by international obligations to the Council of Europe to a democratic way of government. It is our business, the UK and the EU, to do everything we can to hold them to those commitments …” (Q 210)

250. Jim Murphy MP, Minister for Europe, was clear that the conduct of the Russian parliamentary elections in December 2007 was not consistent with the commitments Russia has voluntarily signed up to under the Council of Europe and the OSCE’s Paris Charter (QQ 393, 398). “The electoral registers, the media coverage, the harassment of opponents, are of fundamental significance when it comes to free elections and the observation of them, [these are standards] which Russia herself signed up to and is not adhering to” (Q 398).

251. Gunnar Wiegand of the European Commission felt that progress was being made. The Russian leadership and their civil servants had become much more assertive in establishing and defending their interpretation of common commitments under the Council of Europe and OSCE instruments, as well as under UN instruments. The rulings of the European Court on Human Rights were being increasingly observed and used as case law in the Russian system: “It is not only … that [the European Court on Human Rights is] having an impact on actual rulings in individual cases as a last instance, it is that its rulings are being used by judges in Russia. That is real progress” (Q 295).

252. However, he cautioned against excessive optimism, noting that Russia was the only country of the Council of Europe that had not yet ratified Protocol 14 of the European Convention on Human Rights (ECHR). Protocol 14 would simplify the ECHR regime in an attempt to tackle the problems facing the European Court of Human Rights, not least its growing backlog. It can only enter into force once ratified by all Council of Europe Member States. Russia is the only one not to have done so yet. Entry into force is necessary to allow the EU to accede to the ECHR, as foreseen by the Lisbon Treaty.

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self-censorship is something which is widely spread and certainly the ownership of most of the mass media is also a point which is questioned” (Q 295).

253. In terms of what the EU can do about these human rights concerns, Gunnar Wiegand thought that, while each state had to be its own judge under its own procedures and participatory processes, the EU should remain engaged and continue to express its interpretation of the common commitments. The Commission did this at the political level on various occasions, including in biannual human rights consultations, where there were no taboos. “… all issues are discussed in extenso and we appreciate that openness of the Russian side. We only deplore that the participants of these events are the human rights experts of the Foreign Ministry and do not include colleagues from the competent Interior and Justice Ministries” (Q 295). He also expressed the hope that the discussions could sometimes take place in Moscow as well as in Europe and that the outreach session with NGOs, could also be attended by his Russian counterparts. Gunnar Wiegand also referred to the projects organised under the European Initiative for Democracy and Human Rights instrument, EIDHR. These promoted civil society and supported human rights organisations in Russia.

254. Russian officials we spoke to made clear that they are not prepared to be lectured on how they run their country; and that they are determined that future international agreements to which they are a party contain no didactic elements of the kind, in their view, that figured in earlier agreements negotiated, as they now see it, at a time when Russia was weak. This has implications both for the public positions adopted by Western governments, and for future agreements between Russia and the European Union.

255. Sir Mark Lyall Grant, FCO, described the difficulties of engaging with the Russians on human rights: “it is a challenge and a particular challenge at the moment … It is not that the Russians do not engage, it is that they sometimes question our approach, they question the premise on which we operate and they do not always see us as avoiding double standards” (Q 40).

256. Sir Anthony Brenton thought it was very important for the EU to continue “… to plug away on the democracy/human rights front … they do not yet entirely meet European standards. There are good ways and bad ways of making that point to the Russians but to continue to make our interest and concern clear is a way of bolstering the best elements in Russian society, is a way of encouraging the sorts of developments that we want to see.” The Russians saw themselves as part of Europe, and as carriers of European standards: “If there is an area where they see themselves as being badly out of line with contemporary European performance—and human rights is arguably one of them—it is an embarrassment and an encouragement to them for that fact to be drawn to their attention” (Q 243).

257. Progress on democracy and human rights in Russia will be slow. Meanwhile the European Union has no choice but to deal with Russia as it currently is, imperfect though it may be in many ways which the EU considers of fundamental importance. Criticism may well be necessary from time to time if the Russian government falls short of the standards which both sides have accepted, for example in the Council of Europe and the OSCE. However, the European Union should consider carefully before issuing strongly critical public
statements about Russian actions of which it disapproves, as it would do with any other country.

Negotiating with Russia

258. A key question we addressed as part of this inquiry is: does the EU have a strong hand in its dealings with Russia? Our witnesses frequently pointed to the importance in the relationship of the mutual dependence of Russia and the EU in the fields of energy, trade and investment, among others. Some observers take the view that the EU’s reliance on gas imports from Russia is a source of weakness, but this view was not shared by Sir Roderic Lyne, former British Ambassador to Russia, who commented: “I think the EU has got a very large amount of leverage because it is Russia’s largest trading partner … The aspirations of a lot of the Russian people are to move towards a European standard of living … They feel more at home in western Europe and the European Union than they do in other parts of the world, and I do not think we should underplay this” (Q 145).

259. Sir Anthony Brenton echoed this thought in advocating that the EU should: “… continue to expand the fast-expanding … economic links, human links, social links, investment links, trade links … if Russia is to become a normal European country—and I am confident it will—that is going to happen through a sort of osmosis, through a sort of feeling that they are inside, through a sort of feeling that they are a member of the club” (Q 243).

260. Charles Grant, Director of the Centre for European Reform pointed to the importance of EU solidarity in its dealings with Russia: “if we can hold a united position on Russia then we clearly have more influence over it because the Russians respect power” (Q 145).

261. Robert Cooper at the Council Secretariat reminded us that there is a considerable range of attitudes towards Russia among the Member States. Greece and Bulgaria gained their independence from Turkey in the nineteenth century partly as a result of Russian support (Q 312). Others—Poland and the Baltic States—lost their independence to Russia at much the same time. “In the long run”, Robert Cooper commented, “everyone would be better off by acting together but, in the short run, that does not always appear so to individual Member States at any particular moment”. He explained that the Council Secretariat had a role in trying to find ways of demonstrating to the Member States that “they are better off if they work together” (Q 312).

262. An obvious tactic for the EU’s external negotiating partners is to deal bilaterally with the larger members where they can; and where they cannot, to drive wedges between its members so as to undermine any united negotiating front. When the EU is not negotiating under treaty provisions, it becomes very vulnerable. Calls for solidarity, and a determination to pursue a common line, rapidly crumble amid the conflict of national interests. The other side then seek to pick the Member States off one by one, and are often successful. Many examples of the Russians using this tactic come from the energy field, where EU members feel themselves particularly vulnerable and which we discuss in Chapter 5.

263. Like the Americans, the Russians claim that they “would prefer to deal with a strong and united European Union rather than with a weak and divided alliance” (Ambassador Fedotov Q 417). In practice, both Russia and the US
deal bilaterally where they can if the result is likely to be more beneficial to them, and the tactic is often successful. It is for the European Union so to order its affairs that foreign governments or businesses see the advantage of dealing with it directly. In the areas where this has already happened, the collective negotiating strength of the European Member States is considerably greater than any of them can muster on their own. That is why the EU is one of the most effective powers in multilateral trade negotiations, with a market numbering almost 500 million people; why the EU can impose its competition rules even on major US corporations; and why Russia found itself having to negotiate with the Commission over visa arrangements and transit through Lithuania for Kaliningrad.

264. EU solidarity is also important to support individual Member States when the Russians decide to bring undue pressure on them to submit to their demands on a particular issue. The EU has demonstrated support in the Russians’ dispute with the British over the Litvinenko affair and the British Council; with the Estonians over the Soviet war memorial in Tallinn; and with the Poles over the Russian embargo on the import of meat from Poland. The Russians, needless to say, resent the European Union’s show of solidarity in such cases and seek to confine these matters to the bilateral relationships. Their view remains that it is for great powers to settle great affairs, and for small countries to conform. However, the EU is, as the Danish Foreign Minister Uffe Ellerman-Jensen has put it, designed to make Europe safe for small countries. The President of the European Commission, Jose Manuel Barroso, addressing President Putin at the EU-Russia Summit in May 2007 in Samara, pointed out that: “It is very important if you want to have close cooperation to understand that the EU is based on principles of solidarity.”

265. The EU does have considerable leverage in its dealings with Russia deriving from its position as Russia’s largest trading partner with a market of almost 500 million people. Other links, particularly in the economic and investment field, but also through human and social ties, add weight to the EU’s hand. The mutual dependence in energy (as supplier and customer), is an additional important factor, as we have noted.

266. The EU will always be more effective when it can agree a united approach in its dealings with Russia. This particularly applies when it is negotiating on a basis laid down in Community law (e.g. the common trade provisions of TEC Article 133). When the EU’s leaders stand together, as Chancellor Merkel and President Barroso did at the Summit with Russia in Samara in May 2007, the EU can make maximum impact. Too often, however, Member States act in a way which allows the Russians to drive wedges between them. In future the Member States need to give a much higher priority to standing together than they have done in the past. Once they have drawn up a new strategy for relations with Russia, they should be consistent in applying it.

267. Without allowing any one state or group of states to dominate EU attitudes towards Russia, the European Union and its members have a duty to support vigorously and by all diplomatic means any Member State which Russia chooses to pressurise in an unreasonable and overbearing way.
268. We have noted earlier in this report that the EU is stronger when Member States coordinate EU policy and unite on action. In the case of policy towards Russia this has not often been the case although the 27 Foreign Ministers discussed strategy towards Russia at their informal “Gymnich” meeting on the 28 March 2008, partly in preparation for the EU-Russia summit which will be held in June in Siberia.\textsuperscript{117}

269. Different aspects of the European Union’s policies towards Russia are handled in different areas of the European Union’s complicated machinery. We were struck that they are not brought into a continuing focus, for example by the Ambassadors to the Political and Security Committee (PSC), which is responsible for preparing analysis and recommendations for Javier Solana and the Council of Ministers; nor by the Policy Planning Unit under Dr Solana. It appears that no-one is responsible for taking a strategic overview of the relationship as a whole.

270. We consider that the importance of building a stable and strong long-term relationship between the EU and Russia based on mutual trust and understanding is greater than ever. This, combined with a hard-headed and unsentimental approach by the European Union can help to ensure that the relationship is productive rather than the opposite. The Russians should thus be able to see that it is in their own interests to work productively with the EU.

271. The EU’s attitudes and policies towards Russia have an uncoordinated character. In order to better design and coordinate its overall strategy towards Russia, the European Union should rethink its current policy towards Russia as a matter of priority. An updated approach should be drafted as a collaborative project between the Commission and the Council Secretariat and approved by the Council of Ministers. It should be discussed by the European Council at one of its forthcoming meetings.

Russian membership of the EU?

272. We asked a number of witnesses whether Russia could one day become a member of the EU. Most of those who replied judged that the prospect, if it existed at all, was far distant. Membership of the European Union is much more demanding, and over a wide range of domestic activity, than membership of any other international organisation. Apart from insisting that potential members adhere to the liberal democratic and economic principles set out in the “Copenhagen Criteria”, they are also expected to adopt the full range of EU laws, regulations, legal precedents and international obligations known as the “\textit{acquis communautaire}”.

273. Although the Russians are, as we were told by Vladimir Mau,\textsuperscript{118} discreetly designing new measures to shadow European legislation in an unspoken process of adaptation to the \textit{acquis}, many of those to whom we spoke said that, for political as well as practical reasons, they could not conceive of Russia submitting to the full range of European disciplines in the foreseeable future. A number of people we spoke to added that Russia was in any case

\textsuperscript{117} “EU foreign chiefs to debate future ties with Russia”, EU Observer, \url{www.euobserver.com}, 28 March 2008.

\textsuperscript{118} Meeting, Mr Vladimir Mau, Moscow, 12 December, see Appendix 4.
too large a country to be comfortably accommodated within the European Union’s decision-making institutions.

274. Several of those we met in Moscow suggested that Russia might achieve a formal relationship with the EU of a different kind: such as participation in the European Economic Area, similar to that enjoyed by Norway. However this arrangement entails applying the acquis and making a financial contribution, without having any direct influence over the EU’s decisions. This seems an unattractive option for the Russians. According to Katinka Barysch of the Centre for European Reform, “From the Russian side also, joining the European Union is not a very attractive prospect. Russia … is attached to old-fashioned notions of foreign policy-making” (Q 105).

275. Not joining the EU is also official Russian government policy. Russia’s ‘Medium-Term Strategy towards the European Union, 2000–2010, published in October 1999, explicitly states that during the period covered by the strategy paper, neither Russian membership of the EU nor formal association are on the agenda. However, the Russian Ambassador in London left the question of the future open. The overall framework of Russia’s policies toward the EU, “at this stage at least, could be defined by a quite simple formula: anything but institutions. This means that Russia is prepared to establish as close cooperation with the EU as possible but without being its formal member. We have made our fundamental choice in our foreign policy in favour of forging a strategic partnership with the EU.” It remained “one of the priorities of the Russian Government” (Q 413). However, the EU was an evolving institution. “Who knows what will happen with the EU of 50? No-one can predict how it will develop … and how it will allow Russia to take part in its evolution … one cannot exclude anything but, so far, it is hard to see in the future, in 30 or 40 years, how our children and our grandchildren will see it … Then the new generation of political leaders will decide what to do” (Q 437).

276. We asked a number of witnesses whether they concluded that the European Union should clarify its position on Russian membership, either making clear that it was ruled out in principle, or stating that the European Union looked forward to eventual Russian membership when the relevant criteria had been met. Almost all were firmly of the view that it would be premature for the European Union to make a statement one way or the other on eventual Russian membership of the EU.

277. The EU has no interest in offending the Russians, who consider themselves as having a similar status in the international system to the United States. Katinka Barysch said: “I think absolutely no purpose is served because on the one hand if you invited Russia to join the European Union it would be horrified, but if we made it clear to Russia that it would never join, it would be equally horrified. I do not think any purpose is served by drawing borders around the European Union and you probably do not need to answer the question of the potential membership of Russia” (Q 106). For Sir Roderic Lyne, former British Ambassador to Russia, “the urge from some quarters to

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draw a permanent dividing line around the [European] Union should be resisted. Doors should be kept open rather than closed." \(^{120}\)

278. The issue of Russia’s potential membership of the EU does not currently arise. In the unlikely event that Russia did eventually apply, and if it was judged that Russia qualified, the European Union would need to consider the application on its merits at the time. The EU should continue to insist that Russia meet the standards it has agreed to under the Council of Europe and the OSCE, which are not EU standards but would be relevant in considering Russia’s application if it did eventually decide to apply. The prospect of closer relations with the EU, even if not linked to eventual membership, does serve as an incentive for the building of a free trade area with the EU and for political reforms in Russia aimed at meeting European standards on democracy and human rights. Therefore it would be counterproductive for the EU to rule out Russian membership as a matter of principle.

The Importance of a Long-term Perspective

279. Sir Roderic Lyne summed up the way in which the EU needed to view Russia in a long-term perspective. The EU “should be patient; and honest in its analysis, eschewing wishful thinking. It should recognise that it cannot determine the course of events within Russia”. The EU should understand Russia better, and weigh the consequences of its actions: “This does not mean appeasing; or suppressing criticism; or abandoning our principles. Russians do not respect weakness. But it does mean understanding Russia’s viewpoint and sensitivities; avoiding needless provocation; and above all not taking steps which play into the hands of the most backward and hard-line forces in Russia”. Sir Roderic concluded that “talk of a ‘new cold war’ is absurd. Russia does not represent a threat to the EU; and no sensible Russian sees a threat from Europe … it is not in our interests, any more than it is in Russia’s, for Europe to push Russia away. ‘Strategic Partnership has had to be put into cold storage for the time being, but it should not be dumped in the incinerator. It is a sensible long-term objective, and its time will come again.” \(^{121}\)

280. Sir Roderic expanded on this analysis when he appeared before the Committee, saying: “… we are now in a negative cycle in a long process of transition … which will very probably last for at least another five years and quite possibly 10 or 15, … so I believe that the European Union needs to calibrate its approach to the circumstances which currently exist in Russia … we should firmly reject ideas of neo-containment which are popular in some quarters, particularly on the other side of the Atlantic. We should firmly reject any approaches which are designed to isolate Russia. I think we need in the European Union to develop a shared analysis of what is going on there and a much better understanding of this within the EU” (Q 135).

281. The sensible approach for the EU is to situate its relationship with Russia in a long-term perspective. The European Union is not facing

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a new Cold War but EU-Russia relations are perhaps in a negative phase in a long process of transition which could last for some time. Despite the difficulties, Russia cannot avoid dealing with the European Union on trade, on competition, on customs and frontier controls, and on a variety of other issues involving the European Union’s common standards and regulatory procedures. Even when either side loses sight of it, they are bound by an inescapable common interest.

282. In an increasingly interconnected world, both Russia and the EU have an interest in co-operating on long-term global issues, such as the environment and climate change, as well as on key foreign policy issues, such as Iran, which have a direct impact on their interests.
CHAPTER 8: CONCLUSIONS AND RECOMMENDATIONS

Chapter 2: Russia Today

Russia: a European Country

283. Russia is a country of substantially European history and culture whose government and many of whose political elite regard it as a European country. However, most Russians do not think in these terms because they regard themselves as Russians, first and foremost. Russia shares a border with the European Union, with which it is bound by numerous ties of practical interest. Consequently, the EU and Russia have a mutual interest in building a close relationship, and the need for a practical cooperation with Russia in areas such as border controls is greater than with, say, India or China.

284. The EU should resist any attempts to isolate Russia, which would not be in the interests of the EU, but should rather pursue a policy of engagement at all levels and in all policy areas. In practice what matters are the concrete measures for developing that cooperation between Russia and the European Union which both know is necessary. The EU should recognise that the illusions entertained in the 1990s about the speed of Russia’s transition to democracy have hampered the EU’s efforts to deal with a newly assertive Russia. The current difficulties in the relationship should not weaken the EU’s determination to build a long-term partnership with Russia, based on dialogue, trust and common interests.

Recent Russian History

285. For Russians of all classes the 1990s were a time of national and personal humiliation. For many of them, it was also a time of deep poverty. However unfairly, many Russians attribute their troubles to the attempt to impose on them a system which they now consider as unsuited to Russian conditions. They put the blame not only on the Russian politicians of the 1990s and their Western supporters, but on Western ideas of democracy.

286. President Putin brought stability back to Russia. Associated with this has been an increasing trend to restrict the freedoms of political opponents and the media. Russia is not going back to the days of Stalin, or even to the days of Brezhnev. It is now more open than ever before. For many Russians the restrictions on political freedom have been a price worth paying.

287. Russia’s failure to fulfil the high hopes of the early 1990s that Russia would become a democracy, working under the rule of law, and with human rights, a free media and civil society have led to disappointment in the West. The changes needed to transform an authoritarian continental empire need to go very deep, and are likely to take decades if not generations. The sense of disappointment is mutual. For many Russians the West’s moral standing has been severely diminished. They are disillusioned by their experience of the market economy and the Western model of democracy and see little reason to listen to western criticism or prescriptions.

288. All indications are that the initial period of Mr Medvedev’s presidency will be characterised by a high degree of continuity with the policies of President Putin. Mr Putin, whom Mr Medvedev has appointed as Prime Minister, will
continue to exercise substantial power and influence. The extent to which Mr Medvedev will follow up his recent statements, including those on strengthening the rule of law, with concrete action remains to be seen.

The Economic Situation in Russia

289. The Russian government has not abandoned its consistently declared objective of modernising the Russian economy so that it can compete with the best. However, the pressure to take painful reform measures has diminished.

Problems for the Economy

290. The Russian economy is currently growing, buoyed up by high energy prices, but the prospect for the medium and long term is uncertain. Many questions remain about potential weaknesses and the threats these hold for its future prospects. Among these are demographic decline, which has implications for both Russian economic and security policy; the failure so far to diversify away from reliance on natural resources; and the failure to press ahead with market reform. The EU should continue to support Russian reforms in the economic sphere, which should be of benefit to both Russian and EU firms.

291. The Russians are unlikely to change their views on the need for substantial state involvement in the economy in the near or medium term. They seem, however, to accept that large parts of the private sector should operate free from state control. Both of these aspects of Russian policy have implications for EU policy and they are important for European business, which has largely and enthusiastically invested in the private sector of the Russian economy, and is generally making large profits as a result. The EU should where possible encourage further Russian steps towards improving the climate for foreign investment to provide the best environment for continued investment by European businesses in Russia.

Chapter 3: The Institutional Framework for Russia-EU Relations

The Institutions involved in EU-Russia relations

292. We agree with our witnesses in both the Council Secretariat in Brussels and the Commission Office in Moscow that the passage of the Lisbon Treaty should make it easier to co-ordinate and execute the Union’s policies towards Russia, and therefore make them more effective. A modest increase in numbers in the Moscow office would provide the additional skills needed. In addition, the mechanisms for cooperation between the Council Secretariat, the Commission, and the Member States missions in Brussels should be strengthened.

The Partnership and Cooperation Agreement

293. It is not clear to us how much interest the Russians will have in negotiating a new legally binding agreement similar to the current PCA with normative aspects on human rights. Although it will not be easy, we believe that negotiations on a replacement Partnership and Cooperation Agreement should be started in 2008. An attempt should be made to enshrine the principles of the Energy Charter Treaty and the Transit Protocol in the new
agreement or as a Protocol to it (See Chapter 5). Meanwhile the present PCA should continue to be rolled over.

Chapter 4: Building Closer Cooperation through the Common Spaces

The Common Economic Space

294. The European Union should actively promote the widest possible engagement of Russia in international and multilateral institutions; it should resist any attempt to remove Russia from the G8; it should call for the early entry of Russia into the WTO. Any remaining minor disputes can be dealt with under the WTO’s dispute resolution mechanisms after Russia has joined the WTO. The European Union should in due course promote Russia’s membership of the Organisation for Economic Cooperation and Development (OECD).

295. It is in the interests of the EU to engage the Russians on climate change to a greater degree than at present, despite the Russian reluctance to engage fully.

The Common Space of Freedom, Security and Justice

296. The European Union can help to ensure that ethnic Russians living in the Baltic states are given equal treatment under both national and EU law. The EU can help to manage these understandable sensitivities.

297. We welcome the solidarity that the EU has shown with the UK on the question of the extradition of Andrei Luguvoi.

298. In the last few years, progress has been made in several areas of EU-Russia cooperation on justice and home affairs issues. However, serious questions remain about the commitment of the Russian authorities to the rule of law and the independence of the judiciary, especially in politically sensitive cases. The EU should continue in its efforts to promote Council of Europe, OSCE and other relevant standards with regard to the rule of law, the independence of the judiciary, and judicial processes in Russia. These are standards which Russia has accepted and is committed to upholding.

The Fourth Common Space: Research and Education, including Culture

299. We deplore the attacks on the British Council and its staff and consider that they are not motivated by its activities, but are a part of a wider political strategy to pressurise the UK and the EU into giving ground on other, unrelated issues. Russia’s approach is unacceptable and violates several bilateral and multilateral agreements that Russia has ratified. It is moreover not consistent with a desire to make genuine progress under the Fourth Common Space. The Russian position that this is a purely bilateral matter between them and the UK is neither convincing nor sustainable. The EU should continue to support British efforts to find an early solution over the status of the British Council.

300. We welcome the efforts by the EU and Russia to further research cooperation under the Fourth Common Space. The European Union should continue actively to facilitate all forms of contact with the Russian people, including the provision of scholarships and exchanges and the further simplification of visa procedures for students. EU Member States, and in
particular the UK, should encourage the teaching of the Russian language in its schools and universities.

Chapter 5: Energy

Russian Oil and Gas Production

301. There are serious concerns about whether Russia can supply sufficient gas and oil to meet its current and foreseeable domestic demand and international commitments. In the face of this probable shortfall Russia will need greater efficiency and foreign capital. It is unlikely however that these needs will force the Russians to change their ways and there is little chance at present that foreign companies will be allowed by the Russians to acquire ownership of Russia’s strategic oil and gas resources. However, this has not deterred, and should not deter, European companies from seeking opportunities to invest in the country.

Energy Politics

302. In the current situation it is uncertain whether Russian policy is the action of a country simply pursuing its economic and commercial interests in an old-fashioned and mercantilist way, or whether Russia intends to use its energy exports as a political weapon to impose its will on neighbours and partners. Since a number of gas pipelines run through countries such as Ukraine whose bilateral relations with Russia can affect supplies to Western countries, the EU Member States should therefore take active and coherent measures, involving common funding where necessary, to diversify both sources of supply and transportation routes, including pipelines such as Nabucco, even where these are not obviously commercial (though recognising that Nabucco will not on its own solve the problems).

303. The market will sort out many problems for the supply of gas, as it did after the first two oil shocks. However, on its own the market will not rapidly produce the right results, and considerations of security of supply need to enter into the equation.

Improving the EU’s security of supply and The Third Energy Liberalisation Package

304. For the EU as a whole secure and competitive energy supplies are a highly desirable objective. The EU should further formulate its own energy policy, using the Commission’s proposals on energy liberalisation as its basis. There are ways in which security can and should be improved, notably by having a better internal market in energy, with grid inter-connections and storage, so that if one country has an energy problem with Russia or another country, there are alternative sources for electricity or gas.

305. The creation of genuinely competitive energy markets within Europe and the creation of Europe-wide energy grids should be a primary objective of EU policy. Even those countries (including the UK) that do not import significant quantities of Russian gas directly are vulnerable if supplies to their continental partners are interrupted; or if there is a prolonged period of cold weather. Exposure to a volatile spot market, without adequate storage facilities, and without long term contracts, mean that they could find themselves with soaring energy prices and gas supplies severely curtailed.
Alternative supplies from Norway, even where they are available in sufficient quantity, will not be price competitive. Germany may be reluctant to surrender the competitive advantage it receives from its well developed gas and electrical systems and long term contracts, or France its relative security arising from the scale of its nuclear industry, but agreement between the UK, France and Germany will be a pre-requisite for a genuinely effective market combined with grids and storage systems.

306. Implementing the Commission proposals on the Third Energy Liberalisation Package will not be easy, given the diversity of view among Member States. The collective negotiating strength of the Member States is at present seriously undermined by the willingness of each of them to go its own way. A degree of structured cohesion is necessary if EU energy policy towards Russia is to be effective.

A European Energy Policy towards Russia?

307. We doubt whether the ECT and the Transit Protocol are the right vehicles to achieve the EU’s objectives because of Russian objections. There seems little point in expending further political capital on trying to persuade the Russians to ratify the Energy Charter Treaty and the Transit Protocol as they stand: they are not going to do so.

308. If negotiations get under way later this year for a new PCA the EU should be prepared to explore with Russia whether that instrument could provide a legally binding framework for incorporating energy provisions such as those contained in the ECT.

Chapter 6: The Common Neighbourhood and International Security Issues

EU-Russia Relations — The Wider Context

309. The official Russian view of the international developments of the last two decades is very different from the West’s. Russians draw the conclusion that Russia’s interests do not necessarily coincide with those of the West. They believe that it is up to them to defend their interests, as they understand them, by the best means at their disposal. Most Russians no longer accept that Western countries represent a valid model to follow, both in terms of Russia’s domestic affairs and in terms of its foreign policy.

310. The Russia-United States relationship has always been a key determinant of EU-Russia relations. The attitude of the new US administration will be extremely important and the EU will need strong and direct dialogue with the new administration on Russia.

311. The EU should also listen more carefully to what the Russians say. The EU’s policy-making will be less effective and it will be unlikely to develop its policies towards Russia successfully if it does not understand their views and bear them in mind. That does not of course mean that the EU should not challenge Russian policies and actions if it thinks it necessary.

The Common Neighbourhood

312. The common neighbourhood in the Russian “near abroad” is an area in which both the Russians and the EU have close geopolitical interests. It is
therefore a particularly sensitive area and should be treated as such by both parties.

313. We believe the EU should consult in depth with the Russians over all aspects of the European Neighbourhood Policy with regard to countries which were formerly part of the territory of the USSR, but should not give them a right of veto over EU policy.

314. While Russia may see the EU merely as an unwelcome newcomer and rival in Central Asia, the EU should take account of Russia’s interests and concerns in the formulation of its policies towards the Central Asian countries. Beyond this the EU should seek to engage the Russians in a constructive dialogue about the mutual relationship with the Central Asian countries, and persuade Russia that democracy and prosperity in these countries—which are likely to be strengthened by their relationship with the EU—are also in Russia’s interest.

International Issues

315. Russia’s steadfast backing for Serbia, including in the UN Security Council, contributed to Serbia’s intransigence over the final status of Kosovo. This was one of the factors leading to the failure of the Serbs and Kosovars to reach an agreement through the UN-brokered process in 2007. The EU should recognise that Russia has expressed concerns about separatist movements in Russia and in countries near Russia. The EU should seek to persuade Russia to moderate its position and to encourage the Serbian authorities to show greater flexibility on the status of Kosovo.

316. The Russians may regard the lack of unity between EU Member States on the question of recognition of Kosovo as some justification for their position, despite the decision to proceed with the EU mission to Kosovo. The sooner this disunity is ended or is reduced, therefore, the better.

317. The Russians can be co-operative where there is an identifiable common objective; to some extent this is true in Iran where the negotiations are perhaps the most striking example of the CFSP machinery at work with the Russians. There has also been good cooperation with the Russians over anti-terrorism, and this needs to continue in the future. In general, however, the Russians have not been much impressed by the CFSP. Over Kosovo the best that can be hoped for is an agreement to disagree which does not spill over into other areas.

Chapter 7: Managing the EU’s Strategy towards Russia

Common Values: Human Rights and Democracy

318. Progress on democracy and human rights in Russia will be slow. Meanwhile the European Union has no choice but to deal with Russia as it currently is, imperfect though it may be in many ways which the EU considers of fundamental importance. Criticism may well be necessary from time to time if the Russian government falls short of the standards which both sides have accepted, for example in the Council of Europe and the OSCE. However, the European Union should consider carefully before issuing strongly critical public statements about Russian actions of which it disapproves, as it would do with any other country.
Negotiating with Russia

319. The EU does have considerable leverage in its dealings with Russia deriving from its position as Russia’s largest trading partner with a market of almost 500 million people. Other links, particularly in the economic and investment field, but also through human and social ties, add weight to the EU’s hand. The mutual dependence in energy (as supplier and customer), is an additional important factor, as we have noted.

320. The EU will always be more effective when it can agree a united approach in its dealings with Russia. This particularly applies when it is negotiating on a basis laid down in Community law (e.g. the common trade provisions of TEC Article 133). When the EU’s leaders stand together, as Chancellor Merkel and President Barroso did at the Summit with Russia in Samara in May 2007, the EU can make maximum impact. Too often, however, Member States act in a way which allows the Russians to drive wedges between them. In future the Member States need to give a much higher priority to standing together than they have done in the past. Once they have drawn up a new strategy for relations with Russia, they should be consistent in applying it.

321. Without allowing any one state or group of states to dominate EU attitudes towards Russia, the European Union and its members have a duty to support vigorously and by all diplomatic means any Member State which Russia chooses to pressurise in an unreasonable and overbearing way.

322. We consider that the importance of building a stable and strong long-term relationship between the EU and Russia based on mutual trust and understanding is greater than ever. This, combined with a hard-headed and unsentimental approach by the European Union can help to ensure that the relationship is productive rather than the opposite. The Russians should thus be able to see that it is in their own interests to work productively with the EU.

323. The EU’s attitudes and policies towards Russia have an uncoordinated character. In order to better design and coordinate its overall strategy towards Russia, the European Union should rethink its current policy towards Russia as a matter of priority. An updated approach should be drafted as a collaborative project between the Commission and the Council Secretariat and approved by the Council of Ministers. It should be discussed by the European Council at one of its forthcoming meetings.

Russia membership of the EU?

324. The issue of Russia’s potential membership of the EU does not currently arise. In the unlikely event that Russia did eventually apply, and if it was judged that Russia qualified, the European Union would need to consider the application on its merits at the time. The EU should continue to insist that Russia meet the standards it has agreed to under the Council of Europe and the OSCE, which are not EU standards but would be relevant in considering Russia’s application if it did eventually decide to apply. The prospect of closer relations with the EU, even if not linked to eventual membership, does serve as an incentive for the building of a free trade area with the EU and for political reforms in Russia aimed at meeting European standards on democracy and human rights. Therefore it would be
counterproductive for the EU to rule out Russian membership as a matter of principle.

_The Importance of a Long-term Perspective_

325. The sensible approach for the EU is to situate its relationship with Russia in a long-term perspective. The European Union is not facing a new Cold War but EU-Russia relations are perhaps in a negative phase in a long process of transition which could last for some time. Despite the difficulties, Russia cannot avoid dealing with the European Union on trade, on competition, on customs and frontier controls, and on a variety of other issues involving the European Union’s common standards and regulatory procedures. Even when either side loses sight of it, they are bound by an inescapable common interest.

326. In an increasingly interconnected world, both Russia and the EU have an interest in co-operating on long-term global issues, such as the environment and climate change, as well as on key foreign policy issues, such as Iran, which have a direct impact on their interests.
APPENDIX 1: SUB-COMMITTEE C (FOREIGN AFFAIRS, DEFENCE AND DEVELOPMENT POLICY)

The Members of the Sub-Committee which conducted this Inquiry were:-

Lord Anderson of Swansea
Lord Boyce
Lord Chidgey
Lord Crickhowell
Lord Hamilton of Epsom
Lord Hannay of Chiswick
Lord Jones (from November 2007)
Lord Lea of Crondall (until November 2007)
Lord Roper (Chairman)
Lord Selkirk of Douglas (from November 2007)
Lord Swinfen
Baroness Symons of Vernham Dean
Lord Tomlinson (until November 2007)
Lord Truscott (from November 2007)

Declaration of Interests

Lord Hannay of Chiswick

Chair, United Nations Association UK
Member, Advisory Board, Centre for European Reform
Member, Advisory Board, European Foreign Affairs Review

Lord Truscott

Former Associate Fellow, Royal United Services Institute for Defence and Security Studies, Whitehall
Former Parliamentary Ambassador, The Russian Federation and former Soviet Union, British Council
APPENDIX 2: LIST OF WITNESSES

The following witnesses gave evidence. Those marked ** gave both oral and written evidence; those marked * gave oral evidence only; those without asterisk gave written evidence only.

Amsterdam & Peroff, Barristers/Solicitors, on behalf of Mikhail Borisovich Khodorkovsky

Dr Derek Averre, University of Birmingham

Dr Vladimir Baranovsky, assisted by Sergei Utkin, Russian Academy of Sciences

* Katinka Barysch, Deputy Director, Centre for European Reform

* Sir Anthony Brenton, British Ambassador to Moscow

David Clark, Chairman, the Russian Foundation

* Professor Julian Cooper, University of Birmingham

* Council of the European Union

* The European Commission

The EU-Russia Centre

* His Excellency Mr Yury Viktorovich Fedotov, Ambassador of the Russian Federation

Dr Sabine Fischer, European Institute for Security Studies

** Foreign and Commonwealth Office

* Charles Grant, Director, Centre for European Reform

Group Menatep Limited (GML)

* Professor Phil Hanson, University of Birmingham

** Professor Dieter Helm, University of Oxford

Dr Iris Kempe, Centre for Applied Policy Research

* Professor Anatol Lieven, King’s College London

** Sir Roderic Lyne, former British Ambassador to Moscow

** Jim Murphy MP, Minister for Europe

Dr Sergei Prozorov, University of Helsinki

Pekka Sutela, Head of the Bank of Finland Institute for Economics in Transition (BOFTIT)

Dr Frank Umbach, German Council on Foreign Relations (DGAP)

Sir Andrew Wood GCMG, former British Ambassador to Moscow
APPENDIX 3: CALL FOR EVIDENCE

The Foreign Policy, Defence and Development Sub-Committee (Sub-Committee C) of the House of Lords Select Committee on the European Union has decided to undertake an inquiry into “The European Union and Russia”. The Sub-Committee is chaired by Lord Roper.

Since the Sub-Committee’s report on “EU Russia relations” in 2002, the international environment has changed and Russia has become more assertive. The enlargements of 2004 and 2007 brought the EU and Russia geographically closer together, with several of the new Member States now sharing a common border with Russia. The dialogue on foreign policy and security challenges has grown in depth and breadth, ranging from Kosovo and the Iran nuclear question to the Middle East. Russia exerts considerable influence in the EU’s neighbourhood and further afield in the Caucasus and Central Asia, and is therefore an indispensable partner for dialogue in relation to the EU’s eastern foreign policy objectives. Energy has also moved up the EU-Russia agenda, with unresolved issues including security of supply, the routeing of pipelines, and the control of European distribution and storage assets by state-owned Russian corporations.

Recently the EU-Russia relationship has suffered from mounting tensions on a wide range of issues, including missile defence, energy security and Russia’s domestic politics. The Russians tend to bracket the EU together with the United States and NATO as “the west”, which is sometimes seen as more of a threat than a partner. But beyond the rhetoric, Russia and the EU have a shared interest in maintaining good relations on a wide variety of commercial, economic, and international issues.

Russia has acquired a new confidence, with President Putin wielding a strong grip on the country and the buoyant economy being fuelled by high energy prices. However, this apparent stability hides several underlying factors of vulnerability. The economy is diversifying, and attracting inward investment, but it is still very dependent on the energy sector. Behind the apparent stability which President Putin has introduced, lie weak political and legal institutions, and a considerable degree of corruption. The political landscape is due to change, with parliamentary elections later in 2007 and the presidential election in 2008. Under the constitution President Putin has to step down and there is growing speculation about his successor.

The institutional framework for EU-Russia relations is based on the Partnership and Cooperation Agreement (PCA), which entered into force in 1997. The Agreement defines the main objectives of EU-Russia cooperation, establishes the institutional framework for bilateral contacts, and calls for activities and dialogue in a number of areas. It is a “mixed” agreement covering matters falling under both EU/EC competence and Member State competence. The relationship was extended with the adoption of a new basis for long-term cooperation in 2003, structured around four themes or “Common Spaces”: a Common Economic Space; a Common Space of Freedom, Security and Justice; a Common Space on External Security; and a Common Space on Research, Education and Culture. The PCA has now expired, but its provisions pending the negotiation of a successor continue to apply. These negotiations have been held up due to concerns among some EU Member States, notably Poland.
In the light of the importance of EU-Russia relations and the challenges the EU faces in meeting its foreign policy objectives, the Sub-Committee believes the time is right for a new inquiry into the European Union and Russia, focusing mainly on, but not limited to, foreign policy and security questions, which are at the heart of the Sub-Committee’s remit. It will also review the institutional framework for EU-Russia relations in the context of the forthcoming negotiations on a new Partnership and Cooperation Agreement and assess what added value the EU brings or could bring to the relationship with Russia over and above Russia’s relationship with individual countries.

In the framework of this inquiry, the Sub-Committee will consider written evidence. The Sub-Committee would therefore welcome submissions on following questions:

1. What are the main characteristics of the Russian political, economic and social system, and how are these likely to evolve in the future? What are the likely consequences of these trends for Russian foreign and security policy the future?

2. What is the nature of EU-Russia relations in political, trade, economic, environmental and social-cultural terms? What should be the fundamental objectives of EU policy with regards to Russia? What does the EU have to offer Russia in the context of a negotiation, and how can it best influence Russian thinking and policy?

3. Is the current institutional framework for EU-Russia relations, based on the PCA, the four “common spaces” and the “Northern Dimension” working well? What are the strengths and weaknesses of the institutional framework, and how could it be improved?

4. How successful have the EU’s wide range of cooperation and assistance programmes been in attaining their stated objectives, especially in the fields of foreign and security policy; and rule of law, democracy and human rights? What potential is there for the EU’s new cooperation and financial assistance instruments to be effective in Russia?

5. How can the EU contribute to managing relations between individual EU Member States and Russia? Have the Member States shown solidarity when under pressure from Russia? Is there a need for a greater unity and coherence of approach among the Member States towards Russia?

6. How is the EU perceived from a Russian perspective, and what are the underlying principles of Russian foreign policy towards the EU? Is there an increasing tendency for Russia to bracket the EU together with NATO and the United States, collectively labelled as “the west”? What are the implications of the above for EU policy towards Russia?

7. What impact does the foreign and defence policy of the United States have on EU-Russia relations? To what extent should EU-Russia relations figure as part of the transatlantic dialogue with the United States? What messages should the EU be seeking to convey?

8. How coherent is the EU’s overall policy framework with regards to Russia? To what extent have the Commission, the Council and the Member States adopted a harmonised approach to relations with Russia? Is there effective co-ordination between their cooperation projects and programmes?
(9) To what extent do Russian and EU interests and approaches coincide with regards to political developments in the countries of the former Soviet Union, including Ukraine, Belarus, Moldova, the Caucasus countries, and the Central Asian Republics? Can Russia and the EU collaborate to solve the frozen conflicts in, for example, the Caucasus and Moldova, including by working together in multilateral institutions such as the UN, the OSCE and the Council of Europe?

(10) What cooperation is possible between the EU and Russia on questions of foreign and security policy, including non-proliferation, nuclear safety, multilateral disarmament, and crisis management and peacekeeping? How should the EU seek to deal with Russia’s opposition to independence for Kosovo?

(11) What is the nature of the Russia-EU dialogue with regards to energy questions? To what extent is Russia an indispensable partner, rival or obstacle for the EU in its efforts to attain the objectives of its recently adopted external energy policy?

(12) What is the EU approach to the development of the political situation in Russia, including the rule of law, democracy, human rights, and good governance? What progress has been achieved by the EU, and how could the EU’s approach and policies be made more effective?
APPENDIX 4: NOTES OF MEETINGS IN MOSCOW

The following are informal notes of Meetings held in Moscow. Present at all meetings were the following members of Sub-Committee C:

Chidgey, L
Crickhowell, L
Hannay of Chiswick, L
Roper, L (Chairman)
Truscott, L

Meeting with Mr François Bellon, Head of Delegation of the International Committee of the Red Cross (ICRC) in Russia

11 DECEMBER 2008

Mr Bellon:

There have been no general hostilities in Chechnya for two years, and no humanitarian crisis since 2004. [Humanitarian crisis means, for example, starvation, serious death toll, etc]. Eight hundred members of the armed and security services have disappeared, so have thousands of civilians. But there has been a sharp decrease in the number of arrests which now runs at one a day, and there is now a more orderly process of trial and conviction or release. But the basic problem in Chechnya remains: the desire for independence will resurface at some point in the future.

Meanwhile a significant number of the Russian civilians have effectively left the whole of Northern Caucasus. There are few international fighters reported left there now. The rebels in the Northern Caucasus are now looking for a more Islamic agenda in the region, beyond Chechnya. Armed opposition groups are however attempting, since Beslan, to limit collateral damage and civilian casualties. Their capacity for conducting large-scale sustained operations is now limited.

In contrast to the 99% turnout in Chechnya for the election, the turnout in North Ossetia was only 58%.

More generally the declaration by the Clinton administration in the late 1990s that the Southern Caucasus was an area of US national interest means that the conflict of interests in the region has been further complicated. The Russian attitude to this and other encroachments has been and is that they do not like it, and the West will pay for it. The Russians’ signals are always clear for those who wish to read them, but some do not want to listen to what they say.

No foreign NGOs have been closed down as a result of the new law.
Meeting with Mr MARC FRANCO, Head of Delegation of the EU Commission in Russia and members of the Commission Office:

PAUL VANDOREN, Deputy Head of Delegation; HANS SCHOOF, Head of Operations; TANELI LAHTI, Head of Political Section; TIMO HAMMEREN, Head of Economic, Trade and Agricultural Section; ULRICH WEINS, Head of Science, Technology, Transport, Energy and Environment Section.

11 DECEMBER 2008

Mr Franco:

The activities of the Commission office are directed at two main subjects:

i) Systemic issues, such as the approximation of legislation, accounting standards, the training of judges, economic legislation, citizens’ awareness of rights and duties. On the latter the EU Commission has produced a Russian language handbook for schools.

ii) An active human rights programme.

The Russians prefer to conduct most of their contacts with the EU through Brussels. Consequently on many issues it is Ambassador Chizhov not Mr Franco who takes the lead. This makes life harder for Mr Franco, because it impoverishes the range of his contacts in Moscow. Moreover the Foreign Ministry, to which Ambassador Chizhov reports, is a factor for rigidity in Russia EU relations. The technical ministries such as the Ministry of Culture, or the Ministry of Economics, are more likely than the Foreign Ministry to go for mutually satisfactory deals.

[In answer to a question]. The Commission office in Moscow would not need to change very much when the Lisbon Treaty comes into force, since it was already very effective and well staffed: at most a couple of extra officials would be needed, including a military representative. It was probably amongst the three most effective European missions in Moscow.

The international co-ordination machinery in Moscow is chaired by Mr Naryshkin, a former Kremlin official. The Kremlin is of course the last resort: if there is an interdepartmental logjam, it can only be unblocked by the Kremlin. But the Kremlin machinery for dealing with European matters is inadequate.

The sectoral dialogues are going well, for example on the alignment of legislation. But the administration and the courts are not good at applying the legislation: hence the new Commission programmes to assist in improving the legal machinery.

There is no pressing need for a new PCA, but eventually one will be needed to define the ultimate objective of EU-Russia collaboration, e.g. the creation of a deep free-trade area.

Research and technology. There is plenty of potential for cooperation in areas such as renewable energy. Progress has accelerated in the past two to three years.

Education: the Bologna project and Erasmus scholarships are important. The Commission has produced a brochure in Russian setting out the possibilities for getting scholarships in the EU.

Progress was also being made in justice and home affairs.

[In answer to a question about support for the British Council] The EU is building up a cultural programme based on the activities of national bodies such as the
British Council, the Goethe Institute, the Alliance Française. The first EU cultural cooperation projects should start up next February. The British Council do not want the Commission to take up their problems for the time being, because a negotiation is still in process.

The Commission’s projects are now based on the principle that we should not lecture the Russians. Consultants from the West are barely used, and the exchanges are much more like consultations between professionals on both sides. The Commission is now more willing than before to discontinue projects which the Russians are not interested in, and does not attempt to seek credit where this seemed likely to be counter-productive.

Investment flows are now going in both directions. The Russians are wrong to believe that they have been discriminated against. On the aluminium takeover, Mordashev [owner of Severstal] has admitted that his bid for Acelor had been poorly put together; and the Russians claim that they never actually put in a bid for Centrica [formerly part of British Gas]. Europe’s long term interest is to get Russian inward investment. The Russians already have the right under the existing PCA to go to court if they think they were being discriminated against.

A number of new issues have arisen since the EU had agreed that the Russians should join the WTO: these included discrimination on railway tariffs; export taxes on timber; and Siberian overflights. Compromises are in sight on all of these. But the Russians are now less keen to enter the WTO than the EU is to get them in. They object to new conditionality being imposed. Their line is: ‘First let us in, then we will make suggestions and the compromises for which you were asking.’

On energy the main weakness is that there is no EU policy. The only part of the Commission that the Russians take really seriously is the Competition Directorate, since they know that they can be taken to court.

The Russians exaggerate the extent of EU protectionism. GazProm has 20 joint companies in Europe. An undue fuss is being made about the whole unbundling issue. The basis for reciprocity is simple: ‘We will let you into our pipelines and power lines, provided you let us into yours’.

Russian attitudes to Europe. Opinion polls show that the views of ordinary Russians are now far more pro-European than they were in 1998–9 [at the time of the economic collapse and the Kosovo war]. The EU has some 40 information centres throughout Russia.

The EU co-founded the European Studies Institute which is situated inside the Moscow State Institute for International Affairs (MGIMO). The Institute has a joint board of eight Russians and eight Europeans, and at any one moment about 200 students are doing evening courses there, mostly bureaucrats from the ministries in Moscow.

Mr Franco agreed with the Chairman’s suggestion that more effort should be put into providing distance learning. He would put this to the head of the Institute, Professor Mark Entin.

The EU’s co-ordination machinery in Moscow works particularly well.

**Mr Lahti:** reported on a presentation by the Russian ambassador at large on the South Caucasus: the Russians are playing hard ball, but they do not want trouble and would observe the rules. On the nomination of Medvedev he said that it was too early to judge.

Political Counsellors at EU Missions in Moscow, who had just been meeting, did arrive at common analyses.
Meeting with Mr YEGOR GAIDAR, Director, Institute for the Study of the Economy in Transition

11 DECEMBER 2007

Mr Gaidar:
The Russian economy is diversifying. The oil and gas sector is growing at 1% a year, but GDP is rising at 7% a year. The economy is diversifying into agriculture and manufacturing. Nevertheless the economy will be dependent on oil for the next 10 years. The prognosis of Mr Gaidar’s Institute is that there will be no serious problems in the next 10 years. They tested their analysis, but could find no signs of a possible catastrophe. The main point is that macro economic policy in Russia is in safe hands and is sensible.

The most serious problem is that for the next 10 years the budget and current account will be dependent on the oil price. Many countries which enjoyed a high oil price in the 1970s and 80s, including the Soviet Union, made bad mistakes. The Russian government has learned the lessons, and has created a reserve fund. It is not always easy, politically, to explain to the public why this money is not being spent on the country’s social needs.

‘Running Russia at $80 per barrel and at $20 per barrel are different jobs.’ An oil price of less than $40 a barrel would cause problems. If there were a 15 year low things would become difficult, but still easier than in the Soviet period. The economy started growing after the crash of 1998, even though oil prices then were low and remained low until 2004. Predictions of oil prices are in any case always wrong, so the task is to create a Norwegian size reserve.

The other main problem is the need to stabilise the pension fund. Mr Gaidar’s Institute made proposals last year, but they have not yet been fully developed. A pensions strategy will be approved after the presidential elections. Again Mr Gaidar is looking at the experience of Norway.

Foreign investment and shares in the oil sector have gone up with the announcement of Medvedev’s candidature for presidency. Those in authority would always be wary of foreign investment in the energy sector. But foreign companies are investing nevertheless. As one of their representatives recently said: ‘You are doing everything to push us out, but you are not doing enough.’

Rising inflation is also a problem, and indeed the government is not doing enough to sterilise it. Growth is therefore likely to be considerably lower. But the high value of the rouble allows a substantial increase in the purchase of machine tools for the productive sector.

Demography is also a major problem.

Europe is Russia’s major partner. It is a mistake for the Russians to think that they can dictate Europe’s energy policy. The Commission’s proposal for unbundling is important, promising, but dangerous: the EU needs to consider its policies carefully. The liberalisation of the electricity generating sector in Russia has been successful so far: something real is now happening. Russia’s energy requirements increased by 6.7% last year. As for the Energy Charter, the right way forward was to start a practical negotiation from scratch.

It will be easier to predict the course of future economic reform after the presidential election on 2 March. Reforms were successful in Putin’s first term, and a total failure in his second term. The socio-economic priorities should be
pension reform, health care, education, military recruitment and procurement, budgetary process reform (expenditure side—the revenue side is working effectively) and the energy sector. Russia is not at present a democracy.

On the WTO the Russians are strongly divided. A number of senior people think that membership of the WTO would not be to Russia’s advantage. The issue cannot therefore be used by the EU as a negotiating lever.

On the prospects for a new PCA, things should be much easier now the Polish election is out of the way.

Meeting on EU-Russia Relations with Professor MARK ENTIN, Director, European Studies Institute at MGIMO University; OLGA BUTORINA, Institute for Europe; DMITRI SUSLOV, Higher School of Economics; ANDREI BELY, Higher School of Economics; LAURIE BRISTOW, Deputy Head of Mission, British Embassy.

11 DECEMBER 2007

Ms Butorina: It was clear five years ago that there would be a cooling off in relations between the EU and Russia, partly because both are stronger than they were. There would be no breakthrough in the next two to three years. But longer term prospects were good: the two sides were doomed to cooperate closely. There are two main issues:

(i) The question of values;

(ii) Relations between the EU and the CIS countries: neither Russia nor of the EU have good strategies. A framework agreement is needed between the EU and the CIS which would make it possible to introduce elements of the EU acquis into the CIS countries.

Mr Suslov: Russia EU relations are in a state of stalemate, but not crisis. There will be a technical move forward during the French Presidency, and negotiations on a new PCA will then begin—but they will go on for ever. This is because of disagreements over energy, and because of the logic of the relationship.

An EU-CIS neighbourhood policy would ruin the Russian competitiveness and is therefore not attractive to Russia. The Russians are expected to adopt the EU acquis in areas which are of interest to European businessmen, but not necessarily for the Russians.

The proposal made by Prodi when he was President of the Commission that there should be ‘Everything except institutions’ is not understood by the people in the Kremlin who wrote Putin’s speeches. There is a disagreement within the Kremlin: do the Russians accept European norms? or do they insist on equality? The second tendency is beginning to prevail: that is evident from the marginalisation of Gref and Kudrin. The ‘Europeanisation’ of Russia goes against the revisionist logic of Russia, which was challenging the results of the Cold War. It is therefore very unlikely that the stalemate will be overcome unless EU policies are changed and there is an identification of genuine common aims in the areas of energy, democracy, and the CIS. EU enlargement has weakened the EU, because it goes against the logic of integration. The EU will have to conduct its relations with Russia as an independent player, with its own domestic system.
Mr Bely: The energy sector is the most problematic. There were no difficulties over energy supplies in Soviet times. But with the liberalisation of western economies there were big changes in the energy market. The UK's liberalisation in the 1980s was a consequence of the fact that the UK was self-sufficient in energy. Perceptions between Russia and the EU have changed and the romanticism of the earlier period has disappeared. The Russians do not see how the Europeans expect to be able to get a long-term supply of gas unless there are long-term contracts. Russia is in a period of deep transition: the Russian state has increased its share of the energy sector, but there are also measures of liberalisation. Europe only sees the former. Meanwhile the Commission is proposing to restrain foreign investment: but the only way forward is long-term planning of investment combined with the elimination of mutual restrictions.

Mr Suslov: It is a mistake to interpret the nomination of Medvedev as a sign that Russian liberalism is gaining the upper hand. Medvedev was and is the architect of Russian energy policy. The situation is still flexible but the West should not make false deductions. The way forward is to transform the issue of reciprocity: each side should be given an equal share in the pipeline arrangements of the other. There should not be an attempt to introduce ‘European standards’ for the energy market.

Lord Hannay: The idea of a multilateral EU-CIS framework agreement makes no sense: the Russians would surely not accept to be put in the same box as Ukraine and Georgia. The most sensible way forward is to base ourselves on the existing arrangements under the present PCA. Contrary to what some seem to think, the EU is not going to become a federation. But it is not moving rapidly in an opposite direction either. Attempts by the Russians to divide and rule would simply consolidate the EU's solidarity.

The energy problem is misrepresented. There is no problem about oil, coal, or LNG. The issue is solely one of gas supplies. Although we need to have a contractual framework, it should be negotiated from scratch: the Energy Charter is inappropriate as it stands.

Lord Truscott: The issues of climate change and energy efficiency need to be brought into any energy policy the EU devises.

Mr Suslov: Russia will deal bilaterally with the European countries when it can, and with the EU when it must. It would be a mistake for the EU to get obsessed with energy, since this will get in the way of other agreements with Russia. The best thing is to forget about the idea of an all embracing treaty, and concentrate on agreements on sectoral matters, with a political declaration to cover the whole.

Professor Entin: is optimistic. Developments in Poland are now more favourable. There has been a huge annual increase (20%) in the number of Russian travellers to Europe. Russian anti-monopoly policy is working well, although the Europeans never notice that. His institution is organising courses for officials from the Russian provinces to teach them about the EU.

Mr Suslov: It is crucial to create a new generation of specialists. Russia is unwilling to accept the EU agenda as the precondition for a better Russia-EU relationship.

Professor Entin: twenty-five million people are now connected to the Internet in Russia: they have access to all the information they want, whatever restraints are put on Russian television.
A technical problem is that the judgements of the European Court of Human Rights are not admissible in Russian courts because they are not in the Russian language. A special commission of European and Russian MPs should be set up to consider legislative proposals while they are still in draft to try and ensure that they are acceptable to the two sides.

**Lord Hannay:** We seem to have forgotten that foreign policy issues such as Kosovo, Iran, and the Middle East are bound to affect the EU-Russia relationship.

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**Meeting with Mr VLADIMIR MAU, Director, Working Centre for Economic Reform of the Government of the Russian Federation**

**12 DECEMBER 2007**

**Mr Mau:**

The Academy of the National Economy is directly subordinated to the government. It has just celebrated its 30th anniversary. The emphasis is on business. There are 3,000 MBA students, 5,000 undergraduates, and a thousand civil servants on short training courses. The Institute also does consultancy work for the government. It publishes studies in conjunction with the World Bank and the Gaidar Institute and is currently making a comparative study of corruption in state investment projects in a variety of countries.

The scope for further reform: are people willing to accept reform? The trouble with cheap money, such as Russia now enjoyed, is that people see no reason for reform. High oil prices are an impediment to economic development, and prevent structural and institutional reform. This is true even though Russia has managed so far to avoid the Dutch disease.

Eight years ago Mr Mau was optimistic about the future of the relationship between Russia and the EU: there seemed to be good prospects for a common market, even if Russia was not a full member of the EU. There is no reason why Russia should not accept the community acquis (though not the common agricultural policy and the social legislation), and enter into a relationship with the EU similar to that of Norway. Sooner or later this is inevitable. The prospect has however been pushed into the future because of the results of the last enlargement: it is natural and obvious that the policy of the EU will be dominated for a while by the new east European members, with their difficult historical experience of Russia. But in the long run there is no alternative for Russia to a closer association with the rest of Europe: 55% of its trade went to the EU. Talk of an ‘eastern dimension’ is senseless.

On the trickle down effect of high oil prices, Mr May thinks that oil riches stimulate imports rather than domestic production. The stabilisation fund is something to be proud of. At least it means that that sum of money has not been stolen. But most successful countries do not need the stabilisation fund. The problem is not that Russia needs to diversify its exports: it needs to diversify its domestic production. It is not clear whether the process of creating new state corporations is merely a transitional measure, as Putin has implied. Transitional measures can go on for a very long time. Though many disagree, the privatisation of the 1990s was successful. Privatisation in Britain in the 1980s had had three objectives: political, fiscal, and economic. It was possible to achieve all three in a stable society like Britain, but it was not possible in the turbulent Russia of the
1990s. At that time the most important objective was political: to make any comeback by the Communists impossible. Putin’s policy of buying up the oligarchs and eventually selling the new state corporations on the open market, could help to legitimise property ownership.

Russian energy policy is mostly driven by political considerations: it is not about investment or efficiency, but about the power of the elite. Foreign policy objectives are certainly not the primary aim. Higher oil prices had enabled the Soviet Union, towards the end of its existence, to import 42 million tons of grain a year.

A relationship between Russia and the EU similar to that enjoyed by the members of the EEA is a feasible objective. Mr Mau is currently engaged in discussions inside the government about the long-term development prospects for the Russian economy. All the participants implicitly assume that the benchmark for Russian development should be the European Union. The process is being slowed up by opposition from the Poles: their historical Russophobia would probably take up to 40 years to be overcome.

The depopulation of Russia is a serious problem. Government attempts to stimulate the birth rate will probably not succeed: there are no successful historical precedents. The high level of mortality could be overcome, however, with some basic social policies. There are problems with getting the right mix of migration, but it is clear that migration was necessary. The law has recently been liberalised. However what the Russians dream of is an “Australian” immigration policy: the planned attraction of skilled labour. Incidentally, historical evidence shows that economic growth is always associated with population growth.

Many Russian economists thought in the early post-Soviet years (2000 to 2003) that Russia should adopt the EU acquis. Probably only a third of those people think the same today. But even so, Russian legislation is still in practice being approximated to European legislation. But there are two important limitations on the process. The law enforcement mechanisms in Russia are not capable of ensuring the practical application of good laws; and the human capital available is inadequate. Cooperation in the four spaces of the PCA is helpful in this context.

On WTO membership, the situation is now thoroughly confused. The opposition to Russian membership from other countries is political not economic.

The first obstacle to improvements in Russia’s relationship with the EU is political, and stems from the last enlargement; the second obstacle is the attitude of European business, which is afraid of competition, especially in the agricultural field.

Meeting with MIKHAIL MARGELOV, Chairman; Ambassador VASILY LIKHACHEV; Ambassador IGOR ROGACHEV, Foreign Affairs Committee of the Federation Council
12 DECEMBER 2007

Ambassador Likhachev: Ambassador Likhachev, who had just returned from Switzerland and Luxembourg, had once again noted increased Russophobia in the European institutions. This makes it hard to reach sensible agreements. The matter is very subjective: emotions in Russia are much stirred by the American proposal to put missiles in Poland and the Czech Republic; by the American
position on Kyoto; and by Kosovo. It is necessary first to talk in a very frank way to sort these things out.

The relationship between Russia and Britain is of strategic importance: parliamentarians had a responsibility to carry things forward.

Mr Margelov: European Union matters are dealt with in Moscow in a number of different places. One is through the Parliamentary relationship between the EU Parliament and the Russian parliament. The second is inside the Kremlin, where Yastrzhembski is in charge. Before 2004 there was a special committee inside the Russian cabinet dealing with EU affairs, headed by a Deputy Prime Minister. When he was ambassador to the EU, Fradkov thought that the coordinating task could best be performed by the Russian mission in Brussels. But when he became Prime Minister, that arrangement broke down. There is a shortage of knowledgeable people in Moscow: only 20 to 30 people deal with EU affairs in the Russian ministries, compared with 300 odd people dealing with Russia inside the EU Commission.

The Russian economy is 55% dependent on foreign trade, and 70% of its energy goes to the EU. Therefore Russia is firmly on the hook. So we are interested in a positive agenda for Russia-EU relations. Work on the PCA needs to be revised. Polish meat (which actually comes from India) should not be an obstacle. Russia and the EU need to be more creative in working out a new agenda. The Russian economy is already firmly involved in the world economy: it can never close its doors again.

Mr Margelov had recently talked with the Estonian Commissioner, Simkalas, who had come up with a new idea. The Council of Europe parliamentarians and those in the European Union should get together to discuss all the relevant issues: it is a matter for politicians and bureaucrats.

The visa issue is also important. If a regime for free movement could be set up, it would be a death blow to the Russian isolationists.

Lord Roper: The negotiations over Kaliningrad could be a good precedent for negotiations on a visa regime. In Brussels the Sub-Committee had been much impressed by the progress being made in the Four Spaces. Is there a role for parliaments in developing the Northern Dimension?

Mr Margelov: The Russians are moving from the complex of superiority from which they suffered during the Soviet period through the humiliation which followed 1991 towards the building of a self-confident modern non-empire.

In Russia the WTO is a purely economic matter. But elsewhere politics have got involved and the Russians are being kept waiting outside Brussels. We need to move forward on the Energy Charter. The Russians will not ratify the Transit Protocol: the political elite is concerned at the prospect of losing control. What we need is more cooperation on things like research and development, refining, exploration, extraction.

Ambassador Likhachev: We are living in a period of contradictions in the EU-Russia relationship. In the political sphere there are ‘small volcanoes’. But when we talk of trade, although it might be inaccurate to talk of ‘integration’ with Europe, we can talk of a process of ‘integrative cooperation’. 52% of Russia’s trade is with Europe. 70% of its foreign investment comes from Europe. Russia is the third largest importer from Europe and the fourth largest exporter. Europe
provides 27% of the demand for its gas and 24% of the demand for its petrol. Politics cannot limit these facts. Poland is a very good example. Despite the bad political relationship, and the problem over meat, Poland holds the fifth position in trade with Russia.

A roundtable should be organised to discuss issues of harmonising legislation. ‘Juridical security’ is as important as military and other forms of security.

**Mr Margelov:** Russia wants to be inside the WTO and involved in working out the rules. The arrangements for Norway and Switzerland could provide models for Russia’s relationship with the EU. National security and sovereignty are very important to Russia—in the old Soviet Union, Russia had no separate identity. The closer we are the better it is for us.

**Lord Hannay:** There is no precise model for Russia’s relationship with the EU. Norway for example pays a large sum into the EU budget. Russia needs to have a specific arrangement of its own. But there are practical difficulties. The PCA with its four spaces are functioning reasonably well and producing results. But it is not a good long term basis for the relationship and a new agreement will be needed eventually. However there is no immediate pressure to negotiate one. A free-trade area could be the ultimate aim.

On energy we need a joint regulatory framework. One way forward would be to take elements from the existing Charter and negotiate them into a form that was satisfactory to both sides.

**Ambassador Likhachev:** Ambassador Likhachev wishes the British government would emulate the optimism of the British delegation. The MFA and the Kremlin have been working on the shape of a future EU-Russia agreement for more than a year. The PCA is not such a bad document: of the ten targets listed in article 3 of the PCA, the only one not yet attained relates to a free trade zone between Russia and the EU. WTO entry will solve that. On the whole Russian opinion is in favour of WTO membership, though some sectoral interests, such as agriculture, have their doubts. The Russians had hoped that there would be an appropriate declaration at the last EU-Russia summit, but none emerged, because of Poland. However the new Polish Prime Minister would come to Russia in February [2008], and the issue should then be resolved.

The new agreement should contain a small nucleus of norms, and then a series of agreements on particular sectors. It should be possible to negotiate in a couple of years. That is the Russian objective, and we are very interested in achieving it.

Russia is also a part of Europe.

The problem with Kyoto is the US position. The agreement that will succeed Kyoto in 2012 will depend on for its success on whether everybody signs up to it.

**Mr Margelov:** What we need now is confidence-building measures, like those we had at the time of détente. Confidence on both sides is much diminished. This is partly because of the election campaign rhetoric which had been heard in Russia in recent months and which is now hotting up as the presidential election approaches in the United States.
Mr Primakov: The Russian attitude to the European Union is very positive. EU enlargement had a less negative effect in Russia than NATO enlargement. We have to live together until Russia joins the EU. Russia does want a new agreement to follow the PCA. The chances for a successful negotiation are now greater as a result of the Polish election. The limitations will be lifted.

The Energy Charter is a complicated business. The Russians want to be treated as equals. If there is to be equal access it has to be equal at both ends. The Commission proposals on unbundling seem to be one-sided, since they prohibit foreign control. The Russian experts think the Commission proposals would damage Russian interests, and would be in breach of the PCA and the Energy Charter which provide for national treatment.

On the CFE the movement of Russian forces inside Russia is still restricted, but the Balts have not ratified the Treaty and NATO feels free to move forces into the Baltic states.

If Kosovo becomes independent there will be trouble between Abkhazia and Georgia. The European position is amazing. There will obviously be a knock-on effect in Bosnia. The Bosnian Serbs and the Croats will take advantage of the precedent, and there will be trouble in Macedonia.

Russia is now stable. So is the North Caucasus, despite occasional outbreaks. Chechnya is now run by Chechens. Mr Primakov does not like their methods in all things, but the war is now over.

The economic policy of recent years will continue. The aims are:

(i) To increase the share of Russian gross domestic product (GDP) in the world: this is already happening. Russia is consolidating its position in the world economy. Foreign direct investment into Russia is growing rapidly. Russia invests more in the United States than the United States invests in Russia. This shows that the Russian economic policy is on the right lines.

(ii) There was a dilemma in the 1990s: Russia had to choose between macroeconomic rectitude and a free market, or state involvement in the real economy. Now the dilemma is over. The macro economy is working, but the state is now involved. That is necessary for Russia, where the market still works inadequately, and we need to move away from a commodity-based economy. This is beginning to happen: two thirds of GDP is created on the basis of the domestic market, not on the basis of commodity exports.

(iii) Tax policy needs to be exploited as a tool of industrial policy, e.g. to build up Siberia and the Far East. Only 18 million people live beyond the Urals, right next to overpopulated China.

(iv) Government intervention is needed to bring about a dynamic innovation policy. Some people in the West argued that the problem would be solved by the market. But it was not, because there was not enough competition inside Russia. Now the state is doing it. The problem in the Soviet period was that fundamental science was very good, but it took a long time to implement.
There is an issue over the use of oil and gas money. The Ministry of Finance will not allow it be spent on social objectives and infrastructure, because they fear inflation. They are therefore spending their money on US Treasury bonds. Yet, although we have shown virtue by paying off state debt, corporate debt to overseas providers is now $300 billion.

Putin has suggested that the stabilisation fund be split in two. Half should be used as a reserve, and the remainder spent on social and economic projects. The original reformers [Gaidar and Burbulis] were unaware of the needs of ordinary people. The priority sectors for government expenditure are now education, health, housing, agricultural sector development, and also science absorbing industries.

There is no danger of a return to the Soviet Union: you should not be misled by the widespread and nostalgia for past Soviet greatness.

There are two main dangers:

(i) the tendency, enjoying backing in the West, of the so-called liberals and those with connections to émigré oligarchs, who want to return to the 1990s. These people are not supported by the Russian voter.

(ii) part of the state apparatus is getting too close to business. This leads to corruption.

The West should welcome the Medvedev nomination: he is a democrat.

On energy, Russia and the EU should start a negotiation which should be practical and not based on abstractions.

On the WTO, new obstacles are constantly raised to Russian membership. For example the Saudis were demanding free access to the Russian aircraft market even though they produce no aircraft. No doubt there were other forces behind them. The Georgians were also making difficulties.

As for the overall relationship with the EU, economic links are growing despite political difficulties. The future may be cloudy, but in the long run the horizons are clear.

Russia is irresistibly irreversibly committed to join the international community: but you do need to take account of us. We will not slavishly follow the US lead, as we did in the early 1990s.

Primakov agrees that there is a substantial measure of agreement between the EU and Russia over Iran, since both have the same long-term objectives. There is no agreement over Kosovo.

Meeting with ALEXANDER GRUSHKO, Deputy Minister of Foreign Affairs responsible for EU-Russia Relations.

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Minister Grushko:

Europe is our house and Russia is part of Europe, historically, culturally, socially. Europe is more than the EU. Russia is not planning to join the EU or NATO: Russia is too big and has to consider its relations with other neighbours, for
example China. It is preparing to build a general strategic partnership with Europe everything but membership. This is Russia’s policy towards the EU.

There is a huge potential for healthy economic relations and trade. Fifty to 60% of Russia’s external trade is with the EU. EU capital is bringing investment to the tune of 70% of investment in Russia. Cooperation is also extensive, especially from France, Italy and Germany, in areas such as space, airplane construction and science.

In international affairs and external security, the EU’s strategic concept is very close to what Russia wants. Russia’s position is very close to the EU’s on organised crime, mafias, Iran, Afghanistan and the Middle East. Other areas are international law, the non-use of military methods and eschewing unilateral actions. There is huge potential for combining efforts and synergy in specific cases.

As far as the 4th Space is concerned, culture and technology are close to the heart of Russia’s people. They are happy to have as many visitors as possible for exchanges. Russians are educated as European people, for example in British and French literature. They would like to reinforce the feeling of being in a common European civilisation. Russia wanted to make its education more Western. Russia had joined the Bologna process. There was much internal discussion which had been painful. The British Council, a subject for bilateral relations, had lacked a real basis. Some years ago it had been possible to open everything in the Russian Federation. There had been some problems about cooperation in this area, not just with the UK, which related to taxes and whether operations were profitable or non-profitable. The problems with the Germans and Spanish had been solved but there had been a lack of progress with the UK which had caused systemic damage to the Russian/UK relationship which was not in good shape due to many problems. To solve the British Council problem it would be necessary to re-open negotiations. Russia had been the first to ask the EU for no visas for diplomats. It had been criticised by the media but still considers that a modest example of visa free regime.

There are difficulties in the Russia/EU relationship. Russia managed to build capitalism with the help of the West. The Russians have the impression however that partners are still looking at Russia as in a transit phase. The results are quite impressive: 6–7% growth for 2 years, 10–12% growth in construction, 10–15 % growth in the processing industry. Russia is not therefore becoming just an energy producing state. Russia is trying to diversify and become more modern. Inevitably there will be competitiveness between the EU and Russia, as there is between the EU and the US. President Putin had said that Russia was not afraid of inward investment but Russia would expect to get the same treatment with the penetration of its investment in the West. Russia felt that there was a lack of trust: when a Russian firm bought 5% of EADC it was presented as a Kremlin plan, but it had been a commercial deal. This attitude should be overcome. Unbundling would lead to price rises as each part of the operation took a profit. Gazprom is therefore important as it can combine non-profitable and profitable operations. The EU should digest the new Russia which has our own vision which it will protect, on Kosovo, CFE, the Middle East, international law. But there are more things that unite Russia and the EU than divide them.

Policy in the EU is a kind of lowest possible denominator. Sometimes countries with problems with Russia are pushing the EU, for example, the Poles with the meat issue. This was near solution but a year had been lost. EU solidarity was becoming a ‘brake’ on building situations. There was a tense situation over Russia/EU relations. Russia was prepared to be very flexible. The MFA wanted to replace the PCA, but until it could be replaced, annual prolongation was possible. Russia was following developments in the EU closely. The phenomenon of non-citizenship in Latvia and Estonia should be tackled by the EU in accordance with European Conventions on
protection of the National Minorities. New Member States were still fighting on historical grounds: there were attempts to equate Nazism with Stalinism and to use history as a political instrument. This was not based on a desire to unite peoples. Russia would be patient but could see serious consequences. There were more possibilities than difficulties. Russia realised that the good relations between the EU countries would impact on EU policies but it did not like countries using the EU to solve specific problems. The Netherlands meat problem had been solved bilaterally. In the Polish case, Polish meat was acceptable, but there was a mafia in Poland which was exporting prohibited meat. The Commission tended to consider Russia’s policy as designed to divide Europe but Russia prefers strong partners.

In the regulatory sphere it was not good that the EU (the Commission) was inventing something for itself then trying to project it outside when is was not applicable to Russia. Sometimes the EU pushes, for example, with commercial directives. In the field of energy and electricity Russia is selling many power stations to international companies: ENEL has more than 50% in part of Russia. In the field of gas, predictability, transparency and long-term contracts were needed with guarantees which would make investment in gas pipelines worthwhile. The Commission wants to engage in nuclear fuels negotiations with Russia which breaches EU regulations. Negotiations should be on an equal footing. Russia was prepared to engage in a direct dialogue with individual partners. Russia will formulate regulations with or without the EU, using some of the _acquis_. Understanding where Russia stands is important.

There are two summits a year and 13 sectoral dialogues. But there is no body for conducting external political analysis, unlike the NATO/Russia Council (Russia was training Afghans in counter-narcotics with NATO). Where can subjects such as Transdniestria and Moldova be managed? Russia had been asked by the EU for help in Chad/Sudan. Russia will co-operate but we have to think over different types of such operations: led by the EU, led by Russia, common operations. On Kosovo the message from the EU was that they did not yet have a position, but Kosovo was becoming an EU problem. Russia wants the EU to refrain from any unilateral steps; to support the elements in the Security Council based on the work by the troika; and to support the idea of prolonging negotiations. It should not start with an EU position which cannot be changed. It was important to find a way of cooperating; the Contact Group had done good work. Russia did not exclude Joint Actions. Maybe Russia could cooperate with the EU, or some of the EU, on Nagorny Karabakh, but there was no structure. Russia was present in the police mission in Bosnia-Herzegovina though from the political point of view this was negative for Russia which did not participate in the decision-making process as it would wish.

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Mr Lukyanov: On the Balkans/Kosovo: Europe is destroying principles of international law. Why was Milosevic not stopped earlier? Russia has no interest in the Balkans. The EU is taking responsibility. Let them go ahead and let us see...
what happens. Negotiations should go on as long as possible. Kosovo’s status is absolutely unimportant for us. The Slavic brotherhood is no longer relevant. But no territory should be separated without agreement (in the case of Kosovo, the agreement of the Serbs). The position of Georgia will be much worse after Kosovo but Russia will not make use of the situation.

Mr Baranovsky: Chechnya is settled. Russia’s position on these issues has been consistent. Matters should be settled in accordance with international law. Russia is very emotional about Georgia; its view is that Abkhazia is a separatist issue. People are sympathetic to the West over Kosovo but think the West is being cynical. Their approach was not necessarily a fair one.

Issues of Russian trade tend to become political. It is not fair on the EU’s part to try to undermine Russia’s natural strengths. As far as possible Ukrainian membership of the EU is concerned, whatever the EU does in Ukraine is against Russia. Is NATO still the traditional adversary—maybe the EU now is.

Dr Markov: On the positive side, Russia, the EU and the UK have common interests in stability. On the negative side, the West has lost moral credibility. The 1990s were a catastrophe for Russia, but which the West considered as good. Cheney had criticised Putin but praised Kazakhstan because of the oil. Russia was trying to attain the ideal of democracy. Kosovo is important because if Kosovo declares independence, why not Abkhazia or South Ossetia. If Russia recognised the latters’ independence it would be in conflict with Georgia. Iran as an issue is more important than Kosovo. The Ukraine for us is not another country.

President Putin will be the number one at least for a period. Medvedev might stand down (after being elected President). At Davos some saw Medvedev as quite a poor performer. The Prime Minister’s powers can be increased without changing the Constitution—it could be done in the Duma. Putin would delegate the difficult problems. If Putin were to be appointed party leader, that would send a very bad message to the public in Russia and outside. Putin likes Russia to be a big country which is respected.

Dr Karaganov: The Russian and EU positions on Iran are not so far apart. The less the EU and Russia interfere in Ukraine the better.

Meeting on EU-Russia Energy Relations with VLADIMIR KONOVALOV, President, Petroleum Advisory Board; SERGEI DUBININ, CFO, RAO United Energy Systems (UES), formerly Board of Gazprom; REINER HARTMANN, Chairman, Energy Committee, Association of European Business (AEB), E.ON (Germany); SHAWN McCORMICK, TNK-BP; VLADIMIR MILOV, President, Institute of Energy Policy; LAURIE BRISTOW, Minister, British Embassy, Moscow

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Mr Konovalov: The Petroleum Advisory Forum is an association of Western oil and gas producers in Russia. Investors are looking at Russian law, especially the subsoil law, which has been under revision for the past two years. The Forum has advised the government to move in a market direction. This has not been altogether successful. The Government was now moving towards a law to restrict foreign investment in which foreigners would not be allowed more than 50% investment. Laws are getting bogged down and therefore clarity is lacking. For oil production over 90 cents in the dollar are taxed which is onerous. Taxes are based
on price and quantity, not profit. Western businessmen argue that this was regressive but the Government does not believe the oil industry. However, the Government is beginning to see that investment might not be forthcoming for developing new Greenfield sites in Siberia. There would be a geo-political dimension to big projects. The government was meant to be business-oriented and internationalist. Difficult times lie ahead but foreigners would be there.

**Mr Dubinin:** In the gas industry long-term contracts are vital to secure long term investment. Profitability for the producer and consumer should be equal. Russia was in the long-term Russian and European markets. In the longer term it could cooperate with other gas producers such as Iran. There is a good spot contract market. Nuclear energy is a possibility for the future particularly for its efficiency and the environment.

**Mr McCormick:** In September 2003 TNK-BP was created through the merger of TNK, Sidanco and most of BP’s assets in Russia; BP’s investment represented the single largest by a foreign company in the history of Russia. TNK-BP is primarily an oil company with some gas interests. The company currently produces 1.8 million barrels of oil equivalent per day—of which BP books half, representing 25% of its daily production. But TNK-BP only accounts for 10% of BP’s profits because of high costs pressures and tax take in Russia. After several year of double-digit growth, TNK-BP’s oil output is currently flat because most of it comes from older oil fields initially discovered/developed in the 1970s and 1980s which the company is working hard simply to maintain production. TNK-BP’s future lies in new “Greenfield” projects in which it is investing heavily and it expects to see overall production increase again next year. These are very complex, remote and expensive oil fields to bring on-line—they are ice covered for six months, and in swampy areas for the remainder of the year. For Russia, the largest and most important market is the domestic one, and for exports it is Europe where over 4 million barrels per day are shipped. TNK-BP is the largest exporter of Russian crude, with one out of every 20 barrels consumed in Europe being produced by the company.

In the Russian oil sector overall, nearly 75% of output is produced by “non-state” companies like TNK-BP, which in the gas sector an estimated 85% of production is from state companies. The largest consumer of Russian gas is, again, the domestic market and for exports it is Europe, not Asia, due to infrastructure and location of deposits. In the future, LNG could change that dynamic—and certainly China, Japan, South Korea and the United States are large potential markets.

As a normal course of business, TNK-BP regularly competes with other companies for new oil fields via auctions. The company has won around 35 such new permits in the last two years through this open and competitive process. In addition, TNK-BP has several large and new projects in its development “pipeline” which all require significant levels of capital, technology and trained staff. TNK-BP is fortunate to work in a country where the same amount of engineers graduate from universities annually as they did 20 years ago (this is not true in Europe or the United States). There is fierce competition between companies—and indeed other industries in Russia—for the best candidates, so the company must remain highly competitive.

It is right to say that large amounts of gas are not utilised effectively: estimates of gas flared range between 35–50 bcm annually—the equivalent of nearly half of UK annual demand. TNK-BP is investing $2 billion over coming years to reduce its share of that total.

**Mr Milov:** EU energy policies are based on markets. Russia talks of the unfairness of the 1990s when the oligarchs obtained their money in a controversial manner. Russia is the third largest exporter of coal in the world whereas previously it had
been a net importer. State owned enterprises were the least efficient, and it was this part of the energy industry that has been expanded. The price of oil has risen from $3.5 per barrel to $11 per barrel in 5 years. Russia has the potential to expand its energy sector, but redistribution in favour of the state prevents expansion and production has stagnated.

There are far fewer problems and challenges in the private sector than in the area covered by state control. As far as upstream is concerned, the Russians do not have off-shore experience. Sakhalin 1 and 2, in the hands of international oil companies (IOCs), were producing oil and would soon have gas. Sakhalin 3, 4 and 5, under state control, had nothing and the situation was no different from the mid 1990s. Unfortunately the Russian government was attempting to maximise profits for Russian-run companies and it sees the IOCs as competitors. The model of cooperation with the IOCs as minor partner will not work; the Government only wants IOC resources.

The policy thinking mentality gap between Russia and the EU is fuelling energy security concerns in Europe which is serious. The situation would not change soon. The EU has never been in favour of applying the Energy Charter Treaty (ECT) in their own countries. Article 20 in the Transit Protocol does not apply on the territory of EU Member States, and this destroyed attempts to apply it in Russia. A new agreement is a good idea.

Mr Hartmann: E.ON produces 37 billion cubic metres of gas per annum. It is involved in long-term contracts with Gazprom. It has significant investment in the power sector and recently acquired 5 power plants (in the privatisation of OGK4) at a cost of Euros 4.1 billion. The company found the auction to be well organised, highly professional and transparent, with the participation of several European companies. They now need to consolidate 5,500 people. This privatisation was driven by Chubais who announced a disastrous situation in the power industry. President Putin approved the action. The Russians are not too happy about the approach of Brussels to reciprocity.

The Russians will not ratify the Energy Charter Treaty, part of which—the gas transit elements—should be incorporated into the PCA. The oil and gas industries are indeed separate and different, with gas needing long-term commitment and projects. There had been very positive developments in coal, but merger of Russia’s largest coal producer, SUEK with Gazprom, could undermine competition in primary energy production.

Meeting with Association of European Businesses in the Russian Federation (AEB)

FRANK SCHAUFF, CEO, AEB; ROGER MUNNINGS, Member of the Executive Board, KPMG; JOERG BONGARTZ, Chairman of the Banking Committee, Deutsche Bank; DMITRY CHELTSOV, Chairman of the Transport and Customs Committee, Finland Post Corporation; MARIE RONDELEZ, AEB, Adviser on EU Affairs; Discussion moderator: Chris Bowers, Director, Trade and Investment, British Embassy, Moscow

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Mr Bowers: Many in the UK business community in Russia have a horror story or two about dealing with Russian bureaucracy, but most if not all are smiling
about their profits and future growth potential. Russian Government figures put the UK as the biggest investor in Russia. The UK has particular success in oil/gas and financial services. There are many areas of potential growth and large potential opportunities for UK companies pretty much across the board. But UK medium size industrialists tend to be more convinced of the need to explore or invest in India or China than in Russia, of which some still seem wary. A lot of this is to do with outdated perceptions of Russia. Of major UK companies, HSBC is doing well. Pilkington had trouble setting up but in one year has captured 17% of the Russian market. Boots is in 250 stores. As far as the rule of law is concerned, the Russians are making decent progress but implementation, as ever, remains a problem. The commercial law system is gradually improving and foreign companies are getting a better chance of a fair hearing and ruling. Many in the business community have been encouraged by Medvedev’s nomination. Medvedev is seen as “liberal” in the Russian context.

**Dr Schauf:** The Association of European Businesses (AEB) has nearly 600 members of which the largest groups are Germans, British and French. Most EU Member States are represented (except Malta, Slovakia and Slovenia). The AEB is growing fast with double digit growth of trade in Russia and three quarters of investment from the EU and several thousand companies. The mood is positive about Russia though some companies are facing problems on visas, work permits/immigration issues. Companies also face bureaucratic obstacles: more than 100 stamps are needed to open a chemical plant. Corruption plays a role, thought not a major one. It tends to consist of petty problems with militia on the street. Major companies do not encounter these problems as they can re-locate. There can also be problems with authoritarian structures. Trade Unions are in bad shape though there had been strikes at Ford in St Petersburg and trouble in the automotive industry. Growth rates are impressive. From the business point of view it was valuable that the Russians seem to be adopting some of the *acquis.* The proposal of Medvedev as a candidate for the Presidency is welcome as he is constructive and knows the Kremlin structure and Gazprom.

The AEB had visited Brussels and discussed the WTO issue with Frattini, Piebalgs, Alununia and Mandelson. The Russians say that others are more interested in Russia getting into the organisation than Russia is. Russia’s leaders are not so keen on membership; the problems concern Siberia overflights and timber. The issue of Polish meat had been resolved and it was hoped that the EU could now move on its relations with Russia.

**Mr Munnings:** President Putin was initially keen on WTO membership as legitimising, but he had drifted away as Russia became more powerful. He would probably like WTO membership during his Presidency but the EU would probably not be able to achieve it in time. Membership would however be an important part of the future framework where, together with Russia’s interaction with others, a change has been seen in the last 10 years. KPMG in Russia is the fastest growing business anywhere in the world. 90% of clients and 95% of employees are Russian.

The candidature of Medvedev for the Presidency is seen by “internationals” as a liberal and as a very positive sign. Russians at the liberal end of the spectrum are also happy. The Medvedev/Putin pairing would be popular. President Putin had originally been an internationalist, is now less so and there is uncertainty about his present position. From outside we need to help Russia to engage. This message was conveyed to Brussels during a visit and they had been shocked at the amount of detailed work which was being undertaken. In international
affairs, Putin has been interested in separate poles. The Russians feel European and want a strong Europe. They will pick the best practice from around the world, for example on corporate governance, though they tend to complain if something was not “Russian”. The AEB would produce written evidence for the Sub-Committee on what should be in the new PCA with Russia.

There has been a turn-around in Russia from the beginning of the century which extends to the regions where, for example, modern milking parlours could be seen. The Russians would try to regenerate the economy to produce wealth for the people and would put the home market first, creating national champions for this market. This could lead to international competitiveness. The Russian CBI had drafted a strategic industries paper for the government. Russia had traditionally had a strong scientific community and was keen on the security sector. On energy supplies the Russians could not decide where to go in addition to the Europeans: China or US. Gazprom was a company with strategic assets to the tune of 28% of the world’s supply. The top of the administration know Gazprom well. It was to be hoped that Chubais would sell off the electricity organisation and take over Gazprom.

There were problems caused by unbalanced media representation. When working in Russia one had to understand that what felt like confrontation is just the way the Russians worked. It is necessary to get past this, go straight to the subject and deal with it. Implementation of commercial law takes time but the Russians are pushing it forward. In the courts 70% of cases were won by the taxpayer/company in 2006. Russia just has the edge on China and India in terms of market development. Russian would be a hypercompetitive nation before people thought, and they wanted to be part of the world. What the EU had to offer was the financial sector. The EU is keen to develop the capital market. London could help without damaging itself. Within the EU the Germans and Italians do well, the Irish have some flexibility. Foreign firms are getting good quality MBA employees, though less so in Moscow because of the competition. Labour is not strongly represented but there is legislation on obligations to workers. Oil industry skills are in short supply worldwide and Russia is lacking in offshore skills and experience.

Mr Cheltsov: The issue of timber with Finland is not crucial though important. Finland constituted 6% of Russian trade with the EU countries. Russia was 12% of the Finnish trade (second to Germany which was 12.5%). The Northern Dimension is working. Customs problems have been a serious barrier to trade but a new customs code introduced in 2004 has made a dramatic change and relations with the customs authorities are improving. But major issues are being resolved and cooperation is working well.

Mr Bongartz: Foreign banks are not discriminated against though there is much to do on regulation. Banks, such as Société Générale and Deutsche Bank are doing well. Foreign banks are not allowed to set up branches but need subsidiaries. The Russians have lifted banking capital limitations to 50% and there is room for manoeuvre. Dialogue is good with the regulators and representatives of the Central Bank come to meetings. Discussions are underway about a better settlement system, for example on derivatives regulations. Pension reform is also under discussion. Sometimes people think the Russians are moving too slowly but the financial sector is booming, with over 40% growth recently. It would not slow down. Substantial funding comes from outside Russia.

Ms Rondelez: Discussions are underway on the *acquis* in the investment, banking and energy sectors. The Russians seem to be taking them on board as
the EU spread the *acquis* around itself. However, the Russians could react against this.
APPENDIX 5: GLOSSARY OF TERMS AND ABBREVIATIONS

AEB  Association of European Businesses
CER  Centre for European Reform
CFE  Conventional Forces in Europe
CFSP  Common Foreign and Security Policy
CIS  Commonwealth of Independent States
CMEA  Council for Mutual Economic Assistance
COE  Council of Europe
EC  European Communities
ECHR  European Convention on Human Rights
ECJ  European Court of Justice
ECT  Energy Charter Treaty
EEA  European Economic Area
EIDHR  European Initiative for Democracy and Human Rights
ENP  European Neighbourhood Policy
ENPI  European Neighbourhood and Partnership Instrument
EU  European Union
FCO  Foreign and Commonwealth Office
FDI  Foreign Direct Investment
G8  Group of Eight
ICRC  International Committee of the Red Cross
IOC  International Oil Company
LNG  Liquefied Natural Gas
NATO  North Atlantic Treaty Organisation
NGO  Non-Governmental Organisation
OECD  Organisation for Economic Cooperation and Development
OSCE  Organisation for Security and Cooperation in Europe
PACE  Parliament Assembly of the Council of Europe
PCA  Partnership and Cooperation Agreement
PSC  Political and Security Committee
SCO  Shanghai Cooperation Organisation
TEC  Treaty Establishing the European Community
UNFCCC  United Nations Framework Conventions on Climate Change
WMD  Weapons of Mass Destruction
WTO  World Trade Organisation
APPENDIX 6: MAPS

Two of the maps are reproduced by kind permission of the Secretary of the United Nations Publication Board. The gas pipeline map is reproduced by kind permission of the Energy Charter Secretariat.
APPENDIX 7: MINUTES OF PROCEEDINGS OF SUB-COMMITTEE C ON CHAPTER 7 OF THE REPORT

Thursday 1 May 2008

Present:
Lord Roper (Chairman)
Lord Anderson of Swansea
Lord Crickhowell
Lord Hannay of Chiswick
Lord Selkirk of Douglas
Lord Swinfen
Lord Truscott

The Sub-Committee considered the draft report.

Paragraphs 1–270 were agreed to, with amendments.

It was moved by Lord Roper, to delete the last sentence of paragraph 271 and to substitute—

“Whilst we recognise that the Russian government has no current wish to join the EU and is unlikely to want to do so in the near future, we hope that, one day, Russia may consider applying. Russian membership of the EU would be of inestimable value to relations between Russia and Member States of the EU as well as of great benefit to the Russian people.”

The Sub-Committee divided:

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The amendment was disagreed to accordingly.

Paragraphs 272–321 were agreed to with amendments.
APPENDIX 8: RECENT REPORTS

Recent Reports from the EU Select Committee

Evidence from the Ambassador of the Federal Republic of Germany on the German Presidency (10th Report, Session 2006–07, HL Paper 56)


Evidence from the Minister for Europe on the June European Union Council and the 2007 Inter-Governmental Conference (28th Report, Session 2006–07, HL Paper 142)

Evidence from the Ambassador of Portugal on the Priorities of the Portuguese Presidency (29th Report, session 2006–07, HL Paper 143)


Priorities of the European Union: evidence from the Minister for Europe and the Ambassador of Slovenia (11th Report, Session 2007–08, HL Paper 73)

Session 2007–2008 Reports prepared by Sub-Committee C

Current Developments in European Foreign Policy: the EU and Africa (4th Report, HL Paper 32)

Current Developments in European Defence Policy (8th Report, HL Paper 59)

Current Developments in European Foreign Policy (12th Report, HL Paper 75)

Session 2006–2007 Reports prepared by Sub-Committee C

Current Developments in European Defence Policy (1st Report, HL Paper 17)

Current Developments in European Foreign Policy (16th Report, HL Paper 76)

The EU and the Middle East Peace Process (26th Report, HL Paper 132)

Current Developments in European Foreign Policy: Kosovo (32nd Report, HL Paper 154)

Current Developments in European Defence Policy (34th Report, HL Paper 161)

Current Developments in European Foreign Policy (38th Report, HL Paper 183)
Minutes of Evidence

TAKEN BEFORE THE SELECT COMMITTEE ON THE EUROPEAN UNION
(SUB-COMMITTEE C)

THURSDAY 19 JULY 2007

Present
Anderson of Swansea, L
Boyce, L
Chidgey, L
Crickhowell, L
Hamilton of Epsom, L
Hannay of Chiswick, L
Lea of Crondall, L
Roper, L (Chairman)
Swinfen, L

Examination of Witnesses

Witnesses: SIR MARK LYALL GRANT, Political Director, MR MICHAEL DAVENPORT, Director, Russia, South Caucasus and Central Asia Directorate (RuSCCAD), and MR JASPER THORNTON, Foreign and Commonwealth Office, examined.

Q1 Chairman: Sir Mark and Mr Davenport, welcome to the Committee. We are just beginning, as you know, an inquiry into relations between the European Union and the Russian Federation and we very much wanted to start taking evidence from the Office on some of these broad themes. You will, I think, know already quite a number of members of the Committee who have met you at various stages in your earlier career and we are very pleased to see you this morning. I would like to start with the first question. I wonder whether you would like to characterise the state of the EU-Russian relations at present and say something about the extent to which Russia's interests and those of the European Union converge or diverge not only in political and economic, but also wider international, affairs. What interests does Russia have in developing a cooperative relationship with the European Union?

Sir Mark Lyall Grant: Thank you, my Lord Chairman. Michael Davenport is the Director for Russia and Central Asia and behind him is Jasper Thornton who is the real expert on EU-Russia, so, if you throw me some really difficult questions, I might have to ask him for some help. I think the relationship between the European Union and Russia is an important one because there are clearly some important common strategic economic and political interests. A great deal is made about the amount of dependence that there may be on the European Union side on Russian oil and gas and it is true that around a quarter overall of EU oil and gas imports do come from Russia, much less obviously for the United Kingdom, but for the EU as a whole, and some countries in the European Union receive all their gas essentially from Russia. The converse is also true and the European Union is by far Russia's largest export market and the gas exports in particular are a very high percentage of the contribution to Russia's GDP. Russia also needs European Union direct investment, particularly in the technology in the hydrocarbon sector. The City of London has become the centre of choice for Russian business in terms of capital and we are seeing in London a record number of initial public offerings by Russian companies, so there is a very strong coincidence of interest. There are also the wider political reasons why the EU and Russia need to cooperate, and one can talk about Iran or Kosovo, the Middle East, Sudan, climate change, the global challenges in terms of counter-terrorism, in terms of non-proliferation and in terms of drug-trafficking and organised crime. All those issues, I think, are common challenges for both the European Union and Russia. We have based the overall strategic relationship, as, my Lords, you will know, on the Partnership and Co-operation Agreement which is now 10 years old. It started in 1997, which sets a reasonably good framework for that sort of engagement across the board between the European Union and Russia. However, I think it is fair to say that there are difficulties, that there is an increasing concern within the European Union about some of the trends in Russian policy, both internally and externally, which we can come on to, and also the number of bilateral disputes that Russia now has with members of the European Union, one of which, the ban on Polish meat imports, is actually preventing the conclusion of the mandate for a new Partnership and Co-operation Agreement which has been discussed over recent months within the European Union. The final point I would make, my Lord Chairman, is that of course, although the European Union-Russian partnership is important, there are quite a number of other important fora in which to engage with Russia on these issues, to name but a few, the G8, the UN Security Council, the
Lord Anderson of Swansea: Russia partnership is a subset of that wider Russian
come under the wider EU umbrella. So the EU-
deed commercial links they may have which do not
they may have and cultural links they may have or
EU Member States, have their own bilateral relations
that, all the major EU Member States, or really all the
group dealing with Kosovo and, in addition to all
there are a number of ad hoc groupings, such as what
important fora in which we engage with Russia on
OSCE, the Council of Europe, and all of these are
Sir Mark Lyall Grant, Mr Michael Davenport and Mr Jasper Thornton

Q2 Lord Anderson of Swansea: Sir Mark, welcome.
Do you think that perhaps there is a greater danger
of misunderstanding of Russia by the West because
of an attempt to create Russia in our own image and
to forget the history of Russia, the few windows of
democracy, Kerensky query Yeltsin, that the
prevailing history has been that of authoritarian rule
and that equally the geography suggests that they are
going to have major interests which diverge from our
own? Should we not perhaps, rather than expect in
these grand fora to reach agreements across the
board, focus rather more on areas where there is a
perceived and certain common interest between
ourselves and the Russians in areas like counter-
terrorism and other areas like that?

Sir Mark Lyall Grant: I think that is a very fair point,
my Lord. We are very conscious of Russia’s history,
which is different from that of most European
Member States, but equally Russia does see itself as
a European country. Certainly the leadership in
Moscow does see itself as a European country and it
does aspire to be a member of many of the same
international groupings as countries in the West,
such as the G8. The G7 was enlarged to the G8
precisely to bring Russia on board, despite the fact
that its economy in real terms would not have
justified Russian membership of the G8. Even now,
although the Russian economy is doing very well, the
Russian economy is only the same size as Spain’s,
about 40 per cent of the UK’s economy, so that in
itself would not justify Russian membership of the
G8, but the G7 was expanded to the G8 in
recognition of the fact that Russia did have this wider
strategic global role. However, together with the
rights of membership of these international
organisations, comes responsibilities, so I think it is
reasonable for other members of the groupings to
expect Russia to abide by the essential values of those
groupings, and of course some of those do go to
questions of democracy and human rights. So,
although of course we have to see that in the
historical context, and it is right to do so, I do not
think it would be right for the European Union to
ignore concerns that we have on trends in democracy
or trends in human rights in Russia simply because
there were other important strategic issues to discuss.
I think within the all-encompassing Partnership and
Co-operation Agreement clearly it will be easier to
make progress on some issues than it will be on
others. There has been good progress on counter-
terrorism, there has been good progress on energy
issues and there has been good progress on co-
operation on some of the global issues. There has
perhaps been less progress on questions of
democracy and human rights, as an example, but I do
not think we should compartmentalise too much. I
think what we are looking for in the new Partnership
and Co-operation Agreement is an agreement that is
comprehensive and sets a framework for discussion
of all of these issues, even if some of them are quite
difficult.

Q3 Lord Hamilton of Epsom: Economic ties are
going to be very important between the EU and
Russia. We are very much bemused at the moment
by the oil and gas situation which gives the impression of
a booming economy, but that is about all there is
really at the moment. I would really like to know how
you view the Russian economy. It is extremely lop-
sided, so where is it going and what role can we play
in helping that along?

Sir Mark Lyall Grant: My Lord, the Russian
economy is doing quite well obviously on the back of
the hydrocarbon sector, there is no question of that.
It is not perhaps as diverse as the Russian authorities
would like it to be, but there are other sectors. The
defence sector is very strong and there are quite a
lot of state-owned industries that are also doing quite
well in other sectors, so it is not entirely based on
hydrocarbons, although it is true that the recent
rapid growth has been largely fuelled in that area. I
think we can help in diversifying that economy. It is
in our interests that Russia should have a strong,
expanding economy because that will help to bring
the sort of predictability and stability that we, as
neighbours of Russia, would like her to have. What
we are doing is helping with the transfer of
technology, we are helping with direct investment not
just in the hydrocarbon sector, we are helping
through the instruments that the European Union
has, TACIS, and there are about 30 million euros a
year to go in terms of helping with capacity-building,
helping the NGO sector, civil society, et cetera, in
support of the Partnership Agreement, so there are
some mechanisms and levers that we can use to help
the Russian economy. Equally, our economies are
increasingly based on the private sector and private
business make their own decisions on investments
and of course will make those decisions in the light of
what they see of some of the recent trends in Russian
centralisation and taking greater control in the
Kremlin of the state-owned sector and the pressure that is being brought to bear on some foreign companies that have invested in Russia, particularly in the hydrocarbon sector, so clearly that will affect the investment climate as a whole in Russia.

