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Commercial or Political Interests

Oil and Gas in the Russian Arctic

Erik Larusson

Executive summary

The Russian efforts of developing the natural resources in the Arctic region have intensified during the last years, and the leadership of the country is underlining the importance of speeding up the process of doing do. Putin has states that the current resources on land are depleting, and that a substitute needs to be found. But the Russian state companies Gazprom and Rosneft, the two companies who have been granted licenses to develop the Arctic shelf, are struggling against heavy bureaucracy and tight restrictions. Not the least because the Russian energy sector is considered an issue of national security, foreign involvement is heavily restricted. Furthermore, profitability of such offshore Arctic projects is uncertain, due to large demands for investments and high technology and the need for a high world oil price.

The dubious nature of developing the Arctic thus spurs the question of why the Russian government is so keen on landing these oil and gas reserves. By highlighting the economic viability of developing the northern oil and gas resources and putting them in contrast to other potential reasons for developing the regions resources, this study attempts to present possible drivers for the Russian development of the Arctic oil and gas riches. Furthermore, the question of what the state oil and gas companies do to try to affect the regulations for their Arctic endeavors is studied.

Even though the Arctic is expected to hold large amounts of resources, the economic viability of developing the Arctic region is questionable. The crucial oil price, which recently has experienced a sharp decline, could pose difficulties for the profitability of the oil and gas development projects. Furthermore there are potential development sites on land that do not require the same costs and risks. Russian governmental officials however, have pointed to the development of the Arctic as a way of giving a boost to the Russian economy, not just by sales of oil and gas, but also by using domestic technology and expertise to support the Arctic activities. As a result of the Ukraine sanctions against Russia, Rosneft has stated that it could replace the foreign equipment used in a matter of three to four years.

Having this dubious economic outlook for developing the Arctic, other drivers are suggested. One driver connects to the image-making of Putin. Being one of the first to land resources in the unhospitable conditions of the Arctic is a feather in the hat for Putin, and leads to a positive international reputation.

Another highly topical potential driver is geopolitics. The planned increased military presence is portrayed as a guarantor for the safety and security of the commercial activities in the Arctic, but it should also be able to discourage other powers from engaging in any of the contested sea areas. Furthermore, the increased US interest in the Arctic, as well as the deteriorating relations between Russia and the West as a result of the events in Ukraine, could be seen as factors instigating this driver.

For Rosneft and Gazprom the Arctic is a difficult place to operate and the profits are uncertain. However, their Arctic ventures attract capital investments, something which both companies are in need of. In order to facilitate their work on the shelf, they do try to influence

the leadership. Letters leaked to the media, sent to the president and the government from the state companies, give an indication of how they try to lobby the state and what issues they focus on. One of the major issues the state companies lobbied against was to allow any other actors onto the shelf. To date, it appears as if this has been successful – only Rosneft and Gazprom are allowed access. Another result of the lobbying efforts could be seen in the Interdepartmental Commission for removing administrative barriers for subsoil development. Rosneft had prior to this sent letters to state representatives about the tight regulations and excessive red tape for the oil and gas business. As these letters were surely preceded and succeeded by informal and non-public lobbying efforts, the result is still clear. Both state companies were to be included in the Interdepartmental Commission, which gives them a better position to influence and present their views. Similar lobbying efforts had earlier been attempted by e.g. Lukoil, but without any success. Igor Sechin's arrival as the President of Rosneft has made the state companies' voice stronger and seemingly more influential. His close ties with Putin and his understanding of the political drivers and the commercial realities of oil and gas development in such difficult areas as the High North, has given him a unique position in the development of the Russian Arctic.

About the author

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Introduction

The Russian government appears to be in a rush. As a result of the melting polar ice cap the oil and gas riches at the bottom of the Arctic seas are becoming increasingly accessible, and President Vladimir Putin has made it a top priority for Russia to be one among those nations who manage to extract the valuable mineral resources of the High North. At the same time as Russian economic growth is seriously halting, the sources for the previous economic development, i.e. current oil and gas fields, are being depleted, according to recent statements by the Russian President (Sergeev, 2014). The Arctic is portrayed as a guarantee of continued economic security and wealth of the country.

But the challenges for offshore development in the far north are many. Policies and regulations for Arctic oil and gas exploration and extraction are far from facilitating the work of the state companies of Rosneft and Gazprom, which have received licenses for extracting oil and gas from the northern shelf. Political aspirations, driven by a nationalistic rationale of fear of foreign involvement in the Russian energy sector are at odds with the economic realities of Arctic offshore shelf development. With its one hand the government is pushing for a more rapid development of the northern shelf, at the same time the other stalls the work of the state companies through tight regulations and restrictions. For the average observer, it would probably give the impression of the Russian state being economically schizophrenic. But there is more to it than meets the eye.

The uncertainty characterizing Arctic offshore development, having the resources yet being unproven and future mineral prices unpredictable, leads to various forecasts about when the riches could be extracted, ranging from 10 to 20 and sometimes even 30 years of waiting. Sergey Donskoi, Russian Minister of Natural Resources, has even gone so far as saying, *given the current speed of development*, the resources on the Arctic shelf won't be developed for another 150 years (*Neft i Kapital*, No 10/2010). What is becoming increasingly clear is a dilemma of exploring the Arctic region. Development and protectionism do not go hand in hand, something that is becoming ever so apparent in the context of mineral shelf extraction.

This paper sets out to give an understanding of the balance between political and commercial interests in the Arctic region as well as state energy companies' role in the formation of the regulatory framework for Arctic oil and gas development. The following questions attempt to be answered:

- Which appear to be the general drivers behind the Russian haste towards the extraction of oil and gas resources in the Arctic region?
- How are Russian state oil and gas companies attempting to influence regulations, setting the conditions for the development of the Arctic shelf?
- What results can be observed as a consequence of such efforts?

The scope of the study has been limited to the time after Vladimir Putin won the presidential elections in 2000. It is after the turn of the millennium that more active attention has been

given to the Arctic region and its potential as a resource base for serving the needs of the Russian Federation. Accentuated attention is given to the past 3 to 4 years, when the presence of oil, gas, and shipping companies in the far north has become more palpable.

In order to answer the first posed question, one needs to elaborate on which *commercial interests* are present, and what the *political plan* for the Arctic appears to entail. As for the commerciality, this needs to be put into the context of actual "facts on the ground"; what appears viable in terms of Arctic offshore oil and gas extraction. Regardless of what projects are planned or already embarked upon, having the existing technological and investment gaps, they will take a considerable time to realize. Furthermore, it is crucial to look well ahead, as returns on the large investments that need to go into the projects *now*, are expected to come only after a longer time period. Future demand for the resources is a decisive factor for the extraction of any natural resource.

Following the results of the economic considerations accounted for; the perceived commercial drivers are presented. Political drivers found are then put in relation to the apparent commerciality of developing the Arctic, in order to portray the balance between commercial and political interests/drivers.

The material used for mapping the political drivers and plans for oil and gas development in the Russian Arctic predominantly consists of articles and interviews that have been published in various Russian and international media outlets as well as Russian policy documents. Specific attention is given to Russian newspapers, as it is common practice for government officials and experts to disclose plans, intentions and views through these channels. As for the commercial drivers, I have consulted Russian governmental program as well as reports on future demand on oil and gas. Similar as for the political drivers, Russian and international news articles and published interviews have also been used.

