

Scramble for the Arctic Offshore Oil & Gas Resources in Russia

Nadezhda Filimonova

For several decades high prices of oil and gas have been a major driving force for Russia's economic growth and state prosperity. During this period the state mostly relied on natural resources production in West Siberia. Today the Russian economy is still very dependent on the energy sector, however the traditional areas of energy production cannot satisfy the demand any longer and the state is facing a challenge of finding a new energy supply area. Arctic offshore resources represent an alternative energy supply; however severe climate conditions, environmental risks and high production costs make offshore exploration less attractive. This article examines different approaches and interests of the Russian state and businesses towards the offshore exploration in the region. Convergences and divergences in the stances are discussed, providing an outline for the future development of the Russian energy sector with relation to the on-going international energy market development.

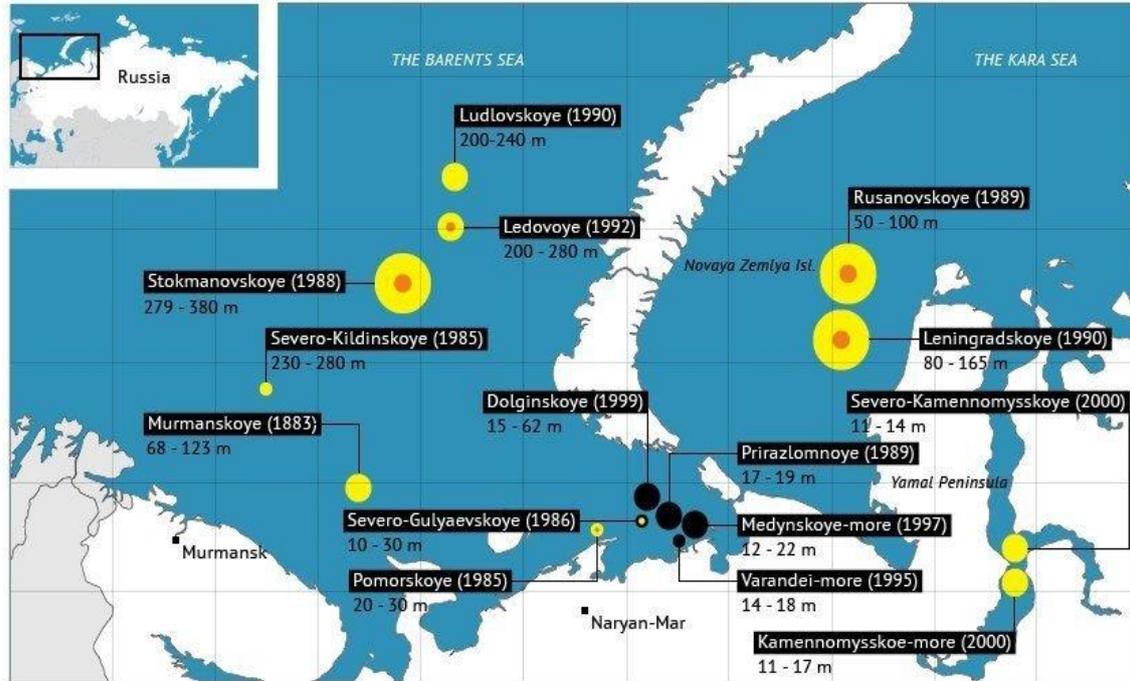
Background

For several decades high prices for oil and gas have been a major driving force in Russia's economic growth, making the country dependent on oil and gas exports and vulnerable to fluctuations in crude oil prices on the world market. From 1996-1998, up to 14-15% of the state's GDP revenues derived from hydrocarbons production and export; from 1999 – 2003 their share increased to more than 20% (Berezinskaya and Mironov, 2006), and in 2012 represented almost a half of the federal revenues (Neftegazovaya Rossiya, 2013). Starting from the 1960s a bulk of hydrocarbon production occurred in West Siberia. Today Khanty–Mansi Autonomous Okrug still accounts for 51% of oil production in Russia (Ria Novosti, 2012). Currently, the state's policy to preserve and expand energy production and exportation faces certain challenges. West Siberian fields are dwindling, and the oil production is predicted to decrease by 19% by 2020 (Kezik and Ermakova, 2012). In addition, geological surveys have been slow paced and modern energy production technology has not been fully introduced. According to “Russia Oil and Gas

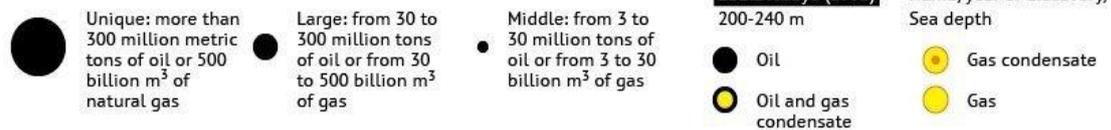
Report”, published in 2011, in the future, an increasing share of energy production will be produced outside of West Siberia (Business Monitor International, 2011).

