

The Eastern Gas Programm is to be corrected...

Gas prices will be decreased by means of budget subsidies

Tags: [Kovykta](#), [RUSIA Petroleum](#), [East Gas Program](#)

The Russian Prime Minister V.Putin hold a fuel and energy meeting in Yuzhno-Sakhalinsk, where he ordered Minenergo and Minprirody, in cooperation with other concerned agencies, Gazprom, and the regional authorities of the Russian Federation to prepare corrections for the Eastern Gas Program.

First, they are to elaborate the clear and long-term pricing policy. The prices for energy resources and for natural gas must not undermine the competitive regional status or bring additional burden for local budgets, business and the population.

Currently, the gas supply resource base in the Far East is, in fact, limited by abilities of two PSA operators, Sakhalin 1 and Sakhalin 2. Sakhalin 1 Operator, Exxon Neftegas Limited, sells gas by itself to the Khabarovsk Krai companies (Khabarovskkraigaz and Khabarovskenergo). However, its production-increasing resources are now limited. The Chayvo investment decision has to be made, and Exxon Neftegas does not want to sell gas on the domestic market, counting for export to China. In this situation, the only remaining source is the gas of Sakhalin 2, not used for loading of the LNG plant. Its estimated volumes are 3-4

bcm annually.

But the problem is that, under the Product Sharing Agreement between the state and the Sakhalin Energy Consortium, the gas can be sold only at prices which correspond with Gazprom's export contracts with the West European companies. In the first quarter of 2011, these prices are significantly higher than \$300/mcm. Whatever the price of electricity on Sakhalin would be, it is clear without any calculations that such price of gas would not come in line with economic development and social stability in the region.

Also, there was a Far East gasification scheme based on the Russian share in the Sakhalin 2 production. Gazprom would have been authorized by the government to get gas from Sakhalin Energy, to deliver it to consumers at the state-specified price and to transfer the money to the budget. But Minfin blocked this option, referring to its non-compliance with the Budget Code.

Finally, V.Putin had to approve another approach based on budgetary subsidies. It was announced that the price of gas for Vladivostok should not have been higher than RUR4 500/mcm, and Gazprom would get

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"0" electricity price growth may undermine nuclear power stations' safety

RosAtom gives an example of Japan

Tags: [Rosatom](#), [Minenergo](#), [FTS](#)

Following the private energy companies, the state-owned Rosenergoatom expressed its discontent with the intent of the authorities to restrain the power price growth.

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Without capacity price indexation, the corporation's profits will reduce for RUR3 bn. In addition, premiums for nuclear power stations (NPS) and hydropower stations (HPS) will be reduced for RUR 15 bn, including RUR12 bn in the account of Rosenergoatom's companies; these premiums are stated by FTS, and the money are allocated for investments and safety.

According to A.Lokshin, Rosenergoatom had to get more RUR38 bn as premiums,

but Minenergo reduced this sum to RUR28 bn, due to the wrong assumption that the corporation had not used the full volume of funds allocated in 2010. Also, FTS increased the share of supplies under regulated contracts, and the profit of Rosenergoatom will be reduced for more RUR1.9 bn. The estimated loss is RUR 27 bn.

According to Rosenergoatom, the volume of funds required for safe operation of NPS cannot be reduced. The premium allocated for these purposes is RUR18 bn. So, the profit of the corporation can be reduced for not more than RUR 10 bn.

The moment to bring the appeal has been chosen very well. Emergencies at the Japanese NPS Fukushima Daiichi have brought high attention to safety of nuclear facilities, and the attitude toward any attempts to reduce the costs in this segment will be very negative.

I.Sechin ordered Minenergo, Mineconomrazvitiya, FTS and Rostekhnadzor, in cooperation with the "Council of the Market" and the Federal Security Service to consider the Rosatom's application and to submit joint proposals.

News brief

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Following private energy companies, the state-owned **Rosenergoatom** expressed its discontent with the intent of the authorities to restrain the power price growth. The Acting General Director of the state corporation Rosatom (which owns 100% of Rosenergoatom) A.Lokshin expressed his complains to Deputy Prime Minister for the Fuel and Energy Complex I.Sechin. ➤ Page 1

Minister for Energy S. Shmatko said that the **Kovykta** field was considered as the priority source of gas supplies to China. ➤ Page 3

Inter RAO got the approvals of the **Federal Antimonopoly Service** for all the deals planned within the future asset consolidation in exchange of the “big additional issue» of the holding company. ➤ Page 4

Shtokman Development AG rescheduled the final meeting of the Boards of the Directors on April 12. At this meeting, the Project’s participants should make the final investment decision on the Shtokman field development, Phase 1, or postpone it. ➤ Page. 5

