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RUSSIA: BACK TO THE FUTURE

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RUSSIA: BACK TO THE FUTURE?

THURSDAY, JUNE 29, 2006

U.S. SENATE,
COMMITTEE ON FOREIGN RELATIONS,
Washington, DC.

The committee met, pursuant to notice, at 9:07 a.m., in room SD–419, Dirksen Senate Office Building, Hon. Richard G. Lugar (chairman of the committee) presiding.

Present: Senators Lugar and Biden.

OPENING STATEMENT OF HON. RICHARD G. LUGAR, U.S. SENATOR FROM INDIANA

The CHAIRMAN. The Foreign Relations Committee meets to examine the current status of political developments in Russia and the future of the United States-Russia relationship. Today's inquiry builds upon two hearings on Russia that the committee held last year. At those hearings, I noted that President Putin's increasingly authoritarian style, his control of the media, and his retribution against political opponents have left the fate of the democracy in Russia more ambiguous than at any time since the collapse of the communist system. These internal developments, coupled with Russia's increasing pressure on its neighbors, its resistance to resolute international action to the proliferation threat in Iran, and its willingness to use its energy supplies for political leverage, have complicated United States-Russian relations.

Russia's membership in the G–8 was once a hopeful sign of its evolution toward a more open society and economy. Now, as Russia prepares to host the G–8 summit in St. Petersburg, the other seven G–8 nations are dealing with the incongruous elements of Russian membership. And while some have called for the United States to boycott the summit, I support the administration's decision to participate. Rather than boycott, we should build cooperation with our allies in challenging negative trends that we perceive coming out of Moscow.

The United States, Europe, and Japan should show strong support for Russian civil society, a free and independent media, the application of the rule of law, and a resolution of conflicts in the region, while keeping under careful scrutiny the implementation of Russia's new NGO law.

Russia is an important country with which the United States must have a working relationship. Attempting to isolate Russia is likely to be self-defeating and harmful to American interests. The dilemma for American policymakers is how to strengthen Russia's respect for democracy while simultaneously advancing cooperation

with Russia on issues that are vital to American security and prosperity. The United States must take the long view. Russia is still in the early stages of a complicated post-Soviet evolution. The United States and Russia do have many convergent goals. We share a strong interest in combating terrorism and safeguarding weapons of mass destruction. Russia's oil and natural gas reserves have provided it with an economic windfall. But, over the long run, it will need to achieve economic diversification and greater integration with Western economies if it is to have more than a one-dimensional economy.

The Putin government's foreign policy and domestic political strategy depend heavily on energy revenues. And, according to the Energy Information Agency, Russia will earn about $172 billion in 2006 from oil exports. For every one dollar increase in the value of a barrel of oil, Russia earns an additional $1.4 billion per year in revenue. In the short run, this influx of hard currency has eased many structural problems of the Russian economy and provided the Putin government with the means to reward supporters. It also gives Russia enhanced influence over nations in Europe and elsewhere who are dependent on Russian oil and natural gas.

This was underscored last January, when Russia stopped pumping natural gas to Ukraine after the two sides had failed to reach agreement on Russia's proposed quadrupling of the price of gas. The agreement that resolved the crisis will soon expire, and President Putin again faces a choice of whether the world should view him as a reliable and productive energy security partner. But, even beyond Ukraine's situation, threats to divert energy supplies eastward and interference in development of energy resources in Central Asia are unacceptable.

The United States must engage with Russia on energy security to send a clear and strong message promoting principles of transparency, rule of law, and sustainability. Efforts under the current United States-Russia energy dialog are an integral part of our diplomatic relationship with Russia and should be expanded and fully supported.

I've introduced Senate bill 2435, the Energy Diplomacy and Security Act, which recognizes the new reality of energy as a national security priority. It enhances United States energy diplomacy capabilities to support the type of rigorous energy security dialog we must have with Russia and other important nations in the global energy equation. Such a dialog must recognize the long-term mutual interests shared by the United States and Russia in stable energy markets.

We are joined by a distinguished panel this morning that will help us examine the trends in Russia and options for United States policy, particularly as they relate to the G–8 summit. We welcome Ambassador Stephen Sestanovich, the George F. Kennan senior fellow for Russian and Eurasian Studies at the Council on Foreign Relations; Dr. Dmitri Trenin, Deputy Director at the Carnegie Moscow Center, in Moscow; and Ms. Amy Myers Jaffe, the Wallace S. Wilson fellow at the Baker Institute Energy Forum at Rice University. And, parenthetically, I would like to say I am pleased Ms. Jaffe will be speaking on domestic energy security issues at the Lugar-Purdue Energy Summit at the end of August. We look for-

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ward to seeing you again on that occasion in Indiana. Now, we thank our witnesses for joining us today. We look forward to their insights.

As I have mentioned to our witnesses, we will try to conclude our hearing sometime in the area of 10:45 to 11 o'clock to make it possible for the committee to have an important markup of the India nuclear security legislation, which we will also take up today in an eventful morning. But we should not be rushed in the process. I ask each of the witnesses to know that your full statements will be made a part of the record, and to summarize, as you wish, but to take time, because we are here to hear you and your counsel today. Then we'll have a round of questions with members who will be joining us.

As my colleague, Senator Biden, our distinguished ranking member, joins us, I will ask him, also, for his opening statement.

Now, we'll recognize you in the order that I first listed your presence, and that would start with the Honorable Stephen Sestanovich. And if you would please proceed, Steve, we'd much appreciate it.

STATEMENT OF HON. STEPHEN SESTANOVICH, GEORGE F. KENNAN SENIOR FELLOW FOR RUSSIAN AND EURASIAN STUDIES, COUNCIL ON FOREIGN RELATIONS, WASHINGTON, DC

Ambassador SESTANOVICH. Mr. Chairman, thank you. It's an honor to appear before your committee again with such distinguished colleagues and to have the opportunity to address the important policy questions you've sketched in your remarks.

It won't surprise you that I'm armed today with many copies of the recent report of the Council on Foreign Relations Task Force on Russia. My hope is that you will instruct committee staff members to remind you of the report's recommendations on a daily basis.

The CHAIRMAN. And to advise members to read the report, perhaps.

Ambassador SESTANOVICH. Let's hope so.

I have prepared a brief written statement, and hope that it can be entered into the published record of this hearing. It touches on a series of issues that I'm sure we will address in the course of our discussion.

First, Russia's economic and social transformation, not only the surge of economic growth in this decade, but the gradual emergence of a middle class, with all that that should mean.

Second, the political transformation that has accompanied these economic and social changes, a centralization of power that has undone much of Russia's post-Soviet pluralism.

Third, the persistence of Russian-American cooperation on first-order security issues, cooperation that is always incomplete and never problem-free, but that serves the interests of both sides. We see this most recently, as you noted, Senator, and most notably, in diplomatic efforts to check Iran's nuclear activities.

Finally, the fourth theme, the erosion of Russian-American partnership on other problems. Even issues that were supposed to involve the clearest examples of common interest, like energy secu-

rity or counterterrorism efforts, have been affected. The most acute disagreements arise from Russia's relations with its neighbors and from Russia's internal evolution.

Mr. Chairman, we're entering a new phase of Russian-American relations, not so tense and dangerous that it should be thought of as a new cold war—one hears this phrase these days—but, all the same, one that will confront us with some unfamiliar choices. For this reason, rather than summarize the analysis contained in the statement I've submitted, I'd like to offer a few thoughts about the dilemmas that American policymakers will face as they try to define this new relationship.

I see three dilemmas—one having to do with the traditional goal of integrating Russia into international frameworks, a second involving the steadily more challenging problem of Russia's relations with its neighbors, and a third involving what a colleague of mine has called Russia's "de-democratization."

First, about integration. We're almost at the 15-year anniversary of the collapse of Soviet communism. Throughout this period, American policy has tried to increase Russian participation in multilateral structures—the G–8, APEC, the OSCE, the WTO, the Council of Europe, even NATO. One could go on: ASEAN, the Bosnia Contact Group, the Mid-East Quartet. In this effort, doubts about how well Russia fits in, whether it has really bought into the group aims and ethos, have generally been overridden by a desire to have Moscow inside the tent. The current controversy over President Putin's chairmanship of the G–8 is just the latest version of this dilemma.

Most people, like the members of the CFR Task Force, I might add, generally favor inclusiveness. But Russia's internal evolution makes the choice a less obvious one. After all, a member that doesn't buy into group norms usually makes the group work less well. There's much to say on this subject, whether in connection with WTO accession or with the OSCE's election monitoring role or with Rosneft's IPO, but let me simply state the dilemma. If we're entering a period in which Russia's lack of buy-in is a greater problem, do we come down on the side of greater inclusiveness or of protecting the effectiveness and integrity of our institutions?

Second, a dilemma concerning Russia's policy toward neighbors. For 15 years it has been American policy to try to develop good relations with almost all the post-Soviet states and to finesse problems that arose when their relations with each other were not good. The approach was usually a workable one, and it particularly served the interests of states that were hoping to expand their ties to the West without provoking Moscow's wrath. But Russia's deteriorating relations with several of its neighbors, and their own readiness to take more dramatic steps, may make this strategy of finesse harder to apply. Remember, several states are now talking about quitting the CIS, the Commonwealth of Independent States, the regional organization that Russia dominates, for good. And applicants for NATO membership now include core constituents parts of the former Soviet Union; for that matter, of the Russian empire.

Here's the dilemma we need to bear in mind. If we value good relations with all sides among the post-Soviet states, will we end up giving vulnerable states less support than they need? If, how-

ever, we offer them fuller support, will we only feed Russia's sense of grievance and stimulate greater confrontation with states that are hard to help?

Finally, a word about Russia's drift away from democratic institutions and values. For 15 years, American policymakers have wanted to see the best in what was happening in Russia. We have sometimes pulled out punches so as not to weaken democratic leaders who were, we thought, doing their best under difficult circumstances. Criticizing them, it was feared, would undercut them and undermine American influence.

Today, this problem looks a little different to all of us. It's harder to think of Russia's leaders as well-meaning democrats simply doing the best they can. And at a time when anti-American sentiment seems to be on the rise in Russia, the question of how to have real influence is more acute than ever.

It frames choices for us like the following. Will speaking out more openly about democracy only identify it as a lever that Westerners use to weaken Russia? Won't we, thereby, weaken support for democracy, even among people who should be its natural advocates? On the other hand, if we confine Russian-American dealings to narrow, practical matters of what we would call national interest, won't we confirm, once and for all, for skeptical Russians, that the United States does not understand, as one Russian friend put it to me recently, the difference between good and evil?

Mr. Chairman, these are genuinely hard questions, and there may be no "one size fits all" answers for them. But we're going to need answers of some kind. Let me venture one suggestion about how—or, more precisely, where—to start thinking about these questions. However cleverly we may analyze these issues in this hearing room, in our government, in the op-ed pages of our newspapers, we're unlikely to hit on good answers—and, still less, on good policies—unless we undertake this effort with our friends and allies in Europe, in both the European Union and in NATO. And we're unlikely to have the influence that we want with any of the post-Soviet space—with the post-Soviet states unless we are pursuing a policy that has been developed jointly with our allies. There are few policy problems more worthy of urgent collective thought with our closest friends than these.

Thank you, and I look forward to this discussion.

[The prepared statement of Ambassador Sestanovich follows:]

PREPARED STATEMENT OF HON. STEPHEN SESTANOVICH, GEORGE F. KENNAN SENIOR FELLOW FOR RUSSIAN AND EURASIAN STUDIES, COUNCIL ON FOREIGN RELATIONS, WASHINGTON, DC

Mr. Chairman, I want to thank you and your colleagues for the invitation to join you in today's hearing on Russia and Russian-American relations.

Your discussion of these questions is important and timely. Not so long ago, Russia's internal evolution and the state of relations between Moscow and Washington were hardly topics of public debate. We can already regret this inattention. Certainly when the leaders of the G–8 agreed in the summer of 2002 to hold this year's meeting in St. Petersburg, they did not imagine that 4 years later legislators, policymakers, and experts might be discussing whether we have entered a "new cold war" with Russia.

Has the cold war resumed? My emphatic answer to this question is no. The interests of neither side would be served by such a conflict, and there is no serious basis for it. But something does appear to have gone wrong with the widely-shared expectation of a few years back, that Russia was rejoining the West. Its internal evo-

lution, its foreign policy, and the outlook of its leaders were thought to be creating the basis for a stronger partnership with the United States and the world's leading democratic states. How differently things have turned out is suggested by the very title of Dmitri Trenin's article in the current issue of Foreign Affairs: "Russia Leaves the West."

I should note here that, to understand precisely what has gone wrong, the Council on Foreign Relations last year constituted an independent task force on U.S. policy toward Russia, under the cochairmanship of John Edwards and Jack Kemp. Its members included distinguished scholars, business leaders, representatives of nongovernmental organizations with long experience in Russia, and former senior officials from administrations of both parties. My remarks to you today are shaped by the conclusions and recommendations of this group, whose report was issued last March under the title, "Russia's Wrong Direction: What the U.S. Can and Should Do."

The Task Force began its deliberations with this assumption, to which it remained committed throughout its work: Russia matters. If one looks at the big issues that affect the security and well-being of the United States now and in the future—terrorism, the proliferation of weapons of mass destruction, tight energy markets, climate change, the drug trade, infectious diseases, human trafficking—it's hard not to notice that Russia is a major factor in almost all of them. The United States will have a better chance of dealing effectively with these issues if Russia is on our side, sees problems the way we do, and can contribute to resolving them.

Of course, it would have been possible to say exactly this at virtually any point in the past 15 years. During most of this period, Russia was treated as a major power largely as a matter of courtesy. In 1998, had the other members of the G–8 doubted Russia's fitness to sit at the same table with them, it would probably have been because Russia was the only one present in danger of an imminent financial meltdown.

The revival of sustained economic growth has changed all this. In the 1990s Russia struggled to pass its annual budget, limped from one unsatisfactory agreement with international lenders to the next, and attracted less foreign investor interest than tiny countries of Central and Eastern Europe. In 2006, Russia will record its eighth consecutive year of growth (a cumulative expansion that has increased GDP by 65 percent), and its fifth consecutive budget surplus. Last week its finance minister announced that Russia will pay its remaining Paris Club debt early. Wage and pension arrears—for years a source of routine hardship for teachers, civil servants, doctors, and millions of other Russians—have virtually disappeared. The national unemployment rate has dropped from 10 percent to 7 percent since 2000; and the number of Russians living below the government's poverty line dropped from 42 million in 2000 to 26 million in 2004 (and strong growth since then has surely reduced the number further).

