The Iasi-Ungheni pipeline: a means of achieving energy independence from Russia? Moldova’s attempts at gas supply diversification

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Since taking power in 2009, the Alliance for European Integration (AIE) has been trying to end Moldova’s dependence on Russian gas. Currently, natural gas accounts for about 50% of the country’s energy balance (excluding Transnistria), and Gazprom has a monopoly on the supply of gas to the republic. The key element of Chișinău's diversification project is the construction of the Iasi-Ungheni pipeline, which is designed to link the Moldovan and Romanian gas transmission networks, and consequently make it possible for Moldova to purchase gas from countries other than Russia. Despite significant delays, construction work on the interconnector began in August 2013. The Moldovan government sees ensuring energy independence from Russia as its top priority. The significance and urgency of the project reflect Chișinău’s frustration at Moscow’s continued attempts to use its monopoly of Moldova’s energy sector to exert political pressure on the republic. Nonetheless, despite numerous declarations by Moldovan and Romanian politicians, the Iasi-Ungheni pipeline will not end Moldova’s dependence on Russian gas before the end of the current decade. This timeframe is unrealistic for two reasons: first, because an additional gas pipeline from Ungheni to Chisinau and a compression station must be constructed, which will take at least five years and will require significant investment; and second, because of the unrelenting opposition to the project coming from Gazprom, which currently controls Moldova’s pipelines and will likely try to torpedo any energy diversification attempts. Independence from Russian gas will only be possible after the the Gazprom-controlled Moldova-GAZ, the operator of the Moldovan transmission network and the country’s importer of natural gas, is divided. The division of the company has in fact been envisaged in the EU’s Third Energy Package, which is meant to be implemented by Moldova in 2020.

The characteristics of the Moldovan gas market

Moldova virtually does not have its own source of natural gas¹, and so 100% of its gas demand is currently being met by imports from Russia’s Gazprom; the gas is sent to Moldova via a pipeline across Transnistria. In addition, almost all (about 90%) of the electricity produced in Moldova is generated by three gas-fired combined heat and power plants, which jointly meet about 20% of the country’s electricity needs. The remaining 80% is purchased from the Ukrainian company DTEK Power Trade and from Moldavskaya GRES, located in Transnistria and owned by the Russian state energy group Inter RAO UES. Moldova’s biggest gas consumer is its energy and heating sector (43%); meanwhile household and industrial consumers pur-

¹ In August of this year, Moldova’s Economy Minister announced plans to launch prospecting projects for gas (especially shale gas) and crude oil in the country.
chase just 30% and 21% of gas respectively\(^2\). In recent years, Moldova has seen a significant drop in natural gas consumption. Whereas in 2005 the country consumed 1.315 bcm of gas per year (excluding Transnistria), in 2012 the figure dropped to 0.98 bcm\(^3\). The reduction has been linked primarily to a drop in consumption by households and power companies. In the first six months of 2013 these two groups consumed 8.5% and 5.5% less gas than in the same period the previous year. The drop in demand has been caused primarily by the rapidly rising price of gas: in 2005, Moldova paid around $80 per 1000 m\(^3\) of Russian gas, while by 2012 the price had risen to $382.

The company responsible for the purchase and management of the Moldovan gas network is Moldova-GAZ, established in 1999. Moldova-GAZ also controls the country’s transit pipelines and two gas distributors: Moldovatransgaz, located on the right bank of the Dniester, and Tiraspoltransgas-Prîndrestrovie located in Transnistria. In addition, the company has 18 subsidiaries responsible for regional gas distribution (12 on the right bank of the Dniester and 6 in Transnistria). Although Moldova-GAZ has the status of a national operator, it has been controlled by Gazprom, which holds 50% plus one share of the company. The Moldovan state holds a 35% stake in Moldova-GAZ while the Property Management Committee of Transnistria, managed by the government of the breakaway republic, owns 13.44% of the shares\(^4\). The remaining shares are in the hands of individual investors\(^5\).

Moldova is a major transit country for Russian gas destined for Turkey, Romania, Bulgaria and Greece, amongst others. However, the amount of gas transported through Moldova has been gradually decreasing. From 25.3 bcm in 2005, the transit volumes had dropped to 19.9 bcm by 2012. This represents approximately 11% of Russia’s total gas exports, and generates about $50-$60 million in annual revenue for Moldova. It is likely that if the construction of the South Stream gas pipeline goes ahead as expected, this trend will accelerate, and eventually Moldova’s role as a transit country will become marginal.