**Q4 Lord Lea of Crondall:** President Putin is often referred to as a superb poker player, looking long-term and all the rest of it, and his assessment of who has got whom over a barrel is presumably different from ours. We may think he is overplaying his hand and a point which has not been mentioned, so would you agree, is that it is not just a matter that we rely on them for energy and they rely on us to pay for it and all the rest of it, but the medium-term position on energy is that they have got huge reserves and they are more stable than the Middle East and, therefore, they have got us over a barrel? Would you say that that is more important than any statistic, as you said, of 40 per cent of UK GDP? That is strategically not the point.

**Sir Mark Lyall Grant:** Well, it is part of the point, if I may say so, my Lord. Of course as more European Union countries become increasingly dependent for their oil and gas supplies on Russia, obviously that gives Russia a degree of leverage, if you like, but, equally, they need markets and I think it would be wrong to suggest that this is an entirely one-sided relationship. They need security of demand as much, if not more, than we do security of supply. There are simply not enough outlets for them to sell their gas and oil elsewhere without the European Union buying these products, and their economy would be in as much difficulty as ours would be, if that was interrupted so I think it is a slightly more balanced picture than you are suggesting. Having said that, Russia is a very important, strategic country. It is a nuclear weapon power, it is a member of the United Nations Security Council, its economy is growing, it has got a declining population and its economy may not be as strong as some others around the world, but, nonetheless, it is in our neighbourhood, it is a very important country and we need to have a strategic relationship with it. I would not want to suggest in any way that we can dismiss Russia or treat Russia as though it were a small country in the Middle East. It is not, it is a European country, it is on the edge of Europe, it sees itself as a European country and it should be, correctly I think, a strategic partner both bilaterally and with the European Union.

**Q5 Lord Hannay of Chiswick:** Do we think that there is a level playing field between the European Union and Russia in economic and commercial dealings or do we think that the situation is not quite as rosy as that?

**Sir Mark Lyall Grant:** My Lord, it slightly depends on what you consider a level playing field. There have been well-publicised recent negotiations, negotiations of contract with high-profile, international, including British, investors in the hydrocarbon sector, and those companies declare themselves satisfied with the outcome. It is not for the British Government to say that they should not be satisfied with the outcome. Clearly, they feel that they can do business in Russia, they are making profits in Russia and they will want to continue to invest and do business in Russia, and that is really a decision for them to take in which the Government will get involved as and when those companies ask us to get involved and try and help out, as they frequently do on specific issues, but the recent discussions on these issues have been done between the companies and the Russian Government rather than with the involvement of the British Government.

**Q6 Lord Swinfen:** Can Russia feed itself, bearing in mind that it has had terrible problems in the past? **Sir Mark Lyall Grant:** I find it difficult to answer that question, my Lord. I might ask my colleague as he may know more about the ability of Russia to feed itself. I have not myself heard of any potential difficulties in the short term. **Mr Davenport:** No, I am not aware of any current issue regarding that.

**Q7 Lord Chidgey:** It is good to see you again, Sir Mark, in a different venue of course and on a different subject. I have two things quickly. You mentioned in some of your comments that Russia sees itself as European and I just want to test that a little bit because in my recent dialogue with counterparts in Moscow it was quite clear that that part of Russia sees itself as European and wants to be European, but is there not a much wider dimension which has a bearing on EU-Russian relations and how Russia wants to develop those in the sense that it is a huge, huge country, beyond our imagination, and ethnically so vast and so varied that it is again unquantifiable. I am really going to the point that, yes, the western part of Russia is clearly in every way more connected with Europe, but the eastern and Far Eastern part of Russia is far more tenuous and, therefore, from the point of view of governing Russia and its relations especially with the EU, it is far more difficult and far more threatening internally for the Russians to exercise some form of governance throughout this huge domain. Where does the EU sit in Russia’s thinking about how to help them govern what could almost be considered to be an ungovernable continent, if you think about the Chinese infiltration on the borders in the east because there is no one there, apart from Chinese immigrants in their tens of thousands probably, but who knows?
That is the sort of problem that Russian politicians were explaining to us when we last visited.

*Sir Mark Lyall Grant:* I have just a couple of comments on that. Firstly, of course Russia is a vast country and part of Russia is not in Europe clearly, but I would make the point that I made earlier, that it is a very centralised system and Moscow is in the western part of Russia and the thinking of most of the Russian leadership is in European terms and they do see themselves as European, even if those in Siberia perhaps do not. Secondly, I would assess that the Russians see the European Union primarily through the economic and commercial prism. It is the largest economic bloc in the world by quite a long way and it is, therefore, extremely important for Russia to have commercial and economic links with the European Union. I think they probably find it quite frustrating dealing with the European Union because it is a union of 27 different Member States and, therefore, when it comes to dealing with political issues, it is much easier to deal with the United States than it is to deal with the European Union. Also, and again it is more for the Russians to say than for me, but I would suggest that they would not want to put all of their eggs into the EU basket. They have a strategic relationship with the United States which is extremely important obviously to them both for status and for strategic reasons, and also they need to manage their relationships with the East. They are members of the Shanghai Co-operation Organisation, for instance, and they are very concerned about the threats that may come from the south and the east. I am not suggesting that the EU dominates President Putin’s waking thoughts, I am sure it does not, but I think they would probably see the European Union, as I say, as a commercial and economic power more than they see it in straight political terms.

**Q9 Lord Anderson of Swansea:** How do you see the evolution of the Russian political, legal, economic and social systems? Clearly, our own businesses, for example, have been highly critical of some of the failure of safeguards, for minority shareholders and so on. With what has been characterised as greater authoritarianism, the way that the centre has taken over, that the economic life of the private sector has decreased and the legal sector still has as many pitfalls for business people, do you believe that these institutions are evolving positively or negatively from the Yeltsin era?

*Sir Mark Lyall Grant:* You have taken an interesting benchmark which is the Yeltsin era. I think that obviously since the Soviet times there has been a great deal of positive progress in terms of democratic structures and institutions and I think that Russia does have those structures and institutions now in place, but we do have concerns, as I mentioned, and the European Union has concerns about some of the elements of that democracy agenda in terms of the equality before the law, the independence of the judiciary and in terms of freedom of the press and effective checks and balances, so we do have concerns, but, if you compare it to obviously the Soviet time, there has been very significant progress. If you compare it to the Yeltsin era and the first flush of democratic reform, perhaps there has not been as much progress as ideally we would have liked.

**Q10 Lord Anderson of Swansea:** It is not just democratic, but it is also in terms of the economic sector and of the private sector declining very markedly.

*Sir Mark Lyall Grant:* Indeed, there has been greater state control of the business sector, but there have been some prevailing trends the other way, such as the growth of a middle class which, I think, is very positive in terms of the long-term prospects for Russian development, so clearly it is sort of work in
progress. There was a very rapid reform process economically and politically following the break-up of the Soviet Union and it is not surprising if in market terms there was some correction for a while. Mr Davenport: From the point of view of firms operating in Russia, we of course talk to British companies, as I am sure members of the Committee do, and the message we are getting is a very mixed picture. On the one hand, companies are concerned about the levels of corruption which exist, for example, in the judicial system at all levels, but often pronounced at the lower levels and, on the other hand, they will point to improved efficiency of, for example, the courts dealing with commercial cases, from a low base of course, although there is some measure of growing confidence there, but there is also a concern about the opportunities for political control and manipulation at that level, so it is a very mixed picture.

Q11 Lord Hannay of Chiswick: I just wonder whether you do not think that is a little bit couleur de rose, given the criticisms of, for instance, Mr Illarionovich, who was President Putin’s own sherpa and who resigned in disgust and despair at the direction in which the economy was being led and who clearly has levelled since in public a large number of rather perceptive, it seems to me, criticisms of the way in which politics has intruded into the management of companies and that the rule of law does not really prevail, et cetera. Are not some of those criticisms rather well-founded and should they not be of concern to us?

Sir Mark Lyall Grant: Well, they are of concern to us, my Lord, and I have not tried to hide that, but one of the worrying trends that we do watch very carefully is precisely the greater centralised control of the business sector and the distortions that some businesses do face in terms of access to justice, et cetera, in Russia. These are issues, but, as my colleague was saying, when we talk to British companies, they see the picture as mixed. It is not all black, it is not all white and the fact that they are there and doing business and wanting to stay there and do business shows that they can operate in that environment. We hope that the trend that there is towards the greater centralisation of the economic power in Russia is a sort of temporary phenomenon and will not become a permanent phenomenon because we believe that the greater capitalism and devolution of that economic power is going to be a good thing for Russia in the long term and good for our companies too.

Q12 Lord Chidgey: Sir Mark, you have mentioned a number of areas which are of interest to HMG in regard to our relations through the EU with Russia and what you feel are important issues. Can you give the Committee any idea of the main areas of policy that should be dealt with between the EU and Russia now and perhaps over the next five years, and you are familiar with the question, I think, and I want really to couple that with a comment you made earlier about the feeling of being European in Russia, political establishments, if you like, and could we consider in that context how Europe-oriented the institutions are. How do you see Russia, if we were to compare it with the requirements of the Copenhagen criteria and the acquis, in your dealings with the issues that matter most to us in the next five years because, if Russia took part in the test, it would not become an accession candidate for the EU?

Sir Mark Lyall Grant: No, I think it is safe to say that Russia would not meet the Copenhagen criteria.

Q13 Lord Chidgey: So, consequently, we cannot consider it on equal terms as a state which works well with the European states, by definition. It is a different set of rules.

Sir Mark Lyall Grant: No, if Russia were to be a candidate for membership of the European Union, which obviously they are not, there would be a hell of a lot of work for them to do to reach the Copenhagen criteria standards, but in terms of the sort of policy areas, and I outlined some of them in my earlier replies, one of the reasons that we are enthusiastic advocates of a new, updated Partnership and Co-operation Agreement is that over the last 10 years there have been some trends which we think need to be responded to in terms of energy, economy, justice and home affairs, migration issues and counter-terrorism which perhaps need to be given a rather sharper focus in the new agreement than was given in the old agreement, so those are some of the areas of policy which we would like to see covered in the new agreement so that we can sharpen up our dialogue with Russia on those key, critical issues. Another area of importance is a stronger dispute-resolution mechanism, because the current PCA has not got a very strong dispute-resolution mechanism. The new mandate, as agreed within the European Union, would have such a dispute-resolution mechanism and that would help us to resolve some of these common issues between the European Union and Russia before they became full-blown crises, so I think that is important, and also perhaps to give the relationship a stronger legal underpinning and framework than the current agreement does. Those are some of the areas where we would like to see the relationship develop.

Q14 Lord Chidgey: In that context, what effective levers does the EU have in terms of negotiating with the Russians on these key issues, levers that obviously our Russian counterparts would recognise as well? It would be interesting to know how duality sees these critical aspects of the relationship.
Sir Mark Lyall Grant: I think it is difficult, my Lord, to talk about levers. If Russia does not want an updated Partnership and Co-operation Agreement, then obviously we shall not have one, but the indications are that Russia does want to have an upgraded Partnership and Co-operation Agreement, that they do value the relationship with the European Union which is quite heavy in terms of investment of time now on both sides. We are talking about two summits a year, structured relationships all the way down the political chain, joint commissions, et cetera, so there is really quite a heavy bureaucratic process underpinning the EU-Russian relationship and, we would argue, perhaps slightly too much process and not enough substance, but, nonetheless, the process can be important in making sure that we do have a framework for dialogue and tackling some of the difficult issues. The fact that Russia has invested in that and is prepared to invest time and effort in that suggests to me that Russia does see that it has an interest in having a good, stable, secure and strategic relationship with the European Union. I think it is that as much as anything that we can talk about as leverage. We cannot force Russia to look to the European Union rather than the United States or China, but we have to show that there are advantages to Russia in having that sort of secure and stable relationship.

Q15 Chairman: How substantial is the Russian Federation mission to the EU in Brussels? Do they have a significant number of people working there?
Sir Mark Lyall Grant: I do not know. I might have to ask for advice on that.
Mr Thornton: They do. It is one of their most substantial missions and they have invested an enormous amount of time and resources in it.
Sir Mark Lyall Grant: We can write to you with the numbers.

Q16 Chairman: It is something we can pursue when we are in Brussels, but it is quite interesting, in just thinking of the way in which they perceive us, to get some idea of what sort of mission they do have there.
Mr Davenport: Certainly the mission in Brussels is closely involved in the structures for the EU-Russia partnership in terms of monthly meetings and so on.

Q17 Lord Hamilton of Epsom: The founding fathers of the EU were obsessed by the concept of a third world war in Europe between France and Germany. That concept, I think, looks a bit dated now. The only threat actually to European security is from Russia, but of course everybody in the EU is absolutely appalled at the idea of Russia coming into the EU and they keep on saying it is unthinkable. Should we not, as a long-term objective, say that we would like to have Russia in the EU, and I am talking about 20 years hence, but should we not be actually talking to the Russians in terms that they are a hell of a long way from qualifying today, but in time we would like to see them as members of the EU because, if we are worried about security, that would actually do more to secure the security of the Europeans than anything else?
Sir Mark Lyall Grant: I think I would take issue, my Lord, with your premise that the only security threat to Europe was from Russia, but that is perhaps a debate for another day. I am not sure I would share your conclusion either, my Lord. I do not think it is realistic to think of Russia becoming a member of the European Union, and this goes back to the earlier question about the size of Russia and the eastern extent of Russia. I think it would change the nature of the European Union very, very dramatically, and some would say it has been changing dramatically anyway.

Q18 Lord Hamilton of Epsom: How about the membership of Turkey?
Sir Mark Lyall Grant: Well, Turkey is another issue, but Turkey does not extend quite as far eastwards into Asia as Russia does. I think you would be looking at a very, very different European Union construct if Russia were a member, so I think in the longer term, even in the 20-year timescale, we would see Russia as a key, strategic partner of the European Union rather than as an aspirant member.

Q19 Lord Swinfen: You have already, I think, covered quite a lot of my question, but how, in your view, does Russia perceive the EU and what are the underlying principles of Russian foreign policy towards the EU?
Sir Mark Lyall Grant: It is a difficult question perhaps for me, rather than the Russian Government, to answer, but my belief is that Russia does see the European Union mainly through the commercial and economic prism, although they would like to develop a political and security relationship with the European Union because I think they feel that they would get more understanding perhaps from members of the European Union than they would from membership of NATO and perhaps even the OSCE. They do find the EU’s principles and values of solidarity, for instance, frustrating, they do find it difficult to understand why the European Union will base its position on an individual Member State’s bilateral issue with Russia and I do not think they have internalised that that is one of the fundamental attributes of the European Union, so I do think they probably find that relationship frustrating at the political level, but my primary response would be that they do see it through an economic and commercial prism.
Q20 Lord Hannay of Chiswick: You do not think there is any residue of the Soviet attitude towards the European Union which was actually hostile to it and which preferred to deal with the individual Member States of Europe and pursued soullessly, for the whole history of the Soviet Union, a policy of not dealing with the European Union as such, but dealing with the individual Member States, a policy which was pursued quite successfully by the Soviet Union throughout its existence? You do not think there is any residue of that?

Sir Mark Lyall Grant: I think there may be some residue of it, my Lord, in terms of their wanting to engage with individual Member States as well as the Union as a whole. I do not sense any hostility to the concept of the European Union, but I think they probably feel that the recent accessions of countries that were either in the Warsaw Pact or indeed members of the Soviet Union at one point, the accession of those members, they may feel, has changed a little bit the centre of gravity or the nature of the European Union. It is true that those countries that perhaps live closer to Russia and know Russia extremely well do bring to bear in the European Union discussions on Russia a particular viewpoint and that has sharpened up the debate within the European Union about Russia. Obviously they bring a lot of expertise to bear, but they also bring their own unique points of view to bear and Russia may feel that that has shifted the centre of gravity a little bit within the European Union.

Q21 Lord Lea of Crondall: Could I just ask why it is that no one so far has mentioned ideology in all of this? For many, many years, the whole of my life virtually, certainly in the trade unions, the reason a lot of people were against the EU was that the Communist Party, taking the Moscow line, influenced a lot of people and the idea was, “This is a market economy which is certainly something we are trying to destroy and, come the revolution, of course we will have communism”. Now, are you saying that ideology is nowhere at all in any of this anymore? I do not mean that particular ideology, but is there any ideological difference from what we might call the “European model” for which, after all, we did not specify everything in detail, but there is the whole question of no government aides, of public procurement rules and there is a list about a mile long, is there not, but the opposition to that could be ideological to some extent, could it not?

Sir Mark Lyall Grant: It could be, my Lord, but I do not sense a very strong ideology emanating out of Russia today. I visited Moscow a few weeks ago and I did return with a sense that there was perhaps a missing strategy somewhere in Russia’s long-term global positioning. This is just my subjective judgment of course and others will have different views and I do not know if the Russian authorities would disagree with that, but I did sense that a lot of the moves adopted by Russia recently are tactical rather than strategic and it was difficult for me at least to define where the longer-term Russian strategy and ideology is. In the past, as you say, my Lord, it was very clear where it was and it was there and it was a manichaean struggle, but I do not sense that now. There is clearly a nostalgia in some official circles for the past and there is clearly a frustration amongst some officials for what they perceive as humiliations of the 1990s, but I do not think one would say that that is an ideology that unites all the Russian authorities. I confess, I am at a slight loss.

Mr Davenport: I think that is absolutely right, what Sir Mark has said. If there is an ideology, I think it is closer to a nationalist one, a nationalist, statist one. The rejection of communism as the way of running the economy is pretty wholesale, and of course there is a Communist Party still operating which secures very small-scale support. What tends to unite the mainstream of the Russian political spectrum is a nationalist bent and a sense of the importance of Russia’s strength and position in the world.

Q22 Lord Swinfen: How do you think that the Russians see the relationship between the EU, on the one hand, and NATO and the United States, on the other?

Sir Mark Lyall Grant: Again, my Lord, it is a difficult question really for me to answer. I think Russia finds it easier to deal with the United States. They feel that deals can be done, bargains can be made, there can be more cross-cutting sort of strategic discussion at the very highest level with the United States than there can be with Europe where their dialogue tends to be a little bit more siloed into individual sectors, and doing deals with a union of 27 members is obviously slightly more difficult. I think, as I mentioned before, that they would like to use the European Union more as a forum for discussion of security and disarmament issues perhaps than the NATO-Russia Council, which again they find quite a difficult environment. They do not see it as a single body of 28 but as a body of 28 plus one and, therefore, they feel a bit sort of ganged up on in that context. Also, they are perhaps jealous of the United States’ relationship with the European Union, which they feel is a sort of smoother relationship and one where less disagreements surface in the EU-US relationship than do in the EU-Russian relationship. Now, we within the European Union know that the EU-US relationship is by no means straightforward, particularly when it comes to trade issues, but, nonetheless, I think the perception in Moscow would be a bit different.
Q23 Lord Swinfen: Do you think that they would see the EU and NATO as one bloc?
Sir Mark Lyall Grant: No. I think, my Lord, they do distinguish very clearly between the two because of the membership of the United States in one but not the other.

Q24 Lord Anderson of Swansea: Perhaps five years ago they were trying to boost the OSCE, seeing that as an organisation which did not include the US and in which they could have decoupled Europe from the US. Clearly, because of their dislike of the election-monitoring and so on of the OSCE, that has lost favour. Which of the various organisations, NATO, the EU and the OSCE, is currently in favour, if there be such?
Sir Mark Lyall Grant: I think you are right that their enthusiasm for the OSCE has declined rather in recent years and perhaps the Council of Europe too because of the election-monitoring activities and focus, particularly of the OSCE. I would suggest perhaps that the G8 and the UN Security Council are organisations where Russia feels less outnumbered and more empowered with more levers than the other ones that you have mentioned.

Q25 Lord Hannay of Chiswick: You have begun to answer, I think, the question which I was going to put about the current institutional framework of the EU-Russian relations and I take it that the present agreement just goes on and is maintained until a new one is negotiated and it does not lapse just because we have reached the end of the 10-year period, but I wonder if you could also comment a bit on these rather strange animals called the “four common spaces”. I thought that Lord Howe some years ago had driven a stake through the attempts to translate “espace” as “space” and it should be translated as “area” and I take it that that is actually what is meant by the “four areas of policy” which are dealt with and it is a pity that “space” has crept back in again, and it is now more a hobby horse of mine than Lord Howe’s. Do they work? Are they really an effective means of discussion and common effort and co-operation or are they just kind of bureaucratic wheels that spin round?
Sir Mark Lyall Grant: My Lord, perhaps a mixture of the two, but, just to confirm your first point, the existing Partnership and Co-operation Agreement, although initially running for 10 years and the 10 years is obviously up this year, does continue until it is replaced by something else. If we were to overcome the Polish meat blockage immediately, it would still take probably six, nine or 12 months to negotiate the new agreement and then another year or so to ratify it, so the existing arrangement will run for at least a couple of years even in the best overall context. In terms of the four common spaces, they were added in 2003 and do cover four distinct areas: economy; freedom, security and justice; external security; and research, education and culture. I think they have had some benefit and they were reinforced in 2005 by the additions of the roadmaps of how you should implement these different common spaces, but it has become quite a bureaucratic exercise, there is no question. It does have some advantages, and the main one I would characterise is that you can make progress in one area, even if there is blockage in another area, so I think that is a good aspect of it. However, the inverse is also true, that it can operate a little bit in silos and, therefore, it is less easy to take a strategic overview of the relationship as a whole when different parts of the bureaucracy are operating in these different silos and going their own merry way. It is very resource-intensive, it is bureaucratic and we would hope that the new agreement, if it is ever finalised, would enable a slightly more strategic approach and allow for the linkages between the different areas, whilst at the same time allowing some flexibility to make progress in areas where it appears to be easier than in others.

Q26 Lord Crickhowell: So far, we have really been looking at Russian perceptions, attitudes and policies towards Europe and its Member States and you have spoken about some Russian frustration and a feeling that they are held to ransom by individual bilateral disputes. You were also beginning to touch on British policy and the need to sharpen up some areas, such as the legal framework. I really want to reverse the whole process now and look at what the British Government’s priorities are for the development of the EU-Russian relationship and how far they are accepted by the other members of the European Union and what are the main areas of agreement and disagreement between the Member States, so let us really start the process of looking at Europe’s approach to Russia rather than the Russian attitude to Europe, please.
Sir Mark Lyall Grant: The British Government position is that we believe it would be useful to have an updated Partnership and Co-operation Agreement. But we support the Polish Government, because we believe that the Russian ban on the import of Polish meat and livestock is unjustified. It meets the EU phytosanitary criteria and we do not see any justification for Russia continuing with that ban any more than we see justification in Russia continuing some aspects of the ban on British beef, which is still going on, so we hope that Russia will lift that ban on Polish meat which would enable then the mandate to be concluded and the negotiations to begin on the new agreement. The reason that we want the new agreement is that we do believe that some of...
the developments over the last 10 years do need to be factored into the new agreement, and I mentioned one or two of them earlier, including the fact that it would give it sharper dispute-resolution mechanisms, it would give it a more secure legal framework than the existing arrangement and have a greater emphasis on migration, on counter-terrorism and on energy than the original agreement had, which are all areas which have grown in importance over the last 10 years. But, equally, we have our own difficulties. The current dispute that we have with Russia over Alexander Litvinenko is well-known and we have been grateful for the EU solidarity that has been shown. They issued a very good statement on 1 June and another very good statement yesterday of support for our position. We have not sought to hold up the mandate of the new PCA for that, but we have secured agreement within the European Union that there would be an annex to that mandate which would flag up the Litvinenko issue and say that, in the context of the discussions of the new agreement, there needs to be some discussion of the issues around the justice system, the human rights aspects and the legislation of Russia which does allow for direct action taken against Russian exiles overseas, so those are issues we will want to discuss in the negotiations and we will flag that up in the mandate, but we are not seeking to hold up an agreement to the mandate on that basis.

Q27 Lord Crickhowell: That is the British Government’s approach and the other part of the question I asked you was about whether there any great differences between the European countries. Are they taking a general line or are other of our partners going in a different, significant way?

Sir Mark Lyall Grant: Well, that is an agreed position of all the EU Member States and, as I mentioned, EU solidarity is an important aspect of membership of the European Union to which all the members very strongly subscribe, but it will not come as any surprise to this Committee that there is a spectrum of views among the different EU Member States. I mentioned some of the newer Member States from Eastern Europe and from the ex-Soviet Union, who have a particular viewpoint of Russia and of the trends in Russia over recent years which may be rather different from the views of those on the Iberian Peninsula, for instance, and that is natural in a union of 27 members, but we seek to resolve, and I think we are reasonably successful in resolving, those sorts of differences internally and we are very resistant to any suggestion or attempt by outsiders, whether it be Russia, the United States or any other third country, to try and drive divisions between the members of the European Union and to try to exploit any differences of view that there might be.

Q28 Lord Lea of Crondall: It is well-known that in the Treaty negotiations we had a red line about how far common foreign policy should go. The Russians are aware of the role of Mr Solana, not least in the quartet which we will come to later, but in all the myriad things which are happening. My question would be: could it be that it is much easier for the EU to have a common policy on China or Africa or some other part of the world, Latin America, precisely because former communist states do not have the same perception? Of course Germany in particular, and I could mention half a dozen, is 60 per cent reliant on Russian gas already, so are there short-term differences of interest as well as, what you might call, more strategic problems about putting all your eggs in the Solana basket?

Sir Mark Lyall Grant: My Lord, I am not sure the two aspects of your question are linked quite as closely as you are suggesting. Clearly, Solana is an important figure within the European Union and that role will continue—

Q29 Lord Lea of Crondall: It can be strengthened?

Sir Mark Lyall Grant: Well, it will be strengthened.

Q30 Lord Lea of Crondall: How do you think it will be strengthened in reality?

Sir Mark Lyall Grant: Well, I think we are getting on to slightly different territory now.

Q31 Chairman: We are really not discussing the Treaty today, we are discussing relations with Russia.

Sir Mark Lyall Grant: Solana is an interesting figure who does go wider than just the European Union. As an example of that, in the Iran context, Solana is operating on a mandate from the E3+3 which includes not only Russia, but also China and the United States as well as the UK, France and Germany, and Solana is the designated spokesman in direct negotiations and discussions with the Iranian authorities on the nuclear question, so in a sense Solana is operating on behalf of Russia in that particular context. Now, that is a one-off, ad hoc arrangement now, but I can see that sort of formula being used in the future, maybe in the near future if it comes to Kosovo, for instance, so that, I think, is one aspect of the question. But Solana, when he is operating on behalf of all the EU Member States, takes his instructions from the Council and the Council comes to a view. Solana cannot operate independently from the Council and nor will he be able to even after the Treaty amendments are agreed, if they are agreed, so he will still be a representative, as it were, of the wishes of the Member States as a whole. If there are such radical differences between the EU Member States on a particular issue, such as Russia, that Solana is not empowered to put forward any particular policy, then that is the reality of the
situation. But I would underline myself that, from our point of view, an EU common policy and common positions are even more important in respect of the near neighbourhood than they are of those areas further away. It may be easier to have a common position on Burma or China than it is on Russia or North Africa, but I would argue that it is actually more important for the EU to have a united and common position on North Africa and Russia than it is on those other ones.

Q32 Lord Anderson of Swansea: Education—in the 1960s, there was a perception that we in the UK did not understand Russia enough and a lot of money was put into our universities and, alas, much of the effort then evaporated, but is there a view in the European Union, not just in the UK, that there should be a similar process to boost the education exchanges, the study of the Russian language and civilisation within European universities? Is there likely to be more money available for the same purposes as we put money in in the 1960s?

Sir Mark Lyall Grant: My Lord, I might ask my colleague whether he can answer that question.

Mr Davenport: My Lord, one part of the framework for the EU-Russian relationship, precisely one of the four common spaces, is devoted to research, education and culture and within that umbrella this enables, in particular, the European Union and European Commission funding to be directed towards commonly identified areas, and that includes certainly mutually agreed academic links precisely with a view to boosting cultural and educational ties between Russia and individual Member States of the European Union, including through programmes like Tempus. In terms of the education systems of the Member States actually fostering the teaching of Russian culture and the Russian language and so on, I think that is an extremely important point to make. I think it is not specifically an area where EU funding is being directed to any great extent.

Q33 Lord Anderson of Swansea: Could it be?

Mr Davenport: What I was going to say was that the British Council independently has been working with the Yeltsin Foundation and only very recently launched a programme over the next three years for boosting the teaching of Russian in the UK. I think that this is very important because you are right in identifying this as a lack, and the teaching of Russian language, literature and culture has declined.

Q34 Lord Anderson of Swansea: It has collapsed.

Mr Davenport: Here it has collapsed; in other countries it has been maintained at a higher level in some cases. But that is something which should be corrected.

Q35 Lord Boyce: I think you have largely answered much of what I was going to ask in my question but just to knock the nail out of sight, you have implied certainly there is solidarity with the EU towards individual nations in national disputes you mentioned Poland and our own present one. Could you say whether or not you are happy that solidarity is shown when individual nations do have disputes? Do you think, particularly in the case of the new Central and Eastern European States, sometimes that solidarity can lead to a distortion to the rather purist view which one might take of what the EU policy should be towards Russia and does get shifted to other ground in our policy because we are actually trying to provide solidarity with these indigenous people?

Sir Mark Lyall Grant: No, my Lord, I do not think “distorted” is right. Solidarity is an important principle, you mentioned Poland and the United Kingdom; there are others I could mention, Lithuania and Estonia and the recent difficulties over the moving of the statue of the Soviet war dead and the reprisals which Russia took on that. Clearly there needs to be a balance, but I think that balance can be achieved within the European Union. European Union members might have different views on the wisdom or tact with which Estonia took the action that it did in the capital, but the Russian response in terms of the harassment of the Estonian ambassador in Moscow was so disproportionate that obviously that brought together greater unity and solidarity on the part of Member States. To some extent solidarity has to be earned and reasonable. It would not be fair to expect solidarity if there had been no consultation, for instance, on the issues as they arise but, nonetheless, it is an important principle of the European Union, we attach a lot of importance to it and I think most others do as well. We are grateful for the support we have received in the most recent instance.

Q36 Lord Crickhowell: Could we go back to energy. Right at the start we talked about European dependence on Russian oil and gas and their need for markets. You did briefly refer, I think, to progress on energy issues. Could you develop a little on that? What success has the dialogue had so far and are there any other major problems in the energy field that you would like to draw our attention to?

Sir Mark Lyall Grant: I do not think I could point to hugely significant progress in terms of the EU-Russia discussions on energy; they are ongoing. Probably the most important step forward in recent years on this was done through the G8 under the Russian Presidency in St Petersburg in July 2006, which did agree some energy security principles that referred to the importance of diversity and security of supply and also market principles and mechanisms applying
in the energy sector. I think that was probably a more significant stake in the ground, a benchmark that was established than anything that has been done in the EU context. It is important that we judge the attitude and actions of the Russian authorities against the benchmarks that they agreed under their own Presidency of the G8. Obviously we do have some concerns about that but, likewise, the Russians have concerns about the security of demand. They need to be clear that there are going to be outlets for their supply just as we want to be sure that the supply is not interrupted arbitrarily as, we believe, has happened in a couple of cases recently.

**Q37 Lord Hannay of Chiswick:** Could you tell us what the status, if any, of the Energy Charter is which was negotiated and signed by Russia and the 27 Member States of the European Union but never ratified by the Russians? I have heard suggestions by representatives of the major oil companies that they regard the Energy Charter as pretty well dead because of the Russian objections to it. If that is effectively the case, what is there that enables us to ensure there is a level playing field in this area? That is, of course, what the Energy Charter would have done, it would have meant the Russians had access to various parts of our energy industries and we would also have access to theirs. It appears that it is their intention we should not have access to theirs in any ownership sense but only in the sense of being subcontractors to Gazprom, or whatever it is. What is the situation now, in fact, with the Energy Charter? What is the attitude of the Government towards what needs to be done in that area?

**Sir Mark Lyall Grant:** Michael, do you know about the Energy Charter?

**Mr Davenport:** My Lord is absolutely right in identifying this as a serious problem, a serious challenge. Russia has not ratified the Energy Charter Treaty. HM Government continues to regard the Energy Charter Treaty and the principles enshrined therein which, as Sir Mark said, in parallel with the St Petersburg summit, highlighted the very same issues, as fundamental to developing the sort of relationship internationally on energy that we need. We have certainly not given up on Russia taking this forward, we continue to press for that. It is, however, true that there is great reluctance. Another way of pressing our UK and EU interests in this, of course, coming back to a previous question, is the negotiation of a successor agreement to the Partnership and Co-operation Agreement because, as was previously highlighted, energy security would be a key area to address there.

**Q38 Lord Hannay of Chiswick:** If I could finish up on that point, presumably you would recognise the difference between the Energy Charter and the G8 Communiqué in St Petersburg is that one is a legal and binding set of agreements which is to some extent justiciable and the other is just some nice words written on a piece of paper?

**Mr Davenport:** Yes. You are right and we would not give up. Of course, we would hope that the Partnership and Co-operation Agreement’s successor would be more than just nice words.

**Q39 Lord Crickhowell:** It strikes me, talking about these splendid Europe-wide charters and other agreements, what it really comes down to in developing and exploiting Russian oil and gas is very often the negotiations conducted by the individual oil companies and the relationships that they establish. Clearly they have not always been very easy, they think they have got somewhere and then suddenly find they have not quite got it. Presumably, at the end of the day there are these general approaches that a lot will depend, will it not, on the success that individual oil and gas companies have in reaching deals? Presumably both the European authorities and, indeed, the British Government keep in very close touch with all these negotiations. Would you comment at all about the distinction I am trying to make between the general agreements, general approach and general policy, and the way it is developing as far as the individual transactions are concerned?

**Sir Mark Lyall Grant:** You are right, my Lord, there is a certain asymmetry here because within Russia Gazprom has accumulated more and more control over the hydrocarbon sector as a whole and Gazprom is controlled increasingly closely by those in the Kremlin. That, of course, is not the situation for the oil and gas sector internationally and certainly not in this country. Therefore, in these individual negotiations they are between large private sector companies and, in essence, the Russian authorities, sometimes at one remove, sometimes not at one remove. Of course, the British Government—and no doubt other European governments—keep in very close touch with their major companies both here and in Moscow about developments and the progress of those negotiations and, indeed, the changes there are in those negotiations, but we do leave it to the companies to judge whether they feel they are operating on a level playing field or they are being treated fairly. If they want support from the British ambassador or the British Government, then of course we offer them that support at the highest political level, and have done so on numerous occasions in recent years, but at the end of the day the Russians recognise that they do need Western investment and technology. No doubt if they did not, maybe they would not be offering the deals that are available to Western oil and gas companies that they do. They need that investment and their technology...
transfer, so it should be a win-win situation for both sides.

Q40 Lord Chidgey: Sir Mark, as my good and noble friend Lord Anderson is suggesting, we have a problem here understanding how the EU can effectively promote democracy in Russia, let alone here, and the rule of law. You have touched on this in general terms as part of our session today and I think you have been fairly frank about the gap that does exist between perception in our society, the EU’s society and perhaps in Russia of what we mean by democracy and the rule of law, the search for human rights and fundamental freedoms. I do not expect you to give us a treatise on this now, I think we understand both differences, but it does create a huge challenge for the EU to be in a position where our Russian counterparts are willing, in fact, to engage on those issues, let alone the EU being able to promote our vision of those key principles that we enshrined in our own agreements. Is advice bland words here, but the reality of achieving anything I find personally hugely difficult and hugely challenging for us. I wonder what HMG’s position is on that?

Sir Mark Lyall Grant: My Lord, I can answer that. It is clearly challenging to get solid outcomes in this area, but there are mechanisms by which we can try to achieve that. There are structured human rights consultations twice a year, which the Russians do engage with, and that is supplemented by an ongoing dialogue and specific démarches at all political levels, including head of state level and, indeed, at the recent EU-Russia Summit in Samara in May, which I referred to, human rights was a very strong theme of those discussions. On behalf of the EU, Angela Merkel made that very clear in her engagement with President Putin at that summit. There are mechanisms for doing that. The EU also has ongoing direct contact with the NGO sector in civil society in Russia and, indeed, supports various projects directly to NGOs in civil society within Russia. Lastly, I would add that in the new mandate for the new PCA there is a strengthened element of democracy and human rights which we would want to negotiate into the new agreement. There are mechanisms there, do they deliver results? Of course, it is a challenge and a particular challenge at the moment, there is no question about that. It is not that the Russians do not engage, it is that they sometimes question our approach, they question the premise on which we operate and they do not always see us as avoiding double standards. I do not think I am divulging any secrets by saying at the summit in Samara President Putin was trying to draw an analogy between the way the Germans had treated protesters at the Heiligendamm G8 Summit—what has now become the traditional way at G8 Summits, protesters are kept at some remove from where the heads of state and government meet—and the complaints that we made about allowing any protesters to make representations or to turn up at the Samara Summit. One was Mr Kasprow, a human rights champion in Russia, who was prevented from travelling but was not the only one travelling down to Samara. President Putin felt that it was wrong for us to complain about the treatment he was meting out to these demonstrators and protesters because the Germans had done the same thing at the Heiligendamm Summit. Obviously we did not see those two things as comparable.

Q41 Lord Anderson of Swansea: Human rights may be a strong theme, but would you agree that the picture in comparison with the Yeltsin era is relatively bleak and deteriorating to the point perhaps where Russia would not now qualify as a member of the Council of Europe? One thinks of the removals of checks and balances in the political structures, the fact that there is a monopoly of these four television channels in Russia and there have been political assassinations on a larger scale with apparently no redress. Do they take any notice of these dialogues? What evidence is there of their altering practice as a result, or do they go through the motions and say that really this is interference in their internal affairs?

Sir Mark Lyall Grant: My Lord, you have highlighted some concerns. I mentioned right at the start that there are increasing concerns among EU members about Russian policy, both internally and externally. When I mentioned internally, I meant these issues of democracy and human rights, and you have highlighted some specific areas of concern, freedom of the media, checks and balances, independence of the judiciary, et cetera. It is a challenging time and I think if one compared now with perhaps the time of President Yeltsin, there has been some slippage but, as I think I mentioned earlier, given the extent and speed of the reforms that happened after 1989, or in the late 1980s, early 1990s, perhaps some correction was inevitable in the strategic sense. We have to recognise that. We do not have to accept that, but we should look at that with a clear eye and hope it is a short-term correction rather than a longer-term trend, because if it was a longer-term trend and set for some years that would be of very grave concern. My very last point, my Lord, is there are mechanisms within the European Union-Russia partnership that do allow us to address those issues. I would not sit here and claim that we could show some successes in terms of outcomes, that would be wrong because I do not think we can in recent years but, nonetheless, there are mechanisms and we do raise these issues at very regular intervals.
Q42 Lord Anderson of Swansea: Chairman, could I mention one word on the British Council and it would be wrong not to mention it. Would you say a few words about the current nature and difficulties in the work of the British Council?

Sir Mark Lyall Grant: I visited the British Council at the Moscow office a few weeks ago. They do have a very extensive network in Russia doing a lot of extremely good work across the field of English language teaching, cultural exchanges, education support, governance work, et cetera, so it is a very effective and important operation for the British Council. They have been under some recent pressure on the grounds of tax and their overall status in Russia. We believe that pressure is unjustified and obviously we are supporting the British Council very strongly with the Russian authorities on that, but we hope those issues can be resolved and it is a short-term mechanism of putting pressure on the British Council rather than a long-term attempt to close down their activities entirely.

Q43 Chairman: Sir Mark, we are coming to the end of the time when we asked you to be with us. We have two more topics we would like to raise with you, we of the time when we asked you to be with us. We have Q43 Chairman: Chairmen, could I In that case, we can go on for another 10 minutes.

Q44 Lord Hannay of Chiswick: I wonder if you could say with regard to political developments in countries of the former Soviet Union which are now not part of Russia, to what extent Russian and EU interests coincide and to what extent they conflict and, secondly, whether Russia and the EU have any scope for collaboration in dealing with what are called the “frozen” problems, Transnistria, South Ossetia, Abkhazia and Nagorny Karabakh?

Sir Mark Lyall Grant: Yes, my Lord. On the first issue, of course, they vary enormously. Some former members of the Soviet Union are now members of the European Union, at one extreme and perhaps at the other extreme countries, like Belarus, which remain extremely close and umbically linked to Russia. Then you have some of the Caucasus countries that have their own specificity and some big countries in-between, like the Ukraine, where the EU has its own relationship and wants to develop a closer relationship. It is difficult to be categoric, they have all developed in their different ways and the European Union has a different relationship with all of them. In terms of the frozen conflicts, I have to be honest and say that I do not think the European Union per se is really the critical forum for addressing those conflicts. There are some ad hoc arrangements that have built up on the different conflicts, for instance there is the Minsk Group that deals with Nagorny Karabakh, which is the US, France and Russia, and there is also Friends of the Secretary General that deals with Georgia which does include the UK and Germany as well as Russia and the United States. The G8 looks very regularly at these frozen conflicts, particularly at Georgia, Moldova and Transnistria, and the EU itself does not really play a very substantial role. The Moldova-Transnistria dispute probably is more linked to the CFE Treaty and the recent Russian decision to signal a future suspension from that Treaty, therefore it is more of a NATO issue perhaps than a European Union issue. I do not think we can expect the European Union to play a particularly dynamic role in the resolution of those conflicts, but we do think resolution of those conflicts is extremely important.

Q45 Chairman: Does the EU not provide some border monitoring assistance to either the Ukrainian or Moldovan border? A “border assistance mission” I think it is called.

Sir Mark Lyall Grant: There might well be in Moldova-Transnistria on that point.

Q46 Lord Lea of Crondall: This is question 11 and perhaps to get to the heart of it, I think, in scope for co-operation. We have been looking at the Quartet in a different study we have been doing and in that case Russia was taking a low profile, but as soon as it gets rather interesting they go ahead again with their own diplomacy. Do you think that is a pattern? How do you categorise that? We have other different examples and obviously with Kosovo we thought that we had nearly cleared it up and now it is getting very fierce once again. Could you comment on that? We cannot go right through the world but could you comment on those.

Sir Mark Lyall Grant: Perhaps I could compare and contrast three examples. On the Quartet, I think you are right, my Lord, Russia has not played an enormously active role within the Quartet but is an important member of the Quartet. It is important that Russia does use the Quartet as its vehicle for its own diplomatic activity in the Middle East and certainly we want to encourage that. Obviously the former Prime Minister, Tony Blair, has now been appointed as a special representative of the Quartet. He will help to give a little bit more energy and thrust to the Quartet’s role in the region and will be acting on behalf of Russia as well as the other members of the Quartet. I have not sensed that in its own bilateral activities in the Middle East Russia has caused any particular difficulties. Russian objectives in the Middle East are not very dissimilar from ours and I think this is a good area for co-operation. I do not
sense any particular problems on that score. Likewise, but even more so, is Iran which has the 3+3 mechanism, as I mentioned, where Russia has always been an extremely co-operative member of the 3+3, and continues to be so, there has never been any question of a different sense of priorities or objectives. Russia does not want to see Iran develop nuclear weapons, nor do we, and that underpins the whole approach to the Russian nuclear issue, so that is a very close relationship. The third one, and the one you mentioned which is more difficult, is the Contact Group on Kosovo. Russia was a very important member of the Contact Group, but we have now reached such a stage in discussions on the status of Kosovo that it is becoming extremely difficult for the Contact Group to stay united because differences have emerged over pushing through a resolution in the United Nations which would, in effect, bring into implementation the Ahtisaari proposals which have been endorsed by the UN Secretary General and the European Union. That has made Contact Group discussions on Kosovo, which continue, rather more difficult than they have been before, but if there will not be a UN Security Council in the next few weeks, which is a possibility, then I think the Contact Group will come back front and centre because it will be the Contact Group which will need to collectively take forward the next stage of Kosovo status independently and Russia’s role will be important on that. There is no question that Russia’s approach on Kosovo has divided the Contact Group very much.

Q47 Chairman: Sir Mark, on behalf of us all could I thank you very much indeed for having given such a very useful start to our inquiry, we are very grateful to you and Mr Davenport. If we had more time, I could go on at greater length in saying it, but it is our very serious and sincere thanks for your contribution to our work this morning. Thank you.

Sir Mark Lyall Grant: Thank you, my Lord Chairman, and good luck with your report.

Supplementary memorandum by Sir Mark Lyall Grant, Political Director, Foreign and Commonwealth Office

EU-Russia Relations

Thank you for the opportunity to give evidence on 19 July at the opening session of your inquiry into relations between the EU and Russia. I am also pleased to see that plans are underway for you and the Committee to visit Moscow and Brussels after the summer break.

A few points arose during our evidence session on which I thought you might welcome further detail.

We discussed the size of the Russian Mission to the EU in Brussels. I promised to write with specific figures. There are 51 registered diplomats working at the Russian Embassy to the EU.

We also discussed the EU Border Assistance Mission (“EU-BAM”) on the Moldovan-Ukrainian border. The illegal regime in Transnistria is a centre for smuggling, people trafficking, and organised crime. There are a damaging effect on both Moldova and Ukraine. In December 2005, following a request from the Presidents of Moldova and Ukraine, the EU established EU-BAM to improve control of the Ukraine-Moldovan border, including the Transnistria segment. EU-BAM currently has 63 staff, of whom 42 are field officers. These include two UK secondees, whose main duties are to provide training and advice to Moldovan and Ukrainian officials.

The EU has also appointed a Special Representative for Moldova and, alongside the US, has joined settlement talks as an active observer. Other participants in the mediation process are Moldova, Transnistria, the OSCE, Russia and Ukraine (the meditation process is not referred to as the “5 plus 2”).
now largely been used up. The real estate, which was under-utilised in the recovery period, has been beginning to decline just recently. Spare capacity, a major problem in the capital equipment sector, is beginning to feel as if it is running out. The labour force, which has been quite effective, is beginning to decline just recently. There are a number of factors which would tend to slow growth regardless of where you look. The rules of the game are different in different sectors. The rules of the game, particularly in the natural resource sector, but also in some other sectors, are very much more to do with direct state control, a somewhat predictable situation, and considerable uncertainty about property rights. I think in most of the first question and ask you if you would like to say something about the main problems currently faced by the Russian economy; how long can the present rates of growth continue; and what are the problems which might lead to their decline?

**Professor Hanson:** I think there are big question marks. The way I would put it is that the Russian economy is a "curate's egg", and it may or may not be a sustainable curate's egg. What I mean by that is not simply that it is a dual economy in the obvious sense in that there is a natural resource sector and the rest, but in a slightly different sense, in that the rules of the game are different in different sectors. The rules of the game, particularly in the natural resource sector, but also in some other sectors, are very much more to do with direct state control, a somewhat unpredictable situation, and considerable uncertainty about property rights. I think in most of the rest of the economy, loosely speaking, in what is below the politicians' radar (which is quite a large part of the economy) there is quite a lot of "business as normal" anywhere in the world. I think this accounts for a lot of the very different stories that go around about the economy. There are a number of factors which would tend to slow growth regardless of that "rules of the game" problem. The labour force is beginning to decline just recently. Spare capacity, which was under-utilised in the recovery period, has now largely been used up. The real effective exchange rate has strengthened, making competition for non-natural resource sectors really difficult and, in general, the fact that the state has involved itself so heavily in the oil industry has tended to kill the goose that lays the golden egg, it is not as drastic as that, but it has certainly in various ways slowed down the growth of the volume of oil production. Earnings remain high because of the price of exports. There is a balance of factors tending towards some slowdown but I do not see a sort of enclosure, I just see some slow down.

**Professor Cooper:** There is a large measure of agreement. Putin has been a very fortunate President because he has overseen the growth of the economy by 6 to 7% a year over this entire period, partly helped by oil prices but not only that, also by the fact that he has been supported by a very competent team of economic managers and a Finance Minister and Economic Minister and Head of Central Bank who have very sound macroeconomic management, and of course Mr Kudrin, the Finance Minister, has now been promoted, and so there is some guarantee that will continue, but I also agree that there are some quite serious, deeper problems if you look a bit further to the future. My sense is that the rate of growth is beginning to slow down and partly because of capacity constraints there is a growing shortage of skilled labour; the labour force is beginning to contract, and this is going to become more and more of a problem in the coming period, and some problems are now beginning to be experienced such as a serious shortage of skilled technical labour and managerial personnel as well. Another problem is the weakness still of the banking sector. It is still a rather fragile banking system and the credit crisis that now we are experiencing Russia is beginning to feel as well, particularly in the consumer credit field. I think there is some underlying concern in some of the financial circles in Russia of the potential impact of this credit crisis on Russia in the coming months, so that is another source of anxiety. I think the deeper problems are that firstly manufacturing industry is in a very poor state indeed, and much of it is simply not competitive, and the rate of investment there is not very high at the present time, and also the fact in
terms of economic policy over the recent period there has not been much reform but any changes that have been made have increased the role of the state in the economy, and this seems to me to be on the whole an unhealthy development. Particularly now as Mr Putin is overseeing the creation of a number of state corporations, there is a danger that within 12 months we will see about a dozen or so large state corporations playing a very dominant role in the Russian economy.

Q49 Lord Anderson of Swansea: The other constraints presumably would include uneven regional development and on the infrastructure side what can you say about the legal infrastructure for doing business and also perhaps the transport infrastructure? How modern is that and will it be?

Professor Hanson: Just to pick up the last point first, there is now the beginning of a major state infrastructure investment programme which is being done on a public/private partnership basis in which a number of major Western construction concerns are bidding, for example on a section of highway near St Petersburg. That will probably make some difference. As far as the business environment more broadly is concerned, there are two very good measures, both of them associated with the World Bank. One is the Ease of Doing Business ranking, where Russia looks pretty poor on an international perspective, and that is made up of a number of scores on a whole range of different indicators.

Q50 Lord Anderson of Swansea: Including corruption?

Professor Hanson: Including corruption. I was going to mention separately another thing which is undertaken by the World Bank and EBRD together, the Business Environment and Enterprise Performance Survey, which shows an increase in corruption between 2002 and 2005. That is not the standard transparency, international corruption perception; that is going and asking businesses what their experience is of paying bribes. Bribe frequency has gone up in the period during which a lot of this increase in state control has happened. I think that is an unpromising situation.

Q51 Lord Anderson of Swansea: And protection of minority shareholders, that sort of legal environment?

Professor Hanson: I would put it like this—and Julian may take a different view perhaps because I think this is a very difficult question—I have heard the manager of a major Western fund operating in Russia for a long time say that he would rather go to court in Moscow than New York.

Q52 Lord Chidgey: It would be cheaper!

Professor Hanson: I think the big problems that we get our attention drawn to, the sort of treatment that Shell has experienced and TNK-BP and so on and some Russian companies as well, I think that occurs when the judiciary get the message that they have put in place, the Kremlin, are interested in a particular outcome and then they do whatever the message tells them to do, and then the property rights become unclear. However, when there is not a message from on high from the presidential administration, I think a lot of things go through in a fairly reasonable way, give or take quite a bit of corruption (but it is more predictable).

Q53 Lord Hannay of Chiswick: We have not in our questions put the demographic issue to you, but perhaps could you just give a comment on that as it affects all these others? I notice you referred to a shortage of skilled labour but, if my understanding is correct, there is a demographic problem that goes much wider than that, but is possibly longer term than we are looking at. Could you comment?

Professor Cooper: I think it is an extremely serious problem facing Russia and I think Mr Putin is aware of it. Mr Medvedev, the Deputy Prime Minister, is supposed to be finding some answers to this problem and so on, but I think with fairly limited success because the problems are so deep rooted. The United Nations latest update of its forecast is that by 2050 Russia could have only 110 million people compared with 142 million now. That trend will continue for practically the rest of the century. This is a very, very unfavourable picture. It is partly because of a very low birth rate, but the birth rate in fact is not that much lower than many advanced Western European countries. The problem is that there is a very high death rate, and it is the fact that the death rate, particularly of the cohort of men from the age of about 20 to 35–40, is extraordinarily high compared to international standards, partly because of alcohol, increasingly because of smoking, and partly by the extraordinarily high accident rates we have in Russia at the moment—industrial accidents and road accidents—and this very high death rate has been at a high level for a long time now and shows little sign of falling. I think the demographic future for Russia is an extremely worrying one looking to the future, and it will have and is having now already economic consequences. It also has consequences for Russian security. Will Russia be able to maintain the size of armed forces, able-bodied men, that it is able to have at the moment and still have a viable economy, if we are talking about a situation where the people of working age of that cohort is greatly reduced? I think it is an extremely serious problem.
Q54 Lord Hamilton of Epsom: Just going back to the question of companies and how a large number of Russian companies have been registering in London. What is the thinking behind that from their point of view?

Professor Hanson: Part of it is straightforward raising funds for investment. When conditions are reasonably healthy over here (and there has been a postponing of some of them lately) and in the recent past it has been a quite good option for raising money. Obviously the stock market is more liquid and wider and in general more helpful here than in Russia, so that is part of it. Part of it is cashing out. There have been some calculations to the effect that quite a lot of the dollars raised in IPOs have simply been the original founder of the business taking a personal fortune out of it and getting out. The other thing that is going on, of course, is borrowing. While the state has enormously reduced its debt to the outside world, the private sector debt has gone up, and part of that “private sector” is the likes of RosNeft and Gazprom, which are state-controlled, so I think one of the difficult things to assess here is how much of that sort of activity is of a healthy kind and how much is not. The other thing, if I could just mention one related thing quickly, is that a number of Russian companies are going global. They are becoming really serious international players: Rusal is the largest aluminium producer in the world; Severstal and Norilsk Nickel, mainly metals companies in fact. They almost certainly have to run their plans past the Kremlin before doing anything but, by and large, I think what they are doing is expanding in the sort of way you would expect any large company with a strong market power in its own home market to do when it has the possibility of doing so, and I think that is quite a normal development.

Q55 Lord Lea of Crondall: The statistics are a bit confusing but economic growth normally would measure national income output and expenditure to have to be the same thing, so if you have got a 6% economic growth rate with a declining labour input, productivity per man and woman (as conventionally measured) must be very, very high indeed, 8 or 9% logically. Can you comment on whether the elements of productivity increase, which are very high, are to do with technology or to do with management and labour efficiency, because there is no reason for a slowdown of economic growth for demographic reasons on that front, and so can you distinguish the different elements of economic growth, because otherwise we will not understand the picture?

Professor Cooper: In fact, the growth of labour productivity over recent years has not been that high in Russia. It has been 5 or 6% a year rate of growth of labour productivity in the economy as a whole. One problem for Russia now is that the rate of growth of labour productivity is being outstripped by far by the rate of growth of real wages. This means that industrial costs are rising quite rapidly in Russia, and it is one of the reasons why competitiveness of the non-energy non-commodity groups is being eroded rather fast at the present time. Another problem for the Russian economy at the moment is the rate of technological innovation, which would be one way of boosting productivity, is really rather low, and Russia has not been successful.

Q56 Lord Lea of Crondall: So you are implying it is balance of payments constraints even though they have got an oil surplus, otherwise why do you mention competitiveness?

Professor Cooper: Russia wants to be able to export goods, and particularly goods other than energy and metals and chemicals and so on, and is finding it increasingly difficult to do so. The only manufactured goods of that kind that Russia is able to export still on any scale are armaments, and mainly to India and China. There is not much else that Russia is able to export, other than energy and metals and chemicals and so on.

Q57 Lord Lea of Crondall: And that is wage costs rather than technology?

Professor Cooper: Partly because of lack of modernisation, since the end of Communism very little investment has gone into this sector of the economy. Now investment is booming in Russia—this year investment will probably grow by about 18%—and associated with that is quite a large growth of imports, and part of those imports now are machinery and equipment, so I think the re-equipment is beginning but still has a very, very long way to go. The capital stock in much of Russian manufacturing industry is a very out-of-date capital stock with very little modernisation taking place. Even in the defence industry, producing arms which are sellable to China, India and Venezuela, the capital stock is now extremely aged with not much new technology there, so this is very profound problem for Russia.

Q58 Lord Chidgey: I have a supplementary on Lord Hannay’s question about demography. You mentioned to us that the death rates are very high in Russia, but could you make a distinction between the demographic statistics in the Moscow region, where the great centralisation is, and the rural areas? I understand there is a significant difference, particularly for example in unemployment where it is much higher in the regions, and of course the other social consequences of that.
Professor Hanson: Of course in almost every aspect of life in Russia today there is a big difference between Moscow and the rest of the country, particularly the more rural areas, and this is certainly the case, so this very high male mortality does seem to be pretty well across the board, but it does tend to be a larger problem in the big cities and towns, the big industrial industries and big centres of car ownership and so on. Clearly there are quite important regional differences here.

Q59 Lord Chidgey: How much has the economic reform programme affected this? I am thinking particularly of the withdrawal of much of the social services support, pensions and so forth; has that had a marked impact on the general well-being and suicide rates amongst the nation?

Professor Hanson: I think the unrest that there was over so-called reform of social benefits was very much to do with a botched attempt to monetize benefits in kind. There needed to be that sort of change, and the initial move was in fact quite inadequate in terms of the funding that went into it, so people were going to get less in money terms than they got in kind (although that varied regionally in fact) and there was enough discontent about that for that to be rejigged. I do not think that is a prime problem. What you do get is because of the very large disparities across regions in the revenue base for regional government, the centre is redistributing from the centre, and a large number of Russia's regions depend quite heavily on transfers from the central budget, and those transfers have a weak equalising tendency. The last time I actually did the figures, which was probably the figures for 2005, so I will not claim to be totally up-to-date on it, show that it tends to be equalising but only weakly, so that there are huge disparities, first of all, on average between regions but I think, more particularly, where people will observe the biggest differences is between the major cities, including the capital cities of each region, and the hinterland of small towns and countryside where, with some exceptions, conditions are pretty dire. There is quite a lot of movement of people, as you might expect, including of course movement from the far north and the far east, westwards and southwards. There is also movement in general into the towns.

Q60 Lord Crickhowell: One follow-up question again on this demographic issue, the report of the Trilateral Commission I have got in front of me puts some pretty startling figures on it here. It talks about a decline in the working population of about 18 million over the next 20 years, with the economic growth figures we are talking about creating a demand for an additional seven million in the workforce by 2015 alone, which is pretty soon. I am not an economist so what I really want your comment on is what are the consequences? If those stark figures are right, and we have already heard that productivity is not actually rising, what happens?

Professor Cooper: I think this is a major policy challenge. There is some discussion now in Russia on this issue. One line of discussion is that Russia must pursue a positive in migration policy, preferably of Russians. The problem there is that many of the Russians who lived in the rest of the former USSR who want to move back to Russia have already moved back to Russia, or they are in countries where the standard of living may be rising even more rapidly than in Russia and so there is no incentive to go back to Russia. Of course, there is an underlying strain of anxiety in this discussion because the obvious place to get labour from is China, and there is some concern about large-scale Chinese in migration. There is quite a bit of unofficial in migration anyway from China and the Far East and there are some quite difficult policy issues around this. There are various categories of workers in Russia, for example there was a very interesting discussion the other day that in Britain and many Western European countries many disabled or partially disabled people work but in Russia very few do, and it is reckoned there are about two or three million non able-bodied people there who are not employed and the moment who could be employed in the labour force, with some very minor, not very costly policy changes, so there are some labour reserves in the Russian economy which still could be drawn in to ease the situation. I think in the longer term it just means that Russia has to invest more in labour-saving technology, especially in manufacturing industry, which on the whole is still very labour intensive.

Professor Hanson: If I could just add something on that, this does raise the whole question of how much investment there is and could be and should be in the Russian economy. There is no iron law that says because your labour force is going down you will get poorer, it is certainly not as simple as that. Obviously the relationship between dependents and working-age people is crucial. One thing one would expect to see to counter a declining workforce is simply an increase in the growth of investment and an increase in the growth of capital stock and possibly substitution not only of capital but also energy for labour. The Russians do have emerging problem now of domestic energy shortages, which sounds weird given the reserves and so on, but it is beginning to be a problem. There has this year been quite a sharp increase in fixed investment, but a lot of that increase is by state-controlled companies and one has to be a bit sceptical about how effective that would be.

Chairman: Lord Swinfen, I think we have to some extent taken up the issue of financial questions but I wonder whether you would like to pursue it in any way.
Q61 Lord Swinfen: I was just wondering what you thought of Russia’s present domestic and international financial position and how do you see it developing?
Professor Hanson: If I could say a few words first. At the moment, Russia has foreign exchange reserves equivalent to about two years’ imports, which is pretty lavish, and it has continued to run a current account balance of payments surplus for some time. All the projections, including by the Russian Government itself, are for that current account surplus to go down, and possibly to disappear by about 2010–2012. The growth rate of imports is very high and in volume terms much higher than the growth rate of exports, so one would expect that to happen. There is lots of room for it to happen however without it being necessarily damaging. In particular the growth of foreign investment coming into Russia, including foreign direct investment particularly, may well tend to offset that, so you will have a declining, possibly disappearing, current account surplus offset by a net inflow of capital.
Professor Cooper: The other issue is that Russia has foreign currency reserves of $425 billion and a stabilisation fund of another $140 billion, so the reserves are very, very substantial. Foreign debt in government has been reduced substantially, in fact Russia’s foreign debt level now is about 4% of GDP, which many countries of the world are very envious of, but private sector debt, as Phil has said earlier, has been growing very, very rapidly. One of the worries now about the credit crisis is this very rapid accumulation of private company and banking debt with the outside world, and so that could create some problems, but at the moment I think the situation is manageable for the next two or three years. I certainly do not foresee any crisis in relation to the finances or another banking crisis for Russia in this period ahead.

Q62 Lord Swinfen: What is the proportion of private debt to GDP?
Professor Hanson: Private external is about 40% of GDP. The overall foreign debt—private plus public—is still quite modest by EU standards, well below 60%.
Professor Cooper: Russia’s debt situation, it seems to me, is manageable.

Q63 Lord Tomlinson: I would like to turn to the prospects for the Russian energy sector. You referred earlier to the dependency of Russia on energy exports. How easy or otherwise do you believe it will be for Russia to diversify the economy in order to reduce that dependency? Also, to what extent do you think Russia is prepared to either continue or expand its use of energy as a political weapon, or do you think they are primarily concerned with maximising economic advantage from the energy sector?
Professor Hanson: Well, I have to say I am not completely convinced by this notion of a very deliberate strategic long-range manipulation of energy supply as an instrument of foreign policy. I am not saying it does not happen at all but I am not sure—

Q64 Lord Tomlinson: It certainly happened with the Ukraine and Georgia, with near neighbours, when they did not appear to be fully in tune with the political wishes of Russia.
Professor Hanson: That is fair but it is also the case that Gazprom—and it is mainly Gazprom we are talking about in this context of prices for gas—has been pushing, for its own obvious fairly straightforward reasons, to have higher domestic prices for gas, and it has been promised that by the Government although it is not legislated yet. It would like to have the prices for Belarus and the Ukraine and so on going up to the prices it gets in Western Europe. I do not think one needs necessarily to bring in foreign policy manipulation. I agree that in those particular cases it probably did play a part but it is not the whole story. The Russian authorities, by which I mean the presidential administration plus the government (the government is technocrats and the presidential administration is the real source of political power) have consistently been concerned to try and see that the economy diversifies, but it seems—and Julian has made more study of this than I have—as though what they are putting their money on is the relics of the old military-industrial complex being rejuvenated and recentralised, if anything, in terms of ultimate control but opened up to various forms of cooperation with Western partners. You get Boeing’s joint venture with VSMPO-Avisma and Finnmechanica having a stake in Sukhoi and so on. There are some quite pragmatic methods but essentially state-driven technological improvement through that partly defence-related sector. That is what they are aiming at; whether it is going to be successful is another matter.

Professor Cooper: Everyone tends to focus on energy with Russia and probably less attention to the fact that Russia is very rich in many other commodities, including timber, but the problem for Russia is that those commodities are not processed to a very high level domestically. They tend to export the raw materials and minerals in fairly unprocessed form. Timber is mainly exported just as trees with the branches chopped off to Scandinavia. I have done an analysis of the competitiveness in terms of what economists call “revealed comparative advantage” and the most competitive good of all that Russia exports indeed is trees with branches chopped off, unprocessed timber. Of course shortly after I
published that the Russians imposed an export duty on trees with their branches chopped off, much to the anger of the Finns and Swedes because their furniture industries were doing very nicely out of this timber.

Russia’s furniture is not competitive at all, so this offers—and there is a growing realisation and even Mr Putin and Mr Ivanov recently have been saying the answer for us to is to move up the value chain for these minerals and materials and commodities that we produce and produce domestically higher value goods and then export them—the easiest way for Russia to diversify rather than trying to jump into high-technology areas like electronics and information technology, where Russia at the moment is extremely backward by international standards. There are possibilities for Russia to diversify successfully in the coming period. Another problem is that at the moment with the diversification efforts that are underway the state is constantly intervening and taking a leading role. It seems to me if you are going to have successful diversification it has to be left to the private business sector to find the right solutions.

**Q65 Lord Tomlinson:** If I may just come back very briefly, I listened very carefully to what Professor Hanson said and I think it was a fairly balanced view, but it seemed to me that the implication of what you were saying was that Russia will have a greater than ever dependence on energy exports if the proposals that you were hypothesising come into effect. Is that the case and is there a sufficient domestic demand in other sectors if they really do not diversify, for them to survive?

**Professor Hanson:** In terms of domestic demand and domestic production outside the natural resource sector, there has been one striking recent study by the Bank of Finland which shows if you take Russian imports from the EU of 25 through to 2006, and look at how they have grown product group by product group, and you look at domestic production in the same product groups, those imports are outpacing the growth of domestic production so the demand is growing, it is being fed at the margin more by imports than by domestic production. A lot of Russian producers slot themselves into a low-quality part of the product range. An odd thing is quite often surveys of Russian producers say that they do not experience competition from imports, which seems to belie the statistical evidence. What that probably means is that they have settled for some low-quality niche in the market and they are doing okay in that but they are not moving up the scale.

**Q66 Lord Tomlinson:** So the whole of the balance of payments advantage that Russia has got at the moment is totally dependent on energy exports?

**Professor Hanson:** Energy and metals; metals are not insignificant. Could I tie up one loose end there. I think they have got real problems in increasing those export supplies in volume terms, and one of the things that would make a difference to that would be raising domestic prices so you get more energy saving domestically, releasing more for export. At the moment that is still some way off.

**Professor Cooper:** Just one point on why Russia is still producing these relatively low-quality goods. Russia is experiencing a problem that Britain experienced in the 1950s and early 1960s where they had the Commonwealth and Commonwealth preferences, which kept alive a lot of rather backward British industry. Russia has the equivalent in the Commonwealth and Independent States (CIS).

Russia can just about produce about 15,000 tractors a year (in Soviet times it produced 200,000 tractors or more a year) and over half of those are exported to the poorer CIS member countries, and so the CIS, to some extent, is keeping alive backward industries and activities in Russia, and with this move by Putin to more commercial relations, I think there is a growing realisation in Moscow that CIS is not entirely positive for Russia’s economic development.

**Q67 Lord Crickhowell:** Can I go back to the energy issue and the issue that Professor Hanson just began to touch on in his last answer. We have the paradox, do we not, that Russia has vast reserves, particularly of gas, but it is finding it extremely difficult to produce and transport enough to meet its own demand, let alone export demand, and that is partly because of the appalling inefficiency of Gazprom which seems to be spending much of its time doing other things than concentrate on energy and the market prices internally, which encourages maximum waste and inefficiency in the internal market. Am I right in that summary and, if so, where do we go from here? Is there any hope that they will use Gazprom, which they are increasingly using as the instrument, and can they get the investment (which they have rather done a lot of to discourage recently) from the international oil companies which might make a difference?

**Professor Hanson:** If you look at the existing Government energy strategy which is on the relevant Russian Ministry’s website, it gives very, very low expected rates of growth of oil and gas output up to 2020. If you take it from the actual figure for 2005 to the projected figure for 2020, it is less than 1% per annum for both oil and gas production. That strategy is due to be revised next year, but one of the things they are at present relying to some extent on is a very big expansion of nuclear power. That is to say that more electricity will be generated by nuclear power.

That involves a nuclear power building programme which I think is probably not achievable within the
timeframe that they have got for it, which is by 2020. They also want to bring in more coal-fired power stations. Complicating all of this, the doubts that have been raised about Gazprom are entirely convincing, what Gazprom has been doing is investing outside its core area. Amongst other things, it has been buying a lot of the newly divested electricity generating companies so that the centralised, hitherto state-controlled electricity system is unbundleing, selling off its production assets, and Gazprom is wading in and buying a lot of them, which is not what Anatoly Chubais, the father of this electricity reform programme, actually intended, so the monopoly problem is going to be still there.

Q68 Lord Chidgey: Just a quick one on the question of the politiscisation of energy supply, particularly to the West. Can you give us any guidance on how much the previous centralised policy-making rigidity in the Russian energy sector is changing? Certainly briefings that we have had (I have had anyway) talk about the concept that Russia has 400 years of gas supplies to meet the EU’s demand but which did not recognise that things might change over time in terms of our dependency or otherwise on such supplies. That was quite startling. The mind-set was “we have got on current analysis 400 years’ supply and therefore forever you are dependent on what we deign to give you.” That cannot be right. What sort of flexibility is coming into the minds of the central powers, do you think?

Professor Hanson: Specifically in the energy sector I think you are right—at least this is my impression—that a lot of the policy-makers and top managers dealing with that sector think they have got a very strong position: “The world will continue to come to us. We have got such large unproven reserves that everybody in the world will want to come to Russia.” There is some foundation for that. International companies are interested in getting whatever foothold they can in the Russian market, knowing that those reserves are there, but the practice that seems to be evolving is to exclude the large fields, not only in oil and gas but in metals as well, so-called strategic assets, in which a foreign owner would not normally, without special provision, be allowed to have a controlling stake and de facto it seems more likely they would not be allowed as much as a blocking stake, which in Russian corporate law is a 25% plus one share. They are saying, “The world will come to us,” and they are creating a situation in which a lot of the major companies, given what they have been experiencing, are not going to be very encouraged.

Q69 Lord Chidgey: So they are not really recognising that international market forces tend to have a play in this?

Professor Hanson: I think that is right.

Q70 Lord Lea of Crondall: One’s impression, and I would be interested in your comments, is that President Putin has got quite a good grip of energy strategy, and indeed Kyoto and all of that, because Russia is obviously going to benefit enormously from the EU Emissions Trading Scheme. Would you comment on how far this huge transfer to a low relative per capita CO2 emitter is part of Russia’s calculations? They are a win/win situation because it does not matter to them if Siberia gets a bit warmer, does it, he is up there advocating Kyoto because he knows financially he is in a win/win situation. Would you comment on that?

Professor Hanson: I would not claim any special knowledge on the Kyoto front as far as Russia is concerned. The impression I have is that it is not something that looms large in their policy-making. There are individual Russian scholars who say, “Look, we have all this forest, it could create a huge carbon sink and the world should be supporting us because of that, and because our polluting heavy industry has gone down so much, we stand to gain,” et cetera, but I do not see the top policy-makers actually saying very much about this or appearing to pay all that much attention to it, to be honest.

Professor Cooper: If you look at the Ministry of the Economy’s forecasts for the next 20 years or so, the rate of saving of energy in relation to GDP is not very impressive, and the only alternative energy source that Russia shows interest in is nuclear power, I do not see much interest in any other alternative form of energy.

Q71 Lord Anderson of Swansea: Hydroelectric?

Professor Cooper: And of course hydroelectric, yes.

Lord Lea of Crondall: It is energy saving but the point is they are in a very strong negotiating position internationally, where there will be tradeoffs with other policies presumably. That was my point.

Q72 Baroness Symons of Vernham Dean: Lord Chairman, I would like to go back to the question of whether Russia is prepared to use its energy exports as a political weapon. I was very interested. You were quite dismissive about that point in saying that you were not convinced about that manipulation. It has got a very firm hold on the imaginations of a lot of Western governments. You would expect the press to be as sensationalist as they want to be over that as anything else, but it certainly does have a resonance in the thinking of Western governments. It is one of the reasons cited in the importance of getting Turkey into the EU, that there are alternative routes, it is one of the reasons everybody wants to find routes from the Caspian that do not go through Russian territory.
Are you saying all this is fanciful and based on over-febrile imaginations, or can you explain why this has such a firm hold on Western European governments’ psyche if it is all such a misplaced notion?

Professor Hanson: I seem to have painted myself into a corner having dismissed this. What I would say is this: I think the particular disruptions of supply that we have seen were badly managed in themselves and the public relations about them was badly managed on the Russian side and sent all the wrong signals and had something to do with the arrogance of Moscow vis-à-vis Kiev in particular. Primarily they were knock-on effects from dealings between Russia and other CIS countries, they were not aimed at Western Europe, and there is a situation, I think, of mutually assured energy dependence. They depend on the revenue. This oil and gas is bringing about half of the revenue into the Russian federal budget. It is 60% of their total export earnings. They depend on this revenue to a remarkable extent. The one respect in which they are in a stronger bargaining position than we are is that they are a unitary actor, more or less, and the European Union, sadly, is not, although perhaps it is trying to be. I see the real problem for Europe as being the weak prospects for Russia being able to increase its supplies to us as much as we would want. I think we need to diversify. We do not have to appeal to the question of what the motivations of the Russian policy-makers are. We need to diversify because they probably cannot supply increasing amounts over the next few years, and that is sufficient reason in itself. They are hoping in part to continue to get cheap gas from Central Asia and re-sell it to us at a much higher price, and the Central Asian states have a quite clear interest, it seems to me, in having alternative routes. In some cases that might be routes to China rather than westward routes, the proposed Nabucco pipeline for example. There is quite a strong interest, in my view, or there should be a strong interest in Western Europe, in co-ordinating our policies, in particular pushing through as far as possible the Competition Directorate’s unbundling policies—and the real problems are in France, Germany and Italy rather than elsewhere—primarily because Russia’s capacity to supply steadily increasing amounts is in doubt. I think its interest in doing so is pretty hard to avoid.

Professor Cooper: I am in complete agreement with all that and particularly that there are other reasons why we should diversify, not just the fear that Russia may suddenly cut off supplies. It is the case that Russia has not targeted any Western European country directly for cutting off energy. It has been the Ukraine, Belarus and CIS countries, and I think there is an issue there. Russia still does not accept Ukraine, Belarus and all the other CIS countries as fully independent sovereign countries, and somehow you can treat them in a different way than you treat real sovereign independent countries like even Estonia, Latvia and Lithuania. I think the treatment of those countries is in fact different to the treatment of Belarus and the Ukraine. I think they accept they are European countries and must be treated in a different manner and that you do not cut off energy to them in that way. It is a learning process. Although there was a slight return just the other day with the Ukraine, about bad debts in that case, and I was surprised that Gazprom acted so quickly in that case, reviving all these fears in that way again, until that point it seemed to me there were some signs that Russia was beginning to learn the lesson that you do not threaten supplies to Western Europe. I thought that was a slightly backward zigzag, as it were, from what it seemed to me an emerging understanding in Moscow of the correct way to behave, particularly with regard to the European Union and energy supplies.

Q73 Lord Anderson of Swansea: There is serious evidence that Russia is seeking to gain control of the lines of route of energy pipelines evidenced by their deal with Kazakhstan Western pipeline and the attempts of Russia to undermine the Nabucco project. Are we to read that primarily in that (a) their economic interests they are seeking to ensure that they have their own cut of whatever supply comes through their territory, or (b) is it part of a more worrying trend of seeking to gain control over resources? One additional point, I notice from today’s press that the Ukrainians are hailing a great new breakthrough when five states have agreed a new Caspian project which apparently analysts are saying is non-viable. It may be non-viable economically but is it justified politically to avoid total dependence on routes through Russia?

Professor Hanson: The Russian interest so far as Central Asia is concerned is economic but it is also more than economic; there is a strong feeling in the Russian policy establishment that “this is our neck of the woods and nobody else should be interfering in this.” They regard projects like the Nabucco pipeline as in some way an attack on their sovereignty almost. It is hard to over-estimate this degree of paranoia. Sometimes I think it is laid on a bit thick for public effect but the sense that we are out to get them all the time is constantly there. It obviously has quite a lot of public resonance. I think it also is something which is genuinely felt. From my experience of talking to Russians in the foreign policy area, they really do have this feeling that we messed them around in the 1990s when they were weak and now they are strong, at the very least, they should be able to do what they want within the CIS.

Q74 Lord Anderson of Swansea: How worried should we be about that?
**Q75 Lord Anderson of Swansea:** Are the Kazakh reserves sufficient to supply both that new deal they have with Russia and a possible Western project?

**Professor Hanson:** I am honestly not sure on the case of Kazakh reserves but there is a big, big question mark over Turkmen reserves and a question mark about Uzbek reserves as well.

**Professor Cooper:** I get a sense of some concern in Moscow now about the possible evolution of Central Asia in the coming period, because the new Turkmen leader is clearly more independent than Turkmembashiri, the late President Niyazov whom he replaced and showing a real interest in developing new relations with China and the United States as well as Russia. Turkmenistan is vital for the Russian equation because, of course, gas supply to the Ukraine is from cheap gas from Turkmenistan, and Turkmenistan is showing signs they are going to put the price up very sharply. The other source of worry, particularly after the CIS leaders’ meeting just the other day, is that Kazakhstan shows increasing signs of independence from Moscow. Nazarbayev is talking about creating a trading area in Central Asia without Russia and that has caused alarm signals in Moscow, and a feeling that maybe in a post-Putin era, where that close relationship between Putin and Nazarbayev might be broken and he maybe will not be able to establish the same relationship with his successor, that Kazakhstan could become an increasingly independent actor in this situation, and not necessarily to the advantage of Moscow.

**Q76 Lord Crickhowell:** We have already touched on foreign investment to a certain extent in energy. The flight of capital has come to an end and moved into reverse recently. What is Russia’s attitude to foreign investment, particularly in relation to their technological and manufacturing sector where their existing skills are so apparently lacking and where there is such a need for investment?

**Professor Hanson:** I think this is quite nuanced, or it should be. As I said earlier, there is quite a lot of business that goes on in a fairly normal way if it is beneath the political radar, so that in areas like confectionary, or beer, or tobacco, shopping malls, retail networks, I do not think the Kremlin gives a hoot who is providing those, and Western firms are piling in in quite a big way. To an interesting extent, to move to a somewhat more sensitive area, there is quite a lot of development towards greater Western development and Western role in the banking sector which some of the Russian leadership had pinpointed as being a so-called “strategic” sector. In their deal with the US last November on the terms of Russian accession to the World Trade Organisation, they secured an agreement that they could reassert controls on foreign investment in the banking sector if that foreign involvement went above 50%. It is highly unlikely to get to 50%; it is about 20% now in terms of assets, but if you look at where the big deals were last year of inward investment, they were in fact in the services sector largely. Then you have got industries covered by the strategic enterprise/strategic industry law that has been passed, which is a long list of things which are mainly defence-related. It is really saying in effect, “You may go along with private enterprise defence contractors but we do not think they are a good thing and they are going to be state-controlled,” but they still allow within that for minority participation by Western partners. They are aware that they need the technology and they need the finance, and so for example you have the state taking over this huge titanium producer VSMPO-Avisma and then around the same time a deal being struck with Boeing to create a joint venture with the same company. It is kind of state-controlled but with loopholes for Western participation, as in the other area in the energy sector where Gazprom cannot deal with the Shtokman offshore gas field on its own. It knows that it needs both foreign capital and foreign technology and, having initially said that it would do it with Western contractors but not Western partners, it then backtracked and has now bought Total in on that, and may well bring in others. So it is an attempt to control in the so-called strategic areas just how much the Western participation is. I think it is dubious how far that can work but that is what they are trying to do.

**Professor Cooper:** A very interesting case in point now is the motor industry. Everyone knows that the motor vehicle industry in Russia is extremely backward and we have the great big Volga Lada car plant churning out up to almost a million cars a year. It is a very, very backward. They are basically still modernised Fiats dating back to the 1960s and 1970s. That plant was taken over by the state. The state arms
export agency took over the Volga car plant, supposedly to modernise it and make a national champion for the Russian car industry. Meanwhile, the Minister of the Economy, Mr Gref, invited foreign producers to come in and build assembly plants and now it looks that about 10 to 12 projects are going to be signed up. Of course, all the leading world car producers are going to have assembly plants in Russia, assembling up to 200,000 or so cars and very soon the motor industry in Russia will be almost entirely in foreign hands. And now the state-owners of the Volga car plant are talking about the possibility that they may invite a foreign partner maybe in to take over the factory entirely because they have realised that they simply have not got the skills to modernise it. Therefore, the motor industry, I think, within five years’ time or so in Russia could be effectively almost entirely foreign-owned, and the question then is: how prepared will the Russians be to allow other sectors to go the same way? There is still this concern about the strategic industries, but up until recently, some in the leadership were talking about the motor industry as being a strategic industry and we do not hear that anymore, so this is flexible and when Russia realises they are having very real problems in doing it themselves domestically without foreign assistance, then the lesson is learnt that it has to be opened up to foreigners, so I think it may be an interesting period in the coming years where the rules could change quite a bit and that should become more welcoming possibly into areas which at the moment they are frightened to do that. I think the aircraft industry is going to be a very interesting test case because I sense that the Russians are beginning to realise now that they lack the technological capability to produce viable, competitive and modern civil aircraft.

Q77 Lord Chidgey: I want to link the last comments that Professor Cooper made regarding the manufacturing industry with the defence industry which we have had a bit of a discussion on by comparison, for example, with the United States and also with ourselves and, to a degree, France where the defence manufacturing sector underpins employment, the skills base and is a huge part of our industrial economy in all three countries. How does it figure with Russia? Now that there is this political decision to modernise and expand the Russian armed forces, as we understand it, with all the caveats you mentioned earlier, the lack of skills base, lack of technology and so forth, what influence is this going to have?

Professor Cooper: The Russian defence industry, I have studied very closely and have done for many years. It is an extremely interesting picture because, on the one hand, they have one or two very successful companies which are modernising and introducing new technology and those are the companies which have been exporting successfully to India and China mainly and one or two other countries as well, so there are aircraft factories in Russia which are able to produce reasonably modern, competitive aircraft now and the aircraft they are selling to China and India incorporate an increasing proportion of foreign components. The avionics are French and Israeli and many other systems now are foreign and not Russian domestically produced. The Russian armed forces still adhere to a strict position of no weapons supplied to the Russian domestic armed forces can incorporate foreign components and, therefore, the very, very few aircraft being supplied to the Russian Air Force now, the Sukhoi-34, are actually probably inferior to those Russia is exporting to India and China because they are not allowed to have foreign avionics. The sensitive area here that is causing more and more worry in Moscow is electronics. The Russian electronics industry is virtually dead. Russia is unable to produce modern, advanced components and chips and so on, so more and more weapon systems, like radar and air defence systems, in Russia are incorporating their own proportion of imported electronic components and this is causing serious worry in the military leadership in Russia at the moment. I think there is a major problem here. My own view increasingly is that if Russia is going to modernise her armed forces in the coming period and the rate of renewable equipment is still extraordinarily low, notwithstanding money being poured in, the problem is that as the money is poured in, costs are rising even more rapidly, so any extra money going to re-equip the armed forces is being inflated away and with very little benefit in terms of actual end-product weapons being seen by the armed forces. This was seen, in our view, as being a failure of Mr Ivanov, the Defence Minister, and one of the reasons why he was replaced by someone who was an expert on finance and business, I think, was partly to get to grips with the economic situation in the armed forces and the defence industry and the rising costs of armaments. My feeling is that increasingly Russia is not going to be able to re-equip her armed forces in a respectable way over the next decade without increasing foreign involvement.

Q78 Lord Chidgey: And the impact on the manufacturing industry overall is?

Professor Cooper: The defence industry actually has still today in Russia some of the highest technology in the country, so it is extremely important. Mr Ivanov sees the defence industry as a locomotive of the industrial renewal of Russia and my own view is that that is an incorrect perception, that it cannot be. In fact, the defence industry in Russia, in my view, is actually one of the biggest problems facing the Russian economy at the moment.
**Q79 Lord Hannay of Chiswick:** I mentioned to you outside that I would like to address questions not on the list that you were given, inspired also very much by the interesting testimony you both given about how difficult it is to be clear how much of Russian economic policy is really state-centred and state-controlled and how much of it really is responding to fairly normal private sector pressures and influences. The question is: does this lead one to suppose that the EU’s relationship with Russia and its main Member States’ relationship with Russia at state level is crucially important to the development of economic relations between Europe and Russia or is it something in which you could almost have a rather cool political relationship, but a very intensifying something in which you could almost have a rather crucially important to the development of economic relations between Europe and Russia?

**Professor Cooper:** In a sense, this follows on from what we have been saying. In my view, there is a great deal of economic activity in Russia which is in a sense below that kind of state priority level which actually goes on with fairly minimum state interference and intervention. My belief is that British and other West European businesspeople can in fact operate there quite successfully almost regardless of the relations at the top between the EU and Moscow or London and Moscow and so on. There is a lot British business going on with Russia at the moment, notwithstanding all the strains and tensions over the Litvenyenko affair and all the other problems. I think a great deal of business is still going on and I do not see any reason why that should not continue in the future, so I think to some extent it can be decoupled, but if you start talking about the oil industry or the gas industry and maybe a little bit more beyond that, then that is where the problem are because it is political if the state is involved, so those relations, I think, are inevitably going to be affected, but otherwise I think there is quite a lot of scope for decoupling.

**Professor Hanson:** I agree with that, yes.

**Q80 Lord Anderson of Swansea:** Has there been any attempt to single out the UK because the Litvinenko affair?

**Professor Hanson:** In terms of business relations?

**Q81 Lord Anderson of Swansea:** Yes.

**Professor Hanson:** I was just looking at the report, I think it is, in today’s FT where there were some conspicuous absences from a Russian UK business forum of people were due to speak on the Russian side. I think there were some gestures of that kind, but I question whether that affects the business that actually gets done. In that sort of high-profile meeting, there is probably perceived to be a point in making some kind of gesture of, “We’re not happy with you” as a part of the message, but that is just, I think, for effect rather than for practical reasons. I do not think it is necessarily going to affect the actual business that gets done.

**Q82 Lord Anderson of Swansea:** Would it spill over, for example, into relations with Poland?

**Professor Cooper:** Poland is now one of Russia’s largest trade partners with extraordinary growth. I think for this year so far Poland is about the sixth largest trade partner of Russia, a very, very sharp growth of trade regardless of the strained political relations between those two countries’ governments.

**Professor Hanson:** Geography is very powerful.

**Professor Cooper:** Geography is very powerful, yes.

**Q83 Lord Boyce:** You have touched on economic reform and the impression I have got, and I may be wrong, is that it is running into the sand if it has not actually stagnated. Is that correct and, if that is correct, what would kick-start it again? Do we have to wait until Putin moves on to where he is going to move on to? Is there something which is going to happen?

**Professor Hanson:** I think that is the correct perception. There are certain things which are still being struggled along with, like the electricity reform, for example, but there has been practically a dead stop in all other areas. That does not necessarily mean that the business environment is not improving for grassroots reasons, coming up from below, but as far as measures of reform from the top are concerned, I think they have really stopped. I share the view of many Russian reformists that the one thing that would really give a kick-start again to reform would be a fall in the oil price.

**Q84 Lord Hamilton of Epsom:** Of course we are in the business of considering what the relationship between the EU and Russia should be, so what should EU policy be towards Russia?

**Professor Hanson:** I wish the EU had a policy towards Russia! I think, first of all, that a stable relationship in which you minimise the scope for big surprises is worth cultivating. Some of the things that Russia presses for, like some rather more momentous treaty-form successor to the Partnership and Co-operation Agreement, I think that is quite unnecessary. A lot of the everyday business between EU countries and Russia and to some extent between the EU as an institution and Russia will go on. Even if there is no replacement for the PCA, it will not stop business happening. I think that is partly it. I think that we have got some leverage on areas like Russia’s accession to the World Trade Organisation where, okay, there has been an EU bilateral agreement with Russia, but we still have to check that the terms agreed there are being implemented and of course we also play a role in other areas, like the agricultural terms of accession. Ukraine—nobody is expecting
that the EU can really set some sort of timetable for negotiations for Ukraine on accession, but I think continuing to show an interest in that and to hold it out as a possibility is something positive because I think that is something which sort of helps to nudge Russia along. “We should be reforming as well”, even if there is no question of Russia becoming a member in the foreseeable future, at least to sort of show that the process of EU enlargement does not necessarily stop where it has stopped so far. I think they are much more provoked by NATO membership than they are by EU membership.

Q85 Lord Hamilton of Epsom: Would it be to the benefit of Russia in the long term to be a member of the EU? Does Russia feel that it is more European than it is Asian to that extent? I did not realise that the population of Russia is so small, only twice the size of Turkey, these great candidates for European membership, so it strikes me as a bit of an anomaly to actually rule Russia out in the long term. I totally accept that there is no question of their joining in the short term, but should we not be holding out the prospect for long-term membership because it might do something about the Russian paranoia which is really riding quite high at the moment?

Professor Hanson: I think Russia finds the EU particularly annoying, as many other countries do outside the EU, partly because of the difficulty of negotiating, who do you deal with and so on, but also I think they have this strong tradition that the way in which you operate a foreign policy is by deals with other big powers. Russia wants to be consulted, it does not want just to be any old candidate for EU membership, it wants to be somehow on a par, “You should be talking to us and in particular you, the big European powers, you shouldn’t be listening to little squirts like Poland”. It is very much a mindset which is not really in tune with the way the EU operates.

Professor Cooper: A question I like to ask my students is, “Why shouldn’t Russia join the European Union?” and then I say, “Make a comparison with Turkey”, and it is quite difficult to answer. The issue here is that Russia certainly under Putin has made it absolutely clear that it has absolutely no wish to join the European Union. I think one of the problems about this relationship is that we started off with very idealistic views about partnership and co-operation and all kinds of activities which seemed to be unspoken and behind that was always the possibility that we might actually one day even consider Russia as a potential member, so you create mechanisms. It is like the European neighbourhood policy where again there is an ambiguity there with all kinds of positive agreements and so on and so on without explicitly saying, “Yes, you will be able to join at the end of it”, but I think that that ambiguity has also been present in the way the agreements have been structured with Russia to date. In my view, any new relationship replacing the PCA should be one which takes as its absolute starting point that there is no question for the time being of Russia joining the European Union. What we need is a constructive relationship, a framework for a constructive relationship with Russia on all the issues of mutual interest and there is no need to go into minute details about everything under the sun which we tend to do in the agreements we have always had with Russia with the four common spaces and so on, so I am a great supporter of having a very simple, focused relationship with Russia and a very simple, focused agreement, just a kind of framework that would have civilised debate, dialogue, discussion and action on matters of common interest and that is all, in my view.

Q86 Lord Lea of Crondall: Just putting the question from a slightly different point of perspective, when you meet official delegations from the Duma coming over here and indeed when one is wandering around St Petersburg on holiday or whatever, you find enormous patriotism in Russia and horror, if you follow Western historiographical thinking that Stalin can be quoted morally with Hitler or something, absolute shock horror, the immediate identification with the Fatherland and with the great patriotic war, yet, “Are we Europeans?” Yes. We all know that we think they are, Shostakovich, Chekov and so on and all the rest of it, so there is that split personality thing. If you go to Turkey, which you have mentioned, the agenda is hugely dominated, hugely, by all the modernisations, economic, social, political, Kurdistan and so on, all dominated by the prospect of membership and one perhaps does look for something which is somewhere between the two. It is not just any old relationship. You do not need to go back to Napoleon or somebody, but everybody knows that historically we have always had wars and so on, so it cannot just be any other country, but you have got to fit the, “It can’t be any other country” point you have made with the “We don’t need to be anything special in an agreement”. They do not quite fit together. Russia is very keen on its line on Kosovo and Serbia. It is not just any other relationship, is it?

Professor Hanson: I think that is fair. I think, first of all, Russian policy-makers and the circles around them make a distinction between Europe and the EU. They will certainly say in many respects, “We are European”, but the idea of Russia being simply a member of—

Q87 Lord Lea of Crondall: I did not mention membership.

Professor Hanson: Okay. I think we are still casting around for some sort of basis on which to deal with them, to do business with them, in the broadest sense.
political as well as economic, in a way that fits with their view of where they should be. They think they are a great power and that they are back to being a great power. They recognise the supremacy of the US of course, but they think they are on a par with Europe rather than on some sort of course to become a part of the EU. They want to be consulted on things which we do not think non-members should be involved in which they want to be involved in.

Q88 Lord Lea of Crondall: How do you do that?
Professor Hanson: I do not think there is an answer to it. I think there is a complete collision between our way of looking at things and their way of looking at things.

Q89 Lord Hannay of Chiswick: Could I just pursue for a moment the WTO argument which you introduced. I thought, but perhaps I am wrong and you will correct me, that once an entity like the European Union has concluded its bilateral negotiations with an applicant, that is broadly that, and now the Americans have done so too. Secondly, surely the question of, “Do the Russians implement the commitments they undertook?” is something which is much better pursued after they are members of the WTO when the whole of the disputes mechanism comes into play? If, for example, the Russians are misbehaving under the terms they agreed, then it will be possible to retaliate between WTO members or to have a disputes settlement panel. Surely, that is better, is it not, than trying to make out of what presumably remains a formal legal requirement for the unanymity of the WTO members to admit Russia, to try and use that as a lever which I think the Poles seem to be groping for over the meat contest, but I just wondered whether you would comment on whether, as to my mind, getting them to the WTO as soon as possible is a sensible objective.
Professor Cooper: In my view, it is, and I think it would be a great mistake if the EU did raise WTO issues again after having concluded a most satisfactory agreement. It seems to me that that would be wrong. There are individual issues relating to individual European countries and Russia and the WTO, like the Scandinavian countries and timber and putting an export tariff on timber and so on, but that is a separate issue to be dealt with outside of the formal negotiations between the EU and the WTO which have formally closed and been agreed. Russia is still not a member of the WTO and I think it is going to take Russia still quite a lot longer to join the WTO. Russia is signed off now with all but two countries. The problem for Russia is that the longer it drags out, more and more countries join the WTO and then Russia has to negotiate with them and the latest is Saudi Arabia and they have almost got an agreement with Saudi Arabia, and the other one of course is Georgia where Georgia have reopened the negotiations and Georgia is refusing to sign. The problem of why Russia is still knocking on the door of the WTO is the delays in Moscow and particularly now on agriculture where the Ministry of Agriculture absolutely refuses to accept the level of subsidy to agriculture which the WTO partners want Russia to accept and there is a stand-off now. My sense is that even Mr Putin has difficulty in dealing with a very powerful Ministry of Agriculture and insists that he make some concessions in order to sign the multilateral agreement at the final stage, so I think it may well be the end of next year or even 2009 before Russia actually joins the WTO, so I do not think it is at all helpful for the EU to make the process even more difficult than Moscow makes for itself.
Professor Hanson: I agree with that. On the technicality of whether in some sense one could reopen questions about the implementation of bilateral deals, I have never followed a WTO accession negotiation anywhere near as closely as I have this current one with Russia, so I do not know what the past experience has been. What I do see is the Americans, having reached a bilateral deal with Russia, are keeping on nagging about how they will come back over the failure to implement the pledges made on intellectual property rights, so they are treating it that way, whatever the past precedents may be.

Q90 Lord Hannay of Chiswick: My question was whether it is in our interests to do so.
Professor Hanson: No, I agree with Julian, I do not think it is.
Professor Cooper: Otherwise, my perception is that the Americans are actually being very helpful to Russia at the moment in trying to overcome the obstacles because I get the sense that Washington wants Russia to join the WTO as quickly as possible.

Q91 Lord Swinfen: Professor Hanson, you were talking a short while ago about the Russians being a big power, and I think it is. Do you think it would be happier dealing with individual states rather than the EU as a whole?
Professor Hanson: I think it manifestly is happier doing that. I think it is a problem for us and when I say “us”, I mean for the EU as an entity. They clearly find it convenient, for example, over energy, but the kind of relationships that can exist between Eon, Ruhrgas and Gazprom, for example, and Gas de France and Gazprom and so on and so on, those create powerful interests in those countries which work through the national political level to facilitate deals with Russia and that is something which runs completely contrary to what the Competition Directorate of the Commission is trying to do with energy unbundling. That is one example of an issue
where, if the EU could act in a more unified way, it would be very helpful, but I think the Russians find it extremely advantageous to deal with Germany, with France, with Italy, et cetera, as they tend to do, and very often to create circumstances which then make it very difficult for a unified EU policy, as, for example, on energy unbundling, to be implemented.

Q92 Lord Anderson of Swansea: Yes, Russia may perceive it as in their interests to deal with a divided Europe. Yes, individual European leaders, Schröder, Chirac and perhaps Prime Minister Blair went off on frolics of their own and were prepared to be divided. Do you detect partly on Kosovo that there is any greater willingness on the part of the new generation of European leaders, whether Chancellor Merkel or Mr Sarkozy who is in Russia at the moment, to seek a greater solidarity in the face of Russia?

Professor Cooper: I have been watching Mr Sarkozy’s visit with great interest and one senses a special relationship between Paris and Moscow being established very clearly and a very, very friendly discussion on all kinds of issues and so on. Of course many thought that when Mr Berlusconi disappeared from the scene, Italian-Russian relations would be affected, but they clearly have not been at all and, if anything, they are even closer. The only maybe exception to that is Germany, so it does seem to me that we are in a situation, whether we like it or not, where individual European powers are going to carry on behaving in this way, carving out their own separate diplomacy with Moscow, so I think for the EU that this is going to remain an extremely difficult issue, possibly with no solution.

Q93 Baroness Symons of Vernham Dean: Given what you have just said about the desire to have these strong bilateral relationships rather than dealing with the European Union, the European Union policy on all the things we like talking about as the great unifiers of European identity, like law, democracy, human rights, good governance, the growth of civil society, being nice to women, equal opportunities and all those other things, do you think that they do have an effect on what is going on in Russia at any level?

Professor Hanson: I think they have the effect of irritating people in the Russian establishment beyond measure. The one thing they do not like is being lectured. Well, there are quite a few things they do not like!

Q94 Baroness Symons of Vernham Dean: Well, nobody likes being lectured, do they, whatever part of the world you go to. However, they are not only our very close neighbours, but a lot of them are over here. They may not like it as an establishment, but they do not half like coming over and joining in.

Professor Hanson: I think the tradition in Russia is of a Russian public policy, of seeing things in terms of interest. They expect us to be acting in our interests, above all, and not to be driven by something called “value”, so anything we do tends to be taken to be in pursuit of some interest. If we have been lecturing them about Chechnya in the past or whatever it might have been, it has always been seen as a ploy to achieve something else and it is not taken at face value if it is about democracy and human rights and so on. I am not suggesting that we should step back on any of those principles, but I think we will constantly be seen as pursuing much more material interests, whatever we do or say, and where we need to be quite clear is that we do not give in on matters like, for example, extradition of people to whom we have given asylum and things like that. If we can convey by example and by practice that there really is a division between the media and the Government in this country or in any other European countries and a real separation of powers between the judiciary and the Executive, we just demonstrate that by not doing the things they want us to do because they think, “Oh, we (Europeans) will surrender this or that person to them. We will extradite someone to them because it will help us in some other way”. If we can establish that there really are limits to this unified view that they have, they think everything goes together, the Executive, the judiciary, the media, the whole lot, and that everybody is under the thumb and that we just do it in a more discreet way, in a more invisible way than they do.

Q95 Baroness Symons of Vernham Dean: You are academics and you have lots of contacts presumably with Russian academics and you have spoken very particularly in terms of the establishment and I imagine that Russian academics are part of the establishment, but do you have any different sort of dialogue at your level of contact with people who actually are quite interested in how the rule of law fits in with the greater civil society, greater civil freedoms and freedom of speech? Is that a dialogue going on at least at the academic level?

Professor Hanson: It does go on. I was speaking with someone who was at one time the Minister of the Economy. He is an academic now, but before he was an Economy Minister and he is an absolutely, straight-down-the-line liberal, a political and economic liberal. You can talk in very straightforward terms, speaking the same language, with a whole lot of these people. These people seem to me, and I may be wrong, but my perception is that they are now completely sidelined politically, they are marginalised.
Professor Cooper: Over this last year at various conferences and so on, I have had quite a lot of contact with not so much academic Russians, but the self-styled political technologists or spin doctors and so on who are increasingly tough in asserting pro-Putin values and the whole value structures in Moscow now, promoting them and ardently defending those, and of course the key term now is “sovereign democracy”. You can argue it to some extent, but only to a limited extent that the whole idea of sovereign democracy has arisen partly because of Moscow’s irritation at constantly being berated, lectured and hectored by the EU and others about human rights, democracy and so on, so sovereign democracy, as I understand it, basically means, “What we have in Russia is democracy. It is our democracy, as I understand it, basically means, human rights, democracy and so on, so sovereign democracy appropriate to Russia and stop interfering in it. Don’t interfere in it, it’s ours and this is what we regard as democracy”. This is why I think we see this increasingly common ground on these issues between China and Russia because it is a shared perception of both China and Russia, major powers in the world, that, “These are issues which in a sense are for us at home and not for others to decide for us or tell us what to do”, and, I get the sense, even with Russia and Iran. Maybe one thing we should be aware of, I think, is that there may be a growing constituency and what Putin, I think, is trying deliberately and consciously to promote is a kind of bloc of major forces in the world who do not accept the European or Anglo-American view on human rights and democracy and believes that they have an alternative which is equally viable and actually more acceptable for their own people. Whilst of course in the EU we do not in any way play down the value of democracy, human rights and so on, I think we need to be much more subtle in the way we get the message over than we have been.