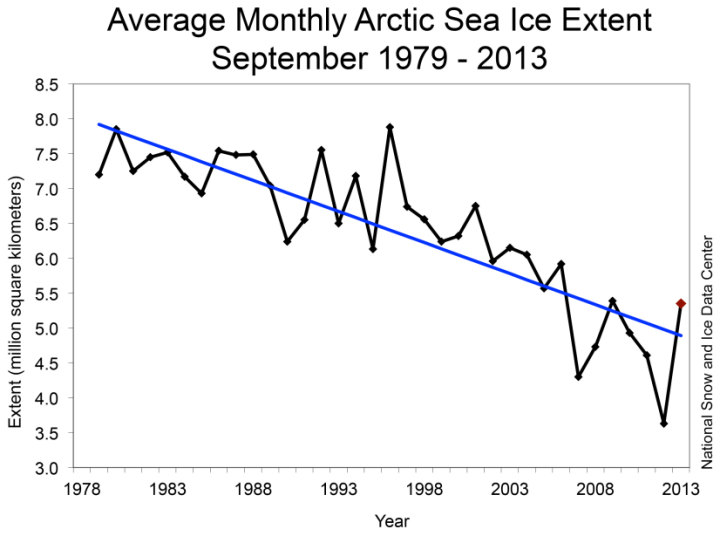
For the second and third questions, correlation between the presented state companies' efforts in influencing regulations and the results should rather be seen as an indicative than a definite correlation, keeping in mind difficulties making clear-cut measurements of influence. For the section dedicated to these questions of state companies' involvement in the Arctic policy orientation, I have chosen to limit the scope of study to primarily Rosneft's conduct. The material is based on leaked letters from state companies to the government which have been published in Russian media, Russian and international news articles, government policy documents as well as official statements and comments from ministries and oil/gas companies.

As a background to Russian energy power and lobbying in Russia, previous work by Russian and international scholars has been used.

Natural resources in the Russian Arctic

Since 1979, the US National Snow and Ice Data Center has retrieved satellite data of the spread the Arctic ice sheet. Typically the maximum ice extent is observed in March while it generally reaches its minimum in the month of September. In September 2013 the average monthly ice extent reached around 5.3 million square kilometers (Sea Ice Extent Sept 2013). This is a reduction of approximately 1.9 million square kilometers compared with the 1979 data – over four times the size of Sweden (Sea Ice Extent Sept 1979). And although the ice extent increased last year compared to the record low in 2012, the downwards pointing trajectory is apparent.

Through these data, we are witnessing a rapid and vivid result of climate change, having an adverse impact on the ecology and wildlife of the Arctic region, but the situation also renders possible various sorts of commercial activities in previously inaccessible areas.



© (National Snow and Data Center, 2013)

Arctic shipping, mineral extraction, research, and tourism have reached the top of the agenda of not only regional, but world politics. Last year 71 ships transited the Northern Sea Route (NSR) off the Russian coastline, a 54 % increase compared to the number of transits in 2012 (NSR Transit 2013). In 2010, only 4 ships made the whole passage.

Some argue that using the NSR could lead to great savings in time and costs for sea transport (especially for regional transport), and a reduced environmental impact due to the shorter trips and lesser fuel consumption (Lunde, 2013). The Arctic flora and fauna however are very fragile and more sensitive than in other parts of the world. The reduced negative environmental impact is thus not uncontested, as even minor emissions or spills could have far-reaching consequences.

The shipping potential applies to a number of port destination couples for transoceanic transport, but the melting ice is predominantly expected to benefit energy companies active in the Arctic and regional resupply. Oil and gas exports directly to energy-craving Asia could become a possibility through the NSR.

Calculations made by the shipping company Tschudi hints that for exports of liquid natural gas (LNG) from northern Norway to Yokohama, savings of up to 6-7 million dollars could be made using the NSR. The reduced distance would cut the transport time by 21 days compared to using the route through the Suez Canal, the company argues.[1] As much as this sounds promising, the amount of ships transiting the NSR is still at a comparably low level. High insurance premiums due to the risky operations in icy waters, additional costs in ice-breaking capacity and the need for having so called ice-pilots (experts on shipping in ice covered waters) aboard the ships transiting the NSR are a few of the reasons the shipping companies are still not embracing this "new" route.

Oil and gas reserves

About a quarter of the world's undiscovered mineral resources[2] are expected to lie under the Arctic shelf. 30 percent of the gas and 13 percent of the yet unfound oil is starting to look accessible for extraction, following the rapidly decreasing ice extent. As most oil reserves are thought to be found within Alaskan exclusive economic zone (EEZ), the major part of the gas is expected to be found in Russian EEZ. Most of these resources are situated offshore.

In 2011, data from a Russian governmental plan for the extraction of Arctic mineral resources was published by the daily newspaper Kommersant. The plan, developed by the Ministry of Natural Resources and Ecology, supplied data on assumed reserves in the northern Kara and Barents seas, believed to hold:

- 430,3 million tons of oil
- 9051,1 billion m^3 of free gas reserves
- 131,1 million tons of natural gas condensate reserves (Melnikov, 2011)

If proven, the amount of gas would be on par with the reserves of Saudi Arabia or almost all North American gas reserves (*BP Statistical Review of World Energy*, 2013) Furthermore, in September this year, the Head of Rosneft, Igor Sechin announced his company believes that "there is as much oil [in the Arctic] as Saudi Arabia has in its proven reserves" (Traufetter and Schepp, 2014). These comments were made a few weeks before Rosneft together with their American partner ExxonMobil struck oil when drilling in the Universitetskaya-1 well, in the Kara Sea. However, there are several difficult challenges that need to be tackled in order to gain access to the mineral riches.

One of the main questions revolves around when these resources will be obtainable for extraction, where some major structural obstacles stand in the way. According to the Russian Energy Charter from 2009, the oil and gas exploration is not going as quickly as the government would like (Carlsson and Granholm, 2013). Firstly, the ice-factor is far from gone, sometimes even aggravated, and will continue to be so for a long term ahead. The increased ice spread last year indicates that even though the long-term trend of retraction is apparent, ice could grow for certain periods, posing a threat to initiated operations. Moreover, the melting of the ice and the so called "ice-free" periods of the year could cause other

difficulties for those willing to initiate operations in Arctic waters. Floating icebergs pose a serious threat to shipping as well as drilling platforms as they risk harming the hull of the boats or the construction of the platforms. Last year, for example, the tanker *Nordvik* was struck by a drifting ice floe, which cracked open a hole in the hull and water started flooding in (Pettersson, 2013).

In order to meet these challenges, there is a growing demand for high technology in oil/gas development and shipping in Arctic conditions. The mentioned governmental plan indicates that investments from the oil/gas companies' side are expected to amount to up to 60-88 % (depending on the chosen variant) of the overall funding needed for the program up until 2030 (Melnikov, 2011). Partly, this funding is meant to cover costs of development or purchases of high technology for Arctic oil and gas exploitation. As stressed in the 2013 Strategy for the development of the Arctic zone until 2020, there is a lack of Russian domestic modern technology for the exploration and extraction of natural resources in Arctic conditions (Ministerstvo Regionalnogo Razvitiya Rossiyskoi Federatsii, 2013).

Most experience and technology for offshore oil and gas development is held by western companies. At the same time investments and involvement by foreign companies in the Russian energy sector is problematic. The high dependence on the exports of natural resources makes this sector an issue of national security, which has led to decisions limiting the participation of experienced foreign companies (Polonsky and Josefson, 2007).