Two alternative bills on offshore oil spill prevention and response will be soon introduced into the State Duma. One of the bills was prepared by the Minprirody. The other was developed with participation of ecological organizations. Both bills aim to prevention of ecological offshore oil spill emergencies, similar to that of in the Gulf of Mexico, in the Russia waters. ➤ Page 7

The Head of the **Bashneft’s** Board A.Goncharuk announced that the Company and **LUKoil** were negotiating about cooperation on the Trebs and Titova oil fields development project. The negotiations will soon be completed. ➤ Page 8

The structures owned by **A.Rottenberg** bought 100% of Gazprom bureniye at the open auction sales. The sum of the deal was RUR4.05 bn, which is slightly more than the initial price (RUR 4 bn). Gazprom bureniye has been sold too cheap. A.Rottenberg has already bought Gazprom’s assets under a similar scheme. In 2008, Rottenberg’s structures bought in trading five contractual companies of the corporation for RUR 8.3 bn (almost the initial price). ➤ Page 7

Rosneft and **CNPC** are at the edge of conflict concerning the oil supply contract terms. The Chinese CNPC insists on revision of the contract signed with Rosneft on gas supplies to China through the ESPO pipeline. The oil pumping tariff within ESPO is uniform – RUR1.815/ton. But, according to the Chinese party, gas transportation to Skovorodino, where the branch to China begins, costs less than transportation to the Kozmino port at the Pacific. ➤ Page 8

Turkey did not give its permit to construction of the **South Stream** gas line on its territory. Russia took no obligations on loading of the Samsun-Jeikhan oil pipelines. This is the result of the visit of the Turkish Prime Minister Recep Tayyip Erdogan to Moscow. ➤ Page 10

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Highlight

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the difference between the purchasing and sales prices. The federal budget for 2011-2013 included almost RUR25 bn for this purpose. After such a generous present, the Primorye had to demonstrate its own generosity towards other regions. FTS lowered the price for the Kamchatskaya heat and energy station (HES), where Gazprom started supplies to last autumn, from RUR11 000 to RUR4 500. Gazprom was promised the subsidies – RUR5.7 bn within three years.

As the result of the meeting, this experience should be applied on Sakhalin, where the first unit of the Yuzhno-Sakhalinskaya HES-1 has been gasified. The price of the matter is approximately RUR2.5-3 bn annually, with the supply volumes 600 mmcm of gas.

In total, gasification of the East under this principle will cost to the budget approximately \$1.5 bn within three years. For now, however, the pricing principle itself is not clear. This is particularly true for gas which is to be produced within Gazprom's projects (Kirinskoye field, Sakhalin 3, Chayanda, etc.).

Second, the Prime Minister ordered to inspect the subsoil use license holders in East Siberia and the Far East. This area has been cleared mainly for Gazprom. As a result, Gazprom has got the licenses for the Kamchatka shelf and Chayanda and will get the rights to the Kovykta field and some other blocks. But this situation may well be used to press the Sakhalin 1 Operator to sell its gas to Gazprom.

Third, the commissions were given to study and determine optimal options of development of the gas transportation system in the Eastern regions of Russia. The Prime Minister personally ordered to construct that absolutely non-efficient Sakhalin-Khabarovsk-Vladivostok gas pipeline which is not supported by consumers or resources. But this fact has seemingly been forgotten.

The fourth area is connected with the increase of production of the liquefied natural gas and relevant export loading terminals. This will promote important diversification of the hydrocarbons sales markets. Before the meeting, V. Putin commissioned the Energy Minister to consider the possibility of rapid construction of the third train of the LNG plant within Sakhalin 2 Project. For today, it can be possible only if Gazprom provides resources from its Sakhalin 2 Project allocated to load the gas pipeline to Vladivostok. This was the reason why the corporation rejected the relevant proposals of Shell without considering them.

Not a word has been said at the meeting about the future of the Kovykta field to be developed by Gazprom. In the meantime, the Minister for Energy Sergei Shmatko announced before his visit to Sakhalin that Kovykta was considered as the priority source of supplies to China. Such an approach to the Chinese questions contradicts the policy of Gazprom, which, following the sales market diversification idea, was trying to sell the West Siberian gas to China through the Altai Project in the first hand. According to the Gazprom's press release on the final round of negotiations with the Chinese oil and gas corporation

CNPC, for the time being, the route has been discussed which is tied to the existing fields owned by the corporation in the Yamal Nenets autonomous district.