Q96 Baroness Symons of Vernham Dean: Women—what about women in political life in Russia? I know there are loads of doctors wherever you look and there are loads of academics, but what about them? Professor Cooper: There has been a major breakthrough just recently. For the first time ever in Russian history, there are two ministers in the Russian Government who are women, and that is a first in Russia.

Q97 Baroness Symons of Vernham Dean: So they are catching up with a lot of the Arab States? Professor Cooper: This is the first time in Russian history they have had two women at once in the same Government.

Q98 Baroness Symons of Vernham Dean: And at what level?

Professor Cooper: One is the Minister of the Economy, a replacement for the very liberal German Gref who was well known in the West, his deputy, Elvira Nabiullina, who is an extremely capable economist and she is now the Minister and I think she will be a very good minister. The other one is the Deputy Finance Minister, Tatiana Golikova, who is now the Minister for Health and Social Policy. That actually is about the only good thing one can say about the recent changes with the new Prime Minister, Mr Zubkov.

Q99 Lord Lea of Crondall: I am quite astonished. You mentioned the Health Ministry and so on, but how on earth is it the case, with such marvellous clinics in St Petersburg and all these places that one goes to, that the expectation of life is so low or falling or something? Is it just resources for health? You say people do not want to be lectured and so on, but can the EU do anything collectively to make some gesture which would be agreed and accepted by the Russians, like, “Can we help you with your health system?” in some collective way? Secondly, is it not in Russia’s interests that they do not get just a bilateral German relationship which is different from the bilateral French relationship or UK relationship and might it not be better for them to have a deeper EU relationship?

Professor Hanson: There have been quite a lot of EU TACIS projects which provided exactly technical assistance and I have been involved with some of them myself, so it has happened, but I do not think it has created a big impact on the Russian political scene, including in the health service, including projects to improve the delivery of healthcare in particular regions of Russia.

Professor Cooper: The position of the health service in Russia, and I think it is true of many of the ex-communist countries, is that in Soviet times there was the basic provision of healthcare and so on, not to the best standard by any means, but at least there was basic provision across the country almost wherever you lived and you would get some reasonable medical care and attention. Since the end of communism, what has happened is that the funding has been severely constrained to strengthen, develop and modernise that health base, but the new rich and the wealthy now have private health provision or they go abroad for health services and so on, so the political constituency to press for better health for all has been weakened as a result of that and it is only recently now that the Russian economic situation has improved that more budget monies are now going into modernising the health service, but there is a lot to be done there.

Chairman: Professor Cooper and Professor Hanson, can I, on behalf of the Committee, say how very
much we have appreciated the time you have spent with us this morning. Can I just add one comment which I cannot normally do with witnesses, that those of us at this end of the table, including Lord Hannay who is no longer here, who have had long and close associations with the University of Birmingham, we are very pleased that our colleagues have been able to learn this morning what a centre of excellence the University has in this particular area. Thank you both very much.
THURSDAY 18 OCTOBER 2007

Present

Anderson of Swansea, L
Boyce, L
Chidgey, L
Crickhowell, L
Hamilton of Epsom, L

Hannay of Chiswick, L
Lea of Crondall, L
Roper, L
Tomlinson, L (Chairman)

Examination of Witness

Witness: Miss Katinka Barysch, Deputy Director, Centre for European Reform, London, examined.

Q100 Chairman: Good morning Miss Barysch, you are very welcome again. We have seen you on a number of occasions before. You are now batting single-handedly because Charles cannot be with us this morning. You know the rules; we are taking a transcript of the evidence and we will send you a copy of the transcript as speedily as we can. We look forward to you annotating it if you do not think it accurately reflects what you said, or intended to say, and letting us have it back. If I can start off on a fairly general range of things, which will give you the opportunity to make what in effect is an opening statement: what do you think are and should be the fundamental objectives of EU policy with regards to Russia? What does the EU have to offer Russia in the context of a negotiation, and how can it best influence Russian thinking and policy? Linked with it, trying to do it for the other side, how do you think that the EU is perceived from a Russian perspective and what are the underlying principles of Russian foreign policy towards the EU, so a fairly general introductory range of points?

Miss Barysch: I believe that the EU is currently in the process of re-thinking its relationship with Russia. For many years we thought, and we should be forgiven for thinking, that Russia, just like most of the other Central and East European countries, was on a fairly linear path towards democracy and an open capitalist economy. A more difficult path perhaps with more setbacks, but we did believe that that was the way Russia was going, and at one point in time Russia itself believed that that was where it was going. What the EU thought it should do was it should offer help and advice and its own best practice, if you want, to help Russia along that path towards democracy and open markets. For most of that time that we tried to help, Russia has gone in the other direction, but it took us an awful long time to realise that what we were trying to do was not actually working. It was very difficult for the EU, partly because it is attached to its own values, of course, and partly because it is a very complex organisation, to re-think that position. We are now in that process of re-thinking and you see a mixture of attachment to the old strategy and the need to come up with something which is perhaps more realistic. You see that mixture in all the documents and statements that currently come out of the European Union where we still talk a lot about values, and we still push what we perceive are our interests and needs, particularly with regard to energy and security and stability in our common neighbourhood, to the forefront.

Q101 Chairman: Can I just follow on that briefly because you said that it took us a long time to recognise that that linear path towards democracy was not going quite as directly as it should be and might even be going in a different direction in part; was that because we were looking through rose-tinted spectacles at Russia and only seeing what we wanted to see? Do you think there were signs there that should have been recognised earlier?

Miss Barysch: Perhaps. I do believe we saw what was happening in Russia but perhaps we did not believe it, and again Russia itself did not say, “We have discarded democracy, we are now practising a different model.” Russia insisted on calling itself a democracy and to the present day Russia insists on calling itself a democracy. There is always a prefix nowadays calling it a “managed” democracy, a “sovereign” democracy, a “Russian-style” democracy. The striking thing about Putinism for me is that he always insists on leaving the full institutions of democracy in place. He hollows them out but he has not touched Parliament and the formal system of checks and balances. Just consider his clinging to the Constitution, he says, “I cannot continue ruling this country as the President because the Constitution does not allow me.” Everybody knows that he is looking for a way to do that anyway, but because Russia never said that it did not care about democratic rules and standards but formally insisted that it was a democratic country, and that it did respect human rights and the principles of democracy, it would have been very difficult for us to make a grand statement about saying, “You now no longer are a member of the club; we have to change our strategy.”
Q102 Chairman: Just before bringing in Lord Anderson and Lord Hannay, can I ask you on the other part of the question: how is the EU perceived by the Russians? From a Russian perspective what do they perceive the EU to be and what are the underlying principles of Russian policy towards the EU?

Miss Barysch: I think there is a slight difference between the Russian political elite and the Russian people. The Russian people traditionally had a rather positive view of the European Union. That has now changed. There was a rather worrying opinion poll that was conducted not too long ago at the behest of the EU Russian Centre in Brussels, where they found that the Russian people now have a much less positive view of the European Union. They perceive it not as something they want to join but as a threat to their economic independence. I think now that only a third of all Russians think that Russia should build a long-term friendship with Europe. At the level of the political elite, my impression for the limited period that I have been working on this issue—which is about five years now—the Russian political elite has always been somewhat disdainful of the European project, simply because I think they have a slightly different attitude towards what power is and how it should be exercised. I am under the impression that a lot of the officials in the foreign ministry and in the Kremlin have a somewhat old-fashioned attitude towards power: it is about the unity of the state; high politics is about security, it is about territorial integrity, it is about sovereignty. If you look at the EU, which is policy-making by committee, it is post-modern, it is mainly about economics, and the two sets do not fit very well together. The Russian politicians always like to say, “Europe is too complicated for us to deal with and we need to deal with the Member States.” To my mind, that view has changed little over recent years. What has changed is that Russian politicians now deem it perfectly acceptable to be very outspoken about their views on Europe.

Q103 Lord Anderson of Swansea: Our focus as a Committee is of course on the European Union, but do you see any parallels with that of NATO and the NATO-Russia Council in that one began with rather expansionist views which are now seen to be illusory, and both are now scaled down, and that just as in NATO where there has been progress, it has been in specific, often specialist areas—air-sea rescue, which Lord Boyce will know about—and perhaps, equally, within the EU we should abandon the rather grandiose concepts and look for areas equivalent to air-sea rescue where we and the Russians have a clear common interest in working together?

Miss Barysch: I think it is very interesting to explore those parallels. The starting positions were probably a little different because Russia saw NATO as an adversary, so you started from the idea of a rapprochement, whereas the EU and Russia started from the idea that we are already living in a common European house, and then we started drifting apart, so the whole thing is somewhat more emotional, at least on the European side at the moment. It is entirely true that in the EU/Russian relationship we are moving away from that grand rhetoric. It is partly because the key ingredients of the EU/Russian relationship are so uncertain. Firstly, we do not know where Russia is going and Russia itself does not know that. Secondly, we do not now where our common foreign and security policy is going. We obviously have internal divisions in the European Union, and now even more so after the enlargement of 27 countries, which does not make it any easier for us to deal with a country that is changing fast and might be going in a direction that we neither like nor understand.

Q104 Lord Anderson of Swansea: Have you accepted the principle of seeking to isolate specific areas rather than grand plans where we can work together?

Miss Barysch: Yes, that is very much the basis of the common relationship, because if you look at what is happening on the institutional side, the basic legal framework for EU/Russia relations is still the Partnership and Co-operation Agreement, which is out-of-date. But we have moved away from the plan of replacing that with another ambitious and grand bilateral agreement and what we are working on now is the so-called “four common spaces,” which is basically a list of projects and areas where if we can work together we will work together. This is a very flexible framework, a “whatever works” framework that allows us to make progress wherever progress is possible.

Q105 Lord Hannay of Chiswick: I wonder whether if in this rather general part of the discussion you could situate the issue of Russia as a conceivable member of the European Union in these perceptions from the two sides? To what extent was the earlier European perception, which you rightly characterise as now being out-of-date, conditioned by the view that perhaps one day Russia might aspire to membership and that therefore the path which it was on was not totally dissimilar to that of other countries who were aspiring to membership? On the Russian side, perhaps there were similar desires to give reality to the rhetoric of the common European home and so on. Could you also comment on the view expressed, I thought very cogently, by that booklet written by Strobe Talbott and Rod Lyne and a Japanese whose name I cannot now recall, called Engaging with...
Russia, which argued that however unrealistic it is, and indeed how undesirable it is to think of Russia as a member of the European Union, it would be a great mistake for the European Union to say flatly Russia cannot ever be a member of the European Union?

Miss Barysch: As far as I am aware, there has never been a serious discussion on either the European side or the Russian side that Russia should join the European Union. I think to have such a discussion at the present point in time or in the foreseeable future would be unrealistic first of all because the European Union itself is still struggling to digest the last enlargement. We see that in the discussions we are having about taking in the Western Balkan countries or Turkey, which is a country which is not as large as Russia but it is a sizable country, and the mere idea of admitting Turkey strikes panic in the hearts of those who still believe in Europe as a political project, and it is also controversial economically, so from the European side the idea that we could take in a country with 11 time zones and a country which at the moment is so far away from fulfilling the Copenhagen accession criteria simply does not warrant the discussion. Even with a country such as the Ukraine, which has a much better prospect of one day joining the European Union, we are not making any promises, for the simple reason that these promises would not be realistic. If you look at the EU’s internal debate further enlargement beyond those countries that are candidates is a distant prospect or a possibility, but to talk about it does not serve any particular purpose because it is just not on the cards. From the Russian side also, joining the European Union is not a very attractive prospect. Russia, as I tried to point out, is attached to old-fashioned notions of foreign policy-making. It likes to be a member of clubs where the “big guys” meet. It likes to be a member of the G8 because that is where the world leaders meet, that is where great powers talk to each other. It likes to deal with the European Union as a whole because it has woken up to the fact that the European Union is an entity that at least has to be taken seriously at some level. If Russia were to join the European Union it would be one member of the club. The EU, at least in principle, tries to uphold the idea that all Member States are equal. For Russia the idea of sitting somewhere between Portugal and Latvia and having the same say as these countries is completely inconceivable. It would be a very different Russia that would perhaps one day want to join the European Union. Another area where the EU and Russia are very different arises because the EU is the epitome of a legal community and everything we do is based on the rule of law. Russia has a very different attitude towards the rule of law and the implementation and enforcement of law in Russia are a huge problem. So long as that is the case, I think even the idea of integrating Russia and the EU more closely is very difficult. Then, as I explained previously, in order to just gain candidate status a country has to comply with the political part of the Copenhagen criteria which say that you have to have a well-functioning democracy, respect for the rule of law and minority rights; and none of these things apply in Russia at the moment.

Q106 Lord Hannay of Chiswick: I am awfully sorry to continue but you have not actually replied to the question as to whether it would be a mistake for the European Union to say flatly now—and this is the concept that President Sarkozy sometimes pursues of drawing a line—that Russia is on the other side of the line, not because it does not fulfil the Copenhagen criteria but because we do not believe that it is conceivable that it could become a member of the European Union, perhaps with some specious arguments about some of Russia being in Asia. I am sorry to press you on this but it is quite useful to know this because the Strobe Talbott “red line” argument was very powerfully that that would be a mistake, even though you have explained (and I think I agree with you) that it is quite unrealistic?

Miss Barysch: That is a very good point. I think absolutely no purpose is served by drawing red lines around Europe. I have made that argument in another context with regard to Turkey because I am in favour of Turkey joining the European Union, and also for those countries that we are not giving so-called membership perspective to at the moment, such as the Ukraine and perhaps Moldova. I think absolutely no purpose is served because on the one hand if you invited Russia to join the European Union it would be horrified, but if we made it clear to Russia that it would never join, it would be equally horrified. I do not think any purpose is served by drawing borders around the European Union and you probably do not need to answer the question of the potential membership of Russia.

Q107 Lord Lea of Crondall: I suppose you could draw up a list—and maybe you could do it or somebody in Brussels might do it—of what are the matters where there is specifically right now an EU/ Russia relationship and illustrate it to show a multiplicity of things that we could be talking about. We have just done a report on the Middle East peace process and looked at this strange animal called the Quartet, and for a long time Russia was a silent party, but now of course it is developing a slightly independent policy not only on Hamas but also, not a million miles away, on Iran. Do you think that if we draw a blank on Lord Hannay’s direction of probing, we could use a long-standing term (not in this context) “special relationship” and see what would be the content of that special relationship? Clearly there
is the Kyoto emissions trading where because of the pipelines there will be a huge amount of specifically EU relations, certainly not bilateral. Would you comment on would there be such a list that somebody could draw up at the moment? What is the content and the number of things where the EU actually has a joint role with Russia and could you categorise the sorts of things?

Miss Barysch: Could I just ask for clarification purposes, are we looking for areas where the EU has dealings with Russia as opposed to the EU Member States’ dealings with Russia, or are we looking at the international scene where the European Union’s and Russia’s interests coincide as opposed to, let us say, the United States and China?

Q108 Lord Lea of Crondall: The first.
Miss Barysch: Then you would have to probably start by looking at what are specific EU competences and take it from there. Russia started taking the EU seriously through trade negotiations because before that, as I said, Russia found it very difficult to understand the EU as a political animal. When Russia got a bit more serious about joining the WTO, it suddenly found out that Brussels matters because Brussels conducts the negotiations, not the Member States, and Moscow had always tried to lobby in the individual capitals for special deals in its trade negotiations and it found that it had to deal with the Trade Commissioner in Brussels. That is when Russia first woke up and saw that the EU actually matters. Then the Europeans were starting to construct a common foreign and security policy. Russia in the beginning did not know what to make of that. It then started taking it terribly seriously and now has moved a little bit in the other direction. What are the specific ingredients? Trade certainly, but we have now struck a deal for Russia’s accession to the WTO and we are thinking beyond that already, whether we could have a free trade area with Russia perhaps. That is an area where Russia will have to deal with the European Union as opposed to the Member States. We are trying to refocus Russia’s attention in the energy sector where at the moment it engages in tried and tested divide and rule tactics where it tries to forge special energy relationships with the individual Member States. At the same time, the European Union is trying to build a more coherent and integrated energy policy as such, so there are two forces that do not quite work in the same direction but, hopefully, if we get our act together in Europe then we would have an EU/Russia energy dialogue and not a German/Russian energy dialogue, a British/Russian energy dialogue and so forth. Another area that springs to mind is the common neighbourhood. The European Union is still in the process of constructing what is called a European Neighbourhood Policy at the moment. It is still at the initial stages, it is not very well resourced, and the incentives are probably not strong enough to make a great difference in the neighbourhood, but again that is an issue where the EU as a whole should act and interact also with Russia and its neighbours. Lastly, as you pointed out in the international area, the Europeans are trying to do things together such as for example in Iran, but obviously Russia deals with the big three Member States.

Q109 Lord Lea of Crondall: The Quartet?
Miss Barysch: And the Quartet. You also mentioned climate change where the EU as a whole takes a position, but on climate change Russia is not at this present point in time a big player because although it has signed the Kyoto Protocol it is not one of the countries that is at the forefront of the climate change debate. It might one day be—

Q110 Lord Lea of Crondall: Is not the lengthening and deepening of such a list going to look quite formidable as the years go by?
Miss Barysch: We have been pointing out to Russia and Russia has never disputed that we have multiple common interests that force us to work together. When it comes to a special relationship I think we do have a special relationship. Russia is our biggest neighbour and we share this potentially unstable neighbourhood. Both Europe and Russia have a strong interest in having stable and prosperous countries along their borders, so that is where we should work together. Energy obviously. Russia sometimes says that we do not agree on what energy partnerships should look like and they say they will sell their energy to the Chinese or the Americans. At the present point in time they simply cannot do that because all their major pipelines go westwards to the European Union, so that special relationship is very much there. What I was always struck by is, despite these various common interests, how difficult our day-to-day relationship often is.

Q111 Lord Hamilton of Epsom: To follow on Lord Hannay’s point about membership of the EU, one of the unhealthy things about Putinism is that he seems to have developed a paranoid nationalism in Russia, an “everybody is against us” attitude, which goes down quite well with the Russians but is extremely unhealthy from the point of view of the EU and its relationships with Russia. Should we not be putting on the table that we do see them as members of the EU ultimately? I do not think there should be any sort of timescale, we are looking way into the future, but you have talked about the Ukraine and Moldova, if they start the process of EU membership it is going to increases the paranoia in Russia that they are the only people who are not part of this. I just think that makes the thing worse. Surely we should be pointing
out that we would like one day to see Russia in the EU? Maybe it will never ever come to anything. It is gesture politics but I think it is terribly important for the EU to say, “We do not think you are an alien country who is just so much on our borders that ultimately you cannot be a member of the club”.

Miss Barysch: That is an interesting idea but I am not sure I would agree with it. I have been a strong advocate of shifting the EU/Russia relationship away from grand rhetoric and towards more realism. We have spent many years pretending that EU/Russia relations are something they are most obviously not. We are now talking about a strategic partnership. I am not sure that we share many strategic objectives and the way we deal with each other on a day-to-day basis does not always look like a partnership to me. Whilst the relationship is tricky and whilst Russia is in a transition period, I just do not see how we could credibly claim that we want Russia in the EU, even in the long term. Russia has no interest in that prospect at the moment. Even if the EU said that at the political level, it simply would not be credible, so although I agree with Lord Hannay that we should not rule it out, if we now made a statement saying “but one day we want Russia in the EU”, I do not see what purpose would be served by that.

Q112 Lord Hamilton of Epsom: Let us turn to the Ukraine. The Ukraine is not a suitable candidate to be a member of the EU today, but nobody would rule out the Ukraine ultimately being a member of the EU.

Miss Barysch: The Ukraine has for many years expressed a strong interest in one day becoming a member.

Q113 Lord Hamilton of Epsom: Hold on, we are not talking about the interests of the country; we are talking about whether they are suitable to be members. The Ukraine is no more suitable today than Russia is.

Miss Barysch: I do believe that the Ukraine is a lot closer to one day becoming an EU member than Russia is. Russia sees itself as a great power. Ukrainian politics is messy but it is a democracy, of sorts. It is a reasonably diversified economy, although heavily skewed towards heavy industry at the moment. It does engage with the neighbourhood policy, which means that, at least in principle, it accepts the idea that it should take over EU rules and laws and norms. Russia does not accept that in principle. On the contrary, it is completely allergic to any idea of taking over EU rules, so I think the two countries are in a very different position.

Chairman: I am afraid we must move on from the general discussion. I have been very liberal in allowing a very wide-ranging discussion, but I am going to be slightly more rigorous on the more specific questions. We move on to one that you have already touched on en passant but the question that Lord Hannay is going to expand on concerns the institutional framework.

Q114 Lord Hannay of Chiswick: I wonder if you could just say how you think the institutional framework actually works. Does it produce results or is it just a lot of wheels spinning around meetings and not much in the way of results? Secondly, could you comment on whether the delay in negotiating a successor agreement stands in the way of the necessary institutional co-operation or whether the roll-over, which is explicit I think in the PCA, and which will take place now next month as I understand it, and presumably thereafter every November so long as there is not another one, whether in fact that is a perfectly satisfactory short-term state to be in, just from the institutional point of view, not from the political point of view?

Miss Barysch: The institutional framework that we have currently in place is a sort of makeshift arrangement. Some of what was initially envisaged in the Partnership and Co-operation Agreement as a structure of expert committees and then moving up the hierarchy until you reached a six-monthly EU/Russia summit is now defunct and some of that has become an area of contention. When it comes to ministerial meetings, for example, Russia has always been in favour of having some kind of EU/Russia Council there to meet all the Member States at the same time, whereas of course the European side insists on Russia meeting the Troika. What we have done is we have been very flexible about this and under the four commons spaces we have set up a new structure of expert groups. The common spaces idea leaves us ultimate flexibility with regards to the institutions. We can have business round tables, we can have expert groups, we can have ministerial meetings, we can have standing committees, we can have ad hoc meetings, and I think in order to take the institutional question out as a contentious issue and just say “we will work with you, let us just talk, what are the objectives, which kind of institutions do we need to achieve that objective” that works fairly well. With regard to the post-PCA agreement, I personally do not think it is too dramatic that these negotiations are being held up at the moment because we have only just got going on the four spaces idea. It took us two years after having agreed on the four spaces idea to work out the so-called road maps, which list all the possible projects that could fill these spaces. We then started talking about the implementation mechanisms for these road maps. We are still in the process of doing that. I think we should give that idea of pragmatic co-operation a little more time to work. As I said, we are in a period of uncertainty in EU/Russia relations. We are in a period where, yes,
Russia does exhibit a certain amount of nationalist paranoia, so at the present point in time to sit down and start yet another grand debate about common values and where this relationship should ultimately end up might be bad timing. I think we should let things settle down a bit. We should build mutual trust and everyday co-operation wherever we can achieve it and then maybe at a later point in time come back to negotiating a big comprehensive agreement with joint objectives and more fixed institution mechanisms. I think at the present point in time it is not a big disaster to roll over the PCA. The PCA is out-of-date, there is no doubt about it, but it has not held us back. When the PCA was concluded there was no common foreign and security policy, for example, yet we do have a political dialogue with Russia. We have co-operation in justice and home affairs. We have moved into all sorts of areas that were not foreseen by the PCA, so it has not held us back, we can roll it over, and we can continue that more pragmatic co-operation in the meantime.

Q115 Lord Crickhowell: Can we move on to the question of EU solidarity or lack of it. You have painted a clear picture of rather changing Russian attitudes, starting out as disdainful and finding it complicated to deal with, then for example on trade negotiations recognising they had to take it seriously. You have said that they now rather like to deal with the EU as a whole. The truth is they also like to take advantage of the lack of solidarity and deal with the Member States towards Russia. We have co-operation in justice and home affairs. We have moved into all sorts of areas that were not foreseen by the PCA, so it has not held us back. Can we roll this out, and we can continue that more pragmatic co-operation in the meantime.

Miss Barysch: There is clearly a need for greater solidarity for our own sake because the EU is obviously based on the idea that we have common objectives and common interests in foreign policy and in energy policy and in the other areas that affect our relationship with Russia. Disagreements over Russia have in recent years sometimes poisoned the atmosphere. That is not very healthy for the European Union because it could spill over into other areas of co-operation. It is also very important that we stand more united in Russian eyes because the way we are divided at the moment, the Russians can almost claim, “We cannot deal with the European Union; there is no EU position, you are divided, you are complicated; we have to deal with the Member States.” When Russia says “Member States” of course it means the big Member States, not the small Member States. That then reinforces the EU internal divisions because the smaller, newer Member States think that their interests are not being taken into account when the EU deals with Russia, so there is an urgent need for more of an internal debate about what the individual Member States want and need from Russia. We have done surprisingly little in this respect. We have various forums where the Member States can meet and talk about their attitudes towards Russia and what should be done, but somehow this has not worked so we probably need more of that.

Q116 Lord Crickhowell: Can I pick up one point that arises from that. You spoke about the desirability of it and you referred to some of the smaller and newer states, but of course the very fact that they have strong views and are near neighbours very often makes it even more difficult for Europe to take up a common position because they resist what the marginal and further away states think should be their position.

Miss Barysch: Yes, and they had a point initially because there was a group of leaders in the big existing Member States that was not really inclined to take the smaller, newer Member States terribly seriously. Instead they took every opportunity to build special relationships with Putin and get photo opportunities and they never liked to criticise him in public. Now all of these leaders—Schroeder, Chirac and Berlusconi—are gone so there is a better chance for EU unity just because at the level of leadership we have had a change-over. Angela Merkel has been both more outspoken about Russia’s democratic shortfalls and she has made efforts to consult the new Member States and take their views into account. When Europe formulates its Russia policy you see Nicholas Sarkozy also being more willing to criticise Vladimir Putin than Chirac was. You see obviously the UK/Russia relationship being somewhat frosty at the moment. I think if there was a common relationship the distinctly pro-European Italians would not throw a spanner in the works so from that perspective you can see a greater chance for EU unity. When the new Member States came in, some of them probably thought that the European Union was a good way of amplifying their own individual criticisms and grievances that they might have had with Russia. That was not a good idea because it allowed the Russians to claim that EU foreign policy is now run from Latvia. That is so obviously not the case, but the Russians particularly like to emphasise that: “Now we cannot deal with Europe any more because it has all become completely ridiculous.” I think we have overcome that phase. You do not see the new Member States taking one position that is distinct from the old Member States. On the contrary, you see some countries having big problems with Russia at the moment—Estonia, Lithuania and Poland—and you see Latvia, for example, having a remarkably good relationship with Moscow at the moment. You see some countries such
as Slovakia and Hungary mimicking a bit what the old Member States have been doing in building special relationships and doing bilateral energy deals. It is not that you have old Europe versus new Europe in dealing with Russia, and I think now at the level of political leadership the constellation is better than it was before. We are also having Polish elections which might help, and from that perspective I think we will see a convergence of views, and I am quite optimistic that we are moving towards a more coherent policy on Russia.

Q117 Lord Chidgey: Can I just turn back now to Russia’s view of the EU. You talked earlier about how Russian foreign policy still seems to be set in the old-fashioned view, particularly amongst the senior political establishment in Russia, and almost set in stone if you like in the traditional, centralised way—this is where the great powers stand; this is where Russia stands—and I am interested to know how Russia is able to adapt, or not adapt at all perhaps, to the very fluid and changing perspectives in the Western world. We are having our own issues about how we deal with the expansion of the EU and all the opportunities and challenges that provides. Is this a more, if you like, frightening perspective for the Russian political establishment in the sense that they are not part of it, whereas we are very much trying to ride the tiger, so to speak? Do they see the situation of relations with the United States, with China, and with India and so forth, as a more comforting scenario than the dynamics in the EU, which are perhaps far less predictable in Russian eyes? Do they see the EU as an irritant rather than an opportunity in comparison to the other global powers?

Miss Barysch: If you listen to Russian rhetoric, you would sometimes think that they see the EU as an irritant, but I think they are fully aware that if they look around their borders and to the wider world, Europe is their most reliable partner, their biggest market, and probably the entity or the bloc of countries that is easiest to deal with.

Q118 Lord Chidgey: By that do you mean the easiest to influence?

Miss Barysch: Certainly easier to influence than, say, the United States or China. I think Russia is fully aware that the potential for partnership with Europe is bigger than with any other country or group of countries. No, they do not quite know what to make of the European Union. I am under the impression they have rethought their attitude towards the EU. Europe at one point in time for Russia was the only game in town, it was the parameter against which everything else was measured. There was a time in the early 1990s when they talked about a “common European house”. Now Russia sees itself as a great power, it has a global perspective, and it no longer thinks that Europe is the only parameter against which it should measure its progress. There is something called BRIC out there and it is a club of rising, emerging powers that has an “R” in it standing for “Russia” and that is a much cooler club at the moment to belong to than the somewhat sclerotic and squabbling European Union. Russian obviously thinks that its relationship with the United States is tremendously important and is also trying to make sense of where China is going. There is not much trust perhaps in Russian/Chinese relations but they are certainly trying to strengthen their ties. I think Russia is struggling to position itself globally and the EU relationship might be the easy bit because it is a very close relationship, it is a relationship that is living day-to-day through trade and through the multiple links that we have with them. Despite the somewhat disdainful rhetoric that is sometimes coming out of Moscow, I think that most Russians are fully aware that the potential for partnership here is greater than with most other countries.

Q119 Lord Anderson of Swansea: Surely the test for EU foreign policy is not whether we can agree on Burma and Darfur but whether we can agree on matters directly affecting our own interests in our own neighbourhood such as Kosovo and Russia. Despite what you say about the change of Chancellor Merkel as opposed to Chancellor Schroeder, President Sarkozy as opposed to President Chirac, and Prime Minister Prodi as opposed to Prime Minister Berlusconi, who stand up more to Russia, they still favour pursuing their own policies on the economic side, particularly on the energy side. Prime Minister Prodi is no different from Prime Minister Berlusconi in respect of Italian oil interests. Do you agree?

Miss Barysch: I agree that on the energy side we run the risk of having a kind of beggar-thy-neighbour policy in energy at the moment where each country scrambles to secure its own energy needs, not really thinking about what its neighbour’s needs might be. I am nevertheless hopeful that if we make some progress in building a more integrated Europe energy market, our interests and needs in the energy sector would coincide and converge and then perhaps we will have a more unified position towards Russia. At the moment I admit that is not happening because you see German companies doing deals with Gazprom, Italian companies doing deals with Gazprom, French companies doing deals with Gazprom and these contracts that they are signing will last for 30 years. How we unscramble these bilateral deals I am not entirely sure. However, I do believe if we make progress with building a more European energy policy then that would really help tremendously. Gazprom making threatening noises...
and Gazprom trying to buy downstream assets in Europe might focus our minds on the need for unity. **Chairman:** I am going to move on to a whole raft of questions on the Russian economy. In order to protect the interests of people who have got interests in later questions, I am going to appeal for fairly short, succinct questions, and the economic ones are capable of shorter, more succinct answers as well, so Lord Hamilton?

**Q120 Lord Hamilton of Epsom:** Putin may think that Russia is a great power but it certainly has not got a great power economy. It is extremely narrowly based. How long can these growth rates go on? There is certain evidence coming through that the renationalisation of the energy sector is leading now to very poor records on new exploration and that sort of thing. What is going to happen to inward investment going into Russia in the future? How do you see all this mapping out?

**Miss Barysch:** At the moment the party is certainly still going on. Russia is growing by 7% a year and has attracted—

**Q121 Lord Hamilton of Epsom:** That is mainly the rising oil price rather than more oil and gas. **Miss Barysch:** Absolutely, it is an oil-dependent economy, but as long as the oil price keeps high, or even rising, the Russian economy seems to be doing very well. They have to be congratulated on their very sensible and responsible macroeconomic management. That could have gone very wrong, if you get that amount of cash flowing into your economy, and to be as responsible as the Russian Government has been in saving a lot of that money, putting it to one side, putting it into funds and working on many responsible proposals on how to spend that money, that is all good. However, now they have the cash sitting here, they have the programmes in place for what they want to do with it—education, infrastructure, modernising their defence forces and what have you—which they do not have is the administration to spend that money. They are sitting on the cash and yet they cannot give it to the local administrations and the agencies because it will be lost or stolen, so that is the biggest problem they have at the moment because that means that the infrastructure is getting increasingly out-of-date and the economy is not diversified.

**Q122 Lord Lea of Crondall:** Is not the Russian economy in some respects part of the European economy now? You wander round St Petersburg—I happened to be there on holiday—and there are euros in the shops and all the usual chains. Although it is a very different place I am talking just about consumers. Forget Christendom or wherever it is, we are talking about consumers here and there are euros and they have got the reserves in euros and da-di-da-di-da and all the usual people who you would expect to be selling cars in Winchester seem to be selling cars there, so in a sense would you say the European Union is there but not there as such, but it is becoming part of the European economy?

**Miss Barysch:** I would very much like to attribute your experiences to our success in EU/Russia relations, but I am afraid it is just good old globalisation, because if you look at the big supermarkets in Russia they are Turkish and Coca-Cola is as ubiquitous as European soft drinks. So I think it is just a sign of the opening up of the Russian economy. It is quite an open economy and fast-moving consumer goods companies are making an absolute killing in the Russian economy because there is so much money flowing around. European companies are taking good advantage of that but it is not a specifically European phenomenon. We have more economic co-operation programmes in place with them than any other group of countries, but obviously the opening that we are trying to achieve in Russia benefits everybody else as well because they can do business more easily in the Russian market. **Chairman:** I am going to move on to the next question and you have got an interest in that one as well. Lord Boyce?

**Q123 Lord Boyce:** I think you have already given an indication of the premium that Russia puts on its energy resources and obviously it seeks an economic value of the energy resources. Do you think that it needs to diversify? Does it think it needs to diversify? It is all good at the moment and it is helping its growth and so on, but is it capable of diversifying? Do you think part of the value it puts on its energy supplies is that it wants to retain it as a weapon as well, which some people have speculated they might want to do, as opposed to just drawing maximum economic benefit from it?

**Miss Barysch:** Let me start on the first part on diversification. For years Russian politicians have said consistently that they want to help diversification because they are aware of the fact that basing an economy the size of Russia with 140-odd million people on just one or two natural resources is very dangerous because global prices tend to fluctuate, the macroeconomic administration is very difficult, and it does not create jobs. Only 1% perhaps of the Russian population works in oil and gas. You need to have that diversification but in order for that to happen and to be sustained, you need a business environment that encourages investment, innovation and competition. Russia has a very difficult business environment in that respect, where you do not have the rule of law, where you do not have an independent court system, where you have state inference, which can be quite pervasive. At the
moment you have state interference mainly in those sectors that are regarded as strategic—energy, some metals, defence and transport—and relative liberalism in the other sectors, so you do have some business dynamism in Russia but, as I said, this is more a consumer play rather than a production play. The manufacturing sector in Russia is not very well developed and as long as the business environment stays as difficult as it is, the outlook is decidedly mixed. On energy as a strategic sector or even a political weapon, yes, obviously there has been a rethink. When Putin first came to power he was talking about breaking up Gazprom, but that is completely off the table now because they have realised that state control over these energy resources is their strongest means of power, not only vis-à-vis domestic companies and businessmen and oligarchs but also vis-à-vis their neighbours, partly as a means of pressure on countries that are going in a direction they do not like, partly because the pipeline monopoly they effectively have allows them to channel Central Asian and Caspian energy resources through their territory, but that they will ever use it as a weapon against the West, I am not entirely sure. They make a lot of angry noises sometimes—that whole debate about reciprocity—but there is no precedent where Russian has used its energy resources as a political weapon against the West.

Q124 Lord Boyce: You already mentioned earlier on the fact that the dialogue tends to be between Russia and individual nations and not Russia/EU. Is there any hope of the EU ever developing a policy for the EU on energy towards Russia whilst individual countries are scrabbling to make sure they maintain their relationship with Russia?
Miss Barysch: I do believe it is possible if we make progress on internal energy market integration so that our interests converge.

Q125 Lord Lea of Crondall: Does the huge importance of energy hold the key to this new kid on the block called sovereign investment companies? The EU has a difficulty with sovereign investment companies because on the face of it, that is not allowed in European competition law the way it is structured in Russia. However, Germany seems to get along with them all right and France seems to get along with them all right. Do you think these sovereign investment companies will present a problem for EU/Russia economic relationships?
Miss Barysch: When the EU put out its new energy liberalisation package, there were some clauses in there that said perhaps foreign-owned investment vehicles and energy companies would not be allowed to buy European pipelines unless European companies in turn are allowed to invest in their home markets. This is a mixture of reciprocity and a debate about sovereign wealth funds. I think the Europeans need to have a lot more debate about how to make that operational. Russia obviously was very upset about that. I do not think we particularly need to be lectured by Russia on energy market liberalisation because I do not think they have much to say about the topic, so we should not be afraid of that. We do need to have a more coherent debate because what we are trying to do at the moment mixes up two things. We either say that no company that supplies energy should be allowed to own pipelines—and I would fully support that—it is called ownership unbundling and if it applies to Gaz de France it also applies to Gazprom, but there is a different issue then here where we say maybe we could allow Gazprom pipelines, if they open up their energy market in turn. That is reciprocity and the two things should not be mixed.

Chairman: Lord Anderson?

Lord Anderson of Swansea: I think my question has been largely covered in terms of the differentiation in Russia between the investment sector and the retail sector.

Chairman: I am happy with that if you are happy with that. Let us move on then to question nine and Lord Chidgey.

Q126 Lord Chidgey: It is a rather extensive question and I will therefore try to keep the question somewhat succinct. In the questions which you have had in advance we talk about what is happening in the manufacturing sector, services, small and medium-sized businesses and agriculture. I would like to home in on the manufacturing sector and particularly the defence sector. Other colleagues may wish to add to these points later. We have heard in previous evidence that the defence sector in Russia is rather strange. It certainly has the same impact on the overall industrial economy, as it does in the major powers such as the USA, Britain, France, in terms of the dependence for the development of the skills base on the defence industry to flow through into the manufacturing and industrial sector. The difference seems to be that the electronics industry in Russia has basically collapsed, we understand, and that of course is the driving force for manufacturing development and research in the Western world. So much so in Russia, we understand that the exports to China and India, for example, are dependent on avionics and electronics imported from other countries such as Israel, but because of Russian defence policy those state-of-the-art electronics are not available to the Russian domestic products in their own defence force. That seems to be a rather strange situation. I wonder if you would like to expand on that particular view for me.
Miss Barysch: I wish I could but I am not a defence expert, so I think I have to pass on it.
Q127 Chairman: If you could give us an overview of the sort of sectors that were outlined. Have you got a broad view of manufacturing, if you cannot get into the specifics of that particular sector?

Miss Barysch: As I said, going back to the question of diversification, Russia is already showing signs of what used to be called the “Dutch disease” because its currency is strengthening and its very large balance of payments’ surplus that it gains from oil and gas exports is shrinking fast because imports are growing so fast. Russia is more and more using its oil earnings just to buy things abroad rather than producing them itself. As I said, it is a very difficult maco-economic management question which so far they have mastered reasonably well. They have a lot of money coming in through the oil and gas sales and this normally pushes up inflation, but what the central bank does is it buys all the dollars, puts them in international reserves, but you will still get a real appreciation of the currency over time. The competitive boost that they got from the 1998 devaluation is now gone, so they need to increase productivity, which is the only way they will be able to compete in manufacturing in world markets. That, as I said, would need investment, innovation and competition, which is where it all falls down. They have that mixture of a rising currency and automatic loss of competitiveness on the one hand and then they do not have the domestic driving forces that would allow them to compensate for that loss of competitively.

Q128 Chairman: In the meanwhile what is happening to the skills base?

Miss Barysch: Russia’s education system is half reformed. Because it is a juggernaut it is very difficult to turn around. What happened is that part of the education system has simply been privatised. You do have business schools where they produce very good graduates that are adequate for the market economy, but there are not enough of them, so they definitely need more investment in the education system and they need to urgently reform the rather rigid higher education system that they have.

Q129 Lord Chidgey: On this section here we are talking about agriculture and how can Russia feed itself. I am not quite sure how this links into the EU, by the way, bearing in mind our own agricultural policies and the CAP and so forth, but are there any implications for Russia in the difficulties that it may have in feeding its population of a closer relationship with the EU or are they totally independent of each other?

Miss Barysch: Russian agriculture has improved over recent years because they made some important reforms such as liberalising the agricultural land market, which went so far and then got stuck. They made it easier for farms to get credit; they introduced some market forces into the agricultural market, and the market responded very well; and there is a relatively vibrant food processing industry in Russia, so agriculture is not the disaster it was a few years ago. It is growing rather slowly at the moment because, as I said, the reforms were started but then they got stuck. Russia certainly does not face any food shortages. A few years ago for the first time in I do not know how long it became a grain exporter again. Now the Government wants to use some of the money it has saved from the oil earnings to subsidise the agricultural sector to a greater extent, which is why its WTO bid is stuck, by the way. The agricultural sector is actually doing reasonably well. Chairman: I think it follows on from this and we have part-covered it but the next question is Lord Boyce.

Q130 Lord Boyce: We have indeed, my Lord Chairman, and it is about economic reform. As you have been implying in your answers, the impression is that economic reform has stagnated for the reasons you have given. Perhaps you would like to say something about what might get it going again. A crash in the oil price would obviously have some effect but are there any other factors that could cause them to get a grip or, as you have implied, must they get their legal system sorted out before they really can shake this out?

Miss Barysch: I believe that administration is most definitely one of the biggest problems that Russia is facing. During his first term, Putin did a lot of very good and sensible reforms but they tended to be the easy ones, the top-down ones: you liberalise, you cut taxes, you do all the things that you do not need a big administrative apparatus for implementation. They did all these things, they were successful, and the tax system has improved immeasurably in Russia but, in order to do the more difficult things that they need to do now, which have to do with local services for example, with improving education and health care and so forth, they would need to have a more efficient professional state administration, and there obviously you have the political obstacles to that. Despite the fact that this is not necessarily a democracy in the Western sense, for Putin and his successor it is very important to be popular and to have popular support. The public sector is large and growing fast. Russia now has many more bureaucrats than the entire Soviet Union had at the time of its collapse. This is where Russia creates jobs and if you start antagonising these people by saying, “I am really not going to allow you to take bribes any more; I really will insist you stick to all the rules and regulations we have put in place.” I do not think that will be very popular.
Q131 Lord Hamilton of Epsom: Do you agree that there is a better functioning capitalist system in Communist China than there is in Russia?
Miss Barysch: That is a very wide-ranging question. Let me try and answer it in this way: if you look at surveys of international companies that do business in both markets, they tend to say that Russia has in some ways a more difficult business environment than China has but their profits are much, much higher in Russia, which is why they all want to be there.

Q132 Lord Hamilton of Epsom: Because there is tonnes of money sloshing around.
Miss Barysch: And because there is less competition, but I would like to leave it at that because I do not feel in a position to compare Russia and China in the two minutes that we have left!

Q133 Chairman: If I can bring you to the very last question, we are now in the run-up period now to the election: have you any thoughts that you would like to share with us in this pre-electoral period?
Miss Barysch: First of all, I would be somewhat reluctant to call it an election, it is a changeover or handover of power. When people now say that Russia cannot reform or Russia cannot do this or that because it is an election period, I do not think that holds quite true because they do not face the same sort of electoral pressures that you would see in Western democracies. The standard assumption seems to be that Putin chooses his successor, whoever that might be; that this successor will then be confirmed in a free, but not necessarily fair, election; Putin will continue to somehow wield power from behind the scenes, and that little else will change. We will still have a managed or sovereign democracy; we will have a mixture of capitalism and state interference; and we will have a foreign policy where Russia tries to dominate its neighbourhood and oscillate between co-operation and confrontation with the West, so that Putinism continues without Putin. I am a little more sceptical because this is a system of power that is closely tied up with wealth. If you move a little bit from your power position to somewhere else a couple of billion dollars might move with you. Since this is the case in a system that has no established institutions for handing over power and it has no property rights, I would expect there to be a few hiccoughs as people try to secure their gains and their positions. I am also somewhat sceptical about the idea that you can plant somebody in the Kremlin and run things from behind the scenes, because I am under the impression that authority comes with sitting on the throne in Russia. It will be the new President who would do all the media and make the decisions and sign the decrees and go to the G8 meetings, and I am somewhat sceptical that you can run Russia from behind the scenes, so I would expect a little more political instability during the changeover period than most other people seem to expect. What strikes me is that on the one hand we say we do not like the Russian system because it is not democratic; on the other hand, we all seem to take an awful lot of comfort from the fact that nothing will change when Putin eventually leaves, but I am not sure that that will hold true.

Chairman: I am going to give the last word to our Chairman who has joined us. Lord Roper?

Q134 Lord Roper: I wonder if I could just ask one supplementary. You have obviously concentrated on the more interesting election, the presidential election; is there anything worth saying about the Dumas election, which we will be getting to first?
Miss Barysch: United Russia will have a majority in the Duma. The only question is whether that will be a simple majority or a constitutional majority. Apart from that it will probably remain a rubber-stamp Parliament.

Chairman: Can I say, Miss Barysch, that you have certainly served the Committee well this morning. You seemed to doubt, when I was saying hello to you before we started, whether you would have enough to keep us going for an hour. You have kept us going for well over an hour and could have kept us going for much longer. Thank you very much indeed. We are very grateful to you. You will get the transcript, as I said at the beginning, and we look forward to receiving it back with any annotations that you care to make to it.
The political relationship between Russia and the West is at its lowest point for two decades.

This could become a “confrontation”, but is not one yet. Neither side is deliberately seeking to confront the other. Relations in areas outside high politics remain generally constructive and friendly. The growing economic interdependence of Russia and the EU is a powerful constraint, including in the energy sector.

The current animosity stems partly from events, partly from reasons internal to Russia, and partly from the inability of Russia and the West to understand each other.

Russian reformers in the early 1990s had wildly unrealistic expectations of the speed with which Russia might be integrated into the West. They now feel let down and rather bitter. The current Russian leadership for the most part does not understand, and does not wish to understand, Western processes. It has no experience of living under the rule of law or the separation of powers; and, sometimes wilfully, it misinterprets Western actions.

We in the West had equally unrealistic expectations about the speed of change in Russia. We tried to assist the transition, but failed to appreciate how deeply humiliating, painful and destabilising the 1990s were for the Russian people.

There are disappointed expectations on both sides—what Solzhenitsyn has called “the clash of illusory hopes against reality”.

Russia is going through a negative or revisionist cycle in a long process of transition. It is not the end of the transition; but we must wait for 10 to 15 years before the first generation of post-Soviet leaders comes to power in Russia.

The economy is now a market-based system. Thanks to high oil prices, but also to sound macroeconomic management and rising domestic demand, it has been through a seven-year boom. The expansion of Kremlin-controlled conglomerates is regressive. More difficult times lie ahead—but a few years hence this may bring the economic liberals out of hibernation and lead to a new drive to modernise the economy. A new generation of Russians engaged in business and a growing middle class look like the most likely agents of change in the country.

Politically, Russia has yet to develop a new model. Gorbachev and Yeltsin gave Russians freedom—and Russians still enjoy wide personal freedom, although some constraints have recently returned. But democracy barely started in Russia. For the past few years the Kremlin has been focusing on control. There is at the moment no political development. But there will need to be: a huge country dependent on a single institutional and a single personality is not stable. As President Putin recently said: “We cannot build Russia’s future by tying its many millions of citizens to just one person or group of people. We will not be able to build anything lasting unless we put in place a real and effectively functioning multi-party system and develop a civil society that will protect society and the state from mistakes and wrong actions on the part of those in power”.

The third, and most difficult, facet of the transition has been Russia’s adjustment to its new status as a smaller and less powerful country than the Soviet Union. Other former Great Powers and Empires, including the United Kingdom, have found this a long and painful process. It has been much more difficult for Russia because the collapse happened without warning; the empire was contiguous; and territories which were regarded as part of the Russian heartland—most of Ukraine and Belarus and Northern Kazakhstan—suddenly became independent. It takes much more than half a generation to come to terms with this—on both sides of the divorce.

In its Common Strategy of 1999, the EU said that it was seeking to build with Russia “a genuine strategic partnership, founded on common interests and shared values”. Similar language is to found in the 1997 Partnership and Cooperation Agreement and the 2004 Road Map for the Common Pace of Freedom, Security and Justice.”
These aspirations have not become reality. We have a conflict of values, for example over the rule of law, which inhibits strategic partnership. Our interests converge in some areas—such as counter-terrorism, WMD proliferation, the environment, trade and investment—and diverge in others. They diverge most strongly in the arc of states from the Baltic through Belarus, Ukraine and Moldova to the Caucasus. These are substantive differences between Russia and the West.

The anti-Western mood in Russia is also being played up for reasons of internal politics. The idea that Russia is besieged and encircled by malign forces is a useful device for binding the nation, deflecting blame, justifying central control and the reinvigoration of the organs of internal security, and discrediting external criticism.

How should the EU and the West respond to this?

— We need to recognise that this a phase which will last for several years, but not for ever. Events within Russia will determine the country’s future course. Our influence is not zero, but it is marginal.
— We need to develop a shared analysis and better understanding within the EU. The process of debate and analysis within Europe is weak and fragmented.
— Founded on that shared analysis, the EU urgently needs stronger policy coordination and a common approach towards Russia.
— The common approach should be based on clear principles, including that the EU:
  — opposes a new division of Europe and seeks to dismantle barriers;
  — wants to see Russia strong, stable, prosperous and modern;
  — acknowledges Russia’s right to defend its own interests and pursue its own independent policies within the parameters of international law and of the sovereign rights of other states;
  — seeks to promote harmonious and stable relations between Russia and all of her neighbours and the peaceful settlement of disputes;
  — is not seeking to expand its influence at the expense of Russia, but will oppose any encroachment on the sovereign rights of any European state; and
  — will defend its own interests and values robustly where they are challenged.

In practical terms, the EU should for the time being shelve the concept of “strategic partnership”. It is premature. It is not what the Russians want. A grandiose new Partnership and Cooperation Agreement would be inappropriate. But, if and when Russia joins the WTO, a Free Trade Agreement would be a practical step forward.

We should also reject the concept of “neo-containment” favoured by some in the United States. It is based on the wrong analysis. Isolating Russia is entirely the wrong approach.

We should instead aim for “neo-engagement”, ie:

— Partnership and cooperation on specific strategic issues—where this is possible. There are many such issues.
— Support for the further development of trade and investment.
— To the greatest extent possible, we should sustain the flow of information, educational and cultural exchanges, and every form of human contact.
— We should seek to invest in the next generation.

In the energy sector, Russia and the EU have a clear mutual interest in sustaining cooperation. The EU is almost the only profitable market for Russian gas exports. However, given doubts about Russia’s ability to raise production and her use of energy as a political instrument, the EU clearly needs to diversify its sources of supply, to avoid deeper dependence on Russia, and to develop an efficient internal market.

Finally, during this difficult period, the EU and NATO need to manage areas of disagreement with Russia in a way which protects Europe’s legitimate interests but does not tip us into real confrontation. These issues include Kosovo, Georgia, Ukraine, Iran missile defence, and the future of the INF and CFE agreements. Handling that agenda will be no easy task.
Examination of Witnesses

Witnesses: Sir Roderic Lyne, formerly HMA Moscow; and Mr Charles Grant, Director, Centre for European Reform, London, examined.

Q135 Chairman: Sir Roderic and Mr Grant, we are very pleased to see you this morning. As you know, we are undertaking this inquiry on the European Union and Russia and we have read writing from both of you which is relevant and important for it. Before we start with our questions, Sir Roderic, you have an opening statement you would like to make?

Sir Roderic Lyne: Yes I have and I have also just today submitted some written evidence so I will not repeat everything that is in that. My argument is that the Russian Federation has changed enormously in the last 20 years and is still changing. I think there is a better than evens chance that 20 years from now Russia will have a modernising and more diversified economy, making better use of that country’s very rich human capital; that it will be developing more effective institutions of governance; and that it will be drawing closer to the European Union, partly impelled by the rise of China and instability in the Middle East. I also think there is a better than evens chance that 40 or 50 years from now Russia will have developed its own form of democracy, which will be, I am sure, different from the forms that we see in this country or other parts of Europe. None of this is to discount the significant possibility of less attractive scenarios. I believe that the European Union and NATO need to frame a long-term vision of the continent of Europe which is designed to include and not exclude Russia—I leave entirely aside the question of membership—and a vision which will attract Russia, (which is, after all, Europe’s most populous nation), towards a closer and more harmonious and more civilised relationship. That is the long term. In the short term, Europe faces a different task. For the past four years Russia and the West have been diverging. I do not agree with those who argue that we are now in a confrontation across the board with Russia, although a lot of political comment and indeed media comment would suggest otherwise, but there is unquestionably an atmosphere of mistrust, anger, and animosity, and this could turn into a confrontation under the pressure of events, a confrontation which I firmly believe neither Russia nor the West as a whole actually wants or intends. I think that we are now in a negative cycle in a long process of transition. I think this is a cycle which will very probably last for at least another five years and quite possibly 10 or 15, and so I believe that the European Union needs to calibrate its approach to the circumstances which currently exist in Russia. The previous objective of building—to quote from European Union documents—“a genuine strategic partnership founded on common interests and shared values” is clearly inoperable for the time being. It should not be binned because as a long-term aspiration it is commendable, but it should be shelved until circumstances change. I think that we should firmly reject ideas of neo-containment which are popular in some quarters, particularly on the other side of the Atlantic. We should firmly reject any approaches which are designed to isolate Russia. I think we need in the European Union to develop a shared analysis of what is going on there and a much better understanding of this within the EU. The process of debate and analysis within the Europe is weak and fragmented. Founded on that shared analysis, I think that the EU urgently needs stronger policy co-ordination and a common approach towards Russia which has been singularly lacking over the past five or so years. I have set out in my written evidence certain principles that I think should be the foundation of that common approach, and in terms of practical enactment, this should be a policy of what I call “neo-engagement” in which we seek partnership and co-operation on specific strategic issues, where this is possible, we support the further development of trade and investment, and to the greatest extent possible we should try to sustain the flow of information and educational and cultural exchanges and every form of human contact, and we should try to invest in the next generation. Given that I have submitted other points in written evidence, perhaps I should leave it at that, my Lord Chairman.

Q136 Chairman: Thank very much indeed, Sir Roderic. Mr Grant, do you have any comments on what Sir Roderic has said or do you broadly follow his approach?

Mr Grant: I do not disagree with anything he said. I guess that, broadly speaking, there are two theories, in the US at least, about what we should try and do about Russia. One of which is to try and engage, find a way of dealing with it and the other way is just to isolate it and surround it and contain it, and most people in Europe go for the former, as indeed Rod Lyne does, and I am very much with those who think we have to try and find a way of engaging Russia however difficult it may be.

Chairman: Thank you. Lord Lea?

Q137 Lord Lea of Crondall: I would like to ask Charles a point because we perhaps bowled a googly to his colleague Katinka, with whom he should have been appearing last week, in asking whether we have got a clear list of where the Russians and the EU have to lock hands together where the EU has competence. The word “negotiation” is used in our question, and
clearly sometimes you are negotiating in a multi-
lateral forum, the best example being the WTO, and yet there are many issues where the EU does have competence and we have to do bilateral and so on. Do you think it would be useful analytically to be clear what the list is of where we have to do things
together because the EU has competence and where,
secondly, the EU per se and the Russians have some
standing, like the Quartet in the Middle East, et
cetera? Are we clear where the competences are at the
moment before we speculate on some fantasy about
the future of the world and would you see a forward
creep of competences rather than some strategic, big
piece of architecture?

Mr Grant: I will go through in a moment some of the
areas where I think we should try and work with the
Russians, but in most of these areas you cannot
simply say the EU has competence or the Member
States have some competence, because in most things
that the EU does the EU has some competence and
Member State have some. Trade is an exception
where really the Member States do not have any
competence at all. In most of the things that we may
be talking about in the next few minutes, competence
is divided. Let me mention three areas on which I
think the EU should focus in its relationship with
Russia. My starting point for this is I think we have
to be realists in dealing with the Russians. As Rod
said, the old idea that Russia was a big Poland which
would gradually move to Western liberal democracy
as it became richer is now seen as rather silly in
European government circles. Apparently Bernard
Kouchner, the French Foreign Minister, said at a
recent meeting of foreign ministers: “face à la réalité
il faut être réaliste”—faced with the reality of the way
Russia is changing, we have to be very realistic—and
in my view that realism should lead to co-operation in
three areas. One of them of course is the energy field
where the Russians and Europeans do have a lot of
shared interests and we both have concerns. They are
cleared that the liberalisation of the European
energy market may make it difficult for them to strike
long-term supply contracts with European energy
companies. They are concerned that they may not be
able to buy downstream distribution networks if the
Commission’s plans for liberalisation go too far. We
are of course concerned that they might one day just
cut off supplies, but the real concern we have is not so
much that; it is rather they will not have enough gas
to give us. Most projections show that demand for
gas from Europe, from Russia itself, and maybe other
places, is going to outstrip supply in a few years’
time, so we have concerns. I think it is quite clear to me,
given that we have a mutual interest in having a fairly
productive and fruitful relationship on energy,
particularly gas, that we probably can strike bargains
and do deals and do compromises. The second area
is integrating Russia into the international financial
system, which is of course happening hugely. Russian
companies are raising money on the London Stock
Exchange. A lot of Russian companies, and now
sovereign funds, have spare funds which they wish to
invest in Europe and America, and they are concerned, they say, about protectionism in the EU
and us excluding them. We are concerned of course
about whether these sovereign funds and other
investors are transparent and operate independently
of politicians and so on. Each has its concerns but
again it is in the self-interest of Russia to allow its
multi-national companies to become truly multi-
national in the sense that we would mean, outside
Russia. It is in our interests to help integrate Russia
into the global financial system because that means
Russia is probably an easier country to deal with. The
third area and the most difficult area—it is a more
political area—is the common neighbourhood that
we share with Russia, but I think we have very clear
mutual interests and that Russia and ourselves
should welcome the fact that if Moldova, the
Ukraine, Belarus and the Caucasus republics become
prosperous, stable and democratic that is actually
good for both of us. Not everybody in Russia will see
it that way because the Russians tend to see this as the
geo-political “Great Game” and they tend to assume
that any democratic force in our common
neighbourhood is automatically going to be a pro
-Western force that will do its best to undermine
Russian interests. There is a risk that this may
become a self-fulfilling prophecy. To conclude my
answer, in all these areas, David—oil and gas,
financial integration and what we do about our
common neighbourhood—competence is divided
between the Member States and the EU, so it would
be wrong to see it simply as an EU competence or a
Member State competence.

Q138 Lord Hannay of Chiswick: Would it not be the
case, in your view, that there is in fact a division
which is slightly different from the division between
Community competence and Member State
competence which is more important, and that is the
division between matters that are dealt with between
businesses and individuals and matters that are dealt
with governmentally? Amongst the latter of course
there is the subdivision between Community
competence and Member State competence, but
would you not feel that that is an important
distinction, because in the areas which are covered by
the private sector such as trade and investment (and
you said trade was a Community matter and of
course it is trade policy that is a Community matter
not trade; trade is conducted by European companies
and that in the area which is in the private sector, as
it were) and cultural links and educational links and
so on, it is in Europe’s interest to have the least
possible regulation, the least possible governmental
involved because that just cuts across what our long-term objectives are, and that then puts a little bit better into proportion the discussion about which bits of the governmental activity are handled by Europe as whole, the Union, and which bits by the Member States?

Mr Grant: Yes I agree that when it comes to cultural and educational links, you do not really need very much at government level or EU government level for these links to happen. I guess in one of the areas that I mentioned, in energy, it is very much both: a lot of the energy links are what the oil and gas companies do in Russia and in the EU, but also they are operating within a framework of rules set by the EU which obviously influences and limits what the companies can do. Equally, on the question of financial links, if the EU or some EU governments do decide to limit investments by sovereign funds then obviously that is a constraint on what the private sector operators can do.

Q139 Chairman: Before I call Lord Anderson, Sir Roderic, is there anything you would like to add to what Mr Grant has just been saying?

Sir Roderic Lyne: I think the common neighbourhood point is very important but this is not confined to the European Union. I think it is extremely important that we also think of NATO in this context. One of the most active questions within the broad East/West dispute over this neighbourhood is whether or not countries like Georgia and the Ukraine are going to enter NATO. I do not think you can divorce that from the question of the EU’s relationship with the Russian Federation and the other post-Soviet States. The Russians certainly look at these two things as part and parcel of the same problem from their point of view, which is one of Western encroachment into what they have traditionally regarded as part of their zone of influence, and indeed in the case of Ukraine as part of the Russian heartland. Only the other day Putin was reminding the Russian public that 17 million people whom he classified as Russians lived in Ukraine. That is about one-third of the population. I think that figure is broadly accurate. This is extremely delicate territory and I can see no way in which we are going to reach an accommodation easily with the Russians over this because, as history shows, when empires break up—whether you say Turkey and Armenia or you say the United Kingdom and the Republic of Ireland or France and Algeria or 50 other examples—it takes a very, very long time for emotions to subside. We have got to frame policies here that respect the rights of those countries, that defend our legitimate interests in them and their rights very robustly, but which at the same time do not lend themselves to misrepresentation in Russia in a way that will make the situation in Europe more dangerous or that will allow new dividing lines to spring up.

Q140 Lord Anderson of Swansea: I thought I heard Mr Grant say that there was very limited governmental involvement in cultural exchanges. Certainly at one level there is—when the Kirov comes here that will be so—but there will be a very important governmental involvement and EU involvement not just, as Sir Roderic knows all too well, with the British Council and the governmental cultural agreements but also in terms of the encouragement or otherwise of Russian studies in our university. For example, I am old enough to recall the Hayter money which was in the 1960s I think to encourage Russian studies. That seems to have run into the sands. To what extent do you think there should be greater encouragement of Russian studies and the Russian language generally in European universities as an important priority of the European Union, with all the other pressing matters, and perhaps Sir Roderic could say a little more about the relevance of the British Council cultural exchange and the Russian view of those cultural exchanges with the West?

Sir Roderic Lyne: On the first point I can offer some small encouragement which is that a union of three universities based around the School of Slavonic and East European Studies, which has the rather complicated acronym of CEELBAS, the Centre for East European Language-Based Area Studies, has recently been awarded a large grant from government funds to promote particularly postgraduate studies not only in Russian but in East European language-based areas, and I am the chairman of the advisory committee of this particular initiative. I think that there is at the moment, because of the expansion of trade, a very high demand for Russian speakers, and the prospects for graduates looking for jobs will be more attractive. The problem after Hayter was that we were training Russian graduates who then could not get work in their field. Now it is rather different so one hopes that this pull factor will encourage more people to develop language skills.

Q141 Lord Anderson of Swansea: That is a UK initiative rather than an EU initiative?

Sir Roderic Lyne: CEELBAS is a UK initiative.

Q142 Lord Anderson of Swansea: Are there similar initiatives at an EU level?

Sir Roderic Lyne: I am afraid I have got no idea at all.

Q143 Lord Anderson of Swansea: Should there be?

Sir Roderic Lyne: I think a lot of the EU’s effort in Russia should be put into areas relating to education, and I have always argued that in discussions with the
EU, because I really do think that investing in the next generation in Russia is probably the most helpful thing we can do. On the British Council, I had a letter from the British Council last week telling me, rather sadly, that they were going to, not formally close nine of their regional centres in Russia but transfer them to local partners, so I think the British Council label is going to go off them. I was glad to be told by the Council that they are going to remain in Moscow, St Petersburg and Ekaterinburg. They have been under attack for the past four years. It has been a backhanded compliment to the effectiveness of their work that rather old-fashioned Soviet-style forces have been attacking their work. I think it is has been enormously important and that they have sown seeds that will eventually germinate in Russia. There have been some provinces in Russia in which every single English teacher has belonged to the local British Council resource centre. In the Krasnoyarsk region the British Council helped to promote a very important reform of the local educational system, which one hopes will then get rolled out in other areas. I think it has been an example of what we should be trying to do in Russia. The Council was attacked because it had a British Government label on it and because people were looking to retaliate against the British Government, and they have had a tough time as a result. However, that does not invalidate what they were doing at all.\(^1\)

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\(^1\) Since this Evidence was heard, the Russian authorities have demanded the closure of the British Council centres in St Petersburg and Ekaterinburg, apparently as a further act of political retaliation. Their reasons for doing so have been rejected by the British Government.
Mr Grant: I would perhaps say following on from that I do think there are some very small signs of encouragement that the EU is beginning to learn to think as one on Russia rather than as 27 separate Member States. I say “very small” signs, but I think we have seen it this year, largely in response to Russia’s behaviour—and I agree with Rod Lyne that if we can hold a united position on Russia then we clearly have more influence over it because the Russians respect power—at the Samara Summit between the EU and Russia in May when Merkel publicly criticised Putin for not allowing demonstrators to travel there. He was really riled about this and I saw this when I myself was part of a group that met Putin at Sochi in September where he referred back to Merkel’s criticism of him, and then produced a counter-criticism about how the Germans often arrest demonstrators and the German police treat demonstrators so badly, so he is clearly very upset by that. Secondly, of course we had a statement on Litvinenko giving some solidarity with the British after the expulsions, and it was not certain that we would get that statement because some other Member States did believe that we overreacted and that it was the wrong thing to do. I know a lot of German diplomats felt that, but everybody signed up to that statement. I was not there but those who did attend the informal meeting of the EU Foreign Ministers in September did report back that there was a mood that even if some of those present did not welcome the prospect of an independent Kosovo, it would be quite wrong to allow the Russians to decide the issue of Kosovo’s future, and if the Russians did bully us in this way then we should not allow them to and we should stand together on Kosovo. Some of the governments which do not really want an independent Kosovo are now taking the view that if is what most EU countries want they should go along with it. I think there is a small feeling of solidarity, encouraged to some degree by the change of leadership. Berlusconi, Chirac and Schroeder have gone and they did take the view that you should never criticise Mr Putin on anything. Their three successors are different. Prodi is not particularly critical of Putin but he has not, like Berlusconi, said that Putin is the world’s greatest democrat. Clearly Sarkozy is very different to his predecessor. He accused Putin in his August speech to the Assembly of French Diplomats of behaving with a certain brutality in his use of energy policy. This is a different world and I think the new Government in Poland—of course it is very early days yet—will help because this mood of greater unity toward Russia has been rather undermined by the Poles, in my view, taking a rather extreme, sometimes antagonistic, view on Russia, although of course they have plenty to be upset about because the Russians have behaved very badly to Poland. However, I think the new Government in Poland holds out a promise of a more middle-of-the-road view on Russia, so I think there is a real prospect of Europeans learning that they can achieve more in dealing with Russia if they have a common line.

Q146 Lord Hannay of Chiswick: Following that point, would either of you feel that it is correct to characterise Russian policy as fundamentally that of “divide and rule” politics towards the European Union, that they show no interest whatsoever in doing business with the Union unless the Union shows a degree of unity that forces them to do business with it, and that over this period, which Rod Lyne described as fairly lengthy, at least the next five years, what you have said about the desirability and effectiveness of unity is going to be true in spades because there will be continuing Russian efforts to divide and rule?

Mr Grant: Yes I do. I think their policy is very much divide and rule. They say, and I have heard Putin say they would like a strong, united Europe but I do not believe it for a minute. There is one kind of united Europe they would like which is a Europe united on an anti-American position, but rather like the Chinese they have understood that if Europe does take a common view it is not going to be the Chirac/Schroeder Europe as a counterweight to the US model at all. I think they have a particular problem in dealing with the EU in two respects. Firstly, Russians do not respect small countries at all. It is part of their view of the world, because they are very big, I suppose to be fair to them, and when they see a small country blocking an EU policy they say, “This is not serious. Why should we take your club seriously when you allow these little countries with tiny populations and tiny economies to decide things?” They just do not get that in the EU small countries are important. Secondly, on EU institutions, they really do not like the European Commission at all. I suppose many people in this country would agree with them that it is a complicated, arrogant, bureaucratic, difficult organisation to deal with but, nevertheless, the fact the EU has delegated certain powers to the Commission, particularly in areas that matter to the Russians such as energy policy, trade policy, the rules applying to their companies in Europe, is something they find very hard to cope with. Supra-nationality or the post-modern world, to coin Robert Cooper’s phrase, is not a world they are comfortable in. Russia is a very, very modernist state and it has an old-fashioned 19th Century view of great power politics, and the EU does not fit in with their view of the world very easily, in my view.

Sir Roderic Lyne: I fully agree with what Charles has said. It is a very old tactic of divide and rule and they do prefer to handle relations bilaterally with big
countries in Europe. Very few Russians understand how the European Union works. They absolutely fail to understand the notion of the acquis communautaire. In the early 1990s there were some extremely unrealistic ideas that Russia could very rapidly become a member of the European Union, which showed how little it is understood. Now there is a lot of disillusionment around; there is a sense that they have been rejected. Neither proposition is true. It is going to take some years, I think, for a more sophisticated understanding to arise. I think it is particularly important that, when we are dealing with Russia, we do not fall into the trap—as we saw in recent years before the advent of Chancellor Merkel who has a very good understanding of Russian and I think has handled policy superbly—of allowing ourselves to be picked off one against the other. I remember a clear example of this five or six years ago, which was when the Chechen representative Zakayev went to Denmark for a conference and the Russians punished the Danes in every way they could. They more or less isolated them within Russia. There was absolutely no solidarity from the European Union behind the Danes when this happened, which was deplorable. As far as this country is concerned, yes, we are having a tough time with Russia at the moment but we are only part of a wider picture in which the Russian relationship with Western Europe and the United States has gone to a very low point. I think it is completely in our interests when we have to deal with something like the Litvinenko affair to do it on the widest possible basis and to actually have support, as again we had from Chancellor Merkel, from our European partners.

Q147 Lord Crickhowell: We have really moved on a question, and almost dealt with the one that I was going to come back to, which is this whole questions of relationships. We have heard in previous evidence that really the Russian attitude has changed from a view of almost total disinterest in dealing with Europe; and puzzlement and bewilderment about how it operated, which you say is still there; to them finding that on some issues like on World Trade negotiations and so on that it was a force that it really had to recognise; yet wanting to exploit the differences and wanting to deal with the big states. Then Europe, in pulling together and trying to get some unity, has the difficulty that the new small states have sometimes taken very different views and attitudes, and it has found it difficult to find common ground for that reason. In earlier evidence we have heard that on the whole that great gulf between the new members, the small states and big Europe, has begun to improve and there is more common ground being found. Do you see Europe beginning to find a way of dealing with its new structure and find common ground? Although I understand Russia likes to deal with the big powers, insofar as Europe does find common ground on big issues like trade, they are surely going to want to deal with Europe forming itself in that situation as a big power in a sense?

Mr Grant: Yes, there are Russian technocrats in the system, the trade negotiators, who do appreciate the merit of the EU and understand it, but there is a huge lack of knowledge of the EU in general in Russia, particularly in the think-tank community, as Rod said. My worry about European unity towards Russia, despite what I said a moment ago about small signs of a greater solidarity emerging, is in the energy field because the different European governments still have very different perceptions of their own self-interest and their own national interest in how to deal with Russia. The counter-argument to what we said is that so long as we have very different views on energy, we will have different policies on Russia, which will affect areas other than energy, and the Russians will continue to divide and rule. We see this where Gazprom has long-term supply contracts with quasi monopoly energy companies in Germany, France, Italy, Spain and others, and the governments of Germany, France, Italy and Spain are rather reluctant to support the Commission’s plans to completely liberalise the European energy market and go for so-called unbundling, separation of supply from distribution. My own view is that the Commission is probably going to get half the cake and it will make some progress here, but the European governments are very divided on this. One reason they are divided is that some are more dependent than others on supplies from Russia. Those, like Germany, which are dependent on supplies from Russia are reluctant to do things that could annoy the Russians in the energy sphere. That is part of it, so there is a great lack of unity and solidarity in the energy sphere, and I think until we work out a more common line there the Russians will continue to divide and rule.

Q148 Chairman: Sir Roderic, is there anything on that point that you would like to add?

Sir Roderic Lyne: It is extraordinary that we have a Single Europe Market but we do not have a Single European Energy Market. If Europe is going to become serious in its dealings with Russia it has to find a way of adopting a common policy that respects the fact that our markets are mostly run by private sector companies. It is not some grand deal and it ensures that Gazprom (or any other Russian company but we are talking really about Gazprom here) trades with Europe on a level playing field and not as a political entity. I think Europe is grinding towards a realisation of that. Russian behaviour has forced the Europeans to face up to the fact that they cannot afford to be too dependent on Russia, both...
because, as Charles said earlier, the Russians are failing to increase their production, and also because they have shown from time to time that they are ready to use energy as an instrument, so I would put this at the very, very top of the list of subjects on which Europe now needs a more effective and co-ordinated policy. I think that is viable but difficult; it needs a lot more work. There are some great experts in this field, and I am not one of them, but I hope that you will hear from some of them, people like Dieter Helm, who wrote a superb article on this subject in September.

Q149 Chairman: There is a very good article in the Financial Times this morning by Daniel Yergin and Simon Blakey of Cambridge. Sir Roderic Lyne: Yes, a little unrealistic. They are great experts but I think they are over-optimistic in thinking that you can actually persuade the Russians to adopt a more liberalised internal model in the near future, so I think they are founding their suggestions on slightly sandy ground, unfortunately. I would love to believe it but I do not think it is true.

Q150 Lord Anderson of Swansea: What I think our witnesses are pointing out is a possible divergence in terms of EU solidarity between the political superstructure and the economic substructure. There may or may not be improvements in solidarity, for example, on matters like Kosovo, but that is still a question mark because of the interests of countries like Spain and the Basques and so on. It is important that there has been a change of senior leaders, but how can one get out of the long-term contracts in terms of gas and oil supply which have been agreed, which are for about 30 years in some cases? The economic side is going to prove extremely difficult and even very strongly pro-European leaders like Prodi seem to be very happy to see their oil and gas companies reach these long-term contracts. If there are such long-term contracts are you suggesting that they be renegotiated or has the pass already been sold in terms of economic solidarity in this key energy sector? Mr Grant: Others are more expert than me on this particular area, but my understanding is that there has been a change of senior leaders, but how can one get out of the long-term contracts in terms of gas and oil supply which have been agreed, which are for about 30 years in some cases? The economic side is going to prove extremely difficult and even very strongly pro-European leaders like Prodi seem to be very happy to see their oil and gas companies reach these long-term contracts. If there are such long-term contracts are you suggesting that they be renegotiated or has the pass already been sold in terms of economic solidarity in this key energy sector?

Q151 Lord Lea of Crondall: Can I ask our visitors have they got our list of questions? Okay, could I ask question two then please. Sir Roderic Lyne: This is how is the EU perceived from a Russian perspective and what are the underlying principles of Russian foreign policy towards the EU? Chairman: I think it would be better if you did ask the question, Lord Lea.

Q152 Lord Lea of Crondall: Because we are all over the place, it is not quite clear whether our visitors really understand our agenda of questions; that is why I am asking. Question two reads as follows: is the current institutional framework for EU-Russia relations, based on the Partnership and Co-operation Agreement (PCA), the four common spaces and the “Northern Dimension” working well? What approach should the EU adopt towards the negotiation of a new agreement? Sir Roderic Lyne: I think the EU should not attempt to negotiate a grand, overarching new agreement on the lines of the PCA because the PCA was posited on the idea that Russia was moving towards a situation in which we could say that we had common interests and shared values; and that simply is not the case at the moment. I think that the four common spaces agreement, the roadmap for the common spaces, contains a lot of good stuff, but I am not sure how much of it is being implemented. For example, the treatment of the British Council, which we were discussing earlier, runs directly contrary to some of the provisions in the relevant common space. I do not think we are going to move forward with the Russians through these very large agreements. I think a much more productive approach at this present stage is for us to negotiate on individual, separate issues with the Russians, some of which will lead to agreements perhaps in the area of energy as we were discussing, and some of which may lead to an agreement with them if we have a shared interest...
somewhere and should so proceed. It is right and useful that the European Union should have formal procedures for meeting the Russians at summit and other levels. I think that this dialogue is important and necessary. However, I do not think that we should have agreements which simply are unrealistic and do not reflect the actual state of affairs.

**Lord Lea of Crondall**: In that case, is all of this a bit of a waste of time? It is obvious that the Russians like to talk to big fish, and Merkel happens to be the President of the Council of Ministers at the time or whatever, that is fine—but I would just like to check in the light of your answer—I do not know whether Mr Grant agrees with your line of answer—what special relationship is there? I am just not clear where we are going

**Q153 Chairman**: Mr Grant, perhaps you could answer the question and particularly comment on Sir Roderick’s comments that he feels in the present circumstances an attempt to negotiate a new PCA is probably a mistake.

**Mr Grant**: I am fairly agnostic on this. I guess I probably think like the EU officials on this, which is that if we could use the PCA to try and get Russia to sign up to the principles of the European Energy Charter, which would basically force the Russians to open up their energy markets a bit and allow foreign companies to do more in Russia in the energy sector, then that would be a good thing about the PCA, but the Russians have indicated that they are not prepared to do that. Maybe Roderic is right that there is not much point in going through all the fandango of these complicated negotiations if we do not think we are going to get much out of it. On the other hand, I am not sure I totally support the Polish Government’s attitude to this in the way they vetoed the start of the talks. My understanding is that they probably bear some of the blame. Meetings were arranged to try and sort out the problem of Polish meat exports and the Poles simply did not turn up to the meetings, so there was an effort in the summer to resolve this, I think the Russians made some effort to resolve it. Because the Poles have vetoed the start of the talks, it allows the Russians to make fun of the EU and say, “Isn’t the EU ridiculous. It can’t even agree to start talks with us.” There might be an argument that having a process of negotiation with the Russians in itself is of some use just to keep the two sides engaged but I do not have strong views and I would not want to differ much from what Rod Lyne said on that.

**Sir Roderic Lyne**: Could I add two points. There is one quite good example of EU negotiation with Russia leading to specific results and that was when Russia was persuaded eventually to accede to the Kyoto agreement. I think looking ahead what is very important is the timing of Russian accession to the World Trade Organisation. Every year we are told that it is going to be next year that it happens. It is not now going to happen this year and so it is not quite clear when that is going to happen. If and when it happens it will open the way for the European Union to negotiate a free trade agreement with Russia, which I think would be enormously to the advantage of both sides, certainly to the European Union. I would much rather focus on that than a wider agreement full of flowery phrases that are simply not credible to our own public opinion or indeed to people in Russia.

**Q154 Lord Lea of Crondall**: Would you therefore agree that in this area of institutional framework, what we are groping for is not so much an institutional framework for the sake of having an institutional framework; it is trying to be a bit clearer about how the big issue, landscape, the canvas on which the picture is painted is organised? You have just mentioned Kyoto and I think that is hugely important. The Russians and Putin played their cards, would you agree, or their chess game very, very skilfully. The development of the EU Emissions Trading Scheme could be of great interest. This is one issue separate, and then another issue separate and another issue separate. Could you talk about how the key issues should relate to any framework or special relationship, or does that not matter and should we just deal with blocks of important issues?

**Sir Roderic Lyne**: I think it does matter partly because the Russians like to have a framework. This is a procedure that they understand and if you have a set of meetings between the Russian Government and the European Union that cover different areas of our relationship, it allows a framework through which you can then deal with specific problems. If I could mention another example—there was a successful negotiation over the question of transit to Kaliningrad after the entry of Lithuania into the European Union. At the beginning of that process there was a lot of heat and light. Some very serious detailed work was done in negotiation using that framework and a successful conclusion was agreed, so it can work and I think it is necessary.

**Chairman**: Lord Swinfen, we have already taken some of the energy points but I wonder if you would like to continue.

**Q155 Lord Swinfen**: To what extent do you think Russia is prepared to use its energy exports as a political weapon or do you think it is primarily interested in the economic aspects of energy export?

**Sir Roderic Lyne**: It needs the economic benefits. 60% cent of Russia’s export revenues come from the export of oil and gas, around 80% from the export of raw materials overall. It is desperately dependent on this. A lot of the Russian budget is funded from the
experts talk about the weakness of their position in a sense. There is growing supply shortage, inadequate infrastructure, Gazprom is one of the world’s most inefficient organisations and has diversified itself in 100 different ways into non-energy fields. The gas is being sold in large quantities at uneconomic prices and is very inefficiently used in Russia. If they are going to try and use it as an instrument in these situations, does it not at least give Europe particularly a very strong position indeed in standing up to its use as an adverse instrument against Europe? Europe’s negotiating position, I think it has been indicated in some earlier remarks, is going to be quite strong if we use it sensibly. It is an economic instrument which has great weaknesses, has it not?

Mr Grant: Obviously there is mutual dependency. As Rod said, the pipelines all go west at the moment, so that does give us leverage, which is why I actually think that we will probably negotiate and find compromises on some of these questions. I think the Russians have one precise objective which is to control the energy infrastructure in the former Soviet Union, and sometimes they say this explicitly. Of course if you look at what they are doing in their disputes with Belarus and the Ukraine on energy, they want control of the pipeline networks in those countries. I think it is the same in Moldova. They want to recreate this single system for energy supplies. I think they would be quite happy if it went beyond the former Soviet Union into parts of Europe too. They have of course bought supply depots and they have got stakes in various distribution networks in Europe. They do not have a majority stake yet in any single major distribution network that I am aware of but they have certainly bought bits and pieces of energy infrastructure in Central Europe and a little bit in Western Europe. I think this is a monopolistic objective. I have heard Putin say that, “You in the West have your cards, you have your high technology, you have your aerospace industry; we do not have that, we have only have one card we can play, which is our energy system, and do not think we are going to let you into it.” He did not use the phrase “crown jewels” but he was saying “This is Russia’s crown jewels and we would be crazy to let you in.” From a Russian nationalist point of view I think he is right.

Sir Roderic Lyne: The weakness of their position, as you rightly say, is in their poor production and mismanagement of the resource, but the strength of their position is in their ownership of enormous reserves. There are only three areas of the world—West Africa, the Middle East and Russia—which have got that sort of potential and every energy company in the world would like to have access to those reserves, including the ones in the Arctic.

Q156 Lord Crickhowell: We have already talked about the weakness of their position in a sense. There is growing supply shortage, inadequate infrastructure, Gazprom is one of the world’s most inefficient organisations and has diversified itself in 100 different ways into non-energy fields. The gas is being sold in large quantities at uneconomic prices and is very inefficiently used in Russia. If they are going to try and use it as an instrument in these situations, does it not at least give Europe particularly a very strong position indeed in standing up to its use as an adverse instrument against Europe? Europe’s negotiating position, I think it has been indicated in some earlier remarks, is going to be quite strong if we use it sensibly. It is an economic instrument which has great weaknesses, has it not?

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Q157 Lord Hannay of Chiswick: I take those points but would you not agree that it must be in our long-term interest to wean the Russians away from this totally mercantilist approach to energy policy? It may not be easy to do so but it would be a pity to give up on it. I detect in both your replies a fatalism about the Russian attitude to their energy situation. It is not actually the case that if we were sitting in the Kremlin we would do the same. The British Government did have to take decisions in the 1970s about whether or not to interfere with the direction of North Sea oil exports and it decided deliberately that it would not interfere because it was not in our national or economic interests to do so. So I do not think we would come to the same conclusion. I do not think we want the Russians to continue to come to the same conclusion. I would like you to say whether you think we should just simply throw in the towel, as it were, on things like the Energy Charter and that sort of thing or whether we should politely but persistently continue to say we think it is in your interests as well as ours that we should have a more private sector-oriented, liberalised energy sector.

Mr Grant: In the long term I am more optimistic. For the reasons that have been mentioned, they will have a real problem exploiting new resources. They do not have the technology or the expertise and we have the technology and the expertise, so if they are serious about exploiting things offshore particularly—they have no offshore expertise—in some of the very cold areas I am told by energy experts they will need Shell and BP and the American companies too. Again Rod knows much more about it than I do, but I know that they certainly have not wanted to kick Shell out of Sakhalin because Sakhalin is about offshore rigs and they cannot do offshore rigs; they need Shell. Therefore I am optimistic that they will see that it is in their interests to allow Western companies to operate in Russia and I think the quid pro quo will be some liberalisation of the market, but I do not think it is going to happen yet because they are rather short term in their view.
Sir Roderic Lyne: Gazprom has never operated offshore and Gazprom has never built LNG so they need that consortium to build the LNG plant. I do not think we would have invented Gazprom but I think we, like them, would have surveyed what assets we had and would have said energy is the only one that seems to give us leverage in the international political arena. I am not pessimistic for the long term, rather like Charles, but I do not think the Russians will change their policies because we tell them to do so. I think that life itself, as they would say, will cause them to change their policies. Five years ago, before the flood of oil money hit Russia, there were very serious plans being made for the reform and restructuring of Gazprom to break it up and turn it into a commercially effective company. They were shelved in early 2003 for political reasons. Extremely intelligent people within the Russian system realise full well that this is a very, very intelligent model. I think when life becomes more difficult again in the future, as it will do at some stage, they will return to this issue, just as they have recently broken up the electricity generating company because the electricity generating industry in Russia needs massive investment and they simply were not going to get this in a single unified company, so it is being sold off in blocks, part of it on the London Stock Exchange. It will change when the need arises. At the moment the need for restructuring and reform is covered over in thick layers of dollar bills and those layers will thin out. I think, in the next five years.

Q158 Lord Anderson of Swansea: I do not think anyone disputes that Western companies will continue to operate in Russia. The question is the nature of that operation and the nature of control. Is it likely that they will see the involvement of Western companies as contractors, as technical advisers, but the control so far as we can plan will still be under the Russian monopolies?

Sir Roderic Lyne: They would be far from the first country to do that. I think that Western independent oil companies are prepared to accept working with different models and they accept that sovereign governments have the right, whether it is Saudi Arabia or Russia, Nigeria, or indeed the North Sea, to decide on their own regimes. It is not only that they need the technical input of Western countries, they also need the investment. Developing the Yamal Peninsula, which is the next big gas province in Russia, is going to cost in the order of $100 billion, possibly more, which is beyond the resources even of Gazprom. If you start talking about the Arctic and the Stokmann field you are talking about even more astronomical sums. Certainly they will want Western companies—and not just suppliers and contractors—to play a role as partners but they do not want them owning the resource in very large quantities and they do not want them in the driving seat as far as decisions are made. The most successful partnership up to now has been the TNK-BP partnership. That was deliberately constructed—and I declare here that I am adviser to BP but I do not speak for the company or take decisions in the company—on a 50/50 basis. If BP had gone for 51/49 in BP’s favour it would not have happened or, if it had happened, it would have been reversed, so I think there are a number of workable models. I am struck by the fact that the Russian Government has recently reinvited foreign companies into the Stokmann project, starting with Total and I think others Chevron, Statoil, Norsk Hydro are quite likely to come into that because I do not think it can be achieved without them.

Q159 Lord Hannay of Chiswick: Switching from energy and all these other areas, although they have foreign aspects to them, to looking at Russian foreign policy, is there any discernable pattern to this policy beyond a heavy-ish dose of post-imperial nostalgia? How do they rank the importance of their big partners—United States, Europe, India and China—and how seriously can we take their claim that they are in favour of multi-lateralism when they seem to use their position in most multi-lateral institutions simply to block Western or American policies even when there is not a very obvious Russian national interest at stake Kosovo being a case in point where it really is quite difficult to see what the Russian national interest in that is, except for mucking everyone else about and showing them that they are still there? Could you characterise a little bit Russian foreign policy and its likely development?

Sir Roderic Lyne: I think Russia is in favour of multilateralism in the same way that the United States is. That is to say where it is to Russia’s advantage to use it, it will do so, and otherwise it will not. Russia’s case being much weaker than the United States, the advantage lies more often in using multilateralism and using Russia’s position on the UN Security Council. I was struck when I served in Geneva by how weak Russia was in Geneva because the Security Council did not matter there. What did matter was your economic weight and at time I was there in the late 1970s Russia was not a significant donor to the UN and other bodies in Geneva and actually was more or less ignored by everybody. I think the most important focus of Russian foreign policy is on what they call the “near abroad” or what we might call the “common neighbours”. That is where the greatest effort goes, that is where the greatest concern is. That is also where there are divisions within Russia about whether or not they are pursuing the right policy within the Russian elite. The objective is fairly clear, it is to every extent possible exercise influence over the former Republics of the
Soviet Union and the areas on Russia's borders. With regard to the United States, Russia has relatively little trade with the United States and does not have a very wide agenda with the United States. It is predominantly focused on arms control and nuclear issues, but of course there is a great desire on the part of the Russians still to be seen to be taken seriously by the United States. I felt that President Bush was right to extend an invitation to President Putin, rather controversially, to go to Kennebunkport this year to discuss the issue of theatre missile defence, and although at the moment, judging from the visit of Condoleezza Rice and Bob Gates to Moscow the week before last, those discussions are not going particularly well, I am told that behind the scenes they have not actually hit the buffers either and that there is something of a serious negotiation going on between the United States and Russia about INF, missile defence and CFE. I hope that is true and I think that is correct. I think that is the main Russian agenda towards the United States. I think China is a very interesting case because the official line in both Peking and Moscow is that the relationship between Russia and China has never been better, not in 300 years. The leaders meet up to five times a year; the contentious issues on the border have been resolved; trade is in the order of $40 billion a year and rising; China is the biggest market for Russia's arms exports; they have the Shanghai Co-operation Organisation; they have had one or two joint military exercises, and everything is hunky-dory. If you actually ask a Russian strategic thinker—there are a few such—what their biggest concerns are as they look ahead at Russia's future, you get the one-word answer “China”, and I have even had that from a very senior general in Russia. The Russians are enormously concerned about how over the next 20 or 30 years they can accommodate the rise of China not only as an economic power but as a military power, a military power that they themselves are helping to develop. I think the Chinese view of Russia is one that is less than flattering. I do not think they are terribly impressed by the effectiveness of the Russians and I think you have got a fair degree of tension under the surface in that relationship that will limit the scope to which Russia and China (which make common cause on quite a lot of international questions at the moment, particularly at the Security Council) will really work closely together in the world of the future. I am not one of those who takes an alarmist view of these two large emerging authoritarian countries teaming up together against the rest of us because I really do feel very strongly that Russia has a huge concern about China. It has drafted legislation designed principally to prevent the Chinese from buying too much into the up-stream resources in Siberia, just to take one example. You have a 3,400 kilometre stretch of the Amur River, which is the common border, without a single bridge across it. There are many other factors that one could throw into the mix. Is there a coherence to Russian foreign policy? No, I think it is essentially short term and opportunistic. Russia is a country that is led by people who were born and brought up and formed in the Soviet Union, and that will be the case for another 10 or 15 years, people who instinctively think in Great Power terms and wish Russia to be a great power, and wish Russia to be taken seriously. Now that Russia has got its economy and its internal affairs onto a slightly firmer footing than it was 10 years ago, the Russians want to assert their right to an independent foreign policy and to show that they can be a factor, not all the way round the globe—essentially they are more or less nothing in Africa and hardly active in Latin America—but in the Middle East for example to show that they do have a point of view that is as legitimate as anybody else's. I do not think it is specifically anti-Western; I think it is more trying to say, "We are here, we have interests, and you need to take account of us too".
ask for a foot and you should just take no notice of what they do, recognise an independent Kosovo, contain Russia, exclude them, penalise them. However, there is another view, associated with Henry Kissinger, which is that we need some grand strategic bargain. Maybe there is a method behind their madness. Maybe by being so difficult in so many areas they are actually reaching out to us and they want to do a big deal. To judge from press reports in the Herald Tribune yesterday and on Saturday that seems to be the line of the State Department in Washington. There does seem to be a view in Washington now that it is worth trying a bargain on CFE because there is a possible compromise on CFE. On missile defence, whereby the current American line seems to be that we should promise the Russians not to activate any system unless we both agree on line seems to be that we should promise the Russians not to activate any system unless we both agree on

Q161 Lord Anderson of Swansea: Kosovo?

Mr Grant: And in return they have to be reasonable on Kosovo. Some of those directly involved in the Kosovo diplomacy tell me that the Russians are being quite reasonable, or at least the Russian member of the so-called Troika is apparently being very reasonable. Whether his bosses will allow him to go on being reasonable I do not know, but there is at least a possibility now of some kind of bargain. Perhaps I will say one more word on missile defence. The Russian opposition to missile defence—and again Rod would know a bit more about this than me—seems to me to be genuine rather than feigned. It is not just a tactic; I think they are genuinely upset by it. I have heard American diplomats say that in the 1990s we promised the Russians that we would never put any “something” into the new members of NATO until East European countries joined NATO. Some people say advance military systems, some people say military bases, some people say significant areas they are actually reaching out to us and they want to do a big deal. To judge from press reports in the Herald Tribune yesterday and on Saturday that seems to be the line of the State Department in Washington. There does seem to be a view in Washington now that it is worth trying a bargain on CFE because there is a possible compromise on CFE. On missile defence, whereby the current American line seems to be that we should promise the Russians not to activate any system unless we both agree on

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Q162 Lord Crickhowell: I was interested in Rod Lyne’s introduction to this because he talked about American defence systems and China as well and almost as a throwaway remark at the end he mentioned the Middle East. Members of this Committee took part earlier this week in a debate on Afghanistan, the Middle East, on our Report on Europe, the Peace Process, and so on. The central area of foreign policy anxiety for most of us in Europe and the West is in fact what is going on in that broad area from Afghanistan across to the Mediterranean. Could you say a tiny bit more about the Russian views about it and how they are likely to evolve because this is the area, surely, as much as anywhere, where Europe is likely to come up against relationships on important foreign policy issues with Russia.

Sir Roderic Lyne: In the Cold War we automatically found ourselves on the opposite side to the Russians in every regional conflict around the world, including the Middle East. That is absolutely not the case now. I think the Russians are playing some tactical games around the whole area of the Middle East and Central Asia but I think that the broad strategic objectives of Russia are broadly the same there as our own. I would even go further; the Russians have been very much part of the same diplomacy as ourselves over North Korea. They were extremely supportive in Afghanistan in the early stages of the operation and they are not obstructing it now. They did create difficulties in Uzbekistan but that was because they believed that the Americans had said they would establish a base and leave rather quickly, but they are not actually wishing us to fail in Afghanistan, which would be very bad for their own interests. They think we may well not succeed there. They have not sought to make life difficult for ourselves in Iraq, although the Russian Government felt, as a lot of people in Europe felt, that it was a mistaken decision. They will speak about it very much in the same terms as the European debate. They take part in the Quartet on the Middle East. They do not actually have a lot of leverage there. They are happy to be included in the game. I do not think they are trying to make that significantly more difficult. They wish to retain strong relationships where they have them because they think that does give them some leverage. That obviously means with countries like Syria, to which they sell armaments. Then you come to the country which is at the moment more or less at the top of the American list and that is Iran. For the past five, six or seven years we have been discussing with the Russian Government the problem of the likely development by the Iranians of nuclear capabilities. I think that President Putin has seen this as an area where he has diplomatic leverage because Russia has a relationship with Iran, America does not and the European Union does not have much of one. Russia does not want a nuclear-armed Iran. It would be much closer to Russia than it would to us, let alone to the United States of America. I think the Russians are more pessimistic than many people in the West about the chances of preventing that from
happening. Quite a lot of Russians will argue that we are going to have to find ways of living with it, but I think what they are trying to do on Iran is to show that at times they can be helpful, at times they can be less helpful, and that therefore it is very much in the Western interest to deal with them in a way that encourages them to be more helpful. This is classic diplomatic leverage. Again this is being played with enormous adroitness by President Putin, but they are not backing Iran against us. There are circumstances in which that could change and I think we are approaching potentially a rather dangerous point here. I think that if the Americans were to use military force against Iran, the Russians at that point would come out on the other side and there would be a risk that the Russians would actually send additional armaments to Iran. I do not think they would send people to fire them but I think that we would run into that risk. That is the point at which they would part company, but for the time being they have not parted company.

Q163 Lord Swinfen: Following your remark on Russia’s concern with a rising China, Sir Roderic, is there any migration from a highly populated China across the border into a lowly populated Siberia?

Sir Roderic Lyne: There are a lot of people in Moscow who believe that there are two million illegal Chinese immigrants in Siberia. These are people who never go to Siberia. I do go there from time to time and when I was in Vladivostok last year I was told by my driver that there were indeed two million illegal Chinese immigrants, but they were not in Vladivostok, they were in Moscow! There is a lot of mythology here. The short answer is that there has not been a huge migration, although the Russians are very worried about that. Even though that area of Russia is depopulating. The Chinese come across to gamble, they come across to trade, some of them, in small numbers, come across to work, but the Russian authorities are not prepared to do what might be economically rational and invite them in in large numbers to help develop the economy.

Q164 Lord Lea of Crondall: Just on that point, when I was in Kursk I was talking to the Chairman of the Oblast and this came up and he said, “Of course, have you noticed how many Chinese restaurants there are around here?” as if it was obvious that wink, wink, wink, they are not really Chinese restaurants. I said, “No, I haven’t seen any Chinese restaurants; take me to one.” sort of thing, and he shut up and changed the subject. It is the same point—the paranoia is there but I am not sure the Chinese illegal immigrants are. Can I come to the question I was really wanting to ask about which is what you might call non-state actors in all of this. We have got a string of people mentioned here—the United States, Europe, India and China—but of course, arguably, it is the non-state actor called al-Qaeda which is the spectre haunting Europe, it is the spectre of our times. For 100 years we lived under the spectre haunting Europe of Communism; now haunting Europe is the spectre of Islamism. A colleague of ours in this House has written a rather interesting book on exactly that theme. The issue is Islamism, not state actors per se, but in all of the manifestations, whether in Iran, Iraq, and so on—is the fear of the New Armageddonism, if I can call that an “ism”. The theory is that there is a very much more important spectre/issue which we ought to discuss as such, and not just talk about bilateral relations between Russia and whoever.

Sir Roderic Lyne: I think that is one of a number of areas where we do have a very large common interest with Russia, but it is not the only one, because proliferation of weapons and dealing with the environment are other such areas. I do not think that our analysis exactly coincides with the Russian analysis. President Putin, particularly in his earlier period, used to present the Chechen War as being the front line of defence of Europe against Islamic terrorism. There was quite a lot of evidence that there was some direct involvement of al-Qaeda in the Chechen war, nevertheless the Chechen War did not happen because of al-Qaeda, indeed it is a conflict that has been going on for the better part of 150 years, and it would have happened irrespective of al-Qaeda. It was a situation that al-Qaeda perhaps tried to exploit but it was not the main dimension of that. We have had some small elements in the last few years of successful co-operation with the Russians in dealing with specific elements of international terrorism. There was one operation that interdicted the sale of Russian surface-to-air missiles of a small kind to America through Britain that actually led to a court case which therefore became a public affair, in which British, Russian, American intelligence and security agencies co-operated to interdict an operation. I do not think that at this moment you have got a huge problem of Islamic terrorism in Russia, but I do think you have got a number of stresses and strains of different kinds in different parts of Russia. There is a lot of instability in the North Caucasus not just in Chechnya. Some of that, but not all of it, is religiously based; some of it is based on ethnic groups and subgroups of a very complicated kind. There is a great fear in Russia that extremist Islam could spread into cities to the north which have got large Muslim minorities, but for the most part those Muslims have not been radicalised and have lived very peacefully and in large number in Russian cities with relatively little trouble, although there have been a number of racial incidents, which I think I would separate very clearly from terrorist incidents, where they have been in some places.
demonised because of the colour of their skin and their religion.

Q165 Lord Lea of Crondall: You do think that their eggs are in the same basket as us in some sense of Christendom versus Islam? It is impolite to put it quite like that but it is not Islam it is Islamism, in other words Armageddon-ism. 40% of Americans believe in this Armageddon-ism reciprocally. Do you see the ideology of the dispossessed now in the worlds Islamism rather than Communism?

