

## Russia-Ukraine gas talks head for crunch

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MOSCOW: Ukraine is being squeezed from two sides as it tries to renegotiate a gas supply agreement with its former master, Moscow, and advance towards a free trade deal with the EU.

Russia makes no secret of the fact that it would like more influence over Ukraine's energy infrastructure, while the European Union objects to a trial that bolsters Ukraine's negotiating position with Russia in the gas dispute.

Realistically, Ukrainian President Viktor Yanukovich is unlikely either to sell Ukraine's prize asset to Moscow or abandon the trial of his political arch-rival, former prime minister Yulia Tymoshenko.

But EU diplomats discern a possible outcome that gives Russia at least some stake in Ukraine's infrastructure, and endeavours to keep its EU project on track with a reform that makes Ukraine's state oil company, Naftogaz, more transparent and accountable.

The ex-Soviet republic has a tortured gas relationship with Russia. A pricing row between the two powers in 2009 which the controversial deal ended hit supplies to households in some EU countries.

Ukraine's territory offers transit passage for 80 percent of Russian gas supplies to Europe, but its own economy particularly key exporting sectors like metals and chemicals is heavily reliant on Russian gas imports too.

It wants Moscow to free it from a 10-year deal, brokered by Tymoshenko in 2009, which it says saddled it with too high a price for Russian gas and obliges it to import volumes that often exceed its requirements.

But Russian President Dmitry Medvedev says a new deal is possible only if Ukraine joins a Russian-led customs union, an offer that Kiev has declined since it is incompatible with its policy of joining a free trade zone with the EU. He restated his position in forthright fashion on Saturday.

Russian Prime Minister Vladimir Putin, pushing a project that he sprang on Kiev last year, says a review of the gas contract is possible only if Ukraine agrees to merge Naftogaz with the Russian gas exporter Gazprom a move also at odds with Ukraine's hopes for a trade deal with the EU.

“The question is not really about the price of gas, but politics. Russia simply is using the gas contract to achieve its political ends bring Ukraine into its zone of

influence, drag us into the Customs Union,” said analyst Volodymyr Olemchenko.

Kiev is threatening to appeal to an arbitration court in Stockholm to try to overturn the 2009 deal, but even the Ukrainians themselves do not seem to be setting much store by this tactic.

Speaking in Moscow on Monday, Foreign Minister Kostyantyn Gryshchenko remarked drily: “As to the Stockholm arbitration, there is one group of people who are always interested in court action lawyers.”

“We shall probably do everything possible to make their life easier and find a natural decision in the bilateral format.”

EU criticism of Yanukovich over the trial of Tymoshenko, voiced at a meeting of EU foreign ministers on Saturday, was an unwelcome tug of the rope from the other side.

If the “show trial” was not halted, a key agreement on closer ties between Ukraine and the EU could be blocked, they said.

Tymoshenko is charged with railroading Naftogaz into signing an unfavourable deal. The West has denounced her trial for abuse of office as a vendetta by Yanukovich.

But commentators say that abandoning the Tymoshenko trial now is not something the Ukrainians can easily do.

Showing the 2009 deal to have been flawed, or incorrectly put together, is part and parcel of their case for the agreement to be revised.

Though the Ukrainians have given away few details about their negotiating position, the future of Naftogaz is an important bargaining chip in talks with the Russians, Western diplomats say.

Kiev, keen to increase economic integration with the European mainstream, appears to be sticking by a commitment to the EU to restructure Naftogaz to meet European standards. The plan is for it to be reshaped into individual companies covering trade, exploration and transport.

This would almost certainly put its 1,000-km gas pipeline network definitively beyond Moscow’s reach and thwart Putin’s call for Naftogaz to merge with Gazprom.

Ukrainian Prime Minister Mykola Azarov said on Friday that this could be the moment when the gas agreement could be reviewed.

This is not a view shared, though, by Moscow, which senses that the Ukrainians will try to use a radical restructuring of Naftogaz to bolster their case for revising the 2009 gas deal.

Many diplomats believe that Ukraine may be offering Moscow some lucrative involvement in parts of the restructuring that, in the end, it will be difficult to refuse.

“The Ukrainians may be saying: ‘OK. Either we go ahead with restructuring Naftogaz and you lose control of the pipeline or you give us a discount and we will let you into another financially advantageous part of the restructuring.’ This could be the trump card,” said one EU diplomat.

The stakes are high for Ukraine, too, though both politically and economically.

In 2011, Ukraine envisages importing from Russia for its own use about 40 billion cubic metres (bcm) of gas at a cost of between \$264 per 1,000 cubic metres in the first quarter and \$400 per 1,000 cubic metres in the fourth quarter.

Ukrainian Energy Minister Yuri Boiko has asked to slash gas purchases to just 27 bcm next year, drawing a terse response from Gazprom chief Alexei Miller, who has said that Ukraine must buy 33 bcm under the ‘take or pay’ terms of their gas contract.

Ukraine now consumes about 60 bcm of gas annually the 20 bcm difference coming from local production.

At the same time, Ukraine faces losing a considerable amount of the \$3-4 billion it gets per year in transit revenue from Russia when the ‘Nord Stream’ project, which circumvents Ukraine and is due to launch this year.

Gazprom says the pipeline will eventually take 20 bcm of the Russian gas currently transiting Ukraine.