After the autumn visit of President Dmitry Medvedev to China, it was announced that the parties had reached principal agreements on the beginning of the supply of 30 bcm of the West Siberian scheduled on December of 2015. Gazprom and CNPC agreed to conclude the price negotiations and to sign a long-term contract next June. The Deputy Chairman of Gazprom's Board Alexander Medvedev, who is responsible for the commercial side of the negotiations from the Russian side, has said before that he was discussing the financial scheme of the Altai Project with the Chinese and preparing the project documentation, in order to start the construction as soon as the supply contract would be signed.

But three months before the scheduled date, in fact, S. Shmatko announced the change of priorities. This decision, of course, has certain reasons. In early March, the Kovykta project was given to Gazprom. The monopoly company purchased the property of the bankrupt RUSIA Petroleum at the auction sales for RUR25.8 bn. In addition, the corporation agreed on the purchase of the Kovykta-Zhigalovo pipeline from the East-Siberian Gas Company for RUR 9 bn. But no declarations have been yet made on how Gazprom is going to realize this project. Gazprom has made a lot of statements that it will be no need in the Kovykta gas until 2017, and the field is expected to reach its project capacity within the Eastern Program near 2030. It is true, though, that the Program was prepared when Gazprom was standing against the plans of the former field's owner – TNK-BP.

There are two possible options of the Kovykta gas transportation to China: through the Altai Project or through the eastern corridor, with the Chayanda field in Yakutia determined by Gazprom and the state as its priority base. In this case, construction of the Altai may not be necessary. Three years ago, the estimated cost of the construction of the pipeline to the East was \$14 bn, or \$5 mn per one kilometer of the route. The first route is 800-1000 km shorter, and the savings may amount to \$5 bn. But there are also disadvantages which may result in the next delay in signing the contract. First, Gazprom will only have to assess the Kovykta's infrastructure and its ability to reach the project capacity (up to 40 bcm of gas annually), though a lot of preparations were made before the start of production in 2006. Second, the Western routes from Kovykta are less developed than the Altai gas line. The Altai project has the TEO which is being updated now. Third, the core reason of diversification of the supplies will be lost: in theory, Altai allows to redirect the gas not demanded by Europe to China, and vice versa. This will allow to control the buyers. Fourth, Gazprom has principally refused to tie gas supplies to China to a particular field: this would allow the consumer to send prices down.

The Eastern transportation option is not so inconsistent, since no particular negotiations with

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China have been held, and not terms of supplies have been determined. In this case, however, it will be necessary to revise the Chayanda field development schedule, according to which, the first gas should be produced in 2016.

And it is quite possible that S. Shmatko has presented his opinion as the position of the state and Gazprom's management, which has already been decisive on this matter.

InterRAO gets green light

FAS approved the deals crucial for consolidation process

The state-owned energy holding Inter RAO got the approvals of the Federal Antimonopoly Service (FAS) for all the deals planned within the future asset consolidation in exchange of the "big additional issue" of the holding company. The head of the Service Igor Artemiev said that these deals were aimed not to strengthen the position of Inter RAO in the energy industry (though it is evident), but to create the base for exchanges with strategic investors and to attract investments to the industry. The Company's CEO B. Kovalchuk confirmed that Inter RAO planned to perform the "second round" of coming of the foreign investors to the Russia electrical power industry.

But in certain cases, according to FAS, Inter RAO will strengthen its dominance on the market. That was the reason why FAS has ordered the energy holding company to get rid of some generating or sales assets. These orders are not very strict, though, and Inter RAO is planning to avoid their fulfillment.

The key problem FAS faced while considering Inter RAO's claims is connected with the free power flow zone (FPFZ) Ural, which unites the most part of the Southern and Middle Ural. The zone's borders are determined by grid limitations which do not allow free transfer of significant power volumes. In the result of the purchase of WGC-3 from Norilsk Nickel, the share of Inter RAO's capacities in the FPFZ Ural will increase from 26.1% to 29.7%. As a result, FAS has ordered the holding company to sell 883 MW of the assets (i.e. the Southern Urals hydropower station (HPS) WGC-3) within three years. Until this station is sold, Inter RAO will have to sell 70% of electric power by price-accepting applications within the whole first price zone of the wholesale power market (the European part of Russia and the Urals). These applications include the volume of sold power only, not the price; so, they have no influence on the price-setting.

In addition, Inter RAO must reduce its shares in TGC-6, Volzhskaya TGC and Bashkirenergo to the level lower than 25%. Initially, the holding company asked for the permit to

obtain 27.25% shares of Bashkirenergo controlled by the Joint Stock Financial Corporation (JSFC) Sistema; 26.08% shares of TGC-3; and 32.21% shares of Volzhskaya TGC (controlled by IES Holding of Viktor Vekselberg). Inter RAO has a half of the year after the deal's completion to reduce its share packages and four years to close its participation in these three energy companies. The state corporation's managers have said before that they plan to get the control share in the assets where they owned more than 25%. The FAS prescription may prevent that.