Mr Grant: I think Russians do see it that way and that is why it is quite hard to have a conversation between people from the EU and Russia on this because the prejudice and hostility towards Islam that I have seen in Russia is quite unlike anything you get in most parts of Europe. Despite the fact there are quite a lot of Muslim people living in Russia most of whom, as Rod says, are well integrated and not a problem, when you talk to Russians about Europe and European values they immediately start talking about Christianity. They start lecturing us for allowing too many Muslims into European countries. They all seem to think, bizarrely, that due to the rate of birth of Muslims, 30% of the British population will be Muslim in 10 years’ time. I have had very sophisticated, well-educated academics saying that to me. They do think, rather like some people in Washington think, that Europe as an entity is being undermined by rapidly breeding Islamic terrorist fundamentalists in their midst. A lot of Russians seem to say that. On the question of Islamic fundamentalism spreading beyond the Caucasus, I do not think it has spread very much, but I was quite recently in Kazan and there, where it is an autonomous republic, certainly I picked up from a meeting with Shaimiev, the President of Kazan, that they are very worried about Islamism spreading. Some of the people in Guantanamo Bay are from Kazan. I think there is a growing worry about that. If I may come back to say one thing on China. I think the China-Russia relationship is going to be one of the most interesting and important relationships in the world in the next 50 years and you might want to talk to a guy called Bobo Lo who is from Chatham House. He is just finishing a book on the China-Russia relationship. I am not sure what is going to happen. There is the Bob Kagan thesis which is that we will see an axis of autocracies because values are going to matter a lot in foreign policy in the future and therefore whatever mutual dislike there is between Russian and Chinese leaders they will be forced to work together to oppose the Europeans and Americans, who will go round preaching democracy. That thesis is not impossible but equally I take Rod’s point that the dislike among the leaderships is quite strong. I have spent some time in China talking to people about Russia and they do not take Russia seriously. They see it as a minor and unimportant country. The paranoia that many Russians feel towards China is extraordinary. I have talked to Khloponin, who is the Governor of Krasnoyarsk, and he was saying, “If we do not do something the whole of Siberia will be yellow in 10 years’ time.” If you look at a map Siberia is nowhere near where the Chinese people live—you have got the Gobi Desert in the way, so I think there is a lot of paranoia there that shows no signs of diminishing.

Q166 Lord Anderson of Swansea: In Kazan I was told of quite substantial Wahabi money going into the libraries there which was causing some concern. Obviously the major Russian concern in terms of Islam would be in Chechnya, Ingushetia, Dagestan and that area, but does it go beyond that and, more importantly for our inquiry, to what extent are there discussions between the European Union and Russia on counter-terrorism?

Sir Roderic Lyne: I am not aware of discussion between the EU and Russian on counter-terrorism. I think it is mostly being done bilaterally between the major EU governments and I think there is probably some of it in NATO rather than the EU. By its nature it tends to be handled in a fairly confidential way.

Q167 Lord Anderson of Swansea: Is there co-operation?

Sir Roderic Lyne: To a degree, yes, there is recognition that we are all against terrorism. I think the co-operation is inadequate because it is extremely hard for agencies that were so opposed in the Cold War, and in the case of Russian agencies are still essentially I think fighting the Cold War, to cooperate with their former opponents. I do not speak for those agencies but that was my experience, that we had levels of co-operation in this but we were always disappointed that we could not get deeper in face of this problem.

Q168 Lord Anderson of Swansea: Can I move on to the next area. Firstly, it would be very helpful for me if you were to define what is “liberal imperialism”, in the Chubais sense?

Sir Roderic Lyne: I remember reading the phrase when Chubais first used it and I felt sad that an intelligent Russian economic liberal like Chubais was talking in those terms. The short answer is I do not know, except that it was a reflection of the need of a political leader (which he is partly) to chime in with the nationalist mood in Russia which believed that Russia should be the dominant regional force. It is not a suggestion, as I understand it, that Russia should reclaim sovereignty over the newly independent countries but the suggestion was that Russia had a natural right to leadership—and sometimes we hear Americans talking in those terms
too, but that was my understanding. I think there is a very, very deep-seated belief in Russia that Russia does have a natural right to leadership of the neighbouring countries. I think that when Putin described the collapse of the Soviet Union as the “greatest geo-political catastrophe of the last century”, he was actually articulating a view that is shared by 98% of ethnic Russians—I say ethnic Russians—not because they want Communism back but because the Soviet Union was their country and losing two-fifths of your population overnight without warning is a terrible shock to people.

Q169 Lord Anderson of Swansea: Is there a real difference between views in terms of lost influence in respect of the former Soviet Union, hence the neuralgic reaction to the loss of the Baltics for example, to Georgia, Moldova and Ukraine and that of the former Soviet Empire, those countries just beyond the borders? Is there a marked difference in the approach?

Sir Roderic Lyne: Yes, they knew they were occupying countries in Eastern Europe that they did not really have a right to occupy and that sooner or later they might have to pull out and allow Poland to become Poland again or East Germany to become East Germany. I think to a degree there was acceptance also that the Baltic States, which had been independent between the wars, had a right to independent statehood. After all, Gorbachev allowed that to happen before the break-up of the rest of the Soviet Union. I still think that most Russians find it very, very hard to think of Ukraine and Belarus as separate nations, as independent sovereign states, because I think they were seen as part of the Russian heartland. If we come back to the notion of Christendom, the notion of Russian Christendom is of course very different from ours because you have a very illiberal, nationalist, xenophobic, anti-modernistic Russian Orthodox Church which again saw this as part of its bailiwick. The Caucasus and Central Asia were areas that they were fairly happy to get rid of, except that Northern Kazakhstan was really seen as Russian territory and they developed all the resources in Northern Kazakhstan and all the gas from Northern Kazakhstan goes into the Orenburg collection centre and it was mainly populated by Russians and they used it as a nuclear testing ground to horrific effect. I think there is a distinction in there between what they still feel to be Russian heartland and the rest.

Q170 Lord Crickhowell: The last question on the list you were given is about comments in the pre-electoral period. Can I take up two of Sir Roderick’s opening comments. I thought one was pretty pessimistic in that in 40 to 50 years’ time, I think you said, we might have something that we would like to think of in the West as democracy, and then there was a much more confident view about the developing economy. We have got a rapidly declining population in Russia and a rapidly declining workforce to cope with this economic growth. Is that not going to be quite a problem in the developing economy? How is that going to affect domestic politics and would you comment, please, on sovereign democracy? Clearly at the moment the Russians feel that instability is something that they do not like and prosperity is something that they do, and sovereign democracy seems to be a better way than the instability that arose as people tried to move towards something like Western democracy. We are now into an electoral period and I am not quite sure where Putin is going to emerge from it. Would you comment on how you see the internal political situation developing in Russia?

Sir Roderic Lyne: Perhaps I will take democracy first. The Duma elections which will take place on 2 December will not be fair, but nevertheless are important. They are not fair because the terms of the election have already been rigged by setting a percentage threshold and only having people elected to the Duma on party lists, and by the central and regional electoral commissions making it extremely hard in many areas for smaller parties to get registered, plus the fact that central television is controlled by the Kremlin and appearances on it will be manipulated to support United Russia. Despite all of that, the voting will not be a total fraud or farce. The extent to which you can manipulate voting varies from region to region. It is more manipulable in the North Caucasus than it is in most of Russia and it is being seen as a real trial of strength to show how well United Russia with Putin at the head of the list (albeit curiously not a member of the party whose list he heads) do, whether the Communists are anchored at their 15% and so on. The general attitude to democracy in Russia is that democracy equals the 1990s equals a complete nightmare, and if that is what you are offering the Russian population, they do not want that. They would like to have more law and order. They would like to have much less corruption. Corruption is very high on the list of complaints of the Russian populace, but they are much more comfortable with Putin and the sort of rule he has given them than with what happened in 1990s, and anyway they think that those leading democratic figures were all tainted and a lot of them were allied with big business and oligarchs. I think there is a very important distinction to be made between freedom and democracy. Essentially what Gorbachev and Yeltsin gave Russia was freedom, although Gorbachev did institute what has probably been the fairest election in terms of voting that Russia has had in the 1989 elections to the Congress of People’s Deputies. Democracy in Russia has never
ever happened; it has no history. The country has not yet really started down the road to democracy. Certainly Putin in his seven years in power has talked the talk about democracy, or sovereign democracy or managed democracy but almost always qualified democracy, but he has done nothing genuinely to develop democracy because it has all been top-down. Parties have been invented by the Kremlin top-down. Russia has not yet got to the start line. We need to remember how many hundreds of years it took us to develop democracy in this country, that it came bottom-up and it was based on things like property-owning middle classes. You have now got in Russia a property-owning middle class of maybe 30 or 40 million—it depends how you classify it—maybe 50 million people that did not exist 15 years ago, that at the moment is not terribly involved in politics but as we go down the road in future generations will wish to be more so, many of whose leading lights have had exposure to the world that their parents never had so at least they have some understanding of how democratic countries work. That is why I believe that it cannot happen quickly. I will not guarantee that it will happen at all. There are those who say that Russia is doomed always to remain authoritarian but, as I said, I think there is a better than evens chance that over a period of about two generations Russia will develop a model of this kind, partly because Russian leaders keep saying “this is what we want”. I would rather Mr Putin says, “I am a democrat like Mahatma Gandhi and I want democracy in this country,” even if he is not doing it, than the reverse, Putin himself at the meeting that Charles Grant attended in Sochi (which I was not at) recognised a) that he had failed to develop democracy in his time in power, and b) that Russia needed it. It was a very striking sentence he used there where he said it does not provide a stable future for the country if it depends on one man and one institution, it needs a broader base, and he is absolutely right. If I can turn briefly to the economy, I think the private sector of the Russian economy is developing in quite an effective way. You are seeing better run companies and companies that are run according to principles of governance that we can at least begin to recognise. That gives me considerable hope for the future of the Russian economy because the better private sector companies are beginning to show that they can compete on a global stage. The problem at the moment is that too much of the economy is lumped in the state sector and is under Kremlin control. As I said earlier, until that model is proved once again to be inefficient then it will remain. One of the factors that will put it under strain is precisely the one you mention of demography, that over the next 10 years Russia is set to lose maybe seven million people over a period when, if the economy continues to grow at 6 to 7% a year (which it may not do) it will need more millions of people and that will cause huge pressure on productivity, on investment, on efficiency, all the things that these great big state agglomerations do not stand for.

Mr Grant: I agree with all that. I think sovereign democracy for Putin means autonomy and it is defined in relation to the US. It is about Russia not having to do what the US wants it to do. There is a paranoia about the US that is very strong in the Russia ruling elite and sovereign democracy is an answer to the problem they have about America dominating the world and CNN ruling the airwaves and so on.

Chairman: I would like to thank you both very much. We really have appreciated the time you have given and indeed the wisdom you have given to us this morning. I cannot remember witnesses ever having been heckled quite as much as you were this morning by various interruptions but thank you very much. We may well be coming back to Charles. We are going to be looking into the foreign affairs aspects of the Reform Treaty and we may want to talk to you about that. In the meantime, thank you very much indeed.
Russian population. For this considerable time to establishment but of a very large majority of the supported by a consensus not just of the Russian considerable time to come, and that is because it is policy course is most probably now set for a very we need to recognize is that Russia’s basic foreign actual conflict. To achieve this, I think the first thing as a whole and, above all, of course, do not threaten within bounds that do not threaten the relationship friction on others but the level of friction is kept deep co-operation on key matters co-exists with friends, they mix a relationship in which real and to say that they are not enemies, they are not always which exist between member states in Asia, which is it is possible under certain circumstances, it is not likely and it is certainly not necessary. What I would say we can hope to work for is something like the relations which exist between member states in Asia, which is to say that they are not enemies, they are not always friends, they mix a relationship in which real and deep co-operation on key matters co-exists with friction on others but the level of friction is kept within bounds that do not threaten the relationship as a whole and, above all, of course, do not threaten actual conflict. To achieve this, I think the first thing we need to recognize is that Russia’s basic foreign policy course is most probably now set for a very considerable time to come, and that is because it is supported by a consensus not just of the Russian establishment but of a very large majority of the Russian population. For this considerable time to come, if change in policy does occur, it is unfortunately on balance more likely to be in a direction disadvantageous to us and to our interests, that is to say, in a more nationalist direction. In the long term I am actually quite confident about an eventual Russian move to greater democracy. One factor in this will be that it will depend on pretty open relations continuing with the West and strong Western inputs into Russia, both economic and cultural—not only into Russia itself but also via the huge numbers of Russians who now live in the West. Even in those circumstances though we have to remember that any Russian party, even under a full democracy, which will hope to be elected will always have to be seen by the Russian people as tough defenders of Russian national interests, just as any American party which hopes to be elected by the American electorate has to be seen as tough defenders of American interests. As far as the EU is concerned, there are two obvious issues, I would say. One is actual; the other may now be receding. The first is obviously energy, of which you must have heard an enormous amount in the course of your deliberations. I am more sanguine about this than many people because today and for a considerable time to come the dependence is of course mutual; the Russians are just as dependent on energy markets in Western Europe as we are dependent on them—eventually Russian move to greater democracy. One is actual; the other may now be receding. The first is obviously energy, of which you must have heard an enormous amount in the course of your deliberations. I am more sanguine about this than many people because today and for a considerable time to come the dependence is of course mutual; the Russians are just as dependent on energy markets in Western Europe as we are dependent on them—even more so in a way. Russia cannot direct most of its gas away from Europe without huge and completely unprofitable investments in restructuring its existing production towards pipelines towards the Far East and new liquid natural gas infrastructure. The people in charge of Russia’s energy sector, are state-ists but they are, after all, businessmen and they are certainly very interested in profits. I do not think they are going to do this. When it comes to new fields, like Shtokman, it could be very difficult; to achieve this, I think the first thing we need to recognize is that Russia’s basic foreign policy course is most probably now set for a very considerable time to come, and that is because it is supported by a consensus not just of the Russian establishment but of a very large majority of the Russian population. For this considerable time to come, if change in policy does occur, it is unfortunately on balance more likely to be in a direction disadvantageous to us and to our interests, that is to say, in a more nationalist direction. In the long term I am actually quite confident about an eventual Russian move to greater democracy. One factor in this will be that it will depend on pretty open relations continuing with the West and strong Western inputs into Russia, both economic and cultural—not only into Russia itself but also via the huge numbers of Russians who now live in the West. Even in those circumstances though we have to remember that any Russian party, even under a full democracy, which will hope to be elected will always have to be seen by the Russian people as tough defenders of Russian national interests, just as any American party which hopes to be elected by the American electorate has to be seen as tough defenders of American interests. As far as the EU is concerned, there are two obvious issues, I would say. One is actual; the other may now be receding. The first is obviously energy, of which you must have heard an enormous amount in the course of your deliberations. I am more sanguine about this than many people because today and for a considerable time to come the dependence is of course mutual; the Russians are just as dependent on energy markets in Western Europe as we are dependent on them—even more so in a way. Russia cannot direct most of its gas away from Europe without huge and completely unprofitable investments in restructuring its existing production towards pipelines towards the Far East and new liquid natural gas infrastructure. The people in charge of Russia’s energy sector, are state-ists but they are, after all, businessmen and they are certainly very interested in profits. I do not think they are going to do this. When it comes to new fields, like Shtokman, it could be very different. On the other hand, the Russians certainly will try to capitalise, within certain bounds, on any advantages they see and therefore we do need to think coherently about how to advance bargaining chips and counter-pressure of our own. I should say that the latest news on this does appear to be rather positive: in their
latest negotiations with the EU the Russians have indicated a willingness to make certain changes to their laws. They have also given Statoil 24% of Shtokman on top of Total getting 25%, which is perfectly reasonable, a common international deal. The second question, and for me potentially a very acute one, is the question of where the eastern borders of the European Union and NATO should lie. The enlargement of the EU, the subject of this Committee, is not of course actual and will not be for a very long time to come. EU enlargement to Ukraine, Committee, is not of course actual and will not be for a very long time to come. EU enlargement to Ukraine and the Caucasus may never happen but, even more importantly, if it does, it will be as a result of an internal transformation in these societies which has already in effect made them part of the West, just as had happened in central Europe before those countries joined the European Union. NATO, in my view, is much more dangerous because that can happen much more quickly and without a fundamental transformation of the societies. It is worth remembering that until the latest events in Georgia, there was a very serious push for a Georgion membership action plan with NATO at the next NATO summit, yet every possibility that after that you would have had the same events occurring; in other words, they obviously were not ready. I believe that such a push for further NATO enlargement in the short to medium term would be disastrous as far as relations with Russia are concerned. On the one hand, it would be extremely provocative. On the other hand, it would be very tempting to Russia because we could not actually defend these places in a crisis. The holding open of NATO enlargement also makes it much more difficult to solve a number of specific issues, because there is a strong tendency in Moscow at the moment to hang on to every possible bargaining chip in order to counter such a move. So I do believe that relations with Russia are problematic, that full partnership is not possible and that we do need to draw certain lines against Russian influence. The question is where we draw those lines.

Q172 Chairman: Thank you very much indeed, Professor Lieven. Perhaps I can begin the questioning by asking a rather general question, some of which you have begun to address in those remarks. What do you feel should be the fundamental objectives of European Union policy with regards to Russia? What does the European Union have to offer Russia in the context of a negotiation, and how can it best influence Russian thinking and policy?

Professor Lieven: The single most fundamental interest is peace. That may sound melodramatic but we should not forget that West European countries have fought several catastrophic wars with Russia in modern history and there are developments which could make that a not absolutely impossible scenario in future. The first is peace. The second is stability. Both of these things are necessary if progress is to occur in Russia and in the former Soviet Union. On the basis of this also a relationship which is good enough that we can resolve future unexpected crises. We have the kind of basis to do that without them spiralling into disaster. Finally, of course, we have a very strong mutual interest in economic growth, their investment in us, our investment in them. Russia’s need for European investment is one of our strongest suits. The problem is, of course, it is difficult to orchestrate from a policy point of view because it is the product of innumerable business decisions. Nonetheless, the Russian establishment is aware, as I think the eventual Shtokman deal indicates, that they do very badly need Western investment. We can play on this both when it comes to improving the transparency and legality of Russian business but also, in the last resort, if it comes to warning the Russians that a complete meltdown of relations will have serious implications for Western business investment.

Q173 Lord Anderson of Swansea: In respect of enlargement of NATO, you referred to Ukraine and Georgia. You used two arguments; one, that it would be provocative and two, that these countries could not be defended in a crisis. I agree with that but, of course, those same arguments were used against the expansion of NATO to the Baltic countries, which has proceeded fairly smoothly.

Professor Lieven: I think that the case of Ukraine and Georgia is vastly more dangerous. In the case of Georgia, because after all, unlike the Baltic States or the Central Europeans, it has an unresolved war with two separatist republics backed by Russia. If we make an alliance with Georgia, we are actually committing ourselves to Georgian reunification, if necessary by military force. In the case of Ukraine because it is simply much more important to Russia emotionally and morally. I have had quite sensible Russians, sometimes after a few glasses of vodka, it must be said, saying that “If there were ever a situation in which NATO was going to evict us from Sebastopol, we should do what the Americans would do if anyone offered to evict them from Pearl Harbour”, in other words, fight. I would add one third thing, which is that as latest developments in Georgia and Ukraine indicate, indeed that internally these countries are nowhere near ready for such a move.

Q174 Lord Anderson of Swansea: With that explanation I of course agree. You began by saying that the Western or EU attitude to Russia had veered from catastrophism to euphoria; equally, the Russian
Professor Lieven: Yes. They were hoping of course American. It obviously has not worked very well? What would be your advice to the European Union in the current context about negotiating a successor to the PCA?

Professor Lieven: It obviously has not worked very well. However, it has not worked very badly, as I think the deal over Shokman indicates. The Russians started with, in a way, a wildly optimistic and almost super-French view of the EU as a future superpower with which they could negotiate as power to power and, of course, they then discovered that the EU does not work like that at all. The Russians are very disappointed in the EU, it must be said, because they complain, much like Kissinger, with his “Where’s the telephone number?”

Q175 Lord Anderson of Swansea: But also anti-American.

Professor Lieven: Yes. They were hoping of course after the Iraq war that the EU would emerge under French and German leadership as a real counterbalance to America, which has not happened. I think when it comes to the general framework, part of the problem is that the EU, partly for reasons of principle but also of course because of what it is, it is always looking for structures, for formal rules, for general agreements based on general principles which will govern everything. Of course, the EU in practice by no means always follows that itself but the Russians’ idea of reciprocity is on a case-by-case basis: you give us that, we give you that; we do this, you do that. Yes, we can change certain rules and you can change other rules but they are not going to tie themselves, into a general framework which would bind them directly.

Q176 Lord Anderson of Swansea: As we move from the PCA, what, in your judgement, should we move towards?

Professor Lieven: I think it is more important to draw up a set of general principles and aims, and then decide individual cases on a more ad hoc basis while keeping those principles in mind, rather than committing ourselves to rules, strict rules, which then continually break down in practice and lead to bad blood. That said, of course, we probably do need some kind of formal agreement but almost more for propaganda and atmospheric processes, because if we do not get it, it will be seen and portrayed as a great step backwards. But, to be honest, I am not sure that, in practical terms, this is the most important objective.

Q177 Lord Chidgey: May I move on to Member States and solidarity? Professor, I would like to link this concept of what the range of options may be among Member States to your opening remarks regarding the sort of partnership that we in the EU could have with Russia. It occurs to me that you will have as many different opinions of what our relationship might be with Russia as there are members of the EU. So the concept of developing a common position and the possibility of forging greater unity and coherence of approach among Member States may well be impossible to have. I wonder if you could link that therefore with your views on what sort of partnership we might have with Russia in the EU. You mentioned that it might well be similar to those that we aspire to have with Asian states but then there are as many different forms of democracy, culture, religion and whatever in Asia as there are members of the EU. I find it quite challenging. I wonder if you could perhaps reassure us that the challenge can be met.

Professor Lieven: Obviously, the reality of deep divisions of interest and perception among EU Member States just is true; it is there and it is a constant challenge, and I do not think anything I can say or recommend will abolish that. From that point of view, one does also have to think seriously about British policy because, after all, one is talking about players within the EU influencing EU policy rather than the EU making up its mind in some abstract context. What I would say on the score of solidarity is that, as far as the East Europeans, let us say the Balts and the Poles, are concerned, they cannot have it both ways. They do have real fears as regards Russia, some of them, frankly, paranoid, others more real, particularly when it comes to energy dependence. They also of course have real ambitions in the former Soviet space which are seen from the Russian point of view as actually in historical terms expansionist or aggressive. What I would say is this. We have to back the Balts and the Poles in certain circumstances against illegitimate and dangerous Russian pressure, and also just where we think that the Russians are clearly wrong. That could be the case, for example, with Polish meat exports; it could most certainly be the case in future if Russia uses the energy weapon against Poland or the Balts for explicitly political purposes. On the other hand, if we think that on particular issues the Poles and the Balts are wrong, their policies are wrong and they are acting with unnecessary provocation, we cannot allow them to tell us to shut up in the name of European solidarity. That is what I mean about not having it both ways. The problem is, of course, on so
many issues, in doing what they do, the East Europeans have American backing, which brings the whole transatlantic relationship into play. From a Russian point of view, so many things have occurred, actions have been taken, which we and our representatives have said to the Russians clearly in private that we do not approve of, that we do not like, but we have not been willing to say that in public. I think we should be willing to say it in public. For me, that would include most recently the whole issue of missile defence, at least the short-term plans to extend American missile defence to Poland and Eastern Europe, because it does, I think, in strict—maybe paranoid but nonetheless strict military terms undermine Russia’s nuclear deterrent and, from the Russian point of view, that is something they take very seriously.

Q178 Lord Chidgey: Can I ask a supplementary here, Lord Chairman? From what you say, Professor, it would appear that one of the ways of getting a coherent approach amongst Member States is recognizing that the threat of military force of Russia is the unifying aspect of NATO and therefore of the European Union, which I would have thought was the path they would not want to go along but it seems that history is almost repeating itself, that European interests come together when there is a unifying threat from elsewhere, whether it be commercial, industrial, strategic or military. That seems to be an opinion that might find a certain sympathy amongst a range of EU states, which, as I say, is very disappointing if that is the case.

Professor Lieven: I think it is worth saying that I do actually believe in keeping NATO as ultimate residual guarantee against a future insane Russia. I think it is good to keep it there in reserve but that leads straight to my previous point about where the borders are. If you are talking about defensible borders—and by this I do not just mean militarily defensible but defensible in terms of the solidarity of the places that you are defending—once again, we can defend the eastern border of Poland; with somewhat more difficulty we can defend the eastern border of the Baltic states, not because of the military issue but because of the whole ethnic Russian issue within the Baltic states; I do not believe that we can defend the eastern borders of Ukraine, let alone the northern border of Georgia, defined as including Abkhazia and South Ossetia. The thing is, there is a reality about a great difference between the Russian and the West European systems; there is a reality about a latent threat. I think we should frankly acknowledge that and base some of our ultimate planning on it. We should not allow some of our allies to turn a defensive posture into what would be seen by the overwhelming majority of Russians as an offensive posture and which would actually make the possibility of a clash very much more likely.

Q179 Lord Jones: Taking the solidarity theme further, what do you think the Russians are getting from their constant pressurisation of individual EU Member States? What is it in it for them? Is it in the United Nations? Do you think that the EU is up to the challenge of giving good advice and assistance to individual states which are coming under pressure?

Professor Lieven: There is Russian pressure and there are also Russian bribes, especially in the energy sector. The pressure is simply the Russians reacting to policies that they see as anti-Russian and hostile to Russian interests. The question is how far they are prepared to go in the last resort. So far they have not gone so very far. These have, after all, been limited clashes; a clash over Polish meat exports is not refighting the Battle of Poltava or whatever but pressure of a more or less discreet kind will continue and we have to be prepared to push back. One of the ways we can push back is when it comes to Russian investments in Western Europe. Of course, we have to be able to calibrate this in an intelligent way, firstly, because, after all, we do not want the Russians to stop us investing in Russia. That is a good thing from every point of view. Secondly, there are issues of fairness and unfairness involved here. There was a French diplomat who said to me that it probably was not a very good idea to bar Russia from the Airbus consortium on grounds of lack of transparency the week after its chief executive had been forced to stand down for insider trading. The EU has an institutional capacity, for example, a formal, legal capacity to insist on much greater transparency from Russian corporations, and we can use that to hit back. This is what I mean also about making up our policy on a clever tactical basis rather than tying ourselves rigidly to general principles. We can hit back on that. The other Russian policy which is much more difficult to counter is, the Russians going round offering, I cannot remember how many European countries it is, that each of them is going to be the energy hub of Russia’s exports to Eastern Europe. Frankly, if all 11 of them are stupid enough to believe that, we either have to persuade them that they cannot all be, but then some of them can be, or, I suppose, we have to make counter-offers. The problem is that in the energy field, if the counter-offer is Nabucco, for example, and the alternative pipelines across the Caspian, Russia is in a very strong position there and without having to go too far in the direction of absolutely illegitimate moves. It is in a very strong position geographically and, of course, the legal status of the Caspian is genuinely undecided. That is a perfectly legitimate issue under international law and particularly, given the fact that the International Law of the Sea has not entered into general force. The
other reason why the Russians are so strong, or at least why they may not be so strong but we are not so strong in that regard—there is geography and cost, of course, when it comes to building these pipelines but it is also because there is also China. If it comes to real power in Central Asia, in future it may be the Chinese who come first, the Russians who come second and we will come very much third. I always remember a Kazak official saying to me “Look, we want to deal with you, we would like to export to you if possible, and we certainly need your investments, but always remember, in the end, for us, Russia is there, China is there and we are in the middle. Everything we do will be ultimately determined by that irreducible fact.”

Q180 Lord Jones: In all of this, how malignant or benign is Putin? Is he a major force in the pressurisation, or does it just come from the bureaucracy and the Kremlin and so on?

Professor Lieven: No, I think in the end he is a major force. That is what I mean about there being a basic consensus in the end—not necessarily on every issue and, obviously, there have been moves which have been clearly driven by sectional interests, but Putin defined Russia as a great Eurasian power. He has always stressed that Russia is a European country, that it must have good relations with the rest of Europe, with the EU. He has also always stressed that Russia is a great power within Europe. I think part of our problem is that that is a concept which we find very difficult to get our minds round because it is basically a 19th-century concept. On the other hand, it might help us to get our minds round that if we recognized that, to a considerable extent, it is also how the Turks see themselves, one of the reasons why we find Turkey also so very uncomfortable. The difference is, of course, that the Turks are aiming at membership and have a more or less reasonable chance of it. I do think that part of the key problem, as we see from the latest Turkish moves over Kurdistan, is that the Turks are insistent upon retaining a level of freedom of action internally and externally consonant with their historical image of themselves but also, to be fair, consonant with the threats that they see to themselves, which they believe are far greater than those to any other EU member or would-be EU member. I do think that Putin has always at one level genuinely wanted good relationships with Western Europe. He does not want to threaten Western Europe. He is however insistent that the EU recognize Russia’s status as a great power and not simply a member of Russia’s periphery, along the lines of Moldova or Algeria.

Q181 Lord Crickhowell: You have been talking about Russia’s strength and power and its ability to apply pressures on Europe. Clearly, there are abilities to do it in short-term situations but you have said very little about the Russian weaknesses, except to refer to the need for investment. Of course, they have a huge demographic problem; there has been a rapid and substantial fall in their working population, when they economic growth demands a larger workforce. The figures are very startling and you will be very familiar with them. At the same time, we keep looking at the energy thing and clearly, in the short term they can apply pressure but actually they have a mega-problem on energy because their three major oilfields are actually running down and they do not have the new ones in line, they are unable to meet their own domestic supply, let alone their external supply, Gazprom is notoriously inefficient. So there are enormous economic and even energy weaknesses ahead of them which they can probably only resolve with substantial contributions from Europe. Could you just say a little more, because we really have not touched on the fundamental underlying weakness. Putin talks about a great power but actually, even in comparison with Turkey, which you referred to, they are not in population terms a vast country any more, and they have these huge problems ahead of them because of their collapsing birth rate and the demand for a larger workforce.

Professor Lieven: Yes. It should be said though that the birth rate seems to have bottomed out. It has not started increasing again but the decline has stopped. One interesting suggestion is that this catastrophic decline in the birth rate—of course, the other issue is the death rate, which is different—was the product of a move from a Soviet child-rearing system, in which everything was provided by the state, to a much more personal and individual one. Now, as more and more of the population does have the money essentially to take its kids on holiday over the summer rather than send them to pioneer camp, and that is one thing, but also of critical importance, speaking as a father, it is the predictability of future employment. If you do not know where your job or your wage is going to come from, you are not going to have more kids. If you are pretty confident that your wage is secure and is even going to increase, which a great many Russians now are, you are going to have kids, all other things being equal. In other words, there is nothing genetic about the decline of birth rates; they can go down and they can go up again. From the point of view of internal political stability, this is a good thing. Steep economic growth with a declining population is a lot better than steep economic growth which is continually cancelled out by a rise in population, as in India, for example. Of course, the long-term existential threat for Russia is indeed Chinese and Muslim immigration. I have heard concerns expressed about Western Europe from that point of view as well. We think we are probably going to survive, touch wood. I think the Russians will probably survive as well. On the investment in
infrastructure, you are absolutely right, of course, but it must be said that this is a problem that the Russians do now fully recognize themselves. I do not know if perhaps some of you may have read the Financial Times mini-essay on that this morning. They are well aware of their need to invest huge sums in this. There are real questions, of course, about competence, corruption, the role of the private sector and, of course, the role of international investment. The Russians, however, are well aware that the new power of sovereign funds in Asia means that they are by no means simply dependent on Western investment from this point of view, but I do not believe that a state and an elite which is collectively and individually so dependent on oil and gas production is going to allow its cash cow to die of starvation. Historically speaking, when the Russians think that something is very important, they usually do manage to patch it up, while maybe neglecting other sectors. The other thing, of course, from the point of view of dependence, a fascinating question, is the relative balance between oil and gas in the future. Most indications are that relative oil consumption in the world will go down relative to gas, for ecological reasons, for reasons of insecurity of supply from the Middle East, for reasons of price. That makes gas even more important. Moves to clean energy may also increase the importance of gas because of hydrogen. Russia has 12–13% of the world’s gas supplies. It has something like 27% of the world’s gas supplies. Greater importance of gas means Russia’s relative importance goes up in the world, not down. That then raises the question, of course, of how far they can actually use this for leverage and the whole issue of a gas OPEC. That in turn brings one to the question of how far future Russian gas production will be directed towards liquid natural gas because, basically, when you think about it, pipelines are stuck; you cannot wave them around as a weapon because you cannot take them out of the ground. In that sense they are quite different from oil. If you can actually trundle LNG around the world, then of course you can think much more about bringing pressure to bear on particular markets, directing it here or there, as, of course, in the past the Gulf states did.

**Q182 Lord Hamilton of Epsom:** Lord Crickhowell has really taken almost all my questions. The GDP for Russia, we read somewhere, is the equivalent of Belgium and Holland stuck together. The population figures we were given—and can you confirm these—now 140 million, dropping to 110 million over the next 20 years? Fundamentally, the repeated point that Lord Crickhowell made, the reason why the GDP is going up is because the oil price is going up, not because they are producing any more oil. This emperor really does not have any clothes. I understand what Putin is playing at; he wants to rebuild a great feeling of nationalism and pretend they are a superpower. They are not a superpower and they are going the wrong way, and one day reality has to dawn, has it not?

**Professor Lieven:** They do not want to be a superpower. They are very clear about that. Superpower for them implies what the Soviet Union was in the world, what America is today. They have given that up. They know they have no significant role in Latin America, Africa, etc. They are determined to be a great power on the territory of the former Soviet Union and, of course, from that point of view, you get into the question of relative strength. In the end, all real power in the world is relative; it is to do with power relative to other people. They are a great power relative to Ukraine, Kazakhstan, Georgia, and they are also a great power in military terms relative to us. That is more ambiguous.

**Q183 Lord Hamilton of Epsom:** They are not spending as much money as us.

**Professor Lieven:** No, but then they do not need to, in terms of purchasing power.

**Q184 Lord Hamilton of Epsom:** If I can just pick that up, we could beat them in a conventional war tomorrow.

**Professor Lieven:** I do not think so.

**Q185 Lord Hamilton of Epsom:** We certainly could, because our technology is miles ahead of theirs.

**Professor Lieven:** Who would we beat them with?

**Q186 Lord Hamilton of Epsom:** We would beat them in the air because our avionics are just of a different dimension.

**Professor Lieven:** It is a question of where we fight them. That was my whole point about borders.

**Q187 Lord Hamilton of Epsom:** Wars are won in the air.

**Professor Lieven:** I happen to have just been reading Robert Pape’s book about air power and I have to say that I think the historical evidence suggests that is a very questionable proposition. The point is that on the ground . . . Firstly, let me say very clearly—I warned against catastrophism—I do not think we are going to fight them.

**Q188 Lord Hamilton of Epsom:** I am not saying that but I am just saying, in terms of our relative military positions, we could beat them.

**Professor Lieven:** Where? We would beat them in Poland, yes, because the Poles would fight like crazy. We would lose in Ukraine. We would have a hostile population at our back and we would be hopelessly outnumbered on the ground but, above all—and I
am sorry to say this to an EU Committee—our gallant European allies would not fight. There have been melancholy examples within the British military experience of my parents of the British Army relying on flanking European forces which failed to live up to their role. We should not fantasise about a European defence of Ukraine, which is not going to happen. We should do nothing predicated on the idea that it is going to happen. That is very, very dangerous. I would also say it is immoral. It is immoral to give security guarantees that you do not intend in fact to keep or cannot keep.

Q189 Lord Hamilton of Epsom: That is a separate issue. 
Professor Lieven: On the demographic issue, I am really not sure any more that it is going to go down to 110 million. 130 million, maybe 125 million, yes, but do not forget the Ukrainian population is also falling and the Baltic population has been falling very steeply indeed. So within the territory of the former Soviet Union, it is not just Russia that is going down.

Q190 Lord Hamilton of Epsom: How significant is emigration? 
Professor Lieven: From Russia? Not so very significant any more. It is significant and damaging at the intellectual level. They have lost a good many of their best intellectuals, some of whom may now go back but it must be said, of course, that has been countered to some extent by a very large number of immigrants from the former Soviet Union, especially Ukraine, Belarus, Georgia, going to Russia to work, including some highly educated ones. The Russians cannot challenge America on the world stage but if one gets into the whole business of who is a great power and who is not, South Africa is not a great power on the world stage but it is a great power within southern Africa, and it is a question, once again, of where precisely one is confronting Russia.

Q191 Lord Truscott: Professor Lieven, if I could return to the issue of energy, there has been a great deal of talk around the political use of energy exports as a weapon. You referred to it yourself in the case of Poland. We have had Dick Cheney talking about it in terms of blackmail, Russia using its energy resources to blackmail its neighbours. Putin himself in his PhD thesis, as you know, talked about exploiting Russia’s natural resources to restore its great power status and, whilst I accept what you say about superpower status, Russia cannot be a superpower any more, I think Putin does want to see Russia as a great power on the international stage. I think that is why he is so keen on fora like the G8 and why Russia is keen to get into the WTO. One of my Russian friends, interestingly, said, “Who needs tanks when you have oil and gas?” You also mentioned mutual dependence and there was a case of Gazprom cutting off the gas to the Ukraine, and they said that was purely a commercial decision rather than a political decision. What is your view in terms of the balance between commercial and political interests in the energy sphere or are they so inseparable that you cannot really say that they fit into separate compartments?

Professor Lieven: I am very glad you mentioned the WTO. I should have mentioned that. That is one area, of course, where we do have a real capacity to bring pressure to bear on Russia. It is not quite as strong as some people in the West think that it is because the Russians are more ambiguous on the subject than may initially appear. I had a meeting with some Russian small businessmen recently who were very doubtful about WTO membership from their point of view, but the Russian top establishment, being dedicated to Russian exports, really is interested in the WTO, and we can bring pressure to bear there. On the political uses of energy, I always remember that Dean Acheson, the American Secretary of State, was once asked in condemning terms whether American oil companies were not agents of American political power and influence in the Middle East, to which he replied, “Of course they are”, as if there was no serious question on the matter. The Russians do not see themselves as acting in outrageous moral terms in the view of modern history by treating their own energy companies in this way. As far as Ukraine is concerned, the other thing to remember is, not just from the Russian point of view but in reality, that what the Russians have done is cut their energy subsidy to Ukraine, Georgia, and Belarus as well, an energy subsidy which, to Ukraine, on an annual basis, dwarfed Western aid to the country, $3-$5 billion a year. The Russians are correct in saying that there is no way that the United States, for example, or any other major power would continue to give subsidies without expecting real geo-political benefits in return. They just would not. So undoubtedly Russia is going to go on playing that card. On the other hand, as emerged very clearly from the last crises, they have to be careful about it because, in the end, the Ukrainians, to be blunt, if they are cut off, will steal the gas that is going to us in Western Europe and we will howl about it. Furthermore, if this happens often enough, we will do something, which I firmly believe, by the way, we should be doing, which is we will start thinking and investing really seriously not just in alternative sources of energy, which may be a fool’s errand, but in alternative energy, which we should be doing for the sake of global warming anyway. When it comes to the balance between politics and profit, I think it is worth recognising that, to some extent, individually and collectively for the Russian establishment this is the same thing. These
people have turned themselves into great magnates, personal magnates, very, very rich people, on the strength of having gained control of oil and gas from the oligarchs who took it over under Yeltsin. On the one hand, they are genuinely, I believe, dedicated to the interests of the Russian state, as they see it. They remind me of a saying of Keynes about Clemenceau, that he was a completely cynical politician who had only one illusion: France. But on the other hand, these people like to make huge amounts of money from oil and gas for Russia but also for themselves, and they are not going to cut their throats over that. To emphasise, it is well worth giving the Russians very strongly the idea that the more they play around with these issues, the stronger it makes the impetus in Western Europe for real moves towards alternative energy but, unfortunately, of course, there are terrible problems on our side with this, to take only one issue, German attitudes to nuclear energy, something which our former Prime Minister raised in very acute form. After all, if we are going to do in, depending on Russian fossil fuels, in a way, that is our decision. We can do something about it. It will take us a generation, a lot of money and a good deal of discomfort but the decision is nonetheless in our hands.

Q192  Lord Truscott: You said the aims of profit and politics to a certain extent are inseparable but are they? As we have said, Russia needs a great deal of foreign direct investment to develop its natural resources. It has clearly taken a political decision that it is going to limit that. With Shтокman, for example, they said initially they were going to go it alone. Later on they did bring in the Norwegians and the French. With Sakhalin they put pressure on Western investors there. So you could say that, in a way, to reinforce their control over the strategic energy sector they are discouraging foreign direct investment, which, if you had a purely open market and you increased their foreign direct investment, that would clearly increase the profitability and production in the gas and oil sectors. So in a way, you could say they are putting politics before profit—not that other countries have not done that. The Arabs did it in the 1970s, we are seeing resource nationalism in South America. It is not new but you can argue that they are putting the emphasis on controlling the commanding heights of the Russian economy, ensuring the state controls that, not foreign investors.

Professor Lieven: I think a critical question, which was raised by the Financial Times piece that I mentioned today, is whether in fact they do extend this principle of controlling the commanding heights from the energy sector, where indeed they are actually conforming to the basic international pattern outside the Anglo-American world, which is of state dominance but, if they extend that to more and more sectors of the economy, not just the military industrial complex, okay, that is fairly normal as well, to transport, even to consumer goods, then yes, they will in the end strangle not just foreign investment but domestic investment as well. Western businessmen who I have talked to are certainly not convinced that that is going to happen. They still believe that there are tremendous opportunities in many fields in Russia in the years to come. We will have to see what happens but, clearly, we can go on and on saying to the Russians by definition, “If you want major Western private investment, you have to allow companies to own significant assets in any field not legitimately defined as strategic”. The other thing that I do have to say about the whole Sakhalin business and some others is that if you talk to oil industry people, they will acknowledge in private that they got some very good deals during the period of Russia’s maximum weakness in the 1990s and it was always likely that the state was going to claw that back to some extent. In other words, they do not simply say this is a sign in itself that the state is going to rampage around, confiscating everything, but it is a legitimate source of concern. To some extent, one can hope, I suppose, but the more that—and there are tremendous divisions over this within the Russian Government, over the level of state control which should occur—the more they are into contact was part of their daily business and as part of their daily business running international corporations with the international world of business, it will not be necessary simply for Western officials to tell them repeatedly that they risk strangling themselves in this way; they will be told continuously over drinks by Western business partners, which is the whole informal aspect of co-operation, which I think we sometimes tend to forget about in concentrating on the official and the diplomatic.

Q193  Lord Crickhowell: Some of your recent answers you have been heading away from Russian policies to the important question of European policies. Earlier you talked about the need for Europe to act coherently. What should EU policies be and how likely is it that we are going to act coherently? Are we capable of putting together a coherent approach, on energy particularly?

Professor Lieven: Some of the signs have been pretty discouraging but I would hope that we are capable of acting sufficiently coherently at least to rule out collective extreme policies in one direction or the other. After all, there is still a very considerable dominant weight within Europe—not necessarily, of course, within the structures of the EU but within Europe—of a relatively small number of economies who, if they can act together, can in the end make their voice heard. From that point of view, one is talking once again in Britain about British policies
and how far Britain can co-ordinate its policies with Germany, France and Italy and, to a degree, Spain.

Q194 Lord Crickhowell: You have already referred to the fact that Germany stands in a rather different position on a particular interest which makes it quite difficult to produce coherence on this particular subject.

Professor Lieven: Yes, it does and, as you know, although testifying to this honourable Committee, I do not regard myself as an EU expert. I have only just come back after eight years in America. On the other hand, the EU experts who I do know, it must be said, do not seem to have any very clear or convincing radical answers to this question. I suppose if you break it down into certain specific policies, either by the EU collectively or indeed by Britain on its own, then there are various things that we can do. In ascending level of importance but also of unlikelihood, I think we have to go on supporting and defending human rights in the strict sense in Russia and human rights activists. I really question whether it makes sense to make ostentatious gestures of support for the Russian political opposition which (a) stands absolutely no chance of being elected, even in the most free and fair election, by the way. The majority of Russians will not vote for them because they identify them with the disaster of the 1990s, but secondly, some of these people are pretty fishy. I do not think that it was either legitimate or contributed to British prestige and popularity to see our current ambassador in Moscow parading in front of a line of Russian neo-fascists guarding Kasparov’s demonstration. That is unnecessary. It does nothing but annoy everybody. Secondly, I am very strongly of the opinion that we should not have allowed Zakayev and Berezovsky to come to this country in the first place. Of course, we cannot hand them over to the Russians. Berezovsky, after all, we all know what he is not an extremist by the standards of the Chechen separatist camp but I think we have to recognize that if during the Northern Irish conflict Moscow had ostentatiously hosted even a relatively moderate leader of Sinn Fein, it would not have contributed to good relations between Moscow and London. In my view, it would be a very good thing if these people could be encouraged gently—not to go back to Russia and be hanged, but Berezovsky can go to Israel and Zakayev can go to somewhere in the Muslim world. Thirdly, Kosovo. Firstly, a change of nuance. Too much of the language recently on the part of European countries has suggested that this is an EU/NATO issue in which the Russians basically have no essential say or interest and that their role has been purely a negative one. Two million Russian soldiers died and the Russian empire was destroyed in a war which began with Russia coming to the help of Serbia in 1914, the First World War. From the Russian point of view, they have every bit as good a right to have a say in this issue as the Americans do over the interests of Israel, for example. That is not to say that what they are doing is necessarily correct but a change of nuance in saying “Look, we have got ourselves into a terrible mess here. Please help us to get out of it.” Of course, you have a legitimate say.”

Then, of course, the Russians start talking about the price. Here we cannot move formally at this stage but if we could indicate informally a real willingness to move over time on the issue of the separate states in the former Soviet Union and recognize that there are parallels, which there are, frankly—parallels, by the way not just between Kosovo and Abkhazia and South Ossetia but also parallels between Abkhazia, South Ossetia and Nagorno-Karabakh, on which issue we have taken, I have to say bluntly, because of the Armenian Diaspora in the West, a very different line from those we have taken towards Abkhazia and South Ossetia. We have been stressing de facto independence for Nagorno-Karabakh as part of a common state with Azerbaijan. Here you can also start making public indications that they if they will accept independence with limited partition for Kosovo—in other words the separation of Mitrovitsa, the Serbian areas—we are willing to talk publicly about similar solutions in the Caucasus. The reason why this is not, in my view, unethical or illegitimate or contrary, for that matter, to basic Western or indeed Georgian interests is that there is, in my view, no possibility whatsoever—none—that Georgia will ever get these territories back, unless Russia completely disintegrates as an organised state, which I do not believe is going to happen. If one looks at recent events in Georgia, frankly, arguing to the Abkhaz that they should come back into the state under real Georgian authority is a bit of a joke and an insult. So in that we would just be recognizing reality. Finally, I do think that, for our own sake above all, at some point we have to be willing publicly to oppose American policies and actions, above all, once again, in the field of NATO enlargement, that we view as reckless. One of the problems that the Russians have with the EU, to repeat, is that again and again they have been told in private that we think some of the things the Americans have been doing, like abrogating the ABM treaty, for example, in 2002, was quite wrong and illegitimate but in the end we have never been prepared to say so in public. Finally, we could catch them wrong-footed if we now offered to come fully into the CFE treaty, dropping our opposition because of Russian troops in Transdniestra, which remain, and Russian troops in Georgia, which, by the way, have just been withdrawn. Since the Russians are now using the CFE as a blocking mechanism over the missile
Q195 Lord Hamilton of Epsom: Going back to your earlier remarks about full partnership not being possible—and I do not think anybody would deny that today—you might not have said that though at the time of Yeltsin, I think, and we do not quite know what is going to happen in the future. I strongly feel that we should be very purposefully leaving the door open, by which I do not mean we say we want to see Russia as a member of the EU tomorrow but we should be making absolutely clear we would like them one day, particularly as they have a relatively small decline in population, a tiny GDP and everything else, and they are not this great superpower they think they are, and what we are in the business surely of doing is trying not to feed the paranoia that there is in Russia that all foreigners hate them. If we are actually saying “We would like to see you one day as a member of our club”, not putting any timescale on it or anything else, would that not be a helpful gesture?

Professor Lieven: I certainly think that we should continue to stress again and again that we want Russia as a partner, that we do not regard Russia as an enemy, and so forth and so on. When it comes to actual membership, I do have to say I am very uneasy, as a British subject, at the idea of British troops, British/European allies, guarding the eastern borders of Ukraine. I am equally uneasy about having a European Union border with China along the Amur River, something which, if the demographic trends which you have described continue, could at some point in the future become one of the most dangerous issues in the world, especially as far as Russia is concerned. For similar reasons, I have to say I am very sceptical about bringing Turkey into the EU. That means a European Union border with Iraq and Iran, and we see what is happening on the Turkish border with Iraq at the moment. Given all the worries that we have about the coherence of the EU and the EU’s real ability to draw up and stick to common policies, I do feel that there is something to be said at the moment—and also given the relative decline of the US in terms of global power and, above all, the limitations that we have seen on real American military power—I do think that at the moment and for a good time to come there is a real case to be made for Western and especially European Union strategic modesty in that regard.

Q196 Baroness Symons of Vernham Dean: We have touched on, indeed, we have really focused on quite a lot of Russia’s preoccupations in terms of foreign policy but earlier on this morning you said that you thought the single most fundamental issue for the Russians was peace and then you went on to talk about stability. I suppose you could say those are the fundamental issues for virtually any country in the world. Everyone wants peace, everyone wants stability, most of us think prosperity is quite a good idea too, which is a concomitant of both the other two. What else do you think motivates Russian foreign policy? You have touched on China, briefly on India—what sort of relationships do you think Russia wants to develop with China, with India, with these huge emerging economies to their east? You have talked a lot about Europe and a lot about the United States; let us look east in foreign policy terms for a moment. What about those countries?

Professor Lieven: When I talked about peace as the fundamental interest, I was actually talking as much about us as Russia, and that it is the fundamental interest of the European continent. Once again, I do not want to be melodramatic but history is a long business and 1939 is not that far away, nor is 1914, nor in the context of Sebastopol is the Crimean War, although that is a bit further back.

Q197 Baroness Symons of Vernham Dean: What about the future? What do they want in terms of their relationships with those countries?

Professor Lieven: The first fundamental Russian national interest, leaving aside issues of influence beyond its borders, is of course territorial integrity.

With regard to China, they have deep concerns about the future, but concerns which the Russian establishment, unlike parts of the Russian media, has been very careful to keep private. They have been very disciplined about that, not talking in the future, because of course they are very afraid of Chinese immigration to the Far East. That is one reason why they do now seem finally to be getting their act together as far as a real programme of economic regeneration in the Far East is concerned, but even that has dangers. Rebuilding infrastructure needs labour, and where is the labour going to come from? China again. The ultimate Russian nightmare is a situation in which you have a massive Chinese population in the Far East who essentially, not initially with China’s backing, start to assert themselves as the dominant power and then China, maybe even without wishing to, is forced to come in on their side and you have a situation in which the Chinese outnumber the Russian forces already in the Far East by an order of magnitude. Once again, it is not something the Russian talk about but it is one reason, though not the one only, why they are so insistent on remaining a nuclear superpower, if nothing else. They want to go on massively outclassing the Chinese for as far ahead as they can possibly see. On the other hand, of course, Putin is very insistent on this and I think it marks a certain
shift in Putin’s thinking, the belief that China is a critical Russian partner and ally, and they are clearly balancing with China against US influence, most notably of course in Central Asia now. That is partly balancing. It is also from the Russian point of view a recognition of reality that China is going to become more and more powerful on the continent of Asia and in Central Asia. If the Russians do not want to confront them, which they really do not want to do, they have to try to build up a co-operative relationship.

Q198 Baroness Symons of Vernham Dean: Do you think they feel that threatened?
Professor Lieven: Today, no. In the long run, yes. As I say, for the demographic reasons which have been stated, with good reason. The population of the Russian Far Eastern province around Vladivostok has gone down from 2.7 million to 2.2 million people. There are 74 million people at the last count just in the two adjacent provinces of China. Go figure.

Q199 Baroness Symons of Vernham Dean: Let us take it in a different forum then in terms of foreign policy: Russia’s role at the United Nations, their role on the Security Council. We hear about a crisis. We do not really hear very much about what they are doing in the Quartet in terms of their partnership over the Middle East peace process. There is a certain amount of interest in their relationship currently with Iran, for very obvious reasons. What do you think are their overriding principles about their policies in the Middle East?
Professor Lieven: It is partly, once again, retaining bargaining counters. The Russians have this fantasy, you could call it—it might not be completely that if the Americans get into really serious trouble in future somewhere—about a grand bargain, at which they will sit down with the Americans and they will give up, as they see it, some really important point, say about Iran, in return for the Americans backing off on what they see as vital issues, for example, supporting Georgia, aiming at Georgian and Ukrainian membership. I sometimes call the Russians from that point of view geo-strategic Plushkins, the character in Gogol who hoarded everything. They are hoarding their counters. That is the first step. They see the world in very realist terms from that point of view. They do not always understand the immense barriers, domestic barriers, to America doing something like that. Beyond that, they do want to play a role as an acknowledged great power. Once again, not a superpower but a power with real prestige and influence on the world stage and that is partly, as it is in many countries, for domestic reasons. That does play well to much of the Russian population, it boosts the image of Putin or whoever succeeds him, more or less. Thirdly, in the Middle East, obviously, they are thinking really seriously about how Russia can use international institutions to further leverage its power in the energy sphere. They have not got very far with those discussions yet, partly because, once again, the future of gas in particular in the world is unclear. They want to oppose any further unilateral American or Western interventions which take place without their consent and, to be fair to the Russians, in ways which they see as deeply destabilising. The Russians do point out, after all, that they did warn the Americans about what they were likely to get into in Iraq. They told them clearly “This is not in your interests to do this” and the Americans did not listen. “Do not blame us for what followed.” As far as Israel is concerned, first, one must say clearly that—what Quartet? The Americans have not allowed anybody else to play a really significant role on that issue. They are determined to dominate the agenda themselves and, of course, can because nobody else really wants to confront them, including the Russians. The Russians have taken occasionally a step beyond the European Union, as, for example, by talks with Hamas in Moscow. In any event, the Russians did tell Hamas “You have got to recognize Israel.” That is a categorical first step towards talks. They were talking from the same playbook essentially. The Russians certainly do not want to go back to a situation of explicitly and categorically backing the rejectionist camp in the Muslim world, partly because they tried that before and it really did not get them very far. Key elements of the rejectionist camp collapsed on them but secondly, because they know that that would radically escalate the level of their tension with the United States and they do not want that, they do not see why they should do it. From the point of view of Iran, the Russians are not indifferent to the dangers of an Iranian nuclear force. They see those dangers, however, in rather different terms. They do not take the threat, either of a direct Iranian attack, which they regard as complete fantasy, or of Iran giving weapons to terrorists as at all serious. One reason for that, of course, is that there are very few Shia in the former Soviet Union so there is not a threat of a Shia revolutionary movement, except to some degree in Azerbaijan perhaps at some point, and the Iranians for their part have been very careful not to support or even to show explicit sympathy for the Chechens. So the Russians do not regard Iran as a threat. The threat that they see is that if Iran gets an explicit, a real nuclear force, other states in the Middle East will follow suit automatically, and then of course two things happen. One is that Russia’s status as a nuclear power is diluted, but second thing is you get more Pakistanis, in other words, you get more Sunni states with nuclear forces which could, God forbid, at some stage collapse and then, the Russians, like the Americans, really do begin to worry about threats of
nuclear terrorism against them. I think, as the Russians see it, the most that realistically anyone is going to be able to get the Iranians to do is to do what the Iranians actually want to do, which is to get not nuclear weapons themselves but the potential to build them, and to basically freeze the Iranians under the NPT and hope that you can keep them there by threatening really severe sanctions if they go further than that. Then, there is the other factor that they do want to sell things to Iran, especially in the nuclear field. Then there is the emotional factor, which one should never ignore, which is that they are very tired of being told what to do by the Americans. There is, it must be said, an irrational emotional tendency to push back. I would not say that that adds up to a coherent policy in the Middle East but that is partly, as I say, at least on one critical issue because the Americans do not really allow anyone else a coherent policy.

Q200 Baroness Symons of Vernham Dean: Do you think they feel threatened by the instability in Pakistan?
Professor Lieven: Yes, directly and indirectly. They do worry greatly—too greatly but then so do we; it is not an imminent threat—about the collapse of the state and the fate of the nuclear weapons, but they also worry much more immediately about the impact on Central Asia of a really destabilised Pakistan being used as a base for Islamist militants who would move not just towards India and Afghanistan but further, which has of course happened in the past under the Taliban. Afghanistan was used as a base not just for Al Qaeda but also for Muslim extremist groups trying to destabilise Uzbekistan, Tajikistan and so on.

Q201 Lord Swinfen: How far and how successfully can Russia restore influence beyond its borders, and possibly even control?
Professor Lieven: I do not think it is aiming at control. Control is very expensive. Direct control also leads to revolt. The Russians are aiming, I think, much more at what one might call a neo-colonialist approach or, put another way, the liberal empire idea set forth by Anatoly Chubais (and, by the way, the fact that Chubais set that forward is another real indication of the degree of consensus on these issues now existing in the Russian establishment). How far can they achieve this? They cannot achieve an exclusive sphere of influence. That is now threatened not just by the West but by China as well in Central Asia—I keep coming back to the Monroe doctrine, something the Russians talk about all the time, of course. It is fascinating to see how Uzbekistan has manoeuvred between Russia and China and has developed much greater freedom of action from that point of view, by the way, vis-à-vis us. I think they stand a reasonable chance of retaining predominant influence, which is to say possibly a somewhat weaker version of what America enjoys in the Caribbean and Central America, not ignoring the fact, that Monroe doctrine notwithstanding, the Americans had to swallow first Castro and then Hugo Chavez and have not been able to do anything about it. The Russians will have two go on swallowing Saakashvili and whoever follows him in Georgia, and some uncomfortable people elsewhere as well. I think though that they stand a very good chance of being able to exclude what they would see as a potentially hostile military alliance, i.e. NATO, expanding further on to their territory. I think they stand a very good chance of continuing to be or becoming again the predominant outside investors in several of the other republics. They stand a very good chance, not always, as they see it, to their benefit, of remaining by far the greatest target of emigration from most of the former Soviet republics, something that they like in the case of Ukraine, something that they used as a weapon in the case of Georgia, and something which, frankly, they have to put up with in the case of Azerbaijan in Central Asia, which they control as best they can. I think they stand a reasonable chance that Russian, the Russian language, will remain the biggest medium of exchange, discourse, business, culture, between the states of the former Soviet Union. That is something they are obsessed by, the notion that Russian has to remain an international language, that we are not going to see Russian simply decline to the level of German or whatever. It has to be like Spanish or Chinese—not like English; they do not aspire to that. The funny thing I keep telling the French is that the Russian is very French but I think they stand rather better chances than the French actually. I think they stand reasonable chances of all those things and you could say as long as the United Nations Security Council retains its present slightly weird configuration they will retain the image of, once again, not a superpower but one of the leading states of the world, below China more and more, I think, unless China hits a rock and disintegrates or has a big step backwards, but up there with India and with us.

Q202 Lord Swinfen: What are they doing in the way of looking forward in their influence by educating young people in comparison to the West, educating young people in the countries that surround them?
Professor Lieven: You mean spreading Russian language education in Ukraine?

Q203 Lord Swinfen: I am not talking about Russian language education. I am talking about students going to Russia to receive education in all sorts of different subjects and students coming to the West from the surrounding countries, again, to be
educated in all sorts of different topics in the way of making long-term relations.

Professor Lieven: An enormous amount of that has happened just by decisions of the students themselves. I must say that I looked at this issue a few months ago and I have not looked at it since. There was actually a debate in Russia then about whether students from the former Soviet Union and, if so, from which countries, should in fact be given equivalence of fees and so forth with Russian students, precisely as the basis for spreading this kind of Russian influence but I must confess that I do not know what decision they came to or if they have in fact come to a decision on that. It is an obvious thing for them to do and I think they probably will do it in future, partly as they get more money in order to do it. Education has traditionally, of course, been one of Russia’s great strengths. Putin is very dedicated to trying to restore that. I think they have also real possibilities in that regard.

Q204 Lord Hamilton of Epsom: We know that the Russians like dealing with European notions on a separate basis, one by one. Do they have a coherent policy towards the EU as a whole? What would they like to see happen to the EU? If all their wishes were fulfilled, would they like to see it disintegrate as an entity?

Professor Lieven: It depends on what we do. At present, no, they would not like to see it disintegrate, partly because they are very interested, for their own very good reasons, in the prosperity and the growth of Europe, and they are interested in our investment, they are interested in their investment in us, and our markets. It is not a Russian policy to disrupt or destroy that. What they would really like in their deepest hearts is, of course, frankly, once again, a super-French version of Europe in which Europe is essentially a great power allied with Russia against America. The sensible ones now realise that they are never going to get that. Their nightmare, I suppose, ultimately is of a Polish Europe, a Europe which is where policy towards Russia is made in Warsaw and Riga, and not in Berlin, Paris or even London, and in which the EU does become a kind of battering ram against their influence and interests, especially in the former Soviet Union. To put it at its simplest, they would like there to be one telephone number that they can ring in Europe and they would like when they ring that telephone number to get an answer that they like. If they think there is a reasonable chance of that, then they think the more united Europe is the better. If they think that the answer is going to be in Polish and is an answer that they do not like, then of course they want Europe to be as divided as possible. You could say partly, and certainly that is what they would say, they do not have a coherent policy towards the EU because the EU is not a coherent force, so they cannot have. This is what Russian officials say, of course: “Of course we have to deal with you on a bilateral and individual basis. That is how you deal with us.”

Q205 Lord Truscott: Just moving on to domestic politics, if I may, very briefly, yesterday President Putin was quoted as saying that if United Russia won the Duma elections, he would have the moral authority to continue leading the country. So he made a Margaret Thatcher, “I intend to go on and on” statement. What is your view on that? Do you think he will go on and on and what form do you think his leadership might take?

Professor Lieven: He also, it must be said, made what you could call a very Thatcherite remark about his own party. He said basically they were a completely useless lot without a determined common ideology. He actually said that he was only going along with them because there was not anything better—I do not think Thatcher would ever have said that about the Conservatives. It was rather striking, and certainly reflected his own personal autocracy. Yes, I think that basically he will go on. I think that he has been convinced by enough people that he is necessary to hold things together. One of the fascinating questions—and this for me is the question in the short to medium term—about what happens in Russia is that one of the reasons, apparently, why he has been convinced that he has to stay on in an explicitly very powerful role is that there are real fears that otherwise the ruling group, the establishment, will split. Members of the establishment themselves fear that they are not sufficiently united and disciplined to manage their rivalries without somebody in a real, clear position of authority over them. If it splits, then things really do begin to unravel—not, I fear I have to say, in the democratic and liberal direction that we would wish. I would be much more worried about groups appealing to nationalist forces on the streets, trying to turn these up to now fairly pathetic youth movements into something much more menacing. The stability of the country would then disintegrate and lots of people in the establishment would lose their jobs, and possibly even their freedom—not their lives probably, although that cannot be excluded either. The problem is that if one takes that threat really seriously, then, of course, it will threaten Putin’s position as well, and this is, of course, as many people have said, the critical question. It is not about how he manages his way through the immediate succession and the elections; it is how he manages his future position relative to the next Russian President and whether the President escapes from Putin’s control and decides to continue with a strong presidency. This is not China, with a really strong institutional Communist Party. Putin could not go on still exercising dominant control through
the apparat because there is not an apparat in that sense. I do not know if this version is true, and they do not know. The Russian elites are worried about themselves. They distrust themselves. It is an indication of the fact that although in many ways Russia today is much more of an oligarchy than it ever was under Yeltsin, it still has not really fully gelled as an oligarchy. They still feel they need a leader to keep them under control. One of the fascinating things is that support for Putin staying on in a dominant role comes not just from Russian business, including apolitical Russian business, it also has tremendous sympathy in Western business investing in Russia. What will actually happen? These people do have enormous influence. There is still a degree of military discipline among a good many of these people from the former Secret Service. They are even inter-married to a considerable extent, although, of course, as we all know, that does not necessarily lead to family harmony. They also have immense incentives to stick together. To put it at its bluntest, if I could not get to be a director of Gazprom, I think I would accept a directorship of Rosneft as a pretty acceptable substitute. If you kick over the entire table in an effort to get supreme command, you risk getting nothing and, of course, if you go back to the 1990s and really serious levels of assassination, you risk getting nothing, including your life. Whether that will be enough, including with Putin staying on, to keep them together, I do not know. If I were a big investor, which, alas, I am not, I would not bet the farm on that but I would bet a significant investment in Russia. What will actually happen? Putin does in the interim... There are always the possibilities of one cannot necessarily exclude the former at all, particularly, of course, if Putin does begin to have difficulties with his successor and other people in the apparat and actually genuinely needs mass middle-class support against some of his own former lieutenants. I do not know. I really cannot possibly give any firm predictions on that but that is the kind of thing I will be watching for in the years to come, to see if it happens or not. I would not say therefore, from that point of view, that by no means all the indications we have had out of Russia about future processes are as inherently negative as the Western media usually make out.

Q206 Lord Swinfen: I think I am right in thinking that Putin cannot stand as President again. What position to keep control of Russia would he hold and who would therefore appoint him to that position? Professor Lieven: It is like America. He cannot stand for President next year. He can stand after an interval of four years. He can stand again in 2012, so he can come back. That is the dramatic scenario which so many people have held out. He puts in a standing President for four years, he wants to come back in 2012 and the standing President decides that actually, he rather likes the job and does not want to let Putin come back. What Putin does in the interim... There still appear to be basically now, unless something comes completely from left field, which I myself cannot actually see, two choices. One is to run United Russia in the Russian provinces, the small businessmen I talked about, with a seriously reformist and, in the end, anti-oligarch agenda. If Putin starts to appoint local middle-class people to run United Russia in the Russian provinces, the small businessmen I talked about, with a seriously reformist and, in the end, anti-oligarch agenda or, in the end, does United Russia continue to be a vehicle for the present top elite? I am not sure on that one. I suppose I have to say that the latter is more likely but one cannot necessarily exclude the former at all, particularly, of course, if Putin does begin to have difficulties with his successor and other people in the apparat and actually genuinely needs mass middle-class support against some of his own former lieutenants. I do not know. I really cannot possibly give any firm predictions on that but that is the kind of thing I will be watching for in the years to come, to see if it happens or not. I would not say therefore, from that point of view, that by no means all the indications we have had out of Russia about future processes are as inherently negative as the Western media usually make out.
cannot be as leader of United Russia. I am sure that is one of the reasons why he is thinking about being leader of United Russia. The other problem if he takes the prime ministership is what I talked about, the migration of power between government institutions, because then obviously he tries to make the government, the Cabinet, more and more powerful and the presidency less powerful. Up to now the presidency has been all-powerful and the Cabinet has been an executive. That leads to clash after clash after clash on specific issues in ways that could unravel, frankly, even the closest of relationships, even the closest of friendships. If you find yourself fighting with someone on a daily basis over irritating and not small issues, involving huge amounts of money, the whole question of the direction of the whole infrastructure restoration programme, a figure which has been set at $1 trillion. You can have quite a number of battles over the distribution of $1 trillion if it comes down to a question whether it is the presidency or the Cabinet which distributes them, which is why it looks on balance probably, but not certainly, that it is United Russia that he will go for, and then come back as President in 2012—probably.

Chairman: Professor Lieven, thank you very much indeed. I think the Committee has very much enjoyed the style as well as the substance of the replies which you have been able to give us. We are going to Moscow in a couple of weeks’ time and we will certainly have benefited by the introduction you have given to us to quite a number of the current problems. We will be able to see them much more clearly because of that. Thank you very much again.
MONDAY 19 NOVEMBER 2007

Present Anderson of Swansea, L Chidgey, L
Crickhowell, L Truscott, L
Jones, L

Roper, L (Chairman)
Swinfen, L

Examination of Witness
Witness: SIR ANTHONY BRENTON, Her Majesty’s Ambassador, Moscow, examined.

Q207 Chairman: Ambassador, thank you very much indeed for coming and seeing us here. As you know, some members of the Committee will be coming to Moscow next month but we really felt it would be very useful, as you were here, to take evidence; we are taking a record, which we will not be doing when we are in Moscow. We will of course send you the transcript and you will be able to make any corrections that you wish to at that time. Thank you again for coming. You have obviously had a rather interesting period in Moscow over the last 18 months and we may want to comment on some of that as we go through. I wonder whether I could begin by asking a question whether you have any comment on Russian domestic politics in this pre-electoral period, pre two elections.

Sir Anthony Brenton: Before I answer your question, can I just say it is a great pleasure to be here. My diary is in a certain amount of flux but if I do find myself in Moscow when members of the Committee are also there, I am very keen to do what I can for you. Maybe you can come round for dinner or something. On your question about Russian domestic politics, we are obviously in a certain amount of flux at the moment. There have been a couple of recent surprises. The one thing that I can say is that we will be watching very carefully and we are very keen that Russia conducts its upcoming elections for the Duma on 2 December and then for the president some time next March in the free and fair way which it is committed to do under its obligations to the Council of Europe.

Q208 Lord Anderson of Swansea: Will you comment on the ODIHR decision. Clearly, on any objective analysis, the list headed by President Putin is going to win in any event so why not let people in to monitor? How can we best interpret the attempt to restrict the number of observers from the OSCE arm, ODIHR? What sort of message do they want to give?

Sir Anthony Brenton: I do not think I would want to delve into their minds particularly. We have put firmly on public record our disappointment that the ODIHR observers have not been able to get in because they have not been able to get visas. This is obviously very disappointing and it does raise questions about how the elections will be conducted.

Q209 Lord Anderson of Swansea: It does seem a rather crass position because, if they are going to do well in any event, why not let people in to monitor? What really are they hoping to promote by this proposal?

Sir Anthony Brenton: I think the important point here, without delving into their minds, is that their constitution commits them to a democratic way of government. They are committed by international obligations to the Council of Europe.

Q210 Lord Anderson of Swansea: Can I ask a related question and that is the Mafra Summit and the proposal of President Putin for what he calls a Russian European Institute for Freedom and Democracy. At first sight, this does not wholly accord with the restrictions on monitors in the elections. Again, if I might ask you to look into the mind of the Russian President, what really are they hoping to promote by this proposal?

Sir Anthony Brenton: I think the important point here, without delving into their minds, is that their constitution commits them to a democratic way of government. They are committed by international obligations to the Council of Europe to a democratic way of government. It is our business, the UK and the EU, to do everything we can to hold them to those commitments, and your visit, if you personally are coming in a few weeks’ time, the continuing attention from Western political figures, particularly in the run-up to the current elections, is a very important way to maintain that pressure.
Q211 Lord Anderson of Swansea: That said, what do they hope to achieve by the proposal which is not achieved by the Council of Europe, OSCE and so on?  
Sir Anthony Brenton: I do not think the details of the proposal have been made clear but, as it was explained to me, the idea is—and this is a legitimate Russian concern—that attention to the proprieties of how democracy works, which we have focused very heavily on in Russia, should also be extended to other countries in the European area. The idea was that this institute would operate in all directions.

Q212 Lord Anderson of Swansea: If they do not allow a sufficient number of monitors to their own elections, how well placed are they to seek to monitor other elections? 
Sir Anthony Brenton: I agree that it does not feel entirely consistent.

Q213 Lord Truscott: If I may follow up, Lord Anderson mentioned the Mafra Summit. I think it is quite interesting what Putin said about his personal prospects—I do not know if you are able to comment on that—that he would not change the constitution, he would not alter the balance of power of the executive or change the powers of the presidency, which does not seem to leave a lot of room for manoeuvre if, as he also said, he wants to retain a role in political life in Russia. What you think is a possible role for President Putin’s future career?  
Sir Anthony Brenton: There are two important points here. One is that the Russian constitution is still a very young document. There is no doubt in my mind that the single best thing that President Putin can do to ensure the stability of Russia’s fledging political institutions is precisely to leave at the end of his second term, as he has repeatedly promised to do. If he actually delivers on that promise, that will be a major act on his part in support of Russian democracy and Russian stability. The second thing to say about this is that I think he is right to feel, having been, from the point of view of the ordinary Russian citizen, rather a good President of Russia over the last seven years, that he has things that he can continue to contribute to Russian governance going forward. He has advice that he can offer in the way that departing Prime Ministers can in the UK. I agree with you it is not entirely clear how he would do that, but Russia would lose if it lost President Putin’s advice.

Q214 Lord Swinfen: Is he able to come back as President after a short period of absence?  
Sir Anthony Brenton: Yes, he is. The constitution limits a president to two terms but if a successor were elected and then, for example, fell ill and there was an election, President Putin would be free to stand again.

Q215 Lord Crickhowell: You partly explained their attitude about this “What right has the rest of the world to lecture us, and so on, in these things when so much is going on in the rest of the world?” but you also said that we must continually apply the pressure. What is their reaction going to be if we apply this close and critical look at what is going on? How do they react to that? 
Sir Anthony Brenton: I think it depends which Russian you are dealing with. Their democratic institutions are still quite young, there is still an instinct in some officials’ minds to try and produce the results which they think authority wants, but there is also the instinct in a lot of people’s minds that they want a healthy, open, free, democratic system and they will welcome outside observation which will tend to produce that result.

Q216 Lord Truscott: On foreign policy, if I can ask you, Ambassador, what you see as Russia’s foreign policy objectives and do you see that to a certain extent it is trying to use Russia and the EU as a counterbalance to US power? Alongside that, what do you think are the main security issues facing Russia? There has been a lot of talk about their unhappiness with missile defence and wanting to change the Treaty on Conventional Forces in Europe, so combining those two? 
Sir Anthony Brenton: Looking at Russian foreign policy, we have to remember that Russia has gone through a period of what they regard as national humiliation. They have ceased to be a superpower, the Soviet Union has broken up, they are a significantly smaller, less rich, less influential country than they were at the collapse in 1991. I think one of their main aims and one of President Putin’s main aims is to recreate a strong, stable, successful Russia. That is what an awful lot of Russia’s foreign policy activity has been about. They are particularly concerned to maintain and to reinforce their influence in what they regard as their immediate neighbourhood in the near abroad, in places like Georgia, Ukraine and so on. In regard to their relations with the West, they retain a lot of the suspicions and concerns which are hangovers from the time when the West was in confrontation with Russia during the Cold War. They deeply dislike NATO, they deeply dislike what they see as Western attempts to encircle them and to weaken them in various ways. It is for that reason that they are very hostile in particular to the US plans to site ballistic missiles in Poland and in the Czech Republic. In pursuit of that dislike of Western encirclement, obviously they will carry forward their arguments in different countries in whatever ways they think will appeal in those countries, and there are some European countries which are more sympathetic to those arguments than others.
Q217 Lord Crickhowell: You say they aim to be a strong, stable, successful Russia. They are now, of course, immeasurably smaller than the Russia which was humiliated. They are not even very large in comparison with their neighbours, such as Turkey, in population terms and, what is more, they have a declining population. What do you think therefore in this smaller state Russia constitutes a successful Russia? They are no longer a great power in the sense that America is, a dominant power, but they clearly want to be a great power among the lesser powers. I am not at all clear what they would see as being a strong, stable and successful Russia.

Sir Anthony Brenton: I think you put it correctly. Obviously, they are not in the same league as the United States any more, although in some ways, particularly with regard to strategic nuclear power, they remain very comparable and a very serious global player—indeed, one of the two serious global players—and they see themselves, rightly, as negotiating on that subject with the United States in a position of more or less equality. Apart from that, I think they are looking for a similar level of global influence perhaps to that which we exercise, although in different ways. They are a permanent member of the Security Council, they have significant friends and allies around the world whom they view as particularly attached to them in one way or another. They have one huge trump which we do not have, which is that they are now a very major energy exporter, oil and gas exporter. On the other hand, they are weaker than us in other ways: we have a huge financial sector, which they do not yet have. They see themselves, I think, playing a role of comparable weight perhaps to that of second-ranked powers such as ourselves.

Q218 Lord Chidgey: I am trying to judge how successfully Russia can restore its influence and control beyond its borders. I would like to qualify that concept by saying what does Russia really perceive its sphere of influence to be? If we go back to Soviet times, when Russia was a key, major player in terms of influencing other continents, for example, the classic case of vying for influence with the USA and China, where does Russia see itself in regard to the importance of trying to restore influence in those major continents and major players compared to yesteryear?

Sir Anthony Brenton: First and foremost, of course, they see themselves as having special interests and concerns in their near abroad, in countries like Ukraine and Georgia and so on. Beyond that, they see themselves as having expertise and skills and strengths to bring to key international problems, a conspicuous one being the problem of the Iran’s search for nuclear weapons, where they have been a member of the core group of countries which have tried to address that issue, and on major issues of European security, such as Kosovo independence, where again, they see themselves—they are—one of the core group of countries which have been in negotiation over how that process may or may not go forward.

Q219 Lord Chidgey: Can I ask a supplementary on that? Can I compare again with the days of the Soviet empire, when literally thousands of young people were given free education in University in Russia as part of the wider influence of Russia’s aims. Has that now completely finished? Is it at a lower level? I am thinking of the wider influence, the soft power as well as the hard power.

Sir Anthony Brenton: I am not an expert in this area but my instinct is that most of that has stopped simply because they have been through a period where they have not had any money but they are edging back also to concerns with soft power, with cultural power, with spreading the language and spreading Russian culture. Notably, here in London there is now a Pushkin Festival every year. They are re-engaging on that sort of agenda as well.

Q220 Lord Chidgey: What does Russia see as a threat to restoring their sphere of influence, of being successful in doing that?

Sir Anthony Brenton: As I have said, they are very suspicious of what they see as Western attempts to undermine them and weaken them. There is a very strong current of opinion, not only in Russia as a whole but in the Russian administration, that the West took advantage of Russia when it was weak and wants to continue to do so, and therefore that the West works to undermine Russian positions in places where Russia has an entirely legitimate interest, such as in Ukraine and in Georgia.

Q221 Lord Anderson of Swansea: Some critics with great hyperbole in the Sixties and Seventies talked of the Soviet Union as a Third World power with nuclear weapons. Now we understand that at a government-inspired seminar in St Petersburg in the summer they talked of their ambition of becoming one of the top five economies in the world by 2020. Is this a pipedream? Is it feasible?

Sir Anthony Brenton: No, it is not a pipedream. Their economy has been growing at about 7% a year over at least the last six years, and this is not only oil and gas revenues but the economy is growing across the board, nor is it only concentrated in Moscow. When you come you will see that Moscow is now a boom town, one of the most expensive, fastest-growing, most dynamic economic centres, certainly in Europe and, arguably, in the world. It extends well beyond
Moscow now, to places like St Petersburg, Yekaterinburg, out East. As I say, it is not just oil and gas but they are growing both in their general minerals extraction, in terms of industrial production and in all sorts of ways. On present economic policies, if they can maintain a rather sensible approach, there is every prospect of our dealing with an economically much more significant Russia in a decade and then in another decade after that.

Q222 Lord Anderson of Swansea: But in the top five?

Sir Anthony Brenton: I would not like to predict. There are so many imponderables there, including who else might be in the top five.

Q223 Lord Anderson of Swansea: Is it still a fairly unbalanced economy?

Sir Anthony Brenton: It is very unbalanced at the moment. It is too much concentrated on oil and gas extraction and on minerals extraction but they are as aware of that problem as anyone. This is a highly educated people, a highly technologically competent people, a people who are very capable of carrying themselves forward with the right policies in other areas than purely mineral extraction.

Q224 Lord Crickhowell: Going back to the comment I made earlier about the population problem, at the moment, in order to sustain growth, they need a growing working population but they have in fact got a tiny working population, and the oil and gas which you referred to at the moment is a big problem area for them because they cannot even supply their own domestic market. They have two major fields which are beginning to see the end, they need to find a way of developing their oil and gas, yet they have an economic policy that they require a considerable technological input to develop with the West and Western investment? You express rather greater confidence than some of our witnesses in their ability to maintain this growth factor into the top league. Clearly, they will overcome a lot of their problems but you seem to be rather more optimistic, I think, than some who have identified some of the problems they face.

Sir Anthony Brenton: On the demography side, I do think this problem is overstated. Certainly their population has been falling catastrophically and certainly it will continue to fall for some time yet. It is very striking: I served in Russia between 1994 and 1998 and the one thing you never saw then were babies in prams in parks. Now you do. The other thing which has changed is, of course, their openness to immigration. They have recognized that they have a democratic demographic problem and key skills they are willing to let in, and of course, there are a lot of people out in the former Soviet Union who are keen to get back to Russia to contribute to their growth. There is a problem there but I do not think it is anything like as catastrophic as some people like to assert. On the oil and gas, yes, they do have problems. As you say, they are running into domestic shortages. This is due to the fact that they have not done any serious exploration for the last couple of decades and are living off the proceeds of the exploration period which took place before that. That said, I was very struck by a remark made to me by Lord Brown, the former chairman of BP, who said in effect Russia, eastern Siberia, remains the single large unexplored hydrocarbons province now in the world. If there is any of this stuff to be found anywhere, it is out there and they are pretty confident that it is there. Yes, it is going to take lots of technology; yes, it is going to take fantastic amounts of money; but just from that single remark, from more than that single remark, I conclude that, if they get their policies right, they have very rich prospects in that area.

Q225 Lord Swinfen: Leaving aside oil and gas, are they exporting raw materials or are they exporting finished goods rather than raw materials?

Sir Anthony Brenton: I have not studied their export figures very closely but they obviously have large exports still of things like nickel, iron ore and so on, of which they have a large production. Do you call aluminium a raw material, which of course it is not, or do you call it a finished good? It is the product of an industrial process and they are the world’s largest producer of aluminium now.

Q226 Lord Swinfen: That is a fair point. Bauxite originally. They also have massive reserves resources in the way of timber.

Sir Anthony Brenton: Yes, that is absolutely right. It is extraordinary how inefficient Communism was. The scope simply with the present economy to produce things better and to generate the sort of economic growth that we have been talking about remains huge. A story which I do not want to bore you with but I think it is a rather good story, which I regularly tell in speeches that I give about Russian economic prospects. I have a friend who, in the way of ambassadorial friends, owns a forest out in Siberia, near the Chinese border. This is a working forest; they cut down the trees and sell them to the Chinese for construction purposes. When he took over this forest, which was doing very badly, he looked into the books and he discovered that one reason why it was doing very badly was because of its transport fleet. He had this fleet of trucks which were using amazing amounts of gasoline for no obvious purpose, the drivers kept on falling sick, spare parts
kept on going missing and so on. He called all the drivers together and said, “Guys, I give you your trucks. You are now subcontractors to me; you own the machine you drive.” Instantly, of course, the breakdown rate of the trucks fell close to zero, the sickness rates of the drivers fell close to zero, the disappearance of spare parts fell close to zero and he suddenly had a very profitable transport operation. The scope to do that all over Russia remains huge as it makes the transition out of Communism, and that is where a lot of the growth is coming from.

Q227 Lord Truscott: Of course, it is widely acknowledged that the Russian economy is, relatively inefficient but can that not be overstated to a certain extent? On the one hand Russia is already 20 in the world in terms of the size of its economy, Gazprom is already the sixth largest company in the world, and they have something like the fourth-largest gold and currency reserves in the world. Do you think, whilst it is relatively inefficient, you can overstate the inefficiency of the Russian Federation? Sir Anthony Brenton: Yes. Two points arise here. First of all, Russian bureaucracy is horrendous. The corruption constraints, which add huge additions to industrial costs, remain very high. You can see, as you deal with Russian operations, just how backward, in a way, they are. They operate like British industry used to operate 10 or 20 years ago. But these are bright guys running these things at the top now and they are very internationally oriented and they are keen to make themselves internationally competitive and respectable and, as they do so, so Russia’s economy will grow stronger.

Q228 Lord Jones: Regarding Russia’s relationships with the nations on the periphery, on which you have briefly touched, do you think Russia’s policy is going to lead to difficult relations with the EU with regard to how the EU approaches the periphery? Is there scope for problems there? Sir Anthony Brenton: I think there already are problems. It depends who you are counting in but, of course, a number of EU Member States to sit on the periphery of Russia and do not have perfect relations with Russia. With Poland there is a sort of ancestral tension there which has been imported wholesale into the EU’s general relations with Russia through the fact that Poland is now holding up the Partnership and Co-operation Agreement negotiation. Estonia had a very difficult passage with the Russians earlier this year because they chose to move a war memorial from one part of Tallinn to another. These are not external difficulties for the EU; they are very much part of the EU’s overall relations with Russia.

Q229 Chairman: Would you perhaps like to say something about the countries which are on Russia’s periphery like Ukraine, Georgia and Central Asia, and how far the EU’s policy towards these countries would perhaps lead us into disagreements with Moscow? Sir Anthony Brenton: It varies from case to case, of course. Ukraine is the biggest and most important case, without doubt, and I am a very firm advocate of the EU moving as fast and as clearly as it can to getting a very close relationship with Ukraine—not because that disadvantages Russia particularly. Indeed, President Putin is on record as having said he would not oppose Ukrainian membership of the EU—but because the surest way of giving Ukraine the economic boost and the self-confidence to get over its own internal difficulties and to stabilise the democratic system, which is still developing there, is precisely to draw it into the EU embrace in exactly the same way as we did with Estonia, Latvia, Lithuania, the Czech Republic and so on. Georgia similarly, although Georgia is a little bit further back down the development track, and Georgia is a sensitive and complicated case for a number of other reasons, because there are these enclaves in Georgia which Russia is helping to protect from forcible reincorporation into Georgia. There is no doubt that they do not want to rejoin Georgia. But again, part of the answer to Georgian-Russian tensions is for Georgia itself to become a prosperous, successful nation, without a lot of the hang-ups which currently preoccupy its relationship with Russia and to the extent that the EU opening its doors and helping Georgia to develop economically, we will help that process. Going further east, as you look at Uzbekistan and the “stans”, there are major problems there of governance, apart from anything else, but I do think it is important that the EU stand firm in its view on governance. With regard to Uzbekistan, for example, where there was an appalling massacre a couple of years ago, I think it is important for the prospects of development there that we be very clear on maintaining our democratic values.

Q230 Lord Anderson of Swansea: What is it that they expect from countries like Ukraine and Georgia? Is it respect? Is it some form of political suzerainty, or at least a readiness to look to Russia for leadership, or is it a degree of economic dependence? Sir Anthony Brenton: They rightly say they have historic links with these countries, there are a lot of Russians living in them, there are a lot of real Russian economic interests there. They are in no doubt that they are now independent countries. There is no move at all towards trying to reincorporate them in some form into the Russian empire, but there is a feeling that they have legitimate interests there which
they want to see respected and taken into account as those countries themselves develop.

Q231 Lord Swinfen: Is Ukraine still the bread basket of Russia?

Sir Anthony Brenton: I do not think so. I am not an expert on where they are getting their food from. What is surprising is that Russia is not the bread basket of Russia. If there is one bit of the Russian economy which really does need to develop or redevelop, it is agriculture, the black earth; they have some of the richest farmland in Europe which is scandalously underused at the moment.

Q232 Lord Anderson of Swansea: How fraught are the current bilateral relations between the UK and Russia? You have had an interesting time yourself, including the Litvinenko affair. Does that still rumble on?

Sir Anthony Brenton: As I talk about bilateral affairs, I think it is quite important to distinguish between the economic relationship and the political relationship because the economic relationship remains very strong and very positive. Our exports are rising by about 20% a year, in last year’s figures we were the largest investor into Russia in various sectors, the economic links are strong and growing stronger—Russian industry looks to the City of London, for example, for all of its financial services. I am going to invent this number but I think it is approximately right: something like 40% of the City of London’s IPO activity last year was Russian. So there is a very strong mutual dependence in the economic relationship which neither side has any interest in undoing. The political relationship is undoubtedly very difficult at the moment and the two key reasons for that are the presence of Boris Berezovsky here in London who the Russian regime would very dearly like to get back and try in Russia, and the murder of Litvinenko here in London, which, as you all know, was an appalling murder which endangered a lot of other people as well. We have identified a suspect for that crime, Mr Lugovoi, we have sought extradition, which has been refused, and we have exhibited our dissatisfaction with that conclusion with the expulsions and the other measures we took in July. That affair remains alive and we still remain very keen to extradite Mr Lugovoi but, in pursuing that, we also recognize that there is a lot of serious international business which it is important that we be able to speak to each other about. I have mentioned Iran. I have mentioned Kosovo. Climate change is another example of a subject where Russia has a major role to play, where we need to be talking to them. I think ministers are inclined to divide the subject matter. Yes, Litvinenko remains a real problem for us. We cannot have British citizens murdered on British streets in the way that happened in that case, but Russia is a big, central country in the international system and we need to do business with them on a lot of other issues as well.

Q233 Lord Anderson of Swansea: Ambassador, the British Council. I see that at the Mafra EU-Russia Summit on October 26 the Commission supported the UK about the difficulties faced by the British Council in Russia, pressed Russia to conclude cultural centres agreements which formalised the status of organisations like the British Council quickly, routinely, and without reference to wider issues. What is the current position on the British Council and how likely is there to be some agreement without the Russians trying to get a quid pro quo?

Sir Anthony Brenton: The current position on the British Council is that they are under pressure. The Russians do not like, in particular, their activities in the Russian provinces and are pressing us in effect to close the British Council down other than in Moscow.

Q234 Lord Anderson of Swansea: And in St Petersburg?

Sir Anthony Brenton: No, they are also pressing the British Council to close that. The British Council had a regional network which was locally staffed, which in any case they have now handed over to local owners because that is part of their worldwide policy, to spend money on projects rather than people. They still have three offices in Russia, in Yekaterinburg, Moscow and St Petersburg, and the Russians are pressing them to get out of Yekaterinburg and St Petersburg. As you have said, at Mafra, and indeed separately, we have pointed out to the Russians that under the Vienna Convention on Diplomatic Relations we have a right to pursue cultural activities from our diplomatic representations, which we have in Yekaterinburg, St Petersburg and Moscow, and under a 1964 agreement between ourselves and the Russians the British Council is our agent for that activity. So, in our view, what the British Council is up to is right. It is actually good for Russia. They have trained something like 200,000 English speakers in Russia, to take one rather small example of the things they are doing. It is right and is legally justified and we have been very clear with them that we would take a pretty dim view of any serious attempt to pursue their efforts to close down the British Council in Yekaterinburg and St Petersburg.

Q235 Lord Anderson of Swansea: What are the obstacles to the cultural centres agreement?

Sir Anthony Brenton: For the moment they have frozen the negotiation of the cultural centres agreement in response to our freezing the negotiation on the visa facilitation agreement, which was one of the measures we took post Litvinenko but, in any
case, it was moving very slowly and the reason we think it was moving very slowly was precisely because of Russian discomfort with British Council activity.

Q236 Lord Swinen: What are the activities to which the Russians are actually objecting?
Sir Anthony Brenton: They have not been specific. They just do not like the British Council.

Q237 Lord Truscott: I understand one option would be for the British Council to withdraw to operate from the British Embassy and the British consulates in Russia. What would you think of that?
Sir Anthony Brenton: We are making every effort to keep the British Council operating at the maximum possible extent in Russia. If that requires them to operate out of my embassy, then my embassy will open its doors to them.

Q238 Lord Chidgey: Ambassador, you mentioned a moment ago that in the course of time the British Council have trained 200,000 English speakers. Sir Anthony Brenton: Yes, I need to be careful. I made that number up but a lot, hundreds of thousands.

Q239 Lord Chidgey: What I want to ask you about is that I understand the British Council have trained a good number of teachers of English. Could you tell us whether this has been a problem perceived by the Russians in terms of the influence that teachers trained by the British Council as English teachers might have an ulterior motive or another agenda in terms of teaching in Russian schools or further education or whatever? Is there an issue there?
Sir Anthony Brenton: I would be surprised. There is certainly a narrow, nationalistic stream running in Russia which resents foreign languages and foreign links but that is actually very much a minority view. The sensible people who are running Russia at all levels know that Russia’s future lies as an integrated component of the world economy and they know too that one of the key skills to doing that is having lots of people who speak English. So the sensible people in the system have appreciated and continue to deeply appreciate the work the British Council is doing helping Russians to acquire that skill.

Q240 Lord Swinen: Do the Russians have the equivalent of the British Council here or elsewhere in Europe?
Sir Anthony Brenton: They have one man in their embassy here doing cultural work and they are thinking about expanding that operation. I am afraid I do not know what they have elsewhere in Europe.
Chairman: I think we should perhaps move on to the main area, which is of course relations with the European Union.

Q241 Lord Crickhowell: We are a European Sub-Committee so I would like to ask you now how you think Russia sees Europe, how it regards doing business with Europe as Europe, and how that has changed perhaps as things have developed.
Sir Anthony Brenton: First of all, Russia thinks of itself as being part of Europe—not of the European Union but it thinks of itself essentially as a European country, sharing European values and part of European civilisation. That characterises quite a lot of their relationship both with the EU and with individual Member States. With regard to its relationship with the EU as an entity, they essentially view it as an economic entity. They have very little dealing with it on the political side. You have recorded in the list of questions you sent me the various documents which have been produced in the course of trying to develop that relationship, the latest of which is the Partnership and Co-operation Agreement, the renegotiation of which is hanging fire at the moment until the Polish problem is sorted out. What more can I say? I think they still take dealing with national governments quite significantly more seriously than they take dealing with the European Union as a whole and I think they were quite shocked, for example, by the draft Energy Directive which the Commission produced a few weeks ago, because that, if it were adopted in anything like the form in which it has come out of the Commission, would have very significant implications for Russian interests. It is that sort of event which brings home to them the potential significance of the EU qua EU for them. Most concrete, day-to-day business tends to be done with the Member States.

Q242 Lord Crickhowell: Some have said that they started off by wanting to deal with the EU in the sense of wanting to deal with a single person, a single office, someone they can go confidently to, and they were rather shocked to discover that they could not do that but saw a great opportunity to exploit the differences and play off the European countries one against the other.
Sir Anthony Brenton: I would not have put the sequence quite like that. In areas—and there are a lot of them—where Russian interests differ from the EU, then, like every other country actually, they will look for friends within the EU who will help to represent them and look after their interests. Particularly on the energy front, that has been very much their tactic.

Q243 Lord Crickhowell: You refer to the energy front. Interestingly, you previously referred to the climate change front and said that Russia has a major role to play. Although we are about to debate the Climate Change Bill in this House next week and Britain likes to say that we are taking the lead on these matters, in a real sense, in the whole of the
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environmental world, Europe is going to be more important on climate change, and European policy is probably more important than British policy on its own. Therefore I would be very interested if you could elaborate a little on that remark you made earlier, that Russia has a major role to play. How do you see them playing that role, particularly in relation to Europe?

Sir Anthony Brenton: Russia is, I think I am right in saying, the third largest national emitter of carbon dioxide in the world, a major source of hydrocarbon exports and hydrocarbon suppliers and they own a seventh of the world's surface, including a lot of tundra and other potential areas which are potentially important from a climate change point of view. So obviously, if the world is to have successful negotiations, as we all hope, in getting climate change under control, then getting Russia on board will be a very important part of those negotiations. I have to say we have not actually been very good at that so far, either the UK or the EU as a whole. The Russians are difficult on this subject. Their scientists are not entirely convinced. There is a stream of opinion in Russian business circles that while they are doing so well out of oil and gas a global regime which limits demand for oil and gas is probably not going to be a very good thing for Russia, and Russia is a large, cold country where there is another stream of opinion that actually, a rather warmer world would be a good place from Russia's point of view. So there are all sorts of complications there. It seems to me, in a sense, precisely because there are all those complications there, precisely because we do not see eye to eye on this, there is a very strong argument for the EU and for the UK to engage seriously with Russia on this subject.

Q244 Lord Swinfen: What do you think should be the fundamental objectives of EU policy with regard to Russia and what does the EU have to offer Russia in the context of the negotiations? How can it best influence Russian thinking?

Sir Anthony Brenton: I think the fundamental objectives of the EU with regard to Russia need to be twofold. Firstly, to continue to expand the fast-expanding in any case economic links, human links, social links, investment links, trade links. Finally, if Russia is to become a normal European country—and I am confident it will—that is going to happen through a sort of osmosis, through a sort of feeling that they are inside, through a sort of feeling that they are a member of the club. That is the first thing. The second thing that I think it is very important the EU continues to do is to plug away on the democracy/human rights front. Obviously, there are imperfections there in Russia. Obviously, they do not yet entirely meet European standards. There are good ways and bad ways of making that point to the Russians but to continue to make our interest and concern clear is a way of bolstering the best elements in Russian society, is a way of encouraging the sorts of developments that we want to see and, as I said earlier, the Russians see themselves as part of Europe, see themselves as carriers of European standards and, if there is an area where they see themselves as being badly out of line with contemporary European performance—and human rights is arguably one of them—it is an embarrassment and an encouragement to them for that fact to be drawn to their attention.

Q245 Lord Chidgey: Is there not a contradiction here in the philosophical approach of Russia to Europe? On the one hand, we all understand that Russia sees itself as more European than anything else, yet the more European Russia becomes, the less and less it can claim to be a great power because the whole concept of being closer to the EU is being part of the family rather than being one above the family. That may sound fairly trite in our conversation but, as I understand the way the Russians look at things, this could be a very important factor.

Sir Anthony Brenton: Again, two points. Firstly, Russia’s awareness of itself as a great power is obviously a major impediment to them taking on the constraints of sovereignty which would be involved in actually joining the EU but I do not see it as any obstacle to them getting closer to the EU. If I could add a personal point, I believe I work for the government of something like a great power which nevertheless manages also to be a member of the EU.

Q246 Lord Anderson of Swansea: There are areas of policy outwith national governance and within the competence of the European Union, notably trade policy. To what extent is Russia prepared to modify its own legal systems to provide, for example, greater protection for minority shareholders and so on as a result of pressure from the EU, acting on behalf of national governments as a whole?

Sir Anthony Brenton: I think the answer to that is that there is some willingness; it is slow and it is difficult but there is a willingness in the Russian systems to move towards not just EU but Western standards. The best example of that actually is Russian moves towards joining the World Trade Organisation, which have been slow, difficult, subject to reversals. We are not there yet but there is no doubt in my mind that certainly the economic establishment in Moscow and a very substantial proportion of the business community—not all of it—are pushing Russia more and more to take on the sorts of standards which will make Russian business circumstances compatible with and comfortable for Western businesses and business circumstances. There is another extra motivation in all this, which is that big Russian
businesses now want to become international themselves, they want to invest in the UK, in America, in other parts of the EU, and they know that in order to do that, they have to meet international standards not only overseas but at home as well. So I think it is difficult but I think there is a willingness to move under pressure and under persuasion.

**Q247 Lord Anderson of Swansea:** That includes resolution of commercial conflicts through arbitration outside?

**Sir Anthony Brenton:** Yes, I hope so. One of the things that we in the UK have been very keen to pursue through the next iteration of the Partnership and Co-operation Agreement is precisely proper protection for investors in Russia through proper arbitration and rule-enforcing procedures. That is in our mandate and I do not see that as an unrealistic thing to aim for as we take the negotiation forward.

**Q248 Lord Anderson of Swansea:** Do we, as part of our policy either bilaterally or with the EU, provide any training in those legal norms to provide a greater coverage of the rule of law commercially?

**Sir Anthony Brenton:** I am at the moment getting together some legal firms in Russia, British legal firms, all of which have large offices now in Moscow, precisely to try and set up a scheme of financing young Russian lawyers to come to the UK and get some of our practice. This is not purely from a business point of view; I want them also to understand how a real legal system works from other points of view, notably protection of human rights and so on. That is not a new scheme. That is our attempt and there are other schemes like it.

**Q249 Lord Anderson of Swansea:** Solely on the commercial side, not on the human rights?

**Sir Anthony Brenton:** No, we anticipate it having the two effects. It is very good to get these guys through British law firms and through London because that gives them a disposition towards using us and using our legal norms on the business side, but also it helps them to understand how we operate on the criminal side and the rule of law side, which is an important lesson, I think, for the Russian system to absorb.

**Q250 Chairman:** Just on the question of the WTO negotiations, interestingly, in the letter we have had about the meeting in Mafra, apparently Mr Putin said that while he called accession to WTO a natural process, he said Russia would choose to join only if the conditions for accession met Russia’s national interests, which suggests perhaps a slowing down of his enthusiasm for the WTO.

**Sir Anthony Brenton:** I do not think there is anything new there. I think that has always been Russia’s position and I am sure it has been the position of every other country that has joined the WTO.

**Q251 Chairman:** It suggests that we have not necessarily got very much leverage as far as the WTO membership is concerned.

**Sir Anthony Brenton:** We have the leverage which is given by the lobbies in Moscow, which includes the Finance Minister, which includes the Economics Minister, which includes the leading businessmen who want Russia to be inside the tent, who see the advantages for them, not least in terms of persuading the Russian system to become more transparent in its internal workings, of Russia joining the WTO.