This success story goes beyond the easing of everyday life for the poorest of Russian society, or the burgeoning number of its billionaires, or the strength of the government's credit rating. For the first time in a century, a Russian middle class is emerging. Measured by many Russian sociologists at approximately a quarter of the national population, it reflects changing consumption patterns, the confidence of those who have at last become property owners, the expansion of small business, higher educational levels, greater travel opportunities, and a mindset of new attitudes and expectations.

Any political scientist can tell you that such a social and economic transformation is the essential guarantee of a "normal" political system—and should cement a positive Russian-American partnership. This was the hope and conviction of all who were involved in U.S. policy toward Russia in the 1990s, and I am sure it remains so today. Over the long term, the emergence of a Russian middle class may well play exactly this crucial historical role. But in the short term it has not done so.

Instead, at every level of Russian politics, the dominant trend of the past 5 years has been toward the erosion of pluralism and, in its place, the arbitrary and unregulated exercise of state power. This has been true of relations between the branches of the Federal Government, between center and periphery, between the government and the media, between government and civil society, and between those who wield political power and those who command economic resources.

The result of this concentration of power is easy to summarize: Russia's institutions are less transparent, less open, less pluralist, less subject to the rule of law, and less vulnerable to the criticism and restraints of a vigorous opposition or independent media. In today's Russia there are no real counterweights of any kind to the Kremlin and the state bureaucracy. The most important decisions concerning the future of the nation are made by a handful of people exercising power for which they will not in any meaningful sense be held accountable.

Even where elections continue to take place (and this is for a shrinking number of offices) they are under very careful and effective control. Opposition parties can be kept off the ballot by denying them registration. Once on the ballot, they can be removed in the course of a campaign if they seem to be building too much popular support. They can be denied television time and starved of political contributions. This past spring the leader of one opposition party was actually removed from his post because he had fallen out of favor with the Kremlin.

In 1998, then, Russia may have stood out at the G–8 as the only member on the verge of financial collapse. Today it stands out as the only member moving away from the modem political mainstream.

It is often said that by the end of the 1990s—a decade that brought economic privation, fractious politics, bureaucratic corruption and a seeming breakdown in the effectiveness of state institutions—the Russian people desired relief from disorder. They do not really mind, it is thought, a little authoritarianism if that's what it takes to solve their country's problems. President Putin's centralization of power, in this view, is exactly what the people want.

It is impossible to question Mr. Putin's popularity—polls consistently give him a high approval rating, most recently 70 percent. And if Russians like their President, Americans have no business second-guessing them. But we should not over-interpret Mr. Putin's popularity—or equate it with stability and, still less, effective governance. It is one thing to say that Russians like their leader, quite another to say that they think he is actually solving their problems, or that they like bureaucratic authoritarianism, think it should continue, and would vote for it if presented with serious alternatives in an open political process. The same polls, after all, show that 70 percent of Russians disapprove of the performance of Mr. Putin's government. And although one sometimes hears that he captured strong support for his populist campaign to exile or imprison a number of "oligarchs," a recent poll suggests that ordinary Russians have different priorities: 79 percent answered that it is corrupt state officials that are harming the country most. (Only 12 percent said rich businessmen were doing more harm.)

Similarly, while it is very common to hear that Russians do not understand and are not ready for democracy, polls show that, in fact, strong popular majorities want a vigorous opposition and independent media able to criticize public officials. In this, they seem to know something that President Putin does not. Although he promises to attack official corruption, he has apparently not made the connection between this goal and a competitive political system, bureaucratic transparency and accountability, investigative journalism, and a vigorous nongovernmental sector. To the extent the Kremlin has a policy on corruption, it is this: Systematically to weaken the most potent tools for combatting it.

Mr. Chairman, this reading of Russia's domestic evolution is not a matter of much dispute among informed observers, either here or in Russia itself. Specialists may disagree about certain points, such as how great the differences are between the current situation and that of the 1990s. There are also disagreements about the likely future trajectory of Russian politics—about whether things are likely to get worse before they better, about how unified the current ruling group is, about the time frame over which a more normal system serving the interests of the emergent middle class might take shape.

But these disagreements are at the margin. They do not really alter the basic judgment about the extreme centralization of power in contemporary Russia or about the absence of checks on its arbitrary use. There is, however, more room for disagreement about what all of this means, or should mean, for Russian-American relations.

Let me first focus on what it does not mean. It does not mean that the United States and Russia cannot or should not cooperate on first-order problems involving the security interests of both sides. Some of these issues have lately been a prominent part of the Russian-American agenda, and the record suggests that Washington and Moscow are not having any difficulty working together. Iran's effort to develop its nuclear-weapons options is an outstanding case in point. I doubt that any other issue has been more frequently discussed between Secretary Rice and Foreign Minister Lavrov over the past year. During this same period worries about Russia's internal direction have been more openly expressed by American officials at all levels—most recently, by the Vice President. Even so, Russian and American approaches to Iran have remained broadly convergent. Russia does not refuse to cooperate on security issues because we refuse to call it a democracy.

The same is true of cooperation on the so-called "loose nukes" question. Less than two weeks ago, Russian and American negotiators were able to finalize an agreement to renew the umbrella agreement under which "Nunn-Lugar" programs to improve the safety and security of sensitive, especially nuclear-weapons-grade mate-

rials have been conducted. There is no reason to expect this pattern to change. When cooperation rests on a compelling Russian security interest, disagreement on other matters is not going to derail it.

The fact that cooperation on such issues is possible does not, of course, mean that it is automatic or complete. There remain important differences between the way Russian policymakers view these issues and the outlook of American and European officials. Moscow, for example, appears reluctant to associate itself with a strategy of threatening Iran with international isolation if it continues on its present track. By the same token, it is Russian policy to assure Tehran that it will be able to resume an enrichment program once it addresses questions about past nuclear activities and accepts appropriate safeguards.

Despite these differences, the United States has over the past year been able to win increased Russian support for measures that isolate Tehran. Without forgetting the possibility of disagreements in the future, it should be American policy to create an even stronger foundation for Russian-American nuclear cooperation in general. (For this reason, I might note that the Kemp-Edwards CFR Task Force supported the opening of bilateral negotiations on a so-called "123 agreement"—which would make possible cooperation on civil nuclear energy projects. Without such an agreement, the U.S. lacks the legal and institutional infrastructure to expand cooperation in this field.)

Nonproliferation and nuclear security represent one extreme in Russian-American relations. They are the issues on which two sides have retained an ability to work together, largely unaffected by the negative trends of Russian domestic politics. Unfortunately, these issues do not represent the whole of the relationship. In other areas, cooperation has often given way to discord, even in instances where American policy has until recently taken for granted a strong common interest.

Counterterrorism provides one of the most striking—and in some respects, most surprising—examples. Since at least 2001, the threat of terrorist attacks has been Exhibit A for the argument that in dealing with the new security challenges of our time Russia and the U.S. have to stick together. How then to understand the strange Russian initiative at last year's summit meeting of the Shanghai Cooperation Organization, calling on Washington to end its use of military bases in Central Asia? Access to these bases by NATO and American forces has, of course, only one purpose—to support their operations in Afghanistan. Russia professes to agree with what we and our allies are doing in Afghanistan, but for Moscow this interest was apparently trumped by another factor. Recall that last summer the United States and the governments of the European Union found themselves in the middle of a disagreement with the President of Uzbekistan about what kind of an inquiry there should be into the mass killing of civilians by Uzbek forces. What President Putin apparently saw in this standoff was an opportunity—too inviting to resist—for a partial roll back of the American presence in Central Asia. His stance surely encouraged the Uzbek government's decision to end Western use of the most important airfield in the region. More significantly, it demonstrated that a seemingly strong common interest can easily be subordinated to petty geopolitical point-scoring.

Moscow's confrontation with Ukraine over gas supplies and prices teaches a similar lesson. It would be hard to imagine a more significant Russian interest than its reputation as a reliable supplier of energy to international, especially European, markets. Nothing has ever done more to damage this reputation than the unprecedented decision last January to turn off the gas to Ukraine—and with it, to the rest of Europe. It is still not easy to make commercial sense of this action, since neither Ukraine nor Russia's other European customers (nor for that matter, the United States) disputed the idea that energy relations should be governed by market pricing. The strange Russian handling of the affair—in particular, President Putin's aggressive public role as the lead policy spokesman—made it clear that for Moscow this was in reality a political confrontation, not simply a commercial one. Ukraine's new leadership had come to power in one of the most embarrassing Russian policy debacles of recent years. Now, on the eve of parliamentary elections, the leadership of the "Orange coalition" was divided, and energy clearly seemed a tool for dealing it a further political setback.

Mr. Chairman, this affair was deeply shocking for European policymakers. Subsequent Russian actions and statements—such as the blunt comment last spring by Gazprom management that Russia might simply sell its gas elsewhere if European countries are not willing to cede targeted chunks of their energy infrastructure, or last week's announcement that Russia has no intention of ratifying the European Energy Charter—have only deepened this concern.

These two episodes—one involving counterterrorism cooperation; the other, commercial energy contracts—have a unifying theme. They suggest that over the next several years Russia's interactions with its neighbors are likely to play an increas-

ing—and increasingly negative—role in Russian-American relations. As former prime minister Yegor Gaidar put it recently, Russia has entered a "dangerous period of post-imperial nostalgia." Already the apparent desire to assert a vanished primacy has prompted Russia's leaders to take actions that other governments find irresponsible. It is important to note that Russian policymakers have also shown themselves capable of quick backtracking once they see how deeply counterproductive their actions really are. This rapid learning has kept conflicts from escalating, but it too has its costs. In any country, retreating in the face of fierce international criticism stores up resentments for the future; in Russia it feeds a conviction that the other major powers consistently treat it unfairly.

Mr. Chairman, over the next 2 to 3 years, the U.S.-Russian relationship will sometimes seem like two different relationships, based on different principles and expectations. Particularly on those security issues where the interests of the two sides make it easy and necessary to work together, cooperation will continue. Yet on other issues—indeed, on a growing number of them—disagreement and discord seem more likely.

Without dramatizing this transformation, or calling it a "new cold war," we should recognize that accumulated frictions between Russia and the United States can over time have consequences that go well beyond a downturn in bilateral relations. They raise the prospect of a broader weakening of unity among the leading states of the international system. If growing consensus among the major powers gives way to a new line of division between democrats and authoritarians, if their energy strategies diverge, or if they respond in different ways to terrorism, America's chances of success in meeting global challenges will be reduced. At present, the risk that such divisions will emerge may seem remote, but policymakers in both the Congress and the Executive Branch should not fail to anticipate the tipping point. Americans should understand how much Russia's future course—above all, whether its policies, at home and abroad, move further from the Western mainstream—can affect the outcome.

Thank you.

The CHAIRMAN. Well, thank you very, very much for that excellent testimony and for your entire paper, which will be made a part of the record.

Ambassador SESTANOVICH. Thanks.

The CHAIRMAN. Dr. Trenin, we're delighted to have you again before the committee, and would you please proceed?

STATEMENT OF DMITRI TRENIN, DEPUTY DIRECTOR, PROGRAM COCHAIR, SENIOR ASSOCIATE, FOREIGN AND SECURITY POLICY, CARNEGIE MOSCOW CENTER, CARNEGIE ENDOWMENT FOR INTERNATIONAL PEACE, MOSCOW, RUSSIA

Dr. TRENIN. Thank you very much, Mr. Chairman. It's—is it working? Yeah. Thank you very much, Mr. Chairman. It's a high honor and a rare privilege for me to testify before the committee.

I, too, produced a written statement, which, as you said, will be made——

The CHAIRMAN. Yes.

Dr. TRENIN [continuing]. Part of the——

The CHAIRMAN. In full.

Dr. TRENIN [continuing]. Official record.

Let me highlight some of the things, and expand some of the things, which form the basis of that statement.

I agree, in many respects, with what my distinguished colleague and friend Steve Sestanovich has laid out, but let me add a different dimension to what he has said.

Russia is a country which has what I would call a tsarist political system, with all major decisions taken, essentially, by one institution, the Presidency. Over the past 6 years, the degree of power centralization in Russia has grown dramatically. While authoritarian and overcentralized, however, the Russian political system

rests on the acquiescence of the governed. If you like, this is a version of authoritarianism which is democratically legitimized. Now, this is something which is occasionally not given proper attention.

Seen historically, I do not think that Russia is heading in the wrong direction. Whatever the current ups and downs of Russia's domestic politics are, and Russia's economic development are. Russia—rather, in my view, it has returned to the path of natural development which—that she was forced to abandon by the Bolsheviks. It was never serious to expect Russia to become a liberal democracy after three-quarters of a century of communist rule. By the same token, to regard Yeltsin's Russia as a democracy was wishful thinking. Russia was freer and more pluralist in Yeltsin's times, but this was mostly the result of the state being too weak, rather than the democratic forces assuming a major role in the country's politics.

In the future, as well, there will be no cutting corners. For a number of reasons, Russia's modernization cannot proceed through integration into the European and Euro-Atlantic institutions, as was the case in Central Europe, and could be the case in Eastern Europe, as well. Russia would have to perform the feat of modernization on its own. There are many factors working against that. However, there are several important and powerful factors working for that. And one of the factors is the development of capitalism, and the other one is the openness of the country to the outside world.

I would submit to you that Russia's story is not the story of a failing democracy. I think democracy in Russia is a thing for the future. But, rather, this is a story of evolving capitalism. It's not yet market capitalism, but it's a very real and vibrant, if rough, capitalism.

What I find as a weak point in the criticism of the current Kremlin policies is the assumption, either stated or not, that should pressure on the Russian authorities be kept up at a high level for a sufficiently long period of time, either the Kremlin will relent or it will be defeated in some version of a democratic revolution, and a new, better Russia would somehow emerge. I have been caricaturizing a little bit, but I find this to be a very dangerous illusion.

Positive changes in Russia will come, and they will come from within, but they will need time—and, I would say, a long time—to coalesce. I think that what was highlighted in—at the very beginning of Ambassador Sestanovich's presentation, the growth and the future role of the middle class, is the thing that will ultimately lead Russia on the road to a functioning democracy.

That does not mean, however, that the outside factor has no role in how Russia is developing. However, this outside factor will not be some foreign government's pressure; but, rather, the general openness of Russia, which I have already mentioned, to the outside world, and, in particular, its proximity to the European Union—again, another issue that Ambassador Sestanovich highlighted in his presentation.

Throughout Russian history, impatience with the pace of Russia's modernization has been a recurring theme—and, I would add, a re-

curring problem. It is understandable, but it is not necessarily very helpful.