According to Inter RAO, though, it will be required only if Rosatom and his affiliates, including Rosenergoatom managing the Russian NPS, will not withdraw the holding's capital. Now, the state corporation owns more than 45% of Inter RAO's shares. After the additional issue, this share will be reduced to 15%.

Also, Boris Kovalchuk made to understand that, under certain circumstances, they could avoid the sales of the Southern Urals HPS. He said that, on one hand, new capacities were under construction in the FPFZ Ural under the investment programs of the energy companies (three blocks 400 MW each will be brought to operation at the Southern Urals HPS itself). On the other hand, some older capacities might be withdrawn from operation. As a result, the share of Inter RAO in the Urals generation might be reduced to the end of the three-year term.

In addition, FAS demanded some limitations for power sales companies of Inter RAO: Mosenergosbyt, the Saint Petersburg sales company, Saratovenergo (its control packages are being bought from RusHydro) and the Kuban power sales company (its block shareholding will be obtained from Rosneft structures). The first three sales companies should not prevent other companies from entering the wholesale power market. Within six months, the holding's share in the Kuban power sales company should also be reduced to the level lower than 25% shares. And if Inter RAO saves the Volzhskaya TGC share package, it will have to sell its share in Saratovenergo.

Shtokman is hardly seen

Prospects of the project are getting more vague

Tags: [Total](#), [Statoil](#), [NOVATEK](#)

Shtokman Development AG (SDAG) rescheduled the final meeting of the Boards of the Directors on April 12. At this meeting, the Project's participants – Gazprom, Total and Statoil - should make the final investment decision on the Shtokman field development, Phase 1, or postpone it. Last week, the basic controversies were discussed by the SDAG Operations Committee. Its results have not been disclosed, but it is highly possible that they have failed to overcome existing controversies. Fundamental prospects of the projects are not clear as well. For today, Gazprom has no contracts for gas supplies to Europe not supported by the resource base which is now under development, and the market environment is still highly volatile. It is quite possible that the decisions on the project in general and on the LNG plant construction will be made together again. It means that the united investment decision will be postponed until December 2011.

Shtokman Development was established by the Russian Gazprom (51%), the French oil and gas company Total (25%) and the Norwegian oil company Statoil (24%) to develop the first phase of the Shtokman field development on the Barents Sea shelf. The expected production within this project is 23.7 bcm of gas annually. Gazprom should buy the whole gas volume to ensure return of the investments and profitability of the capital invested by the Project's shareholders. One half of the gas may be used for LNG production and export. The investment decision was expected to be made in the first quarter of 2010, but the shareholders agreed to postpone it. Moreover, they stated that the decision on gas production and transportation on the shore would be made first (in the first quarter of 2011), and then (next December) they would decide on construction of the LNG plant with capacity 7.3 mnt (half of the production volume within Phase 1).

Gazprom is not sure at all whether it need the Shtokman gas in its export portfolio to 2016, as it is anticipated by the existing plans. The European markets are undergoing structural changes, and it is rather unpleasant business for a supplier to sign new contracts in the excessive gas supply environment. Under these conditions, it is logical to decide whether it is worth to get a move on the investment decision with a sum more than \$20 bn. Moreover, the state authorities now have another priority – the LNG projects.

Technical experts of Gazprom dobycha shelf (GDS), which holds the license for the Shtokman field and is currently preparing the documents for the second and third project implementation phases, dispute the technical concept proposed by the foreign companies. The comparison matrix showed that the single-phase (offered by GDS) as well as the double-phase (offered by SDAG) schemes of gas transportation on the shore are technically feasible. Their

capital expenditures will be approximately the same. The single-phase scheme will be a bit cheaper, but not cheap enough to neglect the safety of the vessel and the staff working on it.

Representatives of Shtokman Development's foreign shareholders were openly declaring through February that the project was too expensive and that significant tax preferences were required. But the only preference available for now is the zero LNG export rate. Negotiations with the authorities have been reported to start, but Gazprom is passive, and the state expresses its generosity toward the Shtokman's rival – the Yamal LNG project by NOVATEK and Gennady Timchenko.

This leads to change of priorities by the Shtokman's foreign shareholders. For instance, Total agreed in early March to become a NOVATEK's major participant and strategic partner with 20% share in the Yamal LNG project. The Company's officials still state their will to participate in Shtokman, though the possibility to realize two rivaling projects at once is close to nothing. Both projects anticipate the LNG supply to the Atlantic markets in 6 or 7 years. In addition, the government has already given the Yamal project tax holidays for gas and condensate production and for hydrocarbons export duty. It is rumored that Statoil can follow the French.