**Q252 Chairman:** You mentioned earlier the institutional framework for EU-Russian relations based on the Partnership and Co-operation Agreement, which is coming to an end, the so-called “four common spaces” and also the Northern Dimension. How far do you think they are working well? Do you think there should be changes in the institutional relationships as we look forward to a new agreement?

**Sir Anthony Brenton:** I do not think they are working very well. My impression is that what the EU has accumulated with Russia—and I do not think this is a unique situation—is an awful lot of written-down aspirations with rather little real, material content. I think the important dynamic thing that is happening in EU-Russian relations is not being done by bureaucrats and ministers; it is being done by ordinary businessmen and ordinary people who are more and more travelling, more and more trading, more and more investing and, as they create the close links, I think the agreements will follow. One very important agreement, on the basis of the huge investments we now have, is a decent agreement to protect our investments in Russia.

**Q253 Lord Crickhowell:** We have already in a number of ways begun to touch on the whole question of European solidarity, or lack of it. We have talked about the new peripheral members, who have sometimes rather different attitudes to the old EU members. You have begun to refer to energy, although we may be developing an energy policy, there are profound differences between, for example, German policy and that of some other countries. Would you comment more about the need for European solidarity and how you think perhaps Europe should set about the game?

**Sir Anthony Brenton:** Yes. There has undoubtedly been a problem with EU solidarity and, in particular, a wide range of views with regard to political
developments in Russia. Some EU Member States have been inclined to give Russia a much more tolerant approach with regard to the problems that Russian democracy is having, with regard to the problems of human rights in Russia, than others. Charles Grant's outfit have just produced a report which sets out a typology of different European state attitudes.

Q254 Chairman: Mark Leonard's outfit, I think. 
Sir Anthony Brenton: It is Mark Leonard. That is right. It is a rather good report, which I commend to the Committee's attention. The way he typifies various Member State attitudes to Russia, he gets it pretty close to right, and that disparity of views has undoubtedly been a huge complication for the EU in reacting to developments in Russia. That said, I think things are getting better actually. With the changes of President in France and of Chancellor in Germany, it has been quite striking that the EU are much less widely dispersed on human rights developments in Russia now than they were when I first came into this job three years ago. It was very striking to me that, when Poland blocked the progress of the PCA negotiation, what you would have expected three years ago would have been some key, large Member States ganging up on the Poles to get out of the way, and that did not happen. There was much more sympathy to the Poles' concern in the EU of 27 states that we have now than there would have been three years ago. I think that convergence is important because, obviously, the more the EU can speak with one voice, the more that voice will be heard in Russia.

Q255 Lord Anderson of Swansea: Is it perhaps naïve to have a 27 musketeers' approach of one for all and all for one? Certainly that was seen in respect of the support to little Estonia when Russia tried to bully it. I think there was less readiness to support Poland when it was felt that the Polish government was exaggerating. Has there been a noticeable warming of relationships after the elections in Poland?
Sir Anthony Brenton: The elections in Poland have only just reached their conclusion. I think there are hopes that that will make things easier. Estonia, again, was a very interesting example because the actions that the Russian authorities took against the Estonians were indefensible. I went and called on the Estonian ambassador when she was besieged by youths shouting abuse and throwing things at her residence. It was really indefensible what was done there.

Q256 Lord Anderson of Swansea: There were some attacks which were clearly officially agreed.
Sir Anthony Brenton: Indeed. It seems to me that the fact that the EU, which, again, three years ago would have been much less able in a unified way to have come out in support of Estonia, did do so, is a very good sign of growing EU convergence on these points.

Q257 Lord Anderson of Swansea: Are there other signs of that nature? Certainly from the EU point of view it is rather good that Chancellor Schroeder is no longer there and Chancellor Merkel has taken a rather more hard-nosed position in respect of Russia. 
Sir Anthony Brenton: I could not possibly comment on that, of course, but I think a key upcoming test is going to be the Energy Directive because that is something that the Russians are genuinely interested in. We, the EU, have a very strong interest in being able to negotiate jointly with Russia over energy issues. Russia has become able, because of differences of national interest, because of differences of general political approach to Russia, to deal with the EU states separately on this absolutely crucial issue in our future relations, and for the EU to come together and to establish joint terms, for example, on the conditions in which Gazprom will be able to invest in Europe seems to me to be very important for the future.

Q258 Chairman: Kosovo will presumably be a rather difficult problem both for the EU and Russia in the next few months.
Sir Anthony Brenton: I think Kosovo is going to be very difficult.

Q259 Lord Anderson of Swansea: If I can pick up on Kosovo, some commentators have talked about some grand compact, of Russia trading views on frozen conflicts with a move on Kosovo. Is there anything that you are aware of, or is it still something on which Russia is not moving at all?
Sir Anthony Brenton: I have not seen anything of that sort in the negotiations to which I have been privy, nor have I seen Russia move at all on the issue of Kosovo, where their position is that, unless Serbia agrees, Kosovo cannot become independent.

Q260 Lord Anderson of Swansea: How do you define Russia's national interests in respect of Kosovo?
Sir Anthony Brenton: They have a very strong interest in international stability, and that goes back a long, long way. Part of that interest expresses itself therefore in countries, bits of countries, not becoming independent without the strongest possible international justification, i.e. a Security Council resolution. They also have concerns because they are in effect the protectors of two small bits of Georgia, South Ossetia and Abkhazia, which themselves have
aspirations to independence and which they see as potentially causing problems for them if Kosovo becomes independent.

Q261 Lord Truscott: Back to energy, there was talk of Russia using energy as a political weapon. Do you agree with that concept? Secondly, we have not mentioned China, which is particularly relevant in the energy context. How far do you think bilateral relations between China and Russia are based on energy interests? Thirdly, which you have partly mentioned, how should the EU respond to Russia in terms of ensuring security of supply and all the rest? Do you think—and you did mention this earlier but I would like you to expand on it—that the proposed Energy Directive, which some people have said is potentially protectionist, is the right way to go?

Sir Anthony Brenton: On the energy weapon, a lot of this started, of course, when they turned off the gas to Ukraine coming up for two years ago and I think the charges there were probably exaggerated. They were having an immensely difficult negotiation, they could not reach conclusion by the deadline, and so they turned off the gas. I saw President Putin and others extremely hurt at the charge that they had done this for political reasons. That said, we have seen them use energy supply in relation to political concerns, notably when the trains carrying oil to Estonia stopped running at the height of that crisis. There is no doubt in my mind that in extreme political circumstances this could happen, and therefore this leads to what I have already said about the Energy Directive: I think we need to make sure that we, being the EU, insure ourselves against that risk and the best insurance that I can see, given that inevitably we are going to be very large consumers of Russian gas, is unity, is the EU being able to react as one should we be confronted with that situation. That is the point about the Energy Directive. Of course we do not support protectionism. One of the other things I keep on saying in my speeches around Russia is that we have the most open economy in Europe and that accounts for our very fast growth and our success, and we do not want to limit that. But, for me, we need to build the right political protections in there in case we got into a crisis where the Russians were tempted to use the energy weapon. On China, obviously, the Russians are very conscious of this giant growing up—not to their east; there are bits of Russia which are east of China—to their south-east. They have worked rather hard to develop their relations with China. They have in particular invented a thing called the Shanghai Co-operation Organisation where they work together, they have joint military exercises; they take a less democratically orientated view of international affairs and we do. I think they are very keen to build a close economic relationship, to make sure that there is no real security threat to themselves down there and to work with the Chinese where they can, as they do very frequently in the Security Council.

Q262 Lord Swinfen: Is there much in the way of immigration from China into Russia along that long border?

Sir Anthony Brenton: Yes, there are a large number of Chinese working in Russia, both legally and illegally, and obviously, part of what is at the back of certain Russian policymakers’ minds is an awareness that there is this huge China, full of people, right next to a very empty part of Russia and there are lurking security concerns there—not for now but for perhaps decades down the track. I think probably one of Putin’s historic achievements was to finally agree on the border with China, which he did two and a half years ago, and I think that is a concern at the back of some Russians’ minds.

Q263 Lord Swinfen: Are there sufficient jobs to absorb the Chinese across the border?

Sir Anthony Brenton: I do not think they would cross if they could not get jobs, would they?

Q264 Lord Swinfen: I doubt it but if the land is open . . .

Sir Anthony Brenton: No, there is employment. It is not the most prosperous part of Russia, strangely. You have this bit of Russia which is sitting on the booming Pacific coast which, because of problems with its governance, is just distanced from the metropolis. There are still huge development possibilities there which have not yet been grasped.

Q265 Lord Anderson of Swansea: There is still only a fairly embryonic counter-terrorism element within the European Union but there are clearly areas of common interest with Russian in respect of counter-terrorism. How are such relationships moving?

Sir Anthony Brenton: I am afraid I cannot speak for the European Union as a whole. We certainly work quite hard to build up our links with the Russians on counter-terrorism because they have had their own Islamic fundamentalist problem and there are undoubtedly links between the problem they have faced and the problems that we have faced. I have to say, one of the consequences of the Litvinenko affair has been a certain amount of damage to links between the agencies which normally deal with these things. We have been very clear with the Russians that if we, for example, get information of a real threat to them, which would involve danger to human life, then we would always provide them with information which would be relevant on that, and we would hope they would do the same for us
Q266 Lord Anderson of Swansea: Has it essentially been a one-way street so far?
Sir Anthony Brenton: I do not think so, but I need to be very careful what I say in this area. My understanding is there is a shared interest there, there is a shared competence there, it should be said, and there is scope for co-operation if we could get over the political difficulties we have at the moment.

Q267 Lord Swinfen: Is there co-operation on Afghanistan?
Sir Anthony Brenton: I know the Russians are essentially helpful on Afghanistan. For example, they give over-flying rights, and so on, to troops going in and out of Afghanistan. I do not think we fly in over Russia, but others who are active there certainly do. I know there is quite a lot of co-operation between Russia and NATO on that sort of front. I know also that on the anti-drug exercises in Afghanistan we have quite close links with the Russian authorities on that because they are a major transit route for Afghan drugs.

Q268 Chairman: It is interesting that there was a Memorandum of Understanding between the European Union and Russia signed on this exchange of information on drug abuse, so that was quite important. Ambassador, thank you very much indeed for coming this afternoon and having helped us a great deal in our inquiry. We will be continuing, both here, in Moscow and again in Brussels at the end of this week, to talk to people in the European Union. We are very grateful for your contribution to our inquiry this afternoon.
Sir Anthony Brenton: Thank you for giving me your time. If I am in Moscow, I look forward to seeing some of you out there.

Chairman: Thank you very much indeed.
THURSDAY 22 NOVEMBER 2007

Present Hamilton of Epsom, L
Hannay of Chiswick, L
Roper, L (Chairman)
Truscott, L

Examination of Witnesses

WITNESSES: MR ENÉKO LANDABURU, Director General of the Directorate-General for External Relations, MR GUNNAR WIEGAND, Head of Russia Unit and Acting Director, Eastern Europe, Southern Caucasus and Central Asia, MR PAUL VANDOREN, Deputy Head of the Delegation of the European Commission to Russia, MR FRÉDÉRIC MADURAUD, Co-ordinator of Trade and Economic Affairs, Russia Unit and MR LARS-GUNNAR WIGEMARK, Political Officer, Russia Unit, examined.

Q269 Chairman: Good afternoon, Mr Landaburu. Thank you very much for finding the time to give evidence to us today. I know you have a very busy afternoon, but you are going to be able to be with us for the first part of our time here and you are going to be accompanied by some of your colleagues. We are one of the Sub-Committees of the House of Lords European Union Committee which is responsible for looking at problems of external policy, defence and development. We are carrying out a thematic study on the European Union's relations with Russia. We have taken evidence in London from a number of people who know a good deal about Russia and we are going to Moscow in December where we are seeing people there who know about it, but we felt it was absolutely essential that while we were in Brussels we should be able to see people from both the Commission and the Council to talk about the way in which you saw the development of our relationships. I am here with three of my colleagues from the Committee. We would like to take our evidence formally and, therefore, we are taking a note of what is being said, but if at any stage you feel there is something you would rather say to us privately, please would you indicate that and speak off the record and we will then stop taking the note and that will not be published with the report of the meeting. We will be sending you a copy of the transcript in a few weeks' time for you to be able to make small corrections. We want to avoid any misunderstanding about what is on the record, and for us to be able to use formally in evidence, and what is not. Would you like me to begin, even though perhaps one or two of your colleagues are not yet here?

Mr Landaburu: Please.

Q270 Chairman: We would welcome your views as to what should be the fundamental objectives of European Union policy with regard to Russia, and in which areas do you feel relations between the European Union and Russia have made the most progress in recent years?

Mr Landaburu: Thank you very much indeed. First of all, I would like to welcome you to Brussels and to this Directorate General. We are very honoured to receive you. I would like to say that the subject of your inquiry is a really challenging, very topical and very important one. Speaking more generally, we highly appreciate your reports here in general. I am sure that we will read this one with interest when it is finalised. I know about the rules, that you are transcribing all of what we say, but maybe during this conversation I will give you some personal opinion and I would prefer to do that off the record, as you proposed to me. My colleagues are coming very shortly. It is the team dealing with Russia. Mr Gunnar Wiegand is the head of this unit and he is the Acting Director for Russia now. As I will have to leave you at some point, Mr Wiegand and other colleagues will remain at your disposal to continue the talks and the debate. We have also an information pack which you may find useful for your work. Before going to the specific questions, I would propose to make an opening statement, first of all, in a nutshell, on the main assessment we are doing as far as our links and relationships with Russia are concerned and then, of course, we will come to all the questions you raise and will try to answer them. Some of them are very, very precise and focused and difficult to answer, but we will try to do our best. If I had to define in a word the relationship we have with Russia, I would say that this relationship is complex and there are many reasons for that. The first is that Russia is a neighbour but, at the same time, it is a strategic partner. What does strategic partner mean? Strategic partner means that they are among our most important partners in the world. We have only eight strategic partners in the European Union: the United States, Canada, Japan, Korea, Russia and now China and Brazil. This means that with those kinds of countries we want not only to develop our relationship, to strengthen our co-operation, to deepen our links but, at the same time, we want to raise with them some horizontal issues at international level in order to try to be part of the solution to those big questions. I am referring to
climate change, energy, security, poverty, disease questions and these global issues, so Russia is one of these partners. The second reason why our relationship is complex is because we are still living with the consequences of what was in the past the Soviet Union. The enlargement process, which was very successful for the Union the last time, of course provoked some kind of reaction from Russia. We have to manage this kind of shock for them to now have in the European Union a process of sharing our values, our principles with a lot of countries that were under the control or the influence of the Soviet Union. More than that, some of them were inside the Soviet Union, the Baltic countries. This provoked a political and psychological difficulty which explains some of the difficulties we have in our relationships. Another reason why our relation is complex is that this country has changed a lot over the last few years, and we come from the economic and political changes in this country has changed a lot over the last few years, and we come from the economic and political catastrophe of Yeltsin to a new-found assertiveness on the crest of high energy prices. This is very different from where we were some years ago at the beginning of the mandate of President Putin and now and this, of course, has provoked some dramatic changes in our relations. Another general point I would like to outline is that there is a paradox in our relationship. Our trade and investment is booming. We have very strong energy interdependence. European businesses are rushing to the Russian door and there are huge profits made in the Russian market. I had a meeting yesterday with some representatives of our European firms in Russia and despite a lot of difficulties, of course, they are making a lot of money and are doing a lot of business. This is a trend which is booming but, at the same time, we are going to have more and more difficulties with our relationship and dialogue at a political level. This is the paradox of where we are. What are the difficulties? First of all, of course, in expressing our concern on the implementation of democratic principles and human rights. We were concerned with the limitations placed on OSCE observers to monitor the Duma election. We know it was an awful decision and this is not very positive. We are not happy with all the limitations on press freedom, attacks on journalists, pressure on NGOs, not to mention the situation in North Caucasus. This global development of democracy, lack of democracy in a certain way in Russia, is something which is difficult. Why? Because some years ago we tried to set up our relationship on the basis of sharing the same values and principles. What we have to consider is that maybe we have not got exactly the same kind of values or principles. This is why we need to assess the situation for the future. What are the bases of our relationship? What do we share? What do we not share? What do we need to do? These are important questions for the future. Of course, the EU does not seek to lecture Russia, we have no monopoly of democratic principles, but it is really important to continue to discuss all those important issues in the future. The other difficulties come at an international level, for example Kosovo. I mention that because it is a very topical issue. There it is obvious that we are going to have a difficulty with Russia. I remember two years ago at the Helsinki Summit that President Putin mentioned the point and told us, “Take care with Kosovo because if we accept the independence of Kosovo, this will have some consequence on our relationships to deal with other kinds of frozen conflicts”. Of course, he explained to us that so far we had agreed to defend the principle of territorial integrity against the principle of expression of self-determination and if we changed the application of those principles, this would have some consequences in Abkhazia, he did not mention specifically the point, but we understood what he meant. We cannot say that we are surprised by what they are doing now through Mr Lavrov, the Minister of Foreign Affairs, or the others because they mentioned this. Nevertheless, as I do not expect they will accept any kind of resolution at UN level, we will have to try to make a deal with the Secretary General of the United Nations, Mr Ban Ki-moon, in order to see which way legally we can support some form of independence. This is my own feeling. Russia has linked Kosovo with the frozen conflicts. If in South Ossetia, in Georgia, there are now better expectations, it is not exactly the case of Abkhazia where they are stronger and it is difficult to see any kind of solution in the short-term, as in Nargorna-Karabakh in Armenia. Those would be the questions of friction. On other important international issues we are not exactly on the same line; Afghanistan and Iran, we know what is happening now. With Burma, we are trying to work in the same direction, but there are still some differences. There is a third main point that I would like to mention. The first was the paradox, the second was the international questions, and the third is energy. Energy is a key issue for us and for them also. We are weak there because we have no European policy. We have an accumulation of national energy policies, we understand that, it is a fact, but the lack of strong European policy, as a consequence, has weakened us a lot. With the Russians, if we are united we are strong; if we are divided we are very weak. There is competition among a lot of our Member States. This does not help building up the conditions for Europe to speak with one voice, able to better defend the interest of all of our members. This is the position of the Commission and it is why we proposed a comprehensive legislative package some time ago which will promote the capacity of having a united voice and, in our view, better defend the
interests of all of us. We are discussing the fact that the Russians have not reacted in a positive way to some of the proposals included in this package and we will continue to work in that direction. The fourth point I would like to mention in this introduction is the movement of people, it is another big and important issue. As you know, we have visa facilitation and re-admission agreements which entered into force on 1 June. Now we have a tool, an instrument, in order to co-operate and try to implement a policy on the mobility of people. This is not perfect at all. We will need to improve the provisions of these agreements a lot. Russia is pushing to have the free movement of people without visas. We are a little bit reluctant because we have to take into consideration a lot of elements, including security. I have to say, the situation is much better than it was some years ago because now we have something. It is not perfect, but it is a way to progress. I would like to say as well something on solidarity. Solidarity for us is very important and it is linked with the united position. On this very difficult issue of launching the Partnership and Co-operation Agreement, blocked by a trade problem with Poland, the Russians had to accept our position because Europe had a voice, a position, and this was expressed by Chancellor Merkel and President Barroso at the EU-Russia summit in Samara, Russia. Then we were expressing solidarity with our Polish friends. This is what we need to develop in the future to strengthen our position, there is no other way. I would like to conclude this introduction by mentioning three issues. We succeeded in putting in place the co-operation through four spaces. This co-operation is going well and now we have a lot of substance. There are difficulties in all of the spaces but, nevertheless, we are progressing and this is a stable thing that we have in front of us. In my view, we need to launch the negotiations on this Partnership and Co-operation Agreement as soon as possible because this will provide us and the Russians with an adequate framework which we need in order to have a real negotiation process, including the energy question. In my view, the energy question will be solved or will improve with this global framework and this is important. The question of the WTO accession of Russia is another important issue because all of us have an interest in having Russia among the members of the WTO. The PCA that we have today as a framework is not working well and that is why it is useful to have a new one for one main reason. There are a lot of reasons, but the main reason is we have no structure for implementing this agreement which is able to deal effectively with the problems we have to solve. Russians always want to politicise all the questions and raise the questions at the level of ministers, but it is impossible. There is a lack of a level of officials group in order to be able to solve a lot of difficulties. This would ease it a lot and for the next time it would be very important question. I would like to make my last remark off the record (There followed a discussion off the record) Chairman: Mr Landaburu, thank you very much indeed for a very full introductory remark and we note that those final remarks have not been recorded and, therefore, will not be in the transcript. If I could turn to Lord Hannay and ask him if he would like to follow up some of the things you were saying on the institutional arrangements.

Q271 Lord Hannay of Chiswick: I would like to focus on the institutional arrangements, although I think you have given us the beginnings of answers to some of the questions. How well does the current institutional framework, the PCA as it is now, work and how well do the common spaces work? You spoke quite enthusiastically about common spaces. How does the Northern Dimension work? What are the strengths and weaknesses of this current institutional framework, and in what way could it be improved? Are there other mechanisms and structures for co-operation with Russia? We will come on in later questions to the Energy Charter which is there. All that leads to a question which I would like to ask, and I think you are right in saying that this is, as our American friends would call it, payback time for the Russians. They are paying us back for what went on in the 1990s, for which they were largely responsible themselves, but they are still paying us back for that. Does it make sense to run after them in the context of a new PCA? Does that not simply encourage them to go on paying us back in a fairly unpleasant way? Is it realistic to talk about a negotiation of equals with a country that considers that the only equal in the world is the United States, an illusion which they still seem to nurture?

Mr Landaburu: I will try to provide some elements of the answers and I will ask my colleagues to add some additional comments on that. Lord Hannay, for me what is really crucial, if it is possible to have an equal partner relationship in the future, is to be sure that we are interdependent because we need to have a good relationship with our big neighbour and we need the energy which comes from there. We have to try to set up this condition of equal and fair partnership. From their side, they need to have a stable, mature and clear agreement with us in order to be sure that they will have the resources to set up the conditions of their growth. They have no alternative if they want to progress as a big important and modern country. They need to have our investment and our technology and they need to deal with the European Union, which needs to have a good relationship with Russia. That is my first remark. My second one is that
this team of President Putin, and probably the successor of Putin, has made the strategic choice to have a good relationship and to increase the relationship with the EU and its Member States, with the western countries, because they are also Europeans. Despite all the difficulties we have, at the end of the day it is much easier to have an agreement with them than with a lot of countries very far away. We have the same roots, a common culture, not in everything, but we share a lot of things. Despite the differences of our political personnel, there is a strong capacity to set up something. In my view, this is why we have to try to find a specific way to have a relationship with Russia and not always follow what Washington and the United States are thinking, because they have other kinds of problems and we do not have exactly the same. This does not mean that we have a different kind of approach, but maybe an autonomous one. In my view, it is not by developing assertiveness and aggressiveness that we will have some positive consequences in our defence of our interests with Russia. It is obvious that today there are different sensitivities in the European Union among Member States. It is obvious that the new Member States coming from the Soviet Union influence are much more aggressive. Maybe they want the European Union to have a much stronger position. The western countries and the big ones, the UK, Germany and France, in a certain way are much more pragmatic in defending their own interests. What we need to do is to define some strategic objectives and to try to convince all of our Member States to have this common approach. As far as the PCA is concerned, of course we are progressing a lot in the implementation of the four spaces. We are making a lot of progress, but I do not think the structure of this PCA is an adequate structure in order to make the progress that we need to. Maybe my colleagues will have a lot more concrete knowledge on this.

Q272 Chairman: For the record, perhaps they can introduce themselves when they make their first intervention.

Mr Wiegand: My name is Gunnar Wiegand. I am the head of the unit for Russia and also Acting Director for Eastern Europe, Southern Caucasus and Central Asia. To complement the answer given by the Director General on the Partnership and Co-operation Agreement, it was obviously negotiated at a time when Russia was in a particularly weak situation and we were providers of massive food safety assistance and technical assistance to help in the transition process, both in the political and economic transition process. Therefore, it was a Russian wish to change the agreement and have a different agreement, taking into account the new realities. At the same time, since the conclusion of the negotiations in 1994, and the entering into force in 1997, also a lot has happened on the EU side in terms of our deeper integration. Therefore, there is an objective interest on both sides already for political and institutional reasons to have a new framework. In addition to this there are very concrete interests which the Director General referred to for both sides. It is not only the interests of energy security of supply, it is also the interest of energy security or demand. It is the interest of modernisation and diversification on the Russian side, and on our side it is the interest in new trade and investment opportunities for European companies. While this is a very good, solid framework agreement, it has no preferential access and it has no rules on deep economic integration, which can only be done by a free trade agreement of a very modern type to be included in a new post-PCA agreement. We have no specific provisions at all on energy issues, and we will come to the difficulties later on as regards the Energy Charter Treaty. I would argue, to complement whatever exists at a plurilateral level with bilateral provisions. Beyond the strategic and institutional considerations, there are very concrete economic considerations which argue for entering into such negotiations. I think on this one, also, we have a unanimous position of all of our Member States being in favour of it because we have an agreed mandate which covers a very ambitious comprehensive agenda agreed at the level of Coreper, but not yet agreed at the level of ministers. In the meantime, however, the problem with the institutional structure of the PCA is that the Russian side perceived that it was not delivering the results that the agreement was designed for. Notably, the Co-operation Committee was disbanded and also the one Co-operation Council existing at the time was replaced under the common spaces concept with a series of permanent partnership councils which allowed different sector formations of ministerial meetings. The problem is that our civil servant senior level which would have an overview over all the areas of this relationship, simply does not exist anymore and there are no regular meetings between the people who have an impact in their own system and on the overall relationship. However the common spaces are much more successful than is commonly known and it is probably our fault that we do not make this sufficiently known. The info pack will give you a lot of information about what is happening. Just to give you an idea, alone under the common economic space there are about 40 specific dialogues, including a number of sub-groups which have been established, ranging from an investment dialogue to seven different dialogues on industrial standards in certain key areas like, for example, the automotive or
chemical industry. The purpose of all this is to lead towards regulatory convergence and to prepare, therefore, for future negotiations on deep economic integration. There is a lot of simply getting to know each other, the actors in the different ministries or DGs here, the knowledge about the legislative situation as it is now, how you regulate industries, and there is a strong wish on the Russian side to know how it is done in Europe because 52% of their exports currently go to our market. Finally, on the Northern Dimension, that is even less well known but that is a real success story. I have just come from a senior officials meeting we had yesterday in St Petersburg and we have a very satisfactory and co-operative situation there. As the Deputy Foreign Minister Grushko said yesterday, “It is about projects, not policies”. We have a well functioning partnership on environmental protection. We have also an increasingly well functioning partnership on social issues and health. Next year we will establish, if the ministers will agree, a partnership on transport and logistics, helping to develop the northern axis of the EU interconnections between the north-west and the north-east of our common continent. We will also go into the area of energy efficiency and cultural cooperation. There is a huge number of stakeholders in all this. It is not a centralised top-down process, it is a decentralised bottom-up process and that works very well. A lot of funds of international financial institutions could be mobilised through project grants.

Q273 Lord Hannay of Chiswick: Can I mention one slight paradox. With the United States, the European Union has never had a structure of this sort and most people would say that is one of the reasons why the relationship in the economic field with the United States is such a successful one, why investment flows grow and grow and why regulatory convergence can be achieved and so on. Why should that not be so with Russia?

Mr Wiegand: I had the privilege of being head of the unit for relations with the US for several years. We worked closely with Lord Brittan and his successors in getting ever closer transatlantic relations in the economic field. You had recently at the last EU/US summit another major effort to deepen our ties. It remains by far the most important economic relationship. Still, we have a situation where very often companies have to produce according to two different sets of rules and incur heavy costs for this. Apart from the fact that the United States is not a physical neighbour and we do not have as much untapped potential as we have with Russia, there are two key differences. One is that the United States is a member of the WTO, Russia is not a member, therefore we have an interest in creating bilateral rules with Russia and making sure that our markets can integrate. The other reason is that the investment relationship is by far the most important one in the transatlantic relationship, with €1.4 trillion of investment stock compared with something like €39 billion between the EU and Russia. What a difference this is. Since we have that difference, our companies basically produce, having invested on the other side of the Atlantic, for the needs of the respective market, while with Russia we are very far away from that.

Q274 Chairman: We learned today that the Russian mission here in Brussels to the European Union is probably the largest mission of any third country. How much of the business which you have been talking about occurs here in an interaction between people in the Commission with that mission, or how far does it occur in Moscow between your delegation and Russian ministries? Is it people coming from Russian ministries to Brussels and vice versa? How are the mechanics? This is a very big mission. Is this an important factor in the relationship?

Mr Landaburu: Giving you a more precise answer, it is obvious that they try to have some deep links and deep co-operation at the level of Brussels. The appointment of Mr Chizhov, who previously had been Deputy Minister in charge of Europe for many years, as Ambassador of Russia is something which is a very clear and important signal. For the negotiation of the next framework agreement they have appointed Mr Chizhov as the chief negotiator. This means they want to have a lot of things dealt with in Brussels and from Brussels. On our side, we would prefer to have contacts in Moscow with the ministries and the people. This does not mean we do not want to have a relationship with Mr Chizhov at all, but we have a very important delegation there in Moscow. Mr Vandoren is the number two of our delegation in Moscow. To do our work at a good level and with some quality and to provide to our Member States all the information they and we need, we need to be in close contact with the ministries and not only have a relationship with Chizhov. Of course, a strong delegation from Russia here in Brussels is helpful as well to solve a lot of difficulties. When we prepare, for instance, the summit, and we have two summits every year, having some people who are able to take some decisions at this level is very helpful and this eases the process a lot.

Q275 Chairman: Can I go back to your earlier answer. You quoted figures, first of all, of 1.4 trillion for the cross-investment with the United States and 39 billion, but was that euros or was it dollars?
Mr Landaburu: Euros.
Mr Wiegand: We always count in euros.

Q276 Chairman: I just thought since you were talking about the United States you might be talking about dollars.
Mr Wiegand: The Russian mission to the European Union has a bit more than 100 staff, of which I think something like two-thirds are diplomatic staff. The Ambassador has four permanent Deputy Heads of Mission, which is quite unusual, who cover the four common spaces essentially. Indeed, I think their basic reasoning had been, with the common spaces and the future new agreement, that they would acquire a little bit of the functioning of a Permanent Representation of a Member State to the EU. They also call themselves “Permanent Mission” and that is quite interesting. Certainly there can be no monopoly of contacts via this mission as we have many contacts, but I think our delegation cannot complain about a lack of need from our side of EU interaction in dealing with the government.
Mr Vandoren: In the Delegation of the Commission in Russia we cover everything which is on the scene in EU/Russia relations, in particular with regard to the four spaces, obviously.

Q277 Lord Truscott: On the four common spaces, do you find more engagement from the Russians on some of the spaces they are more interested in and less engagement on the area of common spaces they are less interested in? I am thinking of the development of democracy and justice compared with the economic space.
Mr Vandoren: In my view, the common economic space works relatively well. In that context, we have a number of road maps and dozens of working groups and dialogues which do not necessarily lead to concrete results but, nevertheless, do bring the relevant and competent officials from both sides together to discuss all matters which are relevant on the trade side. Clearly, with regard to justice and home affairs, there is strong co-operation and there is also a strong interest on both sides, as has been demonstrated by the signing of the visa facilitation agreement and the re-admission agreement. There is increasing good co-operation on matters in the fields of culture, education, science and technology, research and development. I would say that probably where it is the most difficult is the common space on external security where, for almost obvious reasons, at least for the time being, we do not see eye-to-eye on a number of key issues and, therefore, the deliverables are less frequent.
Mr Wiegand: I would concur with this and would like to say that the most successful in terms of actual deliveries so far has been the second common space, which is on home and justice matters. There is a very well functioning Permanent Partnership Council, which includes also significantly not only the Russian Ministers of Interior and Justice but also the key Presidential Adviser in this area, Mr Victor Ivanov.
Mr Landaburu: They will meet here tomorrow.
Mr Wiegand: Certainly we have there an area where there is strong commonality of interest to reach concrete results quickly because there is so much impact on our trade, travellers, businessmen, students and so on. The common space with the greatest number of activities, however, and the greatest number of people involved clearly is the common economic space, where, again, I would say that there is huge interest on both sides, but we do have a strong long-term common vision where we want to go, that is deep economic integration. It is much more complicated to reach results, therefore these dialogues need more time. The growth area is the fourth common space, education, culture and research. Research is an area which perhaps did not need the common space because we have an agreement in this area with each other. We had the Sixth Framework Programme and now the Seventh Framework Programme. Russia is the most successful third country taking up the possibilities of our research co-operation. Currently there are 220 projects worth some €2.3 billion where the Russians also put their own money in, so there is very strong co-operation between our research communities. That is positive and, indeed, that is Russia engaging in one of the areas where it has major value-added. The reference to the external security space, the Commission’s only stake in this is the civil protection area where we do have now a Memorandum of Understanding and we want to further expand on this between our civil protection mechanism and EMERCOM in Russia. You will certainly see colleagues in the Council Secretariat, or have already seen them on this common space.

Q278 Chairman: We will be seeing them tomorrow.
Mr Wiegand: They will tell you tomorrow about our intensive political dialogue on common neighbourhood related issues where the Commission fully participates but is not in the lead. The one interesting area where both sides have repeatedly said, “We need to work together”, is peacekeeping, and colleagues will tell you more about this tomorrow. There is great interest on the Russian side in this.

Q279 Chairman: What will change under the European Neighbourhood and Partnership Instrument? I know Russia is not a neighbourhood in this sense, but would there be any change in terms of
funds available for Russia in the future under the new initiative?

Mr Wiegand: When we started our co-operation with the Russian Federation we had the technical assistance instrument Tacis and we started with annual volumes of support of something like 120-130 million ecus at the time and it was support for transition processes. It was a process where all kinds of potential beneficiaries could come up to our Delegation, or the National Co-ordinating Unit, and come up with ideas for funding and we had broad priorities. This has changed a lot over the years, and particularly since the beginning of this year we have the European Neighbourhood and Partnership Instrument, which does not only include our ENP neighbours but also Russia. The basic approach here is one of financial co-operation, which includes co-financing from the Russian side in a number of areas and to an increasing degree it means ownership on the Russian side, it means projects are identified together, but also the priorities in the programming phase are fixed together. We have had good experiences in the programming phase on the National Indicative Programme 2007-2010, which was endorsed a few months ago by the Russian side. The phasing in of the new instrument was a bit slower than we had expected, therefore in the first year, 2007, we have not committed as many funds as we wanted. We have the possibility of committing about €30 million a year. We did commit €17 million this year and next year we would target something between €30 and €40 million. The main emphasis in all this now is rather than providing assistance to a country which requires our help to underpin the implementation of the common spaces, plus specific support for Kaliningrad and, complementary to this, participation in several cross-border co-operation programmes. There is a total of seven cross-border co-operation programmes which involve both Member States and Russia, from the Bering Sea to the Black Sea, and that facilitates a lot of border crossing problem solutions. On the project identification phase we are also trying to work with the Russian side to a very detailed degree, more detailed than in the past. To give you an example, we would like to extend the idea, which we have successfully tested in other industrialised countries, to establish a network of EU study centres in Russia, although obviously there are places where there are concentrations of universities and research institutes, such as Moscow, you will think very seriously about widening it throughout the whole of the Russian space.

Mr Wiegand: That is our intention.

Chairman: I hope that as far as encouraging studies, although obviously there are places where there are concentrations of universities and research institutes, such as Moscow, you will think very seriously about widening it throughout the whole of the Russian space.

Chairman: I think that is very important. Mr Wiegand, you were not present at the very beginning when I said that although we are taking a note of this, there are some parts of the conversation which we may want to have off the record and I just wanted to repeat that. If that is the case, we will stop taking a note, as happened during the closing remarks, as you know, of Mr Landaburu’s remarks. I want to move into an area where this may be the situation. Mr Landaburu, in his remarks, made some comments on the range of attitudes which occur among different Member States and the possible complications which this diversity of opinion may make for those who are attempting to conduct a policy. I wonder whether you would like to say anything further about that or whether you feel that is something one should more appropriately address to Member States rather than the institutions of the Community.

Mr Wiegand: On this issue, I would like to continue with my remarks on the record. It is a normal and integral part of our business, in trying to find the common interests, in trying to formulate EU interests and project them externally, to deal with different approaches Member States have to different relationships. Having dealt with transatlantic relations before, this challenge is not completely unknown to me. We see this with regard to many relationships, in fact, because of the great diversity of history, cultures and political developments in different Member States. However, I would recognise, as the Director General did before, that our most recent rounds of enlargement have placed a considerable challenge on the institutions in Brussels in trying to correctly identify our common approaches and remaining effective in achieving results. However, I think we can say with some pride that throughout the development of EU external
relations and successive rounds of enlargement, each round of enlargement gave an additional dimension and impetus to the development of relations of the EU as a whole with different parts of the world and I do not think this will be different this time.

Q282 Lord Hamilton of Epsom: Can I follow on that because, at the end of the day, as we do enlarge Europe we get nearer and nearer to Russia and we keep on saying, “Europe goes on and on until we reach Russia, but there is no question of them being members of the European Union”. Well, they have got a population of 140 million and dropping, Turkey has got a population of 70 million and rising, and the British Government thinks the Turks ought to be in the EU. The GDP of Russia is that of Belgium and Holland put together. This is not a gigantic country. Perhaps this ought to be off the record. (There followed a short discussion off the record)

Mr Wiegand: (There followed a short discussion off the record)

Q283 Chairman: This has already been touched upon in the introductory intervention, but I wonder if you would like to come back to this question as to on which areas of policy does the European Union most need to present a united front in its relations with Russia. Linked to it, what does the European Union have to offer Russia in the context of negotiations? What are the most important chips that we may have available? How can we best influence Russian thinking on policy?

Mr Wiegand: I will answer the first part of your question, but to answer the second part in a public recording is perhaps not the most appropriate thing to do. On the first one, I think there is a common understanding that the most important part of our future negotiations will be to clarify rules for trade and investment in general and there is a very important component which requires specific rules and that is energy. I would clearly like to underline that there are strong interests on both sides in this, that we have, both overall in our economic development but also with regard to energy in particular, a situation of mutual interdependence and there is huge potential for modernisation and diversification with engagement of European industry in Russia. The current President has in his important speeches repeatedly pointed to how much Russia lags behind in terms of having competitive industries, how much Russian infrastructure has to be modernised to be competitive and says so also at our summit meetings regularly. Our industry is interested in not being only traders and exporters but also being present and being present with clear rules which can be tested where dispute settlement exists.

We have to achieve the situation both via WTO accession and via a bilateral agreement. I would not like to single out exclusively, as some people do, the energy area. I think it is a general challenge for both sides to have clear rules for trade and investment, but there is a particular interest on both sides to have this also in energy, spelt out in more detail because there are no general rules available for the energy side beyond the Energy Charter Treaty, which is a different chapter.

Q284 Chairman: I do not know whether you want to go off the record to attempt any of the others, but if you do not, we can continue with our next question. Mr Wiegand: (There followed a short discussion off the record)

Chairman: Moving on now to energy, if we may. Lord Truscott?

Q285 Lord Truscott: Could you outline what you see as the obstacles to the EU having a common energy policy? You mentioned the Energy Charter and we mentioned the PCA in terms of energy, but I know there are moves afoot to have a new energy directive in terms of access to European markets, for example for Russian energy companies. Can that be seen as protectionist? How do you deal with the balance of encouraging constructive engagement with Russia, yet, in developing this energy directive, avoiding an element of protectionism?

Mr Wiegand: Will you also be seeing colleagues from the energy side of the Commission?

Q286 Chairman: No, we are not seeing anybody from the Directorate General on this agenda.

Mr Wiegand: As President Barroso has said, the proposal which the Commission made in the Third Energy Liberalisation Package is not a proposal for protectionism, this is a proposal to liberalise the internal market, essentially with an unbundling approach between companies which have a production supply function and companies which have a distribution function. The proposals are limited in the whole energy chain from production to retail distribution to wholesale distribution or, as we call them, the transmission networks. There are no restrictions proposed for any other part of the energy chain. That is the first misconception which some have. For transmission networks, the proposal is to simply apply the same rules to external investors as to domestic investors. We want to ensure that third country investors have to obey by the same rules as our own companies to have a level playing field assured. How can this be done? First, they would have to respect the same principle that a company which would be involved in supply or production activities could not acquire more than a minority
share, the same thing for European Union companies, but, secondly, in order to have this made possible for third country investors, there would have to be an agreement which spells out the rules in energy between the country from which these companies would come and us. We think that is an invitation for negotiation but not a protectionist measure.

Q287 Lord Truscott: By minority share, are we talking about less than 50% or are we talking about a blocking share? Obviously with countries like Russia and also some Middle Eastern states where they have heavily state controlled sectors, there is no way they are going to be able to meet the unbundling requirements which we may develop here in the EU, so by its very nature they could say that will impact unfairly upon them.

Mr Wiegand: On the first question, I am not specialised enough to answer that question, so I will have to ask my colleague Frédéric Maduraud whether he can. On the second question, I guess this will be a company decision to be taken by the companies of the type you describe on how they would like to organise themselves if they really want to invest in transmission networks, but it is not possible that we would let the internal market related decisions in the EU be governed by considerations of how companies from third countries are structured. We should not forget that the main purpose of unbundling is to have better and cheaper energy prices in Europe, to have a wider choice for consumers and not to regulate a situation for third country investors.

Q288 Lord Truscott: That is fair enough, providing we do achieve unbundling in the EU, but that is not going to work if we do not achieve it, is it?

Mr Wiegand: That is correct, therefore this will not be the only proposal in this area.

Mr Maduraud: My name is Frédéric Maduraud. I am responsible for the co-ordination of trade and economic co-operations, and I am working with Mr Gunnar Wiegand. I think the proposal does address economic co-operations, and I am working with Mr Lars-Gunnar Wigemark.

Q289 Lord Truscott: Below 50%?

Mr Maduraud: Yes.

Q290 Lord Truscott: We will move on to a completely different subject. To what extent do EU interests and Russian interests coincide in terms of their relationship with countries in the former Soviet Union? I am thinking particularly of countries in the Caucasus and Moldova. How can the EU and Russia collaborate to diffuse some of the tensions in what Moscow used to regard as its backyard?

Mr Wiegand: We will give you our vision and then you will hear the vision of our colleagues on the other side of Rue de la Loi, but we tend to share the same vision. We see huge potential here. We do not use the same term as some of our Russian colleagues do who still like to use the term “post-Soviet space”, we use the term “common neighbourhood” and it means a lot to us. We have included the countries you referred to, Moldova, Ukraine and the three countries of the Southern Caucasus, Georgia, Azerbaijan and Armenia, in the European Neighbourhood Policy. It is worth reading the ENP Action Plans which we have agreed with each of these countries. These are very precise plans with very precise benchmarks where the EU supports politically and with financial means the Reform Agenda of these countries in different policy spheres. This is not an imposition of EU policies, this is support for the domestic reform agenda and it is something which is undertaken upon these countries’ own initiative. It is an offer which we have made. This is not in order to get these countries away from their traditional links, sometimes they are more intensive than in other cases with Russia, but it is to fully take into account the fact that these are sovereign states which take their own decisions about their own policies and the European Union is one of the players in these regions. In fact, there are many beyond even Russia and the EU. We are convinced that we could work very closely with Russia in finding solutions to the problems of the so-called “frozen conflicts”, which unfortunately are not always completely frozen. We would like to work more strongly with the Russian Federation on this. We have, perhaps, the most constructive dialogue with Russia on the situation in Transnistria and the least detailed discussion in terms of finding solutions for the situation in Georgia, and Nagorno-Karabakh is somewhere in between.

Q291 Chairman: Thank you very much. You will be pleased to know that the European Neighbourhood Policy Action Plans do come before our Committee, so we look at them when they are going through. You were saying earlier that we do not necessarily know what is being done, and we have certainly learned a lot this afternoon, but in that particular area, because there is a document which comes before our Committee, we at least are aware.

Mr Wiegand: That is fantastic. We are not used to such close attention to the ENP Action Plans!

Q292 Lord Hannay of Chiswick: These subjects I am about to refer to, I suppose, are a bit more the other side of the road than your side, but in theory one can see lots that the EU and Russia could do on foreign
and security policy, co-operation on non-proliferation, nuclear safety, multilateral disarmament, crisis management and peace-keeping. The theory is clearly quite positive, the practice at the moment seems to fall some way short of that promise because the Russians themselves do not seem to be terribly interested, other than in paying lip service to these. I wonder if you could comment on how it looks. There are a number of areas in which the Russians are basically frustrating what the European Union is trying to do, whether it is over Iran’s nuclear ambitions or many other areas, in particular in Kosovo, where I do not know whether you have managed to identify a Russian national interest which they are defending there but, I am afraid to say, I have not, and where they seem to be pursuing something much closer to a pre-First World War balance of interest policy than one based on the sort of values we all pursue now.

Mr Wiegand: (There followed a short discussion on the record) I would say most of the answers to this question will indeed have to be given by our colleagues at the Council Secretariat, however we are in charge of the Community instruments in some of these areas. In particular in this unit we are dealing also with the programming of our nuclear safety operations where we have spent all the funds since the early 1990s so far on the former Soviet Union with the lion’s share going to Russia and Ukraine, linked to Chernobyl. We have just made a shift for the first 10 years of Soviet assistance, which consisted of a lot of upgrading nuclear power stations to higher safety standards, with delivery not only of technical assistance but also of hardware, to a situation where we basically work much more now on regulatory assistance, supervisory assistance and training assistance. We have a new instrument for this purpose, which is called the Instrument for Nuclear Safety. This provides us with a substantial sum over seven years of €572 million where we will also be able to go to different countries in the future. The lion’s share remains with Russia and Ukraine for the time being. Russia is quite a good partner in working with us on nuclear safety improvement. We are also working with other instruments and there is now the new Stability Instrument which provides for funding also on non-proliferation, living up to the commitments which the EU made at the G7 Summit in Canada a number of years ago. President Prodi made the pledge of delivering €1 billion of funds from the Community budget for non-proliferation related actions. Our nuclear safety is part of the answer, but we also work in a number of other areas. There is Community support here. You are right, these are important challenges going well beyond Russia obviously, particularly on non-proliferation. I guess on the work with Russia with regard to the case of Iran, you will hear many interesting details tomorrow.

Q293 Lord Truscott: It seems to me that one of the issues of with dealing with Russia, especially the EU dealing with Russia, is this question of Russian identity. To a certain extent, it seems like an academic point, but I am not sure it is because it has been said several times during this meeting that Russia is a European country or a European nation or at least has a European attitude. Is it not more a Eurasian country than a European one? If you go to the reindeer herders of the Chuckchi nation in the far north and say, “Well, you are European”, they hardly feel Russian, let alone European. Is it perhaps this identity crisis that Russians have had since the 19th century which in a way makes it difficult for them to deal with us as part of the European family of nations?

Mr Wiegand: Do all nation states not have an identity crisis at some point?

Q294 Lord Truscott: It has been rather a long one with Russia, has it not?

Mr Wiegand: I think we have to be respectful of the incredible size of the country, the incredible diversity of different groups of population in Russia and of the different traditions which this reflects. For the European Commission dealing essentially with very concrete issues, notably of economic relevance, we know that 80% of the Russian population lives geographically in the European part of the country, we know that more than 80% of the industrial capacity is in that part of the country and we have seen repeatedly, the latest in May when the EU turned 50, a strong expression of the European-ness of Russia by its leadership. We have no doubts to express as to the European choice of Russia and we welcome this. However, it is clear to us that Russia has very important interests in Asia, it is also an Asian power and has Asian neighbours as well as European neighbours.

Mr Vandoren: There are perhaps two aspects to what has been said. I think from our point of view, Russia is certainly a difficult partner to do business with, but the Russians see the EU also as a difficult animal or mixture of institutions to do business with.

Mr Wiegand: Not to speak of the Member States!

Mr Vandoren: I am talking about the EU as a whole. I think we have to acknowledge that as well. This is why, if I may say in front of this distinguished audience, that, at least in my view and, I think on the Commission’s side in the view of many, it is very important that the Reform Treaty is put into place so that we will be a stronger partner to negotiate with any third country, in particular with regard to Russia. It is also true that if you look at what happens
sometimes, or what has happened sometimes at summit meetings, there is not always the necessary trust to do business with each other for a number of reasons, which could lead us very far, but this should not be insurmountable. What is important is that we look ahead at the new elections as another new phase to start next year.

Q295 Lord Hamilton of Epsom: All I would say to Lord Truscott is that I do feel Russia looks a lot more European than Turkey! You commented about the four spaces and the one which seems to be working least well is the political situation, democracy and the rule of law and so forth. Has any progress been made in improving it, it does not look like it on the face of it, in terms of the EU’s influence on Russia in terms of democracy and all those areas?

Mr Wiegand: What we can observe is that the Russian leadership and the civil servants working with the Russian leadership have become much more assertive in establishing and defending their interpretation of our common commitments under the Council of Europe or the OSCE instruments, not to speak about the UN. While the Russian Federation fully recognises that there exist these commitments, it is interesting to observe, and I think it should be noted, that in the Russian legal system the rulings of the European Court on Human Rights are being increasingly observed and used as case law, which was not the case before. It is not only about that Strasbourg Court having an impact on actual rulings in individual cases as a last instance, it is that its rulings are being used by judges in Russia. That is real progress. What certainly is not real progress is that Protocol 14 of the Council of Europe Human Rights Convention is not yet ratified as the only country of the Council of Europe, and certainly the Director-General already referred to our continued human rights concerns in a number of areas, notably violations in the Northern Caucasus. We are worried also about the question of media freedom, for example. While people can express their opinion, it appears that self-censorship is something which is widely spread and certainly the ownership of most of the mass media is also a point which is questioned. What can we do about it? We think each state obviously has to be first and foremost its own judge under its own procedures and participatory processes. What we can do in all this is remain engaged and continue to express how we interpret the common commitments we all have entered into. This is done at the political level on different occasions. It is also done in biannual human rights consultations where I can assure you there are no taboos, all issues are discussed in extenso and we appreciate that openness of the Russian side. We only deplore that the participants of these events are the human rights experts of the Foreign Ministry and do not include colleagues from the competent Interior and Justice Ministries. We would also appreciate if we could have these dialogues in Moscow at times as well and not only in Europe and that the outreach session, which we have with NGOs before this, would be attended also by our Russian counterparts and not only by us. In addition to these consultations and the political dialogue at high level, we have also a number of projects under the European Initiative for Democracy and Human Rights instrument, EIDHR, which decides centrally about all projects in third countries. There are many projects in terms of the promotion of civil society and support for human rights organisations in Russia. Finally, I would like to underline that obviously the Russian side has every right to defend its own interpretation and does so in an increasingly vocal fashion. You may have seen at the Mafra Summit recently that Russia proposed the creation of an Institute for Freedom and Democracy in the EU and the reaction of Prime Minister Socrates and President Barroso was, “There is no problem, you are free to establish any institute anywhere in the EU. You are welcome to do so”.

Q296 Lord Hamilton of Epsom: We have heard concerns about the independence of the judiciary as well. Do you share that? A lot of the judges look over their shoulders and wonder what Putin might think.

Mr Wiegand: There are many observers who say that the creation of a full state of law requires, indeed, additional efforts. By the way, that is something you do not only hear from human rights organisations but also a lot from business.

Mr Wigemark: My name is Lars-Gunnar Wigemark. I also work together with Mr Wiegand. On this point specifically on what the EU could be doing more of, of course we speak often first and foremost that the very basis for our relationship on strategic partnership dealings with Russia is common values and I think we, within the European Union, know what those common values are, and specifically we are often thinking of the Copenhagen criteria as the basis for membership of the European Union. When we convey this concept or mantra of common values to the Russians, I do not think it is always clear what we are talking about. We could perhaps be more specific about which commitments Russia has already undertaken. Under international law, Russia is a member of the Council of Europe and it is a member of the European Convention on Human Rights. Mr Wiegand already mentioned the European Court of Human Rights. There are a number of decisions which have been handed down specifically on Russian cases. Where we have seen implementation on the Russian side, even in terms of payments of damages and so on, in other cases there
has not been proper follow-up. One piece of advice would be to be more specific in very concrete terms what we mean by common values, otherwise it will turn into a discussion of cultural values, which I think we are seeing coming more and more from the Russian side.

Q297 Chairman: My own experience going back a long way was when one had specific cases which one was able to point out where there were the problems and one often, even in earlier times, was able to make more progress than by trying to get agreement on generalities. May I just say, we have come to the end of the questions which we wanted to address on the subject of Russia, but something you said earlier made me wonder if I could ask you a further question, which is on the other study we are undertaking at this time and which we are also seeing some other people in Brussels about. We were not intending to ask you questions, but we are doing a study as well on the European Reform Treaty and its implications in these areas. It was when you made a remark about hearing your view and then going to hear what the view was on the other side of the Rue de la Loi. It made me wonder whether when we have a European External Action Service, and both of you are working within that framework, do you think it will mean you will all be singing from the same hymn sheet.

Mr Wiegand: The answer is very simple. We are already now singing from the same hymn sheet with different voices perhaps and in the future we will do it with one voice! We have just one boss and we will be part of one integrated service, so that will make things much easier for everybody. I would like to add one sentence on the previous issue. When we talk about democracy, freedom, human rights and common values, what is important in the new way of interacting with Russia is that we do not discuss these things, as the Director-General said before, with us being the lecturers. We should not forget that the majority of our Member States—and this I can say as a German—are countries which have come out of authoritarianism themselves, be it from left or right, and many are very young democracies. Many of our countries have undergone similar processes as in Russia and have known similar challenges and there are different ways and means to achieve the same standards in the end. What is important in this process is that we accept also when Russia raises critical points with us. Not everything is perfect in EU Member States, and there is one regular item which always comes up and this is minority rights. I can tell you that we are in close contact with a number of Member States to clarify exactly what is happening in this area. We have to be careful there that it is not a one-way dialogue but a two-way street. Finally, on your last question, you can be sure that over the last few years we have learned to interact ever closer together, to put together the Community instruments and policies in external relations with the emerging now much more operational CFSP and ESDP. We are convinced that if we manage to put all these instruments and policies together, not only our citizens would not wonder anymore, and we would be able to be even more effective than we are currently. We hope that the Reform Treaty will be ratified soon.

Q298 Chairman: Mr Wiegand, on behalf of my colleagues, can I say that we are very grateful to you and all of your colleagues for giving up so much time. I am not quite sure whether it was you or the Director General who said at the beginning that you were not sure that people were aware about how much was being done in this area and perhaps the responsibility took place in various places. We have learned a great deal, and I think our report will be a great deal richer because of what we have been able to hear from you this afternoon of the sort of work which is going on in practice. Therefore, we hope when we do come to report, it will at least make sure there is a little bit of wider knowledge in some areas of some of the very important things we have heard about this afternoon. As I say, we are extremely grateful to you all for coming and we have learned a great deal. We look forward to receiving these dossiers. I do not know whether we are going to formally take them as written evidence, it may be that if we wish to we might be able to incorporate some part of it into our report, but they are available for that if we so wish.

Mr Wiegand: On behalf of my colleagues, I would like to thank you very much for the interest you have in the work we do. We are used to interest, but we are not used to such extremely well prepared expressions of interest. I do not know whether you have learned more because you knew a lot of it already, but perhaps you have heard what it means in actual implementation in everyday work. Thank you.

Chairman: Thank you very much indeed.
Lord Hannay of Chiswick: Good morning, Robert. As you know, we are one of the Sub-Committees of the European Union Committee, and we are now carrying out an inquiry on the relations between the European Union and Russia. We have taken evidence in London, looking at the current state of Europe. We are very fortunate to have Sir Roderic as our specialist adviser for this inquiry. We took evidence yesterday from the Commission, Mr Wiegeand, and we will be seeing Patrick Child later on this morning. We had a very interesting session this morning with four ambassador members of the PSC from Greece, Sweden, Finland and Germany, as well as Julian, which gave us an opportunity to realise some of the constraints, but also gave us an opportunity for a rather wide-ranging discussion on some of the more general issues of Russia rather than some of the specifics, which they obviously have to focus on most of the time. I wonder whether you would like to say something on what should be the fundamental objectives of European Union policy with regard to Russia.

Mr Cooper: In the end, what we would like, which is probably true of all countries, is to have a Russia which looks and behaves more like us. At the heart of that is a Russia which is governed by the rule of law, that would make it more predictable and easier to do business with. On the other hand, one ought to recognise that in spite of the various problems, we are dealing with something today which is much easier to deal with than the Soviet Union, so in terms of the foreign policy relationship, it is a completely different relationship. It is not a perfect relationship by any means. I was going to say I do not think anybody in Europe sees Russia as a threat in the way in which the Soviet Union was a threat, but that is probably not completely true. There are people who had bad experiences who probably do see it as a threat, but I do not think most people think of it in those terms. Nevertheless, there are difficulties in dealing with Russia, which are very much to do with the lack of rule of law and the fact that the system, therefore, has got some very unpredictable elements in it.

Lord Hannay of Chiswick: Could we look at issues which do not directly relate to the relationship between Russia and the EU. Perhaps you could say what you think the scope for co-operation is in a whole range of fields: foreign and security policy, non-proliferation, nuclear safety, multilateral disarmament, crisis management, peace-keeping, this sort of area here where it is quite interesting to know before we get into the real bilateral relationship.

Mr Cooper: There are non-proliferation and anti-terrorism fields where we have a good relationship with Russia. In areas of foreign policy the relationship is often co-operative. For example, in dealing with Iran, one would say that although there are difficulties, the balance is broadly positive. Speaking personally, I have got a lot of respect for the Russians’ knowledge of Iran. In the nuclear area, they have had a very intense relationship with the Iranians, and I always find what they have to tell me about how the Iranian system works very valuable. I think they read the Iranians in some ways better than Western countries do because they know them better. Terrorism is not a field I have directly engaged with, but everybody tells me that co-operation with Russia is very good. I have to confess also, I do not know very much about nuclear safety.

Q300 Lord Hannay of Chiswick: Can I follow up on the Iranian one, which is obviously extremely topical at the moment. The picture you have painted is not possibly what one thinks of in public as being the picture because the Russians, along with the Chinese, but more prominently the Chinese, tend to give the public the impression that they are not on the same wavelength as the EU3. Is your positive analysis...
because you do not have to deal with the issue of sanctions, that is dealt with more in New York than here, and you deal with how do we achieve the shared objective of preventing Iran becoming a nuclear weapon state? It does seem as if the co-operation is a bit less good than you state it is, but perhaps you will persuade us otherwise.

Mr Cooper: No, I do deal with sanctions as well, and the Russians are not very enthusiastic about the sanctions. I must say, sometimes I share that feeling. For example in the recent visit of President Putin. Everything that I know about it suggests that they delivered a very tough message in quite a sophisticated way. They deliberately made some rather soothing noises in public, but in private—and this is the impression I get from the Iranians as well as what the Russians have told us in private—they told the Iranians very clearly what they thought the Iranians needed to do and were able to do that at the level of the supreme leader, which not many people get access to. I saw all of that as being positive. On sanctions, the Russians have never been very enthusiastic. Once somebody asked one of our Russian colleagues why the Russians had agreed to sanctions in the first place and they said, “Well, out of despair”, because nothing else seemed to be working. The Russians believe, as we believe, that in the end sanctions, the Russians believe, as we believe, that in the end sanctions saying, one, they do not work and, two, the Russians believe that sanctions in the first place and they said, “Well, out of despair”, because nothing else seemed to be working. The Russians believe, as we believe, that in the end they will have too have a negotiated solution. They do not think the Iranians can be coerced into a solution. They regard sanctions as probably a necessary evil and, therefore, they do not rush into sanctions. My expectation is that we will get another resolution, and the Russians are not necessarily the most difficult people in negotiating it.

Mr Cooper: He has aged a lot though!

Q306 Lord Hamilton of Epsom: I am very interested that you think they have a much better understanding of Iran than others do. From the Russian point of view, how do you see that being constructively taken forward? Are they separately negotiating with them?

Mr Cooper: Yes, because the single civil nuclear programme in Iran is a Russian programme, the reactor at Bushehr, which the Russians have been building for years. Therefore, they are in very, very close contact with the nuclear community in Iran. Although they attempt to keep these two things separate, the fact is they know everybody in the nuclear world much better than anybody else does because they are doing a multi-billion dollar piece of business with them.

Q307 Lord Hamilton of Epsom: Is it right that they are not supplying them with a lot of the radioactive material?

Mr Cooper: So far they have not supplied the fuel for the reactor at all, but I understand they may be about to do that. I think part of Putin’s visit was to do with finally reaching an agreement which would mean they would put the fuel in, but the fuel is owned and controlled by the Russians and they have quite strict provisions about proliferation. For example, If Iran was formally in breach of its Safeguard Agreement with the IAEA, then the Russians would be obliged to stop the co-operation at Bushehr.

Q308 Lord Hamilton of Epsom: In terms of weapons grade material, it will not come from that reactor?

Mr Cooper: No, it has nothing to do with that.

Q309 Lord Hamilton of Epsom: Having said that, do you feel there is a black market which they are buying it on elsewhere?

Mr Cooper: The weapons grade material?

Q310 Lord Hamilton of Epsom: Yes.

Mr Cooper: No, I do not think so because otherwise they would not be trying to make the PI centrifuges work.

Q311 Lord Hamilton of Epsom: That is very significant, is it not, because if that all adds up, they are not about to produce a nuclear weapon?

Mr Cooper: That is a whole different question. (There followed a short discussion off the record)

Q312 Chairman: Again, this is a question where you may feel you would like to go off the record. I wonder whether you would like to characterise the differences in approach among the Member States in terms of policy and approaches and how far those differences
Mr Cooper: I think everybody understands that throughout the European Union there are a vast number of different histories with Russia. Starting at one end of the spectrum, you have a country like Greece whose existence as an independent country in the 19th century was partly a result of Russian support to other countries which lost their existence as independent countries because of Russia, so it is not a surprise that there are a range of very different relationships indeed. It is also true generally that super powers exercise a very large gravitational pull—and this is true of the USA as well as Russia—on individual Member States to the extent that they can pull the European Union apart. There is a prisoners’ dilemma situation. In the long run, everybody would be better off by acting together but, in the short run, that does not always appear so to individual Member States at any particular moment. Precisely the function of the three of us here is to try and find ways of demonstrating to the Member States that they are better off if they work together. The extent to which we work together depends very much on what is happening within the European Union. In the area of trade and economic co-operation where there are well established rules, then the European Union does operate as a unit because that is the law. In the area of energy, for example, there is not a strong EU energy policy and, indeed, even physical infrastructure in energy does not mean there is a single energy market in the European Union. I think probably there will be more co-operation in energy in the future. As internal co-operation becomes stronger, then external co-operation on energy matters will become stronger as well.

Q313 Chairman: In our discussions with the ambassadors from the PSC this morning we were interested to discover that at that level there are discussions on a number of particular issues and the Russian dimension of that, but there is very rarely an opportunity to develop an overall view of attitudes towards Russia and to develop a common analysis of these programmes. How far do you feel the CFSP, and its structures of the Union ought to be an instrument which will help Member States develop common analyses of partners like Russia?

Mr Cooper: Russia is very big and very complicated and it is quite difficult to have a single policy on Russia. I do not know how people see this in the UK. You have commercial relations with Russia, you have relations with Russia in the case of Britain connected with Mr Litvinenko’s death for example, you have relations with Russia concerned with their neighbours and we have stories like the Iran story we were talking about. Whether you can aggregate that and say we have a policy on Russia, I am not sure; inevitably things tend to be discussed piece by piece. I am not even sure how much it helps to say you have a policy on Russia generally, except when you come to the point, as it was with the Soviet Union, where there was a single overwhelming factor, which was one of a threat.

Q314 Lord Truscott: My Lord Chairman, if I can go back to energy, which you referred to, Mr Cooper. In your view, what are the obstacles to having a common approach to energy as far as the EU is concerned? You said it is difficult to have a policy in separate areas towards Russia, but at least we should be moving towards a common approach, particularly in the energy sphere. With regard to that, what do you think is the proper balance between ensuring we have a liberalised, open energy market on the one hand and, on the other, ensuring security of supply and security for our energy infrastructure, because there is obviously a debate going on at the moment about the level of protectionism which Europe might be moving towards?

Mr Cooper: I am not necessarily the best qualified person to answer that question because it is a much bigger question but, nevertheless, I think it is right to regard energy as being different from other commodities because of the central role it plays in all of our lives and economies. Therefore, without exaggerating, I think the best security of supply is a well-functioning market, but in some areas where, for example, you are heavily dependent on gas through pipelines, then there is a certain risk. Of course, the fact that Russia has on a couple of occasions switched off the gas—in fact, on more than a couple of occasions if you take individual cases—has made Member States very conscious of that risk. That is one of the reasons why you see a number of people creating LNG terminals as an alternative. It seems reasonable under the circumstances to pay some insurance premium to have some alternative sources of energy. On the other hand, one ought to understand that Russia is probably more dependent on selling energy to us than we are on buying energy from Russia. They have a very strong interest in being a predictable supplier, so I would say that one should pay an insurance premium, but probably not an absolutely excessive one. There are other ways in which one can improve one’s security, notably by having a better internal market in energy by having connectivity, so that if one country has an energy problem with Russia or somebody else, they have got alternative ways of getting electricity or gas. I think there is every reason—partly for bargaining leverage reasons but also there would be environmental considerations as well—for having a much stronger energy policy in the European Union than we do at the moment. I would predict we will have one in a few years’ time.
Q315 Lord Hannay of Chiswick: What you said seems common sense entirely, that one aspect of an external energy policy which will strengthen the European Union’s hand in its dealings with Russia will be a greater diversification of sources of supply and, per contra, the more we depend on the one source or supply or, at any rate, pipelines which run through one source of supply, the weaker our position is. This is so obvious. Why is it not obvious to all of our Member States, and why do they not draw the appropriate conclusions from it?

Mr Cooper: I think some of them have drawn that conclusion, but from drawing the conclusion intellectually to spending very large sums of money on implementing that takes time. Although some of them have drawn that conclusion, I am not sure all of them have drawn that conclusion yet. I could give you a list of other things where more co-operation would be mutually beneficial but do not occur. Lord Roper would be familiar with the case of weapons procurement as a very obvious case where real gains are missed.

Chairman: Indeed.

Q316 Lord Hamilton of Epsom: That is another debate. You said that an external energy policy is inevitable in a few years’ time, I am not absolutely certain I would go along with that because I think national interests override an awful lot here. I wonder what you would gain by a common approach. I do not think energy is different from anything else. I can see people being unnerved about gas being switched off but, let us be honest, it was switched off for people who were getting subsidised supplies of gas. There is no obvious reason why Russia should subsidise gas supplies to the Ukraine, we can see the historical reasons for doing it. Maybe I would have gone about it differently if I had been the Russians, but I think I would have been quite keen on selling them gas at the market price as the market price has gone up.

Mr Cooper: This is the point which Mr Putin makes to us also!

Q317 Lord Hamilton of Epsom: I think the market is working. It may be that the EU has not got a hold on it, but it does not mean that it is inefficient. It is quite interesting, you switch off the gas in the Ukraine and then people start putting LNG terminals in so start paying a price for it absolutely at once. There is no real reason to believe that the Russians are going to shut off gas supplies for some political reason because it would seriously affect their cash flow. I think the market is working, I am not absolutely certain whether you meddling in it will make it any better.

Mr Cooper: In most cases it is not the EU meddling in it because the gas terminals are being built on a national basis.

Q318 Lord Hamilton of Epsom: That is the point I am making.

Mr Cooper: What happened with Ukraine was there was a dispute between Russia and Ukraine, and you are quite right that the Russians had legitimate points, not least about the amount of gas which was being siphoned off in Ukraine but, nevertheless, we got caught in the crossfire in that because you cannot switch off the gas to Ukraine without switching it off for European countries as well. Although you are right that switching the gas off was a mistake from the Russian point of view because after the long years in which Russia had established great credibility as a reliable supplier, it damaged its reputation very badly at that moment, but it made everybody conscious of the risk and the risk is of the crossfire. You are right, it would be irrational for Russia to do this, but sometimes countries are irrational and the consequences of that are quite serious.

Q319 Chairman: On energy security, have there not been problems with the supply of oil to Lithuania or one of the Baltic States by the Russians at several stages? That is one of the few cases where there has been direct action against a Member State of the European Union, as I understand it. I wonder if we can be told a little bit about how and why the Union reacted.

Mr Johns: That is a branch to the Druzhba pipeline which leads to Lithuania and to the Mazeikiai refinery. It was closed down because the Russians said there was a leak in the pipeline due to cracks. They carried out a feasibility study and apparently came to the conclusion that it was neither technically nor commercially feasible to repair the pipeline. To my knowledge they have not yet supplied that feasibility study to the EU or the Lithuanians, although we did ask for it at the Mafra Summit. The problem is—apparently this is the Russian argument—that the pipeline is privately owned by a Russian company and you cannot, therefore, force a private company to repair at its own cost a pipeline which is not commercially feasible. This is the Russian argument.

Mr Cooper: Perhaps there is another point I might have made in answer to Lord Hamilton. There is some concern about the reliability of Russian supplies, not just because of political considerations but because of lack of investment. That is a point we have made several times to the Russians and I think they have realised this and are thinking about it. Whether they are doing something about it is not yet clear. There are still good long-term reasons for giving oneself alternatives. That is one reason why it would be very nice to have a better relationship with Iran.
Q320 Lord Truscott: Moving on from energy to a less controversial area, European defence! Perhaps you would like to comment on how the EU embryonic defence role, security role, is compatible with Member States’ commitments to NATO, particularly given the background of President Sarkozy’s recent comments that he would like to see the EU’s defence role enhanced under the French Presidency, I wonder whether you could comment on that and also, how the EU should respond, if at all, to Russia’s proposed withdrawal from the CFE Treaty.

Mr Cooper: To start with the second one, which is slightly less complicated, that is not a matter which is handled in the European Union. Nevertheless, it has an impact on European Union’s relations with Russia. They have “suspended” for the moment, whatever that means, but I do not think in the short run withdrawal from the Treaty would pose a direct threat to the European Union but, nevertheless, it is something people feel more comfortable with. We saw the CFE Treaty as part of the structure of the end the Cold War, which provided for transparency in military arrangements and I think made everybody feel much safer. It is very undesirable that Russia should withdraw from it. I think that is the view shared right across the European Union.

Q321 Chairman: The EU does have a special representative in Moldova, and it is possible that if one was able to resolve the issues about the Russian forces in Transnistria, that might create a situation, given the withdrawals of the Russian forces from Georgia, whereby the NATO members would be able to ratify the modified CFE Treaty and that might change the environment in which Russian attitudes might occur. Is there not there also an interaction between EU activities and the CFE Treaty?

Mr Cooper: Yes, the CFE Treaty and all of those arrangements are the context within which we operate. We would like to see the Treaty ratified and continue in existence and, indeed, we would like to see some kind of a deal on Moldova and Georgia. The USA has been making some quite imaginative proposals to try and meet the problems the Russians have raised. Although we are not directly involved, the people who are involved in the US normally keep us informed about what they are doing and we hope very much that they succeed. On the first question, it would be very strange if NATO and the European Union were in some way incompatible or in contradiction with each other because the overlap of the membership is so enormous; and indeed they are not. Occasionally you get elements of institutional rivalry but that is not very serious. In practice we cooperate extremely well together, with one reservation, the reservation being connected to Turkey. At the level of our secretariat here and the NATO secretariat, for example, we work extremely closely on arrangements for the possible future situation in Kosovo where the European Union would be responsible under the Ahtisaari proposals for a very large deployment in the area of police, and NATO would be responsible for KFOR. It is clear there is a boundary line between those two responsibilities where you have to have rather precise agreements and you also need arrangements for intelligence sharing and so on. All of those things worked out extremely smoothly. In another way we operate what is now a rather small military mission in Bosnia through SHAPE with Deputy SACEUR as the Operational Commander. That works perfectly well. From where I sit, although there is a lot of talk about it, I see an extremely good relationship with NATO. The European Union does not do defence in the sense that European military activities are not there to do the classical defence task of defending national territory; that still belongs to NATO. In terms of other military operations, it is not that we are fighting over who does what, there is more than enough to go around. On the contrary, it is a strength for the West that there is more than one option available. For example, we are about to make a deployment to Chad, which has the useful function of providing a backstop for the UN deployment in Sudan, in the Darfur area. Chad would probably not accept a NATO deployment—I do not know why, but the image of NATO is different from that of the European Union—whereas they are quite happy to accept European Union deployment. That seems to me to be a good thing for the West, that one has got alternative bodies available which you can use.

Q322 Chairman: On that particular point, we are obviously following this in our other work and we had a letter saying that you had a force generation conference here on 9 November as far as Chad and deployment was concerned. Has there been any public statement as to how successful that meeting was, and what are the probabilities of deployment under the Irish General?

Mr Cooper: I do not think I am sufficiently up to date on that. I know there are still a couple of shortfalls which, as a matter of fact, are the same shortfalls one finds with almost every deployment and you can probably guess which ones they are.

Q323 Lord Hannay of Chiswick: Helicopters.

Mr Cooper: Helicopters, yes. (There followed a short discussion of the record)

Q324 Lord Hamilton of Epsom: You will be aware that at the moment in the United Kingdom there are furious rows going on about the overstretch in British Forces. With the combination of Iraq and Afghanistan simultaneously, this seems to be too
much for what we have got. At the same time, on a rotating basis Britain contributes to the European Battle Group, which has the unique thing that it seems to never be designed to go into battle, but that is another question altogether. What would happen if it was deployed, because I do not think we could meet the commitment we have undertaken to do because there is a serious amount of double-hatting, if not triple-hatting going on?

Mr Cooper: I do not think I have the expertise to answer that question, which you can put to the British Ministry of Defence. They would probably be better than me to answer that. The only comment I would like to make is Britain is not the only country that is overstretched at the moment.

Lord Truscott: There does seem to be a debate about the way forward for European security. The French seem to be pressing for more institutional changes and the British Ministry of Defence are always saying the focus should be on developing the capability. I wonder what your view is on that. Secondly, another concern vis-à-vis Europe and NATO is the whole question of avoiding duplication, and is there a danger that some of the functions could be duplicated?

Q325 Chairman: We must be a little careful we do not go too far away from our relations with Russia. Mr Cooper: I do not think we know exactly everything that the French have in mind at the moment, but I know when President Sarkozy put forward these ideas, the sentence has always had two halves: one is about strengthening EU defence arrangements and the other is about a stronger French contribution to NATO. I think those two things would be in balance.

Q326 Lord Hannay of Chiswick: In this area of NATO enlargement, possible; missile defence, on the table already; multilateral disarmament instruments under stress whether it is CFE or INF or all these other things, do you not feel there is a pretty strong risk, if not even a likelihood, that the Russians, who seem to be reverting to many old practices, will revert in this area to attempting to split the Europeans from the United States? If so, do you think the Europeans are in a mode to resist that attempt to divide them or are they likely to be a victim of it? How does the prospective election of a new American President affect all that?

Mr Cooper: Yes, right! While you were speaking I was thinking, I am not sure if the US is not split on some of these questions itself. I think probably the best answer I can give is to say that this is not my daily bread. These are things which determine the environment within which the EU operates with Russia, but they are discussed essentially in the Alliance rather than here. They have a big effect on the atmosphere in all kinds of way, and probably they have an effect on other things where the European Union is very deeply engaged, like the Kosovo question. It is not really my business, so I do not think I can give you a respectable answer.

Q327 Lord Hannay of Chiswick: Let us switch away completely from that to the PCA and the role it currently plays and the role a new PCA could play in the EU-Russia arrangements. To what extent do you think it is a high priority to negotiate a new PCA, or is it the case that the common spaces and the existing PCA, which, as I understand, will just go on providing an institutional framework for as far as the eye can see, are, in fact, a reasonably satisfactory way of managing the relationship now? To what extent do you think the tensions which have arisen in EU-Russia relations in recent months make it very dubious that a new PCA of a meaningful kind can in the short-term, or should in the short-term, be negotiated, or is it a very high priority indeed?

Mr Cooper: I will give you my answer but maybe David would like to add something. I think we can probably live without negotiating a new PCA and that probably goes for the Russians as well. There is still more to be done which can be done under the existing PCA, which is by no means exhausted. This was an attempt to see if we could go further. Well, this may not be the right moment for it. In due course it would be desirable, but I do not think it is vital.

Mr Johns: I would agree that it is not necessarily a tragedy if we do not negotiate a new PCA soon. The current PCA will be rolled over and will continue to apply. We have the road maps that were agreed, which have taken our co-operation even further, and they can continue to be implemented. The only disadvantage, of course, is road maps are not legally binding. The interest in a new PCA would be to have some legally binding framework where we could then further intensify our co-operation with Russia. On the other hand, I agree with you entirely that the current atmosphere is not conducive to starting negotiations at the moment. We still have a number of problems which need to be addressed, not least the question of Polish meat where there may be a possible opening in the future with the new Polish Government, but we have to bear in mind that Russia also is in a pre-election period and I do not see much happening on the PCA front in the next few months, certainly not up to the presidential elections. You never know, there might be some miraculous development, but I do not see it coming for at least the foreseeable future. We will continue to co-operate nonetheless on the basis of the Institutional Framework that is in place.

Q328 Lord Hamilton of Epsom: If the existing PCA is legally binding, I cannot believe the Russians have gone along with all the things in it, so what are we
doing to legally enforce the breaches of the existing one?

Mr Johns: Interestingly enough, the Russians present themselves as being one of the few countries in the world that respect international rules. They turn around and accuse the EU, the US, et cetera, of not respecting international rules, they are the only ones sticking to the rules, they say. On the PCA, of course, we have various possibilities to discuss areas where, for example, the Russians do not live up to their commitments, but it is true, the possibilities for forcing them to act are very limited.

Q329 Lord Hamilton of Epsom: Why do we make them legally binding if we cannot legally enforce them?

Mr Cooper: It is a different level of commitment and one hopes that when people accept a legally binding commitment they take it more seriously. The Russians do take legal obligations seriously.

Q330 Chairman: On that question of the negotiations, we have been impressed by the size of the Russian mission here to the European Union. As we were waiting to come in to meet you, we saw Ambassador Chizhov who was waiting for a number of ministers from Moscow who were coming to take part in discussions on the common space dealing with justice and home affairs matters today. There is a lot of business being done. How do you see the balance of the business which is done between the EU and the Russians in Brussels and the EU and the Russians in Moscow? Do you see any changes in that relationship?

Mr Cooper: In terms of formal business, numbers of meetings held, Russia is probably number one, more than with the USA. With the USA there is a much more informal relationship and a rather more productive relationship as well. As between Brussels and Moscow, I see mostly Brussels, I do not know how much there is in Moscow.

Mr Johns: My viewpoint is also entirely from the Brussels' viewpoint. The Council, of course, does not have any representation in Moscow, which is the strength of the Commission because it has a delegation there, and they have very strong contacts and daily contacts with the Russian administration.

Q331 Chairman: On that point, and perhaps straying into the second inquiry which we are undertaking on the Reform Treaty, I wonder if I could ask you whether once there was the existence of a European External Action Service, would that mean that almost automatically in any other major country, such as Moscow, the presence of the European External Action Service would mean that the Council, as well the Commission, would be represented in somewhere like Moscow?

Mr Cooper: (There followed a short discussion off the record)

Q332 Lord Hamilton of Epsom: This question is about the political situation in Russia, which seems to be one of the weaker areas of the four common spaces. Are we making any progress on the rule of law, democracy, human rights and good governance?

Mr Cooper: No, I think is probably the short answer to that.

Q333 Lord Hamilton of Epsom: That is what I had imagined.

Mr Cooper: I was going to say most people would say the situation has got worse, on the other hand, I think a large number of Russians would probably say the situation has got better. At least in a free and fair election it is pretty clear that Mr Putin could be elected for whatever he wanted to be elected for. It is also clear that Russians have very bad memories of the 1990s, which they saw not as being democratic but as being chaotic. Nevertheless, the kind of unhealthy way in which it is difficult to tell whether you are talking to the Russian business community or the Russian political system and the extent to which it seems possible to exploit the law to attack political enemies, none of those things make Russia look very much like a liberal democracy at the moment.

Q334 Lord Hamilton of Epsom: And poisoning people in London!

Mr Cooper: There is that also, yes, and not just in London as well.

Q335 Lord Hannay of Chiswick: Quite a lot of the people who we have taken evidence from have suggested that the European Union's approach to this democracy, human rights and other agenda has proved a rather misdirected and mistaken one in the past, as well as being ineffective, in the sense that it was directed at the concept of Russia becoming more like us, the concept that the Russians would become just another European country. With that in mind, much of the spirit of the Copenhagen criteria hovered over it and this, it has been suggested to us, is a mistake, an overambitious approach which has not worked and is now rejected effectively by the Russians, whether you fly under a rather peculiar label called "sovereign democracy" or whatever it is, it is not what they are doing. Do you feel some redirection of this human rights, democracy, good governance, rule of law agenda is desirable? If so, should it be explicit or should it just come about by a process of osmosis, by a shifting of emphasis? If so, how much of it do we retain in a future relationship if we do decide to shift away from simply trying to make the Russians more like us?
Mr Cooper: It is very difficult to get any other country to do what you want, to become more like us, which I think was the answer I gave to the first question, it is a natural thing for everybody to want because it is easy to deal with people who are like you. Expecting that that is what is going to happen though is a different thing. What is the most effective way of promoting those ideas, democracy, the rule of law? I do not think there is a straightforward answer to that, it depends on particular countries. To some extent, I think intellectually the idea of democracy and the rule of law has won. In some ways they promote themselves because it is what lots of people want and lots of people expect. There are some times when from outside you can contribute to that process, but the primary drive for that has to come from within countries. The EU tries to help that process by supporting NGOs in Russia. How effective that is, I do not know. I guess you may have to talk to the Commission about that because they are the people who are running the programmes and who know what is going on.

Q336 Chairman: We are going to see Mr Franco when we are in Moscow and I think it will be discussed there rather than with the Commission here.

Mr Cooper: He would be the person who would know best. Perhaps I will add one other personal hobby horse, which is that if Ukraine continued in the direction that it seems to be going in, it is certainly a more liberal country now than it was and if it could establish a well functioning democratic government and a rule of law, I think that would have a very big impact on Russia; but directly changing Russia from within countries. The EU tries to help that process by supporting NGOs in Russia. How effective that is, I do not know. I guess you may have to talk to the Commission about that because they are the people who are running the programmes and who know what is going on.

Q337 Lord Hannay of Chiswick: Do you think we should state that is no longer what we are trying to do or do you think it should just be allowed to happen?

Mr Cooper: I do not think we would be allowed to state that because throughout the European Union, although there are variable opinions, it is not what governments want. We have to try and do it in a way which is practical and does not seem aggressive to the Russians.

Q338 Lord Hamilton of Epsom: When the British Government reacted robustly to having a Russian citizen poisoned in London, I do not think there was ever any hope that we were going to get anybody extradited for doing it. On the other hand, it had to be helpful in terms of making the Russians think twice before they would do the same thing again.

Mr Cooper: Yes. I think everybody who deals with Russia would say that one ought to be absolutely clear and firm about principles, preferably in a way which is not aggressive and provocative, but you need to continue to make the points. (There followed a short discussion off the record)

Q339 Lord Truscott: I hope in coming years we will not be asking, "Who lost Russia?" because it seems to me there was an opportunity in the early 1990s to send Russia on the path of Western style democracy, but clearly that window has closed now with Putin, although there is still the opportunity to develop the market economy. I think that is an historical opportunity which was probably lost in Russia’s case.

Mr Cooper: I think this is a world of second chances and I do not think anything is closed. Russia is very different now from the way it was in the 1980s, for example. In the 1990s, undoubtedly there were a gigantic number of mistakes which were made. There are a large number of countries which have moved from authoritarian systems to democracy. Maybe naively, I do not believe it is going to remain exactly where it is now.

Q340 Lord Truscott: I live in hope, but it is just the timeframe you are looking at.

Mr Cooper: The timeframe will be much longer, but I do not know about that.

Q341 Lord Hamilton of Epsom: We do not know and windows that shut open again. If we are developing a middle class in Russia, then in European countries the middle classes want votes and some influence over the country in which they are living. If that emerges, I think democracy will follow.

Mr Cooper: There are schools of thought which say that you can develop a stable authoritarian plutocracy, but we will see.

Q342 Lord Hamilton of Epsom: The jury is out.

Mr Cooper: I also think that life is more complicated than that and things never go quite as they are predicted. The individual wish of individual people to control their lives in the end has an impact. I do not think it is a question of who lost Russia because it really has changed a lot. Although Russia sometimes takes rather an aggressive stance, it does not give the impression that it is planning to invade anybody and, indeed, most of what they talk about is exercising power through economic means. That seems relatively healthy.

Chairman: Mr Cooper, thank you very much indeed for your time and for what has been a very interesting and informative session. Thank you.
FRIDAY 23 NOVEMBER 2007

Present
Hamilton of Epsom, L
Hannay of Chiswick, L

Roper, L (Chairman)
Truscott, L

Examination of Witness

Witness: Mr Patrick Child, Head of Cabinet of the Commissioner for External Relations, Benita Ferrero-Waldner, RELEX, examined.

Q343 Chairman: Good morning, Mr Child. I wonder whether we could begin by talking a little bit about the present basis for the arrangements and the links between the European Union and the Commission and the Russian Federation. I wonder if you would be able to talk about the sorts of projects and technical assistance programmes which we are carrying out and how far this will change with the new European Neighbourhood and Partnership Instrument as part of the financial perspective.

Mr Child: Thank you very much. I know you have already had a session with some of my colleagues yesterday, including the Director General in DG RELEX.

Q344 Chairman: Indeed, it was very helpful.

Mr Child: I will try and add something to what they have said. On your first question about the sorts of projects we are supporting in our relations with Russia, I guess things are in quite a phase of change as Russia becomes a more developed and economically successful partner. The need for the sort of development-related technical assistance we were doing under the Tacis Programme is evolving quite quickly. Under the new European Neighbourhood and Partnership Instrument we will be reducing quite substantially the overall financial volume devoted to our Russia programme. In the new period, we will concentrate on three or four areas. Firstly, education, people-to-people contact and scholarship programmes, and that sort of thing and, secondly, on the work we have been doing in Kaliningrad, supporting the economic and social integration of Kaliningrad into its new immediate neighbourhood. That has been a particular focus of the work of Mrs Ferrero-Waldner as Commissioner. We are also encouraged by the recent signs that the Russians themselves are ready to contribute to the Cross-border Co-operation Instrument which we have in place under the Neighbourhood Instrument and that, therefore, again, will be an important theme. Another area I would mention in the context of the Northern Dimension, is our work on environment issues, particularly in the North of Russia and the Baltic Sea, and I hope that will continue. We are also doing a number of things through our separate Human Rights Instrument in terms of supporting the rule of law, democracy and civil society in Russia, which I think is an increasingly important thing given the recent political developments. Those are the broad lines, but if it would help the Committee, I could certainly ask our services, if they have not already done so, to give you some further background information.

Q345 Chairman: Yes, we have had a copy of this report and we are going to be in Moscow in December and we have an appointment to call upon the Head of the Delegation, so we will have a chance then. We saw his deputy yesterday because he was with your colleagues who we met in RELEX.

Q346 Lord Hannay of Chiswick: Have you had any real problems in handling your programme to work with NGOs as a result of the Russian tendency to clamp down on NGOs generally and, in particular, NGOs who have anything to do with foreigners and, particularly, NGOs who have anything to do with foreigners who would convey money to them? Have you had any problems in that area? Secondly, have you conducted any evaluation of what the consequences of these programmes you have described could be, what the effect has been? It does not seem to us from the evidence we have taken so far that Russians generally have a very benign view of the European Union any longer. Have you conducted an evaluation of that?

Mr Child: It is a difficult area and it is an area which has not become easier recently. There has been a particular project, which may be familiar to the Committee, that we have supported, the Moscow School of Political Studies, which I know has got a lot of sympathy. It has not only been challenging for us to find ways through our financial procedures to ensure the level of support which we believe to be politically justified for that organisation, but also the climate in which it works politically in Russia has not been straightforward. At the last summit with the Russians a few weeks ago, President Putin raised a particular concern about a somewhat similar project we were doing to look at human rights’ issues based in St Petersburg. He was questioning whether this was an initiative which the EU should be supporting and went as far as to suggest that maybe Russia would consider, in return, setting up a similar or other sort of organisation in the EU to look at those...
sorts of issues in the EU. I think the response from President Barroso was, “Well, we have a free society and if you wish to fund such an organisation, that would be perfectly acceptable” we will see where that will lead. As to the question of whether we evaluate the global impact of these sorts of programmes, I am sure it is a drop in the ocean and Russia is a very large and complex society. We have not had the sort of scale of resources to make a very seismic change to the way that these issues are pursued by the Russian Government. Of course, we do have procedures where each individual project is assessed against its objectives and the evaluation of the results. I do not have details of all that, but it is a very difficult environment and it would be foolish of me to pretend that things have got easier in recent months, particularly as the political climate in Russia has developed in light of the presidential elections.

Q347 Lord Hamilton of Epsom: I am interested in the work you are doing on Kaliningrad. Clearly it is in need of help at the moment, but if you are successful in what you are trying to do in linking up locally and whatever—I hesitate to say too successful—then there may come a moment where it is looking like a Hong Kong of Russia, and will that cause problems for Russia?

Mr Child: In all our discussions with the Russians on Kaliningrad, we have stressed, and will continue to stress, the importance of Kaliningrad as part of Russia and that there is nothing in our strategy which intends to call into question the territorial integrity of the Russian Federation. That is a very important message in order to begin a discussion with our Russian friends, not only the ones in Moscow, but also the authorities in Kaliningrad itself where there is a very strong interest. Something Mrs Ferrero-Waldner has sensed clearly in her several visits there is the willingness of the local leaders to take advantage of the economic opportunities which their situation offers in relation to the enlarged Union. There is no prospect of a more fundamental change in the status of Kaliningrad as part of Russia and, of course, to some extent it is for the Russian authorities to decide what sort of economic and social regime to allow to develop there by comparison with other parts of the Russian Federation.

Q348 Lord Hannay of Chiswick: Can we ask you a couple of questions now about the institutional framework of the EU-Russia relationship currently, that is to say things like the PCA, the common spaces, and the Northern Dimension. Are they working reasonably well? What are the strengths and weaknesses of the framework which exists, and what scope is there for improving it without going outside what is currently there? The second half of the question is what priority do you, therefore, attach to negotiating a new institutional framework for the relationship? Is it a high priority, because what you want to do, what the EU wants to do, cannot be done without a new framework, or is it a lowish priority to be pursued as and when circumstances become a little bit more propitious than they are at the moment?

Mr Child: Firstly, I would say that any institutional framework is as successful or as unsuccessful as the political environment in which it is expected to operate. Against that background, I think the PCA and the common spaces are providing a good basis for the relations that we have with Russia. It would be wrong to conclude from the difficulties we have had recently in the discussions on the new PCA that somehow the relationship with Russia had ground to a complete halt. We continue to work and co-operate with Russia on a very large number of issues through, in particular, the PCA and its various sub-committees, also with the specific Northern Dimension Framework in the north and with the framework of the four common spaces. Given the political environment today, both in terms of the EU’s policies and attitudes towards the relationship, which I hope we can come on to in some subsequent questions, as well as the political climate in Russia itself, the present framework is working as well as can be expected. The PCA is, however, very much a product of the time when it was negotiated. It was at a moment when Russia was very much struggling with the challenges of transition, not benefiting from the economic strength which flows from its present energy relationships in particular and, therefore, at a moment when perhaps the readiness on the Russian side to sign up to the core principles and common values, which is very central to the present Partnership and Co-operation Agreement, was greater than perhaps would be the case today. Similarly, I think at the time the political mood in the EU, in the face of the very exciting changes which were taking place in the continent and the opportunities that were perceived there, was perhaps a mood of optimism about the speed and direction of political reform in Russia, which has not completely materialised since. Therefore, if we now take another look at this relationship, clearly the whole discussion on whether we really have a strategic partnership based on common values is one which I think merits a bit more discussion. My first answer is we should not think that because we do not have a new PCA there is nothing to be done with Russia, on the contrary, the relationship will continue on the present basis and, in particular, until the present historical milestones in Russia are behind us, I suspect. However, it is useful, for the reasons I have indicated, to have another look at the relationship and whether we have got the balance right, and I think the discussions on a new PCA provide a good vehicle for that to happen. For example, are there issues like the environment, like
energy, which I would hope would have a more prominent place in a new agreement than they do at the moment? It is also quite important to avoid the EU looking as if we want a new PCA at all costs because I suspect we could then find ourselves in an environment where the costs turn out to be quite high, so it is important we keep some balance in that. That is where the EU consensus is today, that we will continue to work within the existing framework, giving emphasis to those things which are important to us at the moment and also present common interests. We do have the important provisions on the shared values, which are things we must keep reminding the Russians about, particularly against the background of various recent developments and that when the political mood is right for us to return to perhaps a more serious discussion on a new framework relationship, then the new PCA text, or something like that, will be the basis for those discussions.

Q349 Chairman: On the negotiations with the Russians and the amount of business that goes on, we have been quite impressed while we have been here by discovering the size of the Russian mission to the European Union. Presumably most of the work it does is with different parts of the Commission, it tends to be Pillar I business on the whole. How much of the totality of work is done here and how much of it is done through your own mission in Moscow? Is it possible to get an assessment of the relative weights of where business is done? That may be an unfair question.

Mr Child: It is difficult to give a scientific answer.

Q350 Chairman: Yes, impressionistically?

Mr Child: Certainly there is a very strong Russian mission here, just as we have a well developed and well resourced delegation in Moscow and each contributes in a constructive way. There is also the Member State that has the Presidency, particularly in terms of preparing big set piece meetings like the Summits and there is always a big input from those countries. The emphasis of the political work would be coming through the mission here directly to the Commission Services and also to our colleagues in the Council Secretariat when we are talking about some of the CFSP issues which they work on, whereas the more day-to-day co-operation, implementation of our technical-assistance programmes and other financial programmes, there is more emphasis through our mission in Moscow. That is a crude way of looking at the division of labour but, of course, when we come to preparing a Summit, it is all hands to the pump and everybody is involved in it in a very energetic way.

Q351 Lord Hamilton of Epsom: In which areas of policy does the EU most need to present a united front in relationships with Russia? What does the EU have to offer in the context of negotiation? How best can Russian thinking be influenced by the EU?

Mr Child: There was a useful discussion of EU-Russia relations at the informal “Gymnich” meeting of foreign ministers at the end of the summer where there was, more than I have certainly noticed in the past, a shared sense that we urgently need to present a clearer common front to Russia on a large number of issues. Maybe the background of the changes flowing from the EU enlargement, both in terms of attitudes within the EU and also the way the Russians perceived them has made it even more necessary for us to work together on presenting a common front to Russia. I guess the area where most specific questions and issues arise is in the commercial relationships which some Member States have, particularly in the energy sector, but perhaps not only there, where some Member States are more ready to tolerate certain behaviours on the part of Russia than others because they have a different appreciation of the commercial dimension of the relationship. I would say that was perhaps the economic and commercial area where the divergences in Member States’ positions are most felt. Although, of course, the result of that is you can see differences also in their position on some of the other issues, like foreign policy or, indeed, the core values we share with Russia. Across the board there is a need for greater coherence and commonality of position among Member States. I very much welcome that there is a growing awareness of Member States of that need and I look forward to that awareness of the need being translated into a reality of fact.

Q352 Chairman: Can I ask you a follow-up question to that because we had a meeting this morning with five of the ambassadors from Member States to the PSC, including the British one. There were two quite interesting things that they said: first of all, the fact that they very rarely did have a discussion about policy in Russia, they discussed immediate particular points obviously and Russia came up in that direction but, secondly, they also felt that because of the structure of the Union, foreign policy was being done there and energy was being done somewhere else, therefore not only was there not even a full discussion within the Second Pillar as to common policies, but even more so at a macro level, bringing together the different dimensions of the relationships of Russia, not only political, it was that you might make good remarks at a summit, you might make good remarks at a Gymnich, but where was it that this could be put together as a common basis for analysis and reaction development?
Mr Child: I am not surprised that you got that impression from that group of people. Indeed, there are questions which I hope will be easier in the future when we have greater coherence in our external relations which the new Reform Treaty should bring, which will help to bring together the different components of relations with important partners like Russia. There are issues which are not best addressed to me, but to colleagues in the Council about in particular the relationship between the PSC and the Coreper, which has a broader responsibility, for example, for the preparation of summits, including the summit with Russia. I would certainly encourage anything that can be done within the structure of discussion within Member States to find a better place for those discussions to be conducted. I think the reality is that it does only come together at the level of ministers in the General Affairs Council and, even then, they may not have the full awareness of what is being discussed in energy or the Interior Minister’s Council or other formations of the Council dealing with different topics.

Q353 Lord Hamilton of Epsom: You referred earlier to enlargement, can I ask it the other way around. How are the Russians reacting to the fact that enlargement gets nearer and nearer, enclosing them almost, their borders certainly on the west? Mr Child: The Russian response to enlargement, and a desire to be more deeply involved and consulted in the enlargement process and decisions, has been a big feature of the EU-Russia relations in the eight years I have been following them. It is certainly true that some of the more acute discussions we have had recently over, for example, the Polish meat issue or, indeed, the Estonian War Memorial, are part of a broader sense of unease in Russian political circles about what the process of EU enlargement means for what they have traditionally considered to be part of their immediate zone of influence. I guess similar issues arise in the context of NATO enlargement, although that is not something for which we have responsibility, but it is very present in Russian thinking. It also explains why it is so difficult for us to engage in the sort of discussions which I would like to see with Russia on some of the frozen conflicts and issues that arise in the context of our common neighbourhood and in the implementation of the European Neighbourhood Policy in some of the countries of Eastern Europe.

Q354 Lord Hamilton of Epsom: Of course, Poland and the Baltic States are already in, but how about future enlargement? How are they reacting to other countries being candidates in future tranches? Mr Child: At the moment we have commitments for enlargement in the Western Balkans. Of course, we have quite a difficult discussion with Russia at the moment, specifically over the question of the status of Kosovo, but I think that has got less to do with enlargement than broader issues. There are accession negotiations ongoing with Turkey and I am not aware that Russia has a particular axe to grind there. If we were ever to move to a discussion about other candidates, countries that are today covered by the European Neighbourhood Policy, then we might, I guess, provoke some other Russian reactions.

Q355 Lord Hamilton of Epsom: Would you consider the Russian concerns legitimate? If Ukraine, for instance, at some stage said they wanted to be a member of the EU—in theory, that is subject to discussion between the EU and Ukraine, Russia are not a party to that—would we loop them in on the basis that they have a legitimate concern? Mr Child: Few days go past without Ukraine saying they would like to be a member of the European Union. The European Union’s position on that is clear and well established that the focus of the relationship today is the European Neighbourhood Policy. It is perhaps easier to answer that question in relation to how we have handled past enlargements where, indeed, the message from Russia was, we want to be more directly involved in discussions on how Poland or other countries should be brought in and what would be the consequences for Russia on trade in certain key sectors, and whether there are things we should then be discussing with Russia about mitigating the effects of accession in certain areas. The EU has said in response to those Russian concerns, “Of course we are ready to talk to you at any time about the process of enlargement we are working on and we are also open to a discussion on specific issues, but that we were convinced overall the process of enlargement is beneficial for the European Union, for the candidate countries, but also for Russia”. We sought to convince the Russians of those benefits and I think we still have some convincing to do, although the temperature of that debate has diminished.

Q356 Lord Hamilton of Epsom: They have a legitimate concern but they do not have a veto. Mr Child: We would expect them to take a very close interest in the enlargement process and in the consequences that it would have for them, but that is a different question from giving them a direct seat at the table when we are discussing with the candidate country the terms and conditions of its accession into the European Union.
Q357 Chairman: The Kaliningrad transit case was a very particular case and it was unlike almost any of the others because it did have an implication, presumably, for Russia.

Mr Child: Yes, the Kaliningrad transit case was very interesting because it was also linked with the immediate conditions of accession of Lithuania in particular, but also Poland, and also the aspirations of Lithuania to become a full member of the Schengen system within a reasonable time. Therefore, the negotiation that we had to lead at that time was to convince the other Member States that the special regime with the special trains which we were introducing for people transiting from Russia to Kaliningrad was compatible with a future Schengen visa environment while, at the same time, for Russian public opinion demonstrating that there was not a fundamental change which would cut off this important part of the Russian Federation from the rest.