Turning to Russia's foreign policy, one thing I want to stress from the very beginning, that in contrast to the 1990s and the early 2000s, the Russian leadership is no longer practicing accommodation and adjustment par excellence to the international environment; rather, it is seeking to return to the world scene as a major independence player. There is a widespread perception among the Russian leadership that in the 1990s their country was anything but sovereign, that it was weak and overdependent on others, led by the United States. Russia's policies today could be seen as a backlash to that reality or perception, however you choose to look at that.

In this situation, it is a reasonable policy for the United States to look for that in various areas of common ground, and those areas have been richly defined in Ambassador Sestanovich's presentation, and I do not want to go over the same ground again.

But let me focus on one issue in the remaining few minutes that I have, and that is the United States-Russian interaction in the former Soviet Union. Let me state very frankly that the Putin administration's strategic objective is creating a Moscow-led power center in the former Soviet Union. They look at Russia as a great power, and they look at the former Soviet Republics as areas where Russian business influence, political influence, security influence, and cultural influence should be bolstered.

Most of the member states of the still-functioning, still-existing Commonwealth of Independent States are likely to respect Russia's interests and will seek, in return, to draw benefits from their close relations with Russia. However, none of them is likely to become Russia's satellite. I don't think that, even today, one can name a single post-Soviet country that is controlled by Moscow.

Let me address one issue within this context which I think is extremely important and potentially very dangerous. Over the past decade and a half, Russia has internalized both Ukraine's independence and the border that divides the two countries. More recently, it has learned to live with the consequences of the Orange Revolution and Ukraine's political pluralism. However, Ukraine's bid to join NATO and the prospect of a membership action plan being offered to Ukraine at the next NATO summit in Riga, in late November this year, puts this relationship to a very major test. Ironically, the step designed to finally guarantee Ukraine's territorial integrity has the potential of reawakening the sleeping issues, such as the status of the heavily Russian-populated Crimea, home of the Russian Black Sea fleet. The situation is highly complex due to the low popularity of NATO accession among the Ukrainian population, who will need to vote on the issue in the national referendum. There are differences on the NATO issue even among the coalition partners and ambivalence within the principal political parties. The stakes are unusually high, not to be compared with either the Polish-Czech-Hungarian or the Baltic-Romanian-Bulgarian accessions to the Atlantic Alliance. Not only is Ukraine different from Poland or Latvia, the Russia of 2006 is very different from the Russia of 1996, or even the Russia of 2002.

Shall I continue, Mr. Chairman?

The CHAIRMAN. Yes, please.

Dr. TRENIN. In the next few months and years, Ukraine can become a political battleground between the competing domestic forces and also between Russia and the United States with important and not yet predictable consequences for all the parties involved.

To put it very mildly, not everything depends on Russia in the United States-Russian relationship. Russian cooperation on the United States agenda items will depend on how the Russian leadership will judge United States actions on the Russian agenda priorities. Although many in the Russian policy establishment today view the situation in the former Soviet Union in terms of a zero-sum game, and, in their view, with the United States actively working to undermine Moscow's influence in the new states, developments in Ukraine and also in Georgia, which are approaching danger points, call for a serious thinking and dialog which would help avoid misunderstanding and even confrontation which would put the United States-Russian relationship toward a new low.

Let me say, in conclusion, that the title of the hearing, "Russia: Back to the Future?" could be read, in my view, as "Russia returning to the path it quit 90 years ago on its communist adventure," rather than backsliding to Soviet days. It is tsarist, capitalist, open, relatively free, in many respects—though not, I emphasize, in the political sphere—increasingly nationalist, another thing which needs to be highlighted. And Russia is the last former communist country to have discovered nationalism, though of a peculiar post-imperial variety. Russia is also assertive internationally. At this point, it is neither pro-United States nor anti-United States. It is a challenge to deal with Russia, but ignoring or misreading it, as my friend and colleague has said, carries a price.

Thank you very much.

[The prepared statement of Dr. Trenin follows:]

PREPARED STATEMENT OF DR. DMITRI TRENIN, DEPUTY DIRECTOR, PROGRAM CO-CHAIR, SENIOR ASSOCIATE, FOREIGN AND SECURITY POLICY, CARNEGIE MOSCOW CENTER, CARNEGIE ENDOWMENT FOR INTERNATIONAL PEACE, MOSCOW, RUSSIA

Mr. Chairman, ladies and gentlemen of the committee, it is an honor and a privilege to be asked to testify before this committee. Let me address the issues I was asked to comment on in the letter of invitation signed by Senator Lugar.

DEVELOPMENTS IN RUSSIA AND THEIR POTENTIAL IMPACT ON THE FUTURE OF THE UNITED STATES-RUSSIA RELATIONSHIP

Political reform

Russia has a tsarist political system, in which all major decisions are taken by one institution, the Presidency. In fact, this is the only functioning political institution in the country. Separation of powers, enshrined in the 1993 Constitution, does not exist in reality. On the contrary, unity of power and authority has become the new state-building doctrine. All other federal institutions (i.e., the parliament, the cabinet, the high courts) are dependent on, and de facto subordinate to the President and his private office (collectively referred to as the Kremlin). The tradition is back in the saddle.

Over the last 6 years, the degree of power centralization has grown dramatically. Regional legislation has been brought in conformity with the federal Constitution and federal laws. The Federation Council (upper chamber) has ceased to be the regional leaders' club and has become a Russian version of the German Bundesrat, with its members (who proudly call themselves senators) appointed, and recalled, by the regional authorities. The governors of Russia's 88 regions have lost their independence rooted in direct elections, and are now hired and fired by the Kremlin.

Single-mandate constituencies in the elections to the State Duma (lower chamber) are being phased out. From the next election (December 2007) on, only party lists will compete, with the entrance bar set very high (7 percent of the popular vote). The reform of the judiciary has not resulted in expanding its independence. The courts are even more dependent on the authorities, and the State Prosecutor's office has become the principal political instrument in the hands of the Kremlin for dealing with its adversaries.

While authoritarian and over-centralized, the Russian political system rests on the acquiescence of the governed. Vladimir Putin has remained popular throughout the 6 years he has been in power. Above all, he is credited with reinstating stability lacking under both Boris Yeltsin and Mikhail Gorbachev. For this democratically legitimized authoritarian system to continue to operate in the current mode, Putin's successor needs to be genuinely popular.

Managing succession under such conditions is extremely difficult. All indicators point to Putin's desire to step aside when his term is up (spring of 2008) and let a new man take over. Yet, both informal successors (first deputy Prime Minister Dmitri Medvedev and Defense Minister Sergei Ivanov who is also a deputy PM) have obvious problems with electoral appeal. Thus, Putin may make an 11th hour surprise choice in favor of a lesser-known figure who would be able to galvanize support for the supreme authority and allow it to sail smoothly through the succession straits.

There can be no guarantee of a smooth sailing, of course. It is true that political opposition in Russia is no match for the authorities. The Communist party, Yeltsin's former nemesis, has been much reduced in influence and effectively locked up in a niche of elderly nostalgics. The liberals and democrats remain pathetically disunited and are growing increasingly marginal. Nationalists represent a more serious challenge. In the past, the Kremlin was been able to tame them with the help of superloyal Mr. Zhirinovsky. However, a recent project to found a pro-Kremlin nationalist party, Rodina (Motherland), led by Dmitri Rogozin, had to be terminated when the party threatened to spin out of control and become a real opposition force. Currently, the Kremlin's strategy is to give a new lease on political life to Mr. Zhirinovsky; to co-opt the more conformist nationalist elements within the ruling bloc, United Russia; and to present extreme nationalists as a "clear and present danger" (to replace the now emasculated Communists) which can only be effectively dealt with by the Kremlin itself.

It is true that ultranationalism and populism are the biggest threat to Russia's domestic development and to Russia's relations with the rest of the world, starting with its neighbors. The problem is the Kremlin's own political effectiveness.

All the unity of power notwithstanding, the Kremlin itself is far from united. The constellation of clans, which could be visibly represented by the many towers of the Kremlin fortress, is never static. There have always been different interests (including some very material ones), different instincts (depending on the people's past experiences), and different views about the way the world goes and the way Russia should be run. While the President reigns, he acts as an arbiter. As he is preparing to hand over power, the situation becomes highly dynamic.

Grosso modo, there are two competing groups whose membership does not neatly coincide with the popular notions of the siloviks vs the liberals. Both factions agree on the need for a strong authority at home and a great-power policy abroad. They differ (apart from their private business interests) on the degree of bureaucratic control over the economy and the assertiveness and unilateralism in Russia's foreign policy. Thus, it is the internal rivalries and clashes, whether within the Presidential administration, the cabinet, or the ruling bloc as a whole, rather than open political competition, that is likely to mark and shape Russia's politics in the near and even medium term.

The implications for the United States and indeed for all other countries are as follows. One has to accept the reality of a highly centralized political system with a sole decision maker. One needs to acknowledge the weakness of the political forces who seek to modernize the system by bringing the competition into the public domain and turning the presently undivided "authority" into a combination of an accountable government and a professional civil service. One has to guard against the (still distant) possibility of ultranationalists and populists taking over the state machine and pushing Russia down the path of absolute state domination at home and revanchism abroad.

Yet, Russia, seen historically, is not going in the wrong direction. Rather, it has returned to the path of natural development which she was forced to abandon by the Bolsheviks. It was never serious to expect Russia to emerge as a liberal democracy after three quarters of a century of Communist rule. By the same token, to regard Yeltsin's Russia as a democracy was wishful thinking. Russia was freer, and

more pluralist, and the state was very weak, but it was not democratic. In the future, there will be no cutting corners. For a number of reasons, Russia's modernization cannot proceed through integration into the European and Euro-Atlantic institutions, as it did in Central Europe and can do in Eastern Europe. Russia would have to perform that feat on its own. There are many factors working against it. There are a few, however, two working for. One is the factor of money, i.e., indigenous capitalist development. The other one is the country's openness to the outside world.

The economy and social affairs

The effect of high energy prices on the Russian economy is twofold: Robust economic growth has continued for 7 years; but the serious economic reforms started in 2000 have been stopped for the time being. The Russian government now wields substantial financial power. Yet, it has been rather conservative with regard to spending money. The Kremlin has created a stabilization fund as a cushion against a steep fall in oil and gas prices. Russia's currency reserves are third-largest in the world. Moscow has been repaying its foreign debt ahead of schedule.

Russian living standards have been steadily rising since the 1998 financial collapse. In the 2000s, an average annual increase in take-home pay has been in the range of 10 percent. In fact, most Russians have never had it so good in their entire history. This, however, is not how a significant portion of the population view things.

In contrast to Soviet uniformity, Russia's social picture is characterized by striking inequality. The top 10 percent of the population have an income 15 times higher than the bottom 10 percent. The middle class comprises a mere 25 percent, but it shows signs of growing. The future of the country will depend on whether some two-fifths of the population immediately beneath it will rise to join the middle class or finally sink into poverty.

Freedom and independence of the media

Russia's electronic media, a powerful political instrument, are controlled by the authorities. The printed press is relatively free still, although this is changing, but their print runs are very small. The Internet is vibrant and free, with the number of users rapidly rising. It has to be borne in mind, however, that the former pluralism of Russian TV was part of the arrangement between the Kremlin and the oligarchs rather than a result of a genuine development of civil society.

On civil society itself, let me say that the process of its formation is clearly linked with the emergence of the middle class, a long and difficult process. At present, the authorities attempt to build institutions of civil society "from above," even as they seek to minimize or eliminate the role of potential political challengers, such as the former oligarchs, or foreign fenders, who are feared to be promoters of "orange-style" revolutions.

Status of the rule of law in Russia

President Putin's first-term slogan was establishing the "dictatorship of law." He promoted a legal reform, designed by his close associate, Dmitri Kozak. Among other things, the reform introduced trial by jury in the more serious cases, and transferred control over the penitentiary system from the Ministry of Internal Affairs (i.e., the police) to the Ministry of Justice. Not surprisingly, reforming the legal system, traditionally but a tool of the authorities, has proven to be exceedingly difficult. Moreover, President Putin has been using the Prosecutor General's office as an instrument of choice to destroy the power of the more ambitious oligarchs: Berezovsky, Gusinsky, and Khodorkovsky. Since the initial accumulation of capital in Russia was essentially lawless, virtually all new capitalists can be plausibly accused of breaking laws. In this situation, political challengers or business rivals can easily be subjected to selective application of justice.

Yet, property ownership requires protection. It would not be too far-fetched to suggest that the Russian elites will be progressively more interested in establishing a system which would guarantee their possessions irrespective of which group happens to control the Kremlin. The emerging Russian middle class, too, is interested in a system that would protect their rights against both the swindlers in the private sector and the arbitrariness of the government bureaucracy. Small public campaigns have already spontaneously risen in defense of a falsely accused motorist; crooked property developers; and homeowners evicted from their houses without fair compensation.

What should be on the United States agenda at the G–8 summit

The G–8 summit and the bilateral meeting of United States and Russian Presidents in St. Petersburg next month offer a chance to clarify the United States agenda regarding Russia.

While Russia is by no means a priority for U.S. foreign policy, it deserves more attention than she is usually given. Very importantly, to bring positive results and satisfaction, that attention needs to be properly focused.

The United States will be best served by a frank, principled, and realistic attitude toward Russia. American leaders should feel free to raise any concerns that they have regarding developments in Russia or in Moscow's foreign policy. Even as they do it, however, they must realize that their chances of influencing the Kremlin's behavior at home or abroad are at best very limited. They should also be ready to hear Russian criticism of U.S. Government's policies, and Russian dismissal of many U.S. claims as either based on double standards, or disingenuous, or devalued by America's own imperfect record.

The common weak point of many Russian and Western critics of the Kremlin is the assumption, either stated or not, that should pressure on the Russian authorities be kept up at a high level for a sufficiently long time, either the Kremlin will relent, or it will be defeated in some version of an democratic revolution, and a new and better Russia would emerge. This is an illusion. Positive changes in Russia will come, and they will come from within, but they will need time to coalesce. The principal outside factor will not be some foreign government's pressure, but Russia's general openness to the outside world, in particular, the proximity of the European Union.

Americans need to realize that in contrast to the 1990s and the early 2000s, the Russian leadership is no longer practicing accommodation and adjustment par excellence to the international environment. Rather, it is seeking to return to the world scene as a major independent player.

In this situation, a reasonable policy by the United States would be to look for areas of common ground. There are several such clusters. One is nuclear issues, starting with WMD proliferation. Though Russia disagrees with some United States policy options regarding Iran and North Korea, nuclear weapons in the hands of either regime would adversely affect Russia's national security. United States-Russian, although understandably not easy, would further United States nonproliferation goals; a break with Russia on that fundamental issue would encourage the proliferators. Thus, Iran and North Korea should be at the top of the list.