Everything may change at once, if it will be a political will for rapid development of the Shtokman field. If not, the experts will have plenty of time for discussions on advantages of the proposed technical solutions.

The staff merry-go-round in SDAG is a sign of lack of the project's stability. Disputing the development options made the former SDAG management to leave their posts. The Managing Director Yury Kovalev and his First Deputy for Production Erve Madeo from Total had to leave the company last year. Erve Madeo is considered the developer and initiator of the Double-phase gas transportation scheme for Shtokman. This happened when the investment decision was postponed.

Total is replacing its representative once more. Andre Goffart will replace Jean-Ives Durier, who was sent to the Company last autumn to replace E. Madeo, as Vice-President for Development of the Project. The corresponding corporate procedures are now being completed. The reasons for such rapid change are not known. This is likely connected with the areas of specialization of Durier and Goffart. Durier was responsible for safety in Total. The new representative is currently holding the post of Total's Vice President for Development and Engineering in the Middle East. This may be understood as return of the French corporation's interest to the Shtokman development project, as well as its hard assertion of its Shtokman development plan.

Experiments with grid network

ERDF will control Tomsk grid company

The authorities decided to make an experiment, handing the part of distribution networks over to foreign management. The interregional grid companies' holding ERGK (which unites the low-voltage networks) and the EDF's grid subsidiary - ERDF - agreed on the terms of handing the Tomsk distribution company (TDC) over to the French company's management. For this purpose, ERDF creates a Russian subsidiary, planning to get the Tomsk networks into its management in three months. Also, the government should give its permit (the state owns 53% of the ERGK holding).

The parties fixed the key terms. According to them, ERDF will deal with the management, including improvement of the financial, economic and technical Company's parameters, safety improvement, the time of management and the remuneration payment to ERDF. This is not the matter of trust management, ERDF will manage the TDC. For now, the French have no plans to participate in the TDC's capital.

TDC accounts for 0.8% of power transition in Russia, or 5 bn KW annually. It owns the 35-110 KW networks in

Tomsk Region. It is one of the few regional distribution grid companies which did not participate in ERGK consolidation within the electrical power industry's reform. Now, ERGK of Siberia OJSC is the only managing body of TDC. This company owns 52% of TDC shares, it is affiliated in the ERGK Holding. Neft-Activ LLC owns the Company's block shareholding - 25.9%. It is a Rosneft's affiliate owning several energy assets.

According to ERGK, the French company has been informed about the deficiencies of the Russian system, including lack of perfection in tariff regulation, territorial fragmentation of the regional grid companies, and cross-subsidization. However, the tasks set before the trust manager are not disclosed. According to the informal data, the test term of the contract will be one year and a half. Remuneration of ERDF will depend on improvement of financial and technical performance indicators of the Tomsk networks.

Along with this, the decision on possible handover of other distribution grid companies to the foreign management will be made by the results of EDF activities in Tomsk.

We just don't want to live other way

Without allowances for Vankor Russia will face oil production decline

Again, the issue of Vankor preferences has been put to the centre of governmental discussions. The Company's President Eduard Khudainatov sent a letter to the Deputy Prime Minister for the Fuel and Energy Complex and the Rosneft's Board Chairman Igor Sechin, where he asked for extension of the preferences until 2014, when production would reach its project volume - 25 mnt.

The set of presented arguments is standard: without Vankor, the Russian production would demonstrate not the growth for 2.3%, but 0.3% of stagnation in 2010, with further decrease in 2011-2012. Capital investments into the project amount to almost RUR640 bn. Less than half of them has been invested as per the end of 2010 (RUR266.143 bn), and the state holding company is planning to get the missing RUR370 bn from tax savings. Vankor's profitability indicator in dollars is lower than 5%, while the same indicator of the major world oil and gas holdings varies from 16 to 30%, by estimates of Goldman Sachs and Rosneft itself. The President suggests applying the similar

approach to the Yurubcheno-Tokhomskoye field.

In exchange, Rosneft is ready to ensure the required tax payments to the budget. The Company offered Minfin to tie the fiscal burden to the earnings, i.e. to apply the special tax regime.

Mineconomrazvitiya and Minenergo support Rosneft's arguments, according to the letter sent by Deputy Energy Minister Sergei Kudryashov to Igor Sechin. Minenergo has already sent new proposals on preservation of Vankor preferences to the government.

Minfin disagrees. Deputy Minister for Finance Sergei Shatalov said that the oil export duty preferences for the Vankor field would expire on May 1, 2011. This matter is settled, and the current discussions deal with the way to do it. According to Minfin, the Project's IRR has already come beyond 16% and will exceed this level even with regard to capital investments in the sum of RUR600 bn, if the maximal oil duty rate will be reduced to 60%. Rosneft says this is wrong.