Russian oil and gas fields in the Arctic

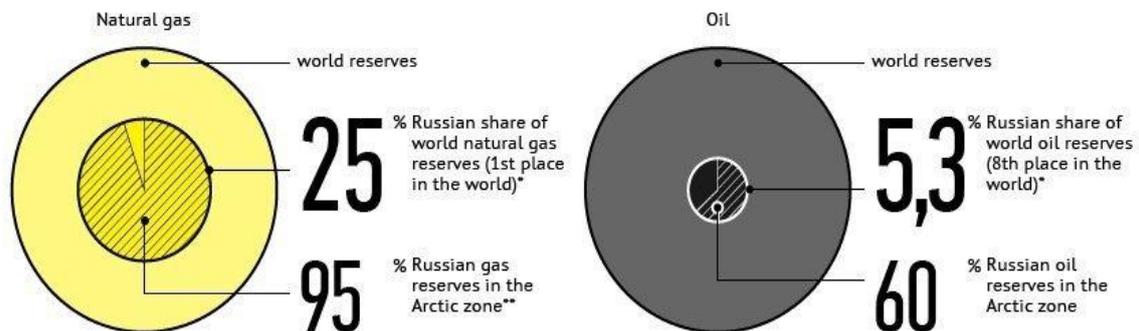
Oil and gas fields containing immense reserves have been found in the Russian section of the Arctic sea-shelf



Field classification



The Arctic in figures



*CIA data
 ** according to Valery Yazayev, Vice Speaker of the State Duma of the Russian Federation; president of Russian Gas Society

Source: Russian Oil and Gas Fields in the Arctic (2011), *RIA Novosti*, retrieved from [http://en.rian.ru/infographics/20111007/167371478.html] on September 10, 2013.

Today, oil and gas resources in East Siberia and on the Arctic continental shelf are viewed by the Russian state as new potential areas for energy production. In 2008 during the Security Council meeting, President Dmitry Medvedev (2008-2012) announced a mission to convert the Arctic region into a resource base of the 21st century, to compensate the dwindling resources in West Siberia (Ilyn, 2008). Recoverable hydrocarbon resources on Russia's continental shelf account for up to 100 billion tons, including more than 13.5 billion tons of oil and about 73 trillion m³ of gas (Ministry of Natural Resources and Ecology, 2006).

The bulk of resources (about 66.5%) are located in the northern seas (Barents and Kara Seas). Apart from the economic reasons for energy supply diversification, offshore development is linked with Russian geopolitical interests in guaranteeing its presence in the Arctic waters via a military component. In addition, offshore hydrocarbon production is associated with the socio-economic development of the Northern regions in Russia.

The "Strategy for the Development of the Arctic Zone of the Russian Federation and National Security for the Period up to 2020", published in February 2013, outlined the policy directions and the mechanisms needed for the relocation of oil and gas production into new areas. The strategy prescribes a development of a natural resource base by implementing new technologies, conducting complex studies on the continental shelf and in coastal zone, forming reserve fund deposits and accomplishing relevant infrastructure projects (Government of Russia, 2013). One of the mechanisms for the tasks' implementation is based on collaboration between state and business organizations, including foreign entities.

Hence, this study provides an analysis of the current state of relations between the Russian government, state-controlled (Gazprom and Rosneft), and private (LUKOIL and NOVATEK) oil and gas companies. The article begins with a brief overview of a legal set of actors and their respective rights for operation on the Arctic continental shelf. Furthermore, it provides a comparative analysis of the Russian government, state and private companies' offshore strategies and interests. Finally, the article outlines the prospective development of the Russian Arctic offshore sector in relation to the energy sector development in other Arctic states, as well as with the on-going changes in the global energy markets.

Subsoil Legislation: Rules for Operation on the Russian Continental Shelf

The Russian legislation on subsoil use is based on article 72 of the Constitution of the Russian Federation. This article states that any possession, use and disposal of land, subsoil, water and other natural resources is in joint jurisdiction of the federal government and the federal subjects (The Constitution, 1993).

The subsoil activity is regulated also by federal laws, decrees and orders issued by the President and the government of the Russian Federation, ministerial resolutions, and by adoption in accordance with federal laws the statutory legal acts of the federal subjects of the Russian Federation. The core federal law in the sphere of subsoil use is Federal Law № 2395-1 "On Subsoil Resources" dated 21 February 1992. The Federal Law regulates issues connected to geological survey, license granting and natural resources extraction and production. The subsoil operations on the continental shelf are operated in accordance with the Federal Law № 183-FZ "On the Continental Shelf", dated 30 November 1995, and the Federal Law № 191-FZ "On the Exclusive Economic Zone", dated 17 December 1998.

Regulation of offshore activities on the continental shelf falls under the jurisdiction of the Ministry of Natural Resources and Ecology and under the respective governmental entities. In particular, the Federal Agency for Subsoil Use (“Rosnedra”) is responsible for geological survey, insurance and license assessment of subsoil use and for auctioning licenses for subsoil use.

According to Russian legislation, the state has exclusive rights on subsoil use – no one can extract subsoil resources without the state’s consent. The right for any resources extraction can be granted in a form of a subsoil license or a state contract.

The 2008 amendments to the Federal Law “On Subsoil Resources” have specified strict criteria for subsoil users who are applying for offshore licenses. The amendments provide an access to offshore activities only to a legal entity with 5 years experience in development of deposits on the Russian continental shelf; established in accordance with the legislation of the Russian Federation and with a government stake of over 50% in its charter capital (Consultant, 2008). Currently, only two Russian state-controlled companies – oil company Rosneft and gas company Gazprom meet the criteria.

The amendments were also introduced to the legislation covering issues of foreign investment in strategic deposits. Under the new amendments, foreign companies are deprived of the right to obtain subsoil licenses and the right to develop strategic deposits, and are obliged to report to a government agency every time they acquire 10% or greater share in a Russian company that works in a strategic sector (Federal Antimonopoly Service of the RF, 2008).