Q358 Lord Truscott: On energy policy, I know this may be more appropriate for Commissioner Piebalgs and his cabinet to a certain extent, but obviously I am interested in your input and RELEX’s input into this. What do you think are the obstacles to a common EU energy policy? Do you think the focus should still be on trying to implement the Energy Charter Treaty as far as Russia is concerned, which seems to be a bit of a dead duck at the moment, or should they be focusing on a different approach? What issues do you think will arise with the whole question of unbundling of supply and distribution assets and the new Energy Directive which is being discussed?

Mr Child: I would be very pleased if you were able to talk Mr Piebalgs and his colleagues because they are also involved in this. We have a fairly clear understanding of what we would like from Russia as a partner in energy, where we want to have reliable supplies which are not influenced by political considerations, but are based on sound and reliable commercial relationships. We would like to have the same sorts of opportunities and access for EU firms and Western firms to get involved in the Russian markets as they have given our open markets in the EU. We think that is particularly important because what we think is needed in Russia is investment and upgrading of the infrastructure, transit infrastructure in particular, which probably requires the capital investment of outsiders and will not only come from inside. If that investment is not made, then the risks for future supply for the EU’s needs are that much greater. Whether, given the political baggage that it now carries with it, the Energy Charter is going to be the vehicle which will help us to deliver that, I do not know. I think it would be wrong for us to abandon that as the central element in our discussions with the Russians, but it may be that at the end of the day we can achieve the same results in other ways and for me that would be very acceptable. If I could answer at least two sentences off the record on the unbundling story and then I will give you another answer. (There followed a short discussion off the record) It was very interesting that the most prominent public reaction to the proposals the Commission made in September on unbundling, which were primarily intended to improve the operation of the internal market, was the possible external consequences and, in particular, what it meant for Russia. If the Commission set out to include some quite tough provisions on reciprocity and what we would expect from third country actors becoming involved in the EU internal market, that was a deliberate and quite important political signal in order to create the conditions within the EU which would make those proposals domestically acceptable.

Q359 Lord Hamilton of Epsom: We were told earlier that in terms of the internal market there should be plans to share, so if somebody gets their gas supply from Russia shut off, they can be bailed out by their neighbour. On the ground, are we making any progress on that front?

Mr Child: I confess, I am not an expert on the details of the interlinking between different energy markets and the debate on strategic reserves, which is sometimes part of the same thing. It is a growing area of discussion, but I think the existence of strong national monopolies in some Member States is a break on progress in that direction, which is precisely the reason the Commission has made the unbundling proposals that we have.

Chairman: Mr Child, thank you very much indeed for taking the time to come and give evidence to us here this morning. It has been very useful preparation for our visit to Moscow next month where we hope to pursue the matter and prepare our report in the early part of next year. Thank you very much indeed. We are most grateful.
1. This memorandum addresses one aspect of the relationship between the European Union and Russia—energy policy.

THE EU OBJECTIVES

2. The objectives of the European Union in respect of energy policy are threefold: security of supply, climate change and competitiveness. Europe relies increasingly on Russian oil, gas and coal. There are many competing sources of oil and coal supplies, but gas is—and will remain—primarily delivered by pipeline and has high storage costs. As the dependency on imported gas rises, and as the alternative pipeline suppliers to Europe implicitly collude, Russia’s will become correspondently of greater importance. Events in Ukraine in 2005–06, the sometimes difficult relationships between the new eastern European members of the EU and Russia, and the difficulties of meeting domestic demand in Russia combine to create serious security of supply problems.

3. These security of supply problems are likely to be reflected in the price of Europe’s energy supplies, and this will impact on the competitiveness objective.

4. Europe’s focus on climate change is also central to the relationship with Russia. The EU invested considerable political capital in gaining Russia’s ratification of the Kyoto Protocol, and the rapid expansion of Russia’s coal, oil and gas industries will not only reduce the effectiveness of global action to combat climate change, but render EU efforts to get Russia to abate its emissions correspondingly more difficult.

UNDERSTANDING RUSSIAN OBJECTIVES AND STRATEGY

5. Russia’s objectives differ considerably from those of the EU. The political and economic transformation of Russia from the economic turmoil of the 1990s (when it ranked alongside Mexico in economic significance) to a major power has been based almost exclusively on fossil fuels. The election of Putin coincided with a doubling of oil prices, and since 2000 the path has been upwards, solving its foreign exchange difficulties (post the default in 1998), and enabling its new surpluses to underpin an expansion of Russian firms (mainly in the energy sphere) into European markets through a combination of strategic partnerships and acquisitions. It is in Russia’s interest to exploit its fossil fuels resources further—by extracting the highest price. For this it needs captured (and secure) customers, a grip on the supply chain and investment in developing its reserves. Russia is—and will remain for at least the next decade—primarily a carbon economy.

6. In pursuit of this objective, Russia has taken a state capitalist model, so that the political elite, the governmental institutions and the large monopoly corporations have become intimately entwined. Gazprom in particular has approached the European market with a strategy to ensure its markets through a significant element of control. It has had several components. The Baltic Pipeline (Nord Stream) has been part of a strategy to reduce the pivotal role of the Ukraine. The deals with the Caspian States to send gas north through Russia have undermined alternative (non-Russian) pipeline proposals to Europe, and the special relationships with large European companies (notably in Germany, but also Italy, Austria, The Netherlands and France) have been developed. Gazprom has bought into European gas network assets, and it has set up its own direct supply businesses in a number of key markets. Finally, Gazprom and Russia have been developing their relationships with potential competitors—notably in North Africa, but also with Norway.
7. It is hard to see what interest the political and business elites in Russia have in credible climate change policies. Though some areas and industries will suffer from global warming, the carbon economy relies on continuing markets for fossil fuels, and climate change will open up very considerable opportunities in the Arctic north. Ice free ports will transform the export route options, and Arctic reserves will become much more accessible. For these reasons, recent flag planting and the stepping up of Arctic military manoeuvres fit within Russia’s overall economic interests.

THE EU APPROACH TO DATE

8. The difference of objectives is fundamental, and any relationship between Russia and the EU needs to recognise these as given. To date, part of the EU’s failure to make much progress on EU-Russian energy relationships can be explained by three fundamental mistakes. The EU failed to appreciate that objectives differed; it failed to speak with one voice as its members responded to Russia’s strategies on a bilateral basis, most notably in the “special relationship” which has grown up between Germany and Russia; and finally it failed to put its own house in order, to build strategic energy resilience.

9. During the 1990s, when Russia was at its weakest, the EU treated Russia as if it were a candidate member (but without the prospect of membership). In this period—which coincided with the enthusiasm for liberalised and competitive energy markets—the EU focussed its energy diplomacy on getting Russia to ratify the Energy Charter (which it had signed) and in particular the Transit Protocol. The Commission appeared to believe that Russia would open up its pipelines to third party access (TPA), and adopt a liberalised structure. Such a strategy was associated with the assumption that the penetration of European and international energy companies into the Russian market—including the ownership of reserves—was sustainable, given the assumption that Russia would need western company expertise.

10. This was fundamentally mistaken: Russia’s interests in exploiting its resources rested on what it described as “security of demand”, but actually meant increasing its market power. TPA was precisely designed to produce the opposite result—and it was rational and inevitable that Russia would resist the spirit (and indeed the letter) of the Energy Charter and the Transit Protocol. Much diplomatic capital was therefore wasted by the EU.

11. The second failure was that the EU failed to speak with one voice. Faced with increased upstream market power from Gazprom in particular, EU member states have pursued a strategy of bilateral relationships with Russia and Gazprom. The most important has been Germany. The relationship between EON and Gazprom is deep and includes share ownership. The Baltic Pipeline is a German-Russian project (even as other partners enter), it was approved by Schroder, and he is now its Chairman. Though there are different tones in the public handling of this relationship with the Grand Coalition, the relationship continues to deepen. Other member countries have responded by making their own separate deals, as the EU as a whole is hamstrung by the special German relationship. Austria and Italy have been notable in following in Germany’s footsteps, and France has now somewhat belatedly joined this process. As a result, Russia has been able to largely ignore further efforts by the EU to get it to ratify the Energy Charter and the Transit Protocol, and has continued to acquire downstream assets across the EU.

12. The third failure has been internal to the EU. Faced with external dependency and market power, the obvious strategy is to build up internal resilience. Completing the European electricity and gas networks increases the ability to render mutual support in the event of a security of supply physical threat, and it has the additional benefit of reducing costs through the economies from portfolio effects. Strategic gas storage—complimenting arrangement for oil strategic stocks—adds resilience. Diversification of sources of supply and of electricity generating technologies forms a further dimension—in particular heading off yet a further dash-for-gas.

13. The Hampton Court proposals, tabled under the UK Presidency in November 2005, and subsequently partially incorporated in the EU Green Paper 2006 and EU White paper 2007, provided a framework for this internal response. Progress however has been slow—and in the case of strategic gas storage practically nonexistent.

14. The EU has placed more political emphasis on climate change, but the link to its relationship with Russia has not featured in this domain except to argue that increasing investment in renewables and energy efficiency are also ways of increasing security of supply.
17 January 2008

ENHANCING THE EU’S APPROACH

15. In reformulating its energy policy towards Russia, the EU should take the Russian objectives as given, and focus on ways which increase its bargaining power, rather than dissipate political capital on trying to turn the Russian energy market into a mirror of the liberalised and competitive approach which has been advocated (but not achieved) internally. Third party access, unbundling and foreign ownership of Russian reserves are not achievable in the short to medium term.

16. On the assumption that Russia (and Gazprom in particular) will continue to act as a monopoly supplier, and seek to extract the maximum economic rent from Europe from its resources, the EU should actively diversify its supplies. Although the EU advocates a market-based approach, it should take account that this is not a level playing field, but rather a highly politicised energy context, in which the individual choice of companies to invest further in gas generation is likely in aggregate to produce an increased dependency for all. The European energy market needs therefore to price in a security of supply premium, and this is best achieved through a capacity market.

17. The EU should encourage steps to increase the internal resilience of its energy sector, and this requires an acceleration of the integration of European gas and electricity grids, mutual support arrangements and strategic gas storage.

18. The EU’s major political obstacle to increasing its energy bargaining power lies in the bilateral deals and relationships being struck between member states and Russia. “Speaking with one voice” requires EU solidarity, and this should be explicitly woven into EU foreign policy, and through a common pooling of long term gas supply contracts.

19. In engaging at the EU level directly with Russia, reciprocal rules for ownership and investment should be developed. As Russia insists on its legitimate rights to determine how and on what terms European companies operate in the Russian energy sector, similarly it is legitimate to insist that Russian companies adhere to the EU’s internal market rules. Where this involves limiting the abuse of dominance, anti-competitive behaviour and structural rules in respect of unbundling, it should be applied within the EU to Gazprom and other countries. The critical issue here is to address competition in the European market as a whole, and not on a country-by-country basis (as at present). Where Russian companies violate competition law, they should be subject to the same sanctions, even though in the case of Gazprom this may involve directly and indirectly imposing fines on the Russian government in respect to its shares in Gazprom. A first step might be for the Competition Directorate to launch a competition inquiry into Gazprom within the EU markets.

20. On climate change, whilst EU foreign policy should use the various multiple relationships to encourage Russia to participate in a post-Kyoto climate change regime, the EU should also focus on those aspects of low carbon technologies which also increase security of supply.

IMPLICATIONS FOR UK FOREIGN POLICY

21. UK foreign policy in respect of Russian energy is in need of a radical overhaul. The UK has focussed almost exclusively on the Energy Charter and the liberalisation agenda, and to date has offered only limited support (through the Hampton Court process) for the focus of energy negotiations with Russia to be set at the EU level. In particular the UK has put most of its efforts into the unbundling arguments, and as a result positioned itself at loggerheads with France and Germany. It has not sought to forge a common external position with these two major powers towards Russia.

22. Part of the reason for this positioning is historic—with excess supplies and North Sea reserves, the UK has had the luxury of considerable self-sufficiency. Having depleted the North Sea as fast as possible (and at the lowest historic prices), the UK’s energy vulnerability is now considerable. Whilst the relationships with Norway are important, the influence of Russia is not thereby much reduced—particularly in respect of price.

23. The UK needs to increase its energy policy resources and its knowledge and understanding of both other EU energy positions and also that of Russia. Energy policy is increasingly a part of foreign policy for both the EU and the UK.

24. Recent statements from the ministers in support of a UK policy of “energy independence” lack much by way of coherence, but it is noticeable that this “independence” in defined at the national and not European
level. To actively pursue diversity of supply—rather than rely on the conventional UK position that this will be delivered by the market—is a radical policy departure. It needs to be explained, and crafted to work with the grain of Europe’s overall energy policy position.

4 January 2008

Examination of Witness

Witness: Professor Dieter Helm, Professor of Energy Policy, University of Oxford, examined.

Q360 Chairman: Professor Helm, we are very glad that you are with us today. As you can see, we will be taking a note of your evidence and there will be a transcript which will be sent to you for you to be able to make corrections. We are also very grateful for the written evidence which you have sent us, which colleagues have found extremely valuable and interesting in preparing for this morning’s meeting. You may want to make a general remark yourself but I would be grateful if, apart from that, you could address the question as to what are the prospects for Russian oil and gas production in the short to medium term, let us say the ten to 20 years period. Professor Helm: My Lord Chairman, thank you for inviting me. Let us go straight to your questions because the questions I have been sent will probably cover most of the things I want to say. Let me try and be as helpful as possible. There is a great temptation to draw a projection forward for output of oil and gas from Russia and then stack that up against likely demands for oil and particularly gas in Europe and then say, “A does not equal B, therefore we have a problem”. The reason I say that is we do not really know what will happen to oil and gas production, particularly gas production, through the period of the next ten or 20 years. Some things we can be fairly certain about and some things are political and economic issues which the country and its leadership will address. On the facts, we know about current production roughly, we know about potential future production, what the reserves might look like, and we know quite a lot about what will be required to get from A to B. Whether they go from A to B is in the realm of uncertainty. In those factual domains, we know that production, particularly in gas, is heavily concentrated on large and now somewhat declining fields and we know that production is fairly stagnant and at risk of even some declines. In terms of future potential, we know that the reserves and resources, again particularly in gas, are vast and we know that further out in the future the Arctic reserves are likely to be very great and as a by-product of global warming these resources are going to be increasingly accessible by sea which transforms their economic prospects. Not particularly bright prospects in the short run but lots in the long-term. The uncertainties are really very important. There are uncertainties about the pipelines to markets and the LNG facilities—the Baltic pipeline is an example which is late and heavily controversial—but in gas you need those pipelines. There are uncertainties about the investment process and how it will be conducted, how efficiently it will be carried out and so on. There is a great deal of uncertainty about the oil and gas price. It is fashionable and conventional now to assume the oil price is going to go up and up from $100 in the way it was fashionable at the end of the 1990s to assume it was going to go down and down from $10. The oil price is now falling and were the oil price to go down to $30 or $40, the investment programme in Russia and the expansion of output of gas and oil will be radically difficult. That is perfectly possible but I am not predicting that. Finally, it is about political objectives. What is the depletion policy? Do the Russians really want to deplete their resources as fast as they possibly can to service whatever we demand in Europe, as in the UK we depleted the North Sea as fast as we possibly could to meet UK demands? Probably not. The question is very much an open one and European strategy and UK strategy ought to take it as an open rather than factual position.

Q361 Lord Crickhowell: I would like to follow up on some of those points. I read with great interest your papers at about the same time as I read David Howell and Carol Nakhle’s book which both addressed the whole question of energy security and the link with climate change and so on in a very similar way. Some of us were in Moscow recently and had a very useful meeting with some of the people working in the oil and gas industry and I want to think particularly about gas. The message we were getting there, and you touched upon the declining fields and so on, was the problem that Gazprom is going to have in actually meeting some of the requirements to provide gas to its own people, let alone export. You have got an oil industry dominated by the private sector, insofar as Gazprom allows them, that is producing the oil, but Gazprom face a shortage of engineers ahead, huge technical problems, huge costs in getting out into this new area where the reserves are and it was spelt out rather vividly to us by the BP representative. Would you elaborate a little on how you see Gazprom, which is not the world’s most efficient organisation, even if it wants to, and you touched on whether it wants to deplete quickly, but assuming it wants to play a major role and continue to have gas as the major contributor to its economy,
doing it without actually doing deals for the technical expertise and investment with the oil companies in the West? Could you elaborate on Gazprom’s abilities?

Professor Helm: I would like to break that down into a series of bits, if you like. The first thing to understand is what is Gazprom’s strategy, what are its objectives and what are its interests. Gazprom is a monopoly and from Russia’s point of view if you wish to extract the maximum economic rents from your natural resources then being a monopoly is not a silly thing to do. That is the first point. All the arguments advanced by the EU and others saying, “You should break yourself up. It would be much better if you were a liberalised competitive gas structure domestically”, from Russia’s point of view it is not clear that is a good idea. The second thing to say is that Gazprom as part and parcel of the political structure in a authoritarian semi-capitalist society has pursued a policy which is common to virtually all resource rich countries around the world now, which is the argument that the state either directly or indirectly through the likes of Gazprom should own the oil and gas. That is what has been so painful for the likes of the BPs, Shells and others. From Russia’s point of view there is nothing insane about that either, that is an extremely rational thing to do. Western companies have been forced into accepting that in the future major oil companies (and this is true around the world because 80–90% of oil and gas has now been nationalised, so Russia is not an exception here), are reduced to a lesser role, doing the producing and maybe the marketing and some of the selling, but they are no longer owning assets. When people look at Shell and BP and say, “How many barrels has it got?” this is not really a relevant question. In Russia the clearest example is the Shtokman field where the Russians have moved to a position of essentially saying that companies like Total and the Norwegians can provide technical expertise, but that is it. This has really major implications for these companies. These companies do not like it. This is a reversal of their historical role throughout the 20th century. Of course, it is in their interests to claim that because Gazprom is a state-run company it is incompetent and, therefore, lacks the skills and they will discover shortly that it is all very disastrous and they will beg the BPs and the Shells and everyone else to come back and help them out. I think that is terribly naïve. It is true that Gazprom is riddled with inefficiencies and it is true that it lacks certain core skills, but that is true around the world, it is not just a Russian Gazprom-type problem. It is also true that Gazprom has certain advantages. It is fashionable to think that resources are best developed in liberalised unbundled competitive structures. Well, one of the best developments of a natural resource done in short order and low cost and very efficiently was by the state-owned British Gas developing the North Sea. I am not advocating state ownership for assets, or thinking that state ownership of assets is a good idea, but one has to remove some of the conventional wisdom which suits certain lobby groups to argue. It is likely that Gazprom will remain inefficient but does that matter to Gazprom when the oil price is where it is and when the revenue flow is as it is at the moment? What would it do with more money? The country is in surplus, it can do all the political pay-offs it wants to do. The owners, managers and senior politicians are getting themselves extremely wealthy as a result, so where is the difficulty? Indeed, put it the other way around, the more nervous the Europeans become about the uncertainty about the gas supplies from Russia, the more they are going to rush to do bilateral deals with Gazprom to secure their own positions. That is what the Germans have done, the Italians, the Austrians, and the Dutch have now followed that policy too. Again, from Gazprom’s point of view this is not a disaster from their perspective even though it may be very troubling from ours. Finally, on the skills issue, it might be true that state owned and particularly authoritarian regimes are quite bad at co-ordinating assets and the skill application to assets, but the education system to produce these skilled people is not necessarily inferior to ours. I suspect if you look at the supply of nuclear engineers in Britain alongside the question of building new nuclear power stations it is not a pretty picture. The technical education of the East Germans has turned out to be extraordinarily useful in West Germany, and of course many of them moved to West Germany when reunification took place. Again, Gazprom and the centralised state are actually capable of directing the education system to produce technocrats for these purposes. Yes it will be inefficient, yes there will be big difficulties, yes Western companies will be welcome to provide technical skills but, no, it is very unlikely that this is going to result in a debacle for Gazprom and a begging for the Western oil companies to come in and take over the oil reserves and sort the mess out.

Q362 Lord Crickhowell: Can I ask one supplementary arising out of that. The implication of what you say is that production may level off or even fall at the existing rate gas fields are coming on. They have got a political problem, have they not, in making sure that their own people have enough gas? Is the implication going to be that that may add to the energy risks for Europe who may find that there is simply not as much gas as they expect coming out of the Russian pipelines or is it all going to come anyway from the Caspian or elsewhere?

Professor Helm: That question raises the crucial issue that the demand for gas in Russia is at least as important for security of supply in Europe as the
potential supply of gas available in Russia, and we should be deeply concerned about that. It is part of the very predictable pattern that countries which are blighted by what we call the resource curse turn out to have these kinds of characteristics. It is no accident that Iran cannot supply enough gas to its domestic population at the moment despite having the third largest deposits in the world. Then you have to say how will the Russians solve that problem. It is pretty obvious in the short run what they are going to do, which is take Caspian gas north. You have to then add Caspian gas to the Russian equation in order to calculate what surpluses are available which can come into the European market. That happens to suit some political objectives as well and it makes the modern great game in the Caspian area of a higher sensitivity in terms of the politics but it also has a practical analogue. Suppose, (because I know the British Minister has been there and met the Turkistanians, as have the Iranians, the Chinese and everyone else), the pipeline comes west to Turkey and then up through Europe and does not go to Russia. It is projected that that will solve our security of supply problem, but it does not. It just means there is less gas available in Russia to service its domestic market and, therefore, there is less gas available from Russia to come into Europe. It helps in bargaining but it needs a certain sophistication to see how those relationships will be affected.

Q363 Lord Hannay of Chiswick: If I can follow up on two aspects of what you have said. You have spoken very convincingly about the Russians’ ability to catch up on their production problems, to provide the skills and so on, but you would not make a distinction between onshore and offshore, would you? Some of the evidence we have had has suggested that the Russians capacity, even within the reasonably near future, to conduct really sophisticated offshore exploration and development is absolutely close to zero. I do not know whether you would like to comment on that. The second is, could you just enlighten us as to whether the Russian Gazprom move to buy into Nigeria is likely to be another damaging choice for us, ie they are putting their investment dollars into Nigerian gas, not into Russian gas.

Professor Helm: Let me take these things separately. Yes, of course the skills for offshore and the skills for onshore are substantially different. There is some commonality but deepwater fields like Shtokman are a completely different ballpark from what they have been doing so far. That says Gazprom needs the skills to do that, but there are a couple of caveats. Firstly, these fields are a long way off. If you are thinking about the energy crunch in the next decade that faces Europe, and particularly the UK, these fields like Shtokman and so on are not really going to come into that play. The time horizon for this is not congruent with the energy security problems that we might have. Once you are beyond 2020 and from then on we may have changed our energy mix quite substantially. That is the first thing. The second thing to say about offshore is that while it is true that they may not have the skills, and the Norwegians in particular do, and to a certain extent the British do from the North Sea, it has to be remembered that virtually nobody had these skills at the beginning of the 1970s and by the end of the 1980s within a 20 year framework we had built an entire North Sea skill set. Similarly, in nuclear power we do not now have many skills in nuclear power in Britain but it does not mean in 15 years’ time we will not have considerable skills. It should not be taken as read that the Russians are incapable of getting up that ladder should they be so minded to do so, and that is a political choice. In the meantime their strategy in Gazprom, as I understand it, is entirely rational. You say to Western companies, “No, you can’t own the stuff and, no, we are not doing the original Shtokman auctions. No, we are not having people politically we don’t like”, which is essentially a rebuttal to the Americans in the Shtokman field, “and, yes, if you now understand as oil companies that you can come in and bring your operational skills and you wish to be paid for your operational skills in deepwater, sure we will come and get you and get lots and lots of British and other small to medium-sized companies who have expertise in these activities”. There are people falling over backwards to do it. From their point of view, it is rather like how do you bring in a whole host of particular skills. The issue will then become: will they treat those skills as an exercise in knowledge transfer to gain independence from overseas companies or will they remain dependent forever. The Chinese strategy in these areas, in clean coal, in nuclear, et cetera, is clearly knowledge transfer. They buy the skills in for a short period of time, and they say “Thank you very much, we now know how to do it. Off you go, we will have our own Chinese nuclear industry”. It is not clear how the Russians will drive that forward.

Chairman: Thank you. Perhaps we can leave the Nigerian question because it does come up more appropriately under our question five.

Q364 Baroness Symons of Vernham Dean: You have described the reluctance to accept foreign and direct investment as a combination of commercial protection of the asset for the future and of political motivation. What is the balance between those in the way that there is this aversion to anything more than a short-term investment in skills, marketing and operational requirements?
Baroness Symons of Vernham Dean: I think here one has to have in mind, the economic fundamentals that lie behind the changing position in Russia. Up until the end of the 1990s, and indeed even when Putin came into power, the assumption was that oil prices would be $10. Some of you may remember The Economist ran a front page in 1999 which said: “Oil $5?” At the end of the 1990s there was no expectation that oil prices were going to go up; in fact, it was expected they would fall. In such circumstances it is unsurprising that the Russian debacle in 1998 happened, the oil and gas reserves were not worth very much and the new Putin regime was very unstable in the way it was structured because it had no money, it was still recovering from bankruptcy. The early years of Putin’s foreign policy and his domestic policy and the activities of Gazprom were all based on the idea that this was an important source of revenue and this was an important way of enriching particular individuals. There was a need to remove the oligarchs, hence the famous meeting in 2000, but beyond that there was a necessity for foreign companies to come in. By 2002-03 and building up to the 2004 election this had been completely transformed. They did not expect this to happen. They suddenly had massive, valuable, oil and gas revenues, so the country was no longer an importer of capital, it was an exporter of capital. It has effectively a sovereign wealth fund, it has large reserves, so instead of having to suck financial flows in it is throwing them out, as indeed is China. This is the bizarre thing, a developing country throwing off reserves. They do not need the money. In such circumstances where you suddenly realise that something you thought was not worth very much is actually going to be worth virtually everything, and that your economy is going to be a carbon economy, it makes great sense to use your leverage to get control, and that was exactly what they did in Sakhalin, with BP and with others.

Q367 Baroness Symons of Vernham Dean: Obviously it can change if the oil price collapses but is there anything internal in the Russian political mind at the moment which would be a spur to changing that, to have a more co-operative position in the world market, or do you just not see that as changing?
Professor Helm: Why would you want to do that? The answer is the following—

Q368 Baroness Symons of Vernham Dean: Because of external factors, because other people have got gas too, the markets change and you might want to hedge your position.
Professor Helm: The most important thing you would do if what you are trying to do is both of those things, maximise the money, asset manage if you like, and help the political elite in that frame, and increase whatever your political objectives are internationally in respect of Russia, fear and all that kind of stuff—your strategy would be to ensure that you get the maximum bucks for your resources. What I have been trying to argue in this particular context for some years now is that in that context it is really quite frightening from the Western perspective but the right rational strategy for Gazprom to pursue is pretty close to what it is doing and it has two or three parts. The first part is to monopolise the domestic resources. That means you want to own the reserves and own the pipes. Secondly, control as much of the downstream market as you possibly can, and that is the buying of the pipes and other assets in Europe. Thirdly, divide and rule and get bilateral contracts with particular countries, particularly Germany, make sure that you go round the ring of Europe and do your politics with all the other sources of supply. It is very easy to add those up. Norway has four million people and more gas than it can possibly cope with. They are never going to be price competitive against the Russians, hence the contracts do not have much price in them. Next Algeria and Libya. They are crucial to supplies to southern Europe, and you have seen the political competition between the French, the Russians and others for access and a role there, including the provision of civil nuclear power. Finally, the Caspian, and we see the game going on there. LNG does not solve this problem because inherently pipeline gas is cheaper except if the pipes are incredibly long. That is why we should take as given that they are going to pursue that strategy and if the oil and gas prices fall they will have to pursue it even harder. We should not have illusions that somehow Russia is suddenly going to say, “Let’s liberalise our market and give third party access and sell the oil and gas to anybody who wants to buy it”. This is an illusion which has cost the Europeans several years in getting their strategy together and it

Q365 Baroness Symons of Vernham Dean: The point I am trying to get at is the wealth has obviously been the means by which they have got this sort of independence of action but is their objective to maintain that wealth for its own sake or is there an objective to have the political place that Russia really wants to be in, ie nationalism, and, if you like, a sense of its reassertion in the world dynamic of superpower status?
Professor Helm: The answer is both but the former is a necessary condition for the latter.

Q366 Baroness Symons of Vernham Dean: Can you see this changing?
Professor Helm: Yes.
will have very serious consequences in the next decade.

Chairman: I am worried about our range of questions, can we move on. We are now going to Lord Hannay on question four.

Q369 Lord Hannay of Chiswick: I think you have answered how far Russian policy is designed to control or influence the supply of gas, so I will not put that question again. Could I put a different question, which is quite a lot of the people we saw when we were in Moscow said that the European Union’s relationship is usually described as one with Russia about energy but in a way that is a misnomer because the problems do not really lie over oil much, electricity not at all, coal not all, they are all about gas and pipelines. Could you just confirm that is a fair assessment of it because it does seem to colour quite a lot of what we talk about. If we talk about energy, despite the fact that Russia is a very large oil exporter, there does not seem to be a big problem because oil is a world market, it is not subject to quite the same criteria as gas. Going on from that, to what extent is Europe’s energy dependence on Russia for gas a source of vulnerability or weakness only or to what extent is there validity in the view that actually there is a dependency on both sides? Finally, what action can the EU take if there really is a fundamental source of vulnerability or weakness?

Professor Helm: The first part is yes, it is overwhelmingly about gas although there are some oil issues and they did slow the oil supply in Germany and cause some disruption. Basically the exposure to Russian oil is somewhat limited and the big game is about gas, so you are right about that. On joint dependency, not really. If one gets one’s Atlas out and looks at where the gas and oil is and where the alternative places it could go to, although Europe is by far the best market for them because it is the most secure, because it is most likely the Europeans will actually pay whereas a number of other countries might not, go back to the whole debate about Yukos, this was all about whether the stuff went to China or Japan and there are alternatives. Finally, as the Arctic melts the options become quite considerable as to where the stuff can go. It is true they are a bit dependent upon us but we are much more dependent upon them when it comes to gas. Going forward, dependency has a certain “real politik” to it and our dependency is going to exist come what may, almost whatever they do, for the next ten to 15 years, whereas they can do something about their dependence on us, and we are going to pay anyway so why should they take us seriously in a negotiation. The final bit about what action is a big question. Ever since the Hampton Court Summit I have tried to set out a set of internal actions which the EU should pursue in strengthening its own resilience, particularly in respect of grids, but, in addition, the huge failure in Europe, and this is deeply political, is the detachment of particularly Germany but then others to form bilateral relationships with Russia and the inability of the British, the Germans and the French to agree an overarching view about energy policy which would enable Europe to speak slightly more with one voice and therefore exploit its multiple relationships with Russia, including the other side of that dependency relationship. That has been a magnificent failure in the sense of scale and it seems to me this is the first episode in which Germany has displayed from its own interests very sensibly the sorts of political and foreign policy strategy which was at the heart of why Mitterrand and Kohl were determined to have monetary union to bind Germany into the European project rather than allowing it to detach. That development of the E.ON/ Russian relationship, the Baltic pipeline, Schroeder’s involvement in it, was a clear signal to everybody else in Europe, “If you don’t get in on this too with Gazprom then you have left out an enormous amount of security”. We have already had one winter in which we have experienced the consequence of not having those long-term take or pay contracts when, of course, Germany did.

Q370 Lord Truscott: I felt I had to challenge your point about mutual dependency and the fact that Russians have other markets, China and Japan, which is undoubtedly true, but it is also a fact that 80% of their pipeline infrastructure leads into Europe. It would take billions of pounds and many years, maybe ten or 15 years, to re-gear that infrastructure towards the east. For the foreseeable future they are dependent on Europe for their markets and their revenues and it is not an easy option for the Russians to just say, “We are going to flog all of our gas to China and Japan”.

Professor Helm: I accept that entirely but my reply is the following: if you were sitting in Gazprom’s headquarters do you think it is ever conceivable that any European country will say, “Okay, we don’t like the way you are behaving in Russia, we don’t like you interfering with the British Council, for example, we are going to stop taking your gas”? The point is the dependency is complete, we have to have the gas otherwise people’s lights will go out. Therefore, from a dependency point of view, how are we going to exercise at our end of these pipes any credible strategy which says, “If you don’t do what we want we won’t buy your gas”. There is no other option and that is the situation we are in. If any individual country in Europe said, “We are fed up with you, Russia, we are not having your gas”, the others are going to take it. Look at their exposure. Look at Italy’s exposure. Look at Germany’s position. Look at Austria and Hungary’s position. Dependency is really about
whether you have a credible strategy to opt out of the relationship. It is right to say of course they need to send the stuff this way but they can be absolutely certain that we are going to take as much as we can get from those pipelines, and that is the problem with dependency.

Q371 Lord Hamilton of Epsom: Following on that point, and we have referred to the bilateral arrangements that have been made between European countries and Russia, does this dependency then reflect itself in a premium in terms of the prices that are being paid by these countries?

Professor Helm: No. The Gazprom strategy is pretty sophisticated and it is partly political and partly economic. At the hub of the Gazprom relationships with Europe is the joint share ownership of E.ON and the partnership with E.ON and the Baltic pipeline and so on that goes with that. The insistence that Gazprom have made, which sadly is entirely rational, that “If you want to buy our gas you must sign a long-term take or pay contract”, that is really the premium, and from their point of view is absolutely right. After all, gas and oil have upstream sunk costs and a natural competitive market will produce long-term take or pay contracts. That is how we did the North Sea, long-term take or pay contracts, it is the right way of doing it. In the UK we do not sign any of those because our market does not allow companies to take those risks because people can switch as final customers. I am not saying they should not be able to. I am simply saying what is called the NETA-based market, particularly for electricity, is peculiarly badly designed to enable serious players to sign long-term take or pay contracts. The real difference between us and what the Germans and the Austrians have done in particular, also now the Italians and the French, is they have signed long-term take or pay contracts. If you want to see the effect, in periods of excess supply, which was 1998 onwards, they have much higher prices in Europe than we do but in deficient supply, as we are quite close to now and as we got to a couple of winters ago, the price in the UK rockets and no gas flows. Why? Because the other side of the Channel have signed long-term take or pay contracts. There was that absurd moment when both the Prime Minister and the then Energy Minister talked in the House of Commons about energy markets behaving irrationally when the price went up in the UK and the gas did not flow for that price. It is absurd. What did they expect to happen? These were long-term take or pay contracts and that is the form. The final thing in a relationship is that Gazprom is not just interested in the short-term contractual position it strikes, it wants the assets too. The other dimension here is if you want a long-term take or pay contract and you want that relationship, “Could we have some of your gas assets, please, could we have some of your pipelines and, by the way, we will expect you to advance our interests in the European market, not yours”, so you find the spectre of Gazprom, BP and other companies making statements about the importance of allowing Gazprom downstream into the markets which is part and parcel of the long-term co-operation that takes place. All of this is entirely rational, entirely predictable, and energy policy in Europe should take that as a given and then work back from that position.

Q372 Lord Anderson of Swansea: Before looking at Russian policy in other countries, I wonder whether the traditional interdependence of supplier-consumer is more than you are saying. Even though the lights would go off in our country and others, if Russia failed to supply us, the loss of a very substantial amount of its revenues which they receive and will continue to receive, and must receive because of the direction of pipelines, would have a substantial impact on them, the elite in their country and so on. I would like to turn to the proper question, my Lord Chairman, which is five and look at various areas and ask you for the significance, political and economic, of Russian policy. I suppose at one level one can see a rather more sinister, tentacle-like extension of Russian policy of seeking to have total control. I would like to look area by area. For example, would you say that the Russian pipeline dependency and in the northern sector and into the Western Balkans are undermining the Nabucco project?

Professor Helm: A very quick comment on your first point. You are absolutely right. I am not saying that Russia does not have an interest in making sure its market is there and we have no influence whatsoever. Indeed, if Europe was to act together in speaking with one voice to Russia the influence would be much greater. It is not a position of hopelessness. I would, however, say that as you build up sovereign wealth funds you buy insurance and, therefore, the degree to which you are vulnerable as an elite to a fall in oil prices or a loss of sales is less. That building up of those sovereign wealth funds is quite important in the equation.

Q373 Lord Anderson of Swansea: Confidence is a factor too.

Professor Helm: Yes, I agree. Of course, there is an interest on both sides but my point is you should think about the influence being vastly greater if it is European as opposed to if it is bilateral. To look at the influence very quickly you have to go round the block, and one really needs a map for this, but if you start at the top Norway has a disputed sea area with Russia in the north in which there is probably carbon resources. Norway has a deep interest in how the Arctic area, and how its foreign policy and politics
plays out and it has a deep interest in its companies’ selling expertise, with the Shtokman and other deep Arctic fields, and it only has four million people and a sovereign wealth fund of at least £300 billion so far. From Norway’s point of view, why compete on price? Secure supplies, yes. The idea that the UK, because it has got long-term contracts with Norway, has solved its reliance on Russia is not the case. It has solved the quantity issue but not the price. Norway is not a problem for Russia in the sense of being a competitor to Gazprom. If we go round the block, Algeria and Libya are serious potential suppliers to southern Europe, Spain and Italy in-between, both of whom are heavily gas dependent, and in particular Italy is terribly vulnerable in terms of the lack of domestic resources. There is a competition that goes on there and it is very sophisticated. For example, in my mind it is no accident that on the one hand President Sarkozy is trying to provide for a Mediterranean strategy and provide civil nuclear power to the North African gas producing states and Total has been allowed into the Shtokman field after the Americans have been pushed out. These are very careful, deep and serious foreign relationships which are being constructed. Russia is working very hard at those relationships too and we will see how those play out. In the Caspian area, and I do not think it is cynical, if you were Russian the big game is to work out where that gas is going to go, north, south, east or west. We have the Iranians arguing about it at the moment and in some difficulty with getting supplies flowing south. We have the Chinese desperate in their resource hunt looking for absurdly long pipeline solutions to get access to those supplies. The Russians have some political control of the region and the history of the Russian empires tells them that this is part of their political control of the region and the history of the region. Looking for absurdly long pipeline solutions to get the energy supply in the Western Balkans?

Professor Helm: Russian diplomacy has been very heavily focused in the Caspian States in Hungary, Austria, Serbia, Bulgaria and Romania. The most notable example, not for scale but in terms of revealing how these things work, is the Hungarian issue and the attempt to detach Hungary on the Blue Stream Project. Similarly, the involvement of Gazprom with the major Austrian company is connected to that Austrian company’s potential stake in the Nabucco consortia.

Q375 Lord Anderson of Swansea: And the Bulgarians have a stake in Nabucco too.

Professor Helm: Absolutely. The Russians have two advantages here. First of all, they have a very clear strategy of what they want, and the second is they have enormous flexibility, so they have got a finger in lots and lots of different pies. “We’ll have a few assets here, we’ll do a swap in Serbia, we’ll take out bits along with component parts, we’ll intervene in the merger debate between the Austrians and Hungarians. We’ll offer them long-term take or pay contracts”. From the Russian perspective, you do not have to fossilise and say, “We must have this particular bit”, you can play a game of opportunity within the framework of a general strategy, and clearly influence on that backyard is not just about oil or gas, it is about the former Soviet Union, the Ukraine, a whole series of political influences which are well beyond my expertise.

Q376 Lord Anderson of Swansea: What are the prospects for Nabucco in your judgment?

Professor Helm: Quite limited, and it is quite a long way off.

Q377 Lord Crickhowell: Can I pick you up on Norway. You have spelt out a strategy which is a Europe-wide, top-down approach, grids and gas storage. You have talked about Norway, and I understand perfectly well that Norway’s population is four and a half million and not a great incentive to sell its gas and it has got political interests that make it want to talk to Russia, but you do not say anything about the desirability of Europe—you referred to the UK—talking to Norway, which David Howell puts a good deal of emphasis on. Should not the Europeans, as top-down and working together, be talking pretty seriously to Norway?

Professor Helm: Yes. Norway has got other interests. Recently they had to abandon all their rigs because of the Russian military activity in their area. There are all sorts of changes in what is going on on their north coast with regard to Russian military forces. There is
a whole series of arguments about the ownership of land which is going to become ice-free to the north of them. There are Arctic Councils to agree about, the issue about shipping rights, the role of Iceland. Once you look at the world from the Arctic down and you imagine it ice-free and you look where the strategic places are and work out that maybe 30–40% of the world’s undiscovered oil and gas may lay up there, and you look at what the Russians and Canadians are doing, et cetera, you suddenly realise that countries like Iceland may become strategically incredibly important, and certainly Norway, and in an historical context they must consider their independence, their political status and how they fit together. I agree entirely that it makes enormous sense to build on what are already very good relations, as I understand it, between the European Community in the widest sense and particularly Britain and Norway in a narrower sense. Yes, I agree with that.

Q378 Lord Crickhowell: Storage is an aspect here because perhaps some of those North Sea facilities may be the place where storage can be provided. 

Professor Helm: It is much more than storage when it comes to the North Sea. This is the natural carbon deposit for carbon sequestration. There is a whole host of relationships to form. Storage is a complex area. The oil companies absolutely loathe the idea that there will be strategic storage in gas. Why? Because if you want security of supply you have to have excess supply and if you have excess supply and you do not pay for it you depress the price. We do not have a proper price for capacity in electricity, we have this very short-termist market in NETA, and in gas from the oil companies’ point of view it is not economically very attractive for the Commission to run a regime in which there is spare supply. My view is that is has to be paid for and there is a serious argument about what it costs and what term structure that storage is on, but the fundamental question is whether the good to the whole, the benefit to all of us, of the security and bargaining power that comes from that is much greater than the sum of the individual parts.

Chairman: Lord Hamilton, I think the question you were going to ask has probably been covered.

Lord Hamilton of Epsom: I think it has, my Lord Chairman.

Q379 Lord Hannay of Chiswick: I just wanted to question slightly what you said about the oil companies hating the idea of storage and sequestration. They too are having to look to a post-Kyoto world where certain obligations may be imposed internationally on—

Professor Helm: Sorry, you mistake me completely. I am not saying the oil companies have any objection to carbon sequestration, this is about strategic gas storage. Sorry if I misled you.

Q380 Lord Hannay of Chiswick: No, I completely misunderstood.

Professor Helm: On the contrary, the oil companies appear to me to be leading the game in terms of thinking about how the North Sea will develop for carbon sequestration.

Q381 Lord Hannay of Chiswick: Sorry, I completely misunderstood you. Could I ask you about the regulatory negotiated framework for, above all, gas but also other energy issues between the European Union and Russia which has come to a grinding halt with the non-ratification of the Energy Charter and in particular its Transit Protocol and the clear indication, and I imagine you would confirm the thrust of your answers, that the Russians are not going to buy into ratification particularly of the Transit Protocol. What can be saved from this shipwreck is the question I would like to put to you. Is it sensible to, as it were, recognise that the Energy Charter is never going to enter into force between Russia and the European Union? If so, is it sensible to try to find a more modest regulatory framework within which, above all, the gas relationship will continue to be operated and which will seek to balance the European interests not only in Russian gas but also in other people’s gas that transits Russia and the Russian interest in downstream? Can that be fitted into an agreement in which there is equality, reciprocity and so on? I think from your extremely useful paper of last September I know roughly where you will come down but I think it would be very useful for the Committee to hear your views on that.

Professor Helm: There were two things going on in the Energy Charter and Transit Protocol discussions. One view, which was the view in the 1990s in the Yeltsin period when the oil prices were low, was that Russia, which at that stage was about the size of Mexico in terms of economic significance despite its vast size, was basically on its way to a liberal democracy, and one way of expressing that was that it would arrive in a position where its laws and structures would look like the EU. It was almost as if it was a candidate member but was never going to be allowed to be a member. In the same way that Bulgaria, Romania and eastern European countries, had to converge on European ways of doing things, so it was thought the Russians would do that. The Energy Charter and the Transit Protocol at that stage were deemed to be essentially the application of what I would call a kind of bastardised British model of how to run an energy system applied to Russia and at the core of that idea was they should open up all their
pipelines and electricity systems to third party access on even terms. The other view about the Energy Charter which has developed subsequently is the notion it is basically a contract resolutions or arbitration body which can sort out disputes between players, and I will come back to that in a moment. The first view was not only falsified by the sharp rise of oil prices, Russia was no longer beholden to Europe, it was no longer in a bankrupt state, but it was utterly absurd for Gazprom to ever accept the idea that third party access should be allowed to its pipes because what that does is minimise its monopoly power. It is the absolute opposite of what you would want to do. For the Europeans to believe that they could bash the Russians into that position could only be based on the idea that Russia was so weak and compliant to European needs because its economy was in such trouble and after the bankruptcy it would need resources into the future, or the Europeans believed the thesis that a liberal capitalist democracy was at the end of the history and we were all going to go there anyway, which you can understand people believed after the collapse of the Berlin Wall. I think that was utterly hopeless and an enormous amount of effort and time was spent on something which clearly was not going to happen, and it is not going to happen going forward. If the Russians sign and ratify it, it will only be in a sense in which it will not be applied. The other idea that there should be an international body which is responsible for helping parties to resolve disputes seems to me to be an excellent idea, but one has to be very careful that it does not have a British or necessarily European label upon it. I will not say it is necessarily a UN function but it is a kind of WTO-type function and it seems to me in the framework of negotiation with Russia to join the WTO this should be part and parcel of that framework. Going down that route is the sensible thing to do. Going down the former route is both hopeless and just creates trouble because every time there is a serious interchange between the EU and Russia, the EU says, “Ratify the Energy Charter, ratify the Transit Protocol” and the Russians say, “No, go away” and that does not help us anywhere. That is why I think it has been misconceived.

Q382 Lord Hannay of Chiswick: Can I just be clear, if you will forgive me for saying so, I think your concept at this very late stage this could somehow be incorporated into the WTO accession negotiations is not terribly realistic.

Professor Helm: That may be right.

Q383 Lord Hannay of Chiswick: Are you saying that the idea of an EU-Russia regulatory framework building on the four spaces or a new agreement with Russia is too narrow for basing what you see as desirable, which is a regulatory framework that could give both sides a degree of predictability, rule of law, et cetera?

Professor Helm: If you look at the pillars in the EU-Russian energy dialogue and the PCA framework what I am really saying is not that that engagement cannot be taken forward but in the energy component of that dialogue one needs to have a harder and more realistic approach to negotiations which start from a clear understanding of the objectives of both parties. Basically the energy pillar in those negotiations has been anchored in the Energy Charter and third party access. I wish it was not true from a European perspective, but all I am saying is it is utterly hopeless to imagine that political and diplomatic capital should be used and expanded on the idea that we will persuade the Russians to admit third party access to their gas network. This will not happen, it is not in their interests, and we are wasting a great deal of time and effort to no net benefit.

Chairman: Thank you very much indeed. That, to some extent, links to the next question from Lord Truscott.

Q384 Lord Truscott: Thank you, my Lord Chairman. Professor Helm, what is your view of the Commission’s Third Energy Package and the alleged discrimination that Russia might face? Would you also comment on the EU’s other efforts to avoid dependency and enhance accessibility to supply and the European idea of boosting renewables, enhancing efficiency and some Member States going down the nuclear road, like the UK? We were talking about dependency earlier but the percentage of gas supplied by Russia to the EU will go down in percentage terms over the coming years although not in absolute terms.

Professor Helm: There are two bundles of EU policy relevant to the energy sector. There is the bundle from last year, a group of directives, initiatives, around the idea of unbundling competitive markets, and then there is the package for 23 January this year which is the environmental side. I will start with the unbundling. I cannot get myself terribly exercised that forcible ownership unbundling in the energy market we now have in Europe is going to do much per se to increase competition. It probably will do a bit but if you want competition you have to have some competitors. If you are on a football pitch and you have got two Frenchmen and a German, or two Germans and a Frenchman, as we have in the UK, plus a Spaniard, you have not got enough to make a really competitive market stick. The big mistake in the internal market in Europe was to allow these mergers and acquisitions which created this market power which means that you are not going to have this idealised market, which was the objective in the first place. It is an interesting question of whether you
measures, like renewables and energy efficiency. In this context it is fashionable for people to argue that environmental intervention be and of what sort. In this context it is windmills. The question is how far should the market would never build a windmill, or hardly any wind power in the UK but for government policy, the which even this government now accepts by having to White Papers and statements and it is a matter of fact energy policy for the last 15-20 years in repeated will not produce security of supply through competition. On the issue of the environment and physical market before you can have the actual goes with a package on the grid side. You need a reason I am in favour of the unbundling provided it developing out of the interests of the players. For that forced collusion. You do not get natural grids developing out of the interests of the players. For that reason I am in favour of the unbundling provided it goes with a package on the grid side. You need a physical market before you can have the actual competition. On the issue of the environment and security of supply measures, it is true that the market will not produce optimal diversity and the market will not produce security of supply through individual decisions. That is contrary to British energy policy for the last 15-20 years in repeated White Papers and statements and it is a matter of fact which even this government now accepts by having to earmark particular technologies. There would be no wind power in the UK but for government policy, the market would never build a windmill, or hardly any windmills. The question is how far should the intervention be and of what sort. In this context it is fashionable for people to argue that environmental measures, like renewables and energy efficiency, are the best way of increasing security of supply. Unfortunately, the best way of increasing security of supply is coal and coal is the growing fuel around the world and it has many sources, it is extremely cheap and is fantastically damaging to the environment. People who argue that pursuing environmental policy and security of supply are necessarily linked, that is not true. If you look at the particular technologies, energy efficiency does reduce demand and in the short-term a lower level of demand might lead to a higher level of security in the short run, but not in the long run. On renewables, most of the renewables policies very unfortunately reduce security of supply, particularly when the renewables penetration goes to high levels. At the extreme you could have a system in which if the wind was blowing nothing else would be needed and, therefore, nothing else would earn any money but if the wind does not blow everything else is needed and it has to earn enormous returns to provide that facility. Hopefully in ten or 15 years’ time it will have some batteries and then wind will be base load and this issue will be transformed, but not in the short run.

Lord Boyce: I wonder if you would say something about the anti-monopoly powers. I rather get the impression from what you have been saying that Gazprom would like to have a dominant position in the European gas market. Do you think the European Union existing anti-monopoly powers could prevent that? That is the theory, but in practice do you think the European Union will want to exercise those powers because individual states may not want them to be exercised because it will upset their bilateral relationships?

Professor Helm: I think the European Union should insist that any company that operates within its boundaries should abide by European law and by the rules of the European Community laid down for its markets. I think Gazprom should be treated like any other state driven company that wished to invest in the European Union and because its motives are not purely the maximisation of profits, they are political and wider ranging, there should be a greater burden of proof applied than if a normal commercial quoted company with transparent accounts wished to acquire assets. Transparency of accounts should be demanded. I have no idea where the money goes in Gazprom. I have never seen any accounts which lead me to understand that. Given the strategy that Gazprom is pursuing, given it has upstream market power, the Commission should ask serious questions to have a look at a competition inquiry into its activities across the market and apply the full force of competition law. Will it do so? No, probably not. Does it have the powers to do these kinds of competition investigations? I am not sure. Part and parcel of a more realistic policy towards Gazprom is to say, “We understand you are trying to maximise your position, we understand your strategy to extract the maximum returns for your resources, why shouldn’t you, but you have to understand that within the EU we want to protect our position too and we are interested in a competitive market, not a political market, and just as we should be concerned about sovereign wealth funds we should be extremely concerned about particular acquisitions which have this broader market power rationale behind them”. I would argue for a much sharper application of competition policy and the rules of the European Union within its boundaries.

Lord Anderson of Swansea: You argue for quite a substantial new agenda for the Commission. Have you been brought in by the Commission as an adviser at all? I notice from your CV that most of your work has been with the British Government, but are you an adviser to the Commission?
Professor Helm: I have no formal post or role in respect of the European Commission but I spend a great deal of time talking to people there and a lot of time in Brussels.

Q387 Lord Crickhowell: I suppose your central recommendation about how the Europeans should deal with the situation is that they should get together and act as a European whole, and you have given some pretty compelling reasons as to why the Germans seem to be unlikely to go down this road, the French with their nuclear dominance are not likely to go down the road and the British for political and other reasons are reluctant to go down this road. In preliminary conversation before this meeting with Lord Hannay he said, “Yes, but Europe under threat sometimes is prepared to come together and act as Europe”. How far do you think it is likely that we can get together and act on a European basis? It is a central recommendation but it may be the most difficult one to achieve.

Professor Helm: My first observation is that nothing substantive seems to happen in the EU unless the Germans, the French and the British agree. That may be too strong a statement and monetary union might be the exception to that, but it seems to me when it comes to the energy debate the question is how are those three countries going to co-operate. So far the British have been banging on against the French and the Germans on the competition agenda and the unbundling. The British energy position could not be more in your face vis-à-vis French energy policy and German energy policy. On a regular basis British officials attack European companies for being bundled and argue they should be broken up and their governments tacitly or explicitly do not want that to happen. The question comes, if fundamentally we disagree with the position that these two other countries wish to take in terms of the structure of their own energy markets, how can we expect them to co-operate with us to protect us, those who now have had to join the European club. The great difference between British energy policy and everybody else for the last 40/50 years has been, “We’ve got plenty of energy and they haven’t”. Germany in the end had to manufacture synthetic fuels in the Second World War. France built its nuclear programme because it does not have natural resources. Suddenly we are terribly exposed. My own view is it will take another few winters before the British Government discovers that actually the exposure to a volatile spot market without much storage and without the long-term contracts that our European partners have is a big disadvantage. It is already true that British prices on the electricity market are moving above the European average and in the coming decade I expect them to be at the top of the European market but very much more volatile in that context. My view is you need quite a lot of pain for people to understand they need to change their political policies and there is a long lag that leads with it. Given that, the understanding between France and Germany, between Merkel who is somewhat more distant than Schroeder was to the relationship, and with Sarkozy who clearly has views about how France will join this club, that gives some grounds for hope that a Franco-German common view on energy policy will gradually emerge. I think it will take time. My real fear is that the UK is on the cusp of a difficult decade in which any nuclear power will not be there because that is 2020 and beyond, the AGRs are in a pretty weakened state and could fail, as they do on a regular basis, we have a dramatic increase in our need to import gas and we have no long-term contracts and that is a terribly exposed position. All of my work on energy policy has led me to the conclusion that energy policy changes after a crisis and not before. My view is at the moment we have the makings of a crisis but the bad news is that it is not anything like big enough yet to force the British to come to an understanding that they will have to agree with the French and the Germans a common energy position. In the meantime, why should the Germans share the benefits they have got of their storage and the long-term take or pay contracts and their relationships with us who told them this is the worst way to organise their market and they should break them up immediately to our benefit. This is an extraordinary position to get to.

Q388 Lord Anderson of Swansea: Can you see any conceivable German interest in a European grid?

Professor Helm: Yes. Germany is geographically surrounded by links with other players and, of course, as France expands its nuclear position and Germany does not that is important to it, but there are also big links between Germany and the Netherlands, Denmark, all round its frame. The question is not whether it has an interest in a European grid as opposed to more bilateral links that suit its own purposes. No incumbent oligopolistic firm will ever want the system optimal outcome; they will want to control the linkages. What Europe is in a network sense is a series of bilateral links between major dominant players, that is why we have such an inferior grid. It is very, very important on the grid position to realise it is not just about security of supply, it is very important too for the competitiveness of the European economy because interconnection creates a portfolio effect which means the amount of power stations you need to secure supply at any point is much less, that is why we built national grids and broke up the local ones. The
Americans are going through the same problem. This is a competitive battle to see who can get the greatest efficiency out of their electricity systems in addition to the security of supply problem.

**Q389 Lord Hannay of Chiswick:** I just wanted to ask you on what you said about Nabucco and about the European grid. Does this lead you to the conclusion that a European policy ought to be prepared to pay a premium in public funds to get those two sorts of ideas going and not just leave them to the market? After all, the whole of energy policy around the world has been filled with interventions by governments to in a way distort the power of the market in particular circumstances where their security might be strengthened by it. Are you suggesting that the EU as such should, for example, put some EU budget money behind constructing a grid that is less bilateral and national than the individual companies might do?

**Professor Helm:** The first thing to say is there are no free markets in energy in a perfect textbook sense. Governments are always involved in energy, they are always intervening, the question is what is the balance, which bits should they go for and which bits should they not. No pipeline like Nabucco can be anything other than political and no company can possibly want to invest in such things without a political framework around it. The first thing the European Union should do is decide which bits of infrastructure matter and put the weight of the European political framework behind it, and that includes the big players talking with one voice about them—that the Europeans could be minded to say to Turkey and other countries affected by the Nabucco framework, “We want this as a priority European project and we are going to put political support behind it”. The second thing is the cost of pipelines is mostly about the cost of capital. Private risk would make these things extremely capital expensive and government guarantees would reduce those costs of capital considerably. The difference between Russia and Europe is in Russia if they want to do something they may not have the technical skills to do it but an authoritarian capital state can make sure infrastructure is built. What we have got to do is find how a liberal democracy can ensure that vital infrastructure, roads, rail as well as energy infrastructure, gets built and I would much rather we spent the money on that than paying for the Common Agricultural Policy.

**Q390 Lord Selkirk of Douglas:** May I ask a general question about Kyoto. What are the possibilities for the European Union working with Russia on post-Kyoto negotiations on climate change? Perhaps in general you can comment on the prospects for cooperation between Russia and the European Union in the present political climate?

**Professor Helm:** On climate change, as I tried to say in the note, I cannot see what interest the Russian elite and government guarantees reduced those costs of capital considerably. The difference between Russia and Europe in Russia if they want to do something they may not have the technical skills to do it but an authoritarian capital state can make sure infrastructure is built. What we have got to do is find how a liberal democracy can ensure that vital infrastructure, roads, rail as well as energy infrastructure, gets built and I would much rather we spent the money on that than paying for the Common Agricultural Policy.

**Q391 Lord Selkirk of Douglas:** Is your general message to us that there should be a greater degree of realism injected into our foreign policy?

**Professor Helm:** Absolutely. If I could summarise the most important point I want to make it is that we should understand and take as given what Russian objectives are and what Russian interests are and we should spend less effort trying to persuade them to change their objectives and more effort in thinking about what to do as they pursue those objectives to strengthen our own position. There are an enormous number of things we can do both on security of supply and on climate change to improve our position, but of the main things that need to be done these things are not easily done at a nation state level, they are European, and this involves the British understanding that having nearly run out of our own natural resources we are now in the same position as the French and the Germans and we have to actively co-operate to produce an outcome between the big powers in Europe at the EU level and this will be a rather challenging problem for British political culture but as an economist, and as someone looking at the energy sector, if we do not do that then we are going to have a serious energy problem and in the UK this will be reflected in high and volatile prices and a lot less security.

**Chairman:** Professor Helm, we have kept you for longer than we originally talked about but we are extremely grateful. I think we have had an extraordinary morning. You might be surprised, you might find some of us queuing up to listen to your lectures in future because this has really been extremely helpful for us in challenging some of our ideas and also giving us a framework to look at this
question which is obviously a central part of the report which we will be preparing. We are extremely grateful. We will be sending you the transcript and we very much look forward to your comments and including them in our report. Thank you very much indeed.
WEDNESDAY 23 JANUARY 2008

Present Anderson of Swansea, L Boyce, L Chidgey, L Hamilton of Epsom, L Hannay of Chiswick, L
Roper, L (Chairman) Selkirk of Douglas, L Swinfen, L Symons of Vernham Dean, B Truscott, L

Examination of Witnesses

Witnesses: Mr Jim Murphy, a Member of the House of Commons, Minister for Europe, Mr Nick Latta, Head of Russia Section, and Mr Martin Shearman, Head of CFSP Group and European Correspondent, Foreign and Commonwealth Office, examined.

Q392 Chairman: Minister, thank you very much for coming to give evidence to us again. As you know, we have been undertaking an inquiry on the European Union’s relations with Russia. We have taken evidence from quite a number of people already. We have visited Moscow, where we had a great deal of help from the Ambassador and saw a number of interesting people, including the Deputy Foreign Minister. You are our last but one visitor. The Committee decided last week that it would invite the Russian Ambassador to come and give evidence to us, and he has agreed to come and do so on 7 February. As you know, we will be taking a note of this and you will be sent a transcript. Can I begin by saying that the European’s formal strategy document, the Country Strategy Paper for 2007–2013, is still based on the proposition that Russia shares “European” values and that these should form the bedrock of the EU-Russian relationship. Your division seems to have come.

Mr Murphy: Which will give me eight minutes to think of an answer!

The Committee suspended from 3.37 pm to 3.43 pm for a division in the House of Commons

Q393 Chairman: Minister, welcome back. I was referring to the Commission’s document, the Country Strategy Paper for 2007–2013, which is based on the proposition that Russia shares “European” values and that these should form the bedrock for the EU-Russian relationship. Do you feel that that represents current realities, and if it does not, does the European Union need to devise a new hard-headed strategy towards Russia which omits the requirements of sharing value but provides a timely approach to and perhaps a long-term framework for cooperation?

Mr Murphy: First of all, My Lord Chairman, thank you for the comments you made, in particular about our Ambassador in Moscow, and I will make sure that the appreciation of your Lordships is brought to his attention, because certainly the Foreign and Commonwealth Office think that Mr Brenton is doing a spectacularly good job in often very difficult circumstances, him and his team, so that is very much appreciated. Perhaps I could also introduce my two co-witnesses, Mr Latta, Head of Russia Section, and Mr Shearman, Head of CFSP Group. In terms of the specific question, I think the previous agreement reflected a reality as was, a shared aspiration and a shared belief that this is the way in which the European Union and Russia’s relations would evolve post-Soviet era. It reflected the wish of Russia at the time, the Russian leadership and the Russian people, and a desire by the European Union to have a sense that together we were part of a collection of nations which shared modern European values. I am sure part of our conversation today will be about whether that is still a valid assessment of the nature of Russia’s aspirations. I think a more beneficial approach is not to have a quasi-European values-type conversation but to embed our strategy on seeking Russia’s continued approval and adherence to multilateral agreements it has willingly entered into. I think that is probably a more constructive framing of our approach rather than a sense of, “We would expect you to sign up to exclusively European values.” It is about getting Russia to adhere to its already voluntarily agreed to commitments in the multilateral environment. I think that would be a more productive outcome. In truth, it also reflects the changing nature of Russian politics and Russian leadership.

Q394 Lord Anderson of Swansea: Minister, your paper in principle takes us through to 2013. Much has changed in the face of Russia. Is there, in your view, a case for a re-writing of the paper, or in any event presumably under the normal processes there will be revisions from time to time?

Mr Murphy: It has to stay relevant to the changes in the nature of the European Union, but also Russian politics and Russian governance. I think you are right in reflecting the change that there has been over recent years in terms of Russia’s posture on the international stage and a re-emergence of diplomatic confidence and international confidence, based
partially on the buoyancy of natural resources and partly because of the changing nature of the leadership at the top of the Russian Government. In fact, we have all rightly expressed opinion, observation, and criticism when appropriate, about the fact that the democratic space in Russia continues to contract. So it is important that as part of any successor agreements the obligations Russia has entered into internationally are reflected, and reflected in such a way that when Russian behaviour conflicts with those international agreements we are very clear about that.

**Q395 Lord Hamilton of Epsom:** The objective of this Committee is to actually suggest that the long-term membership of Russia in the EU should not be ruled out, which does not mean that you make it a candidate tomorrow. If Yeltsin had turned out to be competent and un-corrupt, I suspect we might well be talking in terms of it being a candidate now. Are we not slightly looking short-termist at Putin? This could all change in ten or twenty years time if Russia regards itself as a European nation. Should we rule it out indefinitely as a potential member of the EU?

**Mr Murphy:** In the short and medium term it is of fundamental national and international importance that the EU has a detailed agreed bilateral relationship, absolutely, in terms of trade and so many other issues. As to Russia and formal membership of the European Union, I suspect I will answer this in a similar way to how I have answered the question, “When will you invite Ireland to rejoin the Commonwealth?” A country has to apply and my perspective is that they are in no hurry to see him negotiate his replacement because it is not particularly popular with them in the sense that it is so restrictive. Russia has this view, understandable, that it wishes to be treated as an equal and it therefore becomes more difficult to re-negotiate or to modify, extend if you wish, an agreement which they do not see as treating them in the way they would wish to be treated by the EU. I wonder whether you might like to comment on that?

**Mr Murphy:** On the wider point about bilateralism versus multilateralism, first of all we do value, as the UK Government, very dearly our bilateral relationship with Russia in all sorts of ways—culturally in the art exhibition which has opened this week from Russia, which I have not had a chance to see myself, cultural ties, economic ties of phenomenal importance to the United Kingdom, and of course to Russia and the international environment those bilateral relationships are very important. I think Russia’s approach to these matters, Russia’s preferred position, is a series of bilateral relationships with 27 individual sovereign Member States. Of course, in instances that is inevitable, perhaps even desirable in some instances, but generally the United Kingdom and the majority of European partners do prefer to have a multilateral approach. Examples of that in recent cases, as your Lordships are acutely aware of, are the Litvinenko case and the case of the British Council. We were successfully put in a multilateral environment ostensibly by a bilateral dispute. Other Member States of the European Union can see the potential read-across to their own relationships with Russia, and I think that is the most effective way. The way one can explain it in the Commons in its relative shape, but nevertheless true, is that 27 voices with all sorts of different accents and different languages are much more effective than one when it comes to talking to Moscow. When it comes to the new PCA, the existing PCA stays in place. Of course, it is rolled over until a successor is agreed, but I think it is important and the Government believes it is important that there is a successor to it because again it is a creature of its time. It does not properly reflect the nature of the threat of terrorism. From my recollection, I do not think terrorism is mentioned. The word “terrorism” I do not believe is mentioned in the existing PCA. There is one passing reference to climate change. There is not enough on some of the other issues which have emerged since then, migration and other matters. So there is a need to update it to reflect the challenges which have emerged since, and those are some examples that we are working pretty hard to make sure are reflected in the new PCA.

**Q397 Baroness Symons of Vernham Dean:** Minister, you said 27 voices, but surely the point is that actually it is one voice on behalf of 27. I just wondered...
whether 27 voices (i.e. everybody behaving like a nation state) might not in fact be more effective, 27 ambassadors going and demanding a call, 27 prime ministers ringing up and saying, “I demand to make this point,” would be in some ways arguably more impressive than one voice saying, “I am speaking on behalf of 27,” and the Russians being able to say, “Well, you know, that’s all because they have to act by consensus and the Brits have persuaded them.” I just wondered whether that last point you made was really quite as compelling as you made it sound.

Mr Murphy: I think 27 voices with one message would be compelling, but one voice with one message speaking on behalf of 27 offers the consistency and the clarity, which I think is important in our dealings with Russia, because 27 individual voices offers the opportunity for finesse and nuances of message. I think it is important that there is one clear public message. I think your Lordships and I certainly would celebrate not discussing the Reform Treaty in any great detail, so it gives us another opportunity of welcome respite temporarily from that, but one of the important reforms in the Reform Treaty is the fact that we end this rotating presidency. On our relationship with Russia over the past two to three months, before Christmas we sought and achieved very strong support from our European colleagues. Under the Portuguese presidency we had to go through this chain of accountability and management of the process was through Lisbon. I have no complaint about that. The Portuguese were very helpful. But within three to four weeks we rightly saw another European statement. The chain of influence and coordination went through Ljubljana. It does complicate it, and I do not wish to draw your Lordships into a discussion, that is an opportunity which your Lordships will have another opportunity to observe the process. The electoral registers, the media coverage, the harassment of opponents, all of those sorts of issues are of fundamental significance when it comes to free and open the process was, long-term election observers, not tourists who pop in on the day of the election, wander around chaperoned to selected ballot boxes to declare how peaceful and open the process was, long-term and post-election observers unfettered who have the opportunity to observe the process. The electoral registers, the media coverage, the harassment of opponents, of course, of those sorts of issues are of fundamental significance when it comes to free elections and the observation of them, which Russia herself signed up to and is not adhering to.

Q398 Lord Hannay of Chiswick: Minister, you suggested that rather than use a sort of vague phrase like “shared European values” we should hold the Russians more to account on the commitment they have entered into internationally, by which I take it you mean the commitments under the Council of Europe’s founding documents and the OSCE’s Paris Charter. Do you think the conduct of the Russian parliamentary elections in December was consistent with their commitments under those two documents, and do you think the conduct of the presidential election, which kicked off yesterday against a background of one of the main potential candidates for the presidency being threatened with some rather obscure legal action, is consistent with those commitments?

Mr Murphy: If your Lordships would not find it disrespectful, there is a very straightforward answer to that, and the answer is, no. If your Lordships wish me to expand, I am happy to do so, but it is a very clear no. For example, the clear one in terms of the Duma election was the situation with the election observers, a very public and very clear international commitment that Russia herself entered into willingly now reneged on, and they then sought to share the blame with OSCE and ODIHR. The responsibility for that lies with Russia and Russia’s leadership. In terms of the presidential election there is still an opportunity, despite the incident which has been referred to, for Russia to make good her commitment in terms of international unfettered long-term election observers, not tourists who pop in on the day of the election, wander around chaperoned to selected ballot boxes to declare how peaceful and open the process was, long-term and post-election observers unfettered who have the opportunity to observe the process. The electoral registers, the media coverage, the harassment of opponents, all of those sorts of issues are of fundamental significance when it comes to free elections and the observation of them, which Russia herself signed up to and is not adhering to.

Q399 Lord Anderson of Swansea: Just a quick question on that. There was equally a number of commitments which Russia entered into at the OSCE in 2000 in respect of other matters which they now claim are not relevant because their then president was drunk and incapable and that they are seeking to resile from those agreements as a result on that excuse. Do we go some way towards accepting this?

Mr Murphy: President Yeltsin entered into agreements on behalf of his country, not on behalf of himself, and Russia should honour them.

Q400 Lord Hannay of Chiswick: Could we turn to the Energy Charter, Minister, and its Transit Protocol. As we understand it, the EU entered into a Charter in good faith with an aim of introducing transparency and a sound legal basis for the very large energy transactions between Russia and the European Union, but for reasons which I do not want to go into, and I do not think there is any need to go into, the Russians seem to have decided and to have communicated any number of times that they will not ratify the Energy Charter and its Transit Protocol. Do you assume now that whoever is elected in March that will remain the Russian position and
that there is virtually zero hope of getting the Energy Charter and its Transit Protocol as currently drafted into effect? If you do accept that, do you think there is any value in continuing to try to persuade the Russians to bring it into effect in the face of their determination not to do so? The third part of the question: in that case, is there any sense in trying to save as much as possible of what is in the Energy Charter and the Transit Protocol either under the negotiations for the new PCA or in the discussions on the four bases or in some kind of separate discussion about energy?

Mr Murphy: On each of those points, do we think that post the presidential elections there will be reasons to be more optimistic? Mr Medvedev, we know from his cv that he does not come from a similar background to many of the other prominent individuals and leaders in Russia, so there are some reasons to be optimistic; not naively so, but there are some reasons to be optimistic in terms of his background. I am not sure it would be helpful to second-guess the outcome of that, but the Charter is the only multilateral agreement in play. The additional difficulty we have, notwithstanding the dynamic of the Russian elections, is that Russia has been remarkably imprecise as to what her concerns are. That is the difficulty. It is difficult to respond to concerns which are general in term and in tone and imprecise on any detail. As to whether this should be renegotiated, it partially depends on Russia’s concerns, but we would also have to be convinced that in opening the process there was a political will at a senior level—and it comes back to the first question, of course—that there is a willingness to conclude something which is genuinely in our collective interest and which would then be adhered to. So there is no clear sense—there is an assessment but there is no assertion from Russia—as to what her concerns are with the current process and our assessment is that there is no compelling case that Russia is actually willing to enter into something which is binding and strategically worthwhile. In terms of whether it should be inside the new PCA, my understanding of the Charter is that it is more than, of course, just the EU and Russia, it is the EU, the former Soviet Union and Japan—and North America¹, I am told—so it is intricate in that nature. I think the best way forward is to remain with the Charter, willingly renegotiated if necessary, but only in principle entering into renegotiation if there is something worthwhile on the other side.

Q401 Lord Truscott: Minister, how much (if at all) does the EU need to worry about Russia using energy as a political weapon or at least a tool of foreign policy; and in that context do you have any views on the “Pipeline politics” controversies which there currently are—I am thinking of Nordstream and Nabucco, the South Stream recent agreement with Serbia, the proposed trans-Caspian pipeline system—and are we really witnessing a new great gain stretching from Central Asia through to the Balkans?

Mr Murphy: In general terms for Russia, energy sourcing, routes to market, is part of the wider geopolitics. That is clear by some of the activity. Our worry is not that there will be a wholesale turning off of the tap in future, our actual bigger worry, which I think I perhaps shared with your Lordship’s Committee in the recent past, is that our assessment is within five years with the level of current investment Russia will not be able to meet her domestic demand and her international obligations. That is the bigger concern which we have, very clearly, since I appeared before your Lordships before and that is not a concern which has disappeared at all. It still remains live in terms of the pattern of investment in the Russian energy infrastructure. In terms of the specific oilfields, I warned Mr Latta that this was a question I was going to ask him to make observations on, but certainly there is a number of principles which guide our approach. Firstly, the pipelines are driven by market and our assessment is that if that is the principle, then that would lead to a diversity of routes to market which should not give the European Union in general or any one nation in particular cause for specific concern. It is only when that market is distorted that that difficulty would arise. Therefore, alongside that first principle is the need for strong regulation of the market to avoid the distortion of competition, the distortion of the investment framework around the individual pipelines. As to the specific pipelines, I wonder if Mr Latta could offer his observations? It concerns Poland, it concerns Sweden and others around certain pipelines.

Mr Latta: My Lords, another element which would be key in all of this is the completion of a genuine internal market for gas and energy within Europe. So long as individual Member States are 100%, 90% or 70% reliant on gas from a single source, then there is an unhealthy reliance and a lack of diversity. Once the EU creates a single market, then you should be looking more at 25% of EU gas coming from Russia. That is the headline figure, as opposed to individual Member States importing 100% of their gas from any particular country. Moreover, once you have created a complete internal market and the only issue is that the gas which comes in on any one pipeline suddenly mixes with all the other gas in the network, the power of an individual pipeline to influence the market is reduced. So delivering on this internal EU process of improving the energy market will be a key element in maximising energy security.

¹ The United States and Canada are signatories to the 1991 Energy Charter and are observers to the Energy Charter Conference established by the 1994 Energy Charter Treaty.
Q402 Lord Truscott: I appreciate, Mr Latta, that is the theory but it is difficult to actually implement that, is it not, when the EU Member States cannot agree themselves on the unbundling proposals, for example, liberalising the EU market? Whilst the EU market is not liberalised, that gives the Russians the opportunity to work bilaterally within the market and to develop bilateral relations rather than working in an open, free market?

Mr Murphy: In terms of the unbundling, usually the Government’s argument is well-rehearsed unbundling. In principle we supported the UK citizens’ benefit from the competition which is provided in the UK. Many millions of UK citizens have their power supplied by other European companies. The evidence is that unbundling increases investment and reduces cost, and that is important in the current environment. I think other European citizens should have that opportunity, and so should UK companies. There are some proposals, again as yet unspecified, about a third option from the Commission motivated partly, I think, by German concerns, but again the difficulty is that we are unable to respond to speculation about a proposal which has not yet been tabled. But we are waiting to see the specifics of this as yet to be announced third option from the Commission on completing the energy market. Also—and Mr Latta mentioned this—the tone of the conversation in respect of reliance on Russian imports and Russian gas is different, of course, in different capitals. Lithuania, Latvia and Bulgaria are 100% reliant on imports of Russian gas. Ourselves, Ireland, Sweden, the Netherlands and some others have zero imports of Russian gas. So the tone and the nature of the debate, for understandable reasons, is different in different capital cities but the important thing is to try and get European agreement around this 25% figure.

Q403 Lord Hamilton of Epsom: My question follows on from that. Some of the evidence we have been given indicated that it is in no way in Russia’s interests under any circumstances whatsoever to unbundle either their monopoly of gas supplies or their control of the pipelines, so are we not rather wasting our time believing that is going to happen? The greatest beneficiary of unbundling might well be the European consumer if we had a European grid system which actually extended over the Continent of Europe. Would we not be better off concentrating really on our own home areas rather than trying to bash away at the Russians, who are not going to move on this anyway? It is a complete waste of everybody’s time.

Mr Murphy: We do think it is still worthwhile to continue to press the Russians on it for the reasons we have already spoken about, and we are making progress. Some of the moves in terms of the extension of qualified majority voting, for example, on energy policy may help in this direction and reduce the opportunity for protectionist tendencies within the European Union to block the completion of the single market on energy. It is an added opportunity to give impetus to the completion of the single market on energy, so it is about doing both in parallel.

Q404 Lord Anderson of Swansea: Future generations may say that by failing to have a degree of solidarity against Russia we allowed the tentacles of Russian influence to spread all over Europe. Lord Truscott mentioned the recent purchase of the Serb gas company, the way Bulgaria has reached a pipeline deal with Russia which will lead to spurs going to Austria and Hungary, and in one sense the pass has been sold. We have no grid. Already the Russians appear to have a very substantial influence. What are the prospects of having solidarity, given the fact that when we in the UK did not need solidarity during the good days of North Sea gas in the eighties we were not very keen on it? Are there any real prospects of Europe as a whole having an “all for one and one for all” policy, or is it much too late to do that?

Mr Murphy: I do not think it is. I do not think, if we are all frank with one another, we are ever going to enter into a position where there is going to be a unanimity of approach on every issue. I do not think there is much mileage in investing vast political capital in a deal on unanimity on every issue, but on the big strategic issues it is of fundamental importance, and that is the importance of the success of the PCA agreement, particularly the matters I alluded to earlier which are not currently contained within the existing PCA. Those issues I referred to earlier, climate change, terrorism, migration, and others are judicial cooperation, are the issues which the European Union collectively will seek to form the content of the success of the PCA. It is on those very strategic issues that there is a collective position.

Q405 Lord Anderson of Swansea: Not on strategic energy?

Mr Murphy: I have explained some of the difficulties around that to your Lordships, the reliance of Bulgaria in particular. I think Bulgaria is one of those countries which are 100% reliant. Tone of the conversation is different in different capital cities. The solution to this is, as we alluded to earlier, the

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2 It is difficult to measure for certain the exact volumes of Russian gas imported into the UK. There are no direct gas imports to this country from Russia. Technically the UK can import Russian gas by pipeline only via the Bacton-Zeebrugge Interconnector or the Balgzand-Bacton pipeline (BBL). Given significant Dutch gas production, gas imported via BBL is probably Dutch. Thus the Bacton-Zeebrugge Interconnector is likely to be the main source if any Russian gas imported into the UK. In 2007 imports from Belgium are likely to account for only about 0.5% of inland consumption, making that the absolute ceiling for imports of Russian gas.
twin process of continuing the market inside the EU and energy unbundling inside Russia.

Q406 Lord Anderson of Swansea: But the latest developments certainly assist the Italian-Russian South Stream. Are we assuming that the recent developments are likely to undermine the attempt to have a diversity of supply through Nabucco?

Mr Murphy: Again, with your Lordships' permission, I would ask Mr Latta to talk about some of the individual pipelines, if he is in a position to do so.

Mr Latta: There is a tension inevitably between the competitive agendas for individual pipelines—these are businesses after all—and the geopolitics of the source of gas, the route that it takes to market. South Stream is clearly in competition with Nabucco. If I was a businessman I would talk about the value options provided by the pipelines being distinct to Europe, in that Nabucco does provide diversity of route and supply, while South Stream provides some diversity of route but not of supply. It is for the consumer and for the European Union of 27 to assess the value to us of these different options, to what extent is security important versus the simple cost. Additionally, obviously, there is the question of how much individual pipelines would cost. Therefore, if you move all of these questions to a more commercial footing, the cost of gas coming through them becomes clearer and the consumer ultimately is better informed to make a decision.

Q407 Lord Truscott: If I may make a brief comment on the question, will Nabucco really improve security of supply as far as the EU is concerned because, as the Minister said, the real issue is future shortfalls in the Russian gas supply, and if there are those shortfalls then we are going to have a problem in terms of future supplies for Europe, whether Nabucco exists or not? My second point is really for the Minister. Are we really talking about reciprocity in our relations with Russia in terms of unbundling and open access to markets and pipelines? My understanding at least is that that is not the policy of the Government, that we are not asking for pure reciprocity with Russia, because that is certainly not the case with, say, Saudi Arabia.

Mr Murphy: We are attracted to reciprocity as a principle guiding this. In terms of the other point about Russia five years hence—it is less than five years now in terms of the assessment—in addition to what Mr Latta has already said and what I have alluded to, an additional component of the solution to this is a different business environment where we all have business contacts in Russia, where the degree of bureaucracy (bureaucratic interference, to put it as neutrally as possible) is such that transparency in the market, operation in the market—because notwithstanding the phenomenal UK investment in Russia, the fact is that on occasion investors and business people continue to find that the market is not transparent enough. Again, I put it gently. So that is part of the solution in terms of the investment environment. The second in terms of the five year timeframe is just energy efficiency. Where we can be critical in general and in some specific terms, Russia is intellectually absolutely seized of the energy efficiency argument, which as we all know is a clear read-across in terms of climate change policy, and in fact in some cases engaging with Russia on climate change is much more effectively done through the argument of energy efficiency rather than a way which would be extreme in the United Kingdom.

Q408 Lord Hannay of Chiswick: Surely, Minister, it all comes back to the point you put your finger on, which is the doubts we all have about whether Russia is or is going to invest enough in its gas industry to provide the demand which Europe as a whole is going to put on it. We have heard a lot of evidence, quite compelling evidence, which says that they are not investing enough and that, moreover, they are not going to run their depletion policy to suit us. When one sees not only the developments in Serbia or Bulgaria but also, for instance, their proposal to spend a great deal of money in Nigeria you are left with the feeling that they are not waking up every morning in a sweat wondering how they are going to provide enough gas for the Europeans in five or 10 years’ time. If that is so—and you have put your finger on that issue yourself—then surely the very large investments which would need to be made to have an alternative supply from Turkmenistan, Kazakhstan, and so on, through a pipeline of the type of Nabucco is something which Europe may have to contemplate even if it costs an awful lot of money up front, because finding out in five or 10 years’ time that the Russians are not supplying enough and that the price is going through the roof is not going to be a very comfortable position to be in?

Mr Murphy: In terms of the point about the profile of current investment, our assessment is that the current trajectory of investment and the publicly announced investment portfolio is not substantial enough to meet the obligations I alluded to earlier. It is not just a matter of the Russian state or Gazprom investing, it is also about the business environment. The degree of openness for foreign investment in the sector in Russia is an important component of this debate. In terms of whether the solution to it is the European Union collectively investing in a pipeline network through Central Asia, I return to almost where I started, which is that really if we set a business environment which allows the market to dictate pipeline directions and diversity of routes to market, that gets us to where we need to be. The short answer
to this is that the European Union has not been and is not attracted to the colossal degree of investment which it would require. Your Lordships may, of course, have a different perspective on it and in five years’ time you may say, “Why didn’t the European Union do that?” but it is not currently, I think, in the short term expected to be part of any European agreement with the vast capital investment it would require.

Q409 Lord Selkirk of Douglas: May I ask about what you, Minister, consider to be the most effective way of making clear to the Russians our concerns about violations of human rights? It has been made clear to us that they do not wish to accept lectures from the European Union about domestic political matters. How would you suggest representations should be made which are not counterproductive and which are highly persuasive?

Mr Murphy: I think there are two components to that response. Firstly, which might sound a little counterintuitive, at one level we will continue to support NGOs, civic society, in Russia, even though on occasion that then allows them to be singled out as agents of a foreign government, which is regrettable and does not bear any analysis. For example, we provide funds to the equivalent of the National Union of Journalists in Russia and programmes on prison reform, sensible, reasonable, international norms in both fields. In terms of the most effective way, I think to some degree we have each individually reflected on it in our own way, to come back to this point about on all occasions seeking to do it in a multilateral environment and to contextualise it in terms of agreements which Russia herself as a proud sovereign nation signed up to. I know perhaps each individual would think, “Why don’t we just say this?” but it is counterproductive at all sorts of levels and will not achieve the desired response. It is in the context of international agreements and the multilateral approach, not just the EU but through others, the G8 and others.

Q410 Lord Anderson of Swansea: Minister, over the past six months Russia has hardened its position on Kosovo. It is very likely that after the second round of the presidential elections in Serbia independence will be declared unilaterally and that the Russians will probably prevent any recognition within the United Nations Security Council. Do you see any hopeful prospects at all of Russia’s position in respect of Kosovo moving positively?

Mr Murphy: Not at the moment. Forgive me if that was rather frank, but not at the moment. We have been through a process with the United Nations. We have had a period of discussions through the Troika process. I think we have exhausted that process. The solution now is a coordinated (rather than unilateral) declaration of independence based on the Ahtisaari plans. We remain absolutely convinced of the merits of the Ahtisaari proposals and that the international community has a responsibility entered into in 1999 that we need to fulfil. In terms of the UN process, individual Member States will recognise an independent Kosovo and I think the European Union has a responsibility to create a reality on the ground by a prompt, coordinated response and recognition of Kosovo’s independence to influence the situation on the ground and influence the diplomatic response throughout the rest of the world, not just within the European Union.

Q411 Lord Swinfen: What does this mean for the EU’s increasing responsibilities in the Western Balkans?

Mr Murphy: Some of those who oppose the impending outcome in Kosovo try to overstate the read across the whole of the Balkans and this has a substantial fundamental impact on, for example, Bosnia. The way in which we argue this is that the international community has taken a different response to those issues in the Dayton Accordant and one of the Ahtisaari proposals on the other, so I think there is a willingness across the bulk of the international community to keep the momentum on a solution on each to continue without contaminating one with the other, but I accept in this process that others in fact from our assessment who have neither Kosovo’s nor Bosnia’s interests at heart can contaminate one with the other. Allied to this and of fundamental importance is that whilst never seeking to interfere in Serbia’s elections—the people of Serbia will make their own judgment—the UK’s view is that Serbia has a decision to make which will influence her future for many years to come, but that depending on the posture and the response from the newly-elected government, whichever colour or shape it chooses to be it should have a European perspective, to put it euphemistically, for the opportunity to be part of the European family if it so wishes, as Kosovo should as well. So it is important that Serbia is fully aware—and we will seek to make sure this is the case—of the potential benefit of a successful outcome in Kosovo.

Chairman: Thank you.
Supplementary memorandum by Jim Murphy MP, Minister for Europe, Foreign and Commonwealth Office

I wanted to take this opportunity to make a few observations on the evidence session that the Committee held on 7 February with His Excellency Yuri Fedotov, the Russian Federation’s Ambassador to the UK.

EU-Russia relations

There are many areas on which I agree with the Ambassador. He characterises the relationship between the EU and Russia as one of interdependency. That is exactly how we see it. This is not an arcane point: that interdependency lies behind our wish for a strong, comprehensive partnership between Russia and the EU. I welcome the Ambassador’s continued commitment to a replacement to the current Partnership and Cooperation Agreement. We want that too.

I welcome his view that the new agreement will be legally binding. That is extremely important. And I welcome his saying that he wants the EU and Russia to cooperate on counter-terrorism, though I cannot but point out that Russia has suspended counter-terrorism co-operation with the UK. (It is not true, as he claims, that the UK has suspended co-operation. We co-operate with a range of Russian agencies in international fora such as the G8 Roma-Lyon Group. Moreover, were we to become aware of a likely terrorist attack on Russia or Russians, we would inform the Russian government. I hope Russia would do the same).

Litvinenko

Overall I am pleased that the Ambassador sees partnership as a necessary dimension of a successful Russian foreign policy. Equally, a partnership with Russia is of crucial importance to the EU. But partnerships rely on trust and mutual confidence. And it is on this point that my views diverge from those of the Ambassador. He says that issues such as the Litvinenko case are bilateral problems and not matters for the EU. But there were very sound reasons why the EU saw the situation very differently. Russia’s failure to co-operate constructively on the case raised wider concerns among EU member states about Russia’s approach to judicial co-operation and the rule of law. The case, you will remember, was immensely serious: a British citizen murdered in an EU capital, with hundreds of citizens from 18 EU countries put at risk of radiation poisoning. It is no wonder the EU reacted so firmly.

British Council

Similarly serious concerns underlay the EU’s public criticism of Russia over its treatment of the British Council. The Ambassador confirms explicitly that Russia’s assault was related to the Litvinenko case. I welcome his candour. But I am sure your Committee shared my astonishment that Russia was linking unrelated areas of business, thereby damaging cultural and educational partnerships built up over many years and compounding one failure to uphold the rule of law with another. Mr Fedotov says that the British Council’s activities lacked a firm legal foundation and that the 1994 agreement only mentioned the possibility of opening cultural centres, and that these needed a special additional agreement. That is wrong. The 1994 agreement commits each party to encouraging the establishment, in its territory of cultural, education and information centres of the other party. The agreement does say that the activities of such centres may be the subject of a separate intergovernmental agreement. But this is not a requirement. That is why Russia’s attacks on the British Council are illegal.

Difficulties in developing cultural relations with Russia are not confined to the British Council. On 8 February, the Russian authorities forced the European University in St Petersburg to suspend its operations, citing fire regulations. This followed a visit by tax inspectors to one of the university’s European Commission-funded projects. The project in question had been providing courses, training and publications on election monitoring.

I should point out that the Ambassador observed that Russia does not have cultural centres in the UK. But this is not for any impediment on our part. We would welcome the establishment of Russian cultural centres in the UK, as provided for by the terms of the 1994 Agreement.
Visas

The Ambassador is simply wrong when he says that our visa regime is impeding people-to-people contacts. More Russians than ever are receiving visas to the UK. The visa measures announced by the Foreign Secretary in July 2007 in response to Russia’s failure to co-operate on the Litvinenko case only affect Russian Government officials. No further visa restrictions have been imposed since those measures were introduced. Indeed, we are going out of our way to improve our visa service to Russian citizens. Business travellers enjoy an express visa service. And an online application service will start operating later this month to speed up the visa application process.

But even if this were not so, we could not accept the Russian proposal that we resume talks with Russia on visa facilitation in return for resuming negotiations on a Cultural Centres Agreement that might let the British Council reopen in St Petersburg and Yekaterinburg. I am sure your Committee would be astonished if we accepted the Russian linkage between the two issues.

Kosovo

Ambassador Fedotov also discussed Kosovo in some depth. In what will be an important week for Kosovo’s future, I should not let this opportunity pass to make some remarks on the Ambassador’s points. He suggests that Russia is not opposed to Kosovo’s independence per se, but to the fact that it will be imposed on Serbia against its will. He also says that the negotiations under the Troika showed signs that an agreement between Belgrade and Pristina might be within reach. This is at odds with our assessment, which tallies with the clear view of Ambassador Ischinger, the EU representative in the Troika. Ambassador Ischinger believes that the parties would not be capable of reaching agreement on this issue if negotiations continued, whether in the Troika format, or in some other form. Prime Minister Kostunica made it very clear to the Troika more than once that Belgrade would not entertain any proposal that did not close the door reliably on independence. The UK’s firm view is that in the absence of agreement between the parties, the UN Special Envoy’s Comprehensive Proposal for a Kosovo Status Settlement, providing for supervised independence, is the most viable way forward.

Ambassador Fedotov also says that Kosovo’s independence will set a precedent. Our position remains that, as a matter of principle, there is no universal blueprint that can be applied to every separatist or post-conflict scenario. Each is unique, and individual criteria should be applied. In the case of Kosovo, there are particularly strong grounds for seeing it as unique:

— Its substantial autonomy under the 1974 SFRY constitution was brushed aside by Milosevic in 1989.
— Sustained oppression followed, including violent oppression by the Yugoslav army in 1998-9.
— NATO intervened in 1999 to avert a humanitarian catastrophe.
— UNSCR 1244 was adopted in 1999 as the authority for the UN to govern Kosovo.
— Competence and authority have gradually been transferred to the Kosovo provisional institutions, including the establishment of new ministries.
— UNSCR 1244 provides for a political process to determine Kosovo’s final status.
— We are at the culmination of that process after 14 months of intensive negotiations under [Mr Martti] Ahtisaari, including 15 separate rounds of talks and 26 visits to the region, and an additional four months under the EU/Russia/US Troika.
— This is a sui generis framework without which we might have had to address the status issue earlier in more violent circumstances.

Notwithstanding Russia’s current position, Contact Group Foreign Ministers agreed in January 2006 that ‘the character of the Kosovo problem, shaped by the disintegration of Yugoslavia and consequent conflicts, ethnic cleansing and the events of 1999, and the extended period of international administration under UNSCR 1244, must be fully taken into account in settling Kosovo’s status’.

On the legality of the EU mission, our view is clear: UNSCR 1244 provides for the deployment of international police officers as part of a civil administration to help the local authorities to keep law and order. The ESDP Police and Rule of Law mission will draw its authority from the resolution.

Finally, the Ambassador was right to highlight Russia’s support for international peace support operations. The UK is grateful for Russia’s contributions to date, in particular with capabilities in short supply such as helicopters, and would very much welcome continued and increased Russian support for EU, NATO, UN and other international operations, including through the contribution of helicopters, ground forces and other
capabilities. I am glad that Ambassador Fedotov had the opportunity to make this, and his other points, to the Committee. Whatever our views of his arguments, his contributions add to the serious discussions at hand.

18 February 2008

Further Supplementary memorandum by Jim Murphy MP, Minister for Europe, Foreign and Commonwealth Office

I note the comments that the Russian Ambassador made on the provision of transport helicopters for the EU operation in Chad. I can confirm that Russia has been in consultation with the EU Council Secretariat regarding this proposal, and confirm too that in principle we would very much welcome a continued and increased Russian support for EU, NATO, UN and other international operations, including through the contribution of helicopters, ground forces and other capabilities. I will update the Committees on any progress that is made in relevant negotiations.

We continue to work with all of our international partners on measures to address the global helicopter shortage. The Committee might also be interested to know that the UK has been the primary driving force in promoting NATO initiatives to identify means to generate and mobilise increased helicopter capability among member states.

9 March 2008

Further Supplementary memorandum by Jim Murphy MP, Minister for Europe, Foreign and Commonwealth Office

I very much welcome the interest of the Select Committee in this issue. It is vitally important for the security and prosperity of our citizens that we respond effectively to climate change.

You raise the implications of climate change for the EU’s long-term relations with Russia. Climate change will indeed have an impact on our relations. The EU’s ambitious targets to reduce greenhouse gas emissions agreed at last year’s Spring European Council will drive a restructuring of Member States’ energy economies. This will have significant implications for the EU’s energy partners, including Russia. The effects will be complex, and it is important that we share our thinking with partners like Russia as we implement the ambitious package agreed last year. In addition, as we transit to low-carbon ourselves, we will be developing technologies which may eventually be interesting for Russia’s own response to climate change. It is therefore essential that EU/Russia dialogue on climate and energy helps us understand and take account of each other’s interests. We also need to work with Russia bilaterally and through the EU and other international organisations on securing an equitable and ambitious post-2012 agreement under the UNFCCC (United Nations Framework Convention on Climate Change) process. There are a number of formal processes in which this dialogue can take place: the current EU/Russia Partnership and Co-operation Agreement (PCA), and the draft negotiating mandate for a successor to the PCA, which also covers climate change.

In addition, the draft PCA successor mandate covers conflict prevention and resolution and security co-operation between the EU and Russia: this could include conflicts caused, worsened or prolonged by the effects of climate change.

The EU has also instituted an Energy Dialogue with Russia, one of the main focuses of which is the promotion of energy efficiency in Russia, based on the two sides’ common interest in reducing the energy intensity of Russia’s GDP. Achieving progress in this area would significantly enhance Russia’s contribution to combating global climate change.

With regard to international development, there is a real risk that much of the economic and social progress developing countries have made in recent years could be wiped out by climate impacts, pushing greater numbers of people into spiralling poverty. DFID has been very active in following up the issues highlighted in the above report and I can confirm that DFID was consulted in the preparation of the Explanatory Memorandum. My officials continue to be in regular contact with their DFID counterparts (as with those in other key Government departments) and we will ensure DFID is closely involved in taking forward follow-up recommendations to be discussed in the Council.

On the European Security Strategy (ESS), climate change will certainly be one of the areas addressed in forthcoming ESS work as it did not have sufficient prominence in the 2003 Strategy. We will want the forthcoming examination of the implementation of the ESS—and, as appropriate, proposals to complement it—to take account of the security dimension of climate change. This point is made in the High Representative’s report.
In conclusion, the FCO will be following progress in this area very closely and will continue to liaise with the Solana Cabinet and the External Relations Directorate of the European Commission to ensure that the recommendations produced for the December Council take account of our priorities and offer the best possible outcome for future action. We very much welcome your involvement in achieving this aim, and would encourage parliamentary committees to include discussion on climate change as a security issue whenever they travel overseas.

15 April 2008
THURSDAY 7 FEBRUARY 2008

Present

Anderson of Swansea, L
Chidgey, L
Crickhowell, L
Roper, L (Chairman)

Selkirk of Douglas, L
Swinfen, L
Symons of Vernham Dean, B
Truscott, L

Examination of Witnesses

Witnesses: His Excellency Mr Yury Viktorovich Fedotov, Ambassador of the Russian Federation, and Mr Andrei Pritsepov, Senior Counsellor, examined.

Q412 Chairman: Good morning. Ambassador, as I think you know, this Sub-Committee is carrying out an inquiry, and has for some months been carrying out an inquiry on relations between the European Union and the Russian Federation. We very much welcomed our opportunities in Moscow in December to meet some of your colleagues in the Foreign Ministry and elsewhere and in the Federation Council. We had very useful discussions but we felt that, before we completed our inquiry, we would very much like to put some final questions to you. We are very grateful to you for having agreed to come to see us this morning. We are taking a note of this and the proceedings are being televised but you will be sent a transcript of what has been said in this morning’s session and you will obviously have an opportunity to make any corrections to it. I do not know whether you have an opening statement you would like to make or whether you would like me to ask the first question.

Mr Fedotov: Thank you very much, Lord Roper, my Lords. It is an honour for me to be invited to share with you some of my thoughts about the Russia-EU relations. When you were in Moscow you met with my colleagues and you have heard much more professional estimates of the prospects of our relations. Nevertheless, I am prepared to answer any of your questions. To start with, let me just say a few words to provide the right framework for our conversation. First of all, there are two obvious facts. Russia is Europe, from any possible point of view, be it geography, history, culture, economy, politics, ideologies—by the way, socialism and communism are not Russian inventions—philosophy, human values, relationships, family ties, et cetera. Secondly, Europe without Russia is not Europe in its all-inclusiveness, so any dream of creating a pan-European co-operation without Russia is a myth. This interdependency between Russia and Europe creates a favourable background for relations between Russia and the European Union. As you know, we have always been keen and eager to enhance our interaction with the European Union because we take it from a very pragmatic perspective. It helps Russia to meet new threats and challenges in a globalised world. We believe it helps Europe to do the same. I am prepared to have a discussion with you and to answer your questions and I do not mind if you continue this in an open, televised manner.

Q413 Chairman: Thank you very much indeed. You have to some extent addressed the first question I was going to ask but I will pose it because you might want to develop it. What do you see as the overall policy objectives of the Government of the Russian Federation towards the European Union?

Mr Fedotov: I think the overall framework of our policies towards the EU, at this stage at least, could be defined by quite a simple formula: anything but institutions. This means that Russia is prepared to establish as close co-operation with the EU as possible but without being its formal member. We have made our fundamental choice in our foreign policy in favour of forging a strategic partnership with the EU, and it stays, beyond any doubt, one of the priorities of the Russian Government. Partnership with the EU and leading European nations has always been and continues to be a sine qua non, a necessary prerequisite for a successful foreign policy of Russia. The objective of this approach, as I said, is very pragmatic. It is no secret that we seek closer relations with the EU as the best means of ensuring Russia’s interests in a global world. I think these ties are equally vital for both sides. Only by combining our efforts can we withstand global threats and challenges, and we are determined to continue this course of action.

Chairman: Thank you very much indeed. Before going to the second question, I should apologise to Mr Pritsepov that I did not also welcome him to our meeting this morning. Obviously, if at some stage he wishes to add to something, we would be very glad to hear from him as well and I apologise to him for not welcoming him.

