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Deal between Germany and the US on Nord Stream 2

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On 21 July, the German Ministry of Foreign Affairs and the US State Department issued a Joint Statement of the United States and Germany on Support for Ukraine, European Energy Security, and our Climate Goals. The statement presents the arrangements made by Berlin and Washington on the conditions for the effective withdrawal of US opposition to the Nord Stream 2 gas pipeline. News agencies and the US press had already reported the deal's outline. On the same day, the date for the Ukrainian president's visit to Washington (30 August) was announced. Chancellor Angela Merkel had a telephone conversation with the President of Russia in the evening, the topics of which also included gas transit through Ukraine and the NS2 gas pipeline. According to a statement from the Kremlin, both sides expressed satisfaction at the approaching conclusion of construction work on Nord Stream 2, while the Russian side presented (unspecified) queries regarding the US-German announcement.

State Department spokesman Ned Price said during a briefing on 20 July that the negotiations had been facilitated by the administration waiving the sanctions against Nord Stream 2 AG and its chairman in May, which created a space for Germany to present constructive proposals for concessions, enabling an deal to be reached. The document presented focuses on energy issues, and does not refer to the consequences Nord Stream 2's operation will have for the wider security of the region.

The main elements of the deal are as follows:

1. Sanctions against Russia will be announced in the event it undertakes aggression or other malign actions, including the use of energy as a weapon against Ukraine: both countries intend to coordinate their actions in such a case. Germany declared that it would take action at the national level and would press for a response from the EU. The possibility of applying sanctions to the energy sector was directly indicated. The statement does not include the introduction of a mechanism to suspend supplies via Nord Stream 2 if transit agreement with Ukraine is not implemented.
2. Financial support to transform the Ukrainian energy sector was declared. In the deal, Germany undertook to establish a Green Fund for Ukraine, which it will also manage; its target capital has been set at at least US$1 billion, to which Germany is to make an initial contribution of US$175 million. Berlin will also appoint a special envoy for the implementation of bilateral German-Ukrainian energy projects (mainly related to renewable energy sources, energy efficiency and the transition away from coal), which will have a fund of US$70 million available. The institutional framework of the climate

and energy partnership between Germany and the US which was agreed during Chancellor Merkel's visit to Washington will be used to implement this part of the deal. In addition, Germany will create a *Ukraine Resilience Package* to bolster the country's energy security; this will primarily involve increasing the capacity for reverse flows of gas, and providing technical support to integrate the Ukrainian electricity grid with the EU's. Germany will also support the development of a model to modernise the Ukrainian transmission system. There are also plans to involve Ukraine in German projects to build and develop its cyber-capacities.

3. Efforts will be made to maintain Ukraine's role as a transit state: Germany is to utilise all available leverage to facilitate the extension by up to 10 years of the current transit agreement between Russia and Ukraine (the present one expires at the end of 2024). A German special envoy in this matter will be appointed, and negotiations on this subject will begin no later than 1 September this year.
4. The importance of applying EU law is reaffirmed: Germany has emphasised that it will adhere to both the letter and spirit of the Third Energy Package with regard to the German section of Nord Stream 2, ensuring the implementation of unbundling and third-party access rules to the pipeline, and assessing the risk to energy security involved with the certification of the route's operator.
5. Support for energy cooperation in the region by involving Germany in the Three Seas Initiative was declared. Both countries have promised to help in the development of infrastructure. Germany has declared that it will also expand cooperation in the financial dimension with regard to specific projects in the fields of regional energy security and renewable energy. It was also announced that energy projects of common interest (PCI) will be supported via the EU budget with contributions of up to US$1.77 billion.