The amendments introduced went in line with the general policy towards strengthening the government control in the energy sector and protection of the state’s national security interests. In particular, the “National Security Concept of the Russian Federation”, revised in 2000, prescribed an increase in state control over foreign investment and the introduction of well-grounded limitations on granting subsoil licenses to foreign companies (Security Council, 2000). Adopted in the following year, the “Marine Doctrine for the Period up to 2020” stipulated the protection and implementation of sovereign rights on geological surveys and the exploitation of offshore resources (Security Council, 2001).

Government and Private Energy Companies’ Approaches towards Offshore Oil & Gas Development Policies

The Arctic continental shelf monopoly held by the two companies Gazprom and Rosneft contributed to the emergence of two different approaches towards offshore project development within a political nomenclature in Russia. According to Rustam Tankayev, a leading expert at the Russian Union of Oil and Gas Industrialists, in the Russian energy industry two centers of power have been formed, including the Presidential Commission for the Strategic Development of the Fuel and Energy Sector and Environmental Security, whose executive secretary also holds the Presidency of Rosneft, Igor Sechin (2012-present), and the Government Commission for Fuel and Energy Complex, which is headed by the deputy Prime Minister Arkady Dvorkovich (2012-present) (Topalov, 2012). In general, the deputy Prime Minister advocates for the liberalization of the Federal Law “On Subsoil Resources”; the approach is also supported by the Ministry of Natural Resources and Ecology, Ministry of Economic Development and it stipulates expanding the number of companies that can work offshore, for tax regime facilitation and for an increase in the number of geological surveys conducted on the continental shelf. According to the Minister of Natural Resources and Ecology Jury Trutnev (2004-2012), the development of many

offshore projects will be very expensive and it will require 150 years to examine the hydrocarbon potential of the continental shelf in the Arctic under the current legislation (Melnikov, 2011). Currently, the density of seismic surveys covering the most promising waters of the Arctic Seas, except the Barents and Pechora seas, is not more than 0.15 per 1 km², and for the eastern seas, less than 0.1 km to 1 km² (Rbk Daily, 2013).

Over the past few years, the Ministry of Natural Resources and Ecology has been constantly lobbying for an increase in the number of legal entities that could gain the right to conduct economic activities on the Arctic continental shelf. In 2010 the Ministry proposed the consideration of both national and international offshore operations experience in making its decisions on granting subsoil use licenses for working on the continental shelf. However, the amendments introduced did not receive approval from the Ministry of Energy that called for the need to improve the proposals. In the following year, the Ministry initiated a proposal allowing legal foreign entities to acquire licenses to plots of deposits until the end of the geological survey stage in the relevant area of interest. The proposals also echoed initiatives articulated by the deputy Prime Minister Igor Sechin (1999-2008), who was making an effort into the creation of a strategic alliance together with BP for joint exploration of the offshore deposits in the Arctic. In 2012 the Ministry of Natural Resources and Ecology made a further step towards bringing changes into the existing subsoil legislation. It drafted its “Program for Exploration and Development of the Continental Shelf of Russia for the Period up to 2030” stipulating that private companies could conduct geological surveys without the collaboration or participation of the state-controlled companies, and introduced changes in the tax regime that are dependent on the complexity of the deposit. However, the draft was later sent back for revision by the Prime Minister Dmitry Medvedev (2012-present).

A certain breakthrough has been associated with the government meeting in Novy Urengoy, which was held in the beginning of 2013. However, the results of the meeting confirmed the senior officials’ stance towards preservation of the state-controlled companies’ monopolies on the continental shelf. The outcome of the meeting could be explained by the existing fierce lobby of the state-controlled energy companies and their strong connection with the state officials in the Russian government and the Russian President.

Strong supporters for subsoil law liberalization include private Russian energy companies LUKOIL, Surgutneftegaz, Bashneft and Zarubezneft. These companies have addressed the government and the President several times requesting the opening of the continental shelf for private business. The main argument expressed by the opponents of liberalization is the private companies’ inability to cover the financial costs of the Arctic projects and their lack of offshore experience. However, Zarubezneft possesses experience in working on the shelf projects in Vietnam and regards this as its golden opportunity for establishing a joint venture with the company Petrovietnam in order to work on the Russian continental shelf in the Arctic. In 2012, Zarubezneft acquired shares of the energy company “Arktikmorneftegazrazvedka” which possesses significant experience in the exploration and development of oil and gas deposits on the Russian continental shelf. The procurement of the company has made Zarubezneft eligible to work offshore. However, the government’s decision on allowing the company to proceed with offshore activity is still pending.

Another fierce supporter for liberalization has been the Russian private oil company LUKOIL, which began showing interest in offshore activities as early as the late 1990s. After the approval by the Russian government to grant Rosneft licenses to 12 sites, and to Gazprom licenses to 17

sites, LUKOIL started to consider other alternatives to obtain access to the Arctic continental shelf. During the official meeting with the Russian president Vladimir Putin, the head of LUKOIL Vagit Y. Alekperov expressed the company's intention to launch a geological survey at the Khatanga Bay on the coast of Yakutia. According to an analyst from Sberbank Investment Research Valery Nesterov, LUKOIL has been forced to engage in the least prospective offshore projects in order to display its loyalty to the government, with hopes of getting access to the continental shelf in the future (Melnikov, Popov et al, 2013). However, a few months after, the vice-president of LUKOIL Leonid Fedun stated that "[i]t would be cheaper for the Russian oil companies to develop deposits on the mainland than on the continental shelf" (Muraviev, 2013). Such a radical change in the company's policy has been spurred by a number of factors. The first factor deals with the existing uncertainty concerning the Russian government's legal adoption of the liberalized offshore activity rules, which has forced the company to reorient its development strategy from offshore to onshore deposits. Secondly, the company is facing a problem of a gradual depletion of its deposits and oil production declining. In order to keep energy production at a sufficient level and to maintain the company's competitiveness in the national and international energy markets, LUKOIL is considering purchasing several enterprises in West Siberia and in the Republic of Komi that already own licenses for onshore field developments (Solodovnikova, Melnikov, 2013).