Q414 Lord Anderson of Swansea: Ambassador, welcome. It is probably fair to say that Russian relations with the European Union are going through a fairly chilly period at the moment, not only the individual matters, Estonia, Polish meat, the
Frankly speaking, I would not place all these matters you have enumerated in one box as they are so different one from another. There are strategic relations between Russia and the European Union and there are basic foundations of these relations. One of the most important cornerstones of our partnership is trade and economic relations. The trade balance between Russia and the EU between 2000 and 2007 has enjoyed a fivefold growth. To date, 50% of Russian foreign trade is generated from co-operation with the European Union. Last year it amounted to £140 billion sterling. European countries account for 70% of all foreign accumulated investments in Russia. So it is important for us to keep this co-operation. My country is among the top three exporting countries to the EU and among the top four countries importing European goods and services. As to energy supplies, it is a well known fact that Russia is the number one supplier of natural gas to Europe and the second biggest oil supplier. As for problems with individual EU members, we are trying to resolve them one by one. We are very close now to signing two protocols with Poland on the export of meat and also on other agricultural production. Today the new Prime Minister of Poland commences his visit to Russia. This is an important visit and a wide range of issues will be discussed, bilateral issues, including some sensitive legacies of the past, but also the future of our relations and outstanding international problems, including the controversial plans to deploy an anti-missile system in Poland. We expect it to be a successful visit. As far as Mr Litvinenko’s case, once again, I can say what I say repeatedly to my British colleagues, that that is a bilateral issue which needs to be discussed between the Government of Russia and the UK Government. We do not think that is a matter for the EU. The idea is a free trade zone, which is also under discussion and we can come back to this matter. We have set up a special committee on energy policy, as you know, and we believe that this committee should work more actively. So there are many areas where we can successfully co-operate and enhance our relations with the EU as such and with individual members of the European Union.

Litvinenko affair, but also where the European neighbourhood policy coincides with Russian views of its own neighbours, such as Ukraine. How do you see the current situation in relations between the Union and Russia?

Mr Fedotov: Frankly speaking, I would not place all these matters you have enumerated in one box as they are so different one from another. There are strategic relations between Russia and the European Union and there are basic foundations of these relations. One of the most important cornerstones of our partnership is trade and economic relations. The trade balance between Russia and the EU between 2000 and 2007 has enjoyed a fivefold growth. To date, 50% of Russian foreign trade is generated from co-operation with the European Union. Last year it amounted to £140 billion sterling. European countries account for 70% of all foreign accumulated investments in Russia. So it is important for us to keep this co-operation. My country is among the top three exporting countries to the EU and among the top four countries importing European goods and services. As to energy supplies, it is a well known fact that Russia is the number one supplier of natural gas to Europe and the second biggest oil supplier. As for problems with individual EU members, we are trying to resolve them one by one. We are very close now to signing two protocols with Poland on the export of meat and also on other agricultural production. Today the new Prime Minister of Poland commences his visit to Russia. This is an important visit and a wide range of issues will be discussed, bilateral issues, including some sensitive legacies of the past, but also the future of our relations and outstanding international problems, including the controversial plans to deploy an anti-missile system in Poland. We expect it to be a successful visit. As far as Mr Litvinenko’s case, once again, I can say what I say repeatedly to my British colleagues, that that is a bilateral issue which needs to be discussed between the Government of Russia and the UK Government. We do not think that is a matter for the EU.

Q415 Lord Anderson of Swansea: Colleagues will be coming to the bilateral matters. These are issues where the European Union has shown solidarity in respect of Russia. The question I would like to ask now basically is how do you see relations between the Union and Russia developing over, say, the next five years? As you have said, trade relations are pretty sound. There have been a number of political problems. Where do you see the major problems arising and, perhaps more important, where do you see the most positive areas for co-operation between the Union as such and Russia?

Mr Fedotov: Recently there have been some new developments, not only in trade and economic relations. We have passed an important agreement with the EU on visa facilitation and readmission and this agreement is already in force. It helps people from Russia to travel to the EU, it helps Europeans to travel to Russia. Even more, we have started discussing the possibility of a visa-free regime between Russia and the European Union. Another idea is a free trade zone, which is also under discussion and we can come back to this matter. We have set up a special committee on energy policy, as you know, and we believe that this committee should work more actively. So there are many areas where we can successfully co-operate and enhance our relations with the EU as such and with individual members of the European Union.

Q416 Baroness Symons of Vernham Dean: Ambassador, your answers to Lord Anderson’s questions seem to me to imply that you are very happy dealing with the European Union, with the Commission, with the Council Secretariat on issues of trade but when it comes to other issues, you prefer to deal bilaterally. You spoke particularly about Poland and you spoke about Poland a moment or two ago. Have I misinterpreted or over-read your remarks? What is your view about the relative importance of dealing with the EU through the Commission and the Secretariat rather than dealing with the countries of the European Union bilaterally? You seem to put a lot of emphasis on, I think you said, resolving the issues one by one.

Mr Fedotov: That is a very good question, Lady Symons, and I will try to answer this question. Yes, indeed, it is very important for Russia to maintain a great deal of contacts with the European Commission and even with the Council Secretariat but I would not oppose this to the bilateral context. Even in trade and economic relations, the results we have achieved are mainly due to our bilateral relations with individual EU members, including with the UK. Some matters are being dealt with with the Secretariat but there is always a combination of our interaction with the European Commission and member-states. That is true not only for trade and economic relations; it is also a quite applicable procedure for our political relations. We have special settings to discuss outstanding political issues, be it Middle East, Iran, Former Yugoslavia, human rights, in Brussels with appropriate groups of the EU, but we are also discussing these matters individually with EU members. So I think we are doing both. It is equally important to engage with both respective players, be it multilateral institutions or individual Member States.

Q417 Lord Crickhowell: Can I follow up on that particular question, because this Committee is looking at the way that Europe should operate and develop its policies. Perhaps one of the criticisms that
we might make is that in the past Europe has not been very good at getting its act together, so we have not always presented a European point of view to Russia. Could I put it to you quite straight: do you not find that there is an advantage in that situation? You find it quite useful in negotiating with Europe to be able to pick off the individual countries on individual issues. The fact that Europe is not united or has not in the past been united has proved a tactical advantage. We will come on to energy later but it is an obvious area. Do you find it uncomfortable really dealing with Europe on some issues and do you as a country really prefer to deal with the individual countries because it is easier to come to agreements or perhaps to divide Europe by dealing in that way?

Mr Fedotov: Yes, I think it is of major importance to avoid situations when co-operation between Russia and the EU is held to ransom because of bureaucratic discrepancies or inconsistencies of multilateral institutions or political problems among individual EU members. It is for this reason we would prefer to deal with a strong and united European Union rather than with a weak and divided alliance, with several competing groups of countries, which are sometimes unpredictable and non-transparent. We hope that the EU will soon accomplish its long-awaited cycle of institutional reforms, and this fact will boost its political performance and will help us to engage directly with the European Union. When this day will come we will have to see.

Q418 Lord Crickhowell: That takes us quite neatly to the fourth major question in dealing with Europe, the actual structures that Europe has in place. When some of us were in Moscow before Christmas we visited the EU Commission office in Moscow but much of the relationship will be conducted in Brussels with the Commission. Do you find that arrangement difficult or are there changes that would make it easier for Russia to do business with Europe if the arrangements were different?

Mr Fedotov: I think the Russian representation in Brussels is one of the largest Russian diplomatic missions abroad, comprising 150 diplomats, not only professional diplomats but also experts on specific matters such as agriculture, customs, internal affairs, everything, and that is a very active diplomatic mission. However, it does not mean that, because we have such an active diplomatic mission in Brussels, we are going to close our embassies in the capitals, including in London. The same is true with the office of representation of the EU in Moscow. Of course, I think that my colleagues, the heads of the diplomatic missions, the EU diplomatic mission in Moscow and Ambassador Chizhov, who is in charge of our relations in Brussels, would have given a more detailed and professional account of the situation, but I think we are happy with how this system operates. Of course, there is always room for improvement but it depends also on the level of progress in the institutional reforms in the European Union.

Q419 Lord Chidgey: Ambassador, I want to ask you, if I may, a few questions about the Partnership and Co-operation Agreement between Russia and the EU. In your opening remarks you made it very clear that Russia’s view and policy was that it is almost a given, as we would say, that Russia has very strong partnership links with the EU; it is the point of reference for Russia and Europe but, as we know, of course, at the moment the renewal of the Partnership and Co-operation Agreement is, I suppose we could say, stalled. I wonder what you think the consequences of the Russian Government is of the prospects for that being renewed. What are the weaknesses, as far as Russia is concerned, within the existing agreement and how useful has the co-operation been? Does it still reflect continuing commitment to the four Common Spaces concept? What alternatives do you see?

Mr Fedotov: Thank you for your question. We are not over-dramatising the situation. We are not over-dramatising the fact that now we are witnessing a pause in the consultations on the future of our basic agreement. Moreover, we think this period of reflection has given us an important and necessary opportunity to understand better whether our relations are progressing towards a strategic partnership or not yet. At the previous Russia EU summit in Sochi in 2006 our leaders agreed that the existing PCA will remain in force until it is replaced by the new agreement. From the legal standpoint there is no vacuum and we still have a legal basis which can be renewed as long as it is possible. So I do not think that the existing PCA has many weaknesses, as you say; maybe only one. It was signed over 11 years ago with a different European Union. We would prefer to have a new document but there is nothing wrong with the current PCA. We are not in a hurry. We want to work out a solid document, a new agreement, which already has the tentative name of Russia EU Treaty on Strategic Partnership, which should become legally binding, a politically heavyweight, forward-looking framework document, aimed at facilitating a balanced development of the system of sector agreements. It means that this agreement should be complemented by other agreements, whether it be non-proliferation, co-operation in fighting organised crime, counter-terrorism, immigration, asylum, et cetera. To sum up, we are reasonably satisfied with the current agreement but we are looking forward to getting a new one.
Q420 Lord Chidgey: Could I just ask, as a supplementary, two particular points. Could you tell us what is the Russian Government’s view on the fact that the existing agreement I do not think mentions terrorism at all? You mentioned counter-terrorism in your final comment there but there is hardly any reference to climate change. These two issues are obviously very important to the European Union and the West, and I wonder whether you felt that the Government of Russia feels that the need, in our view, for greater emphasis is something that you could accept and respond to.

Mr Fedotov: Precisely, and I absolutely agree with you. That is another illustration of why we should update the legal basis of our partnership with the EU. We have co-operation in countering terrorism with the European Union, we have important contacts on climate change and I am sure that this co-operation will continue to develop. That is why the new agreement, should include new areas of co-operation between Russia and the European Union that have emerged since this PCA was signed 11 years ago.

Q421 Lord Anderson of Swansea: Ambassador, the Fourth Space refers to research and education, and the cultural relations, Russian civilisation, Russian language studies within the Union is clearly very important indeed in terms of people to people, as was discussed at the recent EU Russia summit at Mafra. Can you indicate to the Committee how you see this key area of research, education, and culture developing?

Mr Fedotov: I think we can only enjoy how this co-operation develops between Russia and the EU. Yet again, sometimes it is hard to make a dividing line when we have this on the basis of our bilateral relations with individual Member States and when it is a result of a co-ordinated policy of the European Commission. Russian and European cultural space and cultural heritage are indivisible. At the moment I think you are able to visit the exhibition at the Royal Academy of Arts, which is a very good illustration of this indivisibility of Russian culture and European culture, the mutual influences. We believe that the opening of the European Institute in Moscow is another important step in this direction. An impressive number of other joint projects are under way. I am optimistic about this.

Q422 Lord Anderson of Swansea: You are absolutely right, Ambassador, to point to the exhibition as a very good example of that co-operation but it would be remiss of us not to mention the British Council in this context. I think it is fair to say that most people in this country are puzzled and saddened by the relationship of the Council, whose aim is to build bridges of understanding between this country and Russia, yet political motives seem to have supervened, frankly, to the cost of those Russian citizens who want to learn English, and those who want to come to this country to study. How do you read this and what is the objection to a cultural agreement which would find a place for the British Council to do its very valuable work within Russia?

Mr Fedotov: Russia does not have concerns about what the British Council is doing in Russia. We believe it is doing well in terms of cultural exchange and education but, unfortunately, the activities of the British Council in Russia lacked legal grounds. As a matter of fact, the 1994 agreement which provides for the development of cultural relations between Russia and the UK on bilateral issues were suspended, including the discussion of the agreement on cultural centres. So, the British Council so far does not have any legal ground for its activities in Russia. Although all the legal problems which are applicable to the British Council offices, for instance, in Saint Petersburg and the Yekaterinburg are also applicable to the British Council in Moscow, as a gesture of good will, the Russian Government is not insisting on the suspension of the British Council office in Moscow. We hope that the situation will improve and we will be able to resume the discussion of the bilateral agreement on cultural centres and that will allow the British Council to have a solid legal foundation for its future activities in Russia.

Q423 Lord Anderson of Swansea: Are those negotiations likely to begin soon?

Mr Fedotov: We are prepared to resume these negotiations as soon as the British side accept that the other tracks should also be resumed, including the visa agreement. I mentioned our progress with the European Union but unfortunately we are lagging far behind the European Union with our bilateral visa problems with the UK. Unfortunately, the visa problem now creates an impediment to contacts between the people of Russia and England and that is very unfortunate. There are other matters, like the suspension of co-operation in counter-terrorism. That was another step taken by the British Government against Russia. What we are basically suggesting is a kind of zero option, coming back to the situation before July last year, which will allow us to resume the negotiations on the agreement for cultural centres. As I said, we were very close to the finalisation of this agreement. That of course will help to establish the legal foundation for the British Council in Russia.
Q424 Lord Crickhowell: Ambassador, this is an issue which the European Community has expressed complete support for the British position on. It is a European issue as well as a British issue. What I find difficult to understand and I found difficult to understand as I listened to you was that you started by saying that there were no concerns about what the British Council was doing in Russia. You pointed to some legal disagreements which you thought could be resolved anyway but you made it very clear, as has your Foreign Ministry in Russia, that what has brought this about, are political differences between the British Government on certain political issues. What I think we all find very difficult to understand is on a cultural issue, an educational issue, an issue on which you say there are no concerns, which relate to your opening statement about Europe and Russia and Russia and Europe, is how political differences can be broken off, interrupted and interfered with. We simply do not comprehend how these kinds of political differences can involve something like the British Council.

Mr Fedotov: First of all, I do not think the suspension of the activities of two regional offices of the British Council, small regional offices, would be a real impediment --- co-operation between Russia and the UK in culture and education. As a matter of fact, this co-operation continues. Even when the British Council was more active in Russia than now, there have always been other direct channels for contacts in matters of culture, education. To take another side of the coin, we have such European institutions as the Goethe Institute, Cervantes, Alliance Française. They continue to operate in Russia because they have a very firm legal foundation and there have been no problems with them. The British Council was established in Russia in 1992 without any agreement. They just came and started to work and only two years later a framework agreement was signed which had a special provision for further consultations in order to get legal status for the offices of the British Council. It would also help us to have the same legal foundation to open a Russian cultural centre. We do not have cultural centres in Russia. Unfortunately, the discussion of this matter has been influenced by the political choice of the British Government to take another legal matter, that of the extradition of Mr Lugovoi, at the highest political level, to make out of it a matter of policy, and that is why other areas of bilateral relations were affected.

Q425 Baroness Symons of Vernham Dean: Ambassador, I think we do need to be clear. You have made some very categorical statements, and your last statement, I think, is at least helpful in so far as it does clarify the issue for us—maybe in a stark way but nonetheless such that one could not misunderstand what you are saying. Can I just be clear about this point though? Are you saying that we can resume the discussions about trying to put the British Council, all the British Council offices, on a legal footing in those negotiations at such time as we resume a discussion about the visa issues, or at such time as we have concluded on the visa issues? You have mentioned very specifically a discussion about terrorism issues and you have also raised quite specifically the extradition issues. That is quite a substantial menu on the side of those (a) agreements and (b) a quite specific issue about extradition. Is that the full menu, if I can put it that way, the full list of the issues that you want resolved before we can begin these discussions, or are you saying that if we all do get together to be able to look at these together, that will be the point at which discussions might be resumed?

Mr Fedotov: The Russian Government has offered the British side an option. A few months ago we suggested that if the British Government is prepared to go back to the situation before July 2007—of course, diplomats were expelled and it is hard to ask to let them back but at least the negotiations on the visa issue must resume, our bilateral contacts on counter-terrorism must resume, and also, in this case, we are prepared to resume consultations on the agreement on cultural centres. That does not mean that the progress in all of these tracks must be inter-related, so to say. The most important thing is to start them. We realise that for the visa issue we need more time because we are only at the beginning stage but on the cultural centres, we were quite close to the finalisation of this agreement. So it is a matter of good will from both sides. Unfortunately, this option which was offered by the Russian Government was rejected by the British side as an ultimatum and that brought us to square one again.

Q426 Lord Truscott: Good morning Mr Ambassador. I am very glad you are here today. Could I just move on to energy matters now, Ambassador. What are, in your view and in the view of the Russian Government, the prospects for the ratification of the Energy Charter Treaty and the Transit Protocol? What are the weaknesses of the existing texts and what do you think might be an alternative way forward? Finally, if I can ask you, Ambassador, Mr Chizhov was quoted today in the Financial Times as saying “We do not mix energy and economic problems with political problems.” Would you agree with that statement?

Mr Fedotov: I think he is right. Why do we have to mix everything in one box? I would say that the Energy Charter Treaty and related documents that
serve as a legal framework for the long-term co-operation in the field of energy were the product of a compromise and mutual concessions. When the ECT was signed Russia expressed some concerns that were set forth in the statement of the chairman of the European Energy Charter conference. While expecting that these concerns would be dealt with as soon as possible, Russia started the process of ratification of the ECT as early as 1996. However, the problems mentioned have not yet been resolved, nor is the ratification process complete. For this reason, the treaty is being implemented but on a temporary basis. For Russia this matter had a crucial importance, as the ECT covers the whole fuel and energy sector, not only oil and gas. Furthermore, ECT ratification will require significant changes in Russian legislative and administrative acts. That is a complex and time-consuming process. Among the unresolved problems is the issue of international transit of energy resources. The State Duma of the Russian Federation has decided that the ECT could be ratified only when the Russian proposals to the Transit Protocol and the Energy Charter are taken into account. There are also other unresolved disputes related to nuclear and energy materials trade and investment regimes, environmental aspects and energy efficiency matters that are also under discussion. So for the time being the Russian position remains unchanged. During the EU summit that took place in Helsinki in 2006 President Putin confirmed that Russia will not ratify the Energy Charter Treaty in its present form because we need to have clarification of these unresolved issues. Our latest contacts with the European Commission have shown that the Russian and EU positions on the key ECT issues still have significant differences. We propose to modernise the treaty by reviewing several of its provisions and supplementing it with additional protocols, focusing on different areas of co-operation like transit, investments, electrical power industry, etc. In particular, the following transit issues that have not yet been settled during further consultations are of special significance for us. Number one is the traditional supplier’s priority right to conclude a new transit contract, right of first refusal; and tariffs on long-term contracts, cost plus a reasonable income formula; and transit protocol’s scope of obligation. The fact is that 95% of Russian gas and 40% of oil are supplied to trade markets by means of transit through other countries. It is important. Moreover, 83% of oil exports from Kazakhstan and 20% of oil exports from Azerbaijan transit through the territory of Russia. Under such circumstances, it is quite obvious that Russia is interested in a lasting instrument that would effectively regulate transit. Such is the position of Russia as of today and we hope that we will continue meaningful consultations with the European Union on this matter.

Q427 Lord Truscott: Do you think that the EU-Russia energy partnership and the principles around it could be enshrined in the new Partnership and Co-operation Agreement?

Mr Fedotov: That is a possibility. It could be enshrined in it, or it could be the subject of a separate document. It does not matter but certainly we need to have a mutually acceptable solution to these unresolved issues.

Q428 Lord Crickhowell: Can I ask a related question, Ambassador? What is the Russian Government’s view of the European Commission’s proposals put forward in September 2007 about a strengthened European energy policy?

Mr Fedotov: As I understand, so far these ideas are not yet in final form, so the official position of the Russian Government on the European Commission proposals to strengthen the European energy policy is under consideration. I think it would be a little hasty to formulate a view on something that has not yet taken its final form. Generally speaking, of course, it is quite obvious that this issue has a paramount importance for Russia, as the leading energy supplier to the EU. I think it would be fair to say that we expect the EU would not make its final endorsement of its energy strategy without consulting Russia or taking into account in some other way Russian concerns. We cannot be away from this process while we continue to be one of the important energy supplies to Europe. By the way, we have an appropriate channel for such discussions, which is the Energy Dialogue, and we hope that this panel will continue to work and will work even more actively.

Q429 Lord Crickhowell: Ambassador, you spoke right at the beginning of this meeting about the interdependence of Russia and Europe. There is no greater example of this interdependence than this issue. Perhaps European policy has not been well thought out and co-ordinated in the past. You have spoken about the vital importance for Russia. What you have said equally makes it clear that it is of absolutely fundamental importance for Europe, our dependence on gas and so on, particularly. Therefore it seems likely that the European position will have to be developed and strengthened and that the European vital interests will also have to be protected and worked out on a mutually supports basis in the coming years. Would you not agree that we are at the start of a really fundamental re-examination of these energy issues? If there are rights and so on that Russia can understandably demand, equally, Europe must be in a position to have balancing and equally effective defence of its own position.
Mr Fedotov: I think interdependence is a key word. You may say that in some ways Europe may be considered as dependent on oil and gas supplies from Russia, but Russia also depends on markets in Europe. There is a mutual interest to have a common policy and to do it in a fair way, without politicising this matter, but doing it for the benefit of the interests of the European Union and Russia and, what is even more important, for the interests of end users of energy products.

Q430 Lord Swinfen: Your Excellency, I want to talk about the World Trade Organisation. What is the Russian view of the EU’s role in the run-up to Russia’s membership of the WTO? How satisfied is your Government with the arrangements for market access for your goods into Europe? What are the main problems connected with imports into Russia from Europe?

Mr Fedotov: I think we do not have major problems with the EU position on Russia’s accession to the WTO. In May 2004 the bilateral negotiations on trade and services with the EU, which account for more than half of our trade, were completed, and so that was good news. Bilateral talks with all interested WTO members are almost complete. Multilateral negotiations aimed at co-ordinating the report of the working group on Russia’s accession to the WTO, as well as on agriculture, which are by no means less complex, are quite intensive and currently under way. So we hope that the EU will continue to provide us with constructive support and assistance during these talks. Of course, the accession to the WTO is a matter of priority for the Russian Government but the quality of accession to the WTO is more important than the timing of the accession. We realise that Russia’s accession to the WTO will affect some Russian industries which have not so far been able to reform enough. It will certainly have an impact on the economic and social situation in Russia. That is why it is taking more time than it took with other countries. We now realise that it is wiser to take our time in the process of negotiation and to have a good quality of accession to the WTO rather than a hasty approach, as has happened in the past with the accession of some countries, who were accepted as members of the WTO but then later on started to renegotiate some of the conditions of their accession. We want to avoid that, and we want to be crystal clear at the very beginning. Of course, we cannot be outside the WTO, and the European factor is important. I quoted earlier figures for our trade with the European Union. The European Union continues to be one of our most important partners in terms of foreign trade, and, this trade will grow after Russia’s accession to the WTO. I hope it will be the same for Russian exports to Europe.

Q431 Lord Selkirk of Douglas: Ambassador, may I ask you what is the Russian Government’s view of the European Union’s Common Foreign and Security Policy? In what areas does the Russian Government see the most scope for co-operation with the European Union on foreign policy and security matters? Which do you see as the most difficult areas?

Mr Fedotov: Both the EU and Russia are in favour of collective efforts to cope with international crises and are eager to promote a multilateral dialogue, to reinforce multilateral institutions such as the UN, to counter the proliferation of WMD and their means of delivery, and to develop effective international institutions to meet the global challenges. As I said earlier, we have a permanent dialogue with the EU. Of course, we have dialogue with Member States but we are discussing with the Commission outstanding international issues like the Middle East, Iran, the European agenda. One of the illustrations of how we can work together on the European Common Foreign Security Policy and the Russian foreign policy is that we are discussing a possible Russian assistance in terms of providing transport helicopters to the EU peace-keeping mission in Chad. There are regular contacts and we may have different views on some matters. No doubt we have different positions on Kosovo, and that is an outstanding issue, but the most important thing is to keep all channels of communication open. We may differ but we must always have the means to convey our positions to each other.

Q432 Lord Selkirk of Douglas: Can I just mention to the Ambassador that the action of the Russian Consul General in Edinburgh was very much appreciated in the Scottish Parliament when he honoured the veterans of the Arctic convoys who worked in the Second World War to bring supplies to Russia. That was very warmly welcomed by the Presiding Officer, the families and the representatives of the different political parties. I thought I should mention that.

Mr Fedotov: Thank you. I take note of it.

Q433 Lord Anderson of Swansea: Ambassador, I was very pleased that you mentioned discussions about the possible use of Russian helicopters in Chad. Is that totally new? When we met Lord Malloch-Brown, the Minister responsible, he mentioned the dearth of helicopters to assist in these areas of great crisis in Africa. Do you see this developing, where Russia has a substantial number of helicopters, of reaching protocols with the Union in having regular co-operation in such areas in the developing world?
Mr Fedotov: As I understand, we are now discussing this matter, the modalities of using Russian helicopters for this particular peace-keeping mission to Chad. Russia has a lot of experience in providing transport helicopters to the peace-keeping operations in Africa. We have done it in many cases: Sierra Leone, Sudan, Democratic Republic of Congo and some other places, and so there is good experience and we are prepared to share this asset with those who are willing to organise further peace-keeping operations, whether it be the UN or the European Union.

Q434 Lord Anderson of Swansea: Do these include heavy lift of equipment which is relevant for peace-keeping and also the transport? 
Mr Fedotov: Yes, it does. I myself once visited and inspected the UN peace-keeping operation in Sierra Leone, and at that time Russia provided the biggest helicopters, Mi-24, which can transport shipments to remote areas and jungles, then smaller helicopters that can be used to transport them to outposts on a lesser scale and also to transport passengers and to carry other cargo. That has been done and the Russian companies which are contracted by UN to do that have a lot of experience. They have experienced pilots and they have equipment.

Q435 Lord Chidgey: Ambassador, you mentioned a few minutes ago in passing that there are disagreements between Russia and the EU on the Common Foreign and Security Policy. You mentioned Kosovo in passing. I wonder if you could elaborate a little because it seems to me that there is a rather confused situation in Serbia, with the Prime Minister, Mr Kostunica, being somewhat opposed to closer co-operation with the EU, whereas the newly elected President Mr Tadic seems to be in favour, and of course co-operation with Europe is, as we know, generally speaking a good thing. We seem to have a bit of stalemate and I wonder whether, from the Russian point of view, this is in fact detrimental to the situation in the Balkans, which was always traditionally an area of special concern with the situation in the Balkans, with the EU, the differences between the two figures within Serbia have a much wider influence on relations between Serbia, Russia and the EU. It seems to me that this is, in a way, important figures in their own area having a far greater impact because of their differences on much wider and far-reaching issues between Russia, in this instance, and the EU. Should we not be trying to find a solution to this?
Mr Fedotov: Just two or three points in this respect. First of all, what is important for Russia is a national consensus in Serbia on the matter of Kosovo. We are prepared to support any solution on the status of Kosovo which is acceptable to Belgrade. If it does not happen and Kosovo proclaims its independence unilaterally, it will mean that for the first time since the Second World War the borders of a European state will be changed without its consent. Borders have been changed: there has been the Dayton Agreement, the divorce of Czechoslovakia, the collapse of the Soviet Union, but in each case an agreement was signed with the consent of the parties. For the first time it is clear that Kosovo is going to proclaim its independence unilaterally, without the consent of Serbia. It is a pity because the last round of talks last year showed some glimpses of hope, some signals, including from Belgrade, that they were prepared to discuss a compromise solution, some very loose status of Kosovo, a Hong Kong-type association or whatever, but all this was rejected because the Kosovan Albanians were assured, notwithstanding the outcome of the discussion, that the Americans and others would support their move towards unilateral independence. So what will happen now? If the independence of Kosovo is proclaimed unilaterally, Russia will not accept it, and we are going to keep this position. I do not think we need to make an outstanding problem of it in our relations, including in our contacts with the European Union. There have in the past been similar situations. You remember the GDR and the Hallstein doctrine of the Federal Republic of Germany. Some countries had diplomatic relations with the GDR, some with the Federal Republic of Germany but that was not a huge problem that prevented these countries having good relations between themselves. Take the example of Northern Cyprus. The only country that recognises Northern Cyprus is Turkey but Greece and Turkey have—sometimes bumpy—relations but they are partners in NATO, they may be partners in the European Union and they have normal good relations. So that happens sometimes, but we cannot accept unilateral independence of Kosovo, not only because of our special concern with the situation in the Balkans, which was always traditionally an area of special interest for Russia, but also because it could create a very dangerous precedent for other people who might wish to unilaterally proclaim their independence following the Kosovo precedent. Of course, one might even adopt a UN resolution saying that this situation is unique, and does not set any precedent but we know that the more we adopt such resolutions, the more precedents are set, so it is better to avoid it. That is why we are very cautious about the unilateral independence of Kosovo and we believe that it might lead to unpredictable consequences for European security.

Q436 Lord Anderson of Swansea: Ambassador, the reality is that within a short period of time Kosovo will declare independence, and the international organisations, certainly the European Union, have
already geared to provide substantial civil assistance. Will Russia block any form of assistance from the United Nations to an independent Kosovo?

Mr Fedotov: There is UN Security Council Resolution 1244, and how it will be dealt with is the great issue, and how the Security Council, which is ultimately the highest authority in terms of international peace and security, will tackle this matter. There is this matter of assistance to Kosovo but there are other matters. What is going to happen to the UN mission there anyway? There is a need to close this mission and how and under what circumstances decisions are to be taken. So I am afraid that a unilateral proclamation of Kosovo’s independence would create a situation of a legal vacuum, so any further decisions of international institutions, including the EU, on Kosovo would lack sufficient legal foundation.

Chairman: Thank you very much indeed. Baroness Symons would like to go back to something that you said at the very beginning of your remarks and ask one final question.

Q437 Baroness Symons of Vernham Dean: Ambassador, at the beginning you gave us a very impressive list of the reasons why Russia is part of Europe, and I think you said Europe without Russia is not Europe. You talked about geography, history, culture, literature, music, art, human rights, values, and family ties. The logic of all of that seems to point towards ever closer relationships, and yet you very specifically drew the line at institutional relationships in the future. I just ask you for a moment to step back from immediate politics, from all our differences that we have about everything. Do you really see it as being impossible that in 20 or 30 years’ time, when we are all old and grey and retired from the political arena, that the logic of the position you articulated about the closeness of Russia—indeed, not the closeness but the integral part that Russia is in terms of its European identity—do you really think that Russia will never have the institutional relationship with the EU and step towards membership of the EU?

Mr Fedotov: If you remember, when I mentioned this principle of anything but institutions, I said, and I quote myself, “The overall framework of our policies towards the EU at this stage could be defined,” but the EU is an evolving institution and the EU of 12 was different to the EU of 27. Who knows what will happen with the EU of 50? No-one can predict how it will develop, what the form and shape of this institution will be and how it will allow Russia to take part in its evolution. Of course, one cannot exclude anything but so far it is hard to see in the future, in 30 years or 40 years, how our children and our grandchildren will see it. We hope they will see the positive development of relations between Russia and the European Union and the development of these Common Spaces in terms of visits, in terms of culture, in terms of education, trade, investment, business and everything. Then the new generation of political leaders will decide what to do.

Q438 Chairman: Ambassador, could I on behalf of the Committee say how very much we have appreciated your coming and answering our questions so fully this morning. Our colleague Lord Hannay, who unfortunately cannot be here because he is out of the country today, told us that you would be able to help us a great deal. He remembers working with you in the United Nations some time ago. What you have been able to tell us will be very helpful for us in clarifying our understanding of the positions of the Russian Government and in completing our report. We really are extremely grateful to you and your colleague for coming and having spent some time with us this morning. Thank you again.

Mr Fedotov: Thank you. Thank you for your attention, thank you for your questions. Unfortunately, Mr Pritsepov did not have the opportunity to say anything. Certainly he contributed to this presentation, you may be sure. For the sake of clarity, if you need it, we may leave you these notes for your report as well. We are looking forward and we hope that your recommendations will be of help for the further development of relationships between Russia and the EU. Thank you very much.

Chairman: Thank you again.
Written Evidence

Memorandum by Dr Derek Averre, University of Birmingham

1. This is an individual submission, written from the point of view of an academic who follows current developments in Russia’s foreign and security policy and has regular contact with Russian academics and policy analysts, and who contributed oral evidence to the recent House of Commons Foreign Affairs Committee inquiry “Global Security: Russia”. It attempts to provide an analysis of the position of Moscow’s foreign policy elite and respond to some of the questions posed by this inquiry.

2. The evolution of EU-Russia relations must be viewed in the broader context of Russia’s foreign and security policy and its governing elite’s response to the challenges thrown up by the contemporary international system. Recent pronouncements by leading Russian officials have represented a clear attempt to challenge the existing international order, based on a claim for equal status and attempts to establish the legitimacy of Russian approaches to foreign policy-making, with the aim of gaining a more influential role in international affairs. Foreign minister Lavrov has called for collective leadership, with the major powers working in concert within international institutions and frameworks, in the face of global challenges and threats; in particular he has proposed a trilateral Russia-US-EU format as a framework for collective decision-making. Underlying this approach is the perception that the Western alliance, which dominated the first post-Cold War decade, has fractured, with splits between the US and Europe on a range of political and economic issues and problems caused by the conflicts in Afghanistan and Iraq and the failure of policy in the Middle East. Rightly or wrongly, the Russian governing elite perceives a shift in global power relations, a general decline in international governance and the reduced influence of Western leadership; this, together with the greater resources at Russia’s disposal, leads Moscow to pursue a “multivector” policy while sustaining pragmatic and selective engagement with the US and Europe.

3. This approach has been transferred to the political-military arena. Former defence minister Sergei Ivanov has pointed to a renewed emphasis on military force in world politics, which has produced not only cooperative responses to common threats but also challenges to Russia’s national security arising from Russia’s exclusion from security decision-making and attempted interference in its internal affairs. In Russian eyes NATO continues to enlarge eastwards without becoming a genuine collective security organisation; the US has announced plans for missile defences in central Europe outside of the NATO framework, which will inevitably impact on relations with the Alliance and the EU. In response, Russia is rethinking its arms control commitments and planning to restore an effective military capability through increased spending on its armed forces (though it should be noted that defence spending has hardly risen as a percentage of GDP in recent years and it is uncertain as yet whether a significant redirection of resources to the military will take place).

4. Moscow’s foreign policy strategy in the post-Soviet space is to seek recognition for and position itself at the centre of regional organisations, in particular the CIS, Collective Security Treaty Organisation and Shanghai Cooperation Organisation, as a means of addressing weaknesses in regional security governance and developing legitimate fora capable of interacting with external states and organisations. Underlying this is Moscow’s support for regimes where challenges to them might spill over into wider regional instability; the volatile situation in the region represents a fundamental challenge to both Russia’s security and its historical self-understanding as the major political and cultural power in the wider region. The emergence of competing blocs, and the aspirations of Ukraine, Moldova and Georgia in particular to establish a closer relationship with Europe—Moscow rejects “unconstitutional” colour revolutions and resents European support for them—is being managed by Moscow using a range of political and economic instruments, including more active support for the separatist regimes in the latter two countries. While Moldova and Georgia have sought greater involvement of external players, including the EU, in resolving the separatist conflicts, Moscow will continue to insist on a central role as an external guarantor of security and aim to maintain existing conflict resolution mechanisms.

5. A final aspect of Moscow’s foreign policy is its response to increasing pressure to adopt liberal values, with the perception now widespread in Europe that under Putin the governing elite is resisting democratic change and the development of civil society in favour of increasing the power of conservative state institutions in what has been termed “authoritarian modernisation”. Moscow is not only mounting a vigorous defence of Russia’s strong state model of governance, seen as key to its re-emergence as a great power, but is challenging the legitimacy of the values underpinning Western approaches to foreign policy-making. It believes that the dialogue on democracy and human rights is a cover for attempts to dictate policy, while states criticising
Russia themselves act “undemocratically” in terms of the fundamental principles of international law, ie sovereignty and non-intervention (divergent—or, to quote Lavrov, “diametrically opposed”—views on the Kosovo question over the last decade is a clear example). Western support for the democracy movements in some of the USSR successor states has been linked with “bloc politics” and Cold War-era attempts to constrain Russia. In recent speeches, both Putin and Lavrov have bracketed the EU and NATO together as organisations seeking to dictate policy to Russia. This narrative—witness Putin’s Munich speech in February 2007—has overshadowed alternative narratives portraying a Russia ready to consider engagement with Europe.

6. To summarise, Russia’s political elite claims a widely shared domestic consensus on values and identity based on a profoundly conservative definition of sovereignty, economic and military strength and peculiarly Russian political models, exploiting fears of instability and of external threats to reassert national security concerns as a prop to the state-building project. The debate in Russia has shifted in Putin’s second term, with even pro-European liberals sceptical that a liberal democratic international order, underpinned by a values-based conception of human rights and freedoms, is a realistic prospect. This may not be fully recognised or accepted in Brussels and many European capitals but accurately reflects widespread Russian perceptions.

7. This rather long preamble is necessary as context to the apparently unpromising development of EU—Russia relations. Unease in Moscow over what it sees as a crisis of governance in the EU (uncertainty of the future constitutional order in a Union of 27+ states) and lack of a coherent external policy for engagement with Russia, and concern in Brussels over Moscow’s insistence on a partnership between equals and the “values gap”—doubts over Russia’s commitment to political, social and economic modernisation which would bring it closer to Europe—have sown mutual mistrust. Added to this are lack of a common strategic “values gap”—doubts over Russia’s commitment to political, social and economic modernisation which would bring it closer to Europe—have sown mutual mistrust. Added to this are lack of a common strategic vision, particularly as regards their shared neighbourhood; a relatively narrow agenda for security cooperation; disputes over trade and energy issues; and an increasingly difficult relationship over human rights, including with the European Court (ECHR).

8. There are, nevertheless, numerous positives in the relationship, though these are often not visible. High-level institutional arrangements are firmly established and an increasingly dense network of contacts between officials and experts across wide areas of cooperation, giving Moscow a privileged and perhaps unique position among Brussels’ external partners, is developing. While stating that Russia will pursue an independent foreign policy course its leaders frequently emphasise the importance of the country’s “fundamental European choice”. Lavrov has repeated the formula “everything but institutions” and has criticised sceptical Russian political analysts for “excessive alarmism and pessimism”. Moscow is acutely aware of negative elite and public perceptions of Russia in Europe and is making efforts to address this problem; the Russian delegation to Brussels is trying to foster closer parliamentary cooperation and seeking greater contributions from the business community and civil society. The ECHR is now part of Russia’s legal system and Moscow appears to want to maintain respect for its provisions. The fact remains, however, that Moscow’s demand for a greater voice in European affairs and acute dissatisfaction with lectures on how it should govern itself spill over into high-level disputes.

9. Keynote speeches by leading EU officials, notably by the then External Relations Commissioner Chris Patten as long ago as February 2004 and by Trade Commissioner Peter Mandelson in May this year—the latter perhaps reflecting a new realism in Brussels following Putin’s Munich speech—suggest that Brussels is aware both of the problems faced and of the institutional shortcomings of the EU and its lack of a foreign policy vision; indeed, Brussels is unlikely to be able to deal more effectively with Moscow unless these shortcomings are addressed. Mandelson emphasised the divergent perceptions arising from difficult negotiations between the two sides and the history of Russian weakness in the 1990s, as well as the lack of coherence between the policies of EU member states toward Russia (exacerbated by the advent of new accession countries). Brussels should insist on respect for key values and on clear and transparent trading rules, he argued, and promote both as being in Moscow’s self-interest as a modernising state, but equally seek to understand the complex policy challenges faced by Moscow and how it perceives Brussels’ policies.

10. Revitalised attempts to engage Russia might thus build on the following guidelines: belief in Russia’s “European choice” and Europe’s ability still to influence Russia’s foreign policy choices, tempered with recognition that it is a long and inevitably winding road due to internal political challenges (as pro-European liberals have pointed out, Russia needs time—it is less than 16 years since it emerged from its “Soviet overcoat” and in the last decade it has experienced two attempted putches, two wars and two financial defaults); respect for Russia’s choice of domestic governance models and avoidance of an inflated normative agenda, while raising concerns (for example, within the well-established human rights dialogue) over specific aspects and firmly defending the principles of the EU’s own governance and commitment to the rule of law; demonstrate consistently the benefits of modernisation, with the aim of achieving greater competitiveness for Russia, through integration into European trading structures and adherence to transparent international norms and
rules; continue to foster wide-ranging exchanges below the diplomatic dialogue with Russian authorities, businesses and public bodies, both at the federal and regional level, scientists, educationalists and representatives of civil society; and promote a more balanced public information campaign about Russia in Europe. A column headline in a quality UK newspaper in the week this submission was written—"Keeping a lid on Putin’s resurgent Russia"—sums up the negative tone prevalent in the media and begs the question: how would translating this advice into policy meet Europe’s own interests, let alone improve relations with Russia, no longer a closed totalitarian state but a complex and multifaceted polity and society?

11. This leads on to the issue of how to put these guidelines into practice, and in particular what needs to be done to secure a meaningful agreement following the expiry of the initial 10-year term of the Partnership and Cooperation Agreement (PCA) in November 2007. A detailed examination of the latter is beyond the scope of this submission (and indeed has been extensively discussed by policy analysts in Europe and Russia) but a few key points are offered. Crucial areas of focus will be the energy relationship, securing agreement on business and trading rules, policy in the common neighbourhood and security cooperation.

12. Both sides accept that the PCA is outdated and have called for a more far-reaching framework for the relationship. Moscow has responded to Brussels’ desire for “ambitious objectives on political and external security cooperation” by proposing a juridically binding Treaty on Strategic Partnership, encompassing all areas of interaction and determining the aims and principles of EU-Russia cooperation, supplemented by sectoral agreements. In terms of legal form, concluding an ambitious and comprehensive mixed (multi-pillar) agreement presents a challenge to the EU, since it would have to be based in EU treaties and ratified by all EU member states as well as the European Parliament. Apart from possible delays due to the lengthy and complicated ratification process, achieving consensus may well be problematic; disparate political sentiments towards Russia in Europe, particularly among recent accession countries mistrustful of Moscow, is likely to prevent giving Russia a privileged position among the EU’s external partners. More realistic (and which the two sides appear to be inching towards) is a headline political agreement, setting out broad principles and aims and restating commitment to shared values, together with sectoral agreements based on the four common spaces (possible with additional protocols on such as Kaliningrad), providing legal continuity with the PCA. It is the scope of the sectoral agreements which is crucial; the aim should be to introduce radically reworked and augmented provisions as a basis on which to build in future. A group of Russian specialists who are in favour of Russia’s “Europeanisation” (and who are arguing for an advanced partnership agreement with the ultimate aim of association) believes that Putin’s administration supports an extensive agreement—in line with its intent to strengthen Russia’s international position as a legitimate partner—rather than a minimalist legal basis for relations with selective integration (supported by other Russian specialists with a negative opinion of the prospects for legislative harmonisation). It should be clearly understood, however, that the agreements will be the subject of long and painstaking negotiation, often subject to political interference, and a coherent strategy on the part of the EU is needed.

13. The Common Economic Space is a key area in which much has already been accomplished. Brussels wants the inclusion of trade provisions, with the regulatory alignment of Russia to EU rules and standards, as the basis for a “deep” free trade agreement following Russia’s anticipated WTO accession. Moscow has, however, hitherto been reluctant to converge on certain EU rules and standards and vested interests in Russia may continue to block some of these provisions, despite the apparent willingness of leading officials to open negotiations on a free trade area, following Russia’s accession to the WTO. The Commission is also keen to include provisions based on Russia’s acceptance of the principles of the European Energy Charter Treaty, but again this has been a matter of dispute and it is unclear what Moscow—given the strategic importance of Russia’s energy sector—will agree to. Russia may give foreign investors access to its upstream reserves in return for allowing Russian companies access to their resources, technology, capital, distribution network and power generation; however, there are substantial European concerns about letting Russian state companies act as transnational majors. Though companies like Gazprom are hardly free-market role models, integrating them into the Western economy may nevertheless prove to be the most efficient way of bringing them, and the Russian system, closer to Western standards and rules and there are prospects for engaging Russia’s support in areas such as nuclear energy and energy conservation. Specialists have argued that Europe’s concerns should concentrate less on whether political rather than commercial considerations will henceforth drive Russian energy policy and more on the potential impact on European economies of a drift to a more étatiste approach to Russia’s large-scale resource industry, making it vulnerable to corruption and poor economic governance and leading to less efficiency and slower output and export growth. The recent Commission paper proposing a framework for external energy policy provides few clues about Russia and it is still unclear to what extent the principles of the Treaty can be incorporated into a post-PCA agreement.

14. The Common Space of External Security also faces difficulties. There has been progress on nonproliferation, counter-terrorism and civil protection, and Moscow has a better idea what ESDP entails; there is positive dialogue on Iran and the Middle East (though approaches often differ and cooperation
remains more at the level of consultation than joint or parallel decision-making). In contrast, approaches to the shared neighbourhood differ sharply and progress has hitherto been marginal. The EU’s argument should be that Moscow’s obsession with countering democracy movements following the “colour revolutions” not only places it on the other side of the fence to Europe but may also mean that it is missing the chance to influence internal developments in these countries and help create stable polities which still retain ties to Russia—Moscow needs to free itself from this logic and engage the efforts of the EU to create a genuine external common security space. It is clear to the more responsible sections of Russia’s political elite that profound changes are under way in its neighbourhood and that it can no longer be regarded solely as Russia’s “sphere of influence” and that a more selective and pragmatic longer-term policy is required. In return a more cohesive EU strategy, based on clearly articulated common positions among member states, one that seeks to coordinate external policy towards Moscow with the European Neighbourhood Policy — and making the latter work—is vital. Reconciling the priorities of new member states and ENP partners, and alleviating Moscow’s concerns over being isolated by current trends in the region, will require substantial long-term political vision and greater coherence in EU policy.

15 October 2007

Memorandum by Amsterdam & Peroff, Barristers/Solicitors, on behalf of Mr Mikhail Borisovich Khodorkovsky

1. As International Legal Counsel to Mikhail Borisovich Khodorkovsky I respectfully submit the following in response to three of the questions posed in the Call for Evidence.

How successful have the EU’s wide range of cooperation and assistance programmes been in attaining their stated objectives, especially in the fields of foreign and security policy; and rule of law, democracy and human rights? What potential is there for the EU’s new cooperation and financial assistance instruments to be effective in Russia?

2. Despite a significant investment on the part of the EU in cooperation and assistance programmes, since the last Partnership and Cooperation Agreement there has been a decided change for the worse in Russia, particularly at the top levels of political power. Militarily, Russia is more menacing now than at any time since the Cold War and Europe is particularly vulnerable to Russian state-controlled enterprises with regards to its energy industry. Democratic reform appears to have ceased and in fact reversed with NGOs under threat and the restrictions on the press at their highest since the Soviet era, in many cases leading to self-censorship. It is, however, on the rule of law on which I would like to focus.

3. The power to prosecute has become the instrument of choice in the Kremlin’s means of achieving its desired political and commercial outcomes. The Kremlin wields great influence through the constant threat of heavy-handed intimidation and unfair incarceration and expropriation. Multiple grievous violations of the Constitution of the Russian Federation have accumulated in recent years, making a mockery of its primacy in the Russian legal system. Numerous other Russian laws have also been disobeyed by the authorities, as have obligations under international treaties and conventions.

4. Russian courts are subject to political interference. Judges exposed to such extrajudicial pressures are often forced to find means to decide a case in favour of the party applying the pressure. As a result, Russian courts are widely believed, inside and outside of Russia, to be far from impartial, particularly in cases where major political or financial interests are involved.

5. The Kremlin exploits legal mechanisms not only domestically, but is increasingly seeking to do so internationally as well. Moscow is eager to settle scores with certain high-profile exiled business leaders who have vexed the Kremlin for not bending to its wishes, and who continue to frustrate the Kremlin through their attempts to influence events in Russia from abroad. Among the prime targets are former Yukos employees.

6. Their record shows that Russia’s prosecutors do not deserve our automatic trust. International cooperation with Russia’s prosecutors depends upon Russia having an independent, properly functioning prosecutorial system. To comply with requests from Russia’s prosecutorial system demands that it meet minimum levels of modernity, justice and legal rigour. All are sorely lacking. In light of the heavily politicised prosecutorial system, such requests must be carefully scrutinised on a case-by-case basis.

7. In a landmark decision issued in August 2007, the Swiss Federal Tribunal ordered Swiss authorities not to cooperate with their Russian counterparts investigating ex-Yukos officials. The Tribunal ruled that the Russian proceedings were politically-motivated and in violation of law, and that Swiss cooperation would be tantamount to complicity in the illegals. This was a major rebuke to the Kremlin, which had sought to portray the Yukos prosecutions as legitimate.
8. A series of events in 2006 and 2007 have further blackened the Kremlin's reputation in matters of the rule of law. Through the betrayals of foreign energy majors with interests in Russia, notably BP and Shell, and the bullying of trade partners, whether Ukraine, Belarus, Georgia, Poland or the European Union, the Kremlin has deeply undermined its reliability as a business partner. Additional worrisome trends are evidenced by the xenophobic and unconstitutional roundup and deportation of Georgian citizens, and the forced closure of Georgian-owned businesses using various regulatory pretexts. Meanwhile, the murders of Andrei Kozlov, Anna Politkovskaya and Alexander Litvinenko are all additional bellwethers of Russia's atmosphere of growing lawlessness.

9. In its September 2006 report on global governance, the World Bank ranked Russia 151st among 208 countries in terms of political stability, democratic voice and accountability, effectiveness of government, quality of regulatory bodies, rule of law and control over corruption. Russia was therefore overall in the league of Swaziland and Zambia, and just ahead of East Timor. Russia's political stability—defined as the perceived likelihood that the government will be destabilised or overthrown by unconstitutional or violent means—was comparable to that of the Philippines and Kyrgyzstan. On the credibility of the state's commitment to policy formation and implementation, Russia was in a group with Pakistan and Tanzania. For regulatory quality, Russia was ranked alongside Madagascar and Senegal. Rule of law in Russia was as effective as in Ecuador, Indonesia and Bangladesh.

10. Worldwide esteem for the Russian leadership is at an all-time low. There is a heavy onus on the Kremlin to earn back its legitimacy and to promote the true rule of law in Russia and respect for international obligations. Otherwise today's Russian leaders may well be responsible for a tailspin into anarchy.

11. Russia under President Putin today is less stable than generally perceived. The consolidation of power in the executive has drastically weakened all other branches of state power. In the absence of a real separation of powers, should discord or crisis befall the executive, the broader political system may be unable to withstand the attendant shocks without collapsing altogether.

12. In an open letter to Kommersant on October 8, 2007, Viktor Cherkesov, a senior public official, stated that intensifying rivalries within the Kremlin inner circle may soon explode into open conflict that could threaten Russia's stability. Former Kremlin adviser Andrei Illarionov compared the infighting to battles between feudal lords, warning that instability and "palace coups" could result. One observer commenting on Kremlin insiders, cited in the International Herald Tribune, stated: "They stood together as long as they were robbing others of their assets . . . But after dividing the spoils, they realized that they can only expand their wealth by robbing one another" (Arrests hint at struggle for power after Putin, 10 October 2007).

13. The ruling clique's desire to maintain power is based in strong measure on insecurities resulting from its multi-year attack on the rule of law. Members of this clique will avoid a real democratic transition at all costs in order to protect their actions from review and redress.

14. According to the Indem Foundation, businesses paid officials in Russia a total $33.5 billion in bribes in 2001—growing almost tenfold to a staggering $316 billion in 2005. In 2006 Russia's own procuracy, slightly more optimistic, estimated graft at $240 billion per year—almost equal to the state's entire revenues. This endemic corruption is not only a hugely burdensome tax within the Russian economy—it has also destroyed accountability across a public administration taking its cues from a Kremlin that flaunts the rule of law at will.

15. Without advocacy for the rule of law, there will not be progress in Russia. Due to the suppression of truly effective political pluralism in Russia, such advocacy will not arise internally. Therefore, without external pressure, an autocratic clan-based system will not generate of its own volition any positive developments with respect to human rights or the rule of law. Therein lies the challenge and the responsibility of the EU today. The window of opportunity to influence developments within Russia is rapidly closing, and the EU should not fail to rise to make every effort to do so.

How can the EU contribute to managing relations between individual EU Member States and Russia? Have the Member States shown solidarity when under pressure from Russia? Is there a need for a greater unity and coherence of approach among the Member States towards Russia?

16. We have learned that in addition to being a commodity essential for our continued economic development and well-being, energy can be wielded against us as a political or foreign policy tool. The EU can ensure that Member States work together to address the issue of energy security. National self-interest is the basis upon which Russia has been able to play EU Member States off against one another, ultimately undermining the EU as a whole. Yet this has not been the case with countries such as Poland, Estonia and Lithuania, which
have been subjected to pressures from Russia and asked for solidarity from across the EU. At the last EU-Russia summit in Samara, the EU, through Chancellor Angela Merkel and President José Manuel Barroso, stated:

17. “We had an occasion to say to our Russian partners that a difficulty for a Member State is a difficulty for all of us at the European Union. We are a Union based on principles of solidarity. We are now 27 Member-States. So, a Polish problem is a European problem. A Lithuanian, an Estonian problem is a European problem as well.”

18. In this context, the EU’s growing dependence on external energy supplies, largely from undemocratic and unstable countries, and particularly dependence on Russia, is worrying.

19. A recent own-initiative report adopted in the European Parliament and drafted by Jacek Saryusz-Wolski, Chairman of the Foreign Affairs committee, stated: “The EU’s 27 Member States need to replace their current preference for energy unilateralism with a new common policy of energy solidarity.”

20. If the EU acts with one voice in relation to its energy concerns, it will be able to secure energy supplies under the best conditions for the future. However the EU will have to muster the requisite political will to act in concert.

21. The EU is Russia’s largest trading partner and has the potential to exert a great deal of influence, through the framework of a Partnership and Cooperation Agreement, over the country for the benefit of its people. No one stands to benefit more from an effective market economy and a culture of respect for human rights and the rule of law than the Russian people themselves. In order to reverse the disturbing trends the EU must use every opportunity to encourage Russia to change course on human rights and the rule of law.

What is the nature of the Russia-EU dialogue with regards to energy questions? To what extent is Russia an indispensable partner, rival or obstacle for the EU in its efforts to attain the objectives of its recently adopted external energy policy?

22. The dynamics of the energy industry have strengthened Russia’s hand in relation to the EU over recent years. Europe is becoming increasingly dependent on Russian energy supplies and the European response has been discordant and divided.

23. Since mid-2006 Russia has surpassed Saudi Arabia as the largest exporter of oil in the world. As stated by Daniel Twining, major economies that are “increasingly dependent on Russian gas and oil exports . . . are rendering themselves vulnerable to the ambitions of an autocratic, imperial state that has not refrained from using energy as a geopolitical weapon and has been ruthless in its treatment of both internal political opponents and neighbouring states” (Putin’s Power Politics, The Weekly Standard, 16 January 2006). Indeed, “fuel diplomacy” has become the primary lever of Russian influence on the geopolitical stage.

24. This influence can be readily seen in Gazprom’s appointment of former German chancellor Gerhard Schroeder as chair of the supervisory board of the $4.7 billion Nord Stream pipeline. Unsurprisingly, it was Mr Schroeder who, for seven years, consistently ignored the gradual rollback of political rights in Russia, and derailed attempts to bring unified Western pressure to bear on Moscow to modify its conduct. Rather, Mr Schroeder focused only on deepening Germany’s commercial and political ties with Russia. Mr Schroeder’s complete absence of criticism of the regressions of the Russian regime only buttressed the intransigence of the Kremlin in its deflection of foreign concerns and criticisms.

25. Although less successfully so than with Germany under Mr Schroeder, other Western governments are also compelled to embrace Russia for its newfound influence in world energy markets. A “business-as-usual” policy of some governments has helped to legitimise the kleptocrats who perpetrated the Yukos expropriation, which The Economist has characterised as “larceny” (Russian oil—Yuk, 28 March 2007).

26. It is the non-market-oriented state corporatism of today’s Kremlin that necessitated the incarceration of Mr Khodorkovsky and the expropriation of Yukos. By jailing Mr Khodorkovsky and expropriating Yukos, the Kremlin cleared the energy sector of any competitors. No one will now build competing pipelines; no one will advocate the break-up of Gazprom; no one will promote the corporate governance and transparency that are anathemas to the state-owned enterprises. The costs of these Kremlin actions are becoming increasingly evident, from mismanagement of state resources and declines in the growth of energy production, to the risks of reliance on an energy supplier whose political stability depends upon one corrupt clan maintaining its grip on power.

27. Meanwhile, the Kremlin’s recklessness was displayed with the cut-off of gas to Ukraine in January 2006 and the cut-off of oil to Belarus in January 2007. Both incidents signalled the Kremlin’s readiness to engage in energy brinkmanship for not only commercial but also political reasons.
28. As a further example of the Kremlin’s unreliability, consider the July 2006 announcement that, despite longstanding engagements to the contrary, Gazprom had decided to shut out all foreign energy majors that had previously been short-listed as potential partners in the multi-billion-dollar development of the Shtokman gas field. Gazprom’s move, nonsensical from a business standpoint, was clear proof of the Kremlin’s readiness to politicise energy. The Shtokman developments demonstrated the unacceptably high risk of assuming that, in dealing with the Russian state, business sense will prevail over political whim and design.

29. Paradoxically, the law, which has been so blatantly disrespected by the Russian procuracy both in procedure and in substance, continues to serve as a pretext where convenient for intimidation or control by the state. The instrumentalisation of law so openly on display in the expropriation of Yukos has now been replicated elsewhere, such as the bullying of BP, Shell and PriceWaterhouseCoopers, with seemingly less and less concern for any semblance of credibility. Extortion has been entrenched as a method of acquisition by the state. An increasingly hubristic Kremlin has calculated that it has space for manoeuvre in disregarding legal and moral obligations—whether with respect to treaty obligations, or business ventures, or commitments to send gas and oil through pipelines without political interference.

30. As a new energy superpower, the Kremlin has become accustomed to abusing the advantages of asymmetrical relations, whether with domestic or foreign energy companies. Facing the brinksmanship of a Kremlin fuelled with the confidence of energy revenues, foreign political and business leaders have lacked a strategic response. Now they must more forcefully advocate a principled commitment to the rule of law in Russia, making clear the costs and consequences of the whimsical attitude towards law that is the norm of the current regime.

11 October 2007

Memorandum by Dr Vladimir Baranovsky, assisted by Sergey Utkin, Russian Academy of Sciences

1. The request for evidence announced by the House of Lords is a timely effort to look again at the complex relationship between the European Union and its biggest neighbour—Russia. Due to its immense role in Russia’s foreign policy, trade, investments, tourism and other areas, the EU constantly attracts attention of experts, journalists and NGOs in Russia.

The Nature and Objectives of the EU-Russia Relations

2. The demand for a certain degree of interaction between the EU and Russia is obvious, but the most appropriate format for the interaction is not yet found. In legal terms, the time is perfect for re-thinking of the relations—the EU-Russia Partnership and Cooperation Agreement (PCA) is about to complete its initial period of action that lasted for ten years. Although the mechanism of an automatic renewal excludes a threat of a legal vacuum, the PCA is gradually losing its meaning, since both Russia and the EU have changed significantly in the last years.

3. The PCA plays a role of a substitute to the missing WTO membership for Russia. The latter is now expected to join this organisation in the nearest future, although the final negotiations may still last for some time. However, this is not an obstacle for Russia and the EU to go forward in their talks in order to prepare a new agreement, since the conditions for further trade arrangements have already been agreed upon.

4. Although political dialogue and cooperation should be organic part of Russia-RU relations, the economic chapters will most probably stay as the key component of the new EU-Russia agreement. The feasible objective of the negotiations is to ensure a reciprocal access to each other’s huge internal markets. The unimpeded flows of investments, business-actors and people would be the best environment for a strategic partnership to thrive.

The Institutional Framework

5. The new partnership agreement would be an asset for the EU-Russia relationship, but it would be a wrong approach to wait until the single new document will move us ahead. A painstaking process of negotiations and ratification will take time, while many improvements can easily be made under the existing PCA.

6. The four Common Spaces could become a long-standing framework for the EU-Russia relations. This formula possesses all advantages and disadvantages of a broad, flexible and non-binding approach. Some parts of the Road Maps represent an insufficiently structured bunch of wishful clauses, and seem to be written in haste. Some fields of possible cooperation envisaged by the Road Maps lack notable substance. Their practical implementation has not been so far very impressive. Revising, broadening and promoting the
implementation of the Road Maps could be a practical interim solution for a while, till the new Agreement is not yet prepared.

7. The Northern Dimension concept is a promising initiative. But its results seem to be conditioned by a constant support on political level. The recent decision to rebuild the Northern Dimension, so that it could reflect the Common Spaces on a regional level, can help to harmonize these two concepts. The regional programmes can bring the EU-Russia high politics closer to people. This is even more so if the EU-Russia cooperation could provide economic development, safer environment and interaction of civil societies on the local level.

8. The institutions set up for ensuring progress in the EU-Russia relations desperately lack transparency. Neither general public, nor experts can regularly get the basic information on the work of the numerous working groups established between EU and Russia. The media are always ready to pay attention to any sort of EU-Russia crises, which easily find their way to the first page of the newspapers, but when it comes to positive achievements, only the insiders who are personally involved in the negotiations may possess this knowledge. EU-Russia eventual initiatives should include an unambiguous commitment of both sides’ officials to provide information to the public.

The Public Perception

9. The image of the EU in Russia is basically positive; it is perceived as a prosperous and relatively efficiently organized area that Russia can use as a sample in various dimensions. However, some tendencies may slightly change this attitude. The EU is also viewed as a huge bureaucratic monster. In addition, it is seen as accumulating certain trends generated by some EU member-states which have disagreements or conflicts with Russia. The most notorious cases are the situation with Russian minorities in Latvia and Estonia, and historical and trade-related arguments with Poland.

10. The most common situation where citizens of the Russian Federation meet directly the rules and mode of action of the EU appears first of all in the visa application process. It remains long and difficult, in spite of the recent efforts to ensure visa facilitation. In a similar way, Russia’s practice of issuing visas is regarded as highly unsatisfactory in many countries of Europe. Numerous cases of humiliation and even personal dramas are extremely harmful to the EU-Russia relations and contribute to negative images of each other in public perceptions.

The Euro-Atlantic Dimension

11. The majority of Russian observers tend to view the United States either as a dominant factor with respect to the EU, or in the context of the US deliberate policy to limit EU ambitions in world politics. Very often the Europeans are perceived either as powerless victims or as submissive clients of the US policy. The divide between the “old” and “new” (ie pro-American) Europeans is another popular theme in Russian political parlance on the EU and related matters. However, on the official level critical remarks to that matter remain relatively moderate.

12. In spite of growing anti-western phobia, the European roots are basically recognized as common societal and civilization parameters both for the United States and for Russia. This promotes Russia’s long-term interest in getting involved in the processes that take place in the Euro-Atlantic area. For the same reason, Russians may experience negative feelings when they find themselves excluded or discriminated from the decision-making in that area.

Common Neighbourhood and Crisis Management

13. The post-Soviet area may become a field of permanent rivalry between the EU and Russia, unless an appropriate modus operandi in the region is developed. Ukraine and Georgia have become the most noticeable examples of “black and white” way of assessing this area by both sides. They both have to make efforts for overcoming the inertia of thinking in terms of confrontational stereotypes, as well as for treating the countries of the region as respected partners.

14. The EU is about to start new large programmes of cooperation with Central Asia. The EU officials insist that they keep contact with Russia on these issues. This dialogue should be constantly maintained in order to avoid another “zero-sum game” starting in the region, which can either become a peaceful crossroad or a source of instability for the whole Eurasia.
15. In Belarus one can see disadvantages of mistrust to each other’s actions that the EU and Russia often show in the post-Soviet area. Both the EU and Russia know well that their cooperation with Belarus will not go far under the current regime in that country. However, concerns of not “giving it up” to the competitor seem to prevail over the obvious desirability and possibility of common approaches.

16. Crisis management is one of the main areas where cooperation between the EU and Russia is supposed to evolve, according to the Road Map on the Common Space of External Security. Paradoxically, this sort of cooperation is the least expected in practice, because the most appropriate cases for joint crisis management exist in the Post-Soviet area, where political disagreements give rise to competition rather than cooperation.

In European countries Russia is often seen as a major obstacle for resolution of conflicts in Moldova and Georgia, while the local disagreements, soured by the recent belligerent history, are neglected. Russia, on its turn, has grievances on the EU’s alleged attempts to block approaches promoted by Moscow.

17. Russia does not seem to believe that the EU could contribute to the post-Soviet conflict-settlement (in Abkhazia, South Ossetia and Transnistria). Their joint efforts are not implausible, but the EU has to convince Russia that (i) such scenario is possible and (ii) it will not play against Russia’s interests.

EU’S FUTURE POLICY

18. The EU and Russia are on the edge of political transformations. The EU tries to quit the tough debate on the Constitution for Europe, and Russia is coming through parliamentary and presidential elections. Any major improvements can hardly be expected in this turbulent period. However, the overall result of the “transition” stage can be predicted rather easily. The EU is to adopt the Reform Treaty that should let the Union to develop further on. Russia is supposed to keep the incumbent political force at power, although slightly restructured. Thus, there is no reason to expect some political miracles that would turn difficult partner in an ideal one. The partners will keep going further their ways and, notwithstanding possible quarrels, these ways give enough space for efficient cooperation in the future.

12 October 2007

Memorandum by Mr David Clark, Chairman of the Russia Foundation

EU-RUSSIA RELATIONS

INTRODUCTION

Relations between the European Union and Russia have deteriorated markedly over the last four years. At the time of the EU-Russia Summit in St Petersburg in May 2003 the relationship was largely constructive and friendly. The EU recognised Russia as a market economy, thereby advancing the goal of WTO membership, cooperation was deepened in areas comprising the “four common spaces” (defined broadly as economic relations, justice/internal security, education/culture and international security) and the institutional basis of the relationship was strengthened with the establishment of the EU-Russia Permanent Partnership Council.

By early 2004 strains were already becoming apparent. In an official communication issued in February of that year the European Commission noted with concern a tendency towards “divergence” on key policy issues and a more “assertive” Russian stance towards its neighbours, including a number of countries that were in the process of joining the EU. While praising aspects of Russia’s political development, it was sharply critical of the country’s overall direction:

“President Putin’s four years in charge have seen a drive to consolidate federal control and strengthen the state apparatus. This has produced more stability, in itself welcome after the uncertainty of the Yeltsin era. This period has, however, also witnessed a weakening of the values to which the EU and Russia (as a member of the Council of Europe and OSCE) are committed. Indeed, reports by international organisations, including the OSCE and Council of Europe, the conduct of Duma elections in December 2003, events in Chechnya and indications of the selective application of the law raise questions about Russia’s commitment and ability to uphold core universal and European values and pursue democratic reforms.”

1 The views expressed in this submission do not necessarily reflect those of the Russia Foundation or individual members of its Advisory Council.

The worsening climate of relations was confirmed when Russia chose to respond to these criticisms by refusing initially to extend its Partnership and Cooperation Agreement with the EU to the ten new accession states. Although this problem was ultimately resolved, it was the start of a trend towards a more assertive and confrontational approach in Russia’s dealings with the EU and its member states. This has led to a number of serious bilateral disputes affecting several EU countries.

In a move condemned as unwarranted by the European Commission, Russia imposed a ban on Polish meat and plant products in November 2005 when diplomatic relations between the two countries declined sharply. The ban remains in force. Oil supplies to Lithuania have been cut off for more than a year in a step many observers interpret as punishment for the refusal of the Lithuanian authorities to sell its Majeika Nafta oil refinery to a Russian company. An acrimonious dispute over the decision of the Estonian government to relocate a Soviet war memorial led to accusations that Russia had resorted to cyber-warfare to disrupt Estonia’s internet communications. The refusal of the Russian authorities to extradite the main suspect wanted in connection with the murder of Alexander Litvinenko in London led to the UK expelling four Russian diplomats, drawing a retaliatory response from Moscow.

Relations at a European level have also been badly affected. Drawing criticism on energy policy and human rights from a number of EU leaders at the Lahti Summit in October 2006, President Putin adopted an openly contemptuous attitude. Two months later the Polish government, with support from Lithuania, vetoed the start of negotiations on a replacement for the Partnership and Cooperation Agreement, due to lapse in November 2007. The EU-Russia Summit in Samara in May 2007 failed to move forward on substance and led to angry exchanges on human rights. In July 2007, despite warnings from Russia’s Deputy Foreign Minister, the European Union adopted a common position in support of the UK over the Litvinenko affair.

The Russian government has also sought to undermine parts of Europe’s political architecture to which it belongs. The election monitoring and human rights roles of the OSCE and the Council of Europe have been actively obstructed and both organisations have drawn fierce allegations of anti-Russian bias from Moscow. Russia’s legally binding obligations as a signatory of the Energy Charter Treaty have been openly flouted.

It is against this background that the European Trade Commissioner, Peter Mandelson, was forced to concede in April of this year that: “Relations between the EU and Russia . . . contain a level of misunderstanding and even mistrust we have not seen since the end of the Cold War”.

DIVERGING POLITICAL VALUES

To reduce these problems to the level of a misunderstanding would seem to be an optimistic assessment of the situation. Instead they reflect a process of political estrangement that has its origins in Russia’s evolution away from democracy and towards a more authoritarian and nationalist style of politics. By definition this is not something that can be addressed through better communication and intensified dialogue. Russia’s ruling elite understands the nature of EU concerns about its political and diplomatic behaviour very well but perceives its interests to be divergent and chooses to pursue them competitively rather than collaboratively. It sees no reason to desist from its current course of action and the EU has so far failed to give it one.

At the heart of this tension is the Russian elite’s rejection of the idea that the western model of liberal multiparty democracy is applicable in Russian conditions. In contrast to the chaotic pluralism of the Yeltsin period, which at least created the potential for democratic progress, the Putin era has been defined by efforts to construct a powerful and controlling state structure as the basis for Russia’s national revival. Although Russia’s leaders claim to be creating their own model of democratic development, it is one that dispenses with many of the principles considered integral to the western idea of democracy, such as the separation of powers, the rule of law, competitive elections, an independent civil society and a free media. In that sense Russia’s recent development reflects a fundamental departure from European political values.

It is important not to exaggerate what this involves. Russia is not retreating into its Soviet past, but it is borrowing selectively from the authoritarian toolbox of that era to create a political order in which all important decisions are taken from the top down. The “political technologists” and Kremlin advisers that perfected the techniques associated with this system dubbed it “managed democracy”. The aim is not to control every aspect of national life in the manner of a totalitarian state, but to manipulate only those aspects of it necessary to monopolise political power and prevent change from below. Many of the rules and institutions of a democratic polity remain in place, at least in a formal sense, but they are prevented from functioning in the manner intended.

— Freedom of speech has been maintained insofar as there is no formal censorship and it remains possible to find strong criticism of the authorities in minority media outlets. But all of the national

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television networks are controlled by the state and slant their coverage accordingly. The intimidation and murder of independent journalists creates a climate of self-censorship that affects the media as a whole.

— Standards of justice may have improved for ordinary Russians, with acquittal rates rising to more credible levels, but there is no real judicial independence and the executive can rely on the courts to do its bidding in the most politically sensitive cases. As the Foreign Secretary noted in his Parliamentary statement on the Litvinenko affair: “both the UN and the EU have reported that the law in Russia is applied selectively”. Courts in the UK and elsewhere in Europe have refused to extradite a number of Russian citizens explicitly for that reason.

— Civil society remains theoretically independent, but increasingly operates within a legal framework that makes it difficult for NGOs that challenge the Kremlin to raise funds and organise. Complex registration procedures, arbitrary tax inspections and national security provisions allow the authorities wide discretion to intimidate or close down organisations they disapprove of. A respected human rights group, the Russian-Chechen Friendship Society, was closed down for “extremist” activities in 2006. President Putin and others also routinely condemn NGO’s as instruments of foreign influence.

— Opposition political parties are entitled to organise and stand in elections, but only on terms that put them at a significant disadvantage. As the reports of international election monitors have noted, the administrative resources of the Russian state and state controlled media are used to favour parties that support the ruling elite. Opposition parties find it impossible to get fair and equal coverage on national television. New electoral laws setting a 7% threshold and abolishing single-member constituencies for elections to the Duma, along with arduous registration requirements for political parties, are designed to shut out independents and those opposed to the current government. It is likely that the forthcoming parliamentary elections will produce a Duma composed exclusively of parties of an authoritarian and nationalist character.

DIVERGING STRATEGIC CULTURES

The speeches and comments of President Putin and his allies make it clear that they associate the reform period of the 1990s with national humiliation and blame Russia’s decline on the imposition of inappropriate western principles. Moreover, they interpret any attempt to pressure Russia into resuming democratic reform as a ploy to weaken her. The “Orange” and “Rose” revolutions in Ukraine and Georgia were seen as hostile, western-inspired events designed to encircle Russia, prompting further Kremlin efforts to restrict political pluralism and subordinate civil society to the state. Authoritarian and nationalist ideas have therefore become fused in the minds of the Russian ruling elite.

In his annual State of the Nation address following the Orange revolution, President Putin asserted his right to define Russia’s political future without reference to western democratic standards:

“Russia is a country that has chosen democracy through the will of its own people. It chose this road of its own accord and it will decide itself how best to ensure that the principles of freedom and democracy are realised here, taking into account our historic, geopolitical and other particularities and respecting all fundamental democratic norms. As a sovereign nation, Russia can and will decide for itself the timeframe and conditions for its progress along this road.”

His chief ideologue and Deputy Head of Presidential Administration, Vladislav Surkov, has termed this approach “sovereign democracy”. In a speech in early 2006 he expanded on this theme and identified the “reduction in national immunity to external actions” as one of four major threats to Russian sovereignty (along with terrorism, military conflict and the loss of economic competitiveness). In this view Russia’s ability to resist westernisation under the guise of political and economic reform (what he called “soft absorption” using “Orange technologies”) is the key to its national revival and its ability to compete with other countries at a global level. So too is its ability to assert national control over its mineral resources and realise its potential as an “energy superpower”.

In many respects the concept of sovereign democracy signifies a reversion to a traditional style of Russian foreign policy thought defined by Dr Bobo Lo, Director of the Russia and Eurasia programme at Chatham House, as “a Hobbesian understanding of the world as an essentially hostile and “anarchic” place; the fear of

7 Vladislav Surkov, Sovereignty is a Political Synonym of Competitiveness, 22 February 2007—http://www.edinros.ru/news.html?id=111148
encirclement by outside forces; and a strategic culture dominated by the geopolitical triad of zero-sum calculus, the balance of power and spheres of influence". The idea of a relationship between Russia and the west based on multilateralism and partnership, envisaged by Russia’s first post-Soviet Foreign Minister Andrey Kozyrev, has been rejected in favour of a competitive model of international relations in which conflicting sovereign interests are asserted through a process of power bargaining.

The result is a strategic culture that conflicts sharply with the one that defines the modern EU where traditional concepts of power politics, such as the balance of power, spheres of influence and the use of force as a routine instrument of policy, have been replaced by voluntary integration, sovereignty sharing, systems of mutual interference and the rule of international law. In some ways this represents the real clash between “old” and “new” Europe in the sense that Russian leaders are articulating ideas that were common in the chancelleries of nineteenth century Europe, whereas the EU represents a conscious break with that tradition. However EU leaders choose to respond, it is important that they recognise this divergence of strategic cultures instead of pretending that it doesn’t exist.

To the extent that the EU provides a pole of attraction for states that were formerly part of the Soviet bloc, and which Russian leaders regard as part of their natural sphere of influence, there is the basis for considerable geopolitical tension whether the EU seeks it or not. As long as countries within Russia’s “near abroad” aspire to follow a European path, the current Russian leadership will tend to see the EU as a normative threat simply by virtue of its existence. President Putin has described the collapse of the Soviet Union as “a major geopolitical disaster of the [20th] century” and although he is not attempting to resurrect it in its old form, the Kremlin makes no secret of its ambition to reintegrate as much of the post-Soviet world as possible under Russian leadership. The EU complicates that project and is therefore increasingly seen as a rival to be neutralised.

The EU could seek to diminish this tension, but only by ignoring its own values and accepting a new continental order that recognised a de facto Russian sphere of influence. That is clearly the aim of Russia’s policy towards the EU. There has already been some slippage in that direction with Jacques Chirac and Gerhard Schroder undercutting EU solidarity by engaging in big power summitry with the Russian President and a reluctance on the part of the EU as a whole to consider further enlargement to the east. Whatever principled objections might be made against this approach, the fact is that it has failed to produce a more cooperative relationship with Russia. On the contrary, it appears to have emboldened President Putin to believe he can divide European opinion and maintain the upper hand.

THE STRATEGIC ROLE OF RUSSIAN ENERGY POLICY

The climate of EU-Russia relations is has been significantly affected by President Putin’s attempts to fulfil Russia’s potential as an “energy superpower” and use it as an instrument of geopolitical leverage. Russia is the world’s largest gas producer and exporter and is currently the second largest producer of oil. It accounts for 45% of total gas imports into the EU, equalling approximately 25% of total EU consumption, along with 27% of EU oil imports. The EU’s dependence on energy imports is set to rise further as domestic sources of hydrocarbons continue to decline and demand continues to rise.

At the same time high energy prices have transformed perceptions of Russia’s relative global position, contributing to high growth rates and substantial export earnings that have allowed the Russian state to pay foreign debts and accumulate a large financial surplus. There are significant doubts about the sustainability of this performance over the next decade with many analysts predicting that a combination of heavy-handed state interference and under-investment will lead to a crisis in Russian energy production. But for the moment policy-makers in Moscow feel that European dependence on Russian energy supplies gives them a decisive edge and they are determined maintain and press home their advantage.

President Putin set out his personal belief in the strategic function of energy policy in an article he wrote in 1999 when he was head of the state security service, the FSB. In it he argued that “the natural resources complex” would be the decisive factor in “the strategy for Russia’s exit from its deep crisis and restoration of its former might on a qualitatively new basis”. Energy policy should not be designed to meet commercial and

8 Bobo Lo, Evolution or Regression?: Russian Foreign Policy in Putin’s Second Term, in Helge Blakkisrud (ed), Towards a Post-Putin Russia, pp 57-71—http://www.chathamhouse.org.uk/pdf/research/rep/R0506Lo.pdf
10 Ivan Krastev, Russia vs Europe: the sovereignty wars, openDemocracy.net, 5/9/07—http://www.opendemocracy.net/article/globalisation/institutions_government/russia_europe
civillian objectives alone, but should be “aimed at furthering the geopolitical interests and maintaining the national security of Russia”. This would be achieved by creating strong, vertically integrated energy companies answerable to the state.

This can be seen as a blueprint for the policy Putin has pursued since 2003 of renationalising Russia’s energy assets and bringing them under state control. The arrest and imprisonment of Mikhail Khodorkovsky and business partner Platon Lebedev on tax charges widely regarded as politically inspired allowed the state to dismantle Yukos Oil, Russia’s largest private oil company, and seize its assets. Major foreign investors, Shell and BP, have also been dispossessed, selling stakes in the lucrative Sakhalin 2 and Kovykta projects to Gazprom at bargain prices in the face of threats to revoke their licences. Proposals to formalise restrictions on foreign ownership of strategic energy projects are contained in a draft Subsoil Law due to be considered by the Duma. This is happening at a time when Russia is demanding unrestricted access and ownership rights for its state-owned companies in European markets.

The trend towards greater state control has been accompanied by an increase in the use of energy supplies as a coercive tool of foreign policy. A number of countries heavily dependent on Russian energy sources have experienced price rises or supply interruptions widely seen as political in motivation. Russia cut oil supplies to Belarus in January 2007 year forcing it to accept higher prices and asset transfers that increase Russian control of its energy distribution network. Gas was cut to Ukraine a year earlier to impose price rises interpreted as punishment for the Orange revolution. Lithuania has been subjected to an econtrol of its energy distribution network. Gas was cut to Ukraine a year earlier to impose price rises interpreted as punishment for the Orange revolution. Lithuania has been subjected to an effective oil embargo since 2006 after deciding to sell its Majeika Nafta oil refinery to Poland instead of Russia. In December 2006 Georgia was forced to accept a doubling of gas prices after it arrested four Russians on charges of spying.

As well as violating international norms, many aspects of this behaviour breach Russia’s binding treaty obligations. Along with fifty other nations Russia is a signatory of the Energy Charter Treaty (ECT), the most important multilateral treaty covering trade in energy products. Although it has not yet ratified the ECT, Russia is provisionally bound by it under the terms of Article 45(1). The Treaty obliges all parties to guarantee investor protection and respect property rights in the energy sector. It also obliges them to facilitate the transit of third country energy supplies across their territory. By expropriating private energy investments and maintaining a pipeline monopoly that prevents EU countries accessing cheaper gas from Central Asia, Russia is clearly not honouring these obligations. Securing Russia’s compliance should be a major objective of EU foreign policy.

The EU also needs to be aware of the various strategies the Russian government is using to increase its energy dominance and to counteract them where necessary. The North European Gas Pipeline planned to connect Russia to Germany through the Baltic Sea is designed to segment the European market and marginalise existing transit countries in Eastern Europe. Likewise, Russian diplomacy in Central Asia, the Caucasus and the Black Sea region is aimed at preventing European countries from developing the infrastructure and relationships needed to access alternative sources of oil and gas. Russian state-owned energy companies are seeking to make major acquisitions in EU energy distribution networks as a way of extending their reach downstream, while at the other end of the supply chain Russia and Iran are exploring the option of turning the Gas Exporting Countries’ Forum into an OPEC-style producer’s cartel.

These and other steps form a comprehensive strategy for maintaining and strengthening Russia’s position as dominant energy supplier. The EU’s response must be to develop a comprehensive strategy of its own to depoliticise energy supplies and ensure that the terms of trade with Russia become more balanced.

**Re-engaging Russia: Interests and Values**

The nature of the divide between Russia and the EU is such that it cannot be resolved by an appeal to common values. To the extent that these exist they have been heavily diluted by the Russian government’s rejection of European norms across a wide range of areas. Even if the ultimate goal is to encourage Russia to return to the path of political and economic reform, as it should be, this is only likely to be achieved by influencing the Russian elite’s perception of where its national interests lie in a more direct material sense.

There are realistic grounds for believing that Russian policy-makers are capable of responding in a pragmatic way to the right mix of incentives and constraints. In the first period of his presidency Putin took a largely cooperative and constructive approach in his dealings with the west, reacting calmly to NATO expansion and the scrapping of the ABM treaty and supporting the United States in its initial response to 9/11. This corresponded with his assessment of Russia’s strengths and weaknesses at that time. Steep rises in energy prices and the belief that Russia’s natural resources offer a shortcut back to world power status appear to have
encouraged the switch to a more assertive and confrontational style of foreign policy based on unilateralism and power politics.

The aim of EU policy must be to counter this and draw Russia gradually into a more balanced rules-based relationship involving reciprocal rights and obligations that are fair and binding. A strategy for achieving this must have two strands. Firstly, the EU must be firm and consistent in its determination to block and punish Russia’s resort to the illegitimate and coercive use of power. Russia only uses these tools to the extent that it thinks they will work. Secondly, the EU needs to open up avenues of progress that offer Russia the prospect of meeting its most important national goals by peaceful and legitimate means. The objective should not be to contain Russia but to channel its energies in a more constructive and mutually beneficial direction.

The following represent some of the main areas where the EU will need to make changes if a strategy of this kind is to become viable:

- **EU solidarity**—The first condition of developing a more effective approach is that European governments will need to adopt a more collective and concerted stance in their dealings with Russia. The EU has more assets at its disposal than is often realised, but only if they are marshalled effectively towards a common purpose. A recent preference for bilateralism among certain member states has artificially strengthened President Putin’s hand by allowing him to play one European government off against the other, often using energy ties to reward or punish accordingly. The trilateral relationship between France, Germany and Russia, in particular, has damaged EU solidarity and undermined its ability to forge a common position. In that respect the EU’s support for the UK over the Litvinenko affair represents a step forward. The change in the political leaderships of some of the larger EU countries, including France and Germany, creates the opportunity for a more effective common policy. This must include a presumption that member states will consult closely on issues of common concern before reaching major bilateral agreements with Russia, such as the project to construct the North European Gas Pipeline.

- **The Partnership and Cooperation Agreement**—The attitude of the EU cannot be to seek a replacement to the PCA at any cost. Russia’s status as a strategic partner has to be conditional on its willingness to respect treaty commitments and observe good relations with EU member states. It should not have been left to Poland and Lithuania to object to the start of negotiations on a new agreement and a cessation of Russia’s embargoes against those countries should be a firm precondition for talks to begin. The EU also needs to insist on the inclusion of clear provisions relating to energy. References to the rules and principles of the ECT would be helpful provided it is made clear that Russia is already legally bound by the treaty. Without this Russia may interpret the agreement as an alternative to the ECT and thus a loosening of its legal obligations.

- **Energy and trade**—The EU is the largest single market in the world as well as Russia’s most important export market. The prospect of closer economic integration, including a EU-Russia Free Trade Area, should be on offer, but only if Russia is willing to respect fair market rules. Energy is by far the biggest single component of bilateral EU-Russia trade, so it is essential that a link is made between closer economic relations and the need for Russia to end its monopolistic and abusive behaviour as an energy supplier. The proposals contained in the Commission’s Third Energy Package include the suggestion of a “reciprocity” rule restricting the ability of companies from third countries to own energy transmission networks within the EU except where an agreement with the relevant third country exists. This would allow the EU to restrict Russian investments in the downstream European energy market unless Russia is willing to open its own energy sector on a similar basis. This proposal should be adopted, with ECT compliance becoming a baseline requirement for third country agreements.

- **Human rights**—As a member of both the OSCE and Council of Europe and a party to the PCA, Russia has accepted a wide range of human rights obligations. These should not be treated as discretionary. The EU-Russia human rights consultations that have been taking place twice a year since 2005 have failed to result in substantive progress and have reached a “dead end” according to leading Russian human rights activists.16 Little information is made available about the meetings, which have assumed a rather ritualistic character. This process needs to be reinvigorated and made more transparent with NGOs formally involved in line with best international practice. If the Russian government will not accept this, the EU delegation should make a point of consulting NGOs formally before each meeting and debriefing them extensively afterwards. The EU should also publish detailed progress reports prior to each meeting and provide a full written report on the discussions afterwards. More generally, the EU’s human rights and democracy promotion efforts in

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Russia need to be stepped up in the face of increased threats to the independence of Russian civil society. Consideration should be given to establishing a European equivalent to the US National Endowment for Democracy to carry out this work at one remove from the EU institutions and member states.

— Ukraine—Getting the EU’s policy towards Ukraine right is critical to influencing Russia in a positive direction. Many Russian liberals believe that the successful completion of Ukraine’s democratic transition would encourage political change in Russia by demonstrating the absence of a cultural barrier to the western model of democracy. Unfortunately the EU, in a mood of caution and introspection, has failed to seize the opportunity presented by the Orange Revolution to consolidate democratic change by putting Ukraine on track for eventual membership. This is a missed opportunity. Ukraine’s integration into the EU would also signal the refusal of European leaders to accept a relationship with Russia based on spheres of influence and open up the Black Sea region as a potential alternative energy corridor. President Yushchenko and other regional leaders met in Krakow to discuss this idea in May 2007, but the EU declined to send an observer to the summit. The formation of a new Orange government in Kiev and the prospect of a new gas dispute with Russia over the coming winter are further reasons why the EU needs to take a more ambitious and involved approach to Ukraine in the future.

Conclusion

The next few years could prove to be a critical turning point in relations between the EU and Russia. President Putin is set to leave office in March 2008, creating opportunities for change in the direction of Russia’s leadership. Although most observers expect that Putin and his supporters will attempt to hold onto power behind the scenes, his departure from the Kremlin means a loss administrative control and it is possible that the new president will prove to be less compliant than expected. It is worth recalling that Yeltsin selected Putin in the belief that it would secure his political legacy.

There are also reasons to believe that the limits of Putin’s statism and energy nationalism will start to become apparent in ways that affect Russia’s perceptions of its national strength over the next decade. The Russian state is not capable of exploiting its natural resources effectively without western investment and technology and there are already signs that production levels are falling to an extent that raises questions about Russia’s ability to meet its domestic and international supply commitments. Even if energy prices remain high, it is likely that Russia is going to feel the squeeze, either through domestic prices hikes or falling export earnings, or possibly a combination of both.

This represents an opportunity for the EU to frame a common policy towards Russia that is firm and constructive in establishing a framework for bilateral relations that meets the interests of both. It essential that the EU recognises this as one of the most important foreign policy challenges ahead of it.

October 2007

Memorandum by the EU-Russia Centre

Summary and Main Recommendations

The EU and Russia are two of the most important, albeit very different, global actors, with many shared interests. The EU has a major interest in assisting the emergence of a strong, stable and democratic Russia, as a close neighbour. However, as a recent study by the EU-Russia Centre on the bilateral relations of EU member states with Russia has shown, this ambition is often hampered by the absence of a common EU approach. (Published 12 October 2007, available from www.eu-russiacentre.org) The UK should seek to promote a common EU approach towards Russia wherever possible.

Trade between the EU and Russia is significant and should be developed further in order to benefit both actors. The EU should work towards formulating agreed aims and objectives for a new Partnership and Cooperation Agreement (PCA), ensuring that discussions neither drift nor are undermined by bilateral disputes between member states and the Russian Federation. Finally, the EU needs to ensure that civil rights and the rule of law remain integral to the EUs relations with Russia.

Main Recommendations

— to define and commit to a common EU approach towards Russia, including a new strategic agreement;
— to emphasise the importance of the rule of law in Russia and to encourage the emergence of a civil society and adherence to civil rights;
— to emphasise the importance of trade relations between the EU and Russia and to promote further development in order to benefit both economies within a clear legal framework;
— to hold Russia accountable to its commitments to organisations such as the Council of Europe, the Organisation for Security and Co-operation in Europe (OSCE) and the EU (within the framework of the PCA); and
— to encourage the EU and Russia to cooperate more on foreign and security policy.

1. The EU-Russia Centre

The EU-Russia Centre is an independent pan-European organisation seeking to promote closer ties between the EU and Russia, to develop ideas about the future of the relationship, and to ensure that both sides adhere to international standards concerning the key elements of a civil society such as democracy, civil liberties and an independent judiciary. Further information can be found at www.eu-russiacentre.org.

This submission outlines the Centre’s main recommendations on the future of EU-Russia relations and identifies the specific areas that need to be addressed and achieved in order to enable relations to prosper.

2. Russia internal

Political power is concentrated in the Kremlin and essentially in the hands of the President. Over 50% of the economy is now controlled by companies chaired by Kremlin officials. The majority of the media is under state control. Civil society is under constant threat. The new law on NGOs which came into force in early 2006 obliges foreign NGOs to inform the government about all their projects, finances and sources of funding. The government may draw on wide powers to prevent projects being carried out. An alarming indicator of the inadequacies of the judicial system is the huge increase in the number of appeals to the European Court of Human Rights in Strasbourg from Russia in the last four years.17 The rule of law and an independent judiciary exist only on paper. Judges deliver verdicts that the state wishes to see, with 99.6% being guilty verdicts; corruption in law-enforcement agencies is widespread and several show trials eg Khodorkovsky, demonstrate that the state often violates or re-writes its own laws.

Research earlier this year by the EU-Russia Centre reveals limited understanding and support for democracy in Russia. Less than a third of Russians understand the importance of the separation of powers and 62% prefer a “strong president” combining executive, legislative and judicial functions. These results testify to the major role played by the state-controlled media in influencing attitudes. (see paragraph 5)

At the same time, the state-controlled media fails to address fundamental social and economic problems. President Putin has been fortunate to preside over an economy which has been bolstered by high energy prices. But he has failed to tackle any of the major social problems such as the poor state of the health service (around 30% of the 142m population cannot afford medical care), the demographic catastrophe with the population shrinking by 800,000 annually, or the dismal standard of pensions (around €50-150 per month).18

Nor has he made much headway in attempts to diversify and sustain the economy. While there is rising foreign investment in Russia this is confined to certain sectors; many potential investors are wary of going into Russia given the absence of any genuine rule of law. The Kremlin has repeatedly announced major investment programmes, most recently at the Sochi economic conference in September, when President Putin announced a $1000bn investment programme in infrastructure over 10 years. But to date there has been little evidence of such announcements being turned into reality.

In the short term it is unlikely that there will be significant changes to the political-economic system. A sharp fall in energy prices would bring pressure on the ruling elite but this does not appear a likely prospect. President Putin’s successor (quite possibly Prime Minister Victor Zubkov) will have to be approved by the current ruling elite and in order to do so will have to promise to protect their interests. The next President will be confronted with a number of social and economic problems (see above) which will require careful political management.

17 Russia is the largest supplier of applications to the European Court of Human Rights. On 1 February 2007 the Court was dealing with 92 150 cases, 20 250 of which (22%) had come from Russia. The number of complaints from Russia is constantly increasing: in 2001 they were 2 490, in 2002—4 716, in 2003—6 602, in 2004—7 855, in 2005—10 009, in 2006—10 569. In 2006 the European court passed 249 judgements concerning cases from Russia, 202 of which the country lost and paid out €1.370 and one million roubles in compensation to victims. Source: http://www.pytkam.net/web/index.php?go=News&n=view&d=629&SNS=c81db9ceae70f43dabe9624290b58 and http://www.bellona.org/articles/justice—european 18 http://www.gks.ru/scripts/db—net/dbinet.cgi
He is also likely to continue the more assertive approach to foreign policy which finds widespread approval internally, partly due to the messages (“a strong Russia is back, confronting the West”) portrayed in the Russian media.

3. Russian foreign policy

The ruling elite is unlikely to endanger its own stability, the inflow of money and the ability to spend this money abroad by embarking on military adventures. Russia will thus continue to seek ways to increase its influence but caution will characterise its foreign policy. President Putin’s more nationalist and assertive foreign policy may have gained him domestic support but few friends abroad, a position that is unlikely to change should he take on the role of Prime Minister following 2008 elections. Indeed it is difficult to think of any neighbour with whom Russia currently enjoys friendly relations. Increasingly Russia tends to lump the EU/the US and NATO together with many politicians and analysts criticising “the West” for seeking to weaken Russia. There is considerable resentment at the alleged neglect of Russia by the US, as Putin believes that he went out of his way to accommodate the US after 9/11 and received little in return. The West was charged with bombing Kosovo, invading Iraq, expanding NATO and promoting the Orange and Rose revolutions. The US decision to install missile defences in Poland and the Czech Republic was met with counter threats and earlier this year Russia announced its intention to withdraw from the CFE treaty. More recently, it has asserted its rights in the Artic and resumed strategic bomber patrols.

At the same time there has been some useful cooperation with Russia in dealing with nuclear safety and proliferation, Islamic terrorism (regarded as major threat by Moscow) and crisis management (North Korea, Middle East). Russian attempts to divide the West and the EU are likely to continue. It is important that the EU is perceived as developing its own united policy towards Russia and not following any line laid down by Washington. The EU and US have different interests (eg trade and energy) with regard to Russia but this should not hinder a frank exchange of views on Russian foreign policy within the transatlantic dialogue.

4. EU-Russia relations

The EU has a major interest in a stable, peaceful, prosperous, democratic Russia that is a reliable trading partner, friendly neighbour and a supporter of an effective rules-based international system. Both sides are committed to a new strategic agreement that would replace the PCA. Russia contends that the 1997 PCA was negotiated during a period of Russian weakness and expects that new negotiations will be carried out by two equals. The EU contends that the PCA needs to be replaced in order to provide a legal base for new policy areas that have been developed over the past decade. These include sensitive areas of legal and police cooperation, foreign and security policy as well as the energy sector. Meanwhile there is much on-going business between the EU and Russia with officials meeting regularly and progress being made in different areas across the four “common spaces.” The networking between large numbers of Russian officials meeting with their EU counterparts should not be under-estimated.

Work with Russia is progressing on many less visible areas, not least in the area of justice and home affairs. Meetings on trafficking of human beings, money laundering and terrorist financing are held on a regular basis between the Commission and the Russian authorities. Passenger data exchange also takes place in the framework of the agreement on Kaliningrad. A priority area should be improving the border crossing points between Russia and the EU.

With regard to foreign and security policy cooperation, Russia has shown little interest in the Common Foreign and Security Policy (CFSP) and yet has sought to play a full part in the European Security & Defence Policy (ESDP). There has been no consensus within the EU, however, to grant Russia any special status. Many member states have also pointed to the difficulties of cooperating with Russia in this sensitive area when there are a number of issues where both sides take very different views eg Kosovo, the frozen conflicts. Nevertheless, given the importance of Russia as a global actor, the EU should intensify efforts to work with Russia in foreign and security policy. The “frozen conflicts” can only be resolved with Russian involvement. Russia is a key player with regard to Iran, an important player in the Middle East and is keen to strengthen the multilateral system. The EU should discuss with Russia possible changes to strengthen international institutions, and seek to cooperate with Russia more in crisis management, peacekeeping operations and civil rescue missions.

Earlier this year the European Commission revised its external assistance programmes. The European Neighbourhood and Partnership Instrument (ENPI) covers Russia but its financial allocation for the period 2007–13 will not be extensive (approximately €250 million for individual country projects out of a total of €12 billion). Conversely, Russia was the largest beneficiary of EU financial assistance under the TACIS programme (40% of all funding from 1991 to 2006). An independent evaluation of the efficacy of that
programme by the European Court of Auditors however, found that the effectiveness of the funds had been low and it could not assess the performance of the projects positively. In a number of cases, the Court observed lack of real dialogue, major delays in implementation and failure to present clear and realistic objectives for the projects that had been financed. Many Russian NGOs, beneficiaries of EC assistance, also refer to the heavy and complicated bureaucratic mechanisms. The ENPI seeks to address the reasons behind such shortcomings, at least as far as the Commission’s role is concerned. The results remain to be seen.

In recent years, trade in goods between the EU and Russia has grown considerably. In 2006 Russia was the EU’s third most important trading partner behind the US and China. EU exports to Russia have more than tripled, while imports have doubled. The sharp rise of energy prices has resulted in a large trade deficit (€70bn in 2006), but the margin has decreased. Energy accounts for two thirds of the EU’s imports while the main exports are machinery and vehicles. In the same year, 32% of the total EU exports to Russia came from Germany, by far the largest exporter, followed by Italy and Finland. Germany also occupies the first place in imports from Russia, followed by the Netherlands and Italy. Even in countries with poor political relations with Russia, such as Poland and Estonia, trade relations have gained considerable momentum in the current decade.

While the PCA arrangements provide for “business as usual” the opening of negotiations on a new strategic partnership has been delayed due to a bilateral Polish-Russian trade dispute. Russian pressure on Estonia and Lithuania, and recent trade disputes with Sweden and Italy, has not helped create an atmosphere conducive for negotiations. Some of the newer member states have pressed the EU to adopt a tougher approach towards Russia, a stance not necessarily accepted by other member states. Chancellor Merkel, put the emphasis on EU solidarity at the Samara summit but at the same time she insisted that solidarity requires responsibility. The EU would be hamstrung in its relations with third countries if every member state sought to block negotiations because of a bilateral dispute. The smaller member states are those likely to benefit most from a common policy towards Russia. Given the political uncertainties on both sides, including changes in leadership of Russia and some of the major member states, the negotiations—whenever they start—may last for at least two years with a further two years for ratification. The EU has a number of strong cards to play including the sheer size of its internal market, its consumption of Russian energy (in a global market), its technology and its know-how in finance, social, environmental and regional issues.

Russia is one of Europe’s main energy providers. Many EU member states (especially new member states) are heavily dependent on Russian natural gas and oil for their domestic energy consumption needs. In absolute figures, Germany is the largest importer of both Russian gas and oil. The past few years have seen a tension in EU-Russia relations because of the rise in energy prices and Russia’s assertive behaviour with some of its other neighbours (Ukraine, Belarus, Georgia, Moldova) in reviewing the terms for energy supplies. This has led to recent proposals from the European Commission for the creation of a comprehensive European energy policy. The latest such proposal, the Third Legislative Package for the EU electricity and gas markets contains safeguards against majority ownership by foreign businesses of EU electricity and gas networks. A clause of reciprocity in unbundling and other legal requirements is proposed. Furthermore, foreign control of a Community transmission system will be permitted only by way of bilateral agreements between the EU and other neighbours (Ukraine, Belarus, Georgia, Moldova) in reviewing the terms for energy supplies. This has led to recent proposals from the European Commission for the creation of a comprehensive European energy policy. The latest such proposal, the Third Legislative Package for the EU electricity and gas markets contains safeguards against majority ownership by foreign businesses of EU electricity and gas networks. A clause of reciprocity in unbundling and other legal requirements is proposed. Furthermore, foreign control of a Community transmission system will be permitted only by way of bilateral agreements between the EU and other neighbours (Ukraine, Belarus, Georgia, Moldova) in reviewing the terms for energy supplies. This has led to recent proposals from the European Commission for the creation of a comprehensive European energy policy.