Seen from the economic perspective, it could be considered somewhat paradoxical. An attempt for a real change/modernization of the Russian economy inevitably would have to allow competition in this sphere to make it more efficient and profitable, alongside with energy-efficiency efforts domestically. Foreign investments in a less restricted oil/gas sphere in the High North would increase, and transfers of high technology for extracting the Arctic resources with them. Below, this issue will be discussed more closely.

Is there a demand?

Forecasting future oil demand is a difficult task and available data is only indicative of future trends. OPEC's World Oil Outlook reports do however attempt to foresee the future in oil. According to OPEC, world demand will rise up until 2035, where the developing world is expected to stand for the major part of this increase, with China in the lead. While western demand goes down, the developing world will not only cover this gap, but exceed it (World Oil Outlook 2013). This increased demand, in connection with a weaker dollar, would serve as a basis for a price surge. In this context, it is interesting to view how Rosneft and Gazprom are targeting the Chinese as a major future Arctic oil and gas customer. China is an interesting export market for Russia, in view of the increasing Chinese demand for energy.

Using the forecasts of OPEC for future oil prices, while taking into account the plan for the state program for development of "new" oil and gas areas including the Arctic, we could get an idea of the future possible gains. In the World Oil Outlook for 2013 the price forecast

expects a nominal average price of around $110 per barrel in the period up until 2020 and $ 160 per barrel by 2035 (World Oil Outlook 2013). Looking at the current "mood" of the market however, these numbers are not set in stone. Statoil's head of field development in Norway, Ivar Aasheim, has said that "most people who make oil price forecasts see lower oil prices going forward than they thought a year ago" (*Reuters*, 2014). Even though the price drop Aasheim refers to is not considerable, it could "squeeze margins" for companies involved in the short term.

The oil price for the Arctic will play a special role, considering the high production costs. Comparing production costs in the Middle East that could go down to as low as $ 4 per barrel, production costs in the Arctic have been assumed to possibly reach $ 100 per barrel (Seidler 2012). Zabotin and Latchininsky assume that oil production costs for extraction in the Russian Arctic would not go below $ 50 per barrel and could shoot up as high as $ 200 per barrel (Latchinsky and Zabotin, 2012). Furthermore, as recent experience has shown, the *type/quality of oil* could also influence the price. The first load from Gazprom's first offshore Arctic oil platform Prirazlomnaya was sold with a discount, due to it being somewhat heavier than the normal Ural oil type (*Neft' Rossii*, 2014). As profitability is questionable in such cases, a mechanism for state subsidies in Arctic offshore development has been introduced – in case of a lower oil price, the level of the subsidies increase. Taking into account the recent fall in oil prices, almost reaching 80 $ per barrel, this price sensitivity is actualized.

The Russian state plan for resource exploitation is divided into four major steps. Only in the last period, the government expects to have full production in the Arctic fields (i.e. in 2026-2030).

Painting a scenario in a 15-20 year time, the plan suggests oil extraction between 40-80 million tons annually (Melnikov 2011). Compared to today's oil output, this is about 7.6 – 15.3 % of the 2013 oil production in Russia (Alpert, 2014). Experts at the consulting group IHS CERA have estimated that in order to reach a 15 % internal rate of return, the oil price needs to be $ 150 per barrel (Terekhova, 2013). As this is not expected for anytime soon, for Arctic development attraction to sustain, governmental support of some kind would be required.

World demand dictates project viability

Technological developments as well as infrastructural enforcements require time, but these are not the only examples of aggravating and retarding factors for natural resource extraction. If demand is insufficient, examples such as the failed Shtokman gas project will appear. This joint project was postponed in 2010 due to expected gas oversupply, and yet no movement to restart the work has been seen (*Oil & Gas Journal*, 2010). Unfavorable world market gas prices and the shale gas revolution in the United States meant that one of the most prominent intended export destinations was seemingly lost.

Furthermore, taxation of these oil and gas development projects has been seen as worryingly high by the industry. Gazprom and its international partners Total and Statoil did not manage to lobby for sufficiently lowered tax rates for the export of natural gas from the Shtokman field, which in addition to the changed outlook for the export market lead to the project being put on permanent hold.

Moreover, even though demand for fossil fuel is expected to increase, there is always the possibility of a break-through in the field of green energy. This could potentially change the picture dramatically for the energy sector and put more economic pressure on the oil producing world, including Russia.

The increasing concern in the western world over Russia using its energy exports as a political tool of exerting power over its customers, has spurred first and foremost European countries to diversify their energy imports. The recent events in Ukraine have further given support to the view of Russia as a non-trustable partner. Russia, understanding the situation, is therefore looking east for a potential replacement for its energy exports. Bulgaria's recent decision (after pressure from the European Commission and Washington) to discontinue the construction of South Stream, set to bypass Ukraine for gas deliveries to Europe, actualizes the need for Russia to reorient itself to the east (Barsukov, 2014). But such a process will take time, and demand great infrastructural developments to be realized. Energy Minister Aleksandr Novak noted long before the Ukrainian crisis that the European demand for gas would go down, at the same time as it increases in the Asia-Pacific region (Kezik and Dokukina, 2012).

In May 2014, Gazprom signed a contract with China National Petroleum Corporation (CNPC) on the supply of Russian natural gas to China for the coming 30 years (Mordyushenko, 2014). Interestingly however, the Russian side did not appear to leave the negotiating table as a winner. For almost ten years, the two countries had argued over the gas price. China, clearly understanding that it had the upper hand in the negotiations due to the uncertainty for Russian gas supplies to Ukraine and Europe, managed to land a lower price than the Russians had hoped for.

Still, the contract, which amounts to $ 400 billion, is historic and with this agreement we are witnessing a decisive shift of Russian energy exports towards the Asian market. For Arctic offshore developments however, this might become a halting factor. The gas delivered under the 30-year contract is not planned on being delivered from Arctic offshore sites, but rather from land fields in South East Siberia (*Kommersant FM*, 2014). The Head of the Analytical Department at the National Energy Security Fund, Aleksandr Pasechnik, argues that Arctic shelf development is no longer prioritized if one looks at the development strategy of the Russian oil and gas industry. Instead, according to Pasechnik, hard-to-recover resources[3] have gained interest amongst the leadership of the country (Bogdanov, 2014).

However, at the same time as Gazprom signed its contract with CNPC, CNPC also struck a deal with Novatek for the sales of LNG from the Yamal LNG production plant, amounting to 3 million tons per year (Staalesen, 2014b).

State Policies and Foreign Involvement

The Arctic zone of the Russian Federation should be used as "a strategic resource base of the Russian Federation, providing the solution for the socio-economic development of the country" (Sovet Bezopasnosti Rossiyskoi Federatsii, 2008). This is the first indicated priority in the Russian Arctic strategy, signed by Dmitriy Medvedev in 2008. The region is set to contribute to meeting the country's needs for hydrocarbon resources as the current ones, according to the Russian government, are being depleted.

The work on a governmental program for the development of the Arctic shelf until 2030 was soon set up. The program focuses on intensified geological/exploration activities in order to locate and start developing the most prominent sites (*Ernst & Young*, 2013, p.7). And the belief in the potential of the Russian North among the political elite is high. The Head of the State Duma Committee on Energy, Ivan Grachev, has stated that:

"The Arctic "storage" holds billions of tons of oil and trillions of cubic meters of gas. Arctic hydrocarbons from Russia can play a major role in supplying the world in the coming decades" (Korotun, 2014).