The current state of affairs around the subsoil legislation clearly manifests the Russian government's position (with certain exceptions of certain Ministries) towards maintaining Gazprom and Rosneft monopolies on the offshore activity and reducing the chances of private companies working offshore. In addition, the recently signed agreements between Gazprom and Rosneft with the foreign energy companies Total, Shell, ExxonMobil, Statoil, CNPC and Eni respectively, for a joint development of deposits on the Arctic shelf have strengthened the state-controlled companies' positions by diminishing criticisms concerning the inability of foreign companies to participate in the Russian offshore projects. The acquisition of offshore licensees by Gazprom and Rosneft and the prescription by the recently released Arctic Strategy on the creation of reserve fund deposits, leave little room for maneuver by private companies to obtain access to offshore activities. In the long term, there are certain possibilities in which the private companies could proceed with offshore activity. For example, Gazprom's and Rosneft's inability to fulfill the geological survey requirements set by the Ministry of Natural Resources and Ecology could force the government to review its position towards subsoil law liberalization. In turn, Gazprom and Rosneft could implement counter action policies to encumber the actions of the Ministry and private companies in order to safeguard their monopolies on the offshore activities in the Arctic.

Gazprom and Rosneft Approaches Towards Offshore Oil & Gas Development Policies

Rosneft and Gazprom have huge economic interests in the Arctic region due to their need to replace the depleting fields in West Siberia and to guarantee their status as reliable energy suppliers.

Gazprom's involvement in Arctic offshore activities dates back to the beginning of the 1990s, when the company became the main decision-maker in the Rosshelf consortium. In 1992 the consortium was granted licences for Shtokman and Prirazlomnoye field development. Several plans were initiated by Rosshelf to develop the Shtokman field from creating a floating

liquefaction plant (in 1996) to building a pipeline from Vyborg to Murmansk and then to Peenemunde in Germany. There were two main debatable factors that the main shareholder in the consortium – Gazprom – considered the Arctic offshore exploration to be feasible by the end of the century. From a legal point of view, the sufficient Russian legislation on the offshore activities regulation was lacking. Economically, the Russian companies were neither financially nor technologically prepared for the project development on their own.

The next threshold in Gazprom's offshore policy dates back to the beginning of the 21st century and was linked with the interest of Gazprom to ship LNG from the Shtokman field to the US market. In 2008 Gazprom together with the Norwegian company Statoil and French company Total set up "Shtokman Development" – a joint venture for financing, construction and operation of the first project's phase. However, changes in the global gas market contributed to Gazprom diminished interest in the field development. In particular, the rapid growth of shale gas production in the US during the past few years has made gas exportation from the field to the American market less likely. In addition, a launch by Qatar liquefied natural gas (LNG) exportation to Europe has caused an increase of gas supply on the global market. This development, in combination with the world economic crisis of 2008/2009, has led to a decline in gas consumption, a decrease in the price of gas, and the emergence of a gas surplus in the world market. As a result, the development of the project has been postponed for an uncertain period of time, and Gazprom's co-partner, the Norwegian company Statoil, left the project in 2012.

Another factor that has restrained Gazprom in its offshore exploration is that the development of Arctic offshore hydrocarbon reserves are connected to technological production challenges, high investment costs and environmental risks, and the profits from hydrocarbon extraction will not be reaped for many years to come. Since 2008, Gazprom has been negotiating with the government regarding tax privileges for Shtokman field development, including the introduction of tax on additional income, reduction of export duties, and lowering taxes on mineral extraction. Currently, the government is working on legislation that will provide certain tax breaks for those projects for which the production will begin after January 2016. In turn, Gazprom is lobbying tax privileges for the projects whose commercial production will start in 2013. The company's position is backed by its plans to start production in the Prirazlomnaya field in 2013 and the granted tax breaks could save Gazprom \$2.4 billion in expenses (Rbk, 2012).

Following Gazprom's stance, Rosneft claims tax reductions from the government for its offshore Arctic projects that the company wants to develop together with its foreign co-partners. Rosneft has also performed as an ardent supporter of Gazprom's rigid stance on denial of the subsoil legislation liberalization. As part of their shared interests, the two companies had plans for joint activities on the continental shelf. Their cooperation in Arctic offshore projects date back to 2002 when Rosneft and Gazprom established "Sevmorneftegaz" – a joint venture to develop the Shtokman and Prirazlomnoye fields. In 2005, Rosneft sold its shares to Gazprom in order to release financial room for further merging with the private oil company Yukos. The Yukos takeover by Rosneft represented one of the first steps in the oil company becoming the world's largest oil producing company, which Rosneft fulfilled in March 2013 by completing the TNK-BP transaction.

In 2006 Rosneft and Gazprom launched a process for a future offshore deposits division by signing an agreement on a strategic partnership for the period up to 2015 with a possibility for a five-year extension. The agreement, in particular, prescribed joint exploration, production,

transportation and processing of hydrocarbons on a fifty-fifty basis. Based on the agreement, the companies intended to jointly participate in tenders and auctions for subsoil use licenses and to exchange the acquired geological information. The signed agreement was first and foremost aimed at reducing confrontation between the two companies and to raise the companies' competitiveness on the internal energy market, since the two companies have been actively fighting for the same licenses, triggering the initial price increase.