Nuclear arms control is another area which needs revisiting. United States-Russian relations are not as amicable as they should be. Mutual suspicions are high. As the bilateral treaties governing nuclear weapons reductions are approaching expiry dates, some thought needs to be given as to the nature of the nuclear weapons relationship between the two nuclear superpowers.

Finally, nuclear energy is a potential area of very productive collaboration. Letting Russia be a significant player in the market presently dominated by the United States and France would be a major incentive for a closer overall relationship between Washington and Moscow. Indeed, it would put a major economic pillar under that relationship, thus stabilizing it.

Another such pillar would be created through United States companies' participation in the exploration of the Shtokman gas field in the Arctic, and the Russian company Gazprom's access to the U.S. LNG market. While Russia cannot be expected to allow foreigners majority stakes in its oil and gas fields, its policy of swapping upstream assets for downstream ones would create real energy interdependence and thus a much higher degree of security.

One way for the United States to contribute to Russia's modernization is through sharing with Russia its best business practices. It is the evolution of Russian capitalism which will push the evolution of Russian society and eventually also Russian polity. In the area of education, creating opportunities for many more Russian students to come to study in the United States would be a major investment in a better future for Russia and a safer world for the United States.

Finally, the challenge of international terrorism and related security threats require closer cooperation in places like Afghanistan. Russia cannot be interested in a U.S./NATO failure in Afghanistan and the return of the Taliban whom Moscow regarded only 5 years ago as the greatest external military threat. The issue of drugs trafficking from Afghanistan calls for joint action between Russia and the United States (and others, including NATO states and the neighboring countries).

Dealing with the problems in United States-Russian relations is as important as exploring the potential of the areas of common ground.

Russia's policies and influence in the former Soviet Union

The Putin administration's strategic objective is creating a Moscow-led power center in the former Soviet Union. This is not a new version of the Russian empire of the U.S.S.R. Rather, the goal is to help Russian companies to acquire lucrative economic assets in the neighboring states (starting with the energy sector), ensure those states' general political loyalty to Russia and full cooperation with it in security matters, and promote the Russian language and culture across the former Soviet space. The principal instruments of this policy, alongside the bilateral contacts, and its symbols, are the Eurasian Economic Community and the Collective Security Treaty Organization.

Most of their member states are likely to respect Russia's interests, and will seek in return to draw benefits from their close relations with Russia. However, they are unlikely to become Russian satellites. Kazakhstan and Belarus, the two countries that are most integrated with Russia economically, are good examples. The former is pursuing a carefully balanced foreign policy, maneuvering among Russia, China and the United States. The latter, though effectively isolated by the United States and the European Union, and heavily dependent on Moscow, refuses to merge into the Russian Federation. Armenia, though it looks to Russia as its historical protector, seeks to strengthen its ties to both the United States and Europe. Uzbekistan, which only last year abruptly turned away from the United States and embraced Moscow, has a long-standing ambition of a regional power, which complicates (also Russia's) relations with the smaller countries, such as Kyrgyzstan and Tajikistan. More ominously, Uzbekistan's Fergana valley continues to be the hotbed of Islamist extremism.

Not all former Soviet countries belong to the Eurasian Economic Community or the Collective Security Treaty Organization. Some of them have come together in alternative communities, supported by the United States, which challenge Russia's policy goals. Among these countries, Ukraine and Georgia are of special importance, from the standpoint of Russia's relations with the United States.

Over the past decade and a half, Russia has internalized both Ukraine's independence and the border dividing the two countries. More recently, it has learned to live with the consequences of the Orange revolution, and Ukraine's political pluralism. However, Ukraine's bid to join NATO and the prospect of a membership action plan (MAP) being offered to Ukraine at the next NATO summit in Riga (late November 2006) puts this relationship to a very major test. Ironically, the step designed to finally guarantee Ukraine's territorial integrity has the potential of reawakening the sleeping issues such as the status of the heavily Russian-populated Crimea, home of the Black Sea Fleet. The situation is highly complex due to the low popularity of NATO accession among the Ukrainian population who will need to vote on the issue in a national referendum. There are differences on the NATO issue even among the coalition partners, and ambivalence within the principal political parties. The stakes are unusually high, not to be compared with either the Polish/Czech/Hungarian or the Baltic/Romanian/Bulgarian accessions. Not only is Ukraine different from Poland or Latvia; the Russia of 2006 is very different from the Russia of 1996 or even 2002. In the next few months and years, Ukraine can well become a political battleground between the competing domestic forces, and also between Russia and the United States, with important consequences for all the parties involved.

Georgia's prospects of joining NATO are more remote. Here, as in Moldova, the relevant issue is the frozen conflicts. Tbilisi's desire to resolve the conflicts in Abkhazia and South Ossetia by imposing a solution, if necessary, contrasts with Moscow's references to the Kosovo model, i.e., promoting a final separation of rebel enclaves. The solution of the Kosovo problem by means of separation and conditional independence, expected by the end of the year, will not lead to Russia's automatic recognition of the breakaway regions, but it would push the situation closer to the red line: Formally revising post-Soviet border arrangements.

Although many in the Russian policy establishment view the situation in terms of a zero-sum game, with the United States actively working to undermine Moscow's influence in the new states, developments in Ukraine and Georgia, which are approaching danger points, call for a serious dialog which would help avoid misunderstanding and avert confrontation which would push the United States-Russian relationship toward a new low.

In conclusion, let me say that the title of the hearing, "Russia: Back to the Future?" should be read as "Russia returning to the path it quit 90 years ago on its Communist adventure, rather than backsliding to Soviet days." It is tsarist, capitalist, open, relatively free in many respects (though not in the political sphere), increasingly nationalist (the last former Communist country to have discovered nationalism, though of a peculiar post-imperial variety), and assertive internationally.

It is neither pro-U.S. nor anti-U.S. It is a challenge to deal with, but ignoring or misreading it carries a price.

Thank you very much.

The CHAIRMAN. Well, thank you, Dr. Trenin, once again, for a very, very thoughtful statement.

I want to recognize, before we come to Ms. Jaffe, the distinguished ranking member of the committee, Senator Biden, for his opening statement.

OPENING STATEMENT OF HON. JOSEPH R. BIDEN, JR., U.S. SENATOR FROM DELAWARE

Senator BIDEN. Thank you very much, Mr. Chairman, for holding this hearing.

And I say to the witnesses, all the flooded tracks along Amtrak kept me from being here on time. I do apologize.

Mr. Chairman, my time and yours and the Senate has spanned the years of Brezhnev, Gorbachev, and a few like Andropov in between, Yeltsin, and Putin. And it's because of that perspective that I'm so concerned about what's going on in Russia today. For most of the last 20 years, Russia has been moving slowly toward Europe, the United States, democracy, and human rights. Obviously, there were a lot of detours along the way, but things were generally headed, in my view, in the right direction.

Since President Putin took office in 2000, Russia has experienced, in my view, the biggest rollback of democracy that's occurred anywhere in the world in decades. The Putin administration has tranquilized the Russian media, muzzled political opponents, neutered the Duma and regional governors, and it has cracked down on the civil society groups, and, I think, to state the obvious, has attempted to undermine the democracy of neighboring countries.

An essential factor enabling and exacerbating these disturbing developments is something you've pointed to often, Mr. Chairman—oil wealth—the oil wealth that Russia possesses. Bullied by the resurgence in global oil prices, even Russia's corrupt and capital-short energy sector has been highly profitable. That wealth has masked fundamental distortions in an increasingly state-influenced energy sector and purchased some democratic support—I mean, purchased some domestic support for Putin and for his administration. That wealth has also become a weapon to threaten and coerce Russia's neighbors and energy customers.

Mr. Chairman, I believe the United States has mismanaged the relationship with Russia over the last 6 years. Many people, myself included, have been speaking about the Kremlin's authoritarian impulses for a long time. Unfortunately, until recently, the administration has not evidenced much interest in such warnings.

I believe that the Putin administration is dealing with two conflicting desires. On one hand, it is determined that Russia be accepted as a great power and respected around the world; on the other, it wants to continue to bully its neighbors, suppress political dissent, and use energy as a weapon of mass disruption.

I hope that President Bush and other leaders of the G–7 will use the summit in St. Petersburg to deliver a simple message, "You can't have it both ways. You can't be a revered great power and a

corrupt authoritarian petrol state at the same time." The two categories are mutually exclusive.

Some Russians have become fond of saying that the West needs them more than they need the West. I'd respectfully suggest that they're wrong, but I learned a long time ago, never tell another man his politics or another country what's in its interest. But, from my perspective, it seems to be wrong.

Despite its recent energy windfall, Russia is facing huge problems. The country's population is plummeting by—has plummeted—is plummeting by over 700,000 each year, mostly due to epidemics such as AIDS, tuberculosis, and alcoholism. Pervasive corruption is rotting the people's faith in the society and its government. And Russia is facing serious security threats from terrorism and instability in the North Caucasus.

The Kremlin would do well to realize the magnitude of these challenges and welcome the assistance of NGOs, civil society groups, and the West in promoting the rule of law and transparency. Russia's government won't be able to use oil and gas money to buy its way out of all this trouble. Unfortunately, some in Russia view any international criticism of the Kremlin as part of a broader plot to weaken their country. If anything, I would argue the reverse is true.

I hope, for Russia, that it's respected—my hope for Russia is that it become a respected, prosperous, and democratic state—strong. I believe that the current policies of President Putin's government work against these goals. They may, in my view, condemn Russia to a future of weakness and instability and deny Russia its rightful place as a great power.

I'm hopeful, if not optimistic, that we can change the dynamics of our relationship with Russia, but, for that to happen, I believe the United States needs to do at least three things. And I will conclude, Mr. Chairman.

First, the President should pick up the phone today and start coordinating with other leaders of the democratic G–7 nations. The Kremlin has been very successful in dividing democratic nations, many of whom share the blame for glossing over the negative trends in Russia. It's time for that to change. The G–7 nations should issue a tough, coordinated statement in St. Petersburg which would make it clear to the world that Russia's recent behavior is unacceptable.

Second, the United States should make sure that NATO provides Ukraine and Georgia with membership action plans by the end of this year. If those two countries are put on track to join NATO, it will help consolidate the reforms that have occurred since the Orange and Rose Revolutions. It would also, I think, defer—deter future Russian meddling in other nearby countries. If Georgia and Ukraine are not offered MAP agreements, I worry Russia will see that as a green light to continue undermining democratic governments in other states. It's time to give these countries the security assurances they need to move ahead with the tough work of building the democracy.

And, last, I believe that the United States and democracies everywhere need to be—need to dramatically increase their support for NGOs and civil society groups working to promote democratic

values in Russia. Despite new laws cracking down on NGOs in Russia, they are still the best hope for promoting freedom, transparency, and the rule of law, in my view. If the West wants democracy to be an issue in Russia's 2008 Presidential elections, we've got to start doing more to help build the infrastructure of democracy now.

Mr. Chairman, again, I apologize for interrupting the witnesses' testimony here, but I am pleased that you allowed me to make my statement at this time, and I'm eager to hear what our last witness, I guess—or maybe there's two more to go, I don't know, having come late—what they have to say, and the recommendations, how we can move forward with these and other needed changes in our relationship with Russia.

Thank you, Mr. Chairman.

The CHAIRMAN. Well, thank you very much, Senator Biden. As you would know, if you had heard all the testimony, your statement fits well into the dialog we were having.

Senator BIDEN. Good.

The CHAIRMAN. These are issues on which we are all expressing opinions before we come into our question-and-answer.

I'd now like to call upon Ms. Jaffe for your testimony. We look forward to hearing you.

STATEMENT OF AMY MYERS JAFFE, WALLACE S. WILSON FELLOW IN ENERGY STUDIES, ASSOCIATE DIRECTOR, RICE UNIVERSITY ENERGY PROGRAM, JAMES A. BAKER III INSTITUTE FOR PUBLIC POLICY, RICE UNIVERSITY, HOUSTON, TX

Ms. JAFFE. Thank you very much, Senator.

It's really a great honor to be here today to submit my verbal, and also written, testimony into the record. I'm very much looking forward to the Purdue summit, and I'm very pleased that someone of your stature has taken up the mantle of focusing on the energy issue. It's such a big challenge for our Nation. I'm glad to see your leadership and Senator Biden's leadership on this issue.

I have this tendency to see everything, everything that my other distinguished colleagues have talked about, only through the energy prism, so let me just excuse myself for that myopia, but I do want to commend your perspective, Senator Lugar, because we really do need to have a shift in approach to our energy diplomacy, and it's important to recognize how things have changed. When, first, Vice President Gore, and, later, President Bush, through Don Evans, began the energy dialog with Russia, the approach was very commercial, and that was appropriate to the time. We did run our approach through the Commerce Department. The focus was on helping open investment to United States investment and making a more competitive energy industry in Russia. And that was a very good goal at the time. But as oil has become more political, as the market has tightened, and as oil producers have felt they have more leverage, the temptation to use oil, and have it become more politicized, has increased, and that means that the United States has to have a different strategy. And I would say that it probably would be not too harsh a criticism to say that, at this moment in time, we have no strategy. And, recognizing that as a first step, and thinking about what we would like that strategy to be—the

second step—is a very important debate and future that we need to take, as a country.

I'll argue, in my written testimony, and a little bit in my verbal, that we really do need to focus on institution-building. Ambassador Sestanovich mentioned all the institutions that are failing with the Russians. I would take a sort of different point of view. We have failed to try to press Russia to accept the binding issues related to energy in, say, WTO or the European Energy Charter, bringing them into the fold of the International Energy Agency. We've missed the opportunity to work together with our allies to use these institutions to demand reciprocity. In other words, Putin and Gazprom and those institutions want to be able to invest freely in Western assets, and there's nothing wrong with that. What's wrong with that is, if we don't insist for the reciprocity in return. And so, I really do think that the multinational institutional frameworks that exist today could be better utilized if we did work with our G–7 allies to really show what we think is important, in terms of free access to energy for trade and investment.

And so, just having a rhetorical reaction on every response, where we just make a declaration about what we don't like, is not as effective if it's not backed up with something which is a real program to talk about what we think the alternative is, what's in it for Russia, what's in it for us, what's in it for the global community.

So, with that as my, sort of, backdrop of where we need to go, let me just make four or five points on questions that I think people are thinking about.

The first thing we have to recognize, in being too threatening about Russian energy, is that actually today Russia is the largest exporter of energy in the world. If we think of Saudi Arabia and some of the other countries as being more important, but actually, on a volumetric basis, if you combine the oil that Russia produces—9.3 million barrels a day—and add to that its gas exports, it's actually larger than Saudi Arabia, and we need to recognize that, because Russia recognizes that.