But first, the hydrocarbons need to be retrieved. In a completely new field of operations, requiring state of the art technology, this is not the easiest task. The Energy Charter from 2009 sets the goal for starting developing the European parts of the Arctic continental shelf in 2015-2022 and in the eastern parts of the Arctic in 2022-2030. In the charter, it is however noted that the exploration work is experiencing difficulties and that it is progressing slowly (Carlsson and Granholm, 2013). The lack of experience and technology for Arctic oil and gas extraction (noted in the most recent Arctic strategy from 2013 referred to above) also takes its toll, and difficulties might not end at the exploration stage, something which the Russians have come to learn during the project of the first Russian Arctic platform – Prirazlomnaya.

The story of Prirazlomnaya has been lined by difficulties and delays. The construction of the platform went on for just about 16 years, including a substantial pause in construction for some years due to a lack of funding. It is a second hand rig, the top built in 1984, which has been developed and reconstructed (some with second-hand parts bought from Norway) in order to meet the icy conditions of the Pechora Sea, where the dedicated oil field is situated (*Nord-News*, 2011) (Kravtsova, 2013).

Environmental organizations have severely criticized the project, calling it a danger to the Arctic environment and wildlife. Despite this, Gazprom, which operates the oil rig, proudly

informed the world through a press release on April 18, 2014 that the first shipment of black gold had been loaded onto a tanker (*Gazprom Neft*, 2014).

Due to the need of complex technology for offshore Arctic exploration and extraction, the costs of operations are higher than in warmer waters. Heavy investments are required, but other associated costs for the Russian state companies can also be distinguished. In order to extract oil and gas in Arctic offshore conditions, in addition to monetary funding, Russia either needs to pay with:

- Time
- Lifted/reduced restrictions for foreign involvement
- Ecological risk-taking

These "payment methods" are not necessarily mutually exclusive. For example, by not having paid enough *time*, Russia has either *lifted or reduced restrictions* for foreign participation to a larger extent, or decided to disregard some *ecological risks* in favor of a quicker road to extraction. For Prirazlomnaya, which is the only example of a completed offshore extraction project in the Russian Arctic to date, it goes without saying that time has been the "currency" mostly used. However, judging from the criticism of the pre-mature relocation of the platform from its construction dock in Murmansk to the oil field in the Pechora sea (in order to avoid increased environmental requirements expected to come into force at a later time), as well as the usage of second-hand construction material, *ecological risk* has evidently also been part of the deal. Maybe it's no wonder that already two months after its first dispatch of oil, a modernization program of the platform has been initiated (Pettersen, 2014).

At the current moment, Rosneft and Gazprom, holding the licenses to develop the sub-oceanic areas of the Barents, Kara and Pechora seas, do not have the technological resources required to develop the Arctic shelf single-handedly (Carlsson and Granholm, 2013). But the regulatory restrictions on foreign involvement are hampering possibilities for greater involvement by foreign companies. Still, despite the restrictions, Rosneft and Gazprom continuously seek cooperation with foreign partners to cover the technology gap.

National security and foreign involvement

The Security Council of the Russian Federation is the consultative state authority, developing the policy decisions on national security issues. Due to the one-sided economy of the country, with an overwhelming reliance on the exports of hydrocarbons, the energy sectors have been declared a national security interest, which means it also ends up on the table of the Security Council. For the last 10 years, the state has increased its ownership and control of the sector, and according to analysts at Gazprombank this share will not be reduced in the foreseeable future (Starinskaya, 2013).

Extensively allowing foreign participation in this economic sphere would, following the logic of the Security Council, give foreigners a tool of control over the Russian economy and ultimately pose a risk to the security of the country. Amongst the political elite, there is

mistrust towards in particular western foreign partners, which in many instances are viewed as malicious tools of their home countries governments. The *Siloviki* (politicians or influential stake-holders from the security services or the military) have increased their power positions during Putin's rule. The ministerial cabinet has experienced a shift from liberal to conservative politicians, which goes along the lines of increased state control and hesitance towards the outside world (Larsson, 2010, p.127). Resources need to be protected in order for Russia to maintain independent - such is the leading thought (Larsson, p.176). It's furthermore important to note that those with more "liberal" (in the Russian political sense of the world) background within the administration also support this idea, resulting in the energy policy taking a nationalistic turn.

Russian law only allows foreign ownership up to 49 percent in companies/projects in the energy sector. However, according to former Deputy Energy Minister Vladimir Milov, Vladimir Putin has another "psychological limit" of 20 percent (Larsson, p.170). The Rosneft strategic cooperation with American Exxon Mobil and the joint venture they set up for developing the Arctic shelf, gave Exxon 33.3 percent of the project, which could represent some kind of compromise between the official and unofficial limits.

In 2010, government officials confirmed that foreign interest in Arctic shelf projects had gone down. The restrictions on foreign participation was admitted as being one of the causes, but it was also underlined that part of the lost attraction had to do with the general economic situation in the world.

The view on foreign technology and know-how is ambiguous in the Russian political and energy expert community. Andrey Denisov, former Deputy Minister of Foreign Affairs, has argued for the legitimate right of foreign companies to work on the Russian market and a more liberalized energy market. German Gref, Head of Sberbank and former minister of economic development, has even gone so far as saying that Rosneft should be privatized. "Stability […] can only be guaranteed by private investors", he argues (Triebe, 2013).

There are others however, who see the usage of western shelf technology as something inherently negative, and this group appears to be growing stronger. Vladimir Drobyazko, Vice President of the Russian Union for Oil and Gas, has argued that in the long run, using western technology for developing the Arctic shelf would place Russia in a position of dependence vis-a-vis its competitors, instead of developing domestic technology (*Izvestiya*, 2013). Such views have another strong supporter within the Russian government. Dmitriy Rogozin, Deputy Prime Minister, responsible for the defense and space industries, is a loud proponent for strong state influence in the economy of the country and nurtures a sharp skepticism towards foreign involvement in the energy spheres. An example of this is the decision on domestic machine tool production which was announced by Dmitriy Rogozin in February (TwitLonger, 2014). The core idea of the suggestion is that any imports of machine tools would only be allowed in case there is no equivalent alternative produced in Russia by Russian companies. For Arctic offshore development, this would have significant implications, not least in the field of shipbuilding.

In this context, the voiced Rosneft plan of opening a shipbuilding center in Murmansk becomes an interesting issue (*RIA Novosti*, 2014a). This plan would however first require oil to be found in the Kara Sea. Exploration work in the Kara Sea is done together with the American oil company ExxonMobil, which is working closely with Rosneft on several projects aimed at the Arctic subsurface resources (Staalesen, 2013b). In the end, this means that at the same time as Rosneft is proclaiming its dedication to partake in the build-up of Russian domestic operations, the money that allows them to do this, comes from abroad. In the wake of the sanctions however, Rosneft has said it could replace the foreign equipment used for exploration and extraction, with domestic production. If this will be possible or not, remains to be seen.

Foreigners and ecology

The importance of foreigners in the Russian oil and gas sphere is decisive for the environmental protection of the Arctic region. Rosneft Vice President Mikhail Leontev for one has said that for ecological considerations in its Arctic endeavors, Rosneft is using the experience of its western partners Exxon, ENI and Statoil. He argues that thanks to these foreign companies' obligations regarding environmental awareness and protection, Rosneft is also maintaining good levels of environmental safety of Russian Arctic development projects (*Gazeta.ru*, 2014).