A further step towards division of powers in the energy sector was made in June 2007 when it was announced by the Ministry of Energy that the Arctic shelf and the Far East shelf would be explored by Rosneft and Gazprom. The announced measures have been implemented in the amendments to the Federal Law "On Subsoil Resources" in 2008.

To safeguard their positions in lobbying for an offshore monopoly and to reduce criticism from the Ministry of Natural Resources and Ecology concerning the low geological survey pace, Gazprom and Rosneft signed a cooperation agreement in 2012 on the creation and sharing of infrastructure for offshore deposits development. The agreement prescribed a development of business partnership between the two companies in order to increase their geological knowledge and to develop a reproduction of the resource base of the continental shelf.

In March 2013, after receiving licensing approval from the government on offshore deposits development, Rosneft heavily criticized the Ministry of Natural Resources and Ecology state program on continental shelf development, calling its main parameters for geological survey overestimated and suggesting establishment of a coordinated agency in order to work out a new document that would encompass the interests of the state-controlled companies. Rosneft also criticized the provision in which the company was obliged to return licenses to unallocated fund deposits in cases where the company had no intention to develop the field (Melnikov and Solodovnikova, 2013).

The delay of the decision on adoption of subsoil legislation liberalization and the allocation of subsoil use licenses to Rosneft and Gazprom without auctions clearly demonstrate the winning position of the state-controlled companies' alliance. However, the alliance between Gazprom and Rosneft for advocating their interests and stance on continental shelf deposits development has been destroyed by the emergent opportunities for Rosneft's gas policy expansion in both internal and external energy markets.

Rosneft vs. Gazprom: Prospective Strategies for Expansion

In Autumn 2012, Rosneft acquired a 51% share of the gas company ITERA, with proved reserves accounting for 372.4 billion cubic meters of gas and 15.7 million tons of condensate (Melnikov and Mordushenko, 2013). The shares acquisition has been done in the framework of cooperation between the two companies aiming at the creation of a joint venture. The merge with ITERA meant for Rosneft an access to the gas market and to existing contracts for gas supply; and for ITERA, energy sources. In 2013 Rosneft continued its gas policy expansion by undertaking certain steps towards reducing Gazprom's gas monopoly policy. During his speech at the Investors' Day in London in April 2013, the head of Rosneft Igor Sechin announced the company's plans to produce 100 billion cubic meters of gas by 2020 that will correspond to 19-22% of the Russian gas market (Chodyakova, 2013).

A month before that, the company expressed its interest in obtaining certain subsoil use licenses, on which Gazprom had a previous claim. One of the major reasons for allocating the licenses to

Rosneft was expressed in the letter by the company's Deputy Chairman of the Director Board Nikolay Laverov, stating that a certain part of the granted licenses would be explored by Gazprom's subsidiary, the private company Gazprom Neft, which represents a direct violation of the subsoil legislation. In addition, the company radically changed its position and supported the stance of the private gas company NOVATEK to diminish Gazprom's gas company monopoly on LNG export. The changes in the company's position have been backed by certain factors. Firstly, the development of the gas strategy by the company satisfied the goals of the "Russian Energy Strategy up to 2030" to create efficient conditions for independent gas producers in Russia. Secondly, 40% of Gazprom's long standing contracts are due this year and not all of the customers share an interest in the contracts' prolongation (Skorlygina and Motushenko, 2013). Thirdly, Rosneft obtained 40 licenses for offshore field's development, which are predominantly gas deposits. According to Igor Sechin, such an amount of gas cannot be implemented in the domestic market (Serov, 2013).

In the dispute between Rosneft and Gazprom the government took a cautious stance. The positive remarks towards LNG export liberalization were expressed by the Russian President Vladimir Putin during the Presidential Commission for the Strategic Development of the Fuel and Energy Sector and Environmental Security meeting and by the Prime Minister Dmitry Medvedev during the latest World Economic Forum in Davos. However, the statements did not contain any concrete plans. Recently, the Ministry of Energy announced its plans to introduce new legal mechanisms of the united LNG export policy by September 2013. Due to Gazprom's rigid position towards its monopoly preservation, it is doubtful that a total abolition of Gazprom's LNG monopoly will occur. The company claims that the existing monopoly on gas exports compensates the huge financial and social burden that the company fulfills inside Russia, including gasification of regions and the implementation of social programs on federal and regional levels.

In turn, Rosneft is gradually fortifying its presence on the gas market and taking steps to weaken Gazprom's position. Firstly, Vlada Rysakova, a former head of the strategic development department in Gazprom, was appointed as a Vice President of Rosneft to manage the company's gas development policy. Secondly, NOVATEK has shifted its partnership priorities from Gazprom to Rosneft. In particular, NOVATEK halted the establishment of a joint venture to explore Gazprom's deposits on Yamal and NOVATEK's deposits on Gydan peninsula (Topalov, 2013). One of the major reasons standing behind the company's interests' switch is the development of the Yamal LNG project which the company is developing together with the French company TOTAL, which holds 20% of the project's shares. It is planned to launch gas production in 2016, however the financial part of the project and the future export contacts depend on the government's decision towards LNG export liberalization. Thirdly, the head of Rosneft announced the company's intentions for the LNG plant construction on Sakhalin by 2018.