It's necessary. But is it sufficient?

Will the approval of new exclusive laws protect Russian shelf from oil spill?

Two alternative bills on offshore oil spill prevention and response will be soon introduced into the State Duma. One of them was prepared by Minprirody, in accordance with the governmental commission after the emergency on the BP's field in the Gulf of Mexico. In mid-February, after several endorsements, the draft was introduced into the government again. It will soon be considered by the Cabinet of Ministers and further submitted to the State Duma. The second bill, developed with participation of ecological organizations, will be introduced by the deputies until the end of March. Both bills aim to prevent ecological offshore oil spill emergencies, similar to that of in the Gulf of Mexico, in the Russian waters.

Key difference of these bills lies in creation of the Reserve fund purposed to finance oil spill prevention and response. The bill developed by Minprirody anticipates introduction of amendments into the federal laws "On Internal Sea Waters" and "On the Shelf". The Ministry intends to make ecological requirements tougher, and its bill specifies the required oil spill prevention activities during drilling and other types of operations performed on oil production platforms. There are three alternatives offered to oil companies: bank warranty; insurance contract; or creation of a Company's reserve fund. The reserve fund's volume of every company will be determined with regard to its working plan, estimated cost of emergency response works, estimated sum required to reimburse the damage to the aquatic environment, in accordance with the calculation method approved by Minprirody.

The concept of an alternative bill "On Protection of the Seas of the Russian Federation from Oil Pollution" was

developed by WWF experts on the base of the U.S. Pollution Act and submitted to Minprirody in 2009, immediately after the emergency in the Gulf. The concept was discussed, expert corrections and comments were taken, including those by the Russian Union of Industrialists and Entrepreneurs and specialized R&D institutions. This concept was put into the base of the bill "On Prevention of Marine Objects from Oil Pollution", which will be introduced into the State Duma by the deputies.

Unlike the corrections made by Minprirody, this bill covers not only oil production, but its transportation along with other processes concerning offshore oil production safety, from engineering of oil production facilities to their withdrawal from operation.

But its key difference from that of Minprirody is an idea to create a special fund to finance the works on oil spill prevention and response. It is expected that this fund will be formed by payments of oil companies. The sum of payments will be determined by share percentage from the sum of insurance under the compulsory civil liability insurance agreement of the oil production asset's owner. Also, this fund will be formed by the money from the federal budget, ecological penalties and other payments. The money of this fund can be used for dedicated missions, including the set of activities aimed to prevent and eliminate oil spills and to compensate the harm to the environment.

Minprirody does not support the idea to create a special fund to finance major oil spill response activities. According to the law "On the Shelf", only the state-owned companies are allowed to work on the Russian shelf, and the burden of the special fund would be placed on them.

Bashneft is picking out partners

LUKOIL is the first in the row

Tags: [LUKOIL](#), [Bashneft](#)

In spite of the market assurance that Bashneft will have Rosneft as a partner in the Trebs and Titova fields development, the Company is going to sign an agreement with LUKoil. The Head of the Bashneft's Board Alexander Goncharuk announced that the Company and LUKoil were negotiating about cooperation in the Trebs and Titova oil fields development project, and the negotiations would soon be completed. At the reception in Washington held on March 10 to celebrate the 20th anniversary of the Company, the LUKoil's CEO Vagit Alekperov denied the fact of negotiations with Bashneft, though confirming the Company's interest in the fields.

The Trebs and Titova fields are located in the Nenets autonomous district. The recovered reserves of category

C1+C2 are estimated in 140.06 mnt (together with category C3 – up to 199.3 mnt). Total oil production may achieve 10 mnt of crude oil annually.

LUKOil owns more than 20 wells on the Trebs and Titova fields, and the bid winner will have to buy them. In total, the Company invested about \$1 bn in development of the Timano-Pechorskaya province and created an infrastructure there, including the pipeline and the Varandey terminal.

It was believed, however, that Bashneft has been given the license to create a joint venture with the state-owned Rosneft; for that, the former refused to participate in the bid, and applications of LUKoil and other claimers were rejected by Rosnedra by formal reasons.

Good owners who buy at a low price

Rotenberg is continuing assets buyup

The structures owned by A. Rotenberg bought 100% of Gazprom bureniye at the open auction sales. The sum of the deal was RUR4.05 bn, which is slightly more than the initial price (RUR 4 bn). Gazprom bureniye has been sold too cheap. It was noted by many investment banks in December. For instance, Slavneft is going to sell the drilling assets of Eurasia Drilling for \$150 mn, including 84 drilling rigs. The business of Gazprom bureniye is larger, while it has been sold for \$141 mn.