The environmental community however is increasingly worried. According to them, unsatisfactory attention is given to the ecological aspects of the endeavors of Gazprom, Rosneft and its foreign partners. The director of the Arctic program of the World Wildlife Fund asserts that there is no available technology for the liquidation of oil spills "in the ice, on the ice or under ice" (Pyzhanova, 2013). Such worries were vividly expressed through the Arctic Sunrise stunt last year, when Greenpeace activists tried to board Gazprom´s Prirazlomnaya oil rig in the Pechora Sea.

But a "no-go" for oil and gas development in the Arctic is highly unrealistic. Even non-littoral Arctic states have openly concluded this. Swedish Foreign Minister Carl Bildt commented the issue by saying it's *pointless* to ban oil extraction in the Arctic. International efforts to address coming challenges in connection to these developments have however been strong, predominantly through the Arctic Council, the leading international institution for Arctic cooperation and discussions. This cooperation has experienced a widely acclaimed exceptionalism in international politics, where the Arctic states have actively avoided differing opinions and conflicts not having to do with Arctic matters. This pragmatic approach has underpinned the successes in signing legal agreements for the Arctic region.

In 2011 a Search and Rescue agreement was signed by the eight Arctic states of Canada, Denmark, Finland, Iceland, Norway, Russia, Sweden and the United States of America, delimiting the responsibility areas and coordination requirements for such operations. Two

years later, the second and latest agreement came into force – this one set out to ensure preparedness for oil spills in the Arctic.

The events in Ukraine have however not left the Arctic region untouched. Cold winds of distrust are causing joint cooperation projects and exercises to be put on hold. Furthermore, western sanctions have given rise to sharp statements from the Russian leadership, which promises to counter sanctions as they escalate. So far the counter sanctions have not yet come to touch areas connecting to Arctic oil and gas development. Instead, it's the West which has put their aim at halting the Russian Arctic exploration and development.

Rosneft Head Igor Sechin, fell victim to American sanctions and US President Barack Obama threats of targeting whole sectors, including the energy sector, have been realized. Firstly, both Rosneft and Novatek ended up on the sanctions list, soon to be follow by Gazprom and Gazpromneft. On June 29, the US introduced a ban on providing technology for deep-water, shale, and Arctic exploration. These measures were a few months later broadened to include exports of goods and services for activities in these spheres (Baker and Higgins, 2014). This is a distinct blow at the Arctic oil and gas development, which for the time being has put western involvement to a halt.

Even though the western oil and gas companies still haven't given any signs of abandoning the Arctic, these sanctions make it increasingly difficult for them to continue their efforts.. Even after the sanctions hit, Rosneft's partner Exxon used a loophole in the law which at first made it possible for them to start drilling for Arctic oil. However, after this possibility was discovered by the US it was closed, tightening the sanctions and making them stricter (Katz, Lakshmanan and Carroll, 2014). However, Exxon views the High North as their new Big Area, and is likely in the Arctic game for the long run. According to analyst Anthony Ruben at Inflection Point Consulting, Exxon's CEO Rex Tillerson expects the sanctions to be lifted in less than a year (Hill, 2014).

Keeping in mind that the western companies teaming up with Russian state oil and gas companies are the ones securing the environmental standards for Arctic offshore development (be they sufficient or insufficient), the consequences are potentially devastating. There is little reason to believe that Russia would simply halt its endeavors into the Arctic as a result of western companies being forced out. President Vladimir Putin's remarks in May about the Russian oil and gas companies being ahead of their foreign partners when it comes to technology for protecting the environment is alarming (Nilsen, 2014). The mere fact that the Russian state energy companies themselves claim to have good standards thanks to their cooperation with western companies further undermines such claims by the Russian President.

The power of state companies – Igor Sechin

Since the wild 1990s in the newly capitalistic Russian Federation, economic power had been centralized to a chosen few individuals, who already at an early stage saw the possibilities of making big money in connection with the transition from command to market economy and the privatization process of previously commonly owned state property. Relations between these individuals, better known as oligarchs, and the government was less than simple, as shown by many experts. What is of interest here is what grew out of these economic power centers with the entry of Vladimir Putin on the scene as the President of Russia at the turn of the millennium.

Putin's rise meant the start of a new era of state capitalism, something that became crystal clear when one of the oligarchs broke the rules set by Putin in the very beginning of his first term. Mikhail Khodorkovskiy, one of the oligarch-entrepreneurs and owner of the oil company Yukos, spent 10 years in federal prison for challenging the superiority of the political leadership and attempting to open up the strategic oil market for foreign companies, when he sought to sell shares of his company to American counterparts.

The current Head of Rosneft, Igor Sechin, has been a companion of Vladimir Putin's since the 1990s, and has grown to be one of the most trusted people by the President. Some have named him the second most influential person in Russia today, a result of many years of close cooperation and loyalty to Putin and his control over the enormous oil company.

Not long before joining Putin in the Kremlin, Sechin started to contribute to the growth of Rosneft. Appointed chairman in the company in 2004 he became a prominent voice with an access to the President, which no one else had (Reznik, Bierman and Meyer, 2014). Mikhail Khodorkovskiy's Yukos was taken over by Rosneft the same year and Sechin was the one who organized the deal. According to Khodorkovskiy, this take-over (through fairly arbitrary interpretations of the law) was a well-planned stunt through fairly arbitrary interpretations of the law. Furthermore, the ex-oligarch has publically pointed out Sechin as responsible for him being sent to prison.

The path towards a bigger state ownership in the strategic energy sector through the Yukos deal had started and shortly after Sechin had taken over the seat as the Head of Rosneft, the Russian-British company TNK-BP was acquired. According to Putin's Press Attaché Dmitriy Peskov, Sechin is a strong proponent of state capitalism – i.e. heavy involvement of the state in the economy, but coupled with a "free-market approach" to business (Reznik, Bierman and Meyer, 2014).

Lobbying in action

For Arctic offshore drilling, Rosneft and Gazprom are the only ones allowed access to the shelf, and any other company interested in participating in the hunt for the Arctic oil and gas, needs to team up with either state company. As a result of the government not being content with the speed Rosneft and Gazprom are keeping in developing the Arctic oil and gas, calls

for liberalizing access to the shelf have been made. In the end of 2012, Vladimir Putin asked the government to investigate the possibilities for liberalizing the shelf.

Already before this, Igor Sechin and Gazprom President Aleksey Miller had sent the President a letter, describing why liberalization would cause harm to the governmental shelf policy:

"[the] adoption of such initiatives is likely to cause substantial harm and a slowdown in the implementation of the state offshore policy, and lead to serious problems in the relations with the foreign strategic partners of the Russian state companies", they wrote (*Gazeta.ru*, 2012a).

These ideas were reiterated in another letter by Sechin after the President's decision to have the government investigate the issue. In the second letter, Sechin went even further, stating that Rosneft would expect compensations from the government if it went through with its intentions (*Gazeta.ru*, 2012b). The question was discussed over the course of 2013, with various suggestions going back and forth. In April 2014, the Ministry of Energy had taken a clear decision – no private companies are allowed on the shelf (Evplanov, 2014).

