

Russia cuts off Ukrainian gas supply

Energy conflict threatens EU shortages

Niall Green
3 January 2009

On January 1, the Russian state-owned energy company Gazprom turned off all gas supplies to Ukraine, following the failure of negotiations with Kiev over a huge disputed bill.

A press statement from the Russian firm noted that gas supplies to Ukraine were cut off at 0700 GMT, immediately after the expiration of the previous year's contract. "The debt to Gazprom for gas supplied earlier was not paid. Despite verbal statements from Kiev, Gazprom did not see any money in its account," claimed Alexei Miller, chief executive of Gazprom.

Without Russian gas, Europe's stockpiles would be exhausted in days. A similar row between the two ex-Soviet republics at the beginning of 2006 led to shortages in the gas supply to the European Union. One fifth of the EU's gas requirements are piped from Russia across Ukraine.

European energy firms have so far reported no drop in supply. Gazprom said it was watching for signs that Ukraine was siphoning off gas bound for Europe by testing pipeline pressure in Slovakia, near the Ukrainian border.

The EU and the United States have urged a quick solution to the row and secured agreement on resumed talks. But there is no easy solution.

Russia is demanding a settlement from Ukraine of over US\$2 billion for gas delivered as well as fines levied for late payment.

Speaking on Russian television in December, President Dmitri Medvedev said that Ukraine "should pay the money to the last rouble if they don't want their economy eventually running up against sanctions and demands from the Russian Federation."

Ukraine's state gas supplier Naftogaz claims it has fully repaid Gazprom. The two countries have also failed to agree on a price for 2009, with Russia pushing to increase the cost of gas to its neighbour. Russian gas is currently

piped to Ukraine at below-market value prices. Gazprom is offering Ukraine a price of \$250 per 1,000 cubic metres of gas in 2009, half the price of the supply to the EU.

Naftogaz maintains it has paid US\$1.5 billion in outstanding bills to Swiss-registered gas trading company RosUkrEnergo, which is joint-owned by Gazprom and two Ukrainian businessmen and acts as intermediary for Ukrainian payments to Russia.

Naftogaz refuses to pay the US\$450 million in fines levied by Gazprom.

Ukraine has confirmed that gas supplies from Russia have fallen significantly. The Ukrainian energy minister stated that gas was being pumped from national reserves, which could be sufficient to last for several months.

President Viktor Yushchenko of Ukraine claimed on 24 December that an agreement had been reached with Gazprom to reschedule repayment. "A portion of the debt will be restructured" over several months, Yushchenko stated.

The European Union has urged Russia and Ukraine to resume negotiations to avoid disruption to the supplies of the rest of Europe. The government of the Czech Republic, new holders of the rotating EU presidency, has urged Ukraine and Russia to "rapidly reach a successful outcome" to the dispute. Moscow and Kiev have claimed that gas supplies to the EU will not be affected by their dispute.

"Usually we supply 390 million cubic metres per day, of which 300 million is transit gas for Europe. Today supplies are running at 300 million cubic metres. We continue supplying Europe in full," said a Gazprom spokesperson of gas supplies through Ukraine. The company says it has also increased the volume of gas piped into Europe via other routes.

However, Gazprom Chairman and First Deputy Prime Minister of Russia, Viktor Zubkov, claimed that the dispute could affect the countries of the EU. "It is not ruled out that the current position of the Ukrainian side

and some of its actions could lead to disruptions in the stability of gas supplies to Europe," he said in a statement in December.

"War of the clans"

Gazprom chief Miller has suggested that Kiev has sought to provoke a wider dispute with Russia, alleging that "political forces in Ukraine" were "very eager to see a gas conflict between our two countries".

Russian Prime Minister Vladimir Putin has warned of "very severe consequences" for Ukraine as a result of the dispute, both in terms of its relations with Russia and the EU. He pointed out that Ukraine was in "a difficult economic situation".

Ukraine's economy was propped up in October 2008 with a \$16.4 billion emergency loan from the International Monetary Fund and has seen its exports plunge while the value of its currency has fallen sharply.

Putin has also suggested that the non-payment of the gas bill had more to do with a "war of the clans" involving Ukrainian Prime Minister, Yulia Tymoshenko.

The company that is acting as intermediary between Ukraine and Russia in the dispute over payments is RosUkrEnergo, an operation established at the behest of Putin in 2004 and half-owned by Gazprom. RosUkrEnergo makes huge profits from its status as the secondary wholesaler of Russian gas through Ukraine, last year buying Russian gas for \$2.27 per million cubic feet and selling it to Europe for as much as \$5.55.

The two leading Ukrainian businessmen in RosUkrEnergo, Dmitry Firtash and Ivan Fursin, jointly own the other half of the firm. With such enormous power and wealth at their disposal, the two figures represent a potential threat to the interests of Tymoshenko as well as likely allies of Moscow, upon whom their lucrative arrangement largely depends.

Tymoshenko has proposed ending RosUkrEnergo's role as go-between over gas supplies. Instead she is seeking to import gas from Russia and sell it directly to Europe, a move that would augment the interests of her government and its supporters in big business. Tymoshenko's multi-million dollar personal fortune was made in the gas industry in the 1990s.

Tymoshenko has also alleged that RosUkrEnergo is controlled by Semion Mogilevich, a Ukrainian-born

oligarch wanted by the FBI in the United States and currently under arrest in Russia on tax evasion charges.

There are opposing suggestions that Russian authorities have exacerbated the gas dispute with Ukraine in order to send a message to Europe that Moscow plans to increase the cost of gas while not tolerating any intransigency regarding payments. On 23 December, speaking to a meeting of major gas producing countries in Moscow, Putin claimed that "the era of cheap energy resources, of cheap gas, is, of course, coming to an end."

Another factor impinging on energy disputes between the two countries is the growth of tensions between Russia and the US over expansion of NATO and the location of American missile systems in Eastern Europe. The gas cut-off came shortly after a visit to Moscow by Yushchenko. During the trip Yushchenko maintained his longstanding position that Ukraine would seek membership of the US-led military alliance. Ukrainian membership of NATO is fiercely opposed by the Kremlin, which sees it as a direct threat from Washington to Russian security.

Speaking at a press conference with the Ukrainian leader, 12 December, Putin said that the question of NATO membership was an internal matter for Ukraine, but warned Kiev to consider the consequences of such a move. He warned that Russia "has its own responses" to a heightened US military presence in the region.

Putin and Tymoshenko were accused by some supporters of Yushchenko of conspiring to undermine the Ukrainian president's regime during the last shut-off of Russian gas supplies in 2006. Fresh presidential elections are due in Ukraine in January 2010, with Tymoshenko likely to run against her former ally, Yushchenko.



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