The second thing we need to understand in worrying about the Ukraine matter is that Russia was going to have a problem supplying Europe with the gas it's promised, regardless of the politics of the Ukraine situation. There was going to be a problem anyway. And in the technical community, people, like the Baker Institute and the Carnegie Endowment, were having conferences about this issue, because it's going to be—it's a—should be—should have been a concern for Europe, and people were—sort of had blinders on, that even though Gazprom was buying up oil companies and saying they want to go into nuclear power and diversifying, that they weren't actually investing in the assets they were going to need to supply the contracts they've promised and fill the new undersea pipeline to Germany and elsewhere, because they weren't really making the kinds of reforms and investments they needed to, to keep—meet that rising demand.

The other point that I'd like to make about the Russian energy sector—and Senator Biden correctly pointed out the retrenchment to go back to a centrally controlled, centrally planned system, and there is that trendline backwards—is that we cannot ever forget

that Gazprom is a monopolist. And, in respect to my colleague, Dr. Trenin, who talked about Russia moving in a capitalist direction, in the energy sector that is not true. There's this shift back to the monopolies really reasserting themselves. When we think about how—what Gazprom's goal is in Europe, and what their ultimate strategies are in the Caspian, we need to go back to Economics 101 and reread the little chapter on monopoly behavior, because Gazprom has been, for decades, a monopoly, and that's all they know. They want to capture the supply, and then they want to control who—that only they get to sell it. And that's their strategy. And it's why, after there was a conflict with Europe, they went right to Algeria to talk to Algeria about forgiving their loans and making a friendship, because they think like a monopolist.

Now that allows me to sort of wrap in the Caspian. We have a fundamental complex situation with energy and the Caspian and the Russians. It's really fundamentally too complicated to be simplistic. On one hand, we understand Russia's monopolistic behavior. I block all the export routes for Caspian countries. That forces them to sell the natural gas to me at a very low price. And then, I make a huge amount of money selling their gas, or my own gas, on to Europe at a huge profit. Like I said, we always need to remember that Gazprom was—you know—started its life as a monopoly.

So, the question is—when we think about the Caspian, fundamentally, we're asking the Russians, "If we go in as a United States policy"—and that has been the traditional United States policy, which is to come up with extra routes, whether it's through Greece, in Bulgaria, whether it's allowing the Caspian countries to get to China on their own, as Turkmenistan is now trying, right?—that means that the fundamental question is, "Are we going to let Russia grab the premium for that gas, or is our foreign policy to let that gas come to market without letting the Russians take a cut?" Because that's—really, it's a just a business proposition. You can—we can make it complicated, about the extension of the Soviet empire and their desire to be a superpower, and that might be what the foreign policy establishment's thinking about, but that's not what Gazprom's thinking about. And when they lever themselves into the domestic scene, they're just thinking as businessmen.

So, the problem that we face, as the United States, is, we have these two desires. One is to make sure that Europe gets reliable supply, and the second one is to make sure that the Caspian countries can sell their energy in a free and unfettered way in a competitive market. The problem is, the logistics of those two goals somewhat conflict with each other, because the Russians can definitely meet their European contracts if they have the Caspian supply. Right? But if the Caspian supply goes to China, or if it's going to other customers in Russia through a different route, then the Russians, if they don't shore up their own sector and don't make their own investments in the Yamal Peninsula, they may actually come up short to supply Europe with the gas that's been promised. So, as I say, it's a very complex game of who's got the barrels and who's going to deliver the barrels. And it really does require some serious thought of strategy on the part of the United States to real-

ly think about what's our top priority and how do we want to order the priorities regarding this question of gas? And it's not just as simple as to declare that it shouldn't be used as a weapon. We need to understand the complexities of the choices that face Gazprom and face the Kremlin, and then also all the different allies whose needs we want to support.

The other thing I guess I should mention is this whole question of the China threat or not the China threat. We tend to start to think about China as a competitive factor. I do like to think about the oil market like a swimming pool. If you put water in, in one end, there's more water in the pool for the whole swimming pool. And so, having the Chinese get supply from somewhere is not necessarily a bad thing, as long as there's enough supply for the global community.

In the latest deal, where the Chinese company, Sinopec, purchased assets from BP–TNK, and even in the negotiations about whether China is going to buy natural gas from east Siberia, the thing we need to remember in thinking about Russian gas exports is that Russia is not an LNG seller. And by that I mean they're not putting the gas on a tanker, liquified, and they can't shift where the tanker goes. They have pipelines. And if the pipeline goes to Europe—and that's the only physical pipeline that exists today—their choice is to either leave the gas in the ground or sell it to Europe. And that is really on—right at this moment—that is really their fundamental choice. And when we look out past 2010, they have more choices, but the economics of taking the gas that's now going to Germany and moving that to China is not as attractive as building new infrastructure to go from east Siberia to China, which would never—that east-Siberian gas would never have gone to Europe anyway. So, the Russians are really, in my opinion, making a bit of a rhetorical statement when they say, "Well, if we don't like the way you behave, and you don't let us buy this or that in Europe, we're shifting our gas to China," because, in the end, the projects that they're talking about doing to China were fields that were never slated to deliver natural gas to Europe. So, we need to understand the bluff. We need to think about what's creating the bluff. And then, we need to not be, sort of, overreactive to it. We need to think about, again, what are our goals, and we need to—I mean, to me, what's interesting in all the rhetoric is that the rhetoric isn't focused on the Caspian, when actually the Caspian probably is the critical conflict point in this whole question of Ukraine and European gas and whether Russia is or isn't a monopoly when it comes to thinking about routes for gas.

At the end of my written testimony, I talk about some things that we've learned since the 1970s about how to deal with monopolies. Right? It is in our interest, and, I do believe, in the long-term interest of the developing middle class of Russia, to have competition in the market. Certainly, it's important to have competition in the global market. But it's also very important to have competition inside the Russian market. And that is our best defense against the kind of concerns we have about the politicization of oil and gas.

And competition can come directly from different suppliers. It can come directly by having more privatization. It can come—competition—our Strategic Petroleum Reserve, in effect, is a means of

competition, because if somebody cuts supply purposefully, we can add supply by having our strategic petroleum reserve. The United States and Europe need to think about whether it's necessary, at this point, to have natural gas stockpiles in storage. And—but, also, alternative energy is also a means of bringing competition in the market, and we also need to be thinking about getting together with our known allies, like Europe and Japan, but also our emerging trade partners, like China and India, and thinking together about these issues.

Thank you very much.

[The prepared statement of Ms. Jaffe follows:]

PREPARED STATEMENT OF AMY MYERS JAFFE, WALLACE S. WILSON FELLOW FOR ENERGY STUDIES, ASSOCIATE DIRECTOR, RICE UNIVERSITY ENERGY PROGRAM, JAMES A. BAKER III INSTITUTE FOR PUBLIC POLICY, RICE UNIVERSITY, HOUSTON, TX

Russia's status as a current and future energy producer is close to unrivaled. It holds the eighth-largest proven oil reserves in the world, but ranks a close second in oil production to Saudi Arabia (at 9.3 million barrels a day), far ahead of most other world suppliers and well ahead of the United States (at 5.1 million b/d) and Mexico (3.4 million b/d). In fact, when both oil and natural gas exports are considered, Russia exports more hydrocarbons than Saudi Arabia.

Thus, Russia's position as a major energy supplier has great significance not only for its own foreign policy development but also for its relationships with major energy consuming countries. During President Putin's first administration, in the aftermath of the September 11, 2001 terrorist attacks on the United States, Moscow responded to its geopolitical circumstances as a growing supplier of hydrocarbons by initiating high-level energy cooperation dialogs with important oil consuming countries, including the United States, China, Japan and the European Union. Breathtaking reorganization and privatization in the Russia industry, while creating growing pains and financial inequities inside Russia's economy, opened the promise to a steady expansion in Russian energy supply and a great opportunity for Moscow to tap its new position as a world energy superpower to build constructive and important links with other world powers.

By President Putin's second term, however, a retrenchment back towards fuller state control and centralization of investment and export policy has aggravated political, bureaucratic, commercial and regulatory barriers that could plague Moscow's ability to deliver secure and expanding supply. Indeed, Russian oil production has been relatively stagnant over the past year, after showing rapid gains between 1991 and 2003 (recovering from a low of 6 million b/d to 9 million b/d). There is still huge potential, with some analysts projecting that identified projects could contribute a further 2 million b/d or more to Russia's oil export rates over the next 5 years. But it remains unclear whether internal conflicts over ownership and control will adversely impact Russia's production rates, ongoing stability of supply, and future export availability. It happens that the areas with the greatest expansion potential are production areas previously controlled by Yukos—whose assets' ownership has been under a disruptive reorganization—as well as prolific areas currently controlled by Lukoil, BP–TNK, and Sugutneftegas, the latter two who are currently fending off interference and investigations by the Kremlin.

The insecure nature of competitive and tense relations between the Russian government, the Russian government-controlled oil and gas monopolies, domestic private industry, and foreign investors remains a barrier to stability of Russian energy supply—both oil and natural gas. It is an area where creative American or multilateral diplomacy (say, under the framework of G–8 cross investment protocols or the European Energy Charter) could perhaps ease pressures on some key projects. But the current trend towards the "politization" of energy, culminating in the short but unexpected cut-off of Russia gas supplies by Russian state gas monopoly Gazprom last January during a conflict between Russia and the Ukraine over pricing and politics, has left a bad taste in everyone's mouth and bodes poorly for Russia's potential status as an energy superpower whose supplier bona fides are willingly and comfortably accepted in the West. To quote Ambassador Keith Smith, "Gazprom's January 1 cutoff of natural gas to the Ukraine was a much delayed wake-up call for Western Europe and the United States regarding Moscow's willingness not only to

use its energy resources as political leverage in Europe, but also to undermine the new democracies that most recently emerged from decades of Kremlin control."[1]

As energy markets have tightened in recent years, the issue of energy security has risen to a higher order concern among major economies. At the same time, key oil producing nations have recognized their enhanced geopolitical position, increasing the leverage of these key suppliers in markets and opening the possibility for greater politization of oil as a commodity as seen in the rhetorical statements of leaders such as Venezuelan President, Hugo Chavez, and in new concerns about Russian energy politics. U.S. foreign policy has not yet adjusted to this new reality of politization. A hint emerged on the United States political scene with the debate whether China's national oil company, CNOOC, should be allowed to purchase United States oil from UNOCAL. But the United States is not fully preparing to deal diplomatically with the emerging challenges of the politization of oil and the Energy Diplomacy and Security Act (S. 2435) recognizes this deficit. There are multilateral institutions and trade and investment protocols that can be tapped to optimize U.S. energy diplomacy to address the politization of oil by large oil exporters and the United States could do a great deal more to enhance energy security by developing a more coherent, less reactive diplomatic strategy.

Attempts to politicize oil are not new. Indeed, even the United States itself is guilty of politicizing oil through its use of economic sanctions against oil exports and investment in countries of concern such as Iran, and previously, Iraq and Libya. But the impact of politically motivated linkages between geopolitical goals and oil were muted in the past because market supply alternatives were abundant enough to prevent any large supplier from gaining much leverage. Indeed, as history showed, Saudi Arabia's King tried to organize the use of the so-called oil weapon against United States support for Israel in 1967 but failed due to plentiful market conditions and lack of consensus among a group of suppliers. It wasn't until market conditions changed in 1973 that a boycott was able to be implemented in a more effective fashion. So it is today. Political actions tied to oil will have more impact because of the greater likelihood of creating a large price swing and the greater difficulty of shifting to alternative supplies.

During the Bush administration's first term, oil market conditions facilitated the possibility of a commercially oriented strategy towards Russian energy. Indeed, a high-level dialog was begun, led in the United States by our Secretary of Commerce, Donald Evans. The dialog was even labeled as "commercial" with bilateral sessions entitled the" United States-Russia Commercial Energy Summit." But as the trendline on United States-Russian relations has worsened and on oil and even natural gas to be viewed more in political terms, the U.S. commercial strategy towards energy dialogs has become less effective. A new strategy is needed that rests more with institution building in the international energy arena and taps the strategic and economic interests of key suppliers while simultaneously protecting the interests of major consumers.

It is in this broader context that the United States needs to consider its evolving relationship with Russia and the question of Russia's geopolitical motivations in setting its international energy policies.

The security concerns of our European allies with regard to the supply of natural gas from Russia has come front and center since the brief tangle with Gazprom last January. However, in the technical community, even prior to the January conflict with Ukraine, questions were being raised about whether Russia was making the kind of investments needed to meet rising European demand for natural gas.

European demand for natural gas currently totals more than 18 trillion cubic feet (tcf) per year. As natural gas production in the United Kingdom North Sea declines, Russian market share could rise from around 28 percent in 2005 to 40 percent in 2015, according to some analyst projections. The Russian state-monopoly, Gazprom, supplied European countries with 4.8 tcf of gas in 2003, and contractual obligations portend an increase to 6.6 tcf by 2010. To meet rising European demand for gas, it was projected that Russia would need to expand development of natural gas fields and associated export routes on the Yamal peninsula and Shtokmanovskoye region, but Gazprom was showing no inclination to press forward with these needed investments. Instead, the state gas monopoly was resisting needed reforms and liberalization in the Russian gas industry and embarking on a new strategy to diversify its asset base to include oil, power generation, and now even a discussion of investment in nuclear power. Gas production has been relatively flat in Russia in recent years, and many analysts were already predicting that Russian gas production could actually decline in the coming years. Some believe that without an influx of private cap-

[1] Testimony before the House Government Reform Subcommittee on Energy and Resources and the Subcommittee on National Security, Emerging Threats, and International Relations.

ital, new exploration and transportation construction activities will fall short of both domestic and export market requirements. Major projects such as field development in the Yamal peninsula take as much as 10 years to implement and discussion of such projects has not progressed in recent years. Instead, Gazprom has spent hundreds of millions of dollars acquiring new diversified assets such as Sibneft, a Russian independent oil and gas producer. The purchase raised new questions about how revenue constrained Gazprom will be able to raise financing for important gas export projects such as the $35 to $40 billion Bovanenskoye and Kharasaveiskoye fields of the Yamal Peninsula and the $20 billion Stockman LNG project.

Thus, the question of the security of Russian gas supply to Europe goes beyond President Putin's near abroad policies towards Central Europe. It also rests with the state of internal policy of reform in the Russian gas industry where independent producers would be able to supplement production by Gazprom were the industry to be properly restructured.