Reports of the upcoming Germany-US deal have been criticised by US politicians and experts. The Republicans' representatives reacted the fastest: Jim Risch, a high-ranking member of the Senate's foreign affairs committee, stated that the proposed compromise enabling the completion of NS2 did not contain any specific instruments that could allow the risks associated with the pipeline to the US's allies and their interests to be minimised. He also criticised the fact that the compromise had been negotiated without the participation of Ukraine and Poland. He also said that no member of Congress was in favour of completing the pipeline, and that mandatory sanctions are still in place which the current administration did not impose. Nor has the US government consulted with Congress the decision to waive the application of the restrictions to NS2 AG and its director. He recalled that the administration has to present another report concerning the entities subject to PEESA sanctions by 11 August, and if it wishes to grant any exemptions, it must also attach a written justification for doing so. The upcoming US-German deal was also criticised by Congresswoman Marcy Kaptur, who said Congress should reject any deal that fails to defend trans-Atlantic security and Ukraine's independence.

Commentary

The deal and the negative effects of Nord Stream 2

- The deal was reached despite the persistent differences between Berlin and Washington over how to approach the NS2 question. It means a *de facto* withdrawal from the imposition of new US sanctions against the investment, and perhaps also a limitation of those which have already been introduced. However, it does not contain any clear declarations in this regard by the US side. This is because the administration needs to cooperate with the US Congress, which initiated and passed the sanctions regulations (CAATSA and PEESCA). If Nord Stream 2 AG is to achieve a legal guarantee of protection as a result of the deal, then cooperation on the part of Congress will be essential.
- Despite its relatively sharp rhetoric towards Russia, the joint statement does not contain any binding commitments to react in the event of aggressive Russian actions; nor does it introduce any concrete instruments which could limit destabilising actions on Russia's part or minimise the negative effects of NS2's launch. In addition, it considers the negative effects primarily with regard to Ukraine, thus marginalising the risks that NS2 poses to other countries in Central and Eastern Europe. According to an unnamed representative of the US administration quoted by the Bloomberg news agency, the vague wording in the joint statement was intentional, and was intended to prevent Russia from preparing a response to any restrictions. Commentators have already pointed out that Moscow will quickly be able to test how real the provisions of the joint statement are.
- How effective the instruments provided for in the deal will prove to be depends on how they will be clarified and operationalised. Allowing NS2 to be completed, despite the US sanctions already in place, will substantially limit the impact of any future restrictions against Russia. Neither Washington nor Berlin can guarantee the continuation of gas transit through Ukraine, as this will depend solely on Russia's goodwill. The effects of the financial involvement in Ukraine's energy transition will to a great degree depend on what strategic decisions Kyiv chooses to take; they are in no way directly linked to the Nord Stream 2 project, nor will they allow for a sufficient compensation for the revenue Ukraine will lose after the pipeline is launched. Similarly, the future of Germany's cooperation with the Three Seas Initiative states will require further discussions and agreements with these countries.

The deal's importance for Germany, Russia and Ukraine

- The deal confirms that the US sees cooperation with Berlin as its top priority. These arrangements favour Germany, which has achieved its aims at relatively low cost. The series of political declarations is the core of the deal, and the scope and form of their implementation will depend on the assessment and decision of the German government. What happens if the declared results are not achieved has not been foreseen. Germany's potential investments in Ukraine's energy sector relate primarily to the areas which it was interested in developing anyway. According to the German media, the funds Berlin has earmarked to support the Ukrainian energy sector were accepted by the Ministry of Finance and set aside in the federal budget. At the same time, the deal means that Germany has officially recognised the project's geopolitical dimension. Both the deal's title and the language it uses regarding Ukraine are symptomatic of the fact that the country was not included in the negotiations.