At the same time, Rosneft expressed its interest in participating in the ExxonMobil project on an LNG plant construction in the Point Thompson Alaska oil and natural gas field, where Rosneft holds a 25% stake. According to Maria Belova, a senior analyst at the energy centre of the "Skolkovo" business school, it is possible that Rosneft can fulfill its agreement obligations by agreeing to participate in the project (Serov, Solodovnikova et al, 2013). In the event of project implementation, Rosneft will have to compete with Gazprom and with its own gas strategy because the ExxonMobil project also targets Asian countries.

Rosneft has also expressed a strong interest in expanding to the Asian markets. The interest has been vividly shown during its latest business tour to China and South Korea. During the visit to China Igor Sechin met the heads of the three leading companies – CNPC, Sinopec and CNOOC. The meeting discussed the prospective participation of Chinese companies in joint projects on exploration and production on the Russian continental shelf. Recently, Rosneft signed an agreement with CNPC to develop deposits in the Barents and Pechora Seas. The company also proposed new forms of collaboration in the field of LNG transportation. The issue of LNG transportation has been raised at the meeting with Rosneft and the South Korean companies KOGAS and STX. For Rosneft the partnership with Korean companies will provide access to technologies and financing, and will open up new markets for LNG export. In addition, countries represent attractive export markets for energy resources since prices on LNG are higher in China and Japan than to the European countries.

The private company NOVATEK has also expressed its interest in expanding its presence in Asian markets. The possibility of Chinese companies joining the Yamal LNG project emerged just after the February Asian business tour. Collaboration with Chinese companies would solve two vital problems: the issue of export markets and the project's financing.

The major rival to Rosneft and NOVATEK – Gazprom – also shares a strong interest in exporting energy resources to Asian markets. In general, Asian markets for Gazprom represent an option for diversification of its gas export markets and a reduction in its dependence on European energy consumption. Gazprom is facing certain difficulties in relation to the European countries, who are also trying to reduce their energy dependence on Gazprom. Specially, Europe is reviewing projects which bypass its traditional gas suppliers. As a result, the Nabucca project has been replaced with a plan to construct a Trans-Anatolian gas pipeline through Azerbaijan and Turkey and it is estimated that the first gas supply will be launched in 2017. At the same time, intensified talks have been launched on the Trans-Caspian gas pipeline construction under the Caspian Sea, through which gas from Turkmenistan will be supplied directly to the European market.

In addition, the prospective LNG supply from North America, Africa or Middle East in the nearest term could reduce Gazprom's share on the European gas export market and could force the company to reduce gas prices. Gazprom has already made certain concessions towards gas price reduction. In January 2013, the company reported that a gas price reduction of 10% had been achieved by Austrian Econgaz, Italian Sinergie Italiane, Slovak SPP, Wingas German and French GDF Suez (Pronedra, 2013).

At the same time, Gazprom faces certain difficulties in relation to the Asian market as well. Despite the recently signed agreement between Gazprom and the Chinese Company CNPC on gas supply from Russia for a period of 30 years, Russia and China have not reached an agreement on the price of the Russian gas deliverance yet. The issue of gas price decrease also represents a challenge in the relations between Gazprom and Japan concerning prospective LNG supply from the "Vladivostok LNG" plant to the Asian country.

On the other hand, there is a time constraint in LNG development by the Russian companies due to growing competition from other countries like the US, which are hoping to start shipping LNG in 2015, as well as Canada and Australia who, like Russia, view fast-growing Asian countries as prospective energy markets. At the same time, Asian countries are also trying to reduce their dependence on oil and gas imports. Chinese and Japanese companies are planning to

launch the development and extraction of shale oil deposits and Japan has already successfully extracted gas from frozen methane hydrate in its coastal area. In addition, the prospective relocation of energy production into new areas with high extraction costs, places a serious challenge for the Russian companies, in particular Gazprom, concerning its future gas price negotiation policy at a time of a prospective increase of the LNG supply.

At the same time, despite the official policy recently expressed by the Russian President Vladimir Putin to develop energy supplies for Asian markets, the European market is still regarded as the major one. In support of this policy, Vladimir Putin must restart the work of the “Yamal - Europe 2” pipeline project, aimed at improving the reliability of deliveries to Slovakia, Hungary and Poland. In addition, Gazprom announced recently its plans to return to the LNG plant building project in Primorsk, which Gazprom had given up in favor of the Shtokman project eight years ago, to supply gas to the European markets (Serov, Timoshinov et al, 2013). In turn, a launch of the LNG project in Primorsk places in question the prospects of Shtokman field development and the capacity of Gazprom to implement offshore energy projects in the Arctic in the nearest future. However, according to Maria Belova, a senior analyst at the business school Skolkovo, an LNG plant in Primorsk will allow Gazprom to circumvent regulations of the EU Third Energy Package (Solodovnikova, 2013).

Simultaneously, Gazprom continues to strengthen its positions on the Arctic continental shelf. One of the major outcomes of Vladimir Putin’s recent visit to the Netherlands was the signing of a memorandum on cooperation between Gazprom and Shell, setting out principles for collaboration in the exploration and development of hydrocarbon reserves on the Russian Arctic shelf. The agreement with Shell, after the misfortune with the Shtokman project, is likely to be seen as a certain confirmation of the company’s intention to be present on the Arctic continental shelf. It is likely that the agreement between the companies will turn into a practical collaboration in offshore energy projects, including a possibility of Shtokman field development, as it was planned by Gazprom after Statoil had left the project. The signed agreement could be also seen as a counterbalance to Rosneft’s partnership with foreign companies. In the continuation of the agreement concluded with Shell, Gazprom has recently been granted four subsoil sites in the Barents and has won a dispute with Rosneft where seven out of eight disputed sites in the Kara Sea were granted to Gazprom. The two companies also agreed on splitting the disputed site in East Siberian Sea. Gazprom will acquire licenses for East-Siberian-2 block and Rosneft will obtain licenses for East Siberian-1 block.