"Liberalization of access to the shelf is the right trend", Aleksandr Novak, Minister of Energy, said in an interview 18 months before the decision had been taken, "the secret of Norway's success lies largely in progressive and careful liberalization of the shelf, but that process did not take one, nor two years to accomplish" (Kezik and Dokukina, 2012). It was understood, that neither would it take "one or two years" for Russia. The lobbyism of the two state energy companies had scored a victory.

As if a speedy development of the shelf was not enough, the government also sees the opportunity to turn the development of the Arctic resources into a driver of domestic industrial build-up in the spheres of oil and gas extraction in difficult conditions. Deputy Prime Minister Dmitriy Rogozin wrote an article in Rossiyskaya Gazeta in March 2014, in which he argues that the Arctic has the potential of becoming a catalyst of Russian industrial modernization (Rogozin, 2014).

In light of this piece, the strife for extensive use of Russian technology and workforce supporting Russian industries and employment becomes clear. By limiting access for foreign companies, Rosneft and Gazprom would ultimately need to use domestically produced technology. This was the core idea of the law proposal presented by the Russian State Duma last year, fixating the required share of Russian equipment used in shelf development to 70 %. Once again, the suggestion was not well received at Rosneft, which sent a letter to the Duma in December. Company Vice President Larisa Kalanda wrote:

"Fixation of norms for obligatory participation of Russian project organizations in all types and stages of work on the shelf could completely hinder extraction of minerals from in these fields." (*Izvestiya*, 2013)

State private partnerships in Russia differ from such cooperation in Europe. In Europe consultation centers are set up which includes private and state representatives. In Russia however, such functions are carried out by ministries and other state institutions (Shokhin, 2011, p.28). A close connection to the state thus facilitates the work of any company (even those with majority stakes owned by the government), aiming to influence the political direction. Aleksey Miller, as well as Igor Sechin, has close ties to Vladimir Putin since the nineties, when they worked together with Putin in Saint Petersburg.

In addition to the December letter by Larisa Kalanda, Sechin wrote another letter in the end of the same month, in which he addressed Putin about the complicated and time-consuming bureaucratic red tape, which the company is required to fulfil for shelf development (*Kommersant*, 2014). Furthermore, Sechin pointed to the need for Rosneft to be able to use the expertise and equipment of their foreign partners more extensively. Putin's response was appreciative, giving the government the task to oversee bureaucratic procedures with the prospects of facilitating viable exploration and extraction work on the shelf. It did not take long before things started to happen. On February 21 this year, the Minister for Natural Resources and Ecology ordered an Interdepartmental Commission to be set up, with the aim of removing administrative barriers for subsoil development (Ministerstvo Prirodnykh Resursov i Ekologii, 2014). The commission includes concerned federal executive agencies and major Russian oil and gas companies, including Rosneft and Gazprom. Interestingly, the tricky and time-consuming bureaucracy had been criticized earlier by the private company Lukoil, without any success.

It appears as the advent of Igor Sechin as President of Rosneft, with his unrivaled influence on the executive power as well as Rosneft's transformation into the world's biggest listed oil company after the TNK-BP acquisition, has not just meant a stronger position for Rosneft, but a stronger position for the Russian oil and gas companies and a positive development for energy extracting field as such. Obviously there are ways other than letters that can be used to lobby one's cause. Unofficial meetings and agreements between Sechin and Putin are likely components of the whole lobbying efforts and successes. But as the tip of the lobbying iceberg, they convey the The ideas and suggestions put forward in the letters, and later government actions which closely seem to correlate with these ideas and suggestions, indicates a strong likeliness that Rosneft has influence on the developments of regulations and policies. Valeriy Nesterov at Sberbank Investment Research believes that based on the broad benefits for the whole oil and gas spectrum Igor Sechin's lobbyism could entail, Rosneft will be able to successfully bring about changes in rules and legislation for shelf development (*Kommersant*, 2014).

Drivers for Arctic engagement

"*Shelf extraction of oil and gas needs to start already in 10-12 years*."

"*Postponing the development of the Arctic region's resources, means that Russia might find it difficult to find demand for its future production*."

"*Untimely development of Russian Arctic gas risks leading to the United States or Australia covering the supply for the perspective Asia Pacific region, whose demand for gas is expected to rise in the coming years*." (Terekhova, 2013)

Such arguments were presented at a meeting at the Ministry of Natural Resources and Ecology in December 2013. The factor of a time-dependent gas demand would give one answer to the reason for the government's apparent rush towards the Arctic riches. In order to meet this demand, the government has attempted to increase the incentives for gas exports. Gazprom lost its monopoly on gas exports in the end of last year when Putin signed a law set out to liberalize LNG exports for those companies which build plants for LNG production (*RBK Daily*, 2013). Novatek and Rosneft are now the two most prominent contenders for exporting liquid natural gas. The opening of the Northern Sea Route means a shorter route to Asia and European countries have voiced their interest in buying Russian Arctic LNG. The French company Total is already involved in Novatek's Yamal LNG project with a 20% share, and Spanish Gas Natural has agreed to buy 2.5 million tons of LNG (Barsukov, 2014).

But according to Aleksandr Kudrin, Head of the Directorate for Strategic Energy Studies at the Analytical Center under the Government of the Russian Federation, the Arctic shelf is far from the only alternative for depleting resources on land:

„There is the question of choosing between the shelf and the development of hard-to-recover resources. In the Bazhenov Shale [West Siberian land area] resources are not less, but most likely greater than on the shelf. Taking into account the existing infrastructure in Western Siberia, the operations costs may be much lower than for implementing offshore projects" (Andrianov, 2014)

Acknowledging this, other factors than securing a new resource base to replace the current ones (which according to the Russian government are depleting) need to be considered. In 2010 Sergey Donskoi, then Deputy Minister of Natural Resources and Ecology said that there have been great oil discoveries on land, and certainly will be in the future as well (*Neft' i Kapital*, 2010). Furthermore the shale gas revolution in the United States is expected to spread further internationally. According to BP forecasts, Russia could become one of the world leaders in the extraction of hard-to-recover resources. Obviously taking their own forecasts with great seriousness, BP, which owns 19,75 % of the Rosneft shares, signed a deal with Rosneft at the end of May on developing shale oil in the Domanik formations, located in the Volga-Urals region (Farchy, 2014).

Still, as Donskoi has pointed out, the Arctic resources make out "unique hydrocarbon reserves, which will be needed both by the country and the world" (Pyzhanova, 2013).

There are furthermore indications, pointing towards Rosneft and Gazprom not having any primary interest in Arctic offshore projects. The risks are extremely high and profitability is unsure and expectedly dependent on state subsidies. Experts who have spoken to the upstream magazine ROGTEC assert that the incentives for the state companies' involvement in Arctic offshore projects merely lie in the possibility to attract capital (*ROGTEC Magazine*, 2013, p.66). The long-term contract signed by Rosneft and the Chinese state oil company CNPC last year, is a vivid example of how interest in Arctic oil has attracted investments. The contract, amounting to $ 270 billion, is set out to supply China with Russian oil over the course of the next 25 years (Rudnitsky and Bierman, 2013). A pre-payment of $ 20 million has been made by CNPC, which Rosneft is planning on investing in the strategic projects. At the same time as such investments are made, the CNPC is furthermore teaming up with Rosneft for developing sites in the Barents and Pechora seas (Staalesen, 2013a). One could argue that this is a win-win situation. Russia gets the capital needed for their state oil and gas companies, while China increases its presence in the Arctic region.