Problematically, Russia is biding its time by grabbing trapped gas resources in Central Asia at very reduced prices, and using those to supplement its own higher priced, lucrative gas sales to Europe. Negotiations between China and Turkmenistan, to conclude an elaborate gas export plan that would create an export grid from Turkmenistan, and including Uzbekistan and Kazakhstan to pipe natural gas to Western China and into China's existing West-East pipeline would throw a monkey wrench in Gazprom's ability to control Central Asian supply. Were the Central Asian states to find an independent outlet for their gas, it would reduce Gazprom's flexibility to meet European demand with its purchases from these Caspian producers. The geopolitics of such machinations is complicated by Russia's own gas sales dialog with Beijing that includes a planned sale of 80 billion cubic meters of Russian gas per year to China via two pipelines. The sale of BP–TNK's Udmurtneft subsidiary to China's Sinopec is the first step in this process, and senior Russian officials linked the sale, which involved the vast majority of the asset to be retransferred back to Russian state monopoly Rosneft, to a demonstration that the Kremlin was serious in its threat that it could shift its supplies to Asia, were Europe to be too belligerent to growing tensions over the Ukraine incident and Russian aspirations to buy into key gas and power companies in Europe.

In analyzing the real impact of Russia's contention that it can shift its sales East, it is important to recognize that this is not an immediate threat. Since Russia does not sell seaborne cargoes of natural gas in the form of LNG, it has little flexibility to change suddenly the flow of its gas exports which are wedded to European markets by pipe. Pipeline connections to China will take years to build, with even the Udmurtneft gas a few years away from delivery. The more ambitious gas pipeline from East Siberia fields to China and Japan remains to be negotiated and would unlikely impact European supplies because supplies from those distant fields were never slated to traverse Russia westwardly. Even if a final deal with China for East Siberia were to move forward this year, which is still questionable, it would be difficult, given the magnitude of the construction entailed, for deliveries to commence before 2009, if even that early. Thus, the United States should not focus its attention on whether Europe's gas is about to be redirected to China because the reality is that for Russia to cut off its sales to Europe, it must spend billions of dollars constructing new infrastructure. In the short term, Russia's only option would be to forego gas exports altogether. The larger risk may well be that Russia cannot meet European needs due to its inability to reform and reorganize its sector in a manner that promotes commercial investment in the supplies needed to fill the new undersea Northern Europe Gas Pipeline (NEGP). There are good reasons to question whether Russia's sector will have the managerial skills, financing, and wherewithal necessary to meet Russia's export goals, even without any interference of intimidation strategies.

There has been no coordinated push by the United States and European Union together to require that Russia reform and open its energy market to foreign investors as a response to the Kremlin's insistence that it can only meet Europe's growing energy demand if it be allowed to buy large stakes in key Western energy assets. We should be using the leverage of international institutions to press Russia to play by the same transparent, competitive rules that guide energy investment and trade in the West. The pipeline monopolies of Transneft and Gazprom are contrary to the European Energy Charter (signed by Russia) and few countries are pressing the Kremlin on the subject of full reciprocity in investment policies even as the Kremlin is yelling for attention to its acquisition aspirations.

Gazprom is a monopolist and thus we shouldn't be surprised when it behaves like one, protecting its interests. Moreover, Russian leaders are responding to the popular sentiments of its locals. A recent poll taken in Russia as part of an academic study on energy and environmental issues by the Russian Academy of Science shows

that 38 percent of Russians surveyed believe that keeping the status of superpower for Russia best meets their individual and family interests than strengthening democracy and freedom of speech (12 percent), with only economic growth mattering more. Less than 10 percent of those surveyed thought continued privatization was important while at least a third favor state regulation and support of basic industries. Over 68 percent felt foreign investment in the oil and gas sector was "not acceptable at all." The dismantlement of Yukos and its competitive market principles were highly popular in Russia as are policies that show that Russia remains a great country on par with other superpower nations. Thus, the temptation to use energy to assert itself, when other avenues are so clearly lacking, will be strong.

The extent to which Russia or any small group of gas exporters will be able to exercise monopoly power or utilize a gas weapon effectively will be determined, among other factors, by technological improvements that will affect the cost and attractiveness of other competing fuels such as coal, nuclear, or renewable energy. Moreover, privatization of gas reserves and gas transport networks present an impediment to the formation of a successful gas cartel and blocks the monopoly power of a state actor such as Gazprom. It will be easier for national, state-owned producers like Gazprom to participate in a cartel than for privately held firms that might have different objectives from the state. Indeed, already, Gazprom responded to pressures on it from Europe by soliciting coordinated strategies with another major European supplier, Algeria, which has long argued for a Gas OPEC.

If a number of private Russia gas producers emerge, it will be more difficult to reconcile their conflicting corporate ambitions, as the Putin administration has so keenly experienced in recent years. Thus, the retrenchment away from privatization and market competition in Russia's energy sector runs against U.S. and global interests and should remain a target for the United States-Russia dialog and the European Union-Russia dialog.

Options available to consumer countries are well known. Deregulating their own energy sectors, to permit utilities more freedom in setting prices, in choice of technology and in contracting with fuel suppliers will have the effect of increasing the elasticity of their demand for gas and limiting the market power of gas sellers. Consuming countries can also actively promote the technologies that will increase competition between gas and alternative energy sources. Also, as the European Union is discussing, strategic inventories of natural gas will help limit the impact of any supply cutoff, reducing the incentive for an ambitious supplier to try to assert its market leverage.

The CHAIRMAN. Well, thank you very much, Ms. Jaffe.

We'll have a 10-minute round of questions.

Let me just begin the questioning by noting, Dr. Trenin, that your colleague, Andrew Kuchins, was with Members of Congress this morning at the Aspen Institute breakfast. It was a wonderful warm-up for our hearing today, because he is just back from an extraordinary trip from the caucasus with the Chinese delegation, observing all the problems that are there. He brought a chart. You will not be able to see it from here, but this is the chart he has. Now, essentially, this is oil in Russia. There is a huge peak, about 1981, and then it comes down rather abruptly, by 1986–1987. Things are getting pretty thin. Certainly, by the time the Soviet Union came to an end, in 1991, we're at a nadir point. But now, the spike goes up. He would not predict that it will continue to spike in quite that way, although who knows precisely what the price of oil will be in the world. He makes the point that you've made today—that the largest exporter is the largest factor in the oil trade, by far. He cites a figure that I hadn't heard before, an estimate that in the last 7 years the gross national product of Russia may have climbed from somewhere around $200 billion a year to $900 billion a year. That is a four-and-a-half-fold increase in the income of the country in 7½ years. That illustrates what a startling development we are looking at, in terms of the amount of income that is available, but it'll also track some charts that Tom Friedman has been showing. There was a great difference between

all of the ferment that was going on in Russia or in other places, for that matter, and when suddenly that oil prosperity changes as people accept stability that comes from being able to pay your debts, to say to the rest of the world, "We're rich, and we're back," and so forth. Thus, the popularity of Vladimir Putin. If we wanted to look at this in a democratic way and have a referendum on Vladimir Putin, the odds are that he would win, with a fairly good plurality, I suspect. And even Mr. Kutchins suggests that the transition in 2008 may be a reasonably smooth one, given what now is called "controlled democracy"—that is, that you pretty well extinguish the hopes of anybody else that is not really on track. The problem for Russia, he would suggest, is after 2008, because, as some of you suggested, of the strategies that the United States plus Europe and the G–7 partners, and other people, may use. They may get brighter about this whole business, as opposed to being all over the place, maybe characterizing current policies, not only in our own country, but elsewhere.

This does explain a part of why things have changed in Russia, and maybe our relationship to this. I don't attribute this to Mr. Kutchins, but others have suggested that Russians see our bantering about democracy as a thought, first of all, that we simply don't have sufficient respect for whatever they are doing, and, second, that it represents a different period, really a sort of a failed period, when there was no oil, there were no prospects; there was indebtedness, supplicants. As Russians come over now, that's one of the first things they say to Joe and to me, "We're not supplicants. We're rich. We're back. We would love to visit with you, cooperate a bit in international relations. We don't want to kick the can down the road into isolationism, but you have to understand, this is different." This is not the case of whether our Nunn-Lugar program goes over and they need contractors. We just signed another umbrella liability agreement, but they indicated that they would be calling more of the shots from now on.

Vice President Cheney's testimony over in the Baltics criticizing Russia was one thing, but then, combined with extolling the virtues of Kazakhstan the next day, and our entertainment of the Azeri President, they made the point, at least in the Kremlin, that, once again, we are harping about democracy and the lack of self-respect and so forth. On the other hand, we're fully prepared to deal with people who are not very democratic. You have all pointed out the dilemma posed by governments in the Caspian region. They have strategically important pipelines running through their territory. And their commitment to democratic values is not yet assured. Nevertheless, the United States must develop strong relations with each of them.

This probably is a good time for the G–8 to meet. We're going to be in Russia. It's going to be Russia-centralized and focused. Many people abhor that thought, but the fact is that the energy agenda was supposed to be uppermost. For Europeans, this is extremely important, because they feel, still, very uneasy after their visit from President Putin. And, as you point out, Ms. Jaffe, it may be an empty threat to send the gas out to the East. But, at the same time, we note the fact that it was even a suggestion that there are alternatives, as opposed to making good the promises to Europe,

the stability that comes to Europe, having that great dependence, the anxiety that comes with President Putin going to Algeria, visiting with President Bouteflika about what the two of them can do, vis-a-vis Europe or each other. This is an opportunity for a much more secure situation, giving more self-respect to the Russians, more certainty to Europeans, and, once again, the United States entering with the Europeans and the Russians into this dialog. We have something constructive to come out with.

Can you suggest some signal points for our U.S. agenda, with that in mind? Please talk about energy, self-respect, the enhancement of the United States-European relationship. Do any of you want to have a try at that?

Yes, Ms. Jaffe.

Ms. JAFFE. I'll take a short stab at that.

There was a time in history when Algeria, with their pipelines to Europe, and also their LNG shipments to the United States East Coast, took this step that Putin is trying to take. In other words, they saw they had a captive market—it's very hard to switch off of gas once you decide to go to gas—so, the Algerians just said, "Hey, we've got you captive, we're raising the price."

And the result of that effort—which maybe people can read up, we just have a book coming out from the Baker Institute that's a case study on it—was that Algeria lost their markets, both on the East Coast—they lost their markets to Trinidad—and in southern Europe, they lost their markets to other suppliers, partly as a result of suddenly being seen as an unreliable supplier.

So, I think that we need to go into this conversation with the Russians, especially taking into account the things that Ambassador Sestanovich and Dr. Trenin have said, where we have to treat them as an equal partner, because this whole question of self-respect and being a superpower is not only just coming from the administration in Russia, it's coming from the public in Russia.

But, also, we have to know what our options are. In other words, if you come in and you say, "Well, you can't act this way," even if we're willing to offer the carrot, like, "Well, let's talk more about reciprocal investments," you have to know what you would do if they're going to continue to take a belligerent stance. We need to actually, unfortunately—because I know the meeting is coming up—we need to know what Europe is proposing, or we are proposing with Europe, to do as the alternative. So, maybe we needed to have flown over to Algeria, as well. Maybe we need to have a plan with European and the United States collaboration on building natural gas stockpiles. Maybe we need to have a plan of what fuels we would use in the future, besides natural gas, if we can't—and an initiative, if we say we're going to have to wean off of Russian gas—that, really, we need to show, not so much, I think, even the administration in Russia, but Gazprom—right?—that there is a plan that might involve our own companies' investments in other countries or an initiative so that we know what we would do to wean ourselves off, because we're in just the same situation as they are. It takes several years to change suppliers when you're coming from a pipeline route. It takes them several years to shift material to Asia. Right? And, really, it's in their best interest to try to at least get some entry into—some better entry into Europe, if that's

what they want, in exchange for what it is that we want, which is to see them actually doing more reform and more investment and having a more competitive marketplace in Russia. And I think the dialog has to come, but, again, we have to get our own ducks in order and know what our alternative would be so that we're coming in from a stronger position.

The CHAIRMAN. Dr. Trenin.

Dr. TRENIN. Let me say—thank you—let me say, Mr. Chairman, that I believe it's a fallacy to regard energy as a weapon. There is no one-side dependencies in energy business. Russia is as dependent on Europe as Europe is dependent on Russia. And that's the way it's going to be.

I think one of the problems of the United States-Russian relationship is that that relationship lacks a solid economic foundation. There's a lot that's going on economically between Russia and the European Union, but not nearly enough between Russia and the United States. So, if some of the projects that are currently being talked about—like Stockman gas field in the Arctic—if those projects become developed and lead to interdependency between the United States and Russia, that would lead to a much healthier political relationship between the two countries and a much stabler—much more stable strategic relationship between Russia and the United States.

Let me also add that the Russian leadership is—as you mentioned, Mr. Chairman—is extremely confident today. And this confidence needs to be taken into account. As you, yourself, said, sir, they will be looking for a coequal relationship, and this is something which is becoming a sine qua non for the Russian leadership.

Let me also say, in all frankness, that in the view of the Russian leadership, the discussion of Russian democracy is—I don't think that they are right, but the way they seem to believe what it is—they think it's a reaction of the United States to Russia emerging as a more independent and more important power internationally. And it's up to the United States policy to disabuse the Russian leadership of that notion.

Let me also add that I do not suggest that there is an automatic Marxist link between increase in the GDP and the formation of the middle class. And clearly this is a long, drawn-out process in Russia.

I do not believe that the oil wealth has much to do, at the lower level, at the—in the middle level—with what I call capitalist development in Russia. Rather, it's property becoming the issue that people are talking about, worrying about, are concerned about. Property is becoming real. The property that people own, not the property that the government owns—the money that's been stashed away in all those stabilization funds and the gold reserves and currency reserves, what have you. But the money that people own. And that's revolutionizing Russia from below.

I think that's what I wanted to say.

The CHAIRMAN. Thank you.

Steve.

Ambassador SESTANOVICH. There's no doubt that the essential precondition of having an effective energy dialog with Russia is an effective energy policy of our own. And, as Amy properly points out,

if we don't have our ducks in a row, we shouldn't expect the Russians to put them in a row for us.

Second point. This is an issue where the rubber really does meet the road when one talks about cooperation with Europeans. Over the past several months, the Europeans have continued to express their shock about what happened in January between Russia and Ukraine. And they have pushed for Russia's ratification of the European Energy Charter. If we believe in strong American-European cooperation on energy issues, I think we have to ask what kind of support we have given to this proposal by the Europeans. How should we respond to the Russian dismissal of the idea last week? Are we going to keep pushing this, or not? Because it has real implications for how the Russian energy sector operates.