Conclusion

In general the offshore energy development in Russia is characterized by rivalry *within* business and political structures and *between* them, although there are certain issues where everyone’s opinions coincide. The government, backed by the state-controlled companies Rosneft and Gazprom, follows a rather rigid stance towards preservation of the state monopoly on the offshore sector through privileges granted to Rosneft and Gazprom. A certain divergence from this position could be seen in the policy of Ministry of Natural Resources and Ecology, which lobbied for the liberalization of the current subsoil legislation. The position is mostly backed by the strong necessity to speed up geological surveys and to re-orient energy production from the gradually depleting fields in West Siberia to new areas, including the Arctic continental shelf. It is rather doubtful that the government will expand the number of actors to conduct oil and gas exploitation on the shelf. There is a small possibility that the private companies will be allowed to

conduct geological surveys under the joint agreement with Rosneft or Gazprom, while the state-owned companies will be responsible for extraction and production.

The political rivalry is also fueled by the hostile relations between Rosneft and Gazprom. While providing a certain degree of support to Rosneft, for instance, by allowing the TNK-BP company purchase, the President has leaned towards the protection of Gazprom's gas export policy by stating that LNG export liberalization should not harm Gazprom's export positions. Thus, a further expansion of Rosneft in the gas market and on the continental shelf, in particular, will depend on the ability of its President, Igor Sechin, to lobby its interests and influence the decisions of the President and the government concerning the future development of Gazprom and the energy sector as a whole.

At the same time, the rivalry brings into question the ability of Russia to effectively implement its energy policy and its goals of expanding exports to Asian markets. In reference to the offshore development, the main concerns are about the time-period for the start of the economic activity on the shelf and with its LNG production, and its existing risks and high costs. The uncertainties around LNG export liberalization and the tough stance taken by Gazprom to preserve its export monopoly also bring into question the possibility of the Yamal LNG project coming into realization by 2017. In addition, there are doubts concerning the feasibility of Gazprom's Vladivostok LNG project and Rosneft's Sakhalin LNG project due to high costs and the existing uncertainty with the gas export markets.

The question also exists concerning the impact of cooperation with foreign companies on the future development of the Russian energy sector and on the ability of the state-controlled companies to independently carry out economic activities on the shelf in the future. For now, it seems that the companies are trying to stake offshore sites in the Arctic, considering offshore extraction from a long term perspective.

Summing up, the uncertainties described above towards internal energy policy development and competition for resources and political sphere of influence inside Russia could lead to a situation where the country will weaken and possibly will lose its position as a main energy exporter to the European and prospective Asian markets. The critical challenge for Russia lies not in growing competition from other energy export countries; rather it is the inability of the state to effectively tackle the current problem of gradual depletion of its West Siberian fields. Thus, the state is facing a critical necessity in clearly defining its energy strategy and undertaking bold steps to introduce changes into the current state of affairs in the Russian energy sector.

References

Berezinskaya O. & V. Mironov (2006). Samaya gravnays otrasl' (The most important economic industry). *Kommersant*. 154 (3485). Retrieved 24.08.13 from <http://www.kommersant.ru/doc/699414/print>

Business Monitor International (2011). *Russia Oil and Gas Report Q 4 2011* (Report). Retrieved 25.08.13) from, http://www.researchandmarkets.com/reports/1945248/russia_oil_and_gas_report_q4.

- Chodyakova, E. (2013). Rosneft brosaet vyzov Gazpromu (Rosneft challenges Gazprom). *Vedomosti*. Retrieved 08.05. 13 from, http://www.vedomosti.ru/companies/news/11486901/rosneft_posopernichaet_s_gazpromom#ixzz2RMa8hk2P
- The Constitution 1993* (Const.) art. 72. Russian Federation. Available from <http://www.constitution.ru/en/10003000-01.htm>.
- Consultant. (2008). Federal'nii zakon o Nedrach (Federal Law on Subsoil Resources) №2395-1 21.02.1992. (Eds.). 29.04.2008 № 58-FZ). Retrieved 25.08.13 from, <http://www.consultant.ru/popular/nedr>.
- Federal Antimonopoly Service of the Russian Federation. (16 April 2008). Federal Law № 57-FZ "Procedures for Foreign Investment in the Business Entities of Strategic Importance for Russian National Defence and Security. Retrieved 25.08.13 from, http://en.fas.gov.ru/legislation/legislation_50727.html.
- The Government of the Russian Federation. (20 February 2013). Strategia razvitiia arkticheskoi zoni Rossiiskoi federatsii i obespechenia natsionalnoi bezopasnosti na period do 2020 goda. (Strategy for the Development of the Arctic zone of the Russian Federation and National Security for the period up to 2020). Retrieved 15.05. 13 from, <http://government.ru/docs/22846/>.
- Kezik I. & A. Ermakova. (2012). Rossiiu zdet padenie nefti (Russia will be confronted by the decline in oil production). *Izvestia*. Retrieved 24.08. 13 from, <http://izvestia.ru/news/535618>
- Ministry of Natural Resources and Ecology (07 March 2006). Proekt Strategii izucheniia i osvoeniia potentsiala kontinental'nogo shelfa Rossiiskoi Federatsii na period do 2020 (Project of a Strategy for developing the oil and gas potential of Russia's Continental shelf for the period up to 2020). Retrieved 25.08.13 from, <http://www.mnr.gov.ru/regulatory/detail.php?ID=20488>
- Melnikov K. (2011). Ot shelfa ne ouidesh (One cannot go away from shelf). *Kommersant*. 198 (4739). Retrieved 14.03.13 from, <http://kommersant.ru/doc/1799668>.
- Melnikov K. and Mordushenko O. (2013). Rosneft vedet dobichou v nedrach Gazproma (Rosneft mining in the Gazprom sub-soil assets). *Kommersant*. 69 (5100). Retrieved 08.06.13 from, <http://www.kommersant.ru/doc/2173760?fp=11>
- Melnikov K. & A. Solodovnikova. (2013). Rosneft vitesniaet Gazprom (Rosneft replaces Gazprom). *Kommersant*. 62 (5093). Retrieved 01.05. 13 from, <http://www.kommersant.ru/doc/2166687>.
- Melnikov K., E. Popov & A. Solodovnikova (2013). LUKOIL zagnali v medvezhii ougol