A. Rotenberg has already bought Gazprom's assets under a similar scheme. In 2008, Rotenberg's structures bought in trading five contractual companies of the corporation

for RUR 8.3 bn (almost the initial price). These companies formed the base of Stroygazmontazh with the annual turnover more than RUR100 bn. Its main customer is Gazprom.

Before being sold, Gazprom bureniye worked at a loss. Its EBITDA in 2010 was, in fact, equal to zero versus RUR640 mn in 2009, with net loss increased to RUR 2.2 bn. As expected, the situation will be improved with appearance of a new owner. Gazprom will pay more for the services rendered and will not be able to delay payments. Volumes of orders will likely be not lower, may be, even higher, judging from the experience of Stroygazmontazh.

It's time to haggle

Rosneft and CNPC failed to agree on tariffs

Tags: [Rosneft](#), [CNPC](#)

Rosneft and CNPC are at the edge of conflict concerning the oil supply contract terms. Immediately after beginning of the supplies in 2011, Rosneft conflicted with CNPC concerning the crude oil price. The Chinese CNPC insists on revision of the contract signed with Rosneft on gas supplies to China through the ESPO pipeline. The oil pumping tariff within ESPO is uniform – RUR1 815/ton. But, according to the Chinese party, gas transportation to Skovorodino, where the branch to China begins, costs less than transportation to the Kozmino port at the Pacific.

In the end of February, ChinaOil, the CNPC affiliate, should have paid \$555.3 mn to Rosneft for the January supply of 1.25 mnt of oil, but the payment was 7% as less - \$516.9 mn. I.e., it followed its own view on the tariff.

The agreement on the supply of 300 mnt of oil to China through ESPO in 2011-2030 was signed in 2009. In exchange for crude oil supply warranties, Rosneft and Transneft received from the China Development Bank the credits for \$15 bn and \$10 bn, respectively. The price of Russian oil for CNPC is tied to Kozmino quotations, China pays for transportation.

According to the agreement signed with CNPC, disputable questions are to be solved in London. However, if the conflict is not solved on the corporate level within a month, the authorities of two countries will likely enter the negotiations. D. Medvedev plans to visit China in April 15-16 to participate in the BRIC summit meeting. The agreements with China on ESPO have been prepared and supervised by Igor Sechin.


This is not the first Rosneft's conflict with China on oil prices. In 2004, the Company received \$6 bn from CNPC for the purchase of Yuganskneftegaz as an advance payment for the supply of 48.4 mnt of oil until 2010, or approximately 8.8 mnt annually. The crude oil price was initially stated by the agreement as the price of Brent minus \$3. In 2007, after purchasing of five Yukos' refineries, Rosneft was not satisfied with this price any more. Sergei Bogdanchikov, the Company's CEO at that time, declared that Rosneft was losing more than \$40 per each ton of crude oil, compared to other areas. Rosneft warned that the contract would not be extended if CNPC did not change the price formula. China agreed to raise the price for \$0.675 only (Brent minus \$2.325).

Energy reshuffle

Tragedy in Japans puts all gas consumption forecast under review

Tags: [Japane](#), [LNG](#)

The Chernobyl syndrome has just been forgotten, when the nuclear industry began threatening the mankind again. Now, Europe will have to increase consumption of natural gas, which is a reliable, ecologically friendly and relatively easily restored substitute of nuclear power. As fate has willed, Europe will have to use the fuel which it has recently considered as a threat to its energy security. Gas has to be rehabilitated very soon, or Europe will face the deficit of energy resources.

The emergency led to failure of 4 of 6 reactors of NPS Fukushima Daiichi. This is almost 2% of the whole Japanese electric power system. When the situation comes to normal, the station's owner, the Japanese largest Tokyo Electric Power Corporation (TEPCO) will likely have to replace the missing capacities by other power generating types, first of all by gas-fed one. TEPCO has certain spare capacities in the areas of power generation and LNG import. Four regasification terminals of  Page 9

Energy reshuffle

Continued from page 8

the Company in the Tokyo district were not destroyed by the natural disaster. Their design throughput is much higher than the existing need.

The terminals Sodegaura LNG, Negishi LNG (controlled by TEPCO together with Tokyo Gas), as well as Futtsu LNG and Higashi Ohgishima LNG (100% owned by TEPCO) can receive up to 100 bcm of gas annually. This is the amount imported by Japan last year through all of their three dozens of terminals. According to the data of the international energy agency, the Japanese gas consumption in 2010 increased to the pre-crisis level, amounting to 100.3 bcm. The imported foreign LNG provides more than 98% of the country's demand.