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The figures cited in this paper come from the official website of Moldova-GAZ; http://moldovagaz.md/menu/ru/about-company/mg-today

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energy market across Europe, and promote competition in the energy sector. Moscow is particularly keen on persuading Moldova to abandon its plans for the implementation of the EU’s Third Energy Package, which Chişinău agreed to adopt when it joined the Energy Community in 2010. This is important for Moscow for both economic and political reasons.

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Under the terms of the Third Package, transmission, sale and production of natural gas would have to be carried out by independent operators. The implementation of the new regulations would therefore require splitting Moldova-GAZ into two legally independent companies, or establishing a transmission system operator independent of Gazprom. This could effectively strip the Russian gas monopoly of its control over Moldova’s transit pipelines. By protecting its economic interests, Russia is also trying to advance its political interests; this is because Chişinău’s potential withdrawal from the Energy Community would also block Moldova’s successful integration with the European Union. At the same time, Russia is also seeking to retain its position as a monopoly gas supplier to the Moldovan market.

To exert additional political pressure on Chişinău, Russia has been bringing up the issue of the so-called Transnistrian gas debt, which has already reached over $4 billion. The debt has been accumulating as a result of a conscious decision by the Transnistrian government (with Moscow’s de facto approval) not to pay for the gas which for years has been supplied to Transnistria under Moscow’s contract with Moldova. Although officially Moldova is not liable for the debt, it has been suggested that a protocol signed between Gazprom and Chişinău in December 2006 is likely to include government guarantees for any debt incurred by Moldova-GAZ. This means that Russia could potentially call in the debt at any point it sees fit. Such threats have been made in the past, for example when Dmitry Rogozin, Russia’s deputy prime minister and special representative of the Russian president for Transnistria, said in April 2012 that “Chişinău does not recognise Transnistria as an equal partner, and therefore Transnistria’s unpaid gas bill will have to be settled by Moldova”. High-ranking Russian politicians have frequently stressed that if Moldova were to agree to withdraw from the Energy Community, it could easily negotiate and sign a new long-term gas contract with Russia. The deal would include a price discount (of allegedly up to 30%) and would resolve the issue of the Transnistrian gas bill. Consequently, Moldova’s ruling coalition has made several concessions to the Kremlin, including a decision to postpone the implementation of the Third Energy Package from 2015 to 2020. However, this has failed to have any effect on Moscow’s position. As a result, the government in Chişinău has abandoned further attempts to appease Moscow and has resisted continued pressure from the Kremlin. In mid-September 2012, President Nicolae Timofti officially stated that Moldova would not swap European integration for cheaper gas from Rus-
sia. Nonetheless, it is difficult to predict whether the country will be able to resist Moscow’s pressure if the price of Russian gas continues to rise, or if gas supplies are disrupted. At the moment, Russian gas is being imported to Moldova under a contract which was extended in December 2012 for another 12 months. According to a statement in September by the Moldovan Economy Minister, Russia has since agreed to a new extension, this time until the end of 2014, although Moscow has not yet officially confirmed this information.

Attempts at gas supply diversification

Since 1991, successive Moldovan governments have failed to take any real steps to diversify the country’s gas supply routes. Throughout this time, Moldova has not had the money to finance the expansion of its cross-border gas network, which is the only way to make the diversification of gas supplies possible. In addition, the relatively low cost of Russian gas since 2005 has rendered any such attempts economically unfeasible. The first signs of a possible policy shift in this area appeared only after a worsening of diplomatic relations between Moscow and Chişinău in 2003\(^\text{10}\); however in the end no concrete measures were implemented. Despite a marked deterioration in relations between the two countries after 2003 and despite a gradual rise in the price of Russian gas, Moldova’s then Communist government not only failed to take any steps towards energy independence from Russia, but its decisions seem to have cemented Russia’s presence on the Moldovan gas market. The pro-Moscow approach was clearly visible, for example, in Chişinău’s 2007 Energy Strategy until 2020 document, which emphasised the importance of Russian gas supplies and envisaged the strengthening of Moldova’s role as a transit country for Gazprom’s gas. Chişinău’s policy changed in August 2009 when power was taken by the AIE.