Nina Pusenkova, at the Institute of World Economy and International Relations in Moscow, has pointed to Rosneft's history of reaching out to the Chinese for investments in their operations, and that such practice continues (Pusenkova, 2013, p.21). Due to the large debts Rosneft incurred through the TNK-BP take-over, the company is in desperate need of money to start paying off that debt. The above mentioned oil agreement with CNPC from last year should be viewed as a part of such a development. According to the insurance company Lloyd's, investments in the Arctic could potentially exceed $100billion (Andrianov, 2014).

Furthermore, the support the state energy companies receive from the government is not for free. Sometimes, this manifests itself by the government forcing the state companies to embark on projects that do not generate any profit and which might leap out of their set business strategy (Larsson, p.139). The profit margins are very small (if at all existing) for any Arctic offshore projects, but as Robert Larsson in his book *Rysk energimakt* (Russian Energy Power) clearly puts it, "[…] profit maximization has to stand back for other societal goals or personal agendas" (Larsson, p.153). The state energy companies are not normal business entities, but tools of Russian policy used to reach domestic and foreign policy goals. The fact that Gazprom's first oil load needed to be sold with a state-supported rebate, and the readiness of the state to give such support, testifies to a strong political ambition. On the one hand, in terms of oil and gas prices, the current levels are not high enough to serve both the economic goals of the government and the extracting companies. If taxes and fees are kept at current levels, the profitability justifies neither exploration nor extraction. On the other hand, if the taxes and fees are reduced, there will not be much money that could go into the Russian state budget. Interestingly, when we now see a sharp decline in oil prices which puts an even bigger question mark over profitability, and when sanctions are hindering influx of western

technology and money, the Russian leadership appears to focus on the region even more intensively.

Not merely economy

Against this background, the rush towards the Arctic appears to revolve not only around the perspectives of the region becoming the new mainstay of the Russian economy, due to its doubtful profitability, but about something more than that. Based on recent developments, one could consider several alternative political drivers behind the development of the Arctic region.

One aspect is image and prestige. There is an inherently perceived prestige in being one of the first countries that is able to overcome the difficult task of getting to the northern shelf resources. Dr. Pavel Baev at the Peace Research Institute in Oslo, argues that this prestige is "closely intertwined" with the economic drivers for developing the region (Baev, 2012, p.6). President Putin has spoken warmly of Arctic development for many years, which has also resonated within the governmental apparatus and amongst its ministers. In the state approval document for initiating the state program "The socio-economic development of the Arctic zone of the Russian Federation for the period up to 2020", it is indicated that expected results from the program is to increase Russia's international prestige (Pravitelstvo Rossiyskoi Federatsii, 2014, p.2). As Larsson argues, the Arctic is a way back for Russia to a great power status – through energy (Larsson, p.156). The influence and presence in the Arctic which faded away together with the break-up of the Soviet Union (a historical event which Putin sees as "the greatest geopolitical tragedy of the 20th century) could be restored. Dr. Sergey Medvedev, a political scientist at the Higher School of Economics in Moscow (which has previously been called a "moron" by President Putin after Sergey Medvedev suggested making the Arctic a wildlife sanctuary under international control), supports this suggestion, saying the development of the Arctic is "imperialism" aimed at contributing to the reassembling of the Soviet Union (Mackinnon, 2014).

In the Arctic this "Soviet restoration" is expectedly going to be less frictional than the efforts of increasing Russian influence through the Eurasian Union, the scope of which already before its initiation has been watered down significantly due to a fear in Belarus and Kazakhstan of too much Russian influence.

Secondly, the development of the oil and gas resources of the Arctic could have general economic significance, as it could be a driver for Russian domestic industrial production (Andrianov, 2014). In addition to the oil and gas projects, this could contribute to positive socio-economic development in the country (especially its northern parts) and contribute to better employment rates. For example, Artur Chilingarov, President of the Polar Academy, Senator of the Federation Council and newly elected board member of Rosneft, has in comments about the Yamal region said that energy development projects and the Northern Sea Route will "increase the prestige of the region and supply the inhabitants with necessary comfort of living and work (*Yamal-region.tv*, 2012). It is obvious however, that these various

aspirations do not go hand in hand. The government wants development to take place soon, but one does not own the appropriate technology for it. When the state companies, realizing their own limitations, point to the fact that they need foreign involvement for a more rapid development, they get criticized by the government for being overly reliant on western expertise.

Thirdly, one could also note a trend that is becoming increasingly evident. For the last year, with intensified attention given to the last six months, President Putin has given an increasing amount of orders boosting Russian military presence in the High North. Putin has called for a united military command to be set up in the Russian Arctic by the end of 2014. A permanent military base has been set up on Kotelny Island (part of the New Siberian Islands archipelago), which according to the Head Commander of the Northern Fleet Vladimir Korolyov will be equipped with missile systems and anti-aircraft defense (Staalesen, 2014c). More such bases are also expected to come at various points along the Russian northern coastline as well as on Russian islands in the Arctic Ocean. For example, the airfield Rogachevo (Amderma-2) on Novaya Zemlya has undergone renovations and a group of MiG-31 is reported to be based there (Krivoruchek, 2014). At a ministerial meeting in October, Defense Minister Sergey Shoigu said that already by the end of 2014, Military units will be deployed along the whole Russian Arctic coast, from Murmansk to Chukotka (*RIA Novosti*, 2014b). Airfields are being restored and radar will be set up during the course of the year. Shoigu has furthermore announced that in 2015 the Russian military will be ready to face intruders both from the north and the east (*RIA Novosti*, 2014c).

The military is there to "protect the security and national interests" of the country, Putin has reassured (Mikhailin, 2013). For the most part, the rhetoric has revolved around protecting the oil and gas development activities, as well as the increasing number of ships transiting the route. But since the US has set out to become more actively involved in Arctic matters, this has prompted a changed mood. At a Security Council session on April 22, Putin said that more frequently, interests of the Arctic states are either intersecting or colliding. Furthermore, he noted that interest from non-Arctic states towards the region is rapidly increasing. These developments mean increased risks for Russia, he argued, which need to be met in order to stay ahead of other actors in the Arctic (*Kremlin.ru*, 2014).

The planned increased military presence could be seen as purely revolving around securing geopolitical interests along the northernmost border. Referring to the protection of the emerging commercial activities would this merely be a way of maintaining pure economic concern. At a conference in March, at which the protection of national interests and maintenance of safety in the Arctic region was discussed, the Commander-in-Chief of the Russian Navy, Viktor Chirkov, claimed that the Polar Regions potentially could be used to form new threats towards Russia. According to Chirkov, the mobile segment of the American anti-ballistic missiles system could be applied in the Arctic region and pose a serious threat to the military security of the country (Banko, 2014).

The melting ice is without doubt erasing what was once a natural geographical protection against attacks from the outside. Putting on your geopolitical glasses, it makes logical sense to deploy military security installations, considering the *perceived* threat from the announced American increased presence in the area. Moreover, the mood on the global political scene is worsening in the wake of the Russian conduct in Ukraine. After the annexation of Crimea and the Russian involvement in the armed conflict in Eastern Ukraine, relations are on a free fall. The calls for extended Russian military build-up post-Crimea should at least to some extent be seen in the light of this changed situation in West-East relations. As Putin recently said during the above mentioned Security Council meeting, Russian conduct in the Arctic needs to take into account the dynamically changing foreign political environment (*Kremlin.ru*, 2014). Perceived threats are however not the same as actual threats, even if one might act on the perceived ones. If there is an actual military threat towards Russia in the Arctic is highly debatable. So far the Arctic capacity of the main "headache" for Russia, the United States, is by far outclassed by the Russians.