- (LUKOIL was forced into the backwater). *Kommersant*. 32 (5063). Retrieved 14.03. 13 from, <http://www.kommersant.ru/doc/2131961?isSearch=True>
- Muraviev, D. (2013). Slantsevaia revolutsia v Sibiri (Shale revolution in Siberia). *Delovaia gazeta vzgliad*. Retrieved 15.05.13 from, <http://www.vz.ru/economy/2013/4/1/626836.print.html>
- Neftegazovaya Rossiya (2013, 20 March). Dolia neftegazovich dochodov v budžete RF v 2012 sostavila potchi 50% (The share of oil and gas revenues in the budget of the Russian Federation in 2012 amounted to almost 50%). Retrieved 24.08.13, from <http://energyland.info/news-show-tek-neftegaz-101374>
- Rbk. (2012, 29 October). Gazprom prosit ou pravutelstva novich lgot (Gazprom asks from the government new tax breaks). Retrieved 10.05. 13 from, <http://top.rbc.ru/economics/29/10/2012/822242.shtml>
- Rbk daily. (2013, 14 March). Rossiiskii shelf izuchen v 20 raz khuzhe norvezhskogo (The Russian shelf is studied 20 times worse than the Norwegian). Retrieved 16.01.13 from, <http://top.rbc.ru/economics/16/01/2013/840614.shtml>.
- Pronedra. (2013). Gazprom snizil tseni na eksportnie postavki v Evropu (Gazprom has reduced export prices to Europe). Retrieved 14.03. 13 from, <http://pronedra.ru/gas/2013/02/14/gazprom-snizhaet-ceny/>.
- Ria Novosti. (2012). Gde v Rossii dobivaut neft' – reiting regionov (Where oil is produced in Russia – regions' ranking). Retrieved 24.08. 13 from, http://ria.ru/research_rating/20120228/578638606.html
- Security Council of the Russian Federation. (10 January 2000) *Konseptsia natsionalnoi bezopasnosti Rossiiskoi Federatsii (National Security Concept of the Russian Federation)*. Retrieved from, <http://www.scrf.gov.ru/documents/1.html>.
- Security Council of the Russian Federation. (27 July 2001). *Morskaya Doktrina Rossiiskoi Federatsii na period do 2020 goda (Marine Doctrine of the Russian Federation for the period up to 2020)*. Retrieved from, <http://www.scrf.gov.ru/documents/34.html>
- Serov M. Gazprom proigral v monopoliu (Gazprom lost the monopoly). *Kommersant*. 27 (5058). Retrieved 08.06. 13 from, <http://www.kommersant.ru/doc/2126773/print>.
- Serov M., Solodovnikova A. and Sarchaiants K. (2013). Rosnet osvivaetsia na Aliaske (Rosneft is settled down in Alaska). *Kommersant*. 58 (5089). Retrieved 12.05.13 from, <http://www.kommersant.ru/doc/2161871>.
- Serov M., E. Timoshinov & A. Pushkarskaya. (2013). Gazprom vozvrashiaetsia na Baltiku (Gazprom returns to Baltic). *Kommersant*. 87 (5118). Retrieved 08.06. 13 from, <http://www.kommersant.ru/doc/2195732>.

- Skorlygina O. & O. Matushenko. (2013). Gazovili stali miagche k klientam (Gas companies have become softer to clients). *Kommersant* 93 (5124). Retrieved 10.06.13 from, <http://www.kommersant.ru/doc/2203425>.
- Solodovnikova, A. (24 May 2013). Gazprom zaniel oboronu na shelfe (Gazprom took up defensive positions on shelf). *Kommersant*. 87 (5118). Retrieved 08.06. 13 from, <http://www.kommersant.ru/doc/2195703>.
- Solodovnikova A. & K. Melnikov. (2013). LUKOIL dovolstvietsia malim (LUKOIL is grateful for small favors). *Kommersant*. 62 (5093). Retrieved 14.03. 13 from, <http://www.kommersant.ru/doc/2166687>.
- Topalov, A. (2013). Gazovaia voina na Gyadane (Gas war on Gydan). *Gazeta.ru*. Retrieved 08.06. 13 from, <http://www.gazeta.ru/business/2013/04/25/5280585.shtml>.
- Topalov, A. (2012). Shelf zavis mezdu Sechinim I Dvorkovichem (Shelf hovered between Sechin and Dvorkovich). *Gazeta.ru*. Retrieved 25.08. 13 from, <http://www.gazeta.ru/business/2012/08/02/4707749.shtml>.