The linchpin of the energy diversification policy pursued by the new government has been the construction of an interconnector between the Romanian and the Moldovan gas transmission networks. In May 2010, the two countries signed a memorandum for the construction of a 43-km pipeline between Iasi in Romania and Ungheni in Moldova, with a nominal annual transmission capacity of 1.5 bcm. In March last year, the project received the status of a ‘national project’, and the prime ministers of both countries officially stated that the interconnector would be operational by December 2012. Despite the political will on both sides, construction work was delayed due to a series of problems, mostly of a legal and financial nature\(^\text{11}\). Moreover, when Gazprom agreed in November 2012 to extend the existing gas contract for another year, the momentum for the project waned further. Moldova also struggled to meet the cost of its 11-km section of the pipeline, estimated at €9 million. Eventually, the EU and Romania agreed to cover Moldova’s share of the bill, contributing €3 million and €6 million respectively. However in August this year, after the tendering process for contractors was completed, Moldova’s share of

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\(^{10}\) Relations worsened after, in the autumn of 2003, the government in Chişinău rejected Moscow’s plan to unite Moldova and Transnistria, known as the Kozak Memorandum.

\(^{11}\) The issue of compulsory purchase orders issued to 40 Romanian citizens to secure land for the planned pipeline proved particularly problematic.
the cost was reduced to €6.65 million\textsuperscript{12}. Meanwhile, the cost of Romania’s 32-km section of the pipeline, estimated at €20–€22 million, is to be covered almost entirely by Bucharest, with only a small contribution (€4 million) from the EU. Further delays to the project have been caused by a political crisis in Moldova, which affected the country for five months from the beginning of this year. The crisis eventually abated in late May when a new government, led by Iurie Leance, came to power. The subsequent relative stabilisation of Moldova’s political scene allowed for work on the project to be resumed. On a visit to Chişinău in mid-July, Romania’s president Traian Basescu announced that construction of the pipeline would begin on 27 August, with a view to completing the project by December 2013.

Reaching the pipeline annual transmission capacity of 1.5 bcm would require the construction of a new compression station and a gas pipeline running from Ungheni directly to Chişinău.

According to the timeframe announced in 2012, the implementation of the project was likely to take about seventeen months. It is therefore unlikely that the project could be completed and launched within just four months\textsuperscript{13}. In fact, at the start of the construction work, Prime Minister Leanca revised the earlier completion date to April 2014, although it should be stressed that this date is also just a projection\textsuperscript{14}. According to press reports, the parliament in Bucharest has not yet ratified an agreement on the section of the pipeline running under the border river Prut, which is to link the two legs of the pipeline. This delay, in turn, is preventing the governments from launching a bidding process for potential constructors of this section\textsuperscript{15}. It is also unclear how the estimated completion date will be affected by the unexpected increase in the total cost of the project. Until August of this year, the interconnector was expected to cost approximately €19 million, although those estimates have since proved inaccurate. Although the cost of the Moldovan section of the pipeline has fallen by €2.4 million (from €9 million to €6.6 million), the cost of the Romanian section has actually risen by €11 million (from €10 million to €21 million). Consequently, just a few weeks before the launch of the construction work, the total cost of the interconnector unexpectedly rose by 40%, reaching €28 million euro\textsuperscript{16}. It also seems that the delays in the im-

\textsuperscript{13} For comparative purposes, the construction of a 50-km pipeline between Ungheni and Bălți took Moldova-GAZ about 12 months. Moreover, a contract regulating the financing of the project, signed between Moldova and the EU on 8 August 2013, sets the length of the project at 17 months: http://www.mec.gov.md/comunicate/contractul-de-finantare-a-contractiei-gazoductului-iasi-ungheni-a-fost-semnat/

\textsuperscript{14} Just a few days after the official launch on 27 August, construction work was suspended. According to Romanian press reports, the work is to be resumed in October.