Let me mention a couple of those implications. It is a pipe dream to think that we're never going to—that we can end our energy relations with Russia. We wouldn't want to. These relations are mutually beneficial. Yet it is an important objective of the United States, and of all energy consumers, that energy producers act like commercial entities rather than like arms of the state.

If you look at the board of directors of the monopolies that Amy has talked about, you'll discover that they're Mr. Putin's assistants. This is not just a matter of corporate governance. These monopolies are managed by, directed by Mr. Putin's staff. And that's an arrangement that is unlike what you have in any other G–8 country.

If the European Energy Charter were to be ratified, it would have implications for the monopoly not only that Gazprom exercises, but for other monopolies in the Russian energy sector—pipelines, in particular.

We should, as part of a reinvigorated energy dialog with Russia, address the question of the access to our capital markets of these Russian energy companies. Are we satisfied with the kind of transparency that we see when those companies bring large share offerings to market?

I might add a final point about energy efficiency. To my mind, the single most staggering sentence in the Council on Foreign Relations task force report, which I have invoked many times, is the following, "If Russia used natural gas as efficiently as Canada, it would save three times the total amount of gas it exports to the European Union." Russia is not just the world's greatest energy producer, it's the world's greatest energy waster.

Thank you.

The CHAIRMAN. Well, thank you very much.

Senator Biden.

Senator BIDEN. I thank you all.

You know, when you listen to three qualified and experienced people like yourself, there's certain things that just come through that are self-evident, that we don't talk about, really, up here very much, and policymakers don't talk about much downtown, and that is that there is no energy producer that's not a monopoly, other than us, and a few others. But, I mean, look, let's face it, you know, you don't have anything remotely approaching democracy in Saudi Arabia or in the gulf region or in Venezuela—that's technically a democracy, but it's become a—I think it's become difficult—Nigeria—I mean, you look around, and we talk about the—you know,

the G–8, and we should talk to them. Well, none of the G–8, except one, has, really, energy that they can export. And so, that this really does come down to energy. It's more than energy, but it's energy. You know, "It's energy, stupid, it's energy." And it has—it has many, many complicating ramifications. It's not a straight line. But we would be in a very different circumstance if Russia were China, in terms of energy resources. It would be a completely different world, just as it would be a completely different world if China was a net exporter of energy. And so, I mean, I—it's so simple, but it's so profound.

The second thing is that the whole notion that we are going to deal with not just Russia, but—and Russia, obviously, is the biggest not only producer, but the most consequential nation that possesses that kind of energy, without a clear understanding of what their options really are.

I went through—we went through the whole cold war assuming options Russia had that they never had, but we assumed they had them. We assumed they had capacities they never possessed. And we didn't look—we always looked at it in the—at least in my—I realize all generalizations are false, including this one, as Clemens—Samuel Clemens once said—but we basically looked at them like they were 12 feet tall all the time, and we were probably 6 feet 1 inch, when, in fact, they were really, like 4½ feet tall.

And so, the thing that I'm most impressed with so far today—and I need to know a lot more about, and the question-and-answer period doesn't lend itself to doing it—is with—Ms. Jaffe, I would love to have the most realpolitik look at what are the real options Russia has, what threats are ones that they are able to, relative to the energy sector, actually deliver on, and what timeframe can they deliver them on, so that we don't look at this in a way that—because we have agendas here in the United States. Everybody—the—politically, there are agendas here. And, you know, depending on how you perceive the amount of leverage Russia has today—impacts significantly on what you think your options are and what responses the United States can institute.

One of the things I find—and I don't have as much interaction with Russian officials as my friend—matter of fact, I don't know anybody that has more interaction than the chairman—is that when we start talking about democracy and energy, all they do is point to the gulf, and they say, "OK, great, wonderful. You guys are telling us about being a democracy. I mean, when is the last time you had a conversation with the Saudis about that?" It may have nothing to do with anything, but it's an interesting talking point.

And I guess what I'm getting—the third point here is, it seems it all comes down to one minimum—what you said, Mr. Ambassador—one minimum requirement to be able to arrive at a rational policy from our perspective, and that is, we have to have an energy policy. We don't have an energy policy. We do not have an energy policy. The swimming pool metaphor is a good one. We go ahead and pump all the oil in the—up in the Arctic area, all the oil in the gulf, all the oil in the Atlantic and Pacific. We fill the pool about 2 inches. It's—it affects it, but it doesn't affect price very much. You don't have them saying, "Look, we've got all this oil, we're keeping it home." It's—goes into the pool. It doesn't get as

much flexibility, it doesn't give the world much flexibility when you have a disparity of only two percent between supply and demand out there right now. Not a lot of cushion. So, it's sure in the hell not an answer. It may be useful to do. Forget the polemic arguments about—and the discussions about the environment and all that. Let's assume there was no environmental impact all, everybody said, "Let's do it." Does anybody think you're going to turn to the American people or the Europeans and say, "By the way, now your problem with Russia is really diminished a great deal here," or that we're really going to see gas prices or oil prices drop at all, of any consequence here, or give us more flexibility?

And so, I guess what I'm saying is that the three things I come away with are, we don't know—I've not, at least—I don't know—how real the Russian threats of the use of their energy are relative to their ability to deliver on them, number one. Number two, how almost—how frightening myopic we are. I thought you said something very interesting, Ms. Jaffe. I was impressed with your testimony. You said, "Maybe we should get in a plane and fly to Algeria." We don't do—I mean, you know, what the heck are we doing? What is the extent of our oil diplomacy? What is the extent to which we've actually had—I mean, I've not had anybody come up and say to me that, you know, at the State Department or at the White House they've set up a high-level group that is meeting on a regular basis with all our European allies to determine whether or not there is a possibility of us arriving at some sort of emerging consensus on how we deal with energy. It comes up in the G–8, it comes up in certain summits. But the idea there is not an absolute dialog that is totally continuous, that is—that's a poor way of saying it—that is ongoing, as fundamental as the dialog that took place in 1953, in terms of our physical security and NATO—I mean, it seems to me it's that basic, I mean, you know, for everybody. When are we going to wake up?

So, I guess what I'm—you know, it's obviously not a question, but it is a clarification for me of my thinking—and all of you have suggested that—that no matter what's—how you—how you decide to proceed, one, it's pretty darn important to know what Russia's options really are, and—as hard baked an analysis, we could—as if we are making a judgment, as we were so used to doing for the last 30 years of sitting in the Situation Room, making a judgment of, "What are the real options Russia has with all their nuclear weapons in a war?" We sat down and thought through that in incredible detail. We may have been right, we may have been wrong. But it seems to me we have to be as hard baked about it as it relates to energy, not to use it as a—just to know what our options are.

And, second, it seems to me that if we don't start talking with our allies about our mutual dependence—I mean, I think of it, Mr. Chairman, in terms of, what are our grandkids, when they write their senior thesis at Oxford, as Rhodes Scholars like you were, and hopefully not like I was—what are they going to be writing when they look back and say, "Didn't these guys figure this out? Wasn't it self-evident, in the year 2006, that there were no good guys in the oil business?" I don't mean—I'm not talking about American companies. "There's no good guys in the oil business?" [Laughter.]

I'm not trying to be—I really—I mean it—I mean, you have Saudi Arabia and Venezuela and Nicaragua and Russia and maybe Canada, maybe Mexico, who knows? But I mean, "There weren't a whole lot of good guys, and they sat there while the bad guys, or bad"—wrong word—"by the guys who didn't know how to shoot straight, screwed the world up. And they figured they had to respond by going, 'mea culpa, mea culpa, mea maxima culpa.'" "Please send the pipeline to me, I will give you what you want."

I mean, it's kind of bizarre, when you think about it. Difficult. Difficult, difficult. But it's like, you know—I'll end, Mr. Chairman—you've heard me quote it before, allegedly, although I just read a new book, where I found out that half the quotes Kennedy gave as his weren't his, and who knows whose what quotes, I mean—but this is attributed to G.K. Chesterton, and it may not be accurate, but I've always heard it saying—Chesterton said, "It's not that Christianity has been tried and found wanting; it's been found difficult and left untried." I kind of think that's where we are on this whole relationship with Russia and our allies and our mutual dependents and our needs. We don't seem, in this—our unilateral thinking—we don't seem to quite understand that we can't do this alone. We can't figure this out alone, unless we decide to—just to become totally energy independent, if that were able to be done, if you could wave a wand. But what does that do for us, in terms of our alliances and our—I mean, it doesn't do a whole lot. I mean, it's—I'd like to have it. You give me the choice, I'd take it.

So—and the one question, for the record, I won't even ask you to do it now, because I'm supposed to—I have to leave for 20 minutes before I come back for our meeting—is, Doctor, other than oil, you—you made a very, very important point. You said that we have—we should base our relationship more on a solid international footing relation to—in relation to economic dependent—and mutual dependency. Is there anything other than oil or gas? I can't figure any out. And if there is, if that's the only one, we've got to do a lot of antecedent things to figure out how to get to there first. Because if they—if there's a pipeline coming across the Bering Straits, that's a great thing, except if they get angry and decide—and tell us—and watch everybody, like Nervous Nellies here, saying, "No, no, we're going to divert that pipeline. We're going to go down through northern China." They can't, but we'd sure the hell go, "Oh, my God. I guess they're going to do that, just like all that Siberian gas is going to go to China now, when it would have gone to Europe," when it couldn't have gone to Europe.

End of my comments. Anybody who wants to respond, I invite it, but it's not necessary.

Yes.

Dr. TRENIN. Senator Biden, I was talking more about Stockman, not about Bering. I was talking more about the project for liquified natural gas reaching the U.S. market.

Senator BIDEN. Still energy, right?

Dr. TRENIN. It's still energy, that's right. But you talk as if energy were, today, a basis for the relationship. It's not. In fact, energy and—oil and gas are absent from the United States-Russian economic relationship.

Senator BIDEN. No, I—please don't misunderstand me. Energy is the basis for Putin's ability to act in the way he's acting, which is contrary to the interests of the United States, Western world, the whole world, and his world, in my humble opinion. That's the basis for it. Were he not, were he energy deficient, were he China—we just switch the resources. God wakes—we wake up the next morning, and all the oil and energy that's in Russia is now in China, and all the energy, the lack of it, in China, is in Russia. It's a different world, Jack. It is a fundamentally different world. And old Vladimir's got a problem.

Ms. JAFFE. Let me just respond, Senator Biden, to something that I've said in our dialog, our informal dialog, between the Baker Institute and Chinese think tanks. Fundamentally, you've hit the nail on the head. We have the same strategic interests as China. China is a net importer, they have to worry about the stability of the flow of energy from the Middle East, the same as we. Russia is a net energy exporter, their economy, as Senator Lugar has so correctly pointed out, is tied to the health of the energy market, from a producer-seller point of view. So, I'm not saying we shouldn't have good relations with Russia; they're the most important supplier. But we need to understand and recognize, especially in thinking about our foreign policy, that we have this strategic alignment actually with China, not Russia, when it comes to this issue, because the Russians are on the other side of the issue, and the Chinese are on the same side of the issue as we are, as a major consumer that has to worry about the future of growth of its economy, based on energy supply.

And so, when we think about our diplomacy, we have to have not only diplomacy to deal with our producer-ally-friends relationships, superpowers, whatever, we also have to consider who's in the buyer club. It's not just the European Union and Japan or South Korea. We have to think about India and China and Brazil and those who are in the buyer club, as well.

So—but you're right, you know, quirk of fate, what's under the ground matters. And you cannot get away from the strategic nature of the fact that we are a net buyer, and some countries are net sellers.

Ambassador SESTANOVICH. If I could add two cents, Senator.

One, I think it's important to bear in mind that energy wealth doesn't always keep corrupt regimes in power. And if there's any doubt about that, I suggest President Putin talk to the Shah of Iran.

Senator BIDEN. By the way, it doesn't keep him in power, but what it brings about may not be more beneficial.

Ambassador SESTANOVICH. Excellent point.

You also asked what Russia can do with its energy in the way of coercion, what its options are. It's useful here to compare the use of energy to the way in which nuclear weapons add to a country's power. What was shocking about what Russia did in its confrontation with Ukraine in January was that it was the equivalent of actually using nuclear weapons, as opposed to merely having them in your back pocket as a reminder of how important you were. That got the Europeans' attention. Nobody had used energy as a weapon in that way in a very, very long time.

There's a related question here which is not how big a problem Russian energy is, but how much can Russia contribute to the solution of global energy problems? And, here, I think it's important to pay attention to the limit on its energy production imposed by Russia's political and economic system. For years Russian gas production growth has lagged the international averages. Why? Because Gazprom is a monopoly. It's as simple as that.

Senator BIDEN. Well, I—my observation is that nations usually don't spontaneously recognize those deficiencies, especially coming from those in power who control the monopolies. That has not been historically the case.

I want to make it clear. I do not believe our relationship with Russia should be, or is primarily, based upon energy. The fact of the matter is, Russia forming a more democratic nation is critically important to our security interest and to the development of western Europe and the entire region than almost anything else I can think of. All I'm suggesting is, ironically, the oil has become the impediment, in the short term. It has all—it's the—if you had an enlightened leader in Russia, you could see how the use of energy could be an incredible tool for democratization. It could be a phenomenal—a phenomenal tool. In the hands of an autocrat, who comes out of a system that is—well, anyway, without going—it is a very different tool. It is a very different tool. In the hands of a President of the United States, in the hands of the Prime Minister of Great Britain, in the hands of the President of France, it may be a very different thing. It may not, but I suspect it would be. But I don't want anybody to misread here. I—the point I made was, energy independence on our part would not—would not solve larger problems relating to Iran going nuclear and Russia's implication in, or cooperation or opposition to it. It would not solve the situation, in terms of European unity and how it views its relative strengths or weaknesses. It would not affect a whole range of things that are vitally important to us in the 21st century. It just happens to be the 800-pound gorilla sitting in the middle of the discussion right now, and our failure to understand its impact—not your failure—our failure, as a government, to understand its impact—or, if not understand it, act upon—act upon rational alternatives, seems to me to be not in our interest, not in Europe's interest, and, I would argue, not in Russia's interest. This is not about, in my view—I don't want anybody to misread—this is not about how you keep Russia in a box, how you keep Russia—we are better off if Russia is a thriving economy that has democratic rules. We are better off if it becomes a major economic power in a democratic mold. This isn't about, in my view, keeping Russia in a box. It's about allowing Russia to flourish. If it flourished, we're better off. We're better off. Competitor? Yeah. We're better off.

And so, I just don't want anybody—not the three of you, but anybody listening—thinking that I think we've got to figure out how to, you know, keep Russia from reemerging as a major power. I'd like it to reemerge as a major power, as a major democratic power. That's a good thing, not a bad thing, in my view. I don't think it's a zero-sum game.