Despite the difficulties of achieving a common EU approach towards Russia, it is incontestable that all member states, including the UK, are likely to be more effective in securing their aims by speaking with one voice. This applies to the security of energy supplies, investment protection to tackling international issues such as climate change, Kosovo, Iran and terrorism among other topics. At present, however, Russia finds it relatively easy to divide member states by offering energy deals. These are partly a reflection of short-term political and economic interests, and partly due to the absence of any real EU competence in the energy field. If the EU were given the power to negotiate with Russia on energy it would greatly improve the situation.

At present the EU and Russia seem to be talking “past” each other, with Russia playing the energy power card and (most of) the Europeans insisting on values as part of discussions. It is vital to explain to Russia that a rules-based system is very much in its own interest, not least in helping to provide a more stable environment for domestic and foreign investment. The EU might also emphasise more its willingness to help Russia diversify its economy, bringing know-how and technology that is absent in Russia today. The present lopsided trading relationship is not healthy in the long-run for either side. The EU should stress its desire to see a prosperous, democratic Russia, as a long-term political and economic partner across the board.

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5. Russian views of the EU

How does Russia see the EU? The official line is that Russia is eager to work with the EU. But the state media rarely provide any positive coverage of the EU. According to EU-Russia Centre research undertaken earlier this year, 71% of Russians do not consider themselves to be European and just over half view the EU as a threat to Russian interests The EU, therefore, has a major task ahead in engaging with Russians across the spectrum to inform them about the EU, to emphasise the importance of European values and to strengthen democratic forces in Russia. That engagement needs to take place among the leaders of tomorrow and will only be achieved by developing an understanding and appreciation of one another’s cultures.

There needs to be a vast increase in the number of student exchanges and serious consideration should be also given to abolishing visas, encouraging more visits to EU countries by Russians from all walks of life, giving them exposure to different values and societal systems. This would have an immediate and positive impact on people to people contacts. The previous EU cooperation and assistance programmes (TACIS) had only a marginal effect in Russia and one should not have over-high expectations of the new instruments.

6. Values

The EU and Russia tend to overlook each others’ values. Some member states have downplayed the importance of values in dealing with Russia. But the pendulum is now swinging the other way, partly due to changes in the leadership of several member states, partly due to the urgings of some new member states and partly due to developments in Russia, eg more than 25 journalists have been murdered in Russia in the past five years. The negative view of Russia in Europe was given a further blow with the murders of Mrs. Anna Politkovskaya and Mr. Alexander Litvinenko- both fierce critics of the regime and president Putin personally. These developments are causing concern in Europe about the direction in which Russia is heading. In September 2007, Transparency International ranked Russia as one of the forty most corrupt nations of 180 of the world’s countries, while the World Bank ranked the country as the 106th easiest country to do business from a list of 178. If there is a further slide in popular attitudes towards Russia it may be impossible to get a new treaty ratified by all 27 member states. The bottom line for the EU must be to insist that Russia respects the commitments it entered into on democracy, human rights and the rule of law in the PCA as well as the Council of Europe which it joined in 1996.

CONCLUSION

EU-Russia relations are at a crossroads. While it is tempting for some EU member states to strike bilateral deals with Russia the EU should seek to promote a united front towards Russia and ensure that its values remain at the forefront of any negotiations. A sound and long-term relationship cannot be built between two actors who do not share common values. The EU’s primary interest should be to help promote a stable, democratic and prosperous Russia that enjoys the same civil liberties and rule of law as EU citizens. The negotiations for a new strategic partnership should be judged on whether they promote these aims. The UK should thus strongly support a common EU policy towards Russia.

15 October 2007

Memorandum by Dr Sabine Fischer, European Institute for Security Studies

Question 6: Russian perceptions of the EU

Russian perceptions of the EU have undergone several changes since the breakdown of the Soviet Union. Foreign policy during the early Yeltsin years was mainly focused on the US and NATO. At that time, the Russian leadership saw Washington as its main political partner on the international stage. Later on, it was NATO’s eastward enlargement which provoked the fiercest political reactions from Moscow, reaching a crisis point and the near break-up of relations over NATO’s intervention in Kosovo in 1999. So essentially it was the US and NATO which kept political minds in Russia occupied, the debate being narrowly focused on classical security and military issues. At the same time, the first steps towards EU enlargement went almost unnoticed by the Russian political elite. Although the EU had become Russia’s most important economic partner and deliverer of technical assistance as early as 1995, it did not play a crucial role in Russian debates about foreign policy, European security or international relations in general.

21 Voices from Russia: Society, Democracy and Europe, EU-Russia Centre December 2006.
Russian thinking on international relations and all related matters was, and still is, dominated by classical realist and neo-realist ideas. Throughout the 1990s, the EU from a Russian point of view was seen essentially as an economic integration project rather than a political actor in its own right. In terms of this world view, issues like “normative” or “civilian power”, often associated with the EU’s role in international relations in the Western debate, do not play an important enough role for the EU to be considered as a “heavyweight” player. This perspective certainly obstructed Russian views on political developments within the EU, and the EU’s slowly growing weight in international relations.

At the same time, it was the slow and often uneasy development of EU foreign policy which made it rather difficult for Russian political actors to fit the EU into their picture of the international system. Therefore, while economic relations with the EU (and its member states) figures very high on the Russian agenda, foreign and security policy remained clearly focused on bilateral relations with individual EU member states, the US and NATO.

This changed significantly after 1999–2000. The war in Kosovo led to the deepest crisis between Russia and the West since the breakdown of the Soviet Union. Already in 1999, it was the EU who took over the role as a mediator between Russia and NATO, and it was during the EU summit in Cologne in June 1999 that Russia was brought back to the negotiating table.

The creation of CFSP and ESDP as stronger and more visible instruments of the EU’s second pillar changed Russian perceptions of the EU as a foreign policy actor and also created hopes for more intensive cooperation in the field of security, with the idea that the EU could, ultimately, become an alternative or counterweight to NATO. This motive was particularly important after the war in Kosovo and the resulting “chill” in Russia-NATO relations.

Another motive that was at least as important for the newly elected Russian leadership was strengthening economic partnership with the EU. By the end of the 1990s, significant parts of the Russian political elite had slightly shifted their view on international relations and Russia’s role as a great power. Economic influence and integration in a globalised economic environment were now seen as preconditions for Russia recovering its status as a great power. The economic and financial breakdown in 1998–99 had also left its mark on policymakers’ understanding of the priorities that Russia should set in order to regain a strong position on the international stage. The strengthening of the state and the Russian economy, therefore, and the quest for closer cooperation with the EU as Russia’s most important modernisation partner, became a central issue in Russia’s foreign policy during the early Putin years.

Together with the EU’s emerging profile as a foreign policy actor and its growing political and economic weight in Eastern Europe, this renewed interest in economic cooperation triggered a shift in the way Russian elites perceived and talked about the EU. For the first time since the breakdown of the Soviet Union, the EU was seen as a political actor in its own right. Russian elites seemed to be getting used to the idea that supranational institutions in Brussels could play a role independent from member states’ capitals.

However, there was almost no time for this shift in thinking to translate into practical policy. EU-Russia relations deteriorated quickly after the “Colour Revolutions” in Georgia, and particularly Ukraine. Russia had already watched the development of the European Neighbourhood Policy (ENP) with suspicion and insisted on being acknowledged as having a special position in the EU’s neighbourhood (leading to the Roadmaps for the Four Common Spaces signed in May 2005). Domestic events in Georgia and Ukraine, however, led to a radical change in Russia’s attitude. From a Russian perspective, the EU now became one of the main suspects in what it saw as a plot to try and topple Russia-friendly regimes in the region and roll back Moscow’s influence in its own backyard. Quite a few Russian observers, traumatised by the “Orange Revolution”, even went so far as to see the ultimate goal of this “conspiracy” as the collapse of the Russian government, so that “the West” could gain control over the country and its energy resources. Hence, to a certain extent the EU now became a part of the potentially adversarial “political” West, a category from which it had been excluded throughout the 1990s.

However, this new attitude whereby Russia took the EU seriously as an important actor and possible rival in the former Soviet Union did not last very long. After 2005, the crisis that occurred in the wake of the rejection of the constitutional treaty in the French and Dutch referenda, and resulting paralysis of internal decision-making, led to the EU’s importance shrinking in Russian eyes. This shift is also a function of the fact that Moscow, according to its new image of itself as a global player, now claims to act with total independence. The harmonisation of norms and values, which is at the core of the EU’s foreign policy approach, is alien to this concept. A third reason for the downgrading of the EU in Russian foreign policy thinking is Moscow’s altered perspective on global politics. The perceived decline of the US’s capacity to shape international developments seems to have broadened Russia’s room for manoeuvre. These two developments are mutually reinforcing and weaken, from a Russian perspective, the EU’s weight as a supranational actor. By 2007, Russia has therefore returned—and explicitly so—to a bilateral approach in its relations with the EU.
Russia’s perceptions of the EU, and their implications for Moscow’s policy, have always been a mixed product of changing Russian discourses, internal developments within the EU and the emergence of an EU foreign policy, as well as the global, above all transatlantic, context of EU-Russia relations. Taking into consideration the upcoming elections in Russia, there is no change to be expected before March 2008. As will be discussed below, the EU has lost much of its leverage on domestic developments in Russia. Given Russia’s growing economic strength and the elite’s increasing rejection of any involvement from outside, it will become increasingly difficult for the EU to influence Russian attitudes. The only way out for the EU is to find common positions on the most relevant issues in relations with Russia (namely energy relations, regional relations in the Eastern neighbourhood/former Soviet Union etc) and to pursue them more decisively than has been done in the past.

Questions 4 – 12: EU democracy promotion, technical assistance and democratisation in Russia

The EU has acted as an external promoter of democracy in Eastern Europe after the breakdown of the socialist systems. However, in the case of Russia, the results of this policy remain very limited, and the EU’s scope for action in the sphere of democracy promotion has narrowed down considerably in recent years.

President Putin’s term in office has been characterised by simultaneous processes of domestic political and economic reform and the increasing de-democratisation of the political system. Between 2000 and 2004, several big reform projects were launched by the Russian government, focusing on pressing issues like administrative reform, reform of the civil and social services, and budgetary reform. Since 2005, however, reform processes have stalled, the liberalisation of the social systems reversed, and a strong role of the state in the economy re-established.

The domestic political situation in Russia changed during the same period. What began as a campaign—supported by the US and the EU—aiming to restore the Russian state after its devastating decline throughout the 1990s, ended in a highly ambivalent process of de-democratisation, re-centralisation of the political system, establishment of state control over the party system, media and civil society. At the same time, thanks to revenues from energy exports, an unprecedented stabilisation of the state budget and rapid economic growth, Russia managed to shake off its dependence on external donors.

The EU has been providing technical assistance to Russia since 1992, aiming at promoting democracy and good governance. After 2002, this assistance was explicitly linked to the reform projects of the Russian government. However, any claims as to the overall efficiency of this assistance and its impact on democratisation would have to be very modest. On the micro-level, EU efforts at democracy promotion have run up against difficult conditions of implementation, corruption, and (for most of the time) the lack of a strong state actor pursuing a coherent reform strategy. During the last few years, however, it has been first of all the de-democratisation of the macro-political context, which as prevented the EU and other external actors from having a democratising impact on Russian domestic development. This has been accompanied by the already-mentioned reluctance of Russian elites to accept any foreign involvement in domestic politics or lecturing on democracy and human rights. Last but not least, economic growth and increasing financial independence put the Russian government in a position to fund reform measures from its own resources, whereas TACIS funds for Russia have steadily shrunk in recent years.

The success of external democracy promotion crucially depends on whether political elites and the population in the respective state support the democratisation project. It no less crucially depends on whether a state is strong enough to pursue a policy of democratisation with the support of external actors. During the 1990s the Russian state was too weak to develop a thorough reform agenda oriented towards democracy and the market economy. Hence, external actors did not have a strong partner in their effort to promote democracy in Russia. Furthermore, EU means provided to Russia and the other former Soviet Republics through TACIS have been very limited in comparison to the assistance to the Central and Eastern European (CEE) candidate countries, so that political elites and potential bureaucratic and economic veto players saw little incentive to engage in the project of democratisation. Recently, it is, in contrast, the apparent strength of the Russian state which prevents external democracy promotion in the name of sovereignty.

Although technical assistance in the framework of TACIS has had a positive impact on single reform areas, the EU’s and other external actors’ attempts to promote democracy in Russia have largely failed. With a semi-authoritarian regime firmly controlling the political and societal system, Russia’s growing economic strength and its claim to be treated as an equal partner (which implies the strict acceptance of its sovereignty) the prospects of efficient democracy promotion are doomed for the year to come. Therefore the EU should concentrate on keeping Russia involved in various political dialogues and societal exchange, and on economic
cooperation. The dialogues and sectoral cooperation in the framework of the Four Common Spaces provide a—\text{as measured by the current situation}—good opportunity to prevent Russian isolation and to a limited extent also to further promote international norms and standards.

Questions 8–9 \textit{EU policy coherence and integration rivalry in the Common Neighbourhood/former Soviet Union}^{22}

The Partnership and Cooperation Agreements (PCAs) which the EU concluded with Russia and the other former Soviet Republics throughout the 1990s are mixed trade and economic cooperation agreements, with both the Commission and the member states involved. The aim of these agreements is the deepening of economic cooperation and legal harmonisation between the EU and its partner countries. The agreements codified the support of transformation of the post-Soviet states and societies towards democracy as a main principle. Therefore, in the framework of the Partnership and Cooperation Agreement all relevant actors within the EU committed themselves to the same approach in relations with Russia, largely based on the EU’s identity as a value-oriented actor and civilian power.

However, in the actual implementation process the EU looks much less unified. The Commission is in charge of the coordination of cooperation between the EU and Russia, and of the implementation and administration of TACIS funding and projects. Therefore, it stands out as the main promoter of the goals fixed in the Partnership and Cooperation Agreement. At the same time, its room for manoeuvre always depends on whether there is coherence between the EU and member states, and among member states themselves. In the case of Russia, such coherence is lacking because member states have strong and contradictory interests regarding bilateral as well as multilateral relations with Russia.

Before 2004, EU member states could be divided into two groups with regard to relations with Russia. One group, containing bigger member states like France, Germany and Italy, emphasised Russia’s economic importance and advocated a pragmatic relationship safeguarding EU economic interests, first of all in the energy sector. Anti-democratic tendencies and human rights violations were not seen by these states as reasons to take a more distanced attitude toward Russia. Rather, they argued that Russia should be involved more intensively in European integration processes because this was the only way to promote European values in the Russian political system and society. The other group, most explicitly represented by Great Britain, denounced de-democratisation in Russia and advocated a tougher approach in the EU’s relations with Moscow. However, before 2004, no EU member perceived an immediate security threat emanating from Russia. As a consequence, the debate about Russia within the EU almost completely lacked classical geopolitical and security considerations. This “de-securitised” discourse came to an end with the accession of the Baltic States, Poland and the Czech Republic. Central European states and societies share a traumatic and violent history with Russia, which leads them to have an extremely critical attitude towards Moscow and to advocate a policy of “containment” of Russian influence in Europe.

The inclusion of the Central European perspective shapes the overall European political process on two levels. The new EU members pushed for a more active EU policy toward the states adjacent to EU and Russian borders. Furthermore, they took a much tougher stance in direct relations with Russia, on a bilateral as well as on the EU level. The new members saw the “Orange Revolution” in Ukraine as a window of opportunity to accelerate the democratisation of a key country in the so-called “common neighbourhood” and its closer alignment with the EU. From their perspective, such a development promised not only a desirable spread of democratic values beyond EU borders, but also a significant improvement of their national security. Consequently, the Baltic States and Poland pushed vehemently for strong EU involvement to support the democratic forces in Ukraine during the conflict over the presidential elections, and they succeeded. Later on, Warsaw’s veto in response to a Russian ban on the import of Polish meat and the Estonian monument dispute in early 2007 led to a blockade of the negotiations on the follow-up of the Partnership and Cooperation Agreement, which is due to expire by the end of November 2007. The new member states, thus, are well capable of influencing the EU’s policies towards Russia, and have done so successfully several times since 2004.

Enlargement has added a new dimension to the EU’s Russia policy, which is characterised by strong historical and security components. This has become especially visible in the EU’s and Russia’s growing competition over the common neighbourhood/former Soviet Union.

The EU and Russia approach their common neighbourhood with very different concepts of regional governance. The EU has a post-modern and at the same time hybrid identity. Common values form the basis of internal integration as well as foreign policy. In its relations with non-members, the EU aims to communicate its basic values outwards and to support partner countries in adapting them. Through the

\footnote{Both terms are politically loaded. The EU prefers to speak of a common neighbourhood, glossing over Russian-EU disputes over the territory and its overall fragmentation and polarisation. The Russian use of the term “former Soviet Union”, on the other hand, implies Moscow’s claim for a predominant position in the region.}
“Europeanisation” of its neighbours (the underlying principle of the PCAs as well as ENP), it aims to create a stable democratic and peaceful regional and international environment. EU foreign policy, therefore, transcends state borders and influences domestic political, economic and societal development.

Russian policy, by contrast, is guided by the classical idea of competing zones of influence. Russia claims for itself a dominant position in the CIS. External actors’ presence is interpreted in terms of a zero-sum game undermining Russia’s position and primacy in the region. Although the focus of Russia’s policy towards its neighbours has shifted to profitable economic relations and has been shaped by an attempt to develop soft power skills, Moscow has time and again used economic and energy interdependence as well as its involvement in the protracted conflicts in the region in order to keep “deviant” states under its umbrella. Seen from the point of view of the realist Russian mindset, the EU’s claim for the Europeanisation of adjacent states lacks legitimacy. What Brussels sees as support of internal and external stabilisation is interpreted in Moscow as an attempt to expand the EU’s influence over the region—at Russia’s expense.

If they want to overcome the current misunderstandings in bilateral as well as regional relations, both sides have to critically reconsider their approaches and engage in an open and sincere dialogue. The EU should be aware of the fact that its policy can have unintended geopolitical elements, which might be perceived as a threat by Russia. Russia, for its part, must abandon its outdate zero-sum thinking, because it precludes any form of regional cooperation. This would pave the way for a more constructive policy towards the most pressing problems of the region, above all the protracted conflicts and energy relations. Ultimately, it would help to defuse the most serious tensions in bilateral relations between the EU and Russia.

12 October 2007

Memorandum by Group Menatep Limited (GML)

INTRODUCTION

1. The House of Lords European Union Committee, Sub Committee C (foreign affairs, defence, and development policy) has requested evidence, in its inquiry into The European Union and Russia on, amongst other questions:
   1. What is the nature of the Russia-EU dialogue with regards to energy questions? To what extent is Russia an indispensable partner, rival or obstacle for the EU in its efforts to attain the objectives of its recently adopted external energy policy?
   2. What does the EU have to offer Russia in the context of a negotiation, and how can it best influence Russian thinking and policy? Is the current institutional framework for EU-Russia relations, based on the PCA, the four “common spaces” and the “Northern Dimension” working well?
   3. What are the main characteristics of the Russian political, economic and social system, and how are these likely to evolve in the future?

2. GML Limited (“GML”) (previously Group Menatep Limited), a diversified financial holding company established in 1997 by Mikhail Khodorkovsky, the former CEO of Yukos Oil Company, Platon Lebedev and others. GML remains the majority owner of Yukos, holding approximately 51% of Yukos equity capital through wholly owned subsidiaries, Yukos has now been declared bankrupt and its assets sold, in the main below market value, at forced auctions the principal beneficiary of which has overwhelmingly been Russian state-owned oil monopoly: Rosneft. Tim Osborne is a director of GML. He does not represent Yukos or the individuals mentioned above.

3. We believe GML is in a unique position to comment on issues that crucially affect the European Union’s relations with Russia. It is GML’s belief that the forced dismantling of Yukos was a successful ploy to put key elements of the energy sector in the hands of the state and marked a turning point in terms of Russia’s commitment to domestic property rights and international energy security, not to mention the rule of law. GML currently has a claim under the Energy Charter Treaty (“ECT”) against the Russian Federation for compensation for discriminatory treatment. If successful, the Russian Government will be required to pay compensation totalling not less than $33 billion to Yukos’ former owners; this is the largest commercial arbitration claim ever filed.

4. We provide a background to GML and Yukos at Annex 1 (not printed here) and a briefing on the Energy Charter Treaty, and GML’s claim, at Annex 2.
1. The Russian Federation—An Indispensable Partner?

5. The Russian Federation is the world’s largest gas producer and exporter and is currently the second largest oil producer. Imports from the Russian Federation currently account for 45% of total gas imports (Pipeline and LNG) into the EU, equalling approximately 25% of total EU gas consumption. In October 2004 the New York Times reported that Gazprom was the sole supplier of gas to Estonia, Latvia, Lithuania and Slovakia and provides 89% of Hungary’s gas, 86% of Poland’s and nearly three quarters of the Czech Republic’s. The article also added that, according to data available from the Energy Information Agency at the time, Gazprom supplies 36% of Germany’s gas, 27% of Italy’s, 25% of France’s, 67% of Turkey’s, 65% of Austria’s and 100% of Finland’s. It is also thought that Gazprom supplies the majority of gas consumed by Moldavia, Macedonia and Bosnia Herzegovina. Official DTI estimates indicate that Britain will import 80% of its gas by 2020, with the majority of supplies originating in Russia. The Russian Federation currently supplies 27% of Europe’s oil.24

6. The EU gas supply-side is highly concentrated, with the Russian Federation, Norway and Algeria accounting for over 85% of total gas imports into the EU yet the European energy market remains highly segmented and therefore uncompetitive and vulnerable to monopolistic abuse. One of Russia’s objectives has been to ensure that it remains so. It has used its oil and gas pipeline network to control energy distribution beyond its borders, acquire infrastructure in other countries and prevent new supply alternatives. Despite increasing supply diversification towards LNG, it is likely that the Russian Federation will remain the single largest gas supplier to Europe. Russia is expected considerably to grow its share of gas supplies in the EU in the future. Some industry observers forecast that, by 2030, the EU may depend on Russian imports for up to 80% of its total gas consumption.25

7. The Russian Federation’s dominance of European energy supplies gives rise to the prospect that this power can be leveraged for the political benefit of the Russian Government. This was recognised by Prime Minister Tony Blair MP in May 2007, who said, following the publication of the Government’s 2007 Energy White Paper:

“Increasingly we will be required to look at importing energy from less stable parts of the world . . . As if that were not enough, we are now faced with countries such as Russia, who are prepared to use their energy resources as an instrument of policy”.26

8. Moreover, the Russian Federation has itself demonstrated its willingness to use its energy resources as a tool of its foreign policy. In January 2007, Russia dramatically raised the price at which it sells gas to Belarus from a subsidised $46 per 1,000 cubic metres to around $200 per 1,000 cubic metres. Whilst this increase to market prices for former Soviet states would normally have been welcomed, the suddenness of the move demonstrated the Kremlin’s willingness to use energy as a political weapon.

9. This followed a similar episode in Ukraine in January 2006. In a move that was widely seen as a response to the victory of Western-leaning Victor Yuschenko in the Ukrainian Presidential elections over Kremlin-backed Victor Yanukovich, the Russian Federation restricted the supply of gas to its former ally by means of massively increasing the price from $50 to $230 per 1,000 cubic metres. This was threatened again in October 2007 following the anti-Kremlin victory in the Ukrainian General Election.

10. In both examples, energy supplies were cut off, dramatically affecting end-customers in Europe; Germany, France, Poland and Hungary all experienced significant drops in supplies during the disputes. Cliff Kupchan, former US State Department official and director of the Eurasia Group was quoted in the Financial Times in 2006, as saying: “there is a correlation between the price at which Russia sells gas to its former satellites and their political loyalty to the Kremlin”;27

11. The Ukraine crisis was not the first time Russia has interrupted energy supplies as a way of exerting political pressure on a foreign government: Russia cut energy supplies to the Baltic States when they insisted on the withdrawal of Russian forces in the early 1990s; to Ukraine during a dispute about the future of the Black Sea Fleet in 1993–94; and to Belarus, Poland and Lithuania in 2004. Georgia and Moldova have also experienced price rises after signalling their political independence from Moscow. The recent episode with Belarus is unlikely to be the last.

23 “Europe worried over Russia Gas Giant’s Influence”, 3 October, Julie Dempsey, retrieved from www.energybulletin.net/2389.html
24 “Peril of using energy as an instrument of political pressure, Report, Political Affairs Committee, Marko Mihkelson, 20 December 2006.
25 “Peril of using energy as an instrument of political pressure, Report, Political Affairs Committee, Marko Mihkelson, 20 December 2006.
26 “Peril of using energy as an instrument of political pressure, Report, Political Affairs Committee, Marko Mihkelson, 20 December 2006.
27 Financial Times, 14 March 2006, Arkady Ostrovsky; “Energy of the state: how Gazprom acts as a lever in Putin’s power play”.
2. Negotiating With the Russian Federation—The Partnership & Co-operation Agreement


13. In its negotiations with the Russian Federation, the EU must acknowledge that the Kremlin, and state-owned gas monopoly Gazprom, is equally dependant on Europe as the main end-purchaser of oil and gas. This is a key negotiating tool that the EU must leverage when dealing with the Russian Federation on energy matters and was made in a French Parliamentary Report on Energy and Geopolitics in November 2006.28

“It is time to wring the neck of the notion that the European Union would be controlled by an all-powerful energy supplier against whom it would have its hands and feet tied. Today indeed the relation between the European Union and Russia is too much regarded as a unilateral dependency of the former on the latter—but this analysis is not viable in the long term”.3


15. However, foremost amongst Europe’s failures to hold the Russian Federation to accepted standards and norms of behaviour is the EU’s fundamentally weak position on the Russian Federation’s observance of the Energy Charter Treaty. Eneko Landaburu, Director General of External Relations and Chief Negotiator of the new Partnership and Cooperation Agreement (“PCA”) with Russia, said in February 2007: “its obvious we’re not going to be able to convince the Russian authorities to agree with the ECT” suggesting instead that the “key principles” of the ECT should be incorporated into a new PCA.

16. This position is disturbing in that it might be interpreted as acceptance of the Russian Federation reneging on commitments it has made to the 50 other signatories to this international treaty. The European Union is not empowered to negotiate on behalf of all the other signatories to the ECT but importantly, if the Russian Federation will not abide by its obligations under this Treaty, it is logical to assume that the Russian Federation will only abide by new agreements that are weaker than those already in existence and only whilst it so chooses.

17. This position is also disturbing as it ignores the fundamental truth that the Russian Federation is legally bound by the ECT under Article 45(1) of the Treaty. No new PCA can change the Russian Federation’s status as a legally bound signatory to the ECT irrespective of whether the PCA includes the “key principles” of the ECT or not. This point was made by Chair of the European Parliament’s Foreign Affairs Committee, Jacek Saryusz-Wolski30:

“Emphasises that Russia is already bound by the ECT pursuant to Article 45 thereof31; . . . regards the mere transposition of the ECT principles into the Partnership and Cooperation Agreement as redundant, while acknowledging the added value of provisions clarifying or supplementing the obligations contained in the ECT, in particular those contained in the Transit Protocol”.

18. The British Government has further acknowledged the Treaty’s binding nature on all signatories32:

“The Energy Charter Treaty obliges Contracting Parties to endeavour to accord non-discriminatory treatment to Investors of other Contracting Parties as regards the Making of investments. This obligation is relevant for the 38 Contracting Parties who have ratified the Treaty and for the five Signatories applying the Treaty provisionally”.

19. Russia is one of the countries that apply the Treaty provisionally and is thus legally bound. The Energy Charter Treaty is fully binding on and enforceable against the Russian Federation. The EU should encourage the Russian Federation, to acknowledge and abide by its obligations under the ECT.

20. The Financial Times33 reported, on 29 August 2007, that it had seen draft Commission proposals to reform the European energy sector further by unbundling ownership of production, distribution and supply assets. The FT also reported on a separate Commission document about the implications of unbundling which

29 Peril of using energy as an instrument of political pressure, Report, Political Affairs Committee, Marko Mihkelson, 20 December 2006.
31 “Article 45(1) of the ECT provides for states that have signed but not ratified the ECT to be provisionally bound thereby from signature to ratification, unless they have opted out pursuant to Article 45”.
said the “EU could be vulnerable to a strategy of third countries to dominate the EU markets not only in terms of supply but also by acquiring the networks . . . where investment is driven by other motives than economic ones”. The Commission, according to the Financial Times, proposed several measures to prevent uncontrolled access and ensure reciprocity of investment; the most notable was a proposal to declare Europe’s energy sector a “Strategic Asset” thus restricting access for non-EU states. The FT commented:

“The requirement for reciprocity would be a particular blow to Gazprom . . . which has intense ambitions to expand in Europe and already owns a range of assets and equity stakes in the EU”.

21. The Commission published its draft legislation on 19 September 2007 which included the legal basis for a reciprocity of investment rule. The Draft Directive on Common Rules for the Internal Market for Natural Gas Article 7(a) provides:

1. Without prejudice to the international obligations of the Community transmission systems or transmission system operators shall not be controlled by a person or person from third countries.

2. An agreement concluded with one or several third countries to which the Community is a party may allow for derogation from paragraph 1.

This would appear at first sight to give the Community the power to block acquisition or control of energy transmission assets and a further power to negotiate access to energy markets in third states thus providing the basis for reciprocity rule in the energy sector. However, it is limited to the transmission network.

22. This is a positive step forward but the EU should not limit its rules on reciprocity of investment to the transmission network rather, seek a broader prohibition against ownership by third country companies and individuals of all energy assets, with the prospect of a negotiated exemption for states who provide reciprocal market access in the energy sector to European firms and individuals. The standard for judging such reciprocal access should be full compliance with the Energy Charter Treaty which is binding and enforceable on all signatories irrespective of whether the Treaty has been ratified or not (excluding those signatories which opted out of provisional application under Article 45 (1), which Russia did not).

23. Any new PCA with the Russian Federation must have as its foundation the fact that the ECT is binding on the Russian Federation and build an agreement from there. Any other agreement will inherently be weaker and will allow the Russian Federation to continue its aggressive dominance of Europe’s energy supply market. The ECT is the strongest legal protection available and any replacement is likely to be weaker, given the now much stronger negotiating position of Russia.

4. Russia’s Political, Economic and Social System

24. The politically motivated destruction of Yukos, and the imprisonment of its executives and ultimate beneficial owners, was a turning point in terms of the Russian Federation’s commitment to both international energy security and domestic legal, human, and property rights. It has also become clear, since the beginning of the Yukos affair that the Russian Federation has allowed its criminal justice system to become infected with corruption and political influence. Its courts have become susceptible to outside pressure and inducements to the extent that persecution of political enemies of the state has been facilitated by judges. In October 2004, Chairman of the Russian Constitutional Court, Valerii Zorkin, marked the 13th anniversary of Russia’s judicial reform by saying that the country’s judicial system is in many aspects worse now than it was in the Soviet era. In July 2006 the state controlled oil company Rosneft accepted “the possibility that certain judges may be susceptible to economic, political or nationalistic influences”.

25. Since the December 2004 auction of Yukos’ key production unit, Yuganskneftegaz, the number of people targeted by the Russian authorities in connection with Yukos has risen from 18 to 45 and now includes senior western managers of Yukos and its remaining assets, and Tim Osborne, a director of GML. This is the first time the Russian Prosecutors have targeted western businessmen personally in the Yukos affair and is an alarming escalation in the Russian Federation’s vendetta against Yukos and its shareholders.

26. As reported in The Times, Mr Osborne and the Yukos officers (US citizens) have received no official communication of the accusations against them. The accusations are groundless and were posted on the Russian Federal Prosecutor’s website straight after GML had won a Netherlands court ruling whereby the proceeds from any future sale of Yukos’ international assets would be handled by the Dutch Courts rather than the Russian liquidator. This would ensure that legitimate Yukos creditors would be recognised. The accusations limit Mr Osborne’s ability to travel and discharge his fiduciary duty to manage GML’s claim under the ECT. They further damage his personal and professional reputation and ability to carry on his legal

36 Rosneft Oil Company, IPO Prospectus to the London Stock Exchange, p 52.
practice. Mr Osborne has offered to be interviewed, in London, by the Federal Prosecutor in connection with this investigation but he has received no reply to his offer. The Foreign and Commonwealth Office have sent an official Demarche to their Russian equivalent on Mr Osborne’s behalf.

27. Further, the diplomatic exchange with Moscow over the murder of Alexander Litvinenko highlighted a fundamental inequality inherent in UK extradition law: Russian citizens in Russia cannot be extradited due to provisions in the Russian Constitution; Russian citizens with asylum in the UK cannot be extradited to Russia due to the Government’s view that they would not receive a fair trial; yet British citizens in the UK could be extradited to Russia due to provisions in the 2003 Extradition Act under which the Russian Federation is designated a Category 2 Territory (which permits Russia, on seeking extradition from the UK, to simply provide “particulars of information” rather than a prima facie case). Thus British citizens living in the UK are not protected politically and must rely on the UK courts for protection.

28. The Russian authorities’ prosecution of the Yukos case demonstrates a worrying trend towards Russia’s abuse of its privileges, under international extradition treaties, and the deterioration of the rule of law in the Russian Federation. In two rulings in Bow Street Magistrates Court on extradition requests for individuals connected to Yukos, Judge Timothy Workman refused to allow extradition on the basis that the requests were politically motivated and the defendants would not receive a fair trial in Russia. The Supreme Court in Lithuania made a similar ruling in a separate case and government authorities in the Netherlands and Luxembourg have refused to hand over Yukos-related documents to the Russian Prosecutor. Most recently, the Swiss Federal Tribunal ruled the Russian Government’s prosecution of Messrs Khodorkovsky and Lebedev was politically motivated and refused to cooperate with Russian requests for mutual legal assistance.

29. The Swiss Tribunal’s judgment was delivered on 23 August; the following day Mr Yuri Chaika, Russian Prosecutor General, held an impromptu press conference to denounce the Tribunal’s decision and describe it as politically motivated and an attack on Russia’s sovereignty.

30. As mentioned in 27 above, the Russian Federation is designated by the UK as having Category 2 status under the Extradition Act 2003. The political justification for according Russia this status was that Russia respects fundamental and due process rights in its criminal law. However, in its pursuit of individuals connected to Yukos, the Russian Federation has breached several international treaties relating to extradition and mutual assistance, including the European Convention on Extradition 1957, the European Convention on Mutual Assistance in Criminal Matters 1959, is in breach of Article 3 of the Council of Europe’s Statute and also undermines the Council’s raison d’être: respect by member states for the rule of law and human rights. Values about which the Council has rejected all compromise.

31. The Russian Federation has systematically breached these treaties in its prosecution of the Yukos case. Therefore no request for extradition to the Russian Federation of an individual connected to the Yukos case can be seen as free from political motivations.

32. This evidence is submitted by Tim Osborne, director, by and on behalf of GML Limited.

16 October 2007

Annex 2

The ECT and GML’s Claim

Key Points

In early 2005, GML Limited subsidiaries, Yukos Universal Limited (“Yukos Universal”) and Hulley Enterprises Limited (“Hulley”) who, together, hold a 50.97% shareholding in Yukos, commenced arbitral proceedings claiming damages of not less than $33 billion against the Russian Federation pursuant to the terms of the Energy Charter Treaty (the “Treaty”) which Russia signed in 1994 and by which Russia is legally bound.

This is the largest commercial arbitration claim ever filed.

37 Article 3 prohibits extradition concerning “political offences”. The Russian Federation has been found on three occasions to have nonetheless made extradition requests for such offences, two to the UK and one to Lithuania.

38 Article 2: Assistance may be refused; a—if the request concerns an offence which the requested Party considers a political offence, an offence connected with a political offence, or a fiscal offence;

39 Even the need to combat terrorism does not dispense states from respecting these values, see the Convention on the Suppression of Terrorism (ETS 90) and the Guidelines on Human Rights and the Fight Against Terrorism, adopted by the Council of Ministers in July 2002.
The claims are based upon the Russian Federation’s violation of the provisions of the Energy Charter Treaty which protect investors’ rights in cases where investors are subjected to discriminatory measures by which their investments are expropriated without payment of prompt, adequate and effective compensation.

Substantive hearings regarding Yukos Universal and Hulley’s claims were due to begin on 11th June 2007 in The Hague. The Tribunal has bifurcated the hearing so it will hear arguments on jurisdictional and admissibility issues first and assuming Yukos Universal and Hulley successfully demonstrate that there are no jurisdictional and/or admissibility issues which prevent the claim from proceeding, the merits of the case will then be explored at a further hearing to be set by the Tribunal. The initial hearing was postponed due to sudden unavailability of GML’s nominated arbitrator and is now due to take place in early 2008 although a date is yet to be set.

**Russia and the Energy Charter Treaty**

The Russian Federation signed the Treaty on 17 December 1994 and, pursuant to the provisions of the Treaty, is legally bound thereby, notwithstanding the fact that the Treaty has not, to date, been ratified by the Duma.

Article 45(1) of the Treaty states that:

> “Each signatory agrees to apply this Treaty provisionally pending its entry into force for such signatory in accordance with Article 44 to the extent that such provisional application is not inconsistent with its constitution, laws or regulations”.

The Russian Federation chose not to opt out of applying the Treaty pending ratification when it signed it provisionally. If a country chooses not to apply the Treaty provisionally (such as Australia, Iceland and Norway) they must state their decision when signing the Treaty.

Furthermore the Russian Federation has stated on several occasions that it attaches great importance to the Treaty as part of its energy policy. On 17 December 2002 at the Energy Charter Conference, Andrei Denisov, the then Deputy Foreign Minister and the head of the Russian delegation to the conference stated that:

> “Russia views the Energy Charter as an important instrument for international energy cooperation, and reiterates its intention to continue its participation in discussions on a wide range of issues related to energy transit, trade, investments and energy efficiency within the framework of the Charter process”.

On 28 November 2003, Victor Khristenko, then Deputy Prime Minister of the Russian Federation, met the head of the Energy Charter Conference and the General Secretary of the Energy Charter Secretariat. At this meeting it was confirmed that Russia would participate in accordance with the Treaty to ensure the stability of world and regional energy markets. Going one step further, Russian Finance Minister, Alexei Kudrin said, on 8 February 2006:

> “Russia must develop its gas network in order to provide [pipeline] access to everyone, including private companies, and we are working on it. In that context we are going to ratify the charter [Energy Charter Treaty], although we cannot set a date for the moment”.

However, Presidential aide, Igor Shuvalov, and Foreign Minister Sergei Lavrov have both contradicted this. Shuvalov, quoted in RIA Novosti on 20 June 2006 said:

> “the Russian Federation has signed the Energy Charter . . . The principles contained within it are correct, but Russia will not yet undertaken any commitments to ratify it . . . There are a few things that do not correspond to Russia’s interests”.

Foreign Minister Lavrov said, on 23 October 2006:

> “We share the principles that are laid down in the charter. However, the principles that are laid down in the Treaty to the charter seem unfair to us”.

The Russian Federation however does apply the provisions of the Treaty selectively in its dealings with countries with whom Moscow is on friendly terms, as President Putin said on 12th February 2007, quoted in the Russian Financial Control Monitor:

> “The underlying principles of the charter are acceptable” he said, adding that Russia is using them in relations with German, Italian and Ukrainian Partners”.

It is noteworthy that the Russian Federation still participates in the inter-state cooperation and institutional arrangements of the Treaty. In particular, the Vice-Chairman of the Energy Charter Conference is the Russian Federation’s representative, Mr Ivan Materov (State Secretary and Deputy Minister of Industry and Energy). In addition, the Deputy Secretary General of the Energy Charter Secretariat, Dr Andrei Konoplyanik, is also a Russian national.
Hearings in The Hague

As stated above, hearings regarding Yukos Universal and Hulley’s claims were due to commence in The Hague in early summer 2007 but have been postponed until 2008 due to the sudden unavailability of GML’s nominated arbitrator. GML has since appointed Dr Charles Poncet as its nominated arbitrator. The Arbitral Tribunal will first discuss and rule upon jurisdictional and admissibility issues before examining the merits of the case.

The arbitration proceedings are confidential. However, it is thought that the Russian Federation will argue that it does not have to apply the Treaty due to the proviso contained in Article 45(1) of the Treaty that it should only be applied provisionally to the extent that domestic laws permits it to do so. The Russian Federation may also argue that, constitutionally, it is the Duma, not the Government that has the power to bind the Russian Federation. If that were the case, the Russian Federation should have opted out of provisional application when it signed the Treaty in 1994.

Yukos Universal and Hulley are represented in the proceedings by Shearman & Sterling’s Paris office (led by the internationally renowned arbitration lawyer Emmanuel Gaillard), The Russian Federation is represented by Cleary Gottlieb Steen & Hamilton’s Paris office (Robert Grieg).

Yukos Universal and Hulley has nominated Dr Charles Poncet of, Geneva law firm, ZPGCL to act as an arbitrator with the Russian Federation nomimating as an arbitrator Stephen M. Schwebel, the former head of the International Court of Justice. The chairman of the arbitral tribunal, Yves Fortier of Ogilvy Renault in Montreal, the honorary vice president of the London Court of International Arbitration, was appointed by the Permanent Court of Arbitration in The Hague.

If GML is successful in demonstrating to the Tribunal that there are no jurisdictional and/or admissibility issues which prevent the case from proceeding, the Tribunal will then set a further procedural timetable leading up to a hearing on the merits of the case. It is unlikely that a final decision on the claim will be forthcoming before 2010.

History of the ECT

The roots of the Energy Charter Treaty date back to political initiatives in Europe following the end of the Cold War in the early 1990s. It was clear that opportunities existed for mutually beneficial cooperation between East and West in the energy sector. Russia and many other countries within the Commonwealth of Independent States and Central and Eastern Europe were rich in energy resources. However, the development of these energy resources required major investment. It was to encourage such investment that Russia entered into the Energy Charter Treaty.

Western European states had a strategic interest in diversifying the sources from which they obtained their energy supplies in order to reduce their dependence upon other areas of the world. It was recognised that there was a need to ensure that a commonly accepted foundation existed to develop energy cooperation between states of the Eurasian continent.

In December 1991, the European Energy Charter (or the Energy Charter Declaration) was signed in The Hague. This document was a declaration of political intent to promote cooperation between states within the energy sector. The Energy Charter Treaty was developed upon the basis of the Charter. However, unlike the Charter, the Treaty is a legally binding, multilateral treaty dealing specifically with inter-governmental cooperation within the energy sector.

The fundamental aim of the Treaty is to strengthen the Rule of Law on energy issues by creating a level playing field of rules to be observed by all governments who are signatories to the Treaty, thus minimising the risks associated with energy related investments and trade.

The Treaty was signed on 17 December 1994 and entered into force on 16 April 1998. Alongside the European Community, 51 nations have signed the Treaty. 46 nations have ratified the treaty with 2 nations applying the treaty “provisionally” until it is formally ratified. 3 nations opted out pending ratification, Russia did not opt out and applies the treaty provisionally.

One of the focal points of the Treaty is the promotion and protection of investments within the energy sector. The investment protection regime is found in Part III of the Treaty entitled “Investment Promotion and Protection”. The key provisions are Articles 10 (covering promotion, protection and treatment of investments) and 13 (providing for the compensation of investors whose investment has been the subject of nationalisation or expropriation).

Article 26 of the Treaty provides for a binding international dispute settlement procedure in the event that a signatory to the Treaty and an investor cannot resolve a dispute amicably.
Memorandum by Dr Iris Kempe, Centre for Applied Policy Research

THE 2004 PARADIGM CHANGES AND BEYOND. ADJUSTING EU-RUSSIAN RELATIONS

I. IN 2004: A THREE-FOLD PARADIGM CHANGE

From the early 1990s, European-Russian relations were driven by two key concepts: building a market-based democracy within Russia and using EU enlargement as a mechanism to promote democratic changes throughout Central and Eastern Europe. The year 2004 can be seen as the turning point in this approach, one that has required reshaping relations between the European Union and Russia, a task that remains incomplete. President Putin’s second term in office, which started in March 2004, led to changes in Russia that altered the chaotic but open-minded Yeltsin period into an era characterized by attempts to create a strong state based on (1) recentralisation of the political system, (2) the “dictatorship of law” and (3) a Souverenaya Demokratiya. Since 2004, Russia has staked its claim to a new role in the international system as an energy-based power to be taken seriously in international organisations, in conflict resolution and in fighting against terrorism. Even if Russia and the European Union do not share the same values, both partners need each other and widespread linkages have superseded Cold War thinking.

By 2004 the European Union was a success story of simultaneous broadening and deepening. The EU grew to 27 member-states, eight of them from the former Soviet bloc and sensitive about building new relations with the Kremlin. Since then, however, European integration has suffers from both the failure to adopt the constitutional treaty and a more general enlargement fatigue. Since then, decision making in the EU of 27 depends greatly on national influence and strategic alliance building among members.

The rainbow revolutions in Georgia (2003) and Ukraine (2004) initiated and a new wave of transition, both in the national arena aiming for democracy and a market economy, and closely interlinked to the countries’ international orientation. Georgia and Ukraine, but potentially also other states formerly or still belonging to the Kremlín’s sphere of influence, are struggling for transition, Western orientation and a balanced position with Moscow. The deterioration of relations affects more than just Russia itself. Moscow sees countries such as Ukraine, Georgia, Belarus and Kazakhstan as its “near abroad”. While Brussels regards them as the “new neighbourhood”. Disputes with the Kremlin are also carried out by proxy in these states since the rainbow revolutions highlighted their striving for transition, Western orientation, and a balanced position toward Moscow. As former United States National Security Advisor Zbigniew Brzezinski asserted, democratic and Western-oriented states bordering Russia would be the most reliable guarantee to prevent any kind of post-Soviet power play. As far as Russia is concerned, the paradigm change of the rainbow revolution indicates alternatives for post-Soviet transition while at the same time limiting Russia’s international influence.

II. TOWARDS A NEW FRAMEWORK AGREEMENT

The formula of partnership and cooperation between Russia and the EU has to be perceived as both the guideline and the institutional framework for the EU-Russian relations. These were expressed into the Partnership and Cooperation Agreement which was signed in 1994 but came in force only in 1997. This framework agreement is at a low ebb and not an instrument applying to the 2004 paradigm changes. Both the Finnish EU presidency during the second term 2006, and the following German presidency announced their aim to renegotiate at least some of the outdated Partnership and Cooperation Agreement (PCA) between the EU and Russia. The PCA expires at the end of 2007. Though it is automatically extended every year as long as none of the partners withdraws from the treaty, in assessing the value of the agreement one has to consider the impact of the 2004 paradigm changes.

The search for a new framework remains a rocky road, as the Polish veto in Helsinki EU summit in 29 October 2006 shows, and is bound to lead to a heated debate during the ratification process, circling the issue of “common values” and energy. The experience of domestic development in Russia, as well as the continued strong-handed foreign policy in the neighbouring region has drastically changed perceptions of Russia. It is also likely to provide a stage for the Baltic states and Central and East European countries to criticise Russian shortcomings in implementing democratic values and its tendency to pursue hegemonic external relations.

Russian policymakers point out that in its current form the PCA regards Russia as a transition state en route to a free market economy. Its main principle is the gradual adoption of the EU regulatory framework. Therefore the Kremlin is in favour of a new framework considering Russia and the EU as equal partners, with Russia having been accepted as a market economy facing WTO accession. It should also address more directly the Russian interest in a visa-free regime or, at a minimum, lowered standards for visa for Russian citizens travelling to the EU, as well as closer economic and technological cooperation. The principle of...
equality would also mean that any conditionality concerning domestic developments in Russia be removed from the joint framework with the sensitive exclusion of opting for the rights of the Russian minorities in the Baltic states in particularly.

The lack of a common European Russian Policy

Individual governments have been using EU institutions to pursue narrow national interests, rather than acting within the Union’s framework. To illustrate the current situation one has to differentiate among three groups of actors: first, the group of Russia sceptics, who are guided by legacies of the past and are blocking cooperation with Russia. The Polish veto of the mandate for a new Partnership and Cooperation Agreement, the problem of the Druzhba pipeline in Lithuania and the conflict surrounding Tallinn’s war memorial are all examples. Second are countries that do not care much about Moscow, such as Portugal and Greece. Third are the proponents of fruitful relations with Russia, such as Finland and Germany.

Some countries use tension with Russia in connection with paying historic debts. Others find it useful to distract from other issues (the British position in Iraq for example), while for others it plays a role in domestic politics (competition within Germany’s grand coalition, for example). Beyond this instrumentalisation, national solo acts are first and foremost caused by conflicting values. At the same time, economic initiatives driven by the interests of single EU member states are bypassing deadlocked EU-Russian relations while also taking advantage of other member-states’ reservations. For example, the North Stream gas pipeline, directly connecting Vyborg, Russia, with Greifswald, Germany, literally bypasses Polish, Lithuanian, Swedish and other countries’ economic, security and ecological interests. British-Russian conflict about the ex-spy Alexander Litvinenko who was poisoned by polonium combines economic interests on the one hand with strong value dissonances on the other. While the first motive prevents London from overreacting, the British government convinced the Portuguese EU Presidency to issue a statement on 18 July calling on Russia to extradite Andrei Lugovoi. Both cases show how European solidarity of values can be subordinated to economic interests.

European discussion by building alliances

Since the 2004 three-fold paradigm change, prioritising a European consensus over national interests in EU-Russian relations has been increasingly difficult. Running Russian relations bilaterally, however, includes the danger of undermining the interests of other EU members, circumventing EU processes and challenging the EU’s external capacity in general. Bi-lateral cooperation does have some positive impact in EU-Russia relations.

Alliance building depends on two main factors: geographic and historic proximity. As a reaction to the American military intervention in Iraq, Paris and Berlin used their historic concept of alliance building with Moscow to add weight to their position. This was also the very moment when the concept of “old” and “new” Europe was born, complicating EU policy toward Russia from the other direction. In their strained relations with Russia, Tallinn, Riga and Vilnius coordinate their positions to provide both carrots and sticks. Even when the Baltic states and the Visegard countries share very close positions on Russia, the impact of cooperation is still far from its full potential. Furthermore, the EU’s Russian policy has been restricted by missing alliances between the leading proponents and the sceptics. The results of the May 2007 EU-Russia summit in Samara were an example of how taking each other more seriously would broaden European opportunities. Only once Merkel took Polish concerns more seriously was a moderate outcome possible. Had she not, a complete disaster in European-Russia relations might have resulted. In addition, the lack of cooperation among the different groups offers the Russians opportunities to play members off against each other and to undermine common EU positions.

III. Policy Recommendations

Short term

1. The 2004 paradigm change in EU Russian relations requires readjusting EU Russian policy adequately, a task that has not yet been fully addressed. In a short term Europe has to awake from its illusions about a Westernised Russia. A rentier state that uses energy as a foreign policy weapon is not susceptible to outside influence. So it is time for more pragmatic relations that keep in mind that Europe and Russia need each other for energy and security. At the same time, it would be short-sighted to neglect the risks related to the growing values gap between Russia and the West. In practical terms EU governments and institutions would be well
advised to move from lecturing Russia on democracy, freedom of the media and the rule of law in general to pointed criticism targeted to specific issues.

2. Negotiating a new Partnership and Cooperation Agreement became a litmus test of the state of affairs, but also showed the deadlocks and shortcomings of the mutual relations. Beyond the current blockade situation, one might have some doubts about the far-reaching character of the agreement. The content and actors of EU-Russian relations are dominated by single, even contradictory interests, which can not be simply adjusted in the framework agreement. Therefore thinking in short-term perspectives should be more targeted toward individual agendas such as energy dialogue, the overlapping neighbourhood, European values, etc. Only in the medium-term perspective is building linkages between the different agendas worth considering.

3. The national solo acts have caused more harm than good, therefore it is high time to stop using Russia policy for purposes other than shaping EU-Russian relations. From an institutional perspective, alliance building among member states should used to its full potential. These groupings should combine EU members with differing historic experiences, geographic proximity and economic interests in Russia. Beyond the European perspective, a dialogue on building an asymmetric partnership with Russia should be put on the transatlantic agenda.

4. Putin has been using conflicts with EU member-states to demonstrate Russia’s importance as a global player as well as to pay historic bills, demonstrating his position that the breakdown of the Soviet Union is the biggest tragedy of the 20th century. To reduce the vulnerability of the Central European and the Baltic states would handle this challenge well by overcoming the legacies of the past which might otherwise burden the EU-Russian relation as a whole. Furthermore the new EU Foreign Policy Representative should create a special representative in charge of an early warning mechanism about upcoming bilateral problems that could also have an impact on the entire EU.

Medium and long term

1. Policy-makers should always bear in mind that the last 10 to 15 years in Russia have brought enormous and rapid changes. Continuation of the present situation is probably the last thing that one should expect. The Putin system is at pains to look permanent, but so were its predecessors. Further dynamic development is more likely, and European leaders should be prepared to take the opportunities that present themselves. In this regard upcoming elections—not perhaps the 2007–08 elections but more likely the following ones—should be followed with the considerable attention.

2. Following the assertion that democratic and Western-oriented states bordering Russia would restrict any kind of post-Soviet power play, the West should pay pretty close attention to the outcomes of the rainbow revolutions in countries such as Ukraine and Georgia. Even if Belarus is still dominated by the authoritarian regime of president Lukashenka a high level of human capital, the geographic proximity to Europe and a calculable size of the country would are clearly indicating the country’s need for European affiliation, presuming the necessary regime change. The EU and its member state should be offering all forms of support for further domestic transition and integrate these countries into Euro-Atlantic structures.

3. Adjusting EU-Russia relations can not be isolated from a Gesamtkonzept of a new European Eastern policy targeted at two main aspects: mapping the future architecture of Europe as a whole and developing further European integration, starting with successfully implementing the European reform treaty. This is a point at which bilateral relations with Russia are, for instance, similar to bilateral relations with the new neighbours, and at which the mechanisms of European policy begin to supersede the mechanisms of individual national policy. Over the long-term, national interests will be pursued within the European Union, but beyond its borders, a common European interest will be pursued.

5 November 2007

Memorandum by Dr Sergei Prozorov, University of Helsinki

EU-RUSSIAN RELATIONS: BEYOND THE CONFLICTUAL IMPASSE

Response to the Call for Evidence for the Inquiry into “The European Union and Russia”,
undertaken by the Sub-Committee on Foreign Affairs,
Defence and Development Policy of the House of Lords Select Committee on the European Union

1. For the most part of the postcommunist period EU-Russian relations have developed in a singularly paradoxical manner. On the one hand, the idea of Russia’s progressive “integration into Europe” has remained virtually unchallengeable in both Russia and the EU, serving as the background assumption of any assessment
of EU-Russian relations. On the other hand, there is an abundance of empirical evidence of the increasingly conflictual character of EU-Russian relations from 1995 onwards. We need only recall the sharp divergences between Russia and the EU over the two Chechen wars, the Kosovo crisis, President Putin’s state consolidation policies, the Yukos case, the “colour revolutions” in post-Soviet states, etc. There appears a wide gap between the unchallengeable goal of integration on the level of policy rhetoric and the manifestly problematic state of EU-Russian relations that may well be considered not the exception but the rule throughout the postcommunist period. For example, in 2004, the year when EU-Russian relations sharply deteriorated over the issues of Yukos, Chechnya, Kaliningrad and concerns over Russian democracy, President Putin stated in his address to the Russian Federal Assembly that European integration was not only a matter of economic policy but also a “spiritual question” for Russia. It therefore appears that the rhetoric of integration has acquired a life of its own, entirely detached from the actual state of Russian-European relations. From this perspective, the currently perceived “crisis” in EU-Russian relations, whose intensification is often dated to the Litvinenko assassination in November 2006, should not be viewed as an aberration in the otherwise cooperative pattern of interaction, but a somewhat belated adaptation of foreign policy rhetoric to the actual situation in EU-Russian relations. Thus the present crisis must be understood against the background of the patterns of EU-Russian relations that prevailed throughout the postcommunist period.

2. In Understanding Conflict between Russia and the EU (Palgrave, 2006) I have proposed that conflicts between the EU and Russia arise out of the “mismatch” of the policy logics that the two parties deploy towards each other. Against the facile argument about the EU as the champion of the “integrationist” logic and Russia as the stubborn defender of state sovereignty, it is possible to demonstrate that both the principles of sovereignty and international integration are at work in the policies of both Russia and the EU without coinciding in particular cases. For instance, in the case of Russia’s recurrent proposals for a visa-free regime between Russia and the EU it is evidently the latter that is deploying the conventional instruments of sovereignty in its insistence on the uniform and stringent visa regime for Russian visitors to Europe. The same logic could be observed in the tendency to view socioeconomic developments in Russia through a “security lens”, which resulted in the inflated images of “new security threats” allegedly emanating from Russia, from infectious diseases to organized crime. In such cases we may speak of the pattern of the EU’s exclusion of Russia from the European space, which manifestly contradicts the EU’s own integrationist ambitions. Conversely, in the cases of the EU’s admittedly modest attempts at influencing the sociopolitical situation in Russia through eg technical assistance and policy advice programmes, support to non-governmental organizations or oppositional public figures, it was Russia that has regularly invoked the claims of sovereign equality and non-interference against the expansion of the EU’s “normative power” into the Russian political space. In these cases, which have become increasingly accentuated during President Putin’s second term, we may speak of Russia’s self-exclusion from the space of European politics.

3. These two patterns have arguably dominated the development of EU-Russian relations since the mid-1990s, the main tendency being the gradual abandonment by Russia of the position of the complainant over unwarranted exclusion by the EU in favour of a more assertive “self-exclusive” orientation that devalues concrete moves towards greater integration between Russia and the EU without entirely dispensing with the ideal of integration as such. The key motif in Russia’s policy towards the EU in the second term of the Putin presidency has instead been the demand for symmetric, non-hierarchical interaction, particularly in the sphere of norms and values, in which the EU has been held to exert hegemonic influence on Russia. Russia’s unwillingness to maintain the “subject-object” pattern of relations with the EU was particularly evident in its refusal to participate in the ENP (European Neighbourhood Policy) that succeeded the TACIS programme, which was the key EU instrument of managing the post-Soviet transformation, opting instead for a bilateral framework of the four Common Spaces, whose ineffectiveness is now evident to most observers. In this manner, Russia has visibly upgraded its symbolic status in relations with the EU even though the political and economic benefits of such a decision remain dubious.

4. The contemporary crisis in EU-Russian relations may be understood as the radicalization of the logic of self-exclusion on the part of Russia. This radicalization is most evident in the political sphere, in which the increasingly active European criticism of the authoritarian tendencies of the Putin presidency is either ignored by the Russian party or reciprocated by arrogant reprisals and crude “look at yourself!” arguments. The latter form the substance of the proverbial doctrine of “sovereign democracy”, originally developed in the amateurish theorizing of the Deputy Chair of the Presidential Administration Vladislav Surkov and elaborated in the writings of numerous apologists. As has been noted by critics inside and outside Russia, the notion of “sovereign democracy” ultimately comes down to the first term devouring the semantic content of the second, so that “democracy” begins to denote whatever the sovereign wants it to. Moreover, taking into consideration the conventional definition of democracy as “popular sovereignty”, the term “sovereign democracy” either becomes a classic case of a pleonasm or implies the expropriation of the sovereignty of the people by another
sovereign figure. Whatever its conceptual deficiencies, the discourse of sovereign democracy resonates perfectly with the self-exclusive orientation of Russia with respect to Europe, insofar as it allows to dismiss all European criticism of the anti-democratic tendencies of the present regime while retaining “democracy” as a mode of the regime’s self-identification. In this manner, Russia reserves for itself the sovereign right to define both the content of the concept of democracy and its own correspondence to this concept.

5. As Russia no longer participates in the EU’s technical assistance programmes and does not depend on external financial aid, the EU is deprived of the instruments of conditionality in dealing with Russia and its capacity to influence the course of political developments is strongly undermined. Faced with the self-exclusive orientation on the part of Russia, the EU can either continue, rather half-heartedly, with its project of the expansion of European norms and values to Russia or reciprocate Russia’s self-exclusion with its own self-exclusive project. The first option logically reproduces a conflictual pattern of the EU-Russian interaction (inclusion vs self-exclusion) of the kind that prevailed at least since 2004. This conflict may attain various degrees of intensity, depending on contingent events of such kind as eg the Litvinenko case or Russia’s pullout from the CFE Treaty, but the overall pattern of relations is bound to be marked by a radical incompatibility of the positions of the two parties. In such a scenario, we may expect the introduction by Russia of additional legal and political obstacles to the EU’s involvement in its affairs and the gradual limitation of the domain of EU-Russian cooperation to politically neutral issues, from research and education to energy policy. Indeed, despite the currently fashionable focus on energy policy as the key to the entire field of EU-Russian relations, we must insist on its rather limited role in influencing the overall course of EU-Russian relations. Against the exaggerated fears of Europe’s dependence on Russia’s energy exports, we need only recall that the extent of the dependence is relatively comparable to the situation in the 1970s–early 1980s, which hardly translated into exaggerated fears of Europe’s dependence on Russia’s energy exports, we need only recall that the extent of the dependence.

6. In contrast, the second scenario that consists in the EU’s reciprocation of Russia’s self-exclusive gesture would entail the recognition by the EU of the existence of clear limits to further integration with Russia and thus of Russia’s legitimate difference from Europe in sociopolitical terms. This pattern of development that may be termed “mutual delimitation” is also conditioned by the abandonment of the ideal of Russia’s “integration into Europe”, whose unchallenged status was mentioned above. Opting for this pattern requires a frank admission that in the last decade Russia moved further away from (rather than closer to) Europe and its political system is ever more divergent from the normative standards operative in the today’s EU. At the same time as Russia must renounce its perennial ambition to “enter Europe”, the EU must logically renounce its ambitions to govern the postcommunist transformation in Russia, which is no longer driven by the European ideal and should not be expected to be modelled on the European experience. In this manner, the two parties would bring their grand policy rhetoric in line with the actual state of their relations, thereby bridging the gap that was easily noticeable since the early 1990s.

7. However modest or pessimistic this scenario appears at first glance, it is arguably a more fruitful line of development than the maintenance of the current conflictual impasse in EU-Russian relations, particularly insofar as it would permit a long-overdue revaluation of the EU’s record in promoting democratization in Russia. Without buying into Russia’s defensive rhetoric about the “double standards” employed by the EU in its criticism of Russia’s turn towards authoritarianism, it must be emphasized that the EU has been complicit in this very turn by means of its systematic prioritisation of liberal market reforms over democracy in postcommunist Russia since 1991 onwards. In late 1991 European states wholeheartedly supported President Yeltsin’s recourse to rule by decree in order to push through the programme of neoliberal socioeconomic reforms bypassing the Congress of People’s Deputies. In 1993 Yeltsin’s unconstitutional dissolution of the Congress and the violent suppression of the ensuing popular rebellion similarly encountered Europe’s support. Similarly, the introduction of the new Constitution in December 1993 that granted extraordinary powers to the President, was received as the progressive step along the pathway to democracy. In 1996 the EU endorsed Yeltsin’s candidacy and recognized his victory in presidential elections that were marked by the blatant abuse of office by government officials and unprecedented smear campaigns against Yeltsin’s rival, the Communist Party chairman Gennady Zyuganov. The irrational fear of the Communist revanche in Russia has arguably also motivated the positive European reception of Vladimir Putin as Yeltsin’s successor in 1999.

8. Although the European assessment of the Putin administration grew more critical during the present decade, we must not forget the unequivocally positive assessment of Putin’s liberal economic reforms by the EU, reflected eg in the Tacis Indicative Programme 2000–03 and the National Indicative Programme for Russia 2004 – 06, which were explicitly oriented towards the support of the governmental reform initiatives. And yet,
the reason why these reforms, planned as early as Yeltsin’s first term, were able to be implemented, is the very system of “sovereign democracy” that the EU presently accuses the Russian state of. Indeed, the present assault on the democratic freedoms gained during the late 1980s is frequently presented by the regime’s apologists as the necessary condition for advancing liberal market reforms, stalled during the 1990s by the parliamentary opposition and popular protests, ie by democratic resistance. The contraction of the democratic space in Russia is thus the regime’s solution to the problem of the non-coincidence between liberalism and democracy, the goals of market reforms and the will of the people—a problem that the EU has utterly ignored in its dealings with postcommunist Russia. Putin’s sovereign democracy is nothing other than the most appropriate institutional form for the liberal market reforms, long promoted by the EU and regularly rejected by the Russian voters in relatively free elections. The priority granted by Europe to market reforms over substantive democracy has eventually led both to the destruction of the democratic space, which flourished briefly during Gorbachev’s Perestroika policy, and the perverse mutation of liberal capitalism into a rent-seeking bureaucratic oligarchy with little developmental potential. In this sense, the EU’s assistance to postcommunist transformation in Russia has been a dramatic failure in that it did not achieve the consolidation of either democracy or the market economy in its modern European image. The lesson to be learned from the experience of Russian postcommunism is that a policy that gives precedence to market liberalism over democracy risks sacrificing both.

9. From this perspective, the abandonment of the EU’s policy of “promoting democracy” in Russia might turn out to be a blessing in disguise. Rather than provide a veneer of legitimacy for the Putinite project of “authoritarian modernisation”, the EU’s self-exclusion from further integration with the Russian state must be accompanied by a long-overdue engagement with the wider array of societal actors than the dwindling group of discredited “pro-market reformers”. Unfortunately, since the early 1990s Russia has been paradoxically present in Europe “through its representatives’, be it the political elite or the adventurous tycoons, while contemporary Russian cultural actors, professional associations or non-governmental organizations are barely known in Europe. By the same token, for the majority of the Russian society Europe, with its culture, norms and practices, remains almost as distant as it was during the Soviet period. The future development of Russian-European relations depends on the possibility to discriminate between the Russian society and the existing regime of bureaucratic oligarchy, so that any gesture of dissociation from the latter is accompanied by the active engagement with those societal forces that defend substantive democracy against its “sovereign” expropriation. Insofar as democracy is not a form of state but above all a societal ethos, such a policy is far more likely to succeed in the necessarily long-term project of democratisation than the present deadlock in EU – Russian relations that can no longer be concealed by the rhetoric of “partnership and cooperation”.

September 2007

Memorandum by Mr Pekka Sutela, Head of the Bank of Finland Institute for Economics in Transition (BOFIT)

Reciprocity in EU-Russia Relations

Opinions expressed are those of the author and should not be construed as reflecting the views of the Bank of Finland, Eurosystem or other authorities.

Evidence prepared for the Sub-Committee on Foreign Affairs, Defence and Development Policy of the House of Lords Select Committee on the European Union

The EU has a neighbour, which with a share of aggregate outside trade of just a couple of percentage points is relatively unimportant as a trade partner, especially as far as EU exports are involved. But this country is a key producer of an imported commodity, without which trains would not run, airplanes would not fly, and our every-day life would be highly problematic. The neighbour, naturally, is Switzerland, and the commodity imported to the EU is watches.

There are two reasons why we regard import dependence on Russia and energy, particularly gas, as being hugely more important and problematic than our dependence on Swiss watches. First, Swiss watch production can be easily substituted by either importing watches from other sources like Japan or by establishing sufficiently large-scale production within EU. Quality might not be the same and the brands not quite as prestigious, but workable enough alternatives to Swiss watches would be available at a reasonable cost. Though the need for and availability of energy are not given magnitudes, and there are major substitution possibilities between different energy commodities, there are major sunk costs and economies of scale involved. They make substituting Russian gas with—say—Italian wind-power quite difficult. Second, Swiss watches are produced by a number of private companies quite independent from any political goals the Swiss
authorities might have. Situation concerning hydrocarbons is completely different. Globally, a very major majority of oil resources is controlled either by states or by state-controlled companies. All major exporters of gas to the EU are government-controlled national monopolies. Political and strategic considerations are bound to have a role in their decision-making.

There is a third factor of relevance, distinguishing government-controlled companies in an authoritarian capitalist system like Russia from those in a liberal capitalist country like Norway. The political goal of a liberal capitalist state like Norway is basically very simple: to enhance the welfare of the Norwegians. Though the planning horizon might be longer, this does not differ substantially from the decision making rule of a privately owned company: maximize the owners’ wealth. Therefore, the existence of this political mandate does not make the behaviour of the Norwegian gas producer any less simple, transparent and understandable than it would be without any such political ownership. The goals of an authoritarian capitalist state like Russia are inherently more complex and more poorly understood. This is partially because the whole phenomenon of authoritarian capitalism is not that old, and it is not understood whether the system is feasible in a stable manner and over a longer period of time. The previous possible examples in Germany and Southern Europe decades ago came to an end for a number of basically non-economic reasons, and modern China and Russia differ from them in many aspects. In fact, even the comparison seems hardly founded. Also, authoritarianism as such implies missing or severely limited accountability and gives more room for personalised decision-making, where aspirations may have a variety of motivations. Property rights tend to be badly defined in authoritarian capitalism. This is even more so when the state in question should be seen as a revisionist one in international relations, as may increasingly be the case with Russia. This does not only concern the rights and obligations of foreign companies operating inside these countries, but also the foreign operations of companies based in these countries.

Thus, appetizing as the comparison is, Russian energy is not exactly like Swiss watches. Still, both are basically commodities, and recognizing this, the burden of proof should always be on the one wanting to subject their markets under political decision-making. True enough, increased governmental control over hydrocarbons globally and ensuing energy nationalism are among the major recent shifts in the world economy, but still it is rather less than self-evident that consumers should react to such changes by further increasing the degree of political control of their related markets.

The least that should be expected from Europe is a clear decision on whether we should regard energy carriers as economic or political commodities. As the previous discussions hints, both conclusions can be argued for, but perhaps the EU remains too diverse to be able to make the choice. In addition to more general differences in the existing European variants of liberal capitalism, reflected in matters like attitudes to competition and national champions, EU countries differ widely in existing energy endowments, past investment decisions with their usually very large sunk costs and political orientations concerning the desired future energy mixes. This limits what the calls for common energy policy and speaking with one voice to outsiders might possibly mean in practice. There are a number of layers involved. While some unification of the rules of the energy game as well as interconnecting of previously disjointed domestic markets are feasible and probably should be aimed at, going much further may be both infeasible and also undesirable for other reasons. No European energy policy could convince a number of member nations that going nuclear is one way to the future. Other nations abhor the idea of using more natural gas. Trade policy is in the competence of the Commission, but this is sometimes difficult to detect in the case of trade for energy commodities, partially because so many other dimensions are involved too in decisions on energy. If, as some put it bluntly, the idea were to establish a buyers’ cartel of—say—gas, a simple question arises. What might be the implementation mechanism of such a cartel? In a simple Mafia-type cartel it is four men with guns in a black car. In the case of OPEC, it is something much more complicated and civilized. Nobody has come up with proposals, what the implementation mechanism might be in a European gas buyers’ cartel.

Reciprocity is perhaps the key term in trade policy: concessions in—say—market access should only be granted when the other side also grants similar or comparable advantages. Economists have traditionally had their problems with the concept. One saying, attributed to Joan Robinson, the late Cambridge economist, asks whether you should start throwing stones in your harbour when you see your neighbour doing just that. More often than not, maintaining a trade barrier hinders welfare in the country doing that. If your neighbour starts shooting in her leg, there should be no rational need to emulate that.

Take the example of the gas production chain. Clearly, Russia is hurting itself by limiting as a matter of principle the role of foreign investment in upstream production. It is true that in an energy nationalist world international companies may have no other choice than to accept a role as minority share-holder, co-operator or technology provider, but by limiting as a matter of political principle the set of possible co-operation modes the Russian authorities are beyond any debate, intentionally or not, hurting national welfare. Much technology is available from the shelf, but some should always have suitable incentives to be developed. In the
case of Russia, less than full access to foreign managerial and especially project management skills may well prove the key loss incurred. Making decisions leading to suboptimal behaviour hurts the national interest.

To a degree at least that seems to be understood in Russia. Reflecting their basic differences as liberal and authoritarian capitalisms, there is a clear tendency for the EU and Russia to understand reciprocity in energy matters in divergent ways. For the EU, the more market-oriented partner, it is primarily a matter of commonly agreed access to markets and investments. After rules have been established, let the best competitor win. For Russia, the more state-oriented partner, it is primarily a matter of asset swaps assumedly of similar value. But on the other hand, Total, the French energy company, was given a limited minority role in developing the Shtokman gas field without a Russian company being given some similar access to French markets—not at the same time at least. It remains to be seen whether such access will be enough to facilitate the opening of this huge but very difficult field in anything like the schedules frequently mentioned in the public.

Though it should not be elevated to a matter of black-and-white principles, the just-mentioned basic dissimilarity in interpreting reciprocity remains and will be difficult to overcome, as long as these variants of capitalism continue to diverge in important ways.

Let us continue our practical experience. Should the EU limit Russian access to downstream gas investment by applying one or another interpretation of the principle of reciprocity? The economist’s first answer would be in the negative. If a Russian company is able to make a higher bid, believing that it will be a better operator of a distribution network, it should be allowed to do so. This is so for a number of reasons. It is, first of all, the general rule that the highest bid wins. If a Russian company promises superior performance, it should be given the opportunity to prove that it can deliver. If the attempt consequently fails, the field is open for someone to make a new bid, now for the Russian-owned assets. If the owner acts by general market-based rules, this will take place.

But is the assumption of acting by the rules justified? Before addressing that, let us note that there is also an important wider argument involved. Dmitri Trenin has argued that there are two major Russian social forces for a better society. The first one is the ongoing strengthening of the new middle class. They demand more choice for their money, and therefore drive the modernisation, diversification and opening up of the economy. Perhaps, one might caricature, they—having turned from Soviet subjects to Russian consumers—might one day even turn a new leaf in Russian history by evolving further, into citizens. The other social force is the internationalisation of Russian business. Indeed, it is a peculiar sign of European lack of assertiveness to think as many seem to do that this will rather lead to a Russification of Europe than to a Europeanisation of Russian business.

Still, the economist’s logic fails to convince most ordinary citizens and seemingly also many decision-makers in the EU. Part of the explanation is in the remarkable surviving power of elementary Mercantilist thought. But there are other explanations as well. First, while there is little doubt that Russia would benefit from a more benign foreign investment regime, there does not seem to be much reason to think that Russian producers could actually bring more value into running gas distribution networks or service station chains in the EU area. Others have been practising those skills much longer. So why should the Russian companies make higher bids? Are they overly optimist, burdened with excess cash—or motivated by ulterior aims? That is what the EU citizen is asking.

Second, indeed there is the point made earlier about the unclear character of decision-making rules under authoritarian capitalism. Perhaps the ultimate Russian producer, after having thrown stones in his own harbour, starts doing that in other harbours as well. That—running assets in an economically suboptimal way—would hurt his business interests, but perhaps they do not reign supreme. As pointed out earlier, property rights are unclear under authoritarian capitalism. Therefore, so are decision rules. Decisions like going downstream along the gas production chain, closer to the consumer, make as such eminent business sense. So does the decision to introduce reasonable prices for exported gas—a measure that should also be defended on the grounds of economic efficiency and ecological sustainability. But with unclear property rights and decision rules, suspicions of ulterior motives will always remain.

If a demand for reciprocity along the gas production chain looks asymmetrical, there are other, more complicated examples. What might, for instance, a demand for reciprocity in access to real estate mean, when both the demand and availability of sea-shore properties along the Mediterranean is hugely greater than that along the Black Sea? Or, for that matter, reciprocity in entry to universities?

The September 2007 EU Commission Communication on energy policy has been widely discussed, and rightly so. From the Russian point of view, the premise of granting similar positions to EU and third country companies should be welcomed, not seen as evidence of increased protectionism. It is a different matter that the proposed ownership unbundling principle is not politically feasible, for internal EU reasons. The same is very probably true of the offered derogation, the Independent System Operator. Therefore, this particular
1. Strategic Energy Partnership: In October 2000, the European Union (EU) and Russia have initiated an “energy partnership” to discuss all questions of common interest relating to their energy sectors and mutual energy cooperation. Both sides have declared themselves as “natural partners” in the energy sector. Until 2006, for the EU, Russia had been a reliable energy partner for many years, even during the Cold War and periods of internal difficulties. The overall objective of the energy partnership aims to:

- enhance the European energy security by binding Russia and the EU into a closer economic-political relationship due to long-term nature of investments in energy production and transport;
- open and integrate energy markets on both sides, reflecting the “strong mutual dependency and common interest in the energy sector”; and
- “to improve the investment opportunities in Russia’s energy sector in order to upgrade and expand the energy production and transportation infrastructure as well as improve their environmental impact, to encourage the ongoing opening up of energy markets, to facilitate the market penetration of more environmentally friendly technologies and energy resources, and to promote energy efficiency and energy savings”.

2. In many ways, Russia seems to be the natural energy partner for the EU: It holds the world’s largest natural gas reserves (48 trillion cubic meter), the second largest coal reserves, the eighth largest oil reserves, and being already the world’s largest exporter of natural gas, the second largest oil exporter (only behind Saudi Arabia) and the third largest energy consumer. At present, Gazprom alone supplies almost 25% of the EU’s natural gas needs, and the EU buy’s 70% of Russia’s oil and gas exports. For modernising and expanding its energy sector, Russia needs more than $900 billion by the year 2020. In this respect, the EU appears as the perfect modernisation partner of Russia. The supposed mutual interdependence on energy, trade and investments has been seen as the major strategic factor of the EU relations with Russia. This strong mutual interest and interdependence suggest that energy is an ideal sector in which relations can be progressed significantly—a kind of test case—for the further development of an EU-Russia strategic partnership. Success in the energy sector could then serve as a model for other areas of common interest.

3. Given the political instabilities in the Middle East, the natural solution for Germany and the rest of the EU seems to be to expand imports of oil and particularly natural gas from Russia for satisfying its rapidly growing gas (import) demand. At first glance, there are indeed a number of persuasive reasons (not least the argument of improved political stability) for a drastic escalation of energy imports from Russia, being the EU’s fifth largest trading partner (after the US, Switzerland, China and Japan). However, the results of the “Thematic Groups of the Energy Dialogue” and the newly created “EU-Russia Permanent Partnership Council (PPC)” on Energy in December 2006 to address energy strategies, forecasts and scenarios and other cooperation issues have been limited and rather disappointing due to different strategic interests on both sides and Russia’s renationalization policies of its energy sector. Furthermore, Russian energy export policies, in particular pipeline routes (which are often determined by geopolitical considerations rather than just an economic calculus), are still seen in the Kreml not just as an tool of its economic/energy policies but also as one of its very few effective foreign policy instruments to preserve and maintain its “strategic interests” in neighbouring countries which are either highly dependent on Russian energy sources or function as important transit states. In this light, the EU has been unsuccessful in persuading Russia to pursue a market-oriented energy policy or in aligning the “EU-Russian energy partnership” with market principles.

4. Russian-Ukrainian Gas Conflict of January 2006: The energy conflict between Moscow and Kiev, importing a third of its energy from Russia, has shown that the Russian government and President Vladimir Putin are prepared not only to use its energy to force customers to pay much higher prices almost over night, but also as a foreign policy tool to pressure customers to concede to Moscow’s geopolitical interests. Ukraine’s “Orange Revolution” in December 2004 and the demise of the Kuchma government not only tore it out of Moscow’s
sphere of influence, but was also a personal setback for Russia’s President Vladimir Putin, who had backed in an unprecedented way the losing presidential candidate, Viktor Yanukovich. However, it provoked a national-democratic backlash in Ukraine that ended up strengthening Viktor Yushchenko and increasing international criticism at Putin’s foreign policy toward Ukraine. Shortly before the outbreak of the conflict, Gazprom took steps in order to ensure its leverage by blocking all other regional producers from providing Ukraine with alternative sources by buying up all of their production itself such as those of Turkmenistan. The intended gas conflict was also a new attempt by Putin to influence the forthcoming parliamentary elections in Ukraine in March 2006. As the Russian reformer and head of the liberal Yabloko party, Grigorii Yavlinskii criticised: “Right now, instead of helping Ukraine move along [toward Europe] and moving along with it, Russia is uselessly trying to prevent Ukraine from doing so, and is itself trying to pursue some sort of ‘third way’. In reality, there is no ‘third way’—there is only the Third World”.

5. Furthermore, Moscow was not so much interested at world market prices than to acquire the Ukrainian pipeline system—especially after Moscow took over the ownership of the Yamal-gas pipeline on the territory of Belarus in December 2005. Already before, Gazprom has tried to buy into the gas-distribution networks in Hungary and Poland to regenerate itself as a great power in Europe and beyond. It has also put immense pressure on the Georgian government to cede control over the gas pipelines that ship gas from Russia to Georgia and beyond to Armenia. However, Georgia and Ukraine have opposed any Russian ambitions to take over their pipeline system which would have severe consequences for their pro-Western foreign and security policies.

6. Renationalization of Russia’s Energy and Resource Sectors: Because economic circumstances have changed, the Russian government is now undermining production agreements (Sakhalin 1–2, Kovyktka) that were signed in a period of low energy prices in the early 1990’s, but its flaunting of contractual agreements will permanently scare off investors in the future. Thus Western investors are not permitted to hold more than 49% of Russian companies. This limitation is unlikely to dispel reservations or create an investment-friendly climate in Russia. In practice, western shareholders of Russian energy companies must content generally themselves with much smaller stakes.

7. Implications for the EU: The bilateral ties between European gas companies and Gazprom resemble very much like “cartel-like relations”, which tend not to be very transparent, and very protective of the market position of European importers of Russian energy resources. Until very recently, the EU and its member states have granted Gazprom access to the European downstream assets without opening the consumer markets in Europe as well as the production sector in Russia. But for the EU’s future energy security and liberalizing its energy (and particularly gas markets) it is highly important to guarantee fair competition rules and the reciprocal opening of the Russian energy markets in order to minimize the risk of downstream monopolization of Gazprom and other producers. On 19 July 2006, Putin has signed the new law “On Natural Gas Exports”, which has legalized the Russian gas export monopoly de jure. It has wide-ranging consequences for the EU because any effective downstream competition with a total legal monopoly on the supply end is hardly realistic.

8. Emerging Russian Gas Crisis: Russia’s reputation as a reliable EU energy partner is also undermined by the imminent threat of a dramatic gas shortfall—one that, until mid-2006, both Moscow and Gazprom’s European energy partners completely denied. Although Putin finally acknowledged this supply gap in domestic discussions in September 2006, he did not reveal its full scope or bring transparency to the issue, which is all-important for the European Union.

9. With over 47 billion cubic meters of natural gas reserves (26% of global reserves) but covering 50% of its own domestic energy demand, there are two main reasons for the Russian gas crisis: 1) the decline in output from the vast natural gas fields in the region of Nadym Pur Taz (NPT), and 2) an unwillingness on the part of the state energy giant Gazprom to make timely investments in developing new fields in Russia itself. Although Gazprom has adequate capital, it has failed to develop any major new fields apart from the gas deposits in Zapolyarnoye, which can mitigate the effects of the NPT decline only for a short time.

10. The Research Institute for the Economics of the Gas Industry (NIIGazekonomika), a Gazprom subsidiary, has recommended a dramatic change of strategy: Russia should decrease exports of natural gas to European markets and concentrate instead on developing new gas fields to keep up with domestic demand. The latter will rise up to 654 bcm per year instead of Russia’s Energy Strategy’s estimate of 436 bcm until 2020. Therewith, it has confirmed Western experts who have criticized the lack of investment into new gas fields and pipeline construction and maintenance as a growing threat to the EU’s gas consumption.

11. Gazprom’s and the Kremlin’s priorities are not the modernization of its gas sector or even customer satisfaction, but rather rent-seeking and the expansion of its monopoly power. During the last four years (2003–06), Gazprom has spent nearly 18 billion Euros on the acquisition of shares in companies outside the gas sector backed by the Kremlin’s strong support. This is more than had been invested in the development
of upstream gas production in a decade. As the result of failing investment in the exploration of new gas fields, confirmed by the IEA, a deficit of gas supplies is expected to Russia and Europe of 100 bcm per year in 2010 compared to actual demand. Already today, Russia is increasingly dependent on gas imports from Central Asia and the Caspian region (80 bcm) in order to satisfy domestic gas consumption and maintaining high-price exports to Europe.

12. Meanwhile, also Russian officials have confirmed the gas deficit. On 19 June 2007, the Deputy CEO of Gazprom, Alexander Ananenkov, indicated that the gas agreement with China of 2006 (delivering 80 bcm to China annually) could be given up because Russia needs the gas for its domestic markets as well as for maintaining its gas exports to Europe. On 2 August 2007, the Russian government demanded from the Sachalin-2 consortium to sell all gas to Gazprom and not directly to China, Japan and other Asian markets because of its increasing domestic gas consumption. In November 2007, the Russian Ministry for Economic Development and Trade warned that a gas deficit is emerging in 2010 which could constrain the domestic gas market.

13. Implications for the EU: Russia’s gas production is expected to rise from an estimated 608 bcm in 2003 to 655 bcm in 2010 and 898 bcm in 2030 (IEA in 2004). Net exports of gas are hoped to increase from 169 bcm in 2002 to 182 bcm in 2010 and 274 bcm in 2030. Even in the case that Russia may export as much as gas as originally expected in its Energy Strategy of 2003 (274 bcm in 2030) and would not diversify its gas exports to the Asian and US markets (LNG), it is totally insufficient in regard to the EU’s gas imports in 2030 (488 bcm), which can only be covered by gas imports from other countries and regions such as Norway, the Middle East, Central Asia/Caspian region and Africa. With other words: The EU is forced to diversify its gas imports. In this respect, the EU is in a very favoured position: Unlike any other region of the world, the EU is geographically surrounded by many gas-exporting countries within a range of 3,000–3,500 km, which can be connected by pipelines. However, most of them are considered as politically unstable.

14. Hope on Russia’s “independent” gas suppliers? Theoretically, these independent Russian gas producers could partially close the supply gap if the Russian domestic market were made more attractive by raising prices. Russia’s 2003 national energy strategy foresees independent companies covering roughly 20% of natural gas demand by 2020 (compared with 13% now). Based on its own projections, the IEA hopes that independent suppliers will account for 40% of the market in 2015-meaning deliveries of 260 to 290 bcm of natural gas. Even so, Novatek and TNK/BP are probably the only companies capable of making a substantial contribution. Reserve levels and available capital are already placing limits on gas-producing oil companies like Rosneft, which are also being lured by the prospect of greater profits in the oil business. This means that the more conservative approach in the 2003 national energy strategy, which envisions a contribution of 120 to 135 bcm, or perhaps even 150 bcm in 2015, seems probably more realistic. Moreover, the amount of gas contributed by independent players will depend on their capital resources and on formal guarantees by Gazprom that they will be able to utilize its network. At the moment, both are highly questionable since they undermine the vision of a vertically integrated energy behemoth controlled by the Kremlin. In the future, independent companies are likely to face even greater restrictions in accessing Gazprom’s network. The more quickly Gazprom depletes its own reserves, the more companies it will need to purchase to make up for its gas shortfall. In such a scenario, it is extremely doubtful that the weakened, once-independent companies taken over by Gazprom will be able to maintain their high production levels.

15. Furthermore, a full independence of these gas producers is also a political chimera because they always include other state-controlled companies such as Gazprom (in the case of Novatek) or Rosneft and they must sell their gas to Gazprom for exports since Gazprom has an exports monopoly. And they have to act in respect of the Kremlin’s declared strategic and geopolitical interests inside Russia and beyond. Ownership of the companies does not equal with real independence.

16. Rising EU-Competition with Russia towards Central Asia and the Caspian Region (CACR): Russia’s recent policies of a bilateralism with Hungary, Austria, Italy, Greece and Bulgaria are part of a larger strategy to undermine a common European policy toward Central Asia and in particular the Nabucco-pipeline project, which is of crucial importance for the EU’s energy security and the diversification of energy supply. Russian politicians and advisors to the Kremlin are very frank about their objections towards a direct pipeline between Central Asia and Central Europe. By circumventing Russian pipelines, the Nabucco project would result in a “loss of money and strategic influence” for Russia. From Moscow’s perspective this could potentially trigger “a geopolitical” and “energy crisis”. In that context, German and EU policy-makers are overlooking two important facts:

— Independent gas pipelines from the Caspian region to Central Europe would force Russia to invest in the exploration of new gas deposits in their own territory. This, in turn, would secure long-term Russian as well as European gas supply.
The Russian focus on gas imports from Central Asia has geopolitical reasons and contributes to the “gas crisis” in Russia. Moscow has thus become a less reliable energy supplier for Europe.

17. The aftermath of the EU Spring summit of March 2007 has seen European energy companies, with the backing of their respective governments, intensify their relations with Moscow. In light of such bilateral energy deals, the European Council conclusions run the risk of becoming political lip service. The construction of the Nabucco-Pipeline needs to be supported more decisively by Germany and the EU. The United States’ policy to secure the Baku-Ceyhan and Baku-Erzurum pipelines should be seen as a model in this regard. Otherwise, Russia will be able to successfully undermine the EU’s options to diversify its gas imports even before the first steps of a common external energy policy can be implemented. From a strategic viewpoint this situation is unacceptable for the EU. But short-sighted national special interests are threatening a unified approach to the EU’s external energy policy.

18. Mutual and Symmetric Interdependency between EU and Russia: the argument that pipelines make suppliers and buyers fundamentally dependent on one another is overlooking the following facts at least at the short-term perspective:

— It is only true as long as both sides do not have and do not seek access to alternative markets.
— Both sides must recognise the economic-political interdependence and guide accordingly their strategies and policies. However, that interdependence is not fully been accepted on the Russian side. They deliberately ignore Russia’s corresponding dependency on Europe as a market for Russian gas. In political reality, the EU-Russian relationship can be rather characterised as an “asymmetric interdependency”.
— Russian foreign and security experts have speculated—to some extent rightly—that EU politicians and industrial decision-makers tend to a policy of anticipatory kowtows towards Moscow (“silence for gas”). As the Representative of the EU’s Common Foreign and Security Policies (CFSP), Mr Javier Solana, has warned on 20 November 2006: “We may have to deal increasingly with governments whose interests are different from our own and who do not necessarily share our values. Sitting on huge reserves of oil and gas gives some difficult regimes a trump card. They can use energy revenues for purposes which we may find problematic. And it shields them from external pressure. Thus, our energy needs may well limit our ability to push wider foreign policy objectives, not least in the area of conflict resolution, human rights and good governance”.
— There is a major difference to the situation of the Cold War when Russia proved to be a reliable energy partner: During that days, Russian gas exports to Western Europe were seen in Moscow primarily as an economic tool to earn much-needed hard currency for the USSR as a declining economic and military super power. Today, Putin and his followers are seeing Russian oil and particularly gas exports to the EU-27 not just as a very important economic tool but also as a foreign policy instrument that demands respect for Russian geopolitical interests and ambitions—particularly in Europe and Eurasia.

19. Conclusions and Perspectives: Given the EU’s rising oil and in particular gas (import) demand and its geographical vicinity to Russia, there is no real alternative to a long-term engagement policy towards Russia. The lack of congruence in the EU energy foreign policies towards Russia, however, made it easy for Moscow to “divide and rule” the Union and to enforce the “bilateralisation” of its energy political cooperation with the individual EU member states and their national energy champions.

20. For the EU-member states, a conflict of goals has occurred: The EU’s energy foreign policy will either further complicate EU-Russia’s relations, or given the EU’s consideration of Russia’s energy and security interests, put into question the Central Asia and diversification strategy of oil and gas imports from CACR. However, the EU cannot forego diversifying its imports of natural gas from CACR because (1) the Kremlin is exploiting energy dependencies as means of foreign policy, and (2) Russia solely cannot meet the forecasted EU’s natural gas demand until 2030, if their need does not mitigate. Furthermore, in the light of the EU’s foreign and security interests, it has no alternative than to extend and to deepen its relations with CACR.

21. Putin’s energy foreign policy is in bold contradiction to both the EU-policy of liberalizing the European gas- and energy markets, its neighborhood policy and CFSP. A more long-term energy cooperation with Russia implies a more concrete definition of EU’s own strategic interests in its energy foreign policies, which, however, should not be exhausted in a “Russia first”-policy. Hence, the EU’s strategy should both aim at an energy partnership with Moscow being equally entitled, and be dedicated to a distinct reciprocity in the opening of energy markets on each side.

20 December 2007
The European Union and Russia: Evidence

Memorandum by Sir Andrew Wood GCMG

1. Sub-Committee C of the House of Lords Select Committee on the European Union has called for evidence for its inquiry subsequent to its 2002 report on “EU Russia Relations”. I submit what follows on a personal basis.

2. The EU Russia relationship is for now both as important in principle and difficult to define in practice as it was in 2002. If that remains the case it will be hard to move meaningfully beyond the generalities of the existing Partnership and Cooperation Agreement (PCA) of 1997, despite the fact that both parties argue for the necessity of doing so. There are immediate practical obstacles: the Russian electoral cycle and its possible outcomes; foreign policy differences coupled with the probability that Russia will not soon enter the WTO; and differences of approach among EU member states. These three reflect the absence of clear Russian or EU strategies to inform an effectively renewed and structured relationship between the EU and Russia.

3. Both parties indeed have, as the Sub-Committee’s Call for Evidence put it, “a shared interest in maintaining good relations on a wide variety of commercial, economic and international issues”. Nor would I question the assertion in the Call that the dialogue between the EU and Russia has broadened, at least in the sense that there are now more questions on the table than were evident in 2002, and more established machinery to address them. There is however room for debate as to what we now have can be described, except out of diplomatic politeness, as a dialogue between partners (which for me implies a mutual sense of common purpose based on trust in the general idea that one good turn will secure another in return) or that our exchanges have deepened. Recently, we seem instead to have talked past each other.

Russian Politics

4. I suggested during the oral evidence I gave to the sub-Committee in 2002 that the evolution of democracy (as understood in EU countries) in Russia would prove a critical factor in the relationship between the Union and Moscow.Russia has since then moved further towards a centralised, even personalised, system, with a greatly increased role for the state in the economy. In consequence Russia is now in the midst of a succession crisis. Russia’s focus is internal and its foreign policy attitudes populist rather than dispassionate. Russia is not the only country to act that way, and has the trauma of its last decades to confront too. But it makes healthy and sustainable progress in the EU Russia relationship problematic for now.

5. It will be some time before that changes, even once the electoral cycle is over. Personalities will count, but since no one knows who will have what position come next Spring, the amusement of speculation about people is hardly now worth the ink spilled on it. The only safe predictions are that March 2008 will not bring closure, and that the next Administration will have problems in its inheritance whose resolution will over time make it differ from what we have recently seen in Russia. President Putin has said repeatedly that he will not stand again. He has also said that he will remain a force in Russian politics. That will add to the need for the next President to establish his own independent and in the end superior authority. If the next President is seen merely as the creature of his predecessor, then whatever the position Putin may hold after March 2008 the effect will be to increase still more the dependence of the system on his personal dominance while diminishing his accountability and further undermining Russia’s institutional structure. That is not a mixture fit to last through a full Presidential term with what is likely to prove a complex agenda to address, or to encourage a consistent Russian approach to the EU.

The Economy

6. President Putin has had world economic winds at his back during his two terms, and a team to deliver admirably responsible budget policies. Pressures to spend accumulated surpluses have however grown, and may well increase further over the electoral cycle, including as a new administration finds its way. Russia’s budgetary and balance of payments surpluses are already shrinking, with the latter expected to disappear perhaps as early as next year. The demands of state or state related corporations make up a large proportion of the rising inflow of private borrowing. These trends and a degree of protectionism are set to persist beyond the elections.

7. Russia needs heavier investment than it has so far managed to achieve. Russia’s dependence on a high, even increasing, oil price has not lessened. Diversification, and the renewal of the country’s capital stock, including its housing and transport infrastructure, is becoming more, not less, pressing. The recently drafted
Development Programme, which covers the period until 2020 looks to combine a significant growth of government intervention in the economy with an innovation led scenario to underpin annual growth rates of over 6%. This will be a lot for the Russian bureaucracy to secure, as indeed it would for any government machine. Experience so far is against such ideas leading to less corruption and a more diversified economy. There is a long term logic which points to closer integration between the Russian and EU economies, but also a persistent Russian tradition of fighting mutual dependence.

ENERGY

8. This tension is evident in the energy sector, which the next President will no doubt continue to see as “strategic” and therefore best kept in national hands. The Russian state will find it hard to manage:

- domestic energy demand is increasing at present at around 5% each year. Available data show that Russian oil and gas production has not and will not keep pace with that demand, as well as meeting increasing commitments to Western customers. Investment in new fields has lagged, and cannot now be brought into effective production in good time. Difficult and very expensive decisions will be needed to ensure that the resulting strains are not prolonged, and that competing priorities are satisfied;
- Russia already depends on Central Asian gas, and will do so increasingly. Despite strong pressures on these countries that may not be easy to secure;
- effective use of non-Gazprom Russian gas, will be needed too, and will be easier said than done. It would call for bankable understandings between the independents and Gazprom which would conflict with that company’s monopolistic practices (or an inefficient extension of Gazprom’s reach). Using independents’ gas would also call for heavy investment in processing; and
- in pipelines. Existing ones badly need attention, including the network linking Russia and Central Asia. Construction capacity constraints are likely to prove as real as financial limits.

FOREIGN POLICY

9. For EU countries therefore Russian energy supplies may well get tighter, and the need for clear thinking about why that may be so all the more pressing. The temptation to ascribe difficulties to Muscovite bullying could, and maybe should, be made worse by Russia’s apparently settled and heavily pressed policies of seeking control over the gas pipelines in the transit countries, not least Ukraine. The EU, and its member countries, are likely to continue for some time to have to make their choices against the background of increased suspicion inside Russia of Western motives, and outside it, of Russian behaviour. Untangling that will be hard without some understanding of Russian ideas, which are by no means limited to those at present in power.

10. Difficult as it may be for us to credit, many Russians feel themselves to have been cheated by the West. The argument goes that Moscow gave up its international power and got nothing in return. That argument feeds on a tradition of xenophobia mingled with self-pity, now compensated for by the idea that “Russia is back”. President Putin is not the first to say that the weak are always beaten. The corollary is the conviction that Russia needs to show strength, and surround herself with dependable, even controllable, allies. For those in power, and very probably for their immediate successors, this attitude is reinforced by fear of popular pressure on similarly organised governments within the Kremlin’s neighbourhood. But the ambition to restore Russia’s position as a Great Power is not a policy that resonates in Europe today, and its meaning is fuzzy. It can also make it more difficult to achieve some of Russia’s objectives by heightening outside suspicions, and clouding the country’s negotiating stance. WTO entry is a good example. The Russians have often seen this as a political matter, with their exclusion being politically motivated. They have therefore approached it much as they successfully did the G7 now G8. But as Pascal Lamy pointed out on 28 September, entry is not free. It entails opening the market and adopting WTO rules, with legislation to back it up. Given that the end 2007 date seems now out of reach, and that entry next year too may not happen, we have a row waiting to happen, including in all probability with the EU—and of course a further brake on a renewed PCA, or progress on the Common Spaces.

CONCLUSIONS FOR THE EUROPEAN UNION

11. Calls for action are more attractive than steady as she goes. But what the EU needs now is patience and confidence, while Russia evolves. Russia may be demanding in pressing for EU concessions, and loud in its complaints against EU reluctance to accept state funded investment, but is for now neither much inclined nor well placed for meaningful negotiations with the EU over what the Union might see as substantive advance
on present formulae set out in the PCA, the rhetoric of the “Common Spaces” and still less the Energy Charter. Moscow will continue to look for room in the tension between the approaches of individual member states and the EU as a whole (and who can blame it?), and will as seems good to it lump the Union, NATO and the US together. The EU does not have to take them over seriously when they do. Existing EU programmes (Question 4 of the Call for Evidence) are not likely in the foreseeable to secure more traction than they now have, which is so far as I can tell limited. But the help they can give to individuals, together with their symbolic value, has merit.

12. EU countries should continue to tighten (Question 8) their mutual understanding of how Russia may develop, what that would mean for its policies towards the Union and Russia’s neighbours, and what the Union’s long term view of the relationship may be. This is not to say that there should or could be unanimity of view, but greater coherence would reduce the scope for Russian misunderstanding, and experience suggests that when the EU speaks with one voice as it did after the Orange events it gets attention. The EU will always carry more weight in Moscow if it is seen to be taking US policies into account, which does not of course always mean agreeing with them. Reaching agreement on effective EU energy policies, and paying proper attention to Turkey’s critical role as a candidate and energy transit country are important in their own right and in the context of managing the EU Russia relationship. We should treat Ukraine’s EU ambitions with sympathy. EU interests (Question 9) in ex-Soviet countries have some commonality with Russia’s and we should of course look for ways to work together in resolving frozen conflicts, if only as a way of putting across a view and establishing our right to hold one. But the fact is that EU ambitions to underpin the independence, including the energy independence, of these states run counter to Russian efforts.

13. I have not tried to take the EU’s further governance agenda into account in this survey. I doubt if the Russians have given it much thought, and its exact future shape is uncertain.

12 October 2007