\textsuperscript{15} http://adevarul.ro/moldova/actualitate/pe-santierul-gazoductului-iasi-ungheni-bate-vantul-1_522573c87b855f563dc61c/index.html

\textsuperscript{16} The official cost of the project has been estimated at approximately €26 million. This figure does not however include the additional €2 million required for the construction of a link under the River Prut.
plementation of the project have been partly caused by the ongoing conflict between the President and the Prime Minister of Romania. Both politicians strongly support the construction of the pipeline, but they have been trying to downplay each other’s role in the project in order to gain political advantage. There is also the added issue of the pipeline’s capacity. Under the current plans, the pipeline is to transport up to 1.5 bcm of gas a year, which would meet Moldova’s total energy needs (excluding Transnistria). However, reaching this capacity would require the construction of a new compression station and a 120-km gas pipeline running from Ungheni directly to Chișinău, and the Moldavian capital uses 50-60% of all gas consumed in Moldova. Until the additional infrastructure is in place, the interconnector will be able to work at just 10% capacity, and will only supply enough gas to meet the needs of the areas lying outside Ungheni and the needs of the free economic zone located in the city. Current estimates place the cost of constructing the compression station and the pipeline linking Ungheni with the capital at €20 million and €170 million respectively, and the work is expected to take about five years. At the moment it is unclear how Moldova plans to pay for this project. Although European Commission representative Günther Oettinger has suggested that Brussels could offer Chișinău some financial help with the project, there is no certainty that the EU or any other international organisation would agree to cover most of the cost. Finally, the capacity of the pipeline will also be affected by the state of Romania’s existing infrastructure, which itself requires significant investment.

- The dependence of Moldova-GAZ and of the transmission infrastructure on Gazprom

Theoretically, the interconnector and access to Romania’s gas transmission network would allow Moldova to purchase gas not only from Romania, but also from Hungary and any other EU country linked to the Romanian pipeline network. In reality, however, the distribution of any non-Russian gas through the Moldovan pipelines is rather impossible at the moment. This is because Moldova’s transmission and distribution network, which is owned by Moldova-GAZ, are controlled not by the authorities in Chișinău, but rather by the company’s main shareholder – Russia’s Gazprom. It is almost certain that the Russian gas monopoly will try to protect both its own interests and the interests of the Russian state by obstructing or blocking imports of non-Russian gas to Moldova. Its influence would diminish only if Moldova adopted the EU’s Third Energy Package, which would allow it to break up Moldova-GAZ; this, however, cannot happen before 2020.

Outlook

There is no indication that Moldova will be able to end its dependence on Russian gas before the end of the current decade. At the moment, Gazprom is not only Moldova’s sole gas supplier, but also the sole operator of the country’s gas transmission network. This allows Russia to control the supply of gas to the Moldovan market, and to block virtually any attempts by Chișinău to diversify its gas sources. This, coupled with the

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17 Source: Speech by Moldova’s Economy Minister Valeriu Lazar. See: http://www.kommersant.md/node/19265
18 Some sources suggest the figure to be twice as high.
19 http://www.europalibera.org/content/article/25116402.html

20 The question also remains of whether Moldova-GAZ could potentially take control of the interconnector, especially its Ungheni-Chișinău section, once the construction work has been completed.
lack of an appropriate infrastructure, means that the Iasi-Ungheni pipeline will make only a negligible contribution to opening up the Moldovan energy market to non-Russian gas. Similarly, the interconnector will contribute little to Moldova’s bargaining power in energy negotiations with Gazprom. Moldova’s position is likely to change after the completion of the Ungheni-Chișinău pipeline and once Gazprom is stripped of its control over Moldova’s transmission network; however, this will not happen before 2020.

Meanwhile, it is expected that before work on the interconnector is completed, Russia will seek to take advantage of its dominant position in the Moldovan gas sector. Moscow is likely to try to reduce the support of the Moldovan people for the pro-European coalition ahead of the country’s 2014/2015 presidential elections; it will attempt to persuade Chișinău to abandon its plans for the implementation of the Third Energy Package; and it will seek to hinder Moldova’s plans for closer integration (including energy integration) with the European Union. For example, the Kremlin could achieve this by refusing to renew Moldova’s gas contract in the run-up to the elections, or by instigating disruptions to gas supply during winter time. Such a move could significantly reduce public support for the current government, and ultimately help the Moldovan Communists take power. A change of government would likely prevent the adoption of the Third Energy Package, and guarantee Russia’s continued control over Moldova-GAZ.