The CHAIRMAN. Yes, Dr. Trenin.

Dr. TRENIN. If I may, I think you're absolutely right, Senator Biden. And this is really the fundamental thing that we should be concerned with.

And, of course, we also realize that there is no shortcut to democracy. An enlightened leader—if one transplants an enlightened leader to the position that Mr. Putin occupies today—would probably have to deal with the same elites around him, with the same people who vote for Mr. Putin, and who are constantly supporting Mr. Putin at a pretty high rate. In other words, the problems of Russia are not only confined to the Kremlin.

Senator BIDEN. I agree.

Dr. TRENIN. They are everywhere. And I think that it's the development of a new society. If you like, call it capitalism—it's not market capitalism, but capitalism, still—that is transforming the country and eventually taking it closer to democracy. But we should disabuse ourselves of the notions, which were very popular back in the early 1990s, that somehow Russia could make a great leap forward and become a democracy. It is—it was possible, and it is possible, in some central and eastern European countries, because their modernization was linked to integration into NATO, the European Union, and other Euro—Atlantic European structures. For a variety of reasons, this is not the way that Russia is likely to go.

So, I think that even as we wish Russia to become a democracy, we need to be aware of the current realities of Russia and that this is going to be a long and arduous path.

And there's an—yet there's another thing which I think I would need to highlight. Democracy is—which—when they are in the process of becoming such, the process of democratization, could be accompanied by some pretty ugly things or some difficult things, like nationalism. I referred to nationalism. A more democratic Russia will not necessarily be—I mean, if you just turn the power to the people today, it may not necessarily be a nicer, friendlier whatever. So, I think that it's a complex reality. And as—even as we wish Russia well, wish Russia becoming a democracy as soon as she can make it, we need to realize that this path is going to be a very, very difficult and long one.

Senator BIDEN. I couldn't agree with you more. I don't disagree with a thing you said.

Ambassador SESTANOVICH. Can I just cast a vote for the great-man theory of history instead of the sociological analysis that you've heard from Mr. Trenin? I completely agree that the long-term development of Russia is going to depend on broad social trends of the kind that he's describing, but we shouldn't forget how important specific decisions are that are made by Mr. Putin and his associates in the Kremlin for the answer to this question: Will Russia, in the next couple of years, take steps forward toward——

Senator BIDEN. Transition?

Ambassador SESTANOVICH [continuing]. Modernizing itself in the way that Mr. Trenin has described, or will it take steps backward? The question of whether or not opposition parties are able to participate freely in elections is completely up to people in the Kremlin. The question of whether or not opposition parties are able to get financial contributions for their campaigns from Russians who support them is completely up to people in the Kremlin. The ques-

tion of whether opposition parties are taken off the ballot days before an election is completely up to people in the Kremlin. The question of whether they're even allowed to register is completely up to people in the Kremlin. This is not a matter of broad sociological trends; it's a question of who signs the memo authorizing this or that restrictive policy to be implemented.

So, I think we shouldn't take too long a view, when we can see how specific decisions are made in the Kremlin that block Russia's development.

Senator BIDEN. It would be nice if they had a Madison and a Washington and a Jefferson, but I would agree with the professor that it would still take a helluva lot longer than it took here. I think you're both right, these—this makes—you know, individual leadership matters, that the great-man theory does have—in this country, the great-man and great-woman theory has some relevance, but you have to admit, it would be more difficult. It is necessary, and it's a shame, and it makes me realize—and it sounds somewhat chauvinistic about our country—but, damn, we were lucky in 1776. We were awful lucky to have some pretty damn smart people committed to a completely new notion of governance. And—but even if you had 'em all sitting in Moscow, I think it's going to be a little bit harder.

The CHAIRMAN. Thank you, Senator Biden.

Let me just make a summary comment, and then we'll bring this hearing to a conclusion, although you may have some final comment after my thoughts.

It seems to me constructively this morning that we've had some agreement between the Senators and the panel that our country needs a more well-defined energy policy. I suppose if those who are responsible for our energy policy were here, they would say, "Well, we do have various elements of this," perhaps. But, nevertheless, there appears to be some consensus that it needs to be more sharply defined and understandable to the American people, as well as to Russians, Europeans, Chinese, or whoever; and, as a subset of that, the suggestion that we need a natural-gas plan.

Ms. Jaffe has provided some excellent charts which show all the routes of natural gas to Europe and to Asia, as well as prospective routes, with a red line heading out to China, for example—and this is very helpful, in a geographical sense. We discussed the various countries. Unless each one of us has a photographic memory of the map of Europe or Asia, it may be difficult to transpose where all these lines are and who is intersecting whom, or evading whom. We talk about the Caspian problem, and so forth. So, I commend, to Senators, staff, and, likewise, those observing this hearing, these remarkable charts, just as a basis for getting some grasp of the options that are available to countries that are involved in this.

Now, let me just mention, also, that the thought has been expressed that the United States has an affinity with China with regard to the Russian energy situation. I would indicate that that, likewise, is the case with India for, obviously, some of the same reasons: The dynamic growth of these populations, and huge new demands for energy, now and for the foreseeable future.

Likewise, in our country, we express the thought we need to have energy conservation. Most experts who have written about this

subject have made the point that some of you have made about Russian use of energy—in the case of natural gas, that's the misuse, waste. It goes well beyond the amount that's being exported to Europe or elsewhere, where there seem to be contractual difficulties.

I mention, once again, our legislation in Senate bill 2435. It's not the be-all and end-all, but it expresses the thought that energy policy has to be a cardinal point of our American diplomacy. We need to have, in our State Department, or elsewhere, if the President so desires, people who are actively involved in diplomacy on all of these subjects. In other words, people that might be working with the Europeans with regard to the European charter. As some of you have said, this is really a cardinal point, even as we approach the G–8. Even without the G–8, it is very important. I'm not certain I see that kind of diplomacy going on, nor diplomacy with China, with India, with other energy users, on either substitutes, or more efficient use of energy.

Some Americans would say, "Why should we work with other countries to help them become more efficient in using BTUs?" Well, for the very reasons we're talking about today. On the supply side, the misuse of BTUs, or antiquated machinery or procedures, is extremely costly to them, and they have to become more aggressive in trying to overcome those deficiencies.

In the Corinthia Hotel, in Tripoli, in Libya, where I was in August, I saw many, many people from India and China—in fact, the hotel appeared to be filled with persons from those countries—and as I was visiting with them, and asking them their mission. It was identical—namely, to identify acreage in Libya for areas of dominance, preemptive work. There were a few Americans in the hotel, but they were outnumbered in the process, although they had the same mission. In other words, there was an alliance of sorts. Now, we might have seen it as competitive, and the world may say, "Well, this simply indicates that we're all headed toward collision," but not necessarily so if we identify the mutual interests that we have in this.

This calls for an extraordinary amount of new diplomacy in our Government now, or in any one that may follow this administration. So, our committee's hope is, by having these hearings, inviting experts such as yourselves, taking advantage of a situation like the G–8 meeting, which is a focal point on Russia, on energy, to try to make some points in our own dialog in this country.

Let me just mention one small success story. I was not the only Senator who received letters, but I'll make them a part of the record. These came from the chief executives of Ford and Chrysler.

[The information previously referred to follows:]

FORD WORLD HEADQUARTERS,
Dearborn, MI, December 14, 2006.

Hon. RICHARD G. LUGAR,
U.S. Senate, Hart Senate Office Building,
Washington, DC.

DEAR SENATOR LUGAR: Thank you for your letter of encouragement for our efforts to help transition away from foreign oil dependence. Innovative gasoline-saving technologies are leading the way forward in our product development plans. As you know, we have committed to produce 50 percent of the vehicles we make each year as flexible fuel vehicles capable of running on a renewable fuel by 2012, provided

the fuel is available to consumers and sufficient incentives are in place to encourage the production of these vehicles.

Our commitment to put more flexible fuel vehicles on the road, by itself, will not reduce the nation's dependence on foreign oil. Fuel providers, retailers, and consumers are key elements of any transportation policy equation and must be part of the solution. We need a strong, long-term focus on policies that increase ethanol production, accelerate E85 infrastructure development, and ensure competitive E85 pricing to consumers. Competitively priced renewable fuels and a nationwide refueling network are essential market drivers required to encourage active consumer participation in the federal fight for energy independence. An aggressive energy security strategy of federal tax incentives and loan guarantees for ethanol producers, distributors, and retailers would increase the supply of renewable fuels, accelerate the installation of refueling systems, expand the availability of renewable fuels, and reduce transportation fuel costs for consumers.

Unfortunately, roadblocks to E85 infrastructure continue to arise. Recently, Underwriters' Laboratories (UL) have informed us they do not have a certification protocol for E85 pumps—this has halted development of several new stations and has raised questions about existing stations. Prompt resolution of this issue is necessary to continue the positive momentum.

Ford shares many of the goals in your proposed National Fuels Initiative. We both recognize the need for dramatically increasing the production, distribution, and use of cellulosic renewable fuels. In fact, Ford's Vice President of Environmental and Safety Engineering, Sue Cischke, highlighted a few of our efforts and shared perspectives on a variety of renewable fuel issues as she participated in your August 2006, Energy Security Summit at Purdue University.

Energy security concerns are driving significant investments in all areas of advanced technology vehicles including energy-efficient hybrid electric, clean diesel, and advanced internal combustion technologies. We plan an expanded application of hybrid electric technologies into the Ford Fusion and Mercury Milan in the next few years. We continue to research plug-in hybrids and the associated battery challenges. Our hybrid electric and flexible fuel vehicles represent the best of American ingenuity and engineering excellence.

Ford Motor Company is committed to employing gasoline-saving vehicle technologies, enabling consumers to reduce the nation's dependence on foreign oil. I look forward to continuing our correspondence on these and other important public policy challenges facing our great Nation and the 110th Congress. Thank you for all your leadership in the Senate.

Sincerely,

ALAN MULALLY,
President and CEO.

DAIMLERCHRYSLER CORPORATION,
Auburn Hills, MI, May 12, 2006.

Hon. TOM HARKIN,
Hon. DICK LUGAR,
U.S. Senate,
Washington, DC.

DEAR SENATORS HARKIN AND LUGAR: This is in response to your letter of April 24, 2006, to Dr. Dieter Zetsche, requesting that DaimlerChrysler increase its production of flexible fuel vehicles (FFVs) as quickly as possible to reduce our consumption of petroleum. DaimlerChrysler shares your views that we need to shift the Nation away from petroleum consumption and that renewable fuels can, and must, play an important part in that shift.

Earlier this year, I announced in a speech at the Detroit Economic Club that DaimlerChrysler would add to the 1.5 million FFVs that it had previously produced by manufacturing, by the 2008 model year, just under 500,000 FFVs annually. These 1.5 million vehicles represent about 10 percent of our total production since 1998, and the 500,000 figure is nearly 25 percent of our expected annual production. Both percentages are the highest for any manufacturer, a fact of which our company is very proud.

On April 25th, I had the honor of following President Bush to the podium of the Renewable Fuels Association conference, held in Washington. I announced that for the first time ever, beginning in model year 2007, our Jeep brand will offer flex-fuel vehicles, for both retail and fleet sales. Customers who order our popular Jeep Grand Cherokee or the new Jeep Commander with the 4.7 liter engine option will receive vehicles capable of running on E85 fuel. In addition, the Chrysler Sebring,

Chrysler and Dodge minivans, Dodge Dakota and Dodge Ram pickups, and the Dodge Durango SUV will also offer FFV capability. In total, we anticipate sales of more than 250,000 FFVs in model year 2007, which will then nearly double by the following model year. DaimlerChrysler is fully committed to increasing levels of FFV production.

Our commitment to renewable fuels, though, extends beyond ethanol use. DaimlerChrysler is the only manufacturer to offer a diesel vehicle that leaves the factory fueled with bio-diesel. The Jeep Liberty diesel, manufactured in Toledo, Ohio, is fueled with B5 as it leaves the assembly line. We have also announced that beginning this Fall, we will endorse the use of B20 diesel fuel, for use by our military, government and commercial fleet Dodge Ram customers.

Senators, we share your goals of reducing petroleum consumption and increasing the use of renewable fuels. The actions described above, plus our continuing efforts to improve the efficiency of gasoline-powered vehicles, increase our use of diesel engines—which provide 20–40 percent improvements in fuel economy compared to equivalent gasoline-powered vehicles—and our leadership in fuel cell vehicles—with more than 100 vehicles, ranging from small cars to transit buses, in operation around the world today—are testimony to our commitment.

DaimlerChrysler believes that incentives are the most efficient means to increase production, distribution, and sales of both renewable fuels and vehicles capable of operating on them. In this regard, some of the provisions of your bill, especially those regarding the elimination of a manufacturer's CAFE credits, are of concern to us. But given our shared goal of increasing the number of FFVs, we look forward to working with you and other Members of the Congress to resolve any different approaches we may have on this extremely important issue.

Sincerely,

TOM W. LASORDA,
President and CEO.

The CHAIRMAN. They came, recently, to Washington, within the last two weeks or so and met with several of us. They have written back that they understand the need for alternative energy. They understand the need for fuel economy. They pledge, in this letter, that, quite apart from ads that I—we've all seen in the national papers—that the three companies will provide at least 1 million flexible-fuel cars in this production year. They pledged to increase that to at least 2 million by the 2010 production year.

Now, even that, we might say, is still very slow progress with regard to an entire fleet of cars in this country, but here is a public statement that this is important, in terms of their policy, producing cars in a commercial world in which they have to sell those cars. And then, furthermore, they point out, correctly, that a lot of E85 pumps are going to be required at filling stations around the country. And so, they're very hopeful that their friends in industry will take that seriously.

Here you have advocacy by American business people who have come and visited with Members of Congress. They have come back and written down on a piece of paper to us, "We pledge to do these things," because they are very important for America and for our energy policy, if there are not to be severe adjustments in the standard of life to which we've become accustomed.

The good news is that there were also listeners and dialog that produces results, sometimes of a nongovernmental character. No one has mandated anybody to produce flexible-fuel cars, but there's a recognition, as Americans, that this is tremendously important to do. My guess is that other people in other countries, likewise, may have similar sentiments if they understand that there's a vanguard of the faithful prepared, really, to offer leadership in this regard.

We appreciate your papers and your testimony very much as a part of this dialog. We look forward to staying in touch with all three of you.

And before I conclude this hearing, let me ask if any of you have a final comment for the record this morning.

[No response.]

The CHAIRMAN. Very well. We thank you and ask that you stay in touch, as I've mentioned.

And the hearing is concluded.

[Whereupon, at 10:50 a.m., the hearing was adjourned.]

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