Moreover, Russia has wants to extend its economic zone further north in the Arctic Ocean. Evidence supporting the Russian claim will be submitted to the United Nations Commission on the Limits of the Continental Shelf (CLCS) in spring 2015. The country earlier applied in 2001 but then the CLCS demanded further evidence to prove the Russian case (Staalesen, 2014a). But Russia is not alone in wanting the north. There are competing claims and a decision on delimitation is not expected for several years to come. In the meantime, Russia's military, in addition to protecting the commercial activities in the area and deterring foreign military, is to ensure that no other power attempts to make the contested waters "theirs". Vladimir Putin has declared that Russia *will* accept the judgment of the CLCS when it arrives, but what would happen in the case of a decision in favor of the opposite claims is yet unclear. The annexation of Crimea proved to the world that Russia is ready to disregard international law and results of historic events in order to satisfy its national interests. If or how this praxis will apply to the Arctic region, is something which is left to be seen.

Conclusion

Drivers

The economic viability of developing the Arctic region, as well as the idea that it could substitute the shrinking current resource base, is questionable. The investments required for offshore extraction in the High North are huge and profitability without governmental subsidies is uncertain. Experienced difficulties in exploration and extraction means that the time needed for turning the Arctic into a commercially apt development site for natural resources, with the current policy and pace, is expected to be long. Furthermore, lower oil prices which we are experiencing at the moment, could throw a spanner in the works for the oil companies. Profitability under such circumstances is even more questionable and the government would have to provide support for the companies.

This does not however appear to discourage the Russian efforts of landing the Arctic riches. Rather the government is unhappy about the developments towards this is not fast enough.

One apparent reason for the government's eagerness to extract gas from the continental shelf is so that Russia will be able to supply the Asia Pacific market "in time" before demand it is already met by American supply of shale gas. The liberalized LNG legislation has also indicated the state's readiness to do something in this regard. Furthermore, China is showing an interest in the northern resources and has invested in both Novatek's and Rosneft's' Arctic projects, including preorders of Arctic energy resources.

However, considering the existence of potential development sites on land that require less investments and technology (as well as reduced environmental risks), the pure commercial drivers for a prompt development of the Arctic become less obvious. Gazprom's historical gas deal with CNPC in May did furthermore not include deliveries from the Arctic, which has become down-prioritized in the oil and gas development strategy in favor of hard-to-recover resources.

This dubious commercial nature of the Russian Arctic ventures rather supports the idea of there being other likely drivers behind the efforts of the Russian state than the strict extraction of resources.

Going into a period of weaker growth, the Russian government is faced with the difficult challenge of finding a remedy for its one-sided economy. One suggested ingredient to this cure is to let the Arctic serve as a general economic lift for various domestic industrial complexes and contribute to the socio-economic development of the country, as argued by e.g. Vice Prime Minister Dmitriy Rogozin. This also goes in line with the 2008 and 2013 Arctic strategies, in which it is stressed that development of the Arctic should have positive socio-economic consequences for the northern regions, as well as for the country at large.

Following the logic of the government, accelerated exploration and extraction work would implicate earlier economic advantages from these projects. But the consequences of such acceleration might not be all too positive; using domestic industrial technology, which lags behind its foreign modern analogies, rather risks hampering the oil and gas development and safety of operations. Therefore, the fact that Rosneft claims that it could replace their use of foreign equipment with Russian production in a matter of merely three to four years, is worrying.

Another driver not to be underestimated is the importance of prestige aspects of developing the High North, connecting to the struggle of restoring the respect and influence which was lost at the break-up of the Soviet Union. Prestige and image should be seen as supporting factors for the continued path towards extraction, despite the questionable commerciality – something which is supported by strategy documents as well as experts' opinions.

Finally, and maybe the most topical issue, is the geopolitical or military security aspect. The Ukrainian crisis has shown that there (still) are fundamental differences between the West and Russia. In the Arctic, Russia has viewed increased attention to the Arctic by the US with suspicion. The vastness of the area, and the comparably (to the size of the Russian Arctic) low presence of security arrangements and infrastructure, makes the Russian Arctic a weak spot, keeping in mind the difficulties of controlling the area. At the same time as the military is portrayed as a guarantor for the safety and security of the oil and gas development in the High North, it should also be able to discourage other powers from engaging in any of the contested sea areas that the CLCS is supposed to decide the faith for. How much Putin's assertions about Russia respecting the outcome of the CLCS's decision mean is however for the future to tell. The country's recent bad track record on the respect of international law it is a signatory to gives food for thought. As much as the Arctic is different from Crimea in many ways, one can only hope that the Russian conduct in Ukraine does not set a precedent for the future of the High North.

State companies' involvement

For Rosneft and Gazprom as the only companies allowed access to the shelf, the Arctic ventures attract capital investments. Even though profitability so far has proven low for shelf development, the two state companies who are both in great need of money to pay off debts and to finance new endeavors, maintain an interest in the region.

Potential ways of "going around" the time factor by allowing greater foreign involvement into Arctic projects are stalled by the fear of first and foremost western influence in the energy sector. In order to conciliate the government's calls for speedier development, the state companies are forced to be the "sensible voice" in the development of the Arctic continental shelf. The economic realities for offshore oil and gas extraction are clearer to the oil and gas companies, with a lack of investments and domestic expertise and technology, which is evident in their lobbying, e.g. for eased restrictions on including foreign companies in exploration and extraction work.

The ascent of Igor Sechin as the President of Rosneft, and the company's transformation into the world's biggest oil company, has made the state companies' voice stronger and seemingly more influential. Sechin's unrivaled access to Putin, his political background in the Kremlin and the White House, in addition to his involvement in Rosneft for a decade has given him the understanding of both the political drivers and the commercial realities of developing the High North. Having earned Putin's trust; when Sechin argues for reducing red tape or allowing foreigners to take part in the development work of the shelf to a greater extent, the President listens.

The letters sent by the state companies to the government and presidential office (and subsequently leaked to the media) are one visible way of the energy companies' lobbyism, of which results that seemingly correlate with the ideas put forward in the letters can be observed. As letters undoubtedly are just the tip of the lobbying iceberg, keeping in mind

likely informal interactions and agreements between the leadership of the state companies and the country, the issues they address are indicative of the positions and priorities of the state companies.

Successful results for the state companies can be observer in the continued policy of not allowing licenses for developing the shelf to others than Rosneft and Gazprom. Another palpable outcome that likely can be derived from the lobbying of Rosneft is the Interdepartmental Commission for removing administrative barriers for subsoil development, in which the state companies have been invited to participate. A contributing factor in this regard is arguably the unison view between Sechin and Putin about the importance of state involvement in the country's economy, where Rosneft becomes a useful tool reinforcing the state capitalistic policy direction.

Endnotes

[1] Calculations consider time charter, fuel consumption, Suez tariffs, and NSR tariffs.

[2] Postulated volumes of energy resources that have yet not been proven through drilling.

[3] *"Hard-to-recover resources"* is a broad term used in the Russian energy community to describe resources that are difficult to extract and (according to the energy companies) require government tax breaks. Shale oil/gas and conventional oil are examples of resources included in the definition.

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