- The conclusion of this deal is a success not only for Germany, but above all for Russia. The launch of the pipeline will make it possible to maintain, and potentially also increase, the already significant share of Russian gas on the EU market; to hinder the implementation of alternative projects to diversify the sources of gas supplies; to expand Russia's economic and political influence in Germany; and marginalise the importance of Ukraine on the European gas market.
- Ukraine has been unequivocally critical of the deal; the launch of NS2 will pose a challenge to it not only in terms of energy security, but also politically and economically. The complete suspension of gas transit via its territory will mean a loss of around US$1.5 billion per year for Kyiv, a sum which will not be compensated for by the declared US-German renewable energy investments. Despite its efforts, Ukraine has been unable to obtain specific guarantees that gas transit will be continued after 2024. The Ukrainian gas pipeline system will still be able to function if transit falls to zero (at least in the short term), but its use will be much more expensive. If transit ceases, the virtual reverse flows will be prevented; that will raise the price of the gas Ukraine imports, and will make it either harder or completely impossible for EU traders to use the underground storage facilities in that country.
- In response to the deal between the US and Germany, the foreign ministers of Ukraine and Poland issued a joint statement in which they stated that the failure to block the launch of NS2 will deepen the security crisis in Europe by increasing Russia's scope for destructive actions. Moreover, Ukraine's foreign minister Dmytro Kuleba announced the initiation of consultations with the European Commission and Germany, in accordance with Art. 274 of the Association Agreement regarding Nord Stream 2 as an investment that threatens Ukraine's energy security and violates the EU Energy Union's principle of diversification. The NS2 situation was the subject of the meetings held by the president of Naftogaz, who visited Washington on 21 July, and will also be the main subject of talks during President Volodymyr Zelensky's visit to the US capital (30 August). Meanwhile in an open letter to the speaker of the House of Representatives Nancy Pelosi, the speaker of the Ukrainian parliament Dmytro Razumkov appealed to Congress to continue the policy of sanctions against NS2 and ensure the pipeline is not launched.

A change in US policy on Nord Stream 2 and Central Europe

- The US-German deal demonstrates that the Biden administration is consistently implementing a policy regarding NS2 which differs from that of his predecessors. Opposition to its construction has been withdrawn; the deal also confirms the importance for the United States of improving relations with Germany at the expense of its ties with Ukraine, Poland and some of CEE's other countries. The entirety of the negotiations on NS2, the future shape of the regional gas market, the gas flows in this region, the shape of energy relations with Ukraine, and finally the direction and priorities of the regional energy transition were all held between Berlin and Washington. The consultations with Kyiv and Warsaw, including the visit by a State Department representative, Derek Chollet, to Kyiv and Warsaw on 20–23 July, failed to bring about any changes in the US-German deal that satisfied Poland or Ukraine. Moreover, according to reports in *Politico*, Washington has allegedly put pressure on Kyiv not to criticise the

upcoming Nord Stream 2 deal, hinting that good relations between the two countries are at stake. Finally, during Chancellor Merkel's visit to Washington the US-German climate and energy partnership was agreed; one of its goals will be support from both countries for energy transformation in Central and Eastern Europe, including Ukraine. All this shows that Germany and the US are thinking along the same lines regarding energy reforms in the region, which they intend to implement by means of the instruments they have developed in connection with the new opening in their bilateral relations, including during the discussions on NS2. Thus, the countries of the region have become an object, not an agent, in cooperation between Berlin and Washington. What impact the new US administration's course will have on its bilateral energy partnership agreements with the countries of the region, including Poland and Ukraine, remains open.

The consequences for NS2

- The deal in its current form signs and seals the construction of Nord Stream 2. It will probably also accelerate the commissioning of the gas pipeline by facilitating the process of its technical certification. In this situation, the limitations which may result from the full application of EU energy regulations to the pipeline remain the only real instrument left to influence Russia. The need to maintain the regime of EU law was emphasised in the deal, which may limit Germany's options for offering concessions to Gazprom. The way in which the German regulator applies the rules of the amended gas directive in the case of the pipeline remains of key importance: this applies *inter alia*to the certification of the route operator's independence, as well as the implementation of the principles of third-party access and regulated, transparent transmission tariffs. During this process, the principle of energy solidarity should be taken into account; its importance was strengthened last week by the Court of Justice of the EU's decision on the OPAL gas pipeline. It will also be important for the European Commission to get involved, as it should ensure that the solutions developed by the German side comply with EU law. Meanwhile, Russia wants NS2 to be launched as soon as possible, and to be able to use its capacity to the fullest extent possible. It also cannot be ruled out that it will try to start operating the gas pipeline before the process of certifying the operator has been completed.