So, Japan has no problems with increasing its LNG import. Demand is the thing. The same situation occurred in 2007, when the earthquake led to long shutdown of another big NPS owned by TEPCO - Kashiwazaki-Kariwa. According to preliminary expert assessments, Tokyo Electric Power will require approximately 2.5 mnt of liquefied gas to compensate the missing capacities of Fukushima Daiichi. This is slightly more than 1% of the world LNG market. The Russian Prime Minister Vladimir Putin has already offered a grand swap to his European counterparts: to increase the pipeline gas supplies to the EU for 60 mmcm daily, and the European countries will redirect their contracted liquefied gas to the Japanese market. This idea has some sense, though it is practically unrealizable, since too many players will have to participate. Swaps can be bilateral, but the LNG market in the Atlantic basin is still oversupplied with uncalled volumes, and this allows increasing supplies to Japan without complex schemes with participation of Russia.

The European gas market has already reacted to the Japanese events very sharply. The gas price started to grow after disorders in the Middle East and North Africa, and the Japanese earthquake has stimulated this growth.

Though, there are some long-term possibilities of the gas bubble, namely possible rejection of the plans on bringing new nuclear power units to operation in Japan, as well as in other states. It is impossible to refuse at once from such

generation volumes as 15% in EU, 20% in the USA and 30% in Japan, even willing this very much.

Japan has planned to increase the installed NPS capacity for 30% in 2012-2018 and to assure the increasing power demands of the industry and population. The country was going to put to operation 11 new blocks for 16 MW, including the 7th and 8th reactors on the failed Fukushima. Now, these projects will be at least delayed for a long period or abandoned.

And this requires 10-12 mnt of additional LNG volumes for power generation needs. In fact, that means the guaranteed 10% growth of demand of the world largest gas importer for the nearest 5 years. This are very good news for the market which has been suffering from the supply surplus due to economic recession, production growth in the U.S. and large amounts of the Qatar liquefied gas.

When the Qatar effect is over in 2011 and the country brings its export capacities to the design level of 100 bcm annually, the spot fairy tale in Europe, where the spot prices were significantly lower than those of the long-term contracts all year round, will end.

This forecast does not depend on the decisions made under the nuclear programs of the EU states. It is clear, though, that the position of NPS opponents in Europe will be strengthened after Fukushima. The emotional statements demanding to check everything once more and very carefully confirm this conclusion. Even the government of France, this European nuclear industry's stronghold, has to make careful excuses about impossibility to refuse from NPS. The discussion is evidently turning to gradual closure of such stations.

Today, it is hard to assess the scale of NPS-gas reshuffle in Europe. Reduction of atom for peace-based power generation even to 5% from the current 15% will require compensation from other sources with the amounts of 70 mnt of oil equivalent, or approximately 90 bcm of gas.

Only gas and more expensive renewable power sources meet the EU ecological objectives. Even the half of these volumes is covered by solar and wind stations, the European gas demand will increase for at least 45 bcm annually.

Failed to come to an agreement one again

What does Turkey really want back in return for construction of South Stream on its territory?

Turkey has not given its permit to construct the South Stream pipeline on its territory, while Russia has taken no obligations to load the Samsun-Geikhana oil pipeline. This is the result of the 3-day visit of the Turkish Prime Minister Recep Tayyip Erdogan to Moscow in the fuel and energy area.

Turkey says that Gazprom has not submitted the required documents on the project implementation. The corporation obtained the permit for survey works beginning from May 31 of this year only on February 9.

In its turn, the Russian party mentioned the alternative solution, that is construction of a LNG plant onshore the Black Sea – either instead of the pipe, or together with it. Just before the visit of his Turkish counterpart, Vladimir Putin gave a relevant commission to Sergei Shmatko. With all challenge advanced by this idea when Turkey delays its decision, LNG is the only chance to prove the project's vividness to partners and rivals.

The bargaining will be continued. Turkey is not meeting

its obligations on the Russian gas off-take under long-term contracts. In 2010, the supplied volumes decreased from 19 to 18 bcm, while the minimal off-take level reached 22.5 bcm, when the Blue Stream reached its design capacity. The penalty for incompletely taken volumes in the sum of approximately \$1.5 bn has not been yet paid.

Moscow has declared its readiness to mutual concessions. After his meeting with the Turkish Prime Minister, President Dmitry Medvedev said that Russia was ready to correct the price terms of gas supplies to Turkey, but this process had to be mutual.

Frankly speaking, Turkey will get no advantages from the South Stream construction, since the gas to be supplied to Europe under this project will compete with that of under the projects being constructed on the Turkish territory (Nabucco, ITGI, Poseidon). It means undermining the ambitions of Ankara to become a major power-transiting hub on the way from the Caspian region and the Middle East to Europe.

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