

## The New York Times

### Kremlin Aim of Monopoly Threatens BP Gas Venture

May 29, 2007

By ANDREW E. KRAMER

MOSCOW, May 28 — The Russian government continued Monday to press its strategy of securing for [Gazprom](#), the state-owned natural gas company, a monopoly on exports to Asia.

In doing so, it is threatening an important investment by a big British rival, [BP](#), with methods similar to those used last fall to force [Royal Dutch Shell](#) to sell a controlling stake in another energy development in the Russian Far East, the Sakhalin II project. Gazprom was also the beneficiary in that case.

In the latest move, BP, which operates through a Russian joint venture, [TNK-BP](#), slipped closer on Monday to losing its license to the Kovykta gas field when a Siberian court declined to hear its arguments.

Kovykta is BP's largest natural gas project in [Russia](#) and is valuable because of its proximity to the fast-growing gas markets in China. The project appears to be slipping out of BP's grasp.

The field, near Lake Baikal, is among the largest natural gas deposits in the world, holding the equivalent of three times the annual demand of the United States.

At play, energy analysts say, is a Russian strategy to gain a monopoly in natural gas exports to Asia through Gazprom, similar to its position in Europe, with the scope and range to dictate prices and thwart competition.

President [Vladimir V. Putin](#) has discussed playing the two markets off against each other, a strategy that is based on government control of the export routes.

This would not bode well for private companies like TNK-BP operating in the Russian Far East. Shell's ill-fated development was also aimed at the Asian market. If TNK-BP's field is taken away, a consortium on Sakhalin Island led by [Exxon Mobil](#), also under pressure by Russian environmental regulators, would be the only private energy development in the wider region.

In the latest setback for TNK-BP, the Irkutsk Region Arbitration Court rejected a lawsuit by the company contesting its license terms. The ministry has threatened to strip TNK-BP of its license, saying the company has not developed the field quickly enough.

More broadly, TNK-BP is seen as being compelled to sell a controlling stake to Gazprom or accept Gazprom as a partner.

"They will reach an agreement with Gazprom, or the license violations will get the better of them," Caius Rapanu, oil and gas analyst at the brokerage firm UralSib, said.

Last fall, the campaign against Shell was built as well around a seemingly capricious enforcement of Russian law. Then, the natural resources ministry accused Shell of spoiling salmon-spawning streams on Sakhalin and dumping dredge waste into a bay. Shell disputed those accusations. The pressure on Shell ended when the company sold a controlling stake to Gazprom.

The ministry now accuses TNK-BP, which owns 65 percent of the Kovykta field, of having failed to meet a license requirement to begin supplying natural gas to the region in which the field is situated by the end of 2006.

"There are a lot of parallels with what is going on now and the later stages of Sakhalin II," Chris Weafer, chief analyst at Alfa Bank, said of the Kremlin's tactics. "It is a carrot-and-stick approach to pressing its position."

This has left TNK-BP sitting on vast wealth with no market. To hold onto the field, it shifted focus to unprofitable domestic sales and partially built a pipeline

connecting the huge field to the nearest settlement, a logging town with 5,000 inhabitants.

That fulfilled the license requirement in part. But the license also specified that the company must supply 9 billion cubic meters of gas to the region, based on dated estimates of Siberian demand. Government and industry experts now estimate demand in the area — which borders Mongolia and where the population is declining — at no more than 2.5 billion cubic meters a year; the terms of the license, issued in the early 1990s, had overestimated growth.

“Formally, the Russian government is right,” Pavel Kushnir, an oil and gas analyst at [Deutsche Bank](#) in Moscow, said. “They say that since TNK-BP is not able to meet license obligations, the license should be revoked.”

In court filings, TNK-BP argued that the license requirements contradicted other Russian government documents estimating demand in the Irkutsk region. The judges declined to hear the case.

A spokesman for TNK-BP, Aleksandr Shadrin, said, “We regret the decision of the court.” He added that the company would appeal.

TNK-BP, though, has seemed to emphasize negotiations over pressing its case in the Russian courts.

Alex Turkeltaub, a managing director and political risk adviser with the Frontier Strategy Group, a consulting firm in Cambridge, Mass., said BP would probably “focus on the broad strokes” of a settlement with the Kremlin while using the court case to delay a license revocation. “If they don’t violate one agreement, it will be another,” he said, recalling Shell’s problems with the salmon streams. “Worrying about little details won’t help them.”