



THE KREMLIN PLAYBOOK IN EUROPE

CSD

CENTER FOR
THE STUDY OF
DEMOCRACY

THE KREMLIN PLAYBOOK IN EUROPE



The Kremlin Playbook in Europe analyzes the tools and methods used by Russia to exercise its influence on the continent. In particular, it shows how the Kremlin enjoys considerable surrogate power in some countries because of the oligarchization of their governance systems. It also highlights the effect of blinkered national policies which grant Russian capital access to European financial hubs. The report argues for a common transatlantic approach in the face of these threats.

The report expands the map of Russia's footprint built by previous *Kremlin Playbooks*, which examined Russia's attempts to capture political and economic decision-making in sixteen European countries, by analyzing Greece and Cyprus. Their strategic location in the southeast of Europe and the eastern Mediterranean, common religious traditions, and historic ties make them an object of influence operations by the Kremlin.

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RUSSIA IN THE GLOBAL POWER COMPETITION: THE PLAYBOOK IS HERE TO STAY

In 2016, *The Kremlin Playbook: Understanding Russian Influence in Central and Eastern Europe*¹ was the first comprehensive policy report to expose Russia's approach to inciting and winning (or at least disrupting in Europe) the next great power competition. In the report, the Center for the Study of Democracy (CSD) and the Center for Strategic and International Studies (CSIS), unveiled an unvirtuous cycle of state capture, which has allowed Russia to influence strategic foreign policy decisions in Central and Eastern Europe. In the past decade, the Kremlin has integrated more instruments into this cycle, in order to project its global influence. The enhanced effectiveness of these tools of distributed power in Europe was achieved by having them first developed for domestic use in Russia. The West has additionally enabled the Kremlin's tools by failing to anticipate and then to act on Russia's developing intent to disrupt the European order. Since the collapse of the Soviet Union (and even before that), Russia has had unfettered access to the global economic and financial system and to Western technological and media streams. This access has allowed it to strike and disrupt where opportunity arises – internally (such as elections) or externally (such as war, migration, economic or health crisis).

In 2019, CSD and CSIS published the *Kremlin Playbook 2: The Enablers*.² It expounded on the risks inherent to large Russian investment flows in Europe and analyzed the factors facilitating (illicit) financial flows from Russia, which jeopardize the integrity of open democracies and market economies. By allowing Russian economic influence to cycle through their systems, enablers actively participate in the weakening and discrediting of common European democratic governance structures, as well as their own.

The inventory of European vulnerabilities and dependencies was expanded in *The Kremlin Playbook in Southeast Europe: Economic Influence and Sharp Power*.³ This 2020 report illustrates that even though Russian economic power in the Balkans has declined since 2014, its sway over strategic decision-making in the region remains strong, particularly in the energy sector where it has locked governments in costly infrastructure projects. The report zooms in on the range of sharp power instruments used by Russia to amplify its influence, such as media propaganda, the leveraging of cultural and religious ties, and the sponsoring of civil society activities.

¹ Conley, H., Mina, J., Stefanov, R. and Vladimirov, M. (2016). *The Kremlin Playbook: Understanding Russian Influence in Central and Eastern Europe* (New York: Rowman & Littlefield, 2016). See also: Shentov, O., Stefanov, R., and Vladimirov, M. Eds. (2019). *The Russian Economic Grip on Central and Eastern Europe*. (Routledge Contemporary Russia and Eastern Europe Series, London: 2019).

² Conley, H., Ruy, D., Stefanov, R. and Vladimirov, M. (2019). *The Kremlin Playbook 2: The Enablers* (New York: Rowman & Littlefield, 2019).

³ Stefanov, R and Vladimirov, M. (2020). *The Kremlin Playbook in Southeast Europe: Economic Influence and Sharp Power* (Sofia: Center for the Study of Democracy, 2020).

Building on these findings, the present report further expands on the analysis of Russian influence in Europe. Crucially, it supplements previous research with two new in-depth country analyses of Cyprus and Greece. A number of critical findings emerge from the application of the *Kremlin Playbook* methodology:

- Corruption and state capture have become the instruments of choice in Russia's attempt to disrupt order and restore its dominance in the continent.
- The oligarchization of several European governance systems makes them vulnerable to state capture by Russia and allows the Kremlin to enjoy considerable surrogate power.
- Given the high level of integration among countries in Europe – within the EU but also through looser mechanisms, such as the EEA and accession agreements – the effects of Russian intervention in government decision-making or the economy of individual countries may provide continent-wide leverage.
- A concerted European response has been undermined by short-sighted national policies seeking to attract rogue Russian capital through tax concessions, or cheap Russian gas by circumventing EU energy regulations.
- The dysfunctional state of transatlantic relations facilitates the Kremlin's plans in Europe, especially as Russia's intrusiveness is experienced in different ways by individual countries, institutions and companies.
- Some of the key EU members still imagine Russia as an indispensable ally or necessary evil to be able to withstand global power competition. Their hesitation delays the development, and, needless to say, the implementation, of common policies and institutions, such as an EU-wide rule-of-law mechanism, central anti-money laundering agency or robust screening of foreign investment.

The subversive effects of the Kremlin's power kit will reverberate in Europe particularly severely amidst an environment of crisis. The post-Covid 19 economic crisis has notably weakened transatlantic ties. Along with an estranged United Kingdom, and an insufficient will in Brussels to tackle problems such as corruption and state capture, all this undermines Europe's capacity to shut down the Kremlin's avenues of interference.

It is only through an enhanced understanding of how these avenues are laid out – such as provided by this *Kremlin Playbook* – that a policy of counteraction can be designed and integrated in the European agenda. Moreover, the United States continues to be indispensable in the safeguarding of Europe's security and limiting of Russian and Chinese interference. In light of their role, such a policy can be neither effective nor sustainable without a shared understanding with the United States regarding the nature and urgency of the threat.

THE KREMLIN'S STATE CAPTURE POWER

The exercise of Russian influence in Europe is shaped by two defining characteristics of the political regime in Moscow – autocracy and corruption. In the last two decades, these two strands have come to reinforce each other. As political power became less contestable, it was exploited in ever greater degrees for the private benefit of the Kremlin's inner circle. Conversely, the concentration of wealth in the hands of a few privileged political actors has further crippled what was left of democratic politics. Despite this, Russia has preserved the façade of democracy and market economy, which has allowed it to appear in alignment with the global transition to a Western liberal consensus. This has provided the Kremlin with credible deniability while preserving tight control over the country through its preferred instruments of command – its security services and state-owned enterprises. The resulting state capture⁴ power cemented the Kremlin's grip on Russian society and allowed it to pursue its revisionist foreign policy.

Russia's state capture power exploits and thrives on democratic deficits and governance gaps in Europe. The *State Capture Assessment Diagnostics*,⁵ a novel monitoring methodology, has revealed some **critical vulnerabilities in the public governance of European countries**. Such vulnerabilities provide excellent entry points for the Kremlin and other authoritarian influences. This is particularly worrying amidst the resurgence of great power competition, in which Russia and China have seemingly teamed up to undermine American leadership in the current world order.⁶ Europe is the jewel in the crown in this order and Russia will continue using state capture in its quest for geopolitical redistribution in Europe.

State capture allows the Kremlin to mobilize various resources for its revanchist ambitions, from computer hackers to gas pipelines. In Europe, the Kremlin relies on **state capture institutional enablers** or governance gaps. These may include any combination of lack of integrity and impartiality in politics and government, ineffective (anticorruption, money-laundering, political party financing, etc.) laws, constrained media freedom, judicial incapacity, and others. Thus far, the *Kremlin Playbooks* have revealed four recurrent tools of Russian state capture influence in Europe:

- The promotion of large-scale energy projects that undermine the common energy security and transatlantic foreign policy agenda;
- The support of political parties with anti-Western (anti-NATO and anti-EU) or extremist, divisive agendas;

⁴ State capture is the process of privatization of government functions, which turns institutions rogue without destroying the semblance of democracy and market economy.

⁵ Stoyanov, A., Gerganov, A. and Yalamov, T. (2019). *State Capture Assessment Diagnostics* (Sofia: Center for the Study of Democracy, 2019). The diagnostics tool was developed by the Center for the Study of Democracy in 2019 and piloted in five European countries: Bulgaria, Romania, Czech Republic, Italy, and Spain.

⁶ Colby, E. and Mitchell, A., "The Age of Great-Power Competition: How the Trump Administration Refashioned American Strategy," *Foreign Affairs*, January/February 2020 (New York: Council on Foreign Relations, 2020).

- The locking of strategic companies and/or assets in the West in long-term deals that make them dependent on Russian political cooperation;
- The flooding of the European cyber and media space with disinformation and propaganda via state-run and corporate-controlled news outlets and security services operations.

The Kremlin – private partnerships

The Kremlin has an asset which makes its foreign state capture operations particularly effective. It projects its influence not only through the governmental apparatus but also with the help of its oligarchs, the owners and managers of Russia's highly concentrated industrial and financial wealth. Russia's oligarchs, often appointed by the state, need access to the government to preserve and enlarge their wealth. In return, the Kremlin avails itself of this wealth for its foreign policy purposes. Through its control over the Russian judiciary and law enforcement, as well as the media, the Kremlin can bend to its will any private business undertaking, turning it into a potential instrument of influence. This explains how Russia has been able to have an outsize influence in Europe, despite its relatively less-developed economy.

Russia's effective state capture influence model rests on the confluence of interests between Russian oligarchs and the Kremlin, and between the former and their local counterparts in European countries. Although the oligarchization of domestic politics in these countries has been homegrown, the Kremlin has actively exploited it, going so far as to promote it as a viable governance model. The essence of this process is aptly summarized by Michael Carpenter: "Europe's existential threat is a matter of governance. It is the threat of the corrupt 'oligarchization' of European politics."⁷ Given the EU's prevalent unanimous decision-making, Russia's inroads in some European countries could eventually erode decision-making across the continent.

Among the countries most susceptible to Russian oligarchic state capture influence in Europe are those belonging to the former Soviet Union bloc. In these countries, Russian elites have been "much better placed to exploit these vulnerabilities due to their pre-existing networks and links [...], as well as the development of Russia's own internal state capture system."⁸ These networks have been nurtured by a mutual partnership between Russian and domestic oligarchic groups that operate in partnership to acquire strategic and lucrative assets such as telecoms, refineries, tobacco companies, real estate chains, metallurgical plants and arms manufacturers or to ensure a dominant position in key markets. Local power brokers benefit from Russian political and financial support in engineering the deals. In return, they use various informal and illicit means to ensure preferential regulatory status for the oligarchic partnership.

The two primary channels of the Kremlin's state capture power in Europe have been its **state-sponsored networks of influence and corruption** and the **control over Russia's economic and financial flows**. Their success has been facilitated in large part by weak division of powers with feeble checks and

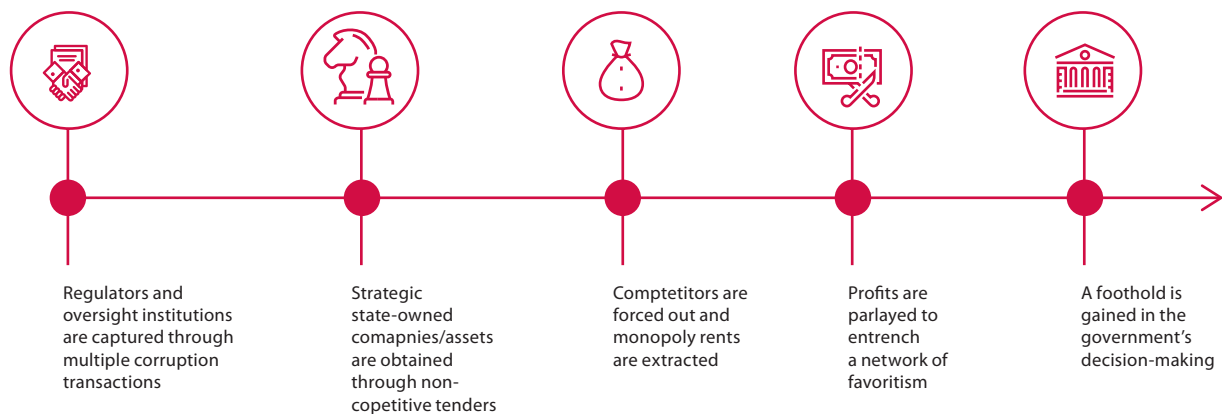
⁷ Carpenter, M., "The Real Threat Facing Europe Isn't Russian Troops. It's Oligarchs," *Newsweek*, May 25, 2019.

⁸ Stoyanov, A. and Stefanov, R. (2019). "State Capture: Kremlin's Influence Amplifier," in Shentov, O., Stefanov, R., and Vladimirov, M., Eds. (2019). *The Russian Economic Grip on Central and Eastern Europe*, 28-43, p. 28.

balances, the exertion of strong government influence or control over popular media, weak civil society, and high corruption among the public administration. These governance deficits have all provided entry points for foreign governments with state capture power.

In addition, many European economies have established flexible legal regimes for companies alongside complex advanced corporate services which elude national regulation. With regard to company law, taxation and incorporation, permissive, and at times opaque business and legal environments, are magnets for shady capital. Lax oversight in this regulatory environment has allowed the Kremlin to strategically entrench its economic network in Europe. In particular, it is large companies in enabling countries, and their networks of ownership in Europe, that provide Russian-owned companies with broad access to the European markets through mergers and acquisitions. A highly developed corporate service provider sector (lawyers, accountants, incorporation agents, etc.) continues to support complex financial schemes and company structures.

Figure 1. The process of the Kremlin's influence on foreign governments



Source: CSD.

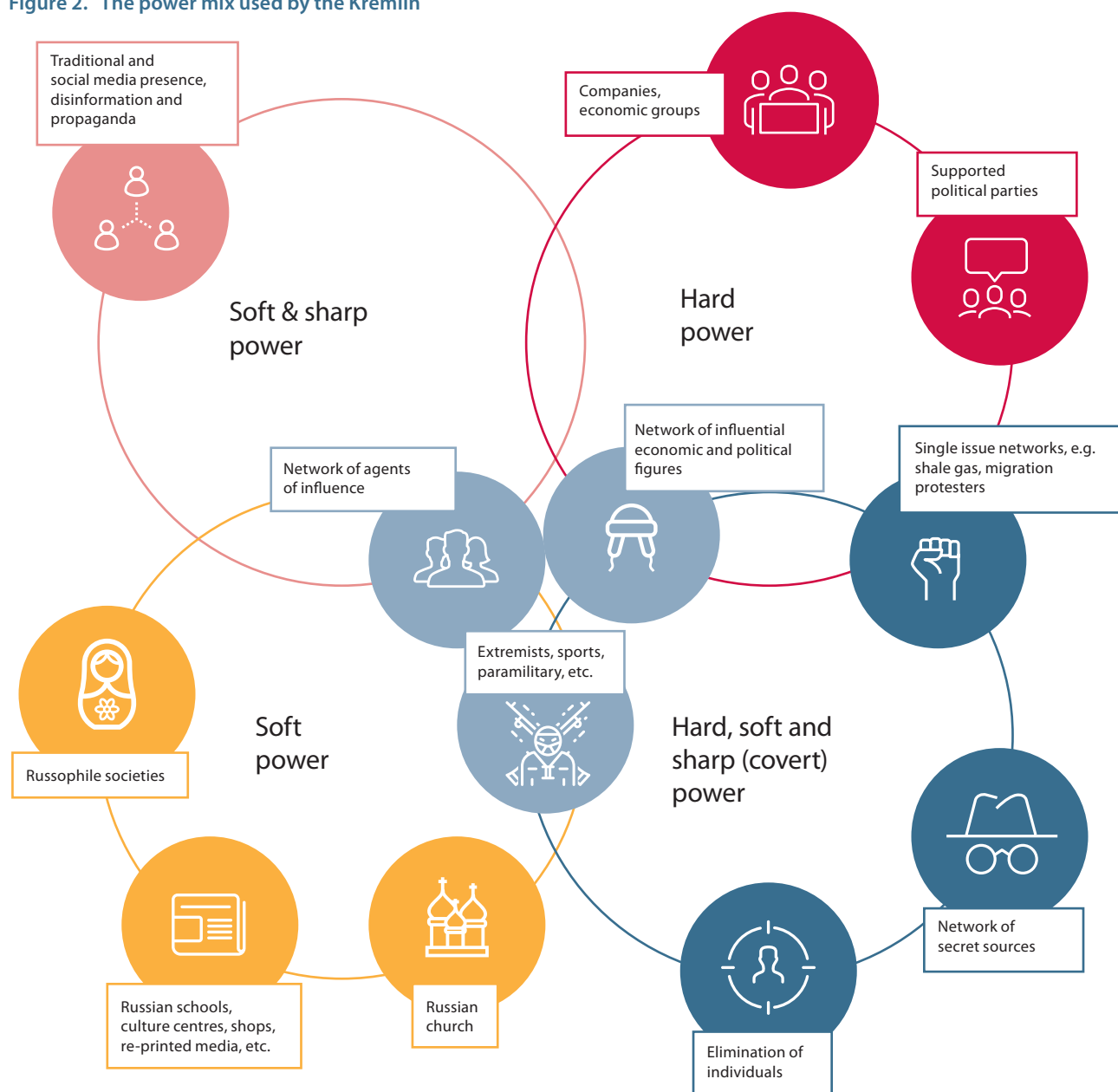
The Kremlin's power mix

The Kremlin has gradually revived both the more traditional elements of its hard power, such as aggressive military and political posturing, alongside covert operations or “active measures”⁹ across Europe. The development of other strategies, while less visible, is no less alarming. For instance, the Kremlin has been cultivating ties – both official and unofficial – with European political parties, in a bid to challenge the existing European order from within. These include engagements with opposition extremist parties in Germany and France, as well as with anti-establishment, anti-European governing parties in Austria, Italy, Bulgaria and Serbia. Clearly, in its choice of political partners, the Kremlin favors those inclined toward obstructionism, and thereby prone to political fragmentation – but also those capable of leveraging their

⁹ A term used by Soviet and Russian security services to denote covert operations intended to disrupt or shape events in other countries. Such operations can also be executed under diplomatic cover: see Prothero, M., “Unit 29155: Putin's Assassination Squad – Suspected of Killings All over Europe – Received Diplomatic Cover from the Russian Mission in Switzerland,” *Business Insider*, March 16, 2020.

parliamentary backing to influence debates of strategic importance to Russia. Indeed, the Ibiza affair or (sting) operation on the then Austrian vice-chancellor demonstrated how vulnerable Europe's political core is.¹⁰ Russia has also sweetened the retirement plans of many European countries' top officials by providing them with lucrative jobs on the boards of state-owned and private Russian energy and banking companies – most notably for German and Austrian former chancellors and ministers. This military-political aggressiveness has been accompanied by constant intimidation by the Kremlin and its foreign ministry. Their targets are the EU, NATO and European institutions, but most of all the most vulnerable countries of Central and Eastern Europe and the Balkans.

Figure 2. The power mix used by the Kremlin

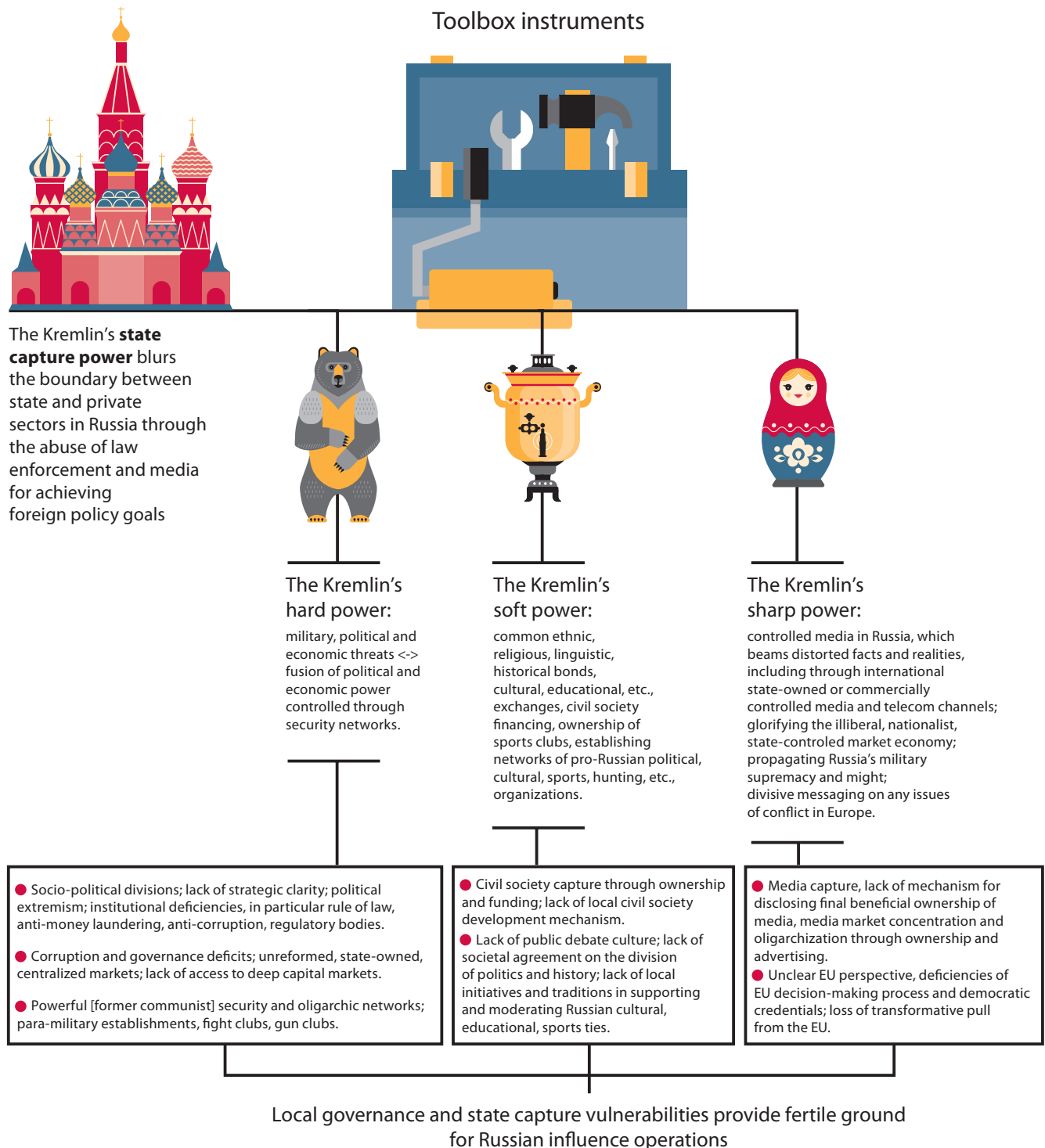


Source: Ruslan Stefanov and Martin Vladimirov, *The Kremlin Playbook in Southeast Europe: Economic Influence and Sharp Power* (Sofia: Center for the Study of Democracy, 2020).

¹⁰ CSD, *The Kremlin Playbook: The Movie*, CSD Policy Brief No. 85, 2019.

The Kremlin's state capture power allows Russia to develop a low-cost, vertically-integrated strategy in order to weave a web of influence in Europe. In some Slavic countries in Central and Eastern Europe, for example, the centuries-old soft power presence of Russia has allowed it to win the favor of national governments via proposals for cultural, church, and youth initiatives. These have subsequently become platforms to disrupt local political discourse while opposing transatlantic views.

Figure 3. How the Kremlin's state capture power targets governance vulnerabilities in CEE and the Western Balkans



Source: CSD.

Media capture

In the Kremlin's state capture power mix propaganda and disinformation have become crucial instruments in the amplification of Russian influence in Europe. Media capture has played an important role due to its "very high impact and importance in the political process and in the institutional checks and balances in EU democracies."¹¹

In using the media to bolster its power agenda, the Kremlin opts for the medium that is most trusted in a given media landscape. While this is typically social media, the popularity of traditional mainstream outlets would also make them candidates for political alliances. Multilingual state-sponsored channels *RT*, *Sputnik*, and *Russia Beyond* service the Russian diaspora but also cater to the Eurosceptic public in Europe. The translation of Russian media content into local languages facilitates coverage favoring the Kremlin's agenda. Journalists – typically freelancers – providing such content are given privileged access to information or areas where other media are restricted – for instance the war in Syria. The credibility of the content is boosted by hack reporters' distributing of content to domestic journalists or overseas media, thus creating the impression that a piece of information is widespread.¹²

Russia's strategy of media capture through the ownership (of media companies but also of telecoms) and control of advertising budgets is compounded by the influence exerted through journalistic proxies which manufacture fake news and disinformation. One effect of the concentration of ownership and advertising is the marginalization of investigative journalism as a major tool for transparency. This is felt particularly strongly in the former communist countries in the east and south of Europe who have weakly enforced media regulations. They depend on large commercial advertisers in small advertisement markets, as well as the oligarchization of the media markets (the oligarchic networks of which exhibit close ties to Russian businesses).

In these countries, the coupling of media ownership with senior government officials and political leaders leads to the concentration of public and private funds in a select few media companies. These are then also often targeted by Russian foreign policy or private interests. Such media channels tend to peddle pro-state capture, paternalistic narratives to please their local political masters, for which the Kremlin typically provides a favorite model in Europe. They could get additional motivation if their owners are included in lucrative deals with Russia. This coupling has given some national governments in Europe control over editorial policy in key media outlets. This has helped to bolster local and Russian political or economic interests, even though the government's official position may appear balanced or neutral regarding the same issues.

¹¹ Rumena Filipova et al. (2018). *Russian Influence in the Media Sectors of the Black Sea Countries: Tools, Narratives and Policy Options for Building Resilience* (Sofia: Center for the Study of Democracy, 2018), p. 13.

¹² Yalamov, T. (2019). "Russian Influence, Trust in Media and Media Capture," in Shentov, O., Stefanov, R., and Vladimirov, M., Eds. (2019). *The Russian Economic Grip on Central and Eastern Europe*.

JUDO ECONOMICS: THE CONDUITS OF RUSSIAN INFLUENCE IN THE EUROPEAN ECONOMY

The most critical variable of Russia's state capture power in Europe is its direct and indirect economic footprint on the continent. It is also the one that is easiest to dismiss as an instrument for influence due to the common misunderstanding that it is solely linked to Russia's economic prowess. While military posturing, political bashing and media propaganda are easier to detect, they can rarely affect the core of the socio-economic fabric of European societies from within.

The basis of Russia's economic influence is rooted in the decades-long **unfettered integration of Russian businesses in the European economy** and the ensuing political networks enabled by a system of patronage and corruption. Since the collapse of the Soviet Union, an estimated USD 1 trillion in Russian funds has flown into the European financial system. This reflects a large network of Russian businesses proliferating in strategic European industries.¹³

The Kremlin has been further emboldened by Europe's lack of adequate response to Russia's economic maneuvering. Together with its member states, the EU has been **reluctant to even acknowledge and monitor, let alone handle the risks of Russia's economic footprint**. The preferred response has been economic sanctions, whose function appears merely symbolic. The difficulty of unanimous vote also serves as a deterrence to effective response. Indeed, Europe's export powerhouses – such as Germany and the Netherlands – seem to believe Europe cannot withstand a great power competition without relying on Russia for resources and as a market for its goods. European leaders have therefore been reluctant to adopt a clear and consistent policy vis-à-vis Russia.

Meanwhile, Russia tries to leverage the EU's economic weight against it – a move central to judo, President Putin's favorite sport. The deepening dependence on Russian energy sources and large markets with limited domestic competition has pushed Europe closer to Russia. The **Russian economic footprint** thus manifests through **direct** (e.g. ownership of assets and companies) and **indirect** (e.g. the promise of large-scale infrastructure projects or access to the Russian market) **control**. Strategic assets controlled by Russian companies across Europe include the largest telecom in Italy, and some of the largest energy and metallurgical businesses on the continent – these indirectly account for a significant exposure of some of the largest banks in Europe. In addition, Russian energy companies have locked their European counterparts into long-term supply, exploration, production, and infrastructure deals, consolidating Russia's decade-long presence in the European energy markets.

¹³ Novokmet, F., Piketty, T. and Zucman, G. (July 2017). *From Soviets to Oligarchs: Inequality and Property in Russia 1905 – 2016*. WID.world. Working Paper Series N° 2017/09.

The Kremlin leverages Russia's economic footprint in Europe to achieve influence along three main paths:

- using the **energy supply dependence** to preserve the dominant position of Russian oil, gas and nuclear majors;
- taking advantage of **regulatory loopholes** and administrative complacency to move large amounts of funds, some from illicit activities, into the European capital, financial and real estate markets;
- capitalizing on the exposure of European companies to the Russian market to create **powerful business-to-business alliances** – these would help to nudge the foreign and strategic policies of governments in a favorable direction.

In light of these strategies, the degree of vulnerability of European countries differs based on their level of energy dependence, the strictness of tax, banking and corporate ownership transparency and the investment exposure of domestic businesses to the Russian market. Nevertheless, the ability of the Kremlin to **deploy and control these techniques in a coordinated manner** continues to sustain and expand Russia's influence over the European economy and politics.

European hospitality for Russian money

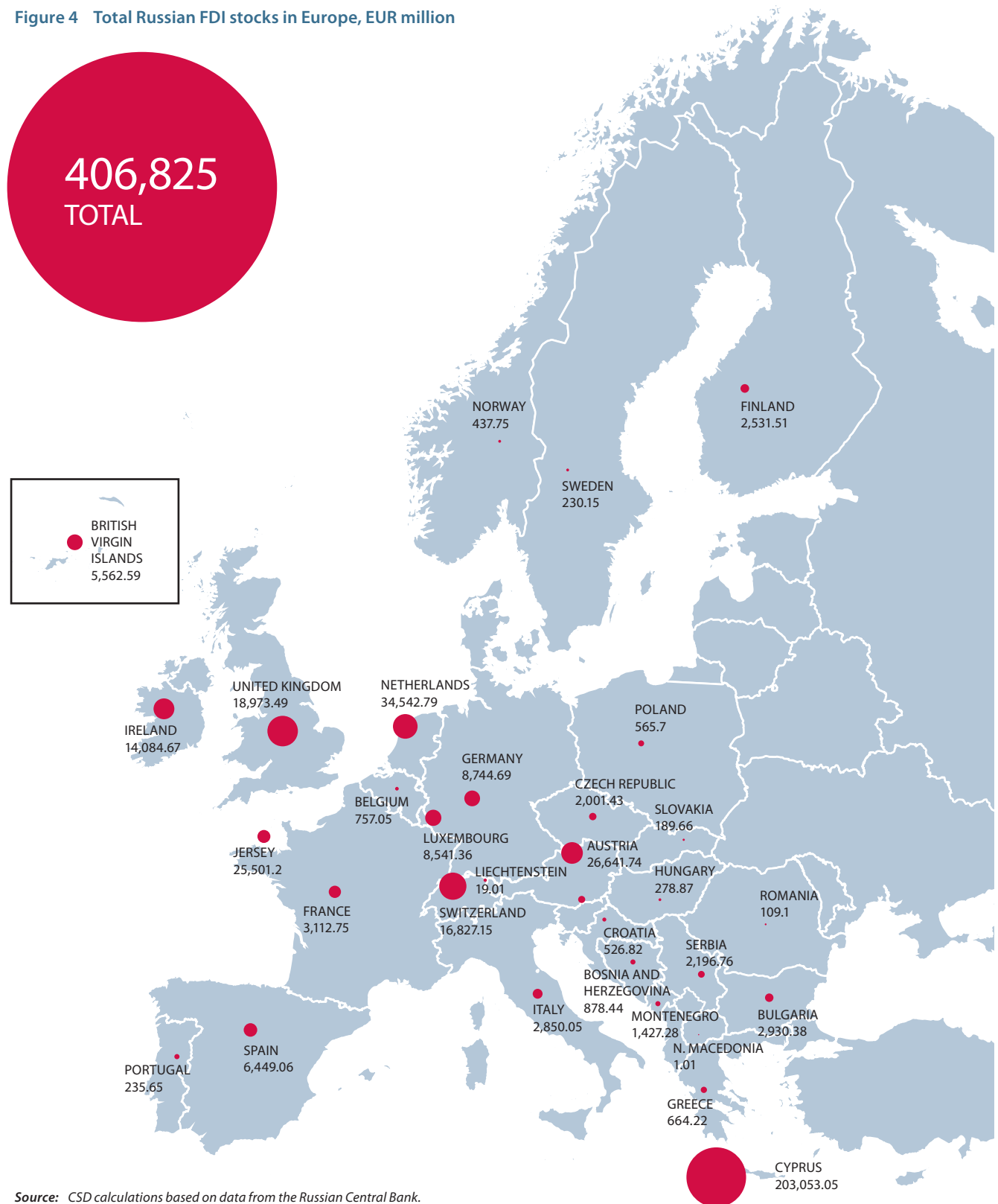
Finance has been an important channel for the growth of Russian economic presence in Europe. The risks inherent to the penetration of Russian funds in Europe have been largely underestimated, if not neglected; **the vetting of financial flows from Russia has been half-hearted at best**, allowing Kremlin's cronies to move enormous amounts of money into the European financial system. For decades, corrupt dictators around the world have used Western financial institutions as a refuge for their wealth. Yet these have mostly been confined to the private operations of senior government officials. Covert capital inflows from Russia, on the other hand, have been used to influence core democratic institutions, such as the funding of political parties and the media. In the past two decades, the amount of funding channeled into Europe has totaled 300% of Russia's national income,¹⁴ which threatens to destabilize the European financial system and thus warrants more careful consideration.

Russian companies have shifted considerable financial holdings to **European financial hubs** notable for their low tax burden, easy registration procedures and lax standards of ownership transparency. Around half of this stock of Russian FDI has been parked in offshore banks in Cyprus, the Netherlands, the British Virgin Islands and Switzerland with most of the operations representing a round-tripping of equity and debt between an EU-based subsidiary and its mother company located in Russia. The rest has been invested in large-scale infrastructure projects, energy, mining and manufacturing assets, as well as real estate.

Russian businesses have used the liquidity and reputation of Western financial hubs to obfuscate corporate ownership networks, avoid taxation and, in some cases, to illicitly move funds out of Russia in order to conceal their true origin. The "Russian Laundromat" case showed that money transfers between shell companies may be used for money laundering, with financial

¹⁴ Ibid.

Figure 4 Total Russian FDI stocks in Europe, EUR million



and security implications.¹⁵ Money laundering schemes involving Russian businessmen and politicians have also been detected in the real estate sector and in the purchase of luxury goods across Europe.

¹⁵ OCCRP, “The Russian Laundromat Exposed”.

Anti-corruption investigations led by Russian opposition politicians have revealed high-level Russian politicians – including the Prime Minister – as well as businessmen with government ties to own luxury multi-million-dollar properties in Italy and elsewhere.¹⁶ According to the Russian central bank, which categorizes cross border money transfers by their purpose, Russian nationals spent a total of almost USD 42 billion abroad in 2019 – up from 31 billion in 2017 – with the UK, Switzerland, Latvia, Spain and the United States being among the most preferred destinations. Russians have spent a total of USD 14 billion on real estate abroad since 2009 or 3.4% of the total Russian FDI abroad.

Box 1. SPV Conduits

The actual size of Russian real estate investments in Europe is probably much higher as many property deals are sealed by private companies, whose transactions are not recorded in the Russian central bank's statistics. It is increasingly apparent that real estate investment is not just a display of conspicuous consumption by Russian wealthy elites but a means of storing and expanding value.¹⁷ A large share of these real estate investments is channeled via offshore special purpose vehicles (SPVs) to lower taxation and make ultimate beneficial ownership untraceable.¹⁸ The deals are structured in such a way as to appear solely in the interest of the SPV, which then enables the assets to be used in inter-company loan schemes for tax avoidance. The reason for this is that both real estate income and capital gains taxes are much lower in such transactions. The use of SPVs in the US real estate market, for example, reveals a loophole in the US anti-money laundering legislation and the Bank Secrecy Act that makes concealing the beneficial ownership very easy. Similar loopholes exist in a number of preferred destinations for Russian real estate investment, including the UK, Switzerland, Spain and Italy.

Although real estate investments are dispersed, their overall economic impact in countries such as the UK, Austria, Italy and Spain is significant due to the dependence of key regions on the real estate market (e.g. tourist resorts). Moreover, in many Western European countries, property investments of between EUR 500,000 and 1 million grant individuals the right to permanent residence or the so-called golden passport. Since 2010, a total of around 300,000 Russian citizens have received a first-time residence permit in an EU country, making Russia among the top five biggest nationalities of new residents to the EU.¹⁹ In addition, the EU received almost 15.4 million visits from Russian nationals in 2019.²⁰ Like the Russian business presence, the increase in the number of Russian residents in the EU also increases security risks as it provides an effective base for the Kremlin to continue its disruptive operations in Europe. In 2019, the European Commission initiated a review of the golden passport regimes in EU countries, asking member states to strengthen oversight to reduce security risks. It has also singled out three countries for their unwillingness to reform their golden passport regimes – Bulgaria, Cyprus and Malta – all of whom have considerable ties with Russia. Never-

¹⁶ RFE/RL, "Navalny Video Accusing Medvedev of Corruption Posted on Government Websites". June 11, 2017.

¹⁷ Fernandez et. al., "London and New York as a safe deposit box for the transnational wealth elite," *Environment and Planning, A: Economy and Space* 48, no. 12 (2016), 2443-2461.

¹⁸ Ibid.

¹⁹ Data from the Eurostat on First Permits in the EU by Citizenship.

²⁰ Federal Tourism Agency at the Russian Federation's Ministry of Culture. Statistics on the Volume of Foreign Travels by Russian Citizens in 2019.

theless, as of 2019, some 20 EU countries still provide visas for investments which may ultimately allow for citizenship rights.²¹

Figure 5. Number of Russian citizens with EU residence



Source: CSD calculations based on Eurostat data.

Domestic intermediaries including **law firms, corporate service providers, consultants, PR agencies** and others have been assisting Russia in its channeling of foreign investment – including in real estate – to business and political activities in Central and Eastern Europe. These financial resources have contributed to the development of patronage networks and the preservation of Russia's dominant position in strategic sectors. Russia has also used these enablers to serve as vehicles for the financing of political parties, protest campaigns and the acquisition of media outlets. At times, Russia has used these subversive tactics to provoke government change, while encouraging the rise of bogus extremist parties, the shift in foreign policy priorities, and opposition to EU common legislative initiatives.

European countries have been both unwittingly and knowingly complicit in Russia's penetration of their economies by Russian economic actors seeking to exploit their lax regulatory standards on financial flows and banking secrecy. For instance, regulatory authorities in the EU have overlooked the possibility that offshore entities may be used to firm up the monopoly status of Russian energy companies in neighboring EU member states, or to channel resources to non-business-related or political activities.

Moreover, Russian companies have systematically used **complicated pricing schemes** to transfer funds to European financial hubs such as the Netherlands, Switzerland, the UK, and Luxembourg. **Tax haven policies** do not only ease the entry of questionable finances from Russia but also result in tax base erosion and profit shifting from fellow European countries. The implementa-

²¹ Vlagyislav Makszimov, "Golden Visas and Passports Still Widespread in Europe, Study Finds," *Euractiv*, March 27, 2020.

tion of such a policy by the Netherlands, for example, has been shown to cost other EU countries billions in foregone revenue from corporate tax.²² At the end of 2019, the Netherlands attracted a stock of EUR 40 billion in Russian investment, following which Gazprom, Lukoil, Rosneft, Gunvor and Inter RAO, five of Russia's largest firms, all moved tens of billions of euro in assets to the Netherlands. There they benefit from low or non-existent withholding taxes on interest and capital gains, negotiable corporate income rates and a flexible bilateral double taxation treaty that allows for massive round-tripping to take place for investment in Russia and the CEE.

Round-tripping through shell companies in places like the Netherlands makes the acquisition of critical assets harder to trace to a specific Russian company or individual. This is because shell companies tangled in a web of intermediaries are able to conceal money-laundering and corrupt transactions involving local officials, and can also be used as vehicles for strategic mergers and acquisitions.²³ It is therefore not surprising that, along with Cyprus and Luxembourg, the Netherlands is, at least on paper, one of the largest foreign investors in CEE.²⁴ Consequently, shell companies with Russian ultimate beneficial ownership invest in regions with more corruption and a higher concentration of extractive industries.²⁵

The layering of profits through a string of intermediaries creates ample opportunities for the siphoning of funds into alternative investments in real estate, telecommunications, and manufacturing. This entrenches Russian entities even deeper in the European financial system. In such a money laundering mechanism, layering is then typically followed by integration – in the Kremlin's case toward political ends, such as active measures, the funding of political parties, electoral manipulation, etc.

Russian oil companies in particular have gained expertise in using trading shell companies that engage in transfer pricing. An example is Lukoil, a private Russian oil company which has been instrumental in many of Kremlin's policies in Europe. Lukoil combined the use of tax-treaty jurisdictions and shell companies to reduce its overall tax bill, hurting in the process the public finances of the countries in which it operates.²⁶ Transfer pricing schemes allow one subsidiary of one holding company to overcharge another – both registered in different jurisdictions – for the sale of a product or service without reflecting general market levels. The subsidiaries in a low-tax country would purchase goods from another subsidiary at a loss, thus reducing corporate taxation for the holding as a whole.

²² Tax Justice Network, "Revealed: Netherlands, Blocking EU's Covid19 Recovery Plan, Has Cost EU Countries \$10bn in Lost Corporate Tax a Year."

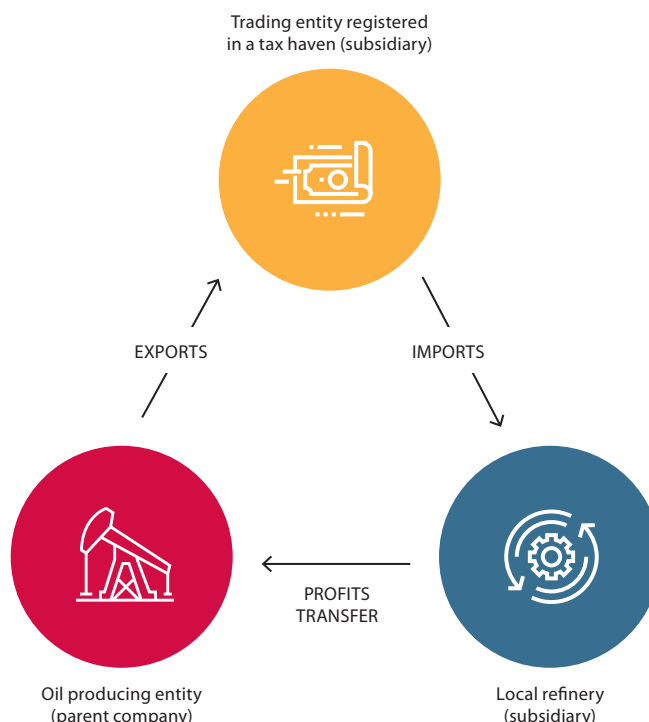
²³ 31% (more than 2 million) of all suspicious transaction reports (STRs) submitted to the national financial intelligence units (FIUs) from 2006 to 2014 originated in the Netherlands, the second highest number after the UK. Europol. (2017). *From Suspicion to Action: Converting financial intelligence into greater operational impact*, (Luxembourg: Publications Office of the European Union, 2017).

²⁴ Although the central bank statistics in Bulgaria shows that the Netherlands is consistently the largest foreign investor, a detailed overview of the company level data pointed that Russian companies stand ultimately behind around 60% of the transactions.

²⁵ Ledyeva, S., Karhunen, P. and Whalley, J., "If Foreign Investment is not Foreign: Round-Trip Versus Genuine Foreign Investment in Russia," CEPIL, WP No. 2013-05.

²⁶ Lukoil has been consistently one of the major foreign investors in a number of CEE countries although the investment flows have been credited to the Netherlands. The reason is that Lukoil has used its Dutch subsidiary for most of its business operations in Eastern Europe.

Figure 6. Transfer pricing scheme through trading shell companies



Source: CSD.

Russia's direct and indirect footprint

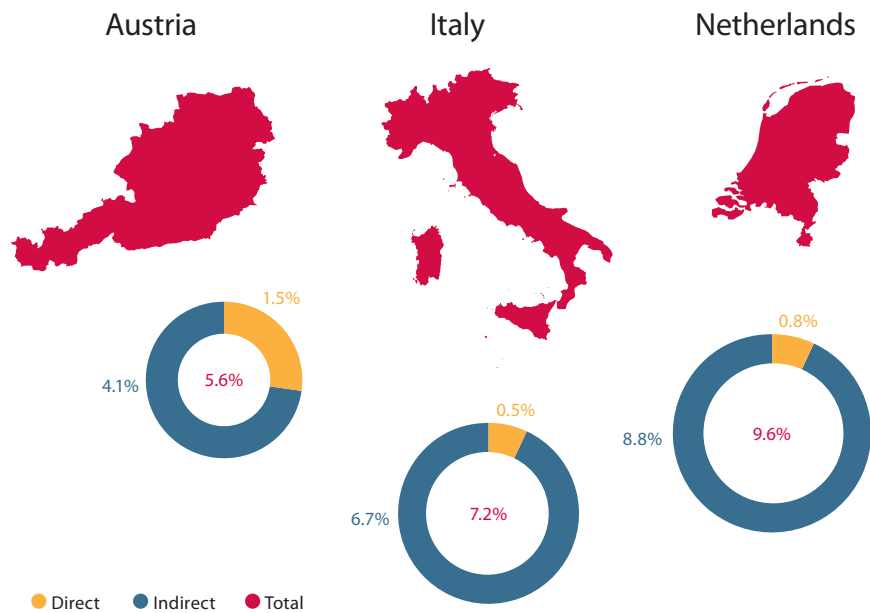
The *Kremlin Playbook* reports chart the Russian economic footprint in Europe – direct and indirect – so as to better understand how structural economic vulnerabilities are translated into political influence in the continent. The analysis of Russian economic presence has two distinct dimensions: its direct manifestation – whereby assets are ultimately owned (either explicitly or through shell companies and offshore accounts) by Russian entities, as well as a domain of indirect influence achieved through European corporate exposure to the Russian market.²⁷

These two aspects exist in differing proportions across the continent. Jurisdictions providing various tax breaks and flexible incorporation regulations – such as the Netherlands or Cyprus – are used to obscure the Russian origin of the money, allowing its investment elsewhere while erasing its traceability to Russia. While this is done for a variety of economic reasons, both legitimate and illegitimate, the political motivations are undeniable. Such a maneuver implicitly acknowledges the toxicity now attributed to Russian capital, primarily for its association with the Kremlin. This is valid both when money is invested in other European countries and when it is “round-tripped” back into Russia as if of European origin.

When European economic champions get involved in Russian-promoted projects, their close ties to national governments provide these deals with significant political cover. This serves the Kremlin's interests by expanding its indirect economic footprint, and thus increasing the exposure of European

²⁷ The distinction is elaborated in Stefanov R. and Vladimirov, M., *The Kremlin Playbook in Southeast Europe*.

Figure 7. Corporate footprint (% share of the Russian companies' revenues out of the total revenues in the economy)



Source: CSD calculations based on corporate databases.

companies to the Russian market. The consequent emergence of “business-political networks” can then ensure that “strategic policies” in the European host country “are in line with these economic projects, and by extension, with Russian objectives.”²⁸

Another avenue of access that European countries provide to Russian influence is the role of big Russian corporations in key European markets. While direct Russian corporate ownership is negligible as a share of the total economies, the **concentration of Russian businesses in a few strategic sectors** – such as energy, telecommunications, metallurgy and banking – makes their indirect impact on the economy much greater. More importantly, however, the largest Russian companies operating in Europe – such as Gazprom, Lukoil, Alpha, Rosatom and Rosneft – exert an enormous influence on the corporate decision-making of national majors through strategic partnerships that involve joint projects, asset swaps, mergers and long-term contracts. Seeing as the Kremlin has much more direct control in Gazprom than any of the European governments in their respective majors, it is difficult, in these joint-ventures, to distinguish economic decisions from the politically-driven ones. Similarly, European economic entities are not looking for such political influence and lack the internal mechanisms for tracing it, let alone for counterbalancing it. In building a strategic relationship with a Russian major, the European companies’ motives lie mainly in advancing their business interests.

Some European companies, such as Germany’s Siemens, risked legal scrutiny by the United States and the European Union after it was discovered that

²⁸ Conley, H., Ruy, D., Stefanov, R. and Vladimirov, M., *The Kremlin Playbook 2: The Enablers*, p. 20.

it had circumvented Russian sanctions in order to supply a Russian energy contractor working in Crimea with gas turbines. Austria's OMV, Italy's ENI, Germany's BASF/Wintershall and the UK/Dutch major Shell have heavily invested in two of the most important Russian gas pipeline projects in Europe, Nord Stream II and TurkStream. Moreover, Shell has striven to remain one of the few foreign oil majors still producing gas in Russia. These all are examples of close coordination of corporate policies in the oil and natural gas sector.

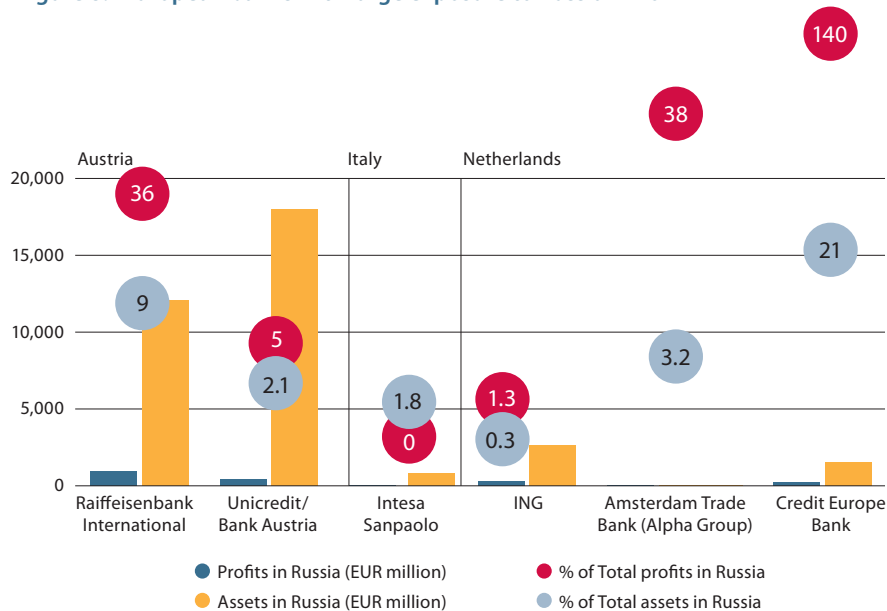
The domination of the Russian economy by the production and export of low-added-value raw materials has made it a big market for European manufacturing goods, new technology and sophisticated financial and insurance services. This **corporate exposure has been a source of economic vulnerability** for countries such as Austria, the Czech Republic, Germany, the Netherlands and Italy, whose biggest companies have been directly affected by the deteriorating EU-Russia relations and economic sanctions.

Alongside the growth of their Russian businesses over the past decade, European companies have become increasingly vulnerable to deteriorating EU-Russia relations. Not surprisingly, many companies in Europe have lobbied heavily for their governments to lift EU sanctions and improve ties with Russia. This happens despite billions of losses in deals with Russian counterparts due to expropriations, the exercising of selective justice and selective protection of property rights, as well as consecutive contractual breaches.

This is illustrated in Royal Dutch Shell's joining of a consortium in 2006 that invested in the Sakhalin-II oil and gas development project. At the time, it hardly anticipated that a dozen years later the consortium would be forced through legal and political pressure to cede control of the project to Russia's Gazprom. Italian companies are also deeply integrated into European supply chains that export to Russia – these include gas importers and retailers such as the oil and gas giant ENI, the electricity generator ENEL (which also operates four plants in Russia), the gas transmission company SNAM, manufacturing giants such as Pirelli, the kitchen appliances firm Whirlpool, the aerospace technology provider Leonardo and the oil and gas services firm Nuovo Pignone; as well as a number of construction contractors, food and beverage exporters and logistics groups. The diversity of Italian companies that have close partnerships with their Russian state-owned counterparts – such as Rosneft, Gazprom and Novatek – explains the heavy lobbying efforts on the part of the Italian industry to lift EU sanctions.

In addition to the energy sector, the **service industry in Europe** depends heavily on Russian business. For example, Austria's two largest banks have concentrated their international expansion in Russian and the CIS region. Italy's largest bank is Russia's biggest foreign-owned lender, and Dutch banks are handling vast amounts of Russian deposits and business transactions. The biggest insurance companies from Austria and Italy also have large operations in Russia and are involved in major deals between domestic and Russian companies.

Figure 8. European banks with large exposure to Russia in 2017*



* The share (%) of total profit in Russia is calculated as the profit/loss of the bank's Russian operation divided by the consolidated profit/loss from the respective bank's annual report.

Source: CSD calculations based on the financial reports of selected banks in the Netherlands, Italy and Austria.

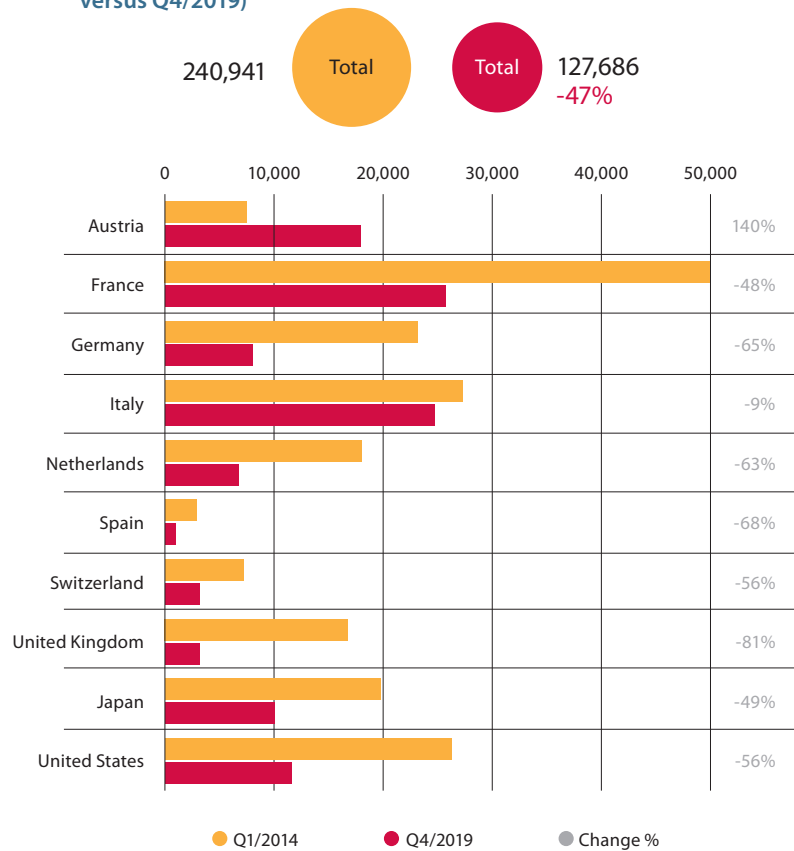
Box 2. The case of Austria

The growth of Russian FDI stocks in Austria over the last decade – from 1% of GDP in 2007 to slightly below 6% in 2016 – has made Russia the second largest investor in the latter year. One explanation for the rise in Russian investments lies in the energy sector. Gazprom's asset swaps, conducted with the Austrian oil and gas company OMV, have been a means to increase the company's capital in the country. OMV was keen to receive new investment in its domestic gas distribution infrastructure, despite the blocking of most of the associated deals by the EU Commission. A more likely explanation for the increase in Russian FDI stocks lies in the services and banking sectors. The three biggest Russian state-owned banks – Sberbank-Europe, VTB-Bank, and Gazprombank (Centrex) – have subsidiaries in Vienna and manage much of their European businesses from the Austrian capital. In 2014, Austria only agreed to the imposition of EU sanctions against Russian state-owned enterprises on the condition that the Viennese branches of Sberbank and VTB-Bank be exempted.²⁹ The influx of Russian FDI to Austria after 2014 has by and large been the result of EU-wide investment flows being channeled through Russian bank branches in Austria in an attempt to circumvent sanctions.

There are other reasons why Russian companies prefer to invest in Austria. Like Switzerland, Austria has a very high threshold for banking secrecy, which it reluctantly agreed to lower after 9/11 and only under strong US and EU pressure. While Austria has a high level of taxation, the instrument of "private foundation" (Privatstiftungen) provides a loophole to shield assets both from taxation and from transparency. In addition, the business climate favors the Russian modus operandi: informal connections, relations, and backdoor-deals are the norm, and on many occasions, formal rule of law is bent towards crony-favoritism. As the geopolitical standoff between the West and Russia heats up, neutral Austria is also perceived as a safe haven to park assets in case of an emergency.

²⁹ Widman, M. "Austria Shields Russian Banks from E.U. Sanctions," *Handelsblatt Today*, July 31, 2014.

Figure 9. Bank exposure to Russia in selected countries (USD million – Q1/2014 versus Q4/2019)



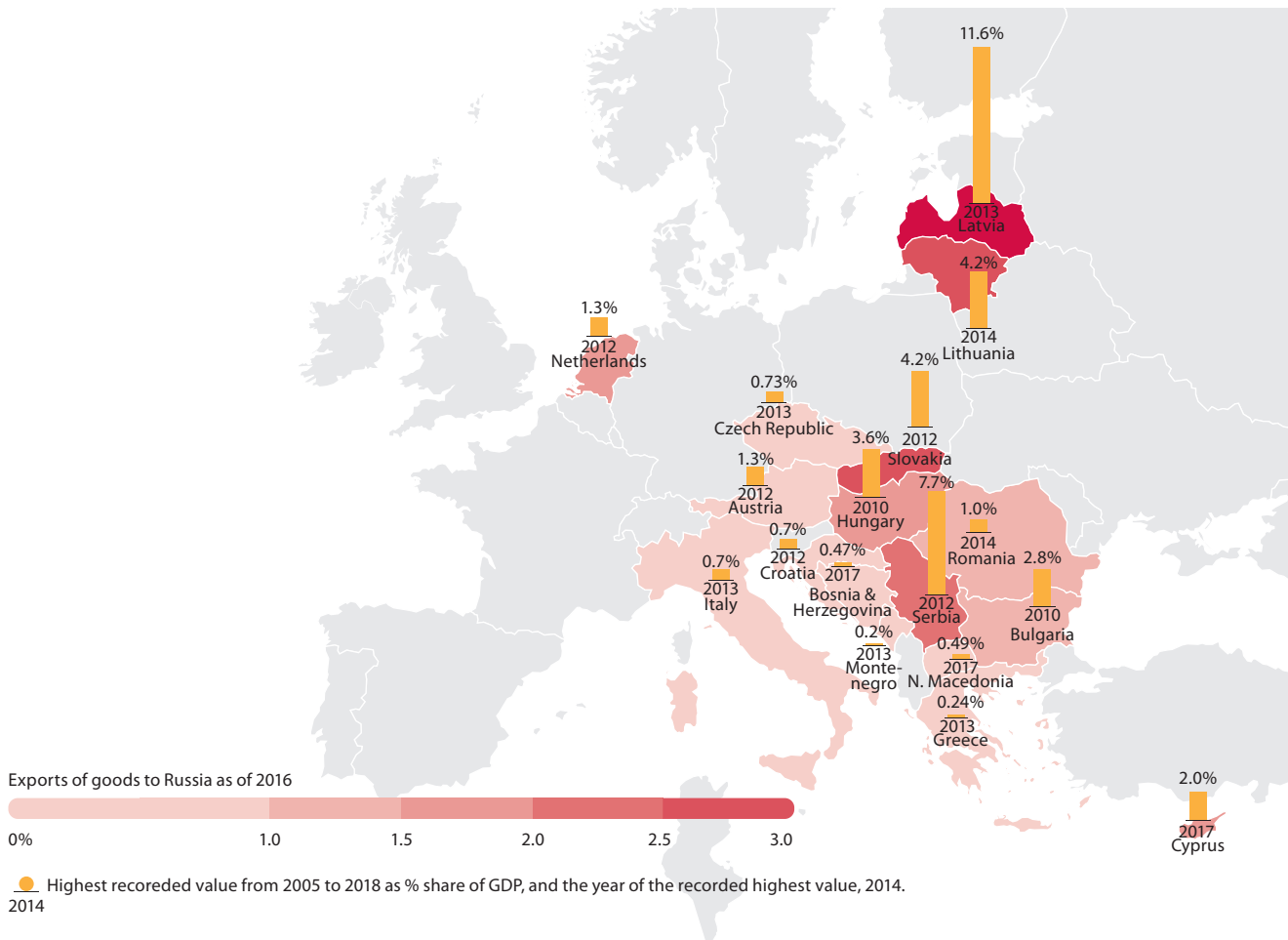
Source: Bank of International Settlements.

In the former Soviet satellites, Russia's economic footprint shows a different direct-indirect ratio. One distinguishing factor is the type of trade dependence. As regards Central and Eastern Europe, two drivers have largely determined the increase of exports to Russia during the past decade. One is the rapid expansion of EU investment in Central European countries following their accession to the European Union. This has led to a structural transformation of these economies towards the manufacturing of higher value-added products, which European companies produce more cheaply there, and then export to Russia. German car manufacturers in Slovakia and Hungary are a case in point. The second driver is the strengthened demand from the Russian economy following the oil price boom of the 2000s.

The lack of a diversified Russian manufacturing quality base has meant the spending of most of the new Russian energy income on European manufactured goods. Russia has thus grown in importance as an export partner for all Central European countries. Some of their biggest firms have become major suppliers in the auto, arms and chemical industries, as well as construction contractors and financial services providers.

Apart from large Western European conglomerates that have set up shop in Central Europe in order to optimize labor and capital costs, home-grown businessmen have also heavily invested in building a business presence in Russia. Due to the size of Central European economies, the impact of this export dependence is felt more strongly in Russia than in Western Europe. Yet it

Figure 10. Exports of goods to Russia as % share of GDP*



* Montenegro dataset starts in 2006, which is the year of the country's independence.

Source: Eurostat International Trade Database (Comext).

is Western Europe's role as a hub for sourcing capital and technology that has made it a key enabler of Russian integration in the European economy.

In Southeast Europe, Russian investments have been growing over the past decade, in some cases substantially. While their share is dwarfed by the total investment coming from the EU, the relative importance of Russia's investments for local economies changes if compared only to the largest European economy, Germany, than to the EU as a whole. It thus becomes evident that Russia's investment presence is comparable to that of the largest EU countries, in particular Bulgaria, Serbia, Bosnia and Herzegovina, and Montenegro. Furthermore, actual Russian investments in the region would be much higher when accounting for all flows ultimately controlled by Russian entities. These include investments channeled through offshore zones such as Cyprus or the use of intermediate investment countries like the Netherlands, Luxembourg, and Austria. The latter countries are amongst the largest foreign investors in Serbia and Bulgaria, for example, and some investments channeled through them are ultimately Russian.

The penetration of Russian corporations has reached the core of the economies of countries such as Croatia, Bosnia and Herzegovina, Montenegro,

Serbia and Bulgaria. In contrast, Russian companies have very little-known presence in Albania, Kosovo and North Macedonia. One possible explanation may be the entry of Russian investments under the cloak of shell companies. In Albania, for example, there is a vast presence of shell companies with anonymous owners. Similarly, some of the largest investments in North Macedonia are made through offshore companies.

Fueling Europe's energy insecurity

Energy has been the most visible and well-studied channel for Russian economic influence in Europe, not least because Russia remains the largest oil and gas supplier to the EU. In 2019, around 39% of all natural gas imports in the EU were from Gazprom, making up around a third of EU's gas consumption.³⁰ While the EU's most energy-dependent member states (those with more than 75% of oil and gas consumption covered by imports from Russia) are in Central and Eastern Europe (Bulgaria, Slovakia, Estonia, Czech Republic, Poland, Latvia, Hungary and Slovenia), the bulk of Russian energy sales go to Western Europe, with Germany, Italy and the Netherlands being the biggest buyers of Russian gas. Given that only a fraction of gas demand comes from the former group of countries, it is a matter of political will to protect these countries through targeted action at the EU level. The EU's anti-trust case against Gazprom, which closed in 2018, was a promising, yet small and inconclusive step. It has taken two years and additional threats of sanctions, for some of the more dependent countries like Bulgaria to claim their benefits from the anti-trust case.³¹ At the same time, the EU has slowly but surely allowed Gazprom to increase its energy footprint in the continent through the continued construction of Nord Stream II and TurkStream.

EU-based companies have expanded their presence in Russia's oil and gas production sector since 2006, during which time Russian companies have been directly marketing their energy products to European consumers. Energy companies in Europe have maintained their ties with Russia even after the 2009 gas supply crisis and the 2014 conflict in Ukraine. Instead of looking for alternative suppliers from the global market – including LNG, whose availability increased after the United States became gas self-sufficient – European companies chose to strengthen their relationship with Gazprom. In the new post-2016 buyer's market, they demanded the renegotiation of their purchase contracts by replacing the oil-indexation in their pricing formula with a spot-based one. Spot-based trading now makes up more than 92% of all deals in Western Europe.³² German companies RWE, EON and Uniper received significant price cuts from Gazprom after arbitration. In light of all this, Gazprom has accepted lower prices and more flexible supply terms in exchange for a bigger market share – a strategy that has been paying off handsomely in the past four years.

³⁰ Eurostat database.

³¹ Georgi Gotev, "Bulgaria Mulls Re-Opening Gazprom Antitrust Probe," *Euractiv*, February 3, 2020.

³² Unlike Central Europe where still around 50% of all supply agreements are oil-indexed, while in Southeast Europe the share is marginal at around 5%.

Box 3. Why gas

There are several trends that explain the continuing surge in Russian gas exports to Europe. One is the likelihood of European gas demand picking up after the end of the Covid-19 pandemic, with natural gas becoming a means to meet the continent's energy transition ambitions. Another is the rapid fall in gas production in some of the biggest European gas fields, including the Groningen formation in the Netherlands. The EU strategy toward the full decarbonization of energy supply has diminished the attractiveness of coal for power generation. As CO₂ emission quotas have become more expensive, coal prices have skyrocketed, leading to their widespread replacement by gas. The increased integration of renewables in power generation has thus stimulated the return of natural gas-fired plants. These plants can provide better market balance between peak demand periods and periods when renewables are not generating electricity. At the same time, natural gas emits three times less CO₂ than coal – this makes it an ideal bridge fuel toward the energy transition to a low-carbon economy.

Europe's increasing gas dependence on Russia has not bothered its governments despite the overarching commitment of EU energy policy to supply diversification and reliability. In fact, the EU has dismissed the pressing need to mitigate some of the main energy security risks faced by member states. Europe has almost completely ignored the twin threat resulting from excessive dependence – on fossil fuel imports from Russia, and on the supply of minerals and rare earths to develop the low-carbon industry from politically unstable and authoritarian states like China.

Having extended purchase commitments, Gazprom's big European clients are working consistently on expanding cooperation through means such as asset swaps and joint infrastructure projects. Germany, which has made the strategic choice to close most of its nuclear power plants by 2023, seems to have been most committed to the expansion of the strategic gas relationship with Russia. This is so despite EU sanctions against Russia for its involvement in the Ukrainian conflict and the vocal opposition from Eastern and Southern European countries that have long been victims of Russia's use of natural gas as a political weapon.

Russia has taken advantage of three **key enabling mechanisms to sustain its dominant market position in European energy supply**:

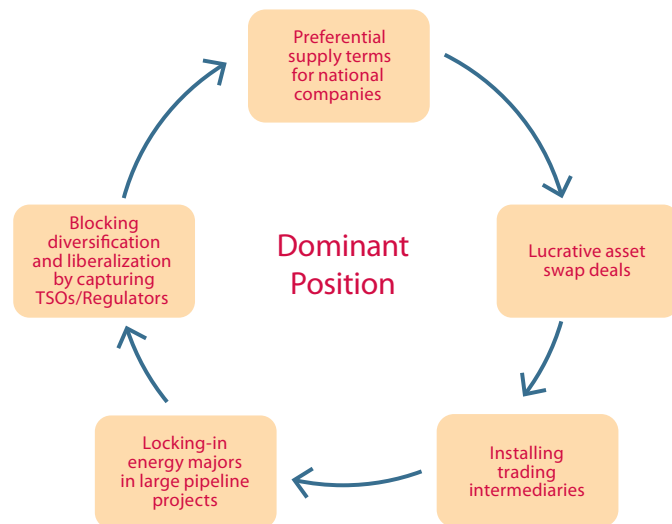
- the expansion of corporate ties with European majors;
- the locking of countries into new infrastructure projects to supply more Russian gas to Europe;
- the renegotiation of pricing and supply terms to preempt any competition from new LNG suppliers.

There exists a wide body of evidence that Russia continues to use Gazprom to punish or reward countries depending on their foreign policy stance on Russian commercial and political interests.³³ Moreover, Southeast Europe's dependence on Russia for natural gas supply has been cemented by long-term gas supply contracts (LTCs) with the dominant supplier Gazprom, containing

³³ See for example Vagin, K. V. (2012). "Russian Energy Policy vis-à-vis Europe: Natural Resources as a Means of Foreign Policy", Thesis. Monterey: Naval Postgraduate School.

highly inflexible strict take-or-pay clauses³⁴ and oil indexation. Although the countries in the region have been gradually changing their contractual arrangements with Russia through means such as the insertion of spot-based pricing terms, the wholesale market players in the region have been overpaying Gazprom by between 15% and 25% compared to average Gazprom prices in Western Europe.³⁵

Figure 11. The effects of Gazprom's leveraging strategy



Source: CSD.

Especially in Southeast Europe, Gazprom's additional profits are reinvested in bolstering the dominance of its intermediaries in the local markets through the expansion of domestic gas distribution networks (as in Bulgaria) or the financing of cultural, media and sports projects. At the same time, the intermediaries put the national gas incumbent at a disadvantage, forcing it to buy at a premium. Covering such premiums often leads to the accumulation of losses, particularly when prices are high globally, when national energy regulators try to safeguard social stability by mandating lower price hikes. The accumulation of gas debts directly to Gazprom or indirectly to its intermediaries may be used as a pretext by the Russian company to leverage supply flows or debt reduction for political purposes.

By implanting politically privileged economic actors in the energy sectors of these countries, Russia has been able to exert much larger impact on the political scene than its corporate or investment presence suggests. Ultimately, Russia has been successful in significantly delaying or preventing the full liberalization of the gas market, as well as key interconnection projects, thus impeding import diversification in some parts of Europe.

³⁴ The take-or-pay clause refers to the existence of a minimum volume to be supplied under a long-term agreement, which has to be paid by the customer even if the latter's consumption is below these minimum quantities.

³⁵ Based on the analysis of customs data on volumes and costs.

* * *

What Russia lacks of the set of geo-economic tools – financial or monetary policy, development aid or economic sanctions – enjoyed by its rival powers, it compensates with a higher conversion ratio of its business into political leverage. The “judo” effect of its economic presence in Europe has been achieved by exploiting the failures of economic governance, the connivance of financial regulators who overlook the influx of dirty Russian money, the inability to implement a common European policy on energy diversification and liberalization, and corrupt decision-makers in the government willing to allow the Kremlin access to strategic national economic assets.

CAPTURE-PROOFING EUROPE

The *Kremlin Playbooks* have drawn up a comprehensive catalogue of the methods used by Russia to pursue its objectives by means of exploiting the vulnerabilities in Europe. The *Playbooks* have also put forth a corresponding **policy agenda for closing these permissive gaps in public governance**. Some policies – such as stricter anti-money laundering regulations, more capable AML enforcers and radically increased transparency of companies' beneficial ownership – are relevant across the continent. Others – preventing the concentration of media ownership, public oversight of the privatization of strategic assets and stamping out political corruption – are particularly lacking in Central and Eastern Europe.

Despite the growing knowledge of the nature and extent of Russian influence, the **long-term political risk** it bears is still underappreciated. The lack of consolidation of measures against the Kremlin's influence into a coherent policy would risk their appropriation by national, partisan or corporate interests. A fractured response to its plans in Europe is exactly what the Kremlin wants.

The failure to acknowledge the potentially corrosive effect of the Kremlin's operations on European public governance and economic integrity borders on willful blindness. **Unless tackled head-on, the transformation of political corruption into state capture** would be extremely difficult to reverse. The greater the consequent rift between democratic rhetoric and action against political corruption, the greater the public disillusionment, further incentivizing the Kremlin to deepen the fissures between and within countries.

The opportunities for the Kremlin to entrench its footprint in the European economy and politics can only be expected to proliferate post-Covid 19: an environment of political, economic and social instability is ideal for its plans to enhance its geopolitical leverage. Even in a post-pandemic Europe, the power grab by some CEE governments during the pandemic will be hard to reverse. Disinformation will find ever more eager audiences in societies that have seen the erosion of trust between the public and the government. Starved financial markets will have even less patience with regulators seeking to vet investors.

It is exactly at this moment of reshuffling of the geopolitical cards that Europe and the United States need to reemphasize **three key components of transatlantic security**:

- the integrity of public governance;
- the freedom and transparency of media, and
- the protection of economies from foreign business capture.

A prerequisite for moving forward in this respect is an awareness of the shared political cost among all European countries of allowing further inte-

Capture-proofing a continent

gration of the Kremlin's proxies. The awareness would arise from a detailed knowledge of the means and amplifiers of Russian influence.

Political corruption – especially when foreign-assisted, as it is in Europe – **cannot be compartmentalized along national borders**. As Russia's experience in the past two decades shows, it inevitably leads to circumscribed media freedoms, a lack of judicial independence, the persecution of the political opposition and, ultimately, to foreign aggression. It should thus be obvious to European politicians that to confront governments which have veered into authoritarianism is not optional particularly when the culprit is the Kremlin.

The European Union has set high rule of law standards for countries wishing to join the club; it is also experimenting with the exercising of punitive actions to counter the erosion of democratic checks and balances in member countries. The EU should also expand its efforts in this direction toward a state capture-proofing policy which would institutionalize the enforcement of democratic governance standards. This effort would require an evidence-gathering mechanism which verifies the existence of capture practices in given economic sectors and regulatory/enforcement institutions.

Such a mechanism is provided by CSD's *State Capture Assessment Diagnostics* (SCAD). Its application to selected countries in Europe has revealed different sources of risk and levels of governance vulnerabilities.³⁶ An essential application of SCAD would be to track the correspondence between a country's level of capture risks and its susceptibility to Russian influence. For instance, assessments have shown that, counterintuitively, the Czech Republic scores lower than Italy and Spain on state capture vulnerabilities. Czech institutions have been more robust in ensuring market competition and in preventing the large-scale penetration of Russian economic footprint.

Regular Europe-wide use of such diagnostics would need to involve a broad coalition of civic actors (in fact, such an alliance would match the use of non-state actors by the Kremlin in its efforts to capture governmental decision-making in Europe). For this to happen, anticorruption must be revived as an EU priority, following the scrapping of EU's anticorruption report in 2017. Among anticorruption priorities, in turn, should be the in-depth review of potential state capture red flags related to large-scale mergers and acquisitions in regulated industries such as energy, banking, telecommunications and health care. In addition, public procurement contracts and large infrastructure projects are areas of concern, having become an easy prey to authoritarian states such as Russia and China. In this respect, the substantial increase of the post-Covid European budget transfers towards member states with different rule of law standards might prop up predatory elites, including some with close ties to Russia, and augment state capture. Mitigating these risks calls for a robust rule of law monitoring mechanism, which European leaders have so far failed to inaugurate.

³⁶ Stoyanov, A., Gerganov, A. and Yalamov, T., (2019). *State Capture Assessment Diagnostics*.

Protecting the medium and the message

Although much has been said and written about the ill effects of Russian disinformation and propaganda in Europe (already a thriving cottage industry), the media landscape in Europe is still not sufficiently protected from capture by foreign authoritarian powers, both in terms of the ownership of media companies and of their information agenda. The two main vulnerabilities that need addressing – as a matter of a transatlantic partnership – are therefore the impact of social media on public discourse and the capture of traditional media in Central and Eastern Europe.

In the realm of **social media**, Russian manipulation is made possible by its structural features, such as a business model that thrives on fake news, disinformation and non-critical consumption.³⁷ Preventing the abuse of social media for political ends, including by foreign powers, requires more than just encouraging the endorsement of codes of practice and establishing oversight boards. An effective defense against social media manipulation can only be achieved by **overcoming the divide on this matter on both sides of the Atlantic** – a divide which only helps the Kremlin. This warrants an urgent policy reckoning in order to preserve freedom of speech standards and reliable public information, while preventing the use of these platforms to stoke division and mistrust.

In **Central and Eastern Europe**, the repression of media freedoms and resulting **media capture** – Hungary, Bulgaria and Serbia being the worst affected – have been exacerbated by the range of means of Russian influence such as shadow editorial control, and the diffusion of the Kremlin's agenda, financial and logistical support to Moscow-friendly outlets. Cash-strapped media outlets have also been lured by the free content produced and disseminated by state-owned Russian channels. The most effective capture tool, however, has been the acquisition of traditional media conglomerates by oligarchs with ties to Russia. To counter this, attempts to acquire media assets need to be routinely reviewed *ex ante* to identify any potential security implications.³⁸

Enhanced economic security

Given that Russian investments can always be subjugated to the political influence of the Kremlin, their security evaluation needs to be prioritized. Western investments in economies most vulnerable to Russian predatory practices should combine commercial objectives with the need to engage and enable these countries to resist state capture.

In terms of reducing Russian leverage, the **enhancement of energy security should be a priority for Europe**. The concentration of oil and gas production – as well as mineral resources used in renewable energy technology – in the hands of authoritarian countries such as Russia and China has significantly increased energy security risks and may undermine the viability of the European energy transition.

³⁷ As US journalist Kara Swisher put it: “The Russians did not hack Facebook. They are customers of Facebook. They are using the platform the way it was built.” As quoted in: Guaglione, S. “[Recode’s Kara Swisher Talks Facebook, Regulation And Fake News](#),” *MediaPost*, June 18, 2019.

³⁸ In February 2020, for example, US Senator Marco Rubio requested a review of the security implications of a planned sale of the Central European Media Group Enterprises to a company with a record of acting as “China’s proxies”; Marco Rubio, (February 26, 2020). [Rubio Requests CFIUS Review of AT&T Sale to Czech Company with Ties to China](#). [Press release].

Europe's dependence on Russian gas is excessively high and – unless addressed through a common policy – may even increase in the future. The combined weight of bilateral supply agreements between European states and Russia add up to a level of vulnerability which an increasingly assertive Kremlin is likely to exploit. Russia's leveraging of this vulnerability in Central and Eastern Europe has been especially effective. This surfaces several regional imperatives, namely a wider and stricter adoption of EU's energy and competition law, as well as the pursuit of energy market integration and an aggressive supply diversification agenda, including via more robust LNG deliveries. In cooperation with the US, the European Commission must enforce competition rules on new trans-border gas infrastructure so as to prevent Gazprom's infamous "pincer" strategy. Allowing Russia to complete and operate the TurkStream and Nord Stream II pipelines will bypass Ukraine, reinforce Gazprom's dominant position in the European market and undermine the viability of diversification projects.

European policies seeking to counter Russian influence should take into account the enabling of the Kremlin's subversive operations by its access to two Western resources – financial markets and technology. A stricter supervision of the penetration of Russian capital would allow Europe to curtail the potentially harmful effects of the Russian economic footprint that may be used to further fracture the European political space. The EU thus needs a **Europe-wide system for reviewing the security implications – for individual nations as well as the Union as a whole – of investments by third parties in European companies or operations**. This is particularly relevant to the financial hubs in Western European countries – in particular the Netherlands, Liechtenstein, Luxembourg, the United Kingdom, and Cyprus, which regularly receive corrupt Russian capital. The priorities for the anti-money laundering infrastructure in Europe are stricter requirements regarding beneficial ownership disclosure and the provision of financial intelligence bodies with more authority. In fact, anti-money laundering should be elevated as a key security concern both for the EU and NATO through the formation of a capable central body.

Given the rising ambitions of authoritarian powers, a strict probing of acquisition attempts – of critical infrastructure and other strategic assets in defense, media, telecommunications, public health, etc. – is of paramount importance. This warrants a much broader conception of security to be defined in the face of hybrid threats emerging from Russia and China.

In the smaller, more susceptible economies of Eastern and Southern Europe, Russia's state corporatism and the weaponization of its trade need to be tackled by a **policy of strategic investment** by the United States and stronger West European economies. In the economies with widespread governance deficits, systemic corruption and consequently heightened risk of capture by illicit capital, US and European investment flows should seek to introduce fair market practices. Economic decision-making across the continent should prioritize security concerns, including radically enhanced financial transparency and the expansion of quality infrastructure investment.

Existing initiatives – such as the Blue Dot Network, a certification mechanism for infrastructure development projects, and the Three Seas Initiative, a joint effort to build North-South infrastructure in Central and Eastern Eu-

rope – would reduce European dependence on Russian energy and stimulate entrepreneurship throughout the continent. Transatlantic cooperation on such initiatives would both boost post-pandemic recovery and fortify Europe’s economy against detrimental foreign influence.

* * *

A strategic approach to a problem requires the foresight to anticipate a chain of consequences. Politically, this means planning beyond the next electoral cycle; in business, beyond the quarterly earnings report. Few countries in Europe are capable of such foresight at the national level. If a “European level” response is to exceed that of the EU, it would serve as a platform allowing individual European nations to project hard power at least in its neighborhood and to withstand the pressures of both Russia and China.

THE FRAYING OF EU'S OUTER RIM

While Russia's revanchist ambitions have the whole of Europe in its view, the methods used by the Kremlin are varied and tailored to the vulnerabilities of the different countries. Given the multiplicity of these methods, a comprehensive mapping and analysis are needed to inform policies that seek to mitigate Russian influence. This is what previous *Kremlin Playbook* reports have achieved through a detailed examination of Russia's attempts to capture political and economic decision-making in sixteen European countries. Their findings have shown that the regime in Moscow seeks to achieve region-specific objectives, such as the exploitation of shared ethnic and religious affinities or through binding regional energy infrastructure projects.

This section examines two countries – Greece and Cyprus – which have experienced the brunt of the Kremlin's influence operations. In their case, analyzing the means used by the Kremlin further illuminates its strategy. Both constitute suitable targets, given their shared religion and historic cooperation with Russia, as well as their strategic location in Southeast Europe and the Eastern Mediterranean. In both countries, as in other Southeast European states, Russia has managed to profit from various deficiencies in the governance of national regulatory institutions by acquiring strategic assets.

Russia is a medium-sized trading partner for **Greece**. Russia's corporate footprint in the country is exercised primarily in two ways. First, through Russians owning major Greek companies. Second, through Greek companies heavily dependent on their business ties with Russia, in areas such as infrastructure, airlines, energy, real estate, media, sports, etc. Among these, Greece's energy sector is by far the most vulnerable to Russian economic influence. Liberalization reforms in strategic sectors of the Greek economy have somewhat curtailed Russia's ability to transform its economic footprint into political leverage. But state capture practices and mismanagement of state monopolies have still allowed Russian companies to gain a foothold in key areas.

In terms of soft power, Russian influence in Greece also benefits from shared cultural and religious roots. These have contributed to the general positive image of Russia in Greece. Yet, Greece's strong western alliance and European orientation prevents its exploitation by Russian interests. The result is that the Greek-Russian relations over the last two decades have been characterized by sporadic deepening while remaining insubstantial.

In the case of **Cyprus**, the analysis of investment and financial flows related to the Russian economic influence in Europe reveals that many corporate ownership network chains developed by Russian companies have either started, passed through or ended up in the Mediterranean island. Cyprus has thus turned into an intermediary hub for Russian funds to enter the Eurozone by the back door. In Cyprus, Russia is by far the biggest foreign economic player with significant presence in strategic sectors of

the local economy. The banking and corporate services are most vulnerable to Russian capture, and the Cypriot financial system has facilitated money laundering and tax avoidance activities by Russian companies and individuals.

Discrepancies in the data published by the Russian central bank and those of Greece and Cyprus (in the case of Greece almost by orders of magnitude) are particularly revealing of the expansion strategy of Russian capital. As discussed above, a widely used method in that strategy is to obscure the origins of the money by rerouting it through various jurisdictions with permissive rules on ownership secrecy. In addition to being an implicit acknowledgment of the growing ill repute of Russian capital, this also indicates that it is used for ends beyond economic productivity and profit.

In the case of Greece, Russian money may appear as originating from Cyprus, Luxembourg, Austria, or the Netherlands. In comparison, Cyprus is a favorite nexus in the placement-layering-integration chain by way of which Russian money ends up in the European financial system.

GREECE: NOT YOUR ORTHODOX BROTHER

KEY FINDINGS

In order to understand the means by which the Kremlin pursues its foreign policy ambitions, it is important to determine the shape and depth of Russia's footprint in the Greek economy. In Greece, as in many countries in Central, Eastern and Southern Europe, this footprint has been transformed into an opaque network of patronage used to influence decision-making in support of Russian interests. Specifically, Russia exploits governance deficits in regulatory institutions in order to acquire strategic assets and companies. These acquisitions in turn provide a strategic advantage in squeezing the competition out of a particular market. The results are monopoly profits that further entrench the same oligarchic networks.

Regarding Russia's influence in Greece, the application of the *Kremlin Playbook* methodology of analysis has yielded several key findings:

- Russian corporate footprint is exercised primarily through major Greek companies which are either owned by Russian citizens or are heavily dependent on their business ties with Russia – both in terms of joint projects or trade exposure. These include some of the most influential business entities in Greece, with interests in sea ports and airports, airlines, energy, real estate, media, sports, etc.
- Corporate networks with significant links to political parties, other businesses, and government institutions act as intermediaries that promote Moscow's interests when necessary. This has been possible because most Russian investment is in sectors where natural monopolies are closely tied to government policy.
- Russia is a medium-sized trading partner for Greece, and both countries engage in occasional bilateral economic relations – especially in certain areas like energy and tourism, which have acquired strategic importance. Despite this, potential vulnerabilities remain.
- Data on Russian FDI in Greece by the Greek and Russian central banks diverge significantly. As is the case of many SEE countries, Russian investments could, in fact, have been channeled through third countries including Cyprus, Luxembourg, Austria, and the Netherlands – countries that are consistently among the largest foreign investors in the region.
- The liberalization and reform of strategic sectors of the Greek economy have curtailed Russia's ability to transform its economic footprint into political leverage. However, its widespread state capture practices and mismanagement of state monopolies have allowed Russian companies to gain a foothold in key areas. These may be used in the future to tip political or economic balances in Russia's favor in Greece and the region.
- As in other SEE countries, Greece's energy sector is by far the most vulnerable to Russian economic influence. The percentage of direct Russian imports of the total annual gas demand is around 65% – a rate that fluctuates depending on the price of liquefied natural gas (LNG) supply. This

provides the greatest opportunity for leveraging import dependence for political influence.

- In light of its important geopolitical position and potential as an energy hub incorporating alternative energy routes, Greece has become a prime target of Russian attempts to control or influence the process of diversification and market liberalization by exploiting governance deficits.
- Several attempts, however, by Russian companies or the Kremlin's local proxies at acquiring stakes in critical infrastructure have fallen through – despite these Russian efforts, Greece did not breach the framework of EU policy and regulations.

An in-depth analysis of Russian influence in Greece should take into account not only the policy objectives of the official political actors, but also the aspirations of the individuals who have become intermediaries on the ground. Although shared cultural and religious roots have contributed to the general positive image of Russia in Greece, these roots cannot decisively anchor relations between the two states. On the contrary, Greece's strong western alliance and European orientation prevents its exploitation as a Russian pawn. Moreover, Greece's close economic relationship with the EU have also circumscribed the flourishing of Greek-Russian economic relations to certain areas of mutual interest. The result is that the Greek-Russian relations over the last two decades have been characterized by sporadic deepening while remaining insubstantial. In the last decade, Russian entrepreneurs have attempted to reformulate the Greek-Russia economic relationship by emphasizing their Greek roots. This narrative has proved to be an effective method of penetration – it has provided a platform for Russia's economic and political interests, while soliciting the sympathy of the public.

THE BACKGROUND

Greek-Russian relations date back to the time of independence – the first Prime Minister of independent Greece, Count Kapodistrias, was foreign minister of the Russian Empire before assuming responsibility for the new state. Later, following the collapse of the Soviet Union, Greece and Russia gradually built up their relationship by signing several cooperation and partnership agreements during the 1990s. A major aim of the Greek governments during this period was to develop deterrence capacity against Turkey.³⁹

In the late 1990s, Greek-Russian relations warmed during the NATO strikes against the Serbian forces in Bosnia and Herzegovina,⁴⁰ as well as after the Kosovo War where Greek public opinion sided with the Orthodox Serbs.

Greek-Russian relations developed further in 2004, when Kostas Karamanlis took over as Prime Minister. He sought to play the role of a mediator between the West and Russia – this would strengthen his country's geopolitical position as well as yield economic benefits. Karamanlis sympathized with Moscow's worldview that Russia was humiliated by the West during the 1990s, while continuing to play a fundamental role in counterterrorism efforts⁴¹ in addition to being a guarantor of global stability. This pro-Russian turn of the Karamanlis government added to his popularity as strong anti-Western feeling remained in Greece after the NATO interventions in former Yugoslavia. This special relationship led to an upgrade of trade relations, accelerated their plans for cooperation in natural gas and oil transportation, and increased tourist flows. However, this convergence was stalled by internal contestation, including from the Prime Minister's own party. Despite Prime Minister Karamanlis' push, the country reestablished a unilaterally pro-Western doctrine that has been a mainstay of Greek foreign policy since the Second World War, until the arrival of the Coalition of the Radical Left (SYRIZA) in 2015.

SYRIZA's term of government was marked by a strengthened commitment to Russian energy interests in the region. Strongly pro-Russian Panagiotis La-

fazanis, who was appointed as the new energy minister, made it clear that the development of energy ties would be the one way to mitigate the economic crisis in 2015. The Greek government consequently signed an agreement to join the new TurkStream pipeline project,⁴² which replaced South Stream as the main conduit for the entry of Russian gas into SEE.

In considering the Kremlin's influence, it is important to note the dominant Greek positive sentiment towards Russia, which buffers Moscow's potential to exert influence. Besides historical reasons, Russian popularity has reflected widespread resentment against the West, which was blamed for imposing austerity on a nation whose economy had shrunk by a third and whose economic sovereignty had been compromised by the financial crisis.

The 2010s have seen increased Russian investment in strategic sectors in Greece, which has allowed for greater influence over government decision-making. However, the government's renegotiation of the bailout program managed by the *troika* (the European Commission, the European Central Bank and the International Monetary Fund), changed the dynamics of the prevailing economic relationship with Russia. Following snap elections in 2015, a coalition government committed to a much higher level of compliance with the EU-mandated requirements over its tax and financial policy. Meanwhile, commitment to Russian energy projects gradually waned.

Overall, the 1976 dictum of Konstantinos Karamanlis, "Greece belongs to the West", is undisputed. In addition, since it is Turkey that seems to pose the most significant threat in the region, the prospect of a Russian-Turkish rapprochement leaves Athens with a perception of vulnerability and the need to stabilize its strategic partnerships. This political development diminished the potential for Russian influence in the Greek economy. This was a significant, albeit not definitive, change from the previous efforts of successive Greek governments to woo Moscow – even at the cost of North Atlantic and European solidarity.

* * *

This assessment uses the robust analytical framework of the *Kremlin Playbook* reports to assess Russia's economic footprint in Greece. The study measures the

³⁹ Grigoriadis, T. and Iordanidis, V. (2014). *Greek-Russian Relations I: Foreign Policy and Diplomacy*. Athens: ELIAMEP.

⁴⁰ Binder, D., "Greece, Turkey, and NATO", *Duke University Press, Mediterranean Quarterly* 23, no. 2 (2012), pp. 95-106.

⁴¹ Although his policy – dubbed "diplomacy of the pipelines" – enraged Greece's Western allies and the right wing of his party.

⁴² Michalopoulos, S., "Tsipras: 'TurkStream' will have another name on Greek territory". *Euractive Greece*. April 9, 2015.

magnitude and the different modalities of Russian economic influence in Greece. It highlights the vulnerable sectors that have been targeted by Russian companies and their local intermediaries. In estimating the Russian economic footprint, the report provides rigorous analysis of trade, investment and corporate presence data, which it then cross-references with a detailed account of the different channels of influence. The assessment shows how both state-owned and private Russian companies have been able to exploit widespread governance deficits in key regulatory institutions to ensure preferential treatment and market status.

TRADE AND INVESTMENT

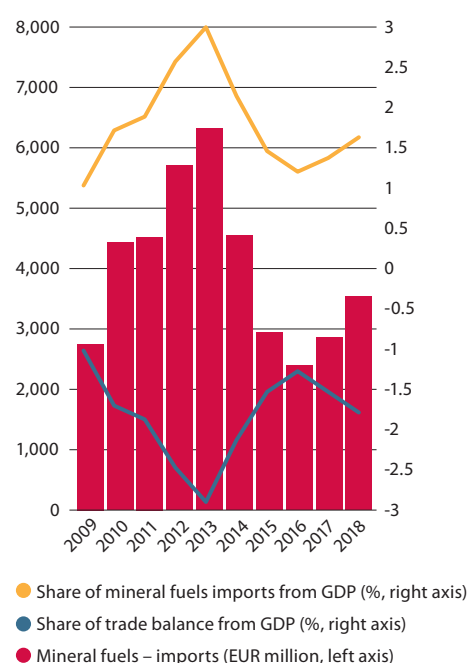
Greece is the most developed country in Southeast Europe, despite the adverse effects of the financial crisis on the country. Its GDP is bigger than that of Albania, Bulgaria, Croatia, Montenegro, North Macedonia and Serbia combined. Greece's nominal GDP is second only to Romania's but its per capita GDP is 70% larger as it has a much smaller population. It is thus logical to assume that Russian economic presence in Greece should at least be proportional to their GDP if the Kremlin is to have a similar potential to influence the economy. However, Russian FDI in Greece is at least two times smaller than that in Bulgaria, Montenegro and Serbia, which have been identified as the three most vulnerable countries to Russian influence in the region.⁴³ The comparison between Russian trade with a number of Balkan countries and Russian trade with Greece reveals a similar picture, but – as demonstrated below – it affects sectors crucial to the Greek economy.

Trade dependence

Greece has been a medium-sized trading partner for Russia and bilateral economic relations between the two countries have not reached a strategically high level. Nevertheless, potential vulnerabilities remain, mostly related to energy imports and the export of tourist services. In both sectors, Russia is a sizable client. Goods imports from Russia have made up on average 7.3% of total Greek imports since 2004. Taking this into account, Russia is the Greece's fourth largest

import partner after Germany, Italy and China. The level of imports from Russia peaked in 2013 at 13.5% of total Greek imports or the equivalent of EUR 6.3 billion. The spike was closely related to the rapid increase in international oil and gas prices – which also reveals some level of vulnerability of the Greek economy in energy sector. In fact, more than 80% of all Russian imports in Greece are mineral fuels. Greece's energy imports have caused a persistent trade deficit with Russia, at around 2% of GDP for most of the last decade. This predicament mirrors that of most SEE countries, where oil and gas imports constitute significant components of trade. Greek exports to Russia have never surpassed EUR 500 million – in fact they have been falling since 2014, reaching EUR 234 million in 2017 or 0.1% of GDP. But although Greek exports to Russia are not huge, they are concentrated in a number of sectors, agriculture being one of the most sensitive. Around 40% of all Greek exports to Russia consist of agriculture-related products, including food products, vegetables and fur/skins. This explains the 50% fall in Greek exports following the fall in disposable income in Russia. This was augmented by the worsening of relations between the EU and Russia, specifically the imposition of EU agricultural products' import ban in Russia. The curb of agricultural exports to Russia contributed to rising discontent among Greek farmers – an influential and well-organized group of voters that no political party in Greece was ready to alienate.

Figure 12. Mineral fuels trade between Greece and Russia



Source: CSD calculations based on data from Eurostat.

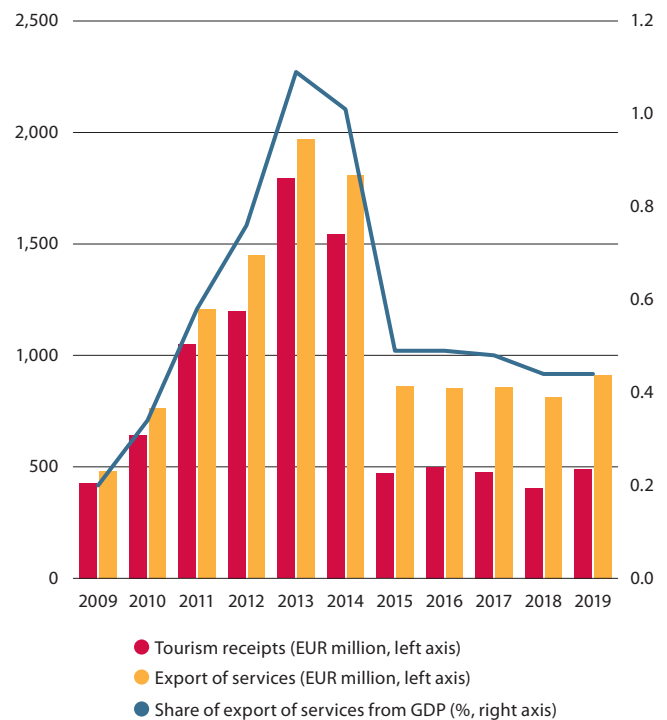
⁴³ CSD (2018). *Russian Economic Footprint in the Western Balkans. Corruption and State Capture Risks*, Sofia: Center for the Study of Democracy.

Moscow was also keen to minimize the potential for anti-Russian feelings in Greece. All these led to a real paradox in bilateral relations, even in the most promising years of their friendship – at sessions held by their joint commission for economic cooperation, both sides were discussing ways to go around the sanctions they had imposed on each other.

Greece is a major exporter of tourist and travel services to Russia, where Russian visitors have played an increasingly important economic role.⁴⁴ This has increased Greek vulnerability to potential exploitation by the Kremlin. Between 2009 – 2013, Greek services exports to Russia quadrupled to around EUR 2 billion before shrinking by 2019.⁴⁵ Respectively inbound travel from Russia from 2005 to 2013 recorded a significant increase (over ten times – from 107,000 visitors in 2005 to 1.35 million in 2013) before falling back to around half a million at the end of 2018. The recent decline has mostly been a result of the Russian economic crisis, the decline in Russian disposable income, the depreciation of the Russian ruble and bigger competition from other tourist destinations in the region – most notably Turkey, Spain and Bulgaria. Tourism receipts from Russia in 2017 reached EUR 478 million. They rose marginally in 2019 to EUR 492 million (see Figure 13).⁴⁶ In addition, the average per capita expenditure of Russian tourists in Greece declined to EUR 654 in 2018, compared to EUR 1,212 in 2005 (or -41.4%). Despite this, it remains 27% higher than the average tourist expenditure recorded throughout the country in 2018 (EUR 514), suggesting that Russian tourists continue to be viewed favorably by tourist businesses in Greece. Regarding average lengths of stay, tourists from Russia stay in Greece 10 days on average (29.6% longer than the country average of 7.7 days). According to the World Tourism Organization (UNWTO), Greece is the 5th most popular destination for Russians.

Tourism aside, within the structure of the bilateral trade ties, energy has been the most visible and well-studied channel to gauge economic influence. Energy trade has been the core culprit for persistent trade deficits and for continued political exertions on the Greek government.

Figure 13. Revenues from Russian tourists in Greece



Source: CSD calculations based on data from the Greek Central Bank and the UNCTAD.

The deficit has been shrinking in light of falling global oil and gas prices since 2014. However, it may start widening again following an expected increase of gas supply. This increase may be made possible by an anticipated expansion of Greece's natural gas consumption so as to replace existing coal-fired power generation.⁴⁷ Indeed, natural gas-fired power plants have generated around a third of the electricity in the country, which is a 10% rise in three years reaching 4.1 bcm/year in 2017.⁴⁸ An increase in gas consumption would mean heightened dependence on Russia, which is the main energy supplier for Greece, and likely to remain so into the foreseeable future. The structure of Greece's natural gas dependence on Russia is discussed in detail in the sections below.

⁴⁴ It is widely believed in the tourist sector – not only in Greece but also in other countries in the region – that Russian tourist operators are regularly advised by Moscow as to the “preferable choice” of tourist destinations for organized groups for summer vacations.

⁴⁵ The latest available data on services trade by country is for the year 2019.

⁴⁶ For more information: Bank of Greece, Receipts by Country of Origin.

⁴⁷ Tugwell, P. “Greece’s Rising Natural Gas Role Has Players Vying for Top Spot”. *Bloomberg*. June 3, 2019.

⁴⁸ Ibid. For more information, DESFA forecast, Development Study 2018 – 2027. June 2017.

Table 1. Ten-year forecast for natural gas demand in Greece

Estimation of natural gas demand (million Nm ³ /year)	Power plant natural gas demand	Other Consumers		Transit of natural gas	Small scale LNG	Total
		Customers connected to high pressure network	Distribution networks			
2016	2,629	386	821	-	-	3,835
2017	2,684	522	905	-	-	4,111
2018	2,218	569	891	10	-	3,689
2019	2,275	570	934	50	1	3,829
2020	2,204	572	990	100	2	3,867
2021	1,921	573	1,039	500	18	4,051
2022	2,229	573	1,085	550	29	4,465
2023	2,454	573	1,122	600	53	4,802
2024	2,422	574	1,163	620	82	4,861
2025	2,326	574	1,193	650	93	4,835
2026	2,294	574	1,225	650	122	4,865
2027	2,340	574	1,255	650	151	4,971

Note: Nm³ is normal cubic meter; LNG is liquefied natural gas.

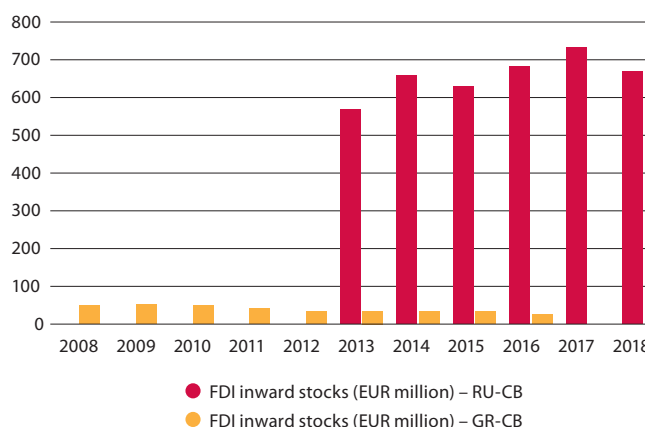
Source: National Natural Gas System Operator of Greece (DESFA).

Investment ties

While Greece's energy trade and dependence on Russian tourists have created macroeconomic channels for Russian influence, investment relations have remained limited. The most important Russian investments in Greece – in terms of size and potential to channel economic influence – have been made by the Savvidis Group (this includes hotels, port infrastructure, sports and tobacco business), Agroiinvest-Mirum, Mouzenidis Travel (one of the largest travel agencies), Prometheus Gaz (a wholesale gas joint venture with Gazprom), Sistema Holding Telecommunications (one of the largest Russian telecommunications companies) and Rosoboronexport Defense (Russian state-owned defense equipment company).

According to the Greek Central Bank, Russian stock of foreign direct investments has remained negligible. It has even declined from around EUR 40 million in 2001 to EUR 25 million in 2019. This represents just 0.1% of the total FDI stock of the country. In contrast, FDI data from the Russian Central Bank reveals a different picture where Russian FDI stocks in Greece reached EUR 733 million by the end of 2017 – this would account for 3% of the total Greek stock of FDI.

Figure 14. Russian inward FDI stocks in Greece



Note: GR = Greece, RU = Russia, CB = Central Bank.

Source: CSD calculations based on data from the Greek and Russian Central Banks.

One explanation for the significant statistical discrepancy in FDI is that the two central banks could be using different methodologies in estimating FDI. Specifically, the Russian Central Bank has a broader definition of foreign investment.⁴⁹ According to its methodology,

⁴⁹ The Central Bank of the Russian Federation, Methodology for measuring foreign direct investment.

FDIs are estimated for all companies with ultimate beneficial ownership in Russia, which could encompass companies with non-Russian residence but with Russian beneficial ownership. For example, a Russian subsidiary in the Netherlands reallocating dividends from its activities in Greece would be considered, by the Russian Central Bank, to be an FDI investment in Greece. In contrast, the Greek Central Bank would not designate such investments as Russian but as coming from the Netherlands. Usually, central banks in the EU estimate foreign direct investments coming only from the intermediate counterpart (a subsidiary of the actual investor), and not the ultimate owner.

As is the case of many SEE countries, Russian investments could have been channeled through third countries including Cyprus, Luxembourg, Austria and the Netherlands – countries that are consistently among the largest foreign investors in the region. In fact, while the Netherlands and Luxembourg make up close to 40% of the total FDI stock in Greece, it was the case that preceding the Cypriot banking crisis in 2012/2013, the Mediterranean island had also represented a tenth of the Greek inward foreign investment. Preferential tax-treaty jurisdictions have been commonly used by Russian entities to avoid taxation and to obfuscate actual corporate ownership in cases of foreign mergers and acquisitions.⁵⁰ There is evidence that Russian funds stand behind the investments from countries with preferential tax-treaty jurisdiction.⁵¹ For example, the Greek-Russian mogul Ivan Savvidis acquired Epsilon TV and the Ethnos and Sunday Nation newspapers in Greece. This was done through the Cypriot company Dimera Media Investments (DMI).⁵²

Greek FDI stock in Russia has remained on average below EUR 100 million with the exception of 2016 when, according to the Russian Central Bank, Greek investments in Russia briefly reached EUR 167 million. There are about 70 Greek companies operating in Russia (mostly in consumer goods and infrastructure) with the most important being the Hellenic Bottling Company-3E (one of Coca Cola's European manufacturing subsidiaries), Frigoglass, Chipita, TOGAS, Plastics of Crete, Prometheas Cement, Copelouzos Group (one of the largest Greek holding companies and a major gas partner of Gazprom), Oxette Jewellery, BSB, Lapin

House, Piraeus Bank and Eurobank (two of Greece's largest banks).⁵³

Some Russian investments have also been channeled into the purchase of real estate in Greece as a way for Russian individuals to benefit from Greece's golden visa scheme. The scheme grants five-year residence permits renewable for third-country (non-EU) nationals who purchase, individually or through a legal entity, property in Greece valued at a minimum of EUR 250,000, or who have taken out a minimum 10-year lease in hotel accommodation or tourism facilities.⁵⁴ Moreover, this Greek investor visa offers unrestricted travel access in the EU. From the launch of the golden visa program until the first quarter of 2019 a total of 4,154 permits were issued.⁵⁵ Chinese investors have been the biggest beneficiaries, as they account for 58% of the issued residence permits, or 2,416, with their share constantly on the rise, while Russian investors take second place with 428 permits issued. The bulk of properties purchased through the program are in Athens which drew 78% of the buyers.⁵⁶

RUSSIAN CORPORATE FOOTPRINT IN GREECE

There are only two visible channels of Russian macroeconomic influence in Greece: energy imports and tourism exports. But to assess Russia's potential economic leverage on Greece, the current report looks also at Russia's presence at the corporate level and company networks that are directly controlled or indirectly critically dependent on Russian business. By using the *Kremlin Playbook* report methodology, the current analysis provides a better understanding of how structural economic vulnerabilities and Russian investment presence in Greece actually help to augment Russian political influence, as well as other important variables at play.⁵⁷ This section of the report provides an over-

⁵⁰ Conley, H., Ruy, D., Stefanov, R., and Vladimirov, M. (2019). *The Kremlin Playbook 2: The Enablers*.

⁵¹ Ibid.

⁵² For more information: [CyprusRegistry](https://cyprusregistry.gov.cy/).

⁵³ For more information: Agora, Offices of Economic and Commercial Affairs.

⁵⁴ The Immigration and Social Integration Code (Law 4251/2014, Government Gazette 1, no 80) contains provisions that facilitate the stay of third-country investors, whose investments are characterized as strategic, via the provision of extended stay time limits for the representatives of investment bodies and their partners. For more information: Law 4251/2014 – Immigration, Social Integration Code and other provisions.

⁵⁵ For more information, [Enterprisegreece.gov.gr](https://enterprisegreece.gov.gr/), Residence permits for property owners/investors (Golden Visa).

⁵⁶ Ibid.

⁵⁷ Conley, H., Ruy, D., Stefanov, R., and Vladimirov, M. (2019). *The Kremlin Playbook 2: The Enablers*.

view on the Russian corporate presence and networks in Greece, by identifying companies with direct as well as indirect links to Russian entities or political structures.⁵⁸ The study analyzes the revenues, assets and employment figures of all Russian-owned or controlled companies in Greece.

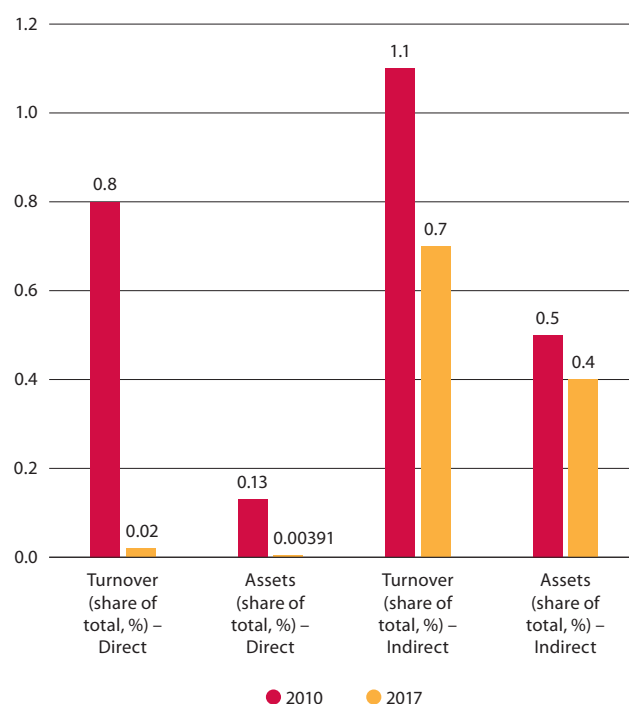
The direct Russian corporate footprint in Greece is small. The available data shows that less than 40 enterprises with Russian ultimate beneficial ownership reside in Greece. Their business activities correlate almost perfectly with Russia's overall investment in Greece and partially reflect trade flows, especially in energy and the export of tourist services. From 2010 to 2017, the share of Russian companies' revenues out of the total revenues in the Greek economy fell from 0.8% to a negligible 0.02%. This reflects the slump in Russian business activities after 2014 as a cumulation of the fall in international oil and gas prices, as well as the Greek economic malaise in the period 2010 – 2017. Similarly, Russian-controlled assets in the Greek economy have shrunk from 0.13% in 2010 to 0.00391% in 2017. This also reflects the lack of major Russian banks operating in Greece, and the fact that Russian companies present do not possess much property, equipment or manufacturing facilities.

Indirectly, there are 32 major Greek companies that are either owned by Russian citizens or are heavily dependent on their business ties with Russia – both in terms of joint projects and trade exposure. Among them are some of the most influential business entities in Greece, including parts of the Copelouzou, Savvidis and Mouzenidis groups. Among the major assets owned by these corporate holdings are shares in the second largest port in Greece (Thessaloniki), one of the countries' airlines (Ellinair), many regional airports, and the strongest soccer club. Russia's total indirect footprint has hovered between around 0.5% and 1% of the Greek economy with a gradual declining trend since 2014. Yet, in the right circumstances, the critical importance of some of these assets, as well as their range of soft power and/or the access they may provide to high-level decision-makers in Greece, could provide substantial leverage to the Kremlin.

⁵⁸ "Direct" control means companies with a clearly identifiable final beneficial owner in Russia. Indirect control means companies, which have between 5% and 100% of the equity controlled by a Russian owner at some point in the ownership chain. While we have detected also companies that are "ideal fronts", i.e. they are completely detached from their final beneficiary owners, legally severing their link with their Russian patron, these have not been included in the present analysis, unless specifically noted. Understanding the mechanisms of such "ideal fronts" is important though to properly perceive the risk of Russian influence in a given country in its entirety.

Importantly, and unlike most of the other SEE countries, Russia has almost no presence in the banking and the financial sector of Greece. Although a very small Russian bank called Kedr opened a branch in the Greek market in 2007, it never had large scale activities. Nonetheless, it was acquired first by Rost Bank and then by B&N Bank, Russia's 12th biggest lender by assets,⁵⁹ with plans to develop a branch network in northern Greece. Ultimately, the bank's plans for expansion fell through, and in May 2018, it closed its Greek branch after being taken over by the Russian central bank in March for recapitalization.

Figure 15. Russian direct and indirect corporate footprint in Greece



Source: CSD calculations based on corporate databases.

Channeling political influence through business links

Although the direct economic footprint of Russian companies in Greece is relatively small, it still provides strong economic levers of influence as it is concentrated in crucial sectors. While Russian corporate presence is not something to be avoided per se, Russian capital has been increasingly used by the

⁵⁹ Standard & Poor's, "Russia-Based B&N Bank's 'B/B' Ratings Affirmed On Acquisition Of Rost Bank; Outlook Remains Developing," December 26, 2014.

Kremlin to carry through its politico-economic interests. The Kremlin has continuously and successfully pushed for the removal of the division between state and business in Russia. This has been done through the indiscriminate deployment of state security and law enforcement against any dissenting business interests. The interrelated factors of the economic crisis in Europe and in Russia, the push for de-offshorization of Russian companies, and the rising assertiveness and control of the Kremlin over Russian businesses at home have paved the way for corporations to be pressured into furthering Russian political interests.⁶⁰ Another means to advance the Kremlin's influence abroad has been the bribery of foreign oligarchic corporate networks – especially those with significant links to political parties, other businesses, and government institutions – to act as intermediaries working in Moscow's interests.⁶¹ This has been possible because most Russian investment is in sectors with natural monopolies (e.g. energy, metallurgy, etc.), where interests are often closely interlinked with government policy.⁶² This is particularly true for some of the newer democracies of Central and Eastern Europe and some of the smaller economies of Western Europe, which have relied on structurally-important national business champions for economic development in the past.

Powerful local economic groups have also actively sought Russian links to secure capital and political backing. This would help them acquire assets and invest in large projects – especially if they lack access to deep capital markets due to reputation or market risks. There is a win-win outcome for both Russian and local private interests – the former finds a way to move their funds out of Russia and the latter acquires financial resources that would not be available otherwise.⁶³ Domestic interests can help Russian partners exploit known governance deficits bordering on state capture – for instance, the ability to influence lawmakers to pass laws sustaining monopolistic market structures, evade tax payments, promote non-transparent public procurement and privatization procedures. In addition, clinching mergers and acquisitions allow for

slush funds to be easily hidden and redirected towards side investments or political activities.⁶⁴ In exchange, Russia can help domestic networks to engage in rent-seeking with national governments.

It is therefore important to uncover and assess the governance risks in these weak areas – specifically, internal economic vulnerabilities where Russian direct or indirect footprint has been the strongest. The combination of economic dependencies and bad governance (culture of corruption and state capture) contributes to a long-term erosion of institutional resilience – the result is a sustained, malign Russian influence in European policy-making.

Big business liaisons – domestic tycoons as points of entry

Copelouzos Group – airports and natural gas supply

The most influential businessman who has been closely linked with Russia's interests in Greece for at least four decades is Dimitris Copelouzos. He has collaborated with Gazprom via Prometheus Gas SA since the fall of the Soviet Union. Prometheus Gas is a joint venture between a Copelouzos Group subsidiary and Gazpromexport (50/50%), which became the key intermediary of the Russian gas supplier in the country. This was despite the fact that until the liberalization of the gas market in 2018, only DEPA – the state-owned wholesale gas supplier – was importing natural gas to Greece. Prometheus Gas is now one of the biggest wholesale suppliers of Russian gas to Greece, with annual sales of around 1 bcm (30% of the total Russian gas sales in Greece) via a long-term contract since 2016. This had become possible after DEPA lost its exclusive right to resell Russian gas to Greece in 2014.⁶⁵ The Copelouzos Group has been behind the development of at least two strategic Russia-led pipelines:

- the Burgas-Alexandroupolis oil pipeline (now shelved) aiming to circumvent the busy Bosphorus Strait for Russian crude oil tankers;

⁶⁰ Conley, H., Ruy, D., Stefanov, R., and Vladimirov, M. (2019). *The Kremlin Playbook 2: The Enablers*.

⁶¹ Shentov, O., Stefanov, R., and Vladimirov, M. (2019). *The Russian Economic Grip on Central and Eastern Europe*.

⁶² Conley, H., Mina, J., Stefanov, R., and Vladimirov, M. (2016). *The Kremlin Playbook: Understanding Russian Influence in Central and Eastern Europe*, p. xiii.

⁶³ Shentov, O., Stefanov, R., and Vladimirov, M. (2019). *The Russian Economic Grip on Central and Eastern Europe*, pp. 29-31.

⁶⁴ Stoyanov, A., Gerganov, A. and Yalamov, T. (2019). *State Capture Assessment Diagnostics*.

⁶⁵ Since December 2018, Gazprom has also begun selling natural gas directly also to the Mytilineos Group, another of the largest Greek conglomerates with significant operations in the metallurgical sector, engineering procurement and construction projects in the industrial sector.

- the Interconnector Turkey-Greece-Italy (ITGI), now Poseidon, which was previously considered as possible southern route of TurkStream.⁶⁶

The Copelouzos Group has also been developing a project for a floating storage regasification unit (FSRU) near the port of Alexandroupolis with the goal of opening a second inlet for LNG imports into Greece.⁶⁷ The project, which is being developed by Gastrade, a subsidiary of the Copelouzos Group, could be transformational for the regional gas market. In combination with the Interconnector Greece-Bulgaria (ICGB), it could potentially provide regional access to the global gas market, which is already becoming competitive against Russian pipeline gas in Europe. The binding market test in May 2020 yielded capacity bookings worth 2.6 bcm/year including 500 million cubic meters per year by the Bulgarian gas supplier, Bulgargaz. The Bulgarian state-owned gas operator, Bulgartransgaz, also signed an agreement in August 2020 to obtain a 20% share in the project. The potential delay in the natural gas supply via the TANAP-TAP pipeline network could make the FSRU a more competitive source of alternative natural gas to the SEE region in the form of LNG deliveries from the global gas market.

The project could help bring about the full diversification of the SEE gas supply away from Russia although it is being implemented by a business group with

strong partnerships with Russian companies and with Gazprom in particular. The Kremlin could use commercial pressure on the group in the future to undermine the SEE region's energy security, a strategy it has been employing successfully all too often in the region.⁶⁸ The Copelouzos Group has been diversifying its portfolio by developing strategic business relationships with Western partners – including U.S. LNG companies such as Cheniere – and joint energy projects with China, while maintaining its role as the key Gazprom intermediary in Greece.

Copelouzos plays a much bigger role in the Greek economy than just as an intermediary for the Russian interests in Greece. The Copelouzos Group is one of the largest holding companies in Greece, whose activities span the production of electricity, the distribution of natural gas, renewable energy technology manufacturing, real estate and infrastructure building. At the same time, Copelouzos is one of the few Greek entrepreneurs who have developed business activities in Russia, especially in the field of infrastructure. He also maintains excellent relations with the Russian state leadership: Copelouzos was one of the first entrepreneurs with whom Vladimir Putin met on his first visit to Athens in 2001.⁶⁹ Since 2006, Copelouzos has also attended all the meetings between Alexey Miller, the CEO of Gazprom, and the Greek government on issues related to energy planning.⁷⁰

Box 4. The physical points of entry – investing in airports

Through its wholly-owned subsidiary, Horizon Air Investments, the Copelouzos Group, together with the foreign investment arm of the Russian state-owned bank VTB, and the German company Fraport AG, formed the consortium Northern Capital Gateway. In June 2009, it won the international tender for the development, reconstruction and operation of the Pulkovo airport in Saint Petersburg, Russia for 30 years.⁷¹ Copelouzos Group participated until recently⁷² owning 7% of the shares.⁷³ The Copelouzos Group has also been collaborating with other Russian companies outside of Gazprom. In June 2017, the Copelouzos Group's subsidiary, Damco Energy, and Russia's state-owned geological holding company Rosgeologiya, signed an agreement to jointly develop a geothermal power plant in northern Greece.⁷⁴

⁶⁶ Confidential Cable from the US Embassy in Greece. “Dimitrios Copelouzos and the Copelouzos Group: Gazprom by any other name?”. Prepared on March 29, 2007, Published by WikiLeaks.

⁶⁷ The FSRU will have a planned annual send-out capacity of 5.5 bcm and a storage capacity of 170,000 cubic meters of LNG and is expected to start operation in 2023. See: Gastrade. The Alexandroupolis Independent Natural Gas System (INGTS) project.

⁶⁸ See further: Rzayeva, G. “Russian Gazprom Shows Renewed Interest in Greek Natural Gas Infrastructure”. *Eurasia Daily Monitor*. Vol. 14, February 2, 2017.

⁶⁹ The Official Internet Portal of the President of Russia, December 7, 2001.

⁷⁰ Gazprom press release, “Visit to Greek Republic completed”, February 2, 2006.

⁷¹ CAPA – Center for Aviation. “VTB Bank-led Group Wins St Petersburg Pulkovo Airport PPP Bid”. July 22, 2009.

⁷² Aguinaldo, J., “Qatar acquires stake in Russian airport”, *MEED*, September 26, 2016.

⁷³ Marchmont. “\$910m Pulkovo loans sought”. April 22, 2010.

⁷⁴ Росгеология. “Росгеология и Copelouzos group договорились о совместной разработке геотермального проекта на севере Греции.” June 1, 2017.

The experience gained from the Pulkovo airport project, and especially from the collaboration with the German company Fraport, motivated Dimitris Copelouzos to start investing in Greek airports as well. Reportedly, the Copelouzos Group used part of its proceeds from the sale of its stake in the Pulkovo airport to help increase the equity stake of Fraport Greece in March 2017.⁷⁵ In April, 2017, Fraport Greece S.A. (73.4% owned by the Frankfurt based airport operator Fraport AG and 26.6% by Copelouzos Group) took over the operation of the 14 largest regional airports in the country, following an international tender for a concession worth EUR 1.23 billion.⁷⁶ The Copelouzos Group also has a 5% stake in the Athens International Airport, with the other stakeholders being the Greek state (55%) and a consortium of privately-owned funds.

The Savvidis Group – tobacco and sea ports

Another prominent businessman affiliated with Russian interests is Ivan Savvidis. A Russian of Greek-Pontian origin, Savvidis was born in Soviet Georgia before

his family moved to Rostov in the 1960s. He owns a diverse portfolio of investments made in the past eight years.

Following his acquisition of Thessaloniki's most popular football club PAOK FC – which is also one of the

Box 5. A tycoon with two homelands

In the late 1980s, Savvidis became the deputy manager at a state tobacco factory in the Rostov region. In 1993, he was appointed as general manager and became a member of the board of trustees. That year, the company was renamed CJSC Donskoy Tabak (currently the fourth largest tobacco company in Russia with a 7% market share), and Ivan Savvidis remained at its helm for around 10 years. In 1998, Savvidis became involved in local politics, and he was elected member of the legislative council of Rostov region. In 2003, he was also elected an independent member of the lower house of the Russian parliament, the State Duma. He was re-elected in 2007, this time as a member of Vladimir Putin's United Russia party.⁷⁷ He served as a member of the Committee for International Affairs which is in charge of relations with the Greek Parliament. Savvidis founded the Agrocom holding in 2004,⁷⁸ which consists of more than 40 different companies operating in sectors such as tobacco, food processing, agriculture, retail and theme park construction with consolidated gross sales amounting to EUR 751 million in 2018.⁷⁹ Savvidis' additional investments in northern Greece have been financed by the March 2018 sale of his Savvidis Donskoy Tabak Company in Russia to Japan Tobacco, for over USD 1.6 billion. As part of the deal, the Japanese firm acquired Sekap, the Greek Cooperative Tobacco Industry, which was also part of Savvidis holding since 2013.⁸⁰

At the peak of the 2012 Greek economic crisis, Savvidis began developing a large business empire through his corporate Dimera Group. Based in Thessaloniki, Dimera Group began exploiting investment opportunities in infrastructure and logistics, hospitality, food production and media.

⁷⁵ Μπελλος, Η. “Με τα λεφτά στο χέρι” για τα αεροδρόμια η Fraport – ολοκλήρωσε αύξηση κεφαλαίου 620 εκατ”. *Ekathimerini*, March 6, 2017.

⁷⁶ Copelouzos Group press release. “Concession of the 14 Greek Regional Airports”.

⁷⁷ For additional information: SAE. “Greek expatriate Ivan Savvidis was decorated with the medal of the Russian Federation”. February 27, 2008.

⁷⁸ For more information Agrocom Group 2018 Financial Results, 16 May 2019.

⁷⁹ In his position, Savvidis was courageous enough to confront the top Russian leadership in defense of his own business interests. For example, Savvidis publicly criticized then Russian PM Dmitry Medvedev in relation to Medvedev's decision to sell a stake in Rostov's existing airport to a company planning to build a new airport. Savvidis business group, which held 51% of the old airport's shares, vehemently disagreed with the construction of a new airport, feeling that this would threaten their business interests in the area. For more information “Ренова” вылетает в Ростов-на-Дону”. *Kommersant Newspaper*. 2 July 2012.

⁸⁰ Japan Tabaco Inc. “JT Group Acquires Russia's Donskoy Tabak”. March 16, 2018.

Box 6. Sekap: A case of political corruption?

The privatization of the Sekap tobacco company reveals how Savvidis has leveraged his political links with SYRIZA to avoid paying the large fine imposed on the company. Before it was privatized by Savvidis, Sekap was fined EUR 37.5 million for tax evasion and for tobacco smuggling.⁸¹ Although the fine concerned the activities of the previous state administration, payment fell to the Savvidis management. In early 2017, Greek courts upheld the fine against Sekap and increased the pressure on Savvidis to transfer the funds. However, in April, the SYRIZA party passed special legislation in the Greek parliament that *de-facto* wrote off the EUR 37.5 million fine. Despite this, the Greek tax administration found errors in the new law and did not implement it. This left the issue open even after Sekap's transfer to Japan Tobacco. On June 7 2019, in the last bill before the Greek Parliament closed for early elections, SYRIZA was able to pass a new law to ultimately annul the Sekap fine.⁸² The new legislation stated that the owner of Sekap is not responsible for payment if the company had not been aware of the fine when its ownership changed hands, also sparing it of any new fines imposed after the sale. Moreover, the amendment protects the company against any negative rulings from pending litigation.

biggest football clubs in Greece⁸³ – Savvidis' popularity and recognition in northern Greece, especially in Thessaloniki, soared. In the following years he invested in hotels, historic buildings, water bottling, printing, etc.

By far the most strategic investment in which the Savvidis Group participated, and that may be of potential interest to the Kremlin, has been the acquisition of a stake in the Thessaloniki Port. This was done through an international consortium involving the German Deutsche Invest Equity Partners (DIEP) and France's CMA CGM (Terminal Link). The deal includes the consortium's commitment to invest EUR 180 million in the next seven years, in order to capitalize on the port's prime location as an export gate for the wider Balkan region.

Savvidis' very close and cozy relationship with the left-wing SYRIZA government has been corroborated in many cases. For instance, Savvidis received the direct support of the Greek government when he claimed the license for a Greek television station in September 2016. His aggressive bids in that process increased the cost for the other participants as well as revenues for the Greek government.⁸⁴ In September 2016, the private television channel Alpha filed a lawsuit against Ivan Savvidis, accusing him of fraud in connection

with the auctioning of four broadcasting licenses. Alpha TV and Savvidis were not among the winners of the specific competition. The permits went to existing channels Skai and Antenna, as well as to a company tied to shipping magnate Vangelis Marinakis, owner of the Olympiakos soccer club. They also went to Yiannis Kalogritsas, the son of a contractor. Alpha's appeal was based on allegations that Savvidis intervened to raise the price of the licenses, to the detriment of other competitors. Ultimately, however, this litigation did not proceed.⁸⁵ Thanasis Papachristopoulos, a lawmaker with the junior coalition partner in the leftist-led government Independent Greeks (ANEL), spoke openly in March 2018 about the "friendly relations" between the former Greek administration and the Greek-Russian business tycoon.⁸⁶

Savvidis also attempted to undermine the Prespa Agreement, which resolved the long-running dispute between North Macedonia and Greece over the name of the former. Intercepted communications in June 2018 showed that Savvidis was working as a conduit for Russia to undermine an agreement between Greece and the then-FYROM,⁸⁷ the signing of which would pave the way for the Balkan country to join NATO. American agencies were able to collect financial data that implicated Savvidis as the source of unlawful

⁸¹ Ekathimerini. "Amendment writes off multi-million-euro fine imposed on tobacco firm SEKAP". 7 June, 2019.

⁸² Ibid.

⁸³ Savvidis first expressed interest in buying the club in 2006, with the assistance of Dimitris Copelouzos, who had appeared as his representative to the then shareholders of the football team.

⁸⁴ ProtoThema. "Ιβάν Σαββίδης: Εκπλήρωσα την αποστολή μου". September 2, 2016.

⁸⁵ Ekathimerini. "Alpha channel sues Savvidis over license auction outcome". September 8, 2016.

⁸⁶ "I will not deny that in my opinion Mr. Savvidis has certain friendly relations with the government," Papachristopoulos said referring to Savvidis. As quoted in: Ekathimerini. "Gov't refutes ANEL MP's comment on 'friendly relations' with Savvidis". March 15, 2018.

⁸⁷ Acronym of the internationally recognized name of North Macedonia at the time.

payoffs to citizens and soccer fans in return for inciting violence against the FYROM name change referendum.⁸⁸ Savvidis also paid opponents of the name change at least EUR 300,000; beneficiaries included FYROM politicians, newly established radical nationalist organizations and Vardar club soccer hooligans who staged violent protests in front of the Parliament building in Skopje.

These activities have helped Savvidis build a very strong public image while quickly developing close relationships with influential politicians. In addition, Savvidis has built a profile as a deeply religious person by developing relations with both the ecclesiastical authorities of Thessaloniki and the leading monasteries of Mount Athos.⁸⁹ This has also positioned him in one of the Kremlin's favorite soft power niches: the Eastern Orthodox Church. Savvidis himself has publicly declared close friendships with former Greek Prime Minister (2004 – 2009) Kostas Karamanlis, Panos Kamenos, leader of the populist far-right party ANEL, as well as Alexis Tsipras the leader of SYRIZA and Prime Minister of Greece during the period 2015 – 2019.⁹⁰

The Mouzenidis Group – international travel

The other well-known Pontian Greek-Russian businessman is Boris Mouzenidis. He has significantly expanded the Russian tourist presence in Greece through his Thessaloniki-based operation. He owns the well-known airline, Ellinair, as well as the travel agency Mouzenidis Travel, the latter of which has been running since 1995 and serves one in two Russians who vacation in Greece. Building upon his tourism know-how, the agency also managed to expand its business ties in the fur industry both in Russia and in Greece. Mouzenidis Travel also signed an agreement which would launch a series of promotional activities and presentations throughout Russia. The agency was subsequently named official partner of the Greece-Russia Year of Tourism in 2017 – 2018. Mouzenidis Group's turnover for 2018 reached EUR 350 million – a cumulative effect of the improved performances of its airline Ellinair, travel services provider Mouzenidis Travel, and the real estate company Grekodom.

In 2018, Mouzenidis Group generated EUR 234 million in incoming cash flows for Greece, in contrast to EUR 208.5 million in 2017. He reportedly maintains friendly relations with the former Prime Minister Kostas Karamanlis, but also with SYRIZA. On April 14, 2016, the Minister of Foreign Affairs Nikos Kotzias appointed Boris Mouzenidis as the Honorary Consul of Belarus, based in Thessaloniki.⁹¹ This is another typical maneuver by Russian-friendly businessmen who gain diplomatic privileges through appointments to such consular positions, often designed for that very purpose.

Weaponization of trade

Another Greek businessman with a Russian connection is Lambros Bartzokas. He represents in Greece the Russian State Consortium Rosoboronexport, which has controlled Russian arms imports to Greece since 2007.⁹² Specifically, Bartzokas is the CEO of Rosoboronservice Hellas SA, the monopoly supplier of Russian defense systems to the Greek army. His controversial public profile stems from accusations of bribery of politicians and officials in order to ensure that the Greek armed forces purchase the OSA AK Russian air defense systems.⁹³

In the last decade, however, Greece has almost stopped procuring weapons from Russia. After the 2008/2009 economic crisis, the political parties in Greece agreed to a reduction in military spending with some of them opposing more extensive military ties with Russia. Consequently, the country's economics and finance ministries routinely call for reductions in defence spending in order to meet Greek obligations to its creditors.⁹⁴ This is despite US President Trump's praising of Greece as one of the few allies to spend 2% of GDP on the military – the United States had increased

⁸⁸ According to the Organized Crime and Corruption Reporting Project, Cvetkovska, S. "Russian Businessman Behind Unrest in Macedonia". OCCRP. July 16, 2018.

⁸⁹ Iefimerida. "Ο Ιβάν Σαββίδης πάνω σε τρούλο τοποθετεί σταυρό σε εκκλησία στο Άγιο Όρος [εικόνα]". August 2, 2016.

⁹⁰ ProtoThema. *Ivan Savvidis Interview*. May 2, 2017.

⁹¹ Iapopsi. "Οι βόρειοι "ολιγάρχες" και η κάθοδος των (εκατομ) μυρίων". May 12, 2017.

⁹² Military and technical cooperation between Russia and Greece started as far back as 1993, and has expanded after the conclusion of a bilateral defense agreement in 1995. This document paved the way for the establishment of a joint Russian-Greek Intergovernmental Committee on Military and Technical Cooperation. Russia supplied Greece with SAM systems, air-cushioned landing craft, Anti-tank guided missile, Infantry Fighting Vehicles, light anti-tank weapons, artillery systems, Mi-26 transport helicopters, as well as small arms for special operations forces.

⁹³ Ekathimerini. "Five convicts appeal fresh indictment over defense kickbacks". June 8, 2017.

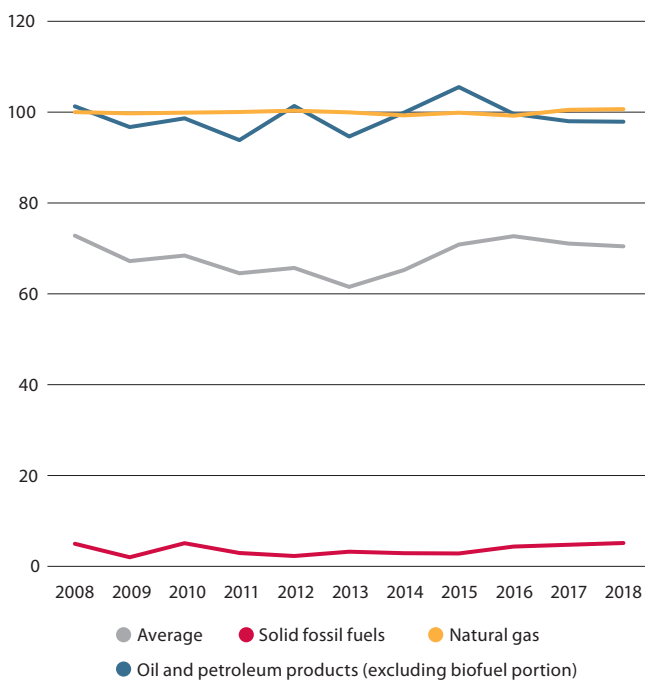
⁹⁴ Tian, N., Fleurant, A., Kuimova, A., Wezeman P.D., and Wezeman, S.T., "Trends in World Military Expenditure, 2018." *Sipri*. April 2019.

pressure on its Western European NATO partners, demanding the rapid modernization of their armed forces and their procurement of new weapons. At present, the prevailing opinion of Greek policy elites is that the country should more consistently orient itself towards its Western partners.⁹⁵ This view has deepened with anxieties caused by Russia's delivery of energy and weapons' assets to Turkey.

ENERGY DEPENDENCE: STRATEGIC ENABLER OF RUSSIAN ECONOMIC INFLUENCE

As in other SEE countries, Greece's energy sector is by far the most vulnerable to Russian economic influence. It also provides the greatest opportunity for leveraging import dependence into political influence. The sector is mainly based on considerable natural gas imports from Russia, as well as a smaller dependence on oil purchases and the so-called "promise of Russian investments" in both of these areas. Russia is the largest oil and gas supplier to Greece, to whose combined mineral fuels sales over the last decade amount to almost EUR 41 billion.

Figure 16. Greece's energy import dependency on Russia, % of total consumption



Source: Eurostat.

⁹⁵ Euro2day. "Το χυροποιείται η συνεργασία της ΕΑΒ με την Lockheed Martin". June 27, 2019.

Greece is Russia's biggest natural gas client in SEE, and will probably remain as such in light of expected increases in natural gas consumption over the next 10 years. In addition, Greece may also play a role in transiting Russian gas to Italy. Greece's dependence on Russian gas has been sustained through a number of long-term contracts with domestic gas distributors including the state-owned DEPA, the Copelouzos Group and most recently the Mytilineos Group, which signed a 10-year supply contract with Gazprom in June 2020, at a time when gas agreements across Europe have become short-term and based on spot pricing fundamentals.⁹⁶

Crude oil

Russia supplies the largest share of Greece's crude oil imports. In 2016, around 25% of crude oil imports to Greece originated from Russia⁹⁷ (down from 33% in 2012), followed by Saudi Arabia, Iraq, Libya and Kazakhstan.⁹⁸ Although substantial, these oil imports from Russia do not necessarily reflect dependence. Crude oil and related products are traded in highly fungible global markets, so substitute supplies can be procured and transported relatively easily in the event that Russian imports are interrupted. Manipulating supplies of crude oil and refined products is generally a less effective tactic than leveraging natural gas dependence.

Besides crude oil imports, the downstream part of the Russian footprint in the Greek oil sector (retail sale of fuels and other derivatives) is not substantial. It includes a network of stations in Athens, Crete and northern Greece, which offer the products of Gazprom Neft Lubricants. Gazprom Neft Lubricants is a daughter company of Gazprom Neft, Russia's third-largest hydrocarbon producer.⁹⁹ Gazprom Neft Aero, another daughter company of Gazprom Neft that specialized in aviation fuel, is present in three Greek airports in cooperation with EKO, a subsidiary of Hellenic Petroleum.¹⁰⁰ In 2017,

⁹⁶ The exact terms of the long-term contract with Mytilineos are not public but the company imported 0.6 bcm in 2019. S&P Global. (2020). "Greece's Mytilineos inks long-term Russian gas import contract". June 2, 2020.

⁹⁷ Liuhto, K. The economic relations between Greece and Russia. February 2018.

⁹⁸ Source: International Energy Agency, Country Data Statistics. OECD/IEA, 2020.

⁹⁹ The operations are done through the locally registered company ACTIV-EU. Gazprom Neft's official website.

¹⁰⁰ Hellenic Petroleum is the most powerful, state owned group in the Greek energy sector, which owns three of the four Greek refineries and has a network of more than 1,700 petrol stations, explorer of oil and gas in the country, and the sole Greek petrochemicals producer.

Box 7. Burgas-Alexandroupolis – a failed attempt?

The Russian footprint in the energy sector had also included the Burgas-Alexandroupolis project. This involved constructing an oil pipeline connecting the Bulgarian port of Burgas on the Black Sea with the Greek port of Alexandroupolis at the Aegean Sea, thus bypassing the congested Turkish straits.¹⁰¹ While it never materialized – mostly due to environmental concerns on the Bulgarian side – it nevertheless seriously impacted the Russian footprint in the Greek oil sector, as well as general relations between the two countries. For most of the first two decades after the Cold War, the project occupied the bilateral energy policies of both Bulgaria and Greece vis-à-vis Russia. It therefore marked a high point of recent Greek-Russian relations.

The project has not, however, been completely forgotten. During the crisis in Russian-Turkish relations after a Russian military plane was shot down in November 2015, alongside the search for alternatives to the TurkStream gas pipeline project, Moscow attempted to revive the oil pipeline project approaching Sofia and Athens.

Serbia's Naftna industrija Srbije, in which Gazprom Neft has a 56% equity share, negotiated with Hellenic Petroleum regarding the drilling of exploration wells in the Greek Continental Shelf. There is also ongoing cooperation between Hellenic Petroleum and Rosneft in the refined oil products trade based on an agreement signed in 2016.

As with other countries in the region, Russia is willing to deepen and broaden its scope in the local market – it tried to exploit the privatization of the Greek energy sector during the financial crisis distress without much success. Under the first Greek bailout agreement with its creditors, Athens committed to attracting about EUR 19 billion by 2015 through the privatization of key assets.¹⁰² The privatization projects of the Greek Privatization Agency included the sale of the state's 35.5% stake in Hellenic Petroleum, as well as the privatization of DEPA and DESFA. In early April 2012, Gazprom Neft was the first potential bidder to express interest in buying into the company.¹⁰³ In this process, the participation of the Russian company was supposed to be

through its Serbian company Naftna Industrija Srbije. Gazprom Neft was mainly interested in buying two of the three refineries owned by Hellenic Petroleum.¹⁰⁴ Simultaneously, Gazprom declared its interest to participate in the privatization of DEPA and DESFA. These first attempts for the privatization of Greece's biggest energy companies were not completed. Russia did not participate in the second attempt to privatize Hellenic Petroleum under the country's third EUR 86 billion bailout program – this time for 50.1% of the company.

Natural gas

Natural gas is an increasingly important energy source for Greece. In 2018, its share in the total primary energy supply and in power generation had risen from 12% and 13% in 2015 to 19% and 26% respectively.¹⁰⁵ With domestic production of only 0.009 bcm in 2016, Greece is heavily dependent on imports of natural gas and vulnerable to potential natural gas supply cuts by Russia. In contrast, Russian gas deliveries have steadily risen, reaching around 3 bcm/yr. In light of these quantities, the degree of Greek dependence – determined as the percentage of direct Russian imports of the total annual gas demand – is around 65% on aver-

¹⁰¹ The idea was conceived by N. Grigoriadis, a close associate of the Greek businessman Spiros Latsis. His group together with that of D. Kopelouzos established the consortium HELPE S.A. – THRAKI S.A., a joint venture between Hellenic Petroleum and Thraki, owned by Prometheus Gas, and began lobbying the Greek, Bulgarian, and Russian governments. For more see Christidis, Y., Armakolas, I., and Paschalidis, P. (March 2017). *Greek-Bulgarian Relations: Present State and Future Challenges*, Eliamep, p. 33.

¹⁰² Greece underwent an economic adjustment program between 2010 and 2018, which included three separate financial assistance packages (bailout agreements) from the *troika* worth a total of EUR 256.6 billion.

¹⁰³ Reuters "UPDATE 1-Gazprom Neft says may buy into Hellenic Petroleum". 6 April 2012. In 2003, Lukoil together with the powerful Latsis Group tried to buy into Hellenic Petroleum. No agreement could be reached on the price; still, the Latsis Group through

its Pan European Oil acquired 45.5% of Hellenic Petroleum. See Дзядко, Т., "“Газпром нефть” собирается поучаствовать в греческой приватизации." *Ведомости*. 08.04.2012; EnergyPress. "Latsis group unlikely to take part in follow-up ELPE sale". August 9, 2019.

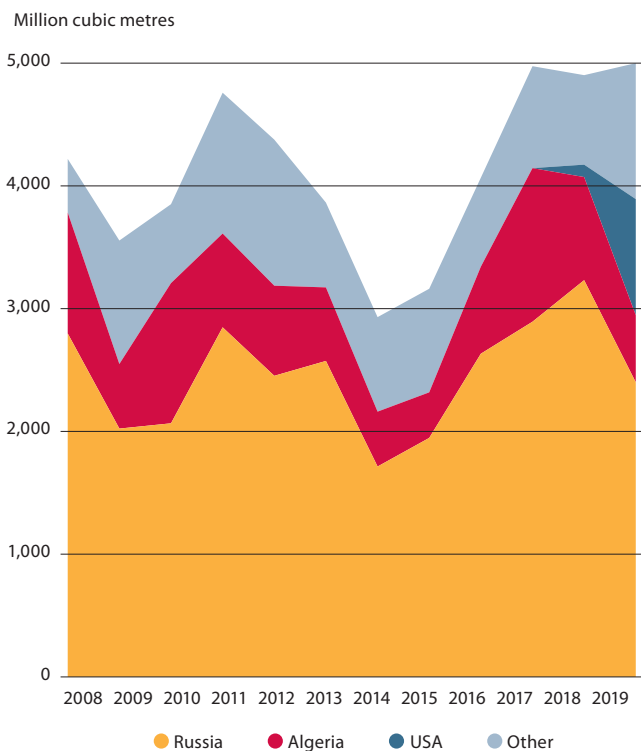
¹⁰⁴ К. Мельников, Е. Кузнецова, А. Гудков. "Греческий бензин ищет российских покупателей". *Коммерсантъ* № 62 от 09.04.2012, стр. 11.

¹⁰⁵ International Energy Agency, Country Data Statistics. OECD/IEA, 2020.

age, which is double that of Europe (DEPA has a gas supply contract for 2.6 bcm/year; other private gas traders have signed separate contracts with Gazprom including Copelouzou's Prometheus).¹⁰⁶ Gazprom sells roughly 3 bcm/year to Greece under a long-term gas supply contract that terminates in 2026. The gas passes through Bulgaria – initially through the Transbalkan pipeline, which goes through Ukraine, Romania and Bulgaria. In the beginning of 2020, the gas began arriving via the TurkStream pipeline before transiting through Bulgaria on to Greece.

However, Greece's gas dependence on Russia is fluctuating year on year as Greece can use its LNG terminal at Revithoussa to import gas from the global gas market.

Figure 17. Natural gas imports in Greece by partner country



Source: Eurostat and commercial data on LNG imports.

As early as 1988, Greece was able to ensure diversity of supply when it signed a commercial agreement to receive supplies of LNG from Algeria's Sonatrach company.¹⁰⁷ In 2007, the newly-operational Greece-Turkey gas

Interconnector pipeline started transporting Caspian/Azerbaijani natural gas via Turkey to Greece. In 2016, LNG imported from Algeria and Norway was nearly 29% of the total gas imports, with 16% passing through Turkey.¹⁰⁸ In 2017, the shares of LNG (from Algeria, Qatar and Norway) and gas transited through Turkey reached 29% and 12% respectively.¹⁰⁹ In 2019, amid the slump in global gas prices, the share of LNG imports in Greece exceeded for the first time pipeline deliveries by Gazprom (2.6 bcm/year vs. 2.4 bcm/year), a trend which is set to continue in 2020.

Despite the growing role of alternative suppliers, the significant role of Gazprom in the Greek gas market is here to stay and is amplified by the fact that from the start the national wholesale natural gas market has been developing in a monopolistic manner. The Greek state-owned Public Gas Corporation S.A. (DEPA) has been the exclusive importer of natural gas in the country. The cornerstone of the Russian economic footprint in the Greek gas sector, laid more than 30 years ago, is the Intergovernmental Agreement for the supply of natural gas between the Soviet Union and the Government of former Greek Prime Minister G. Papandreou, signed on October 7, 1987. This preceded the very construction of the national gas system as well as the September 1988 incorporation of DEPA itself as the ultimate state arm in preparing Greece for the natural gas era.

The initial supply agreement (to last until 2016) was not favorable to Greece as it entailed high prices, inflexible supply terms, including a take-or-pay obligation, and the prohibition of re-exports. Over three decades, consecutive governments tried to renegotiate the long-term deal but Gazprom either refused or offered damaging stipulations. In 2011, despite a 7% cut in prices, Greece still paid higher rates compared with what Gazprom charges in other parts of Europe where competition is steeper. However, Gazprom signed a 10-year extension of the supply contract with DEPA in 2014 – this became effective from 2016, involving the delivery of 3 bcm/year including an 80% take-or-pay clause. In addition, DEPA was able to secure a 15% cut in gas prices after it threatened international arbitration over claims that it had been overcharged by as much as 30%, compared to Gazprom's other European customers.¹¹⁰ The arbitration threat was the result

¹⁰⁶ Calculated from the statistics of DEFA for the imported gas in the National Natural Gas System, Off-Takes, Deliveries, Variation in the Stored Quantities at NNGS (2017); Off-Takes, Deliveries, Variation in the Stored Quantities at NNGS (2016).

¹⁰⁷ Throughout the years, Sonatrach has supplied the Greek gas market with between 0.55 and 1 bcm annually.

¹⁰⁸ See Off-Takes, Deliveries, Variation in the Stored Quantities at NNGS (2016).

¹⁰⁹ See Off-Takes, Deliveries, Variation in the Stored Quantities at NNGS (2017).

¹¹⁰ Keimenoy, M. "Μ. Πίου: Παρέμβαση της Δικαιοσύνης για τις τιμές φυσικού αερίου". *Energy Press*. November 29, 2013.

Box 8. Gaining a foothold through joint ventures

Gazprom has not only been active as an exporter of natural gas in Greece – it has also played a central role in boosting domestic demand by participating in gasification infrastructure projects via its subsidiary joint venture, Prometheus Gas. As mentioned above, its joint venture with the Copelouzos Group had held as its main objective the promotion and marketing of Russian gas in Greece. Prometheus Gas has also been involved in the construction of Greece's domestic natural gas transmission system. In the development of the initial gas infrastructure in the 1990s, it partnered with the former Soviet company, Stroytransgaz, which is now owned by the US and EU-sanctioned Russian businessman Genady Timchenko.¹¹¹ Nowadays, the Greek-Russian joint venture Prometheus Gas has spread its activities throughout the Greek energy sector, thus increasing the Russian footprint and influence in the country. Prometheus Gas has amplified the Russian presence in the gas sector through several partnerships, including with:

- ENEL for the construction of gas-fired combined cycle power stations;
- the Bulgarian state-owned electricity company NEC, for the import of electricity from Bulgaria;
- a number of real estate joint ventures through which Prometheus Gas has developed and continues to manage buildings of a combined over 33,000 square meters in the most attractive business areas of Attica. This has made it a major player in the domestic real estate market.

of a November 2013 investigation conducted by Greek prosecutors into the pricing terms of the Gazprom supply contract. This investigation discovered that the Russian company had abused its dominant position to charge excessive tariffs, thereby limiting the competition on the Greek market.

Since then, Gazprom has positioned itself favorably to benefit from the gradual liberalization of the Greek energy market.¹¹² Following the full unbundling of natural gas distribution and the opening of the retail market, DEPA implemented a special program to reduce its own hold on the wholesale market.¹¹³ In addition, in 2014 the country's Competition Commission forced DEPA to concede capacity to third parties at points of entry to the national gas grid – this included the interconnection point Kulata/Sidirokastro (the entry point of the Russian pipeline in the country).¹¹⁴

Two years later, and after strong pressure from the European Commission, the Bulgarian and Greek gas transmission system operators – Bulgartransgaz and DESFA – finally signed an Interconnection Agreement allowing backhaul capacity¹¹⁵ to be allocated to commercial entities. This would lead to the liberalization of the cross-border gas trading in SEE. Despite the gas liberalization push, DEPA has remained the dominant wholesale supplier in the country, holding 90.4% of the market in 2016.

The liberalization and reform of strategic sectors of the Greek economy have curtailed Russia's efforts to transform its economic footprint into political leverage. Nevertheless, the mismanagement of state monopolies and widespread state capture practices have allowed Russian companies to gain a foothold in key areas.

Gazprom used the gradual deregulation of the gas market to increase its exports. The amount of gas it sold in Greece has increased considerably, covering as much as 80% of Greek demand by the end of 2018. DEPA's exclusive right to procure gas from Gazprom or the Greek market was abolished in 2014. This changed the landscape of the domestic market. In October 2016, Gazprom Export started deliveries of natural gas under contract with its joint venture Prometheus Gas, in excess of the quantities contracted by DEPA. Prometh-

¹¹¹ As of mid-2020, it is an active Russian company in the field of engineering and construction of pipeline systems, oil and gas production facilities etc. The company has been added to the Specially Designated Nationals List on the US Department of the Treasury site because of connections to the 2014 Crimean crisis.

¹¹² The deregulation of Greece's wholesale gas market was based on transposing the third EU Energy Package (Directive 2009/73/EC) into national law in 2011 and harmonization with the European framework in accordance with the country's bailout commitments – *Laws 4001/2011, 4336/2015 and its amendments 4337/2015, and 4414/2016 and Laws 4336/2015 and 4227/2015.*

¹¹³ With quantity offered as a percentage of the previous year's sales volume adjusted upward annually to reach 20% by 2021.

¹¹⁴ The stumbling blocks, including the Siderokastro-Kulata border connection, were dealt with and reverse flow option opened, albeit at a modest 3 million cubic meters per day.

¹¹⁵ A transaction that results in the transportation of natural gas in the direction opposite to the original route of the transmission gas network.

eus Gas reached annual imports/sales of circa 1 bcm¹¹⁶ (approximately 20% share of the Greek market), selling mainly to industries and gas supply companies.¹¹⁷

Gazprom participation in the privatization of DEPA and DESFA

Russia has tried to exploit the Greek financial crisis to take over the most important gas companies: rather than confine itself to gas imports and pipeline construction, Gazprom tried to take over the whole gas supply chain. In May 2013, Gazprom bid for the privatization of the Public Gas Corporation SA (DEPA) and for 66% of the Hellenic Gas Transmission System Operator SA (DESFA), either separately or as a bundle. The EUR 900 million preliminary bid was well in excess of the EUR 550 million offered by the only other rival bidder, the Greek M&M Gas. In the negotiations, Gazprom leveraged its position as the only major international energy company interested in buying DEPA. The purchase of DEPA – along with access to the gas distribution network in Greece – would practically give the Russian company full control over the country's gas market.

Gazprom's participation conflicted with the third energy package of the EU, which entailed a strict separation between the ownership of the supply and transmission companies involved in a project. This was also happening amidst allegations of unfair competition and price fixing, which resulted in the European Commission's launching of an anti-trust probe against the Russian company in September 2012.¹¹⁸ Despite this, the Privatization Agency (HRADF) amended its contractual terms to allow Gazprom to avoid a possible rejection of its bid by Brussels. Under the final terms of the DEPA sale, the deposit for participation in the tender was reduced to 10% from the initial 20%. In addition, even if the EU had decided to block the acquisition, the new terms would have allowed Gazprom receive its deposit back. The government was hoping that Gazprom would be able to strategically deliver cost savings to the Greek industry if it took over DEPA. In return, Athens asked for lower prices of the Russian natural gas supplied to the country. The Greek government shrugged off warnings from both the European Commission and the U.S. –

that the deal would violate EU law, and make Greece excessively dependent on Russia. Despite the active support of the Greek government, Gazprom pulled out of the privatization tender at the last moment, failing to submit a binding bid. It most likely understood that its attempts to buy DEPA would have been blocked by the EU; this later happened in 2014 with their South Stream project.

Another Russian company, Sintez Group, was among the contenders that qualified for the final stage of the tender. Initially, Sintez – through its subsidiary Negusneft – bid for the whole DEPA Group (DEPA+DESFA) and was ready to offer EUR 1.9 billion,¹¹⁹ thus outbidding the rest of the candidates, including Gazprom. Concerns were expressed in the press that Sintez “may become a proxy for Gazprom to acquire control of the Greek gas market.”¹²⁰ This was especially worrying as the group was controlled by Russian oligarch Leonid Lebedev, who at the time was a third term Russian senator. Later, however, Sintez dropped its interest in DEPA, and expressed willingness to privatize only DESFA. This was in line with the company's plans to develop a gas transport hub in the region that included interconnection pipelines with neighboring countries, as well as LNG facilities on the Aegean coast.

Despite its initially ambitious plans, Sintez may have dropped out of the race due to its strained ties with the Kremlin – as well as with President Putin himself, who had publicly criticized Lebedev for not keeping his pre-privatization promises of investing in the Russian domestic energy system.

ENERGY POLICY INFLUENCE: THE INFRASTRUCTURE TOOL

Its important geopolitical position and potential as an energy hub incorporating alternative energy routes made Greece a target of Russian attempts to influence the process of diversification and market liberalization. Russia's main objective was therefore to try to control the country's energy policy options and weave a network of domestic oligarchic interests in the energy sector – this would block the process of diversification and market liberalization. These state capture mechanisms have helped Russia exploit multiple governance deficits,

¹¹⁶ Copelouzos Group, “Natural Gas,” available at: www.copelouzos.gr/en/sector/natural-gas/.

¹¹⁷ It was part of the overall increase of Russia's gas exports to Europe (close to 40%) to a record level of 193.9 bcm even amidst concerns over Russia's cyber espionage activities in Syria and Ukraine.

¹¹⁸ Hope, K., “Russians line up for Greek gas sale”. *Financial Times*, January 10, 2013.

¹¹⁹ Reuters, “Russia's Sintez top bidder for DEPA, at 1.9 bln euros-paper”. February 12, 2013.

¹²⁰ Hope, K., op.cit.

as well as extend its business portfolio in strategic sectors of the country's economy – especially infrastructure. Over the years, Russia has made considerable effort to acquire crucial Greek infrastructure. While most attempts have not been successful, they reveal a clear pattern of strategic interest.

Successive Greek administrations have maintained a strategic position vis-à-vis Russia-led energy projects. These include the now-defunct South Stream gas pipeline that would ship Russian gas through the Black Sea and the SEE region to the Baumgarten gas hub near Vienna. The Russian pipeline undermined the EU's Nabucco project which aimed to channel Caspian Azeri gas to clients in Central Europe. Greece's aim has been to become a regional natural gas transit hub for Russian as well as alternative gas supply – such a status would improve the country's energy security and lower gas import prices.

To this end, Greece promoted renewable energy sources and facilitated investments in solar, wind, biomass and geothermal projects in line with the EU's Energy Union initiative. It also joined some of the EU's most important gas diversification projects, such as the Southern Gas Corridor,¹²¹ in order to reduce its dependence on Russian gas while strengthening the security and flexibility of Greece's energy supply. After 2010, Greece was almost exclusively financed by its European creditors. Many of its policies were dependent on the agreement of the *troika*, which also impacted the country's energy policy.¹²² It thus became imperative for pro-EU governments to show that Greece's alignment with EU energy goals and norms could produce tangible economic benefits for the country, even as it plunged into a depression. From 2010 onwards, the main goal of Greece's energy policy has been to maximize energy security through multiple alternative cost-efficient and competitive energy interconnections.¹²³

Gas pipelines

Over the past three decades, a main energy objective of the Kremlin and Gazprom in SEE has been to se-

cure a future gas transit route to Central and Western Europe – this would circumvent Ukraine and at the same time preserve Russia's European markets. A common conviction among Greek policy-makers and business leaders has been that Russian gas projects would provide a stable, relatively cheap supply of natural gas, new jobs for Greek engineering and construction firms, as well as a favorable atmosphere for further expansion of Russian investments: tourism, Greek exports, etc.

In the 2010s, the South Stream pipeline was the main instrument of Gazprom's Southern export strategy, with the goal of completely circumventing Ukraine as a transit country. By mid-2010, the Greek Parliament had ratified an intergovernmental agreement on South Stream. In addition, a project company had been created and an agreement signed between DESFA and Gazprom to enable the start of construction works. The Greek government put all of its eggs in the Russian gas basket as the South Stream project was gradually linked to all other outstanding issues, including the privatization of DEPA and DESFA, and the renegotiation of the existing long-term gas supply contract with Russia. When Gazprom announced its plans to shelve the Southern route of the South Stream project and concentrate on its Balkan dimension only (Bulgaria, Serbia, Hungary and Austria), the Greek government continued negotiating with Gazprom in order to include Greece in the pipeline route. This policy continued even when it became increasingly clear that the EU would block this project due to its inconsistency with EU energy and competition law.

By the end of 2014, the South Stream project had been cancelled – this was not only a considerable economic setback for Russia but also a serious blow to its foreign policy. The Russian government immediately replaced South Stream with an amended version – TurkStream. This new initiative – driven by an agreement between Gazprom and the Turkish state-owned gas supplier BOTAS – operated on similar terms albeit on a smaller scale.¹²⁴

The birth of TurkStream allowed the Kremlin and Gazprom to (try to) pit Greece against Bulgaria in the competition to secure continuation of the pipeline from

¹²¹ Europe's Southern Gas Corridor Strategy founded on the necessity to maximize the imports of non-Russian gas via non-Russian controlled territory, so as to establish an additional route of supply diversification.

¹²² For more information: Lekakis, J. N. & Kousis, M., "Economic Crisis, Troika and the Environment in Greece". *South European Society and Politics* 18, no. 3 (2013), pp. 305-331.

¹²³ Greek Ministry of Foreign Affairs, "Energy Diplomacy," available at: www.mfa.gr/en/energy-diplomacy/.

¹²⁴ The new pipeline, which would consist of only two pipeline strings with half the capacity planned for South Stream, would again pass through the Black Sea but would instead link directly to Turkey. The first line of TurkStream would deliver gas directly to the Turkish market, while the second would continue towards Europe either via Bulgaria or Greece.

Turkey. Gazprom's initially announced plans were to secure the transit of natural gas through Greece. This natural gas would be directed northwards through the Western Balkans, passing through North Macedonia, Serbia and then on to Hungary and Austria. This would simultaneously punish Bulgaria for the failure of the South Stream project, as well as exploit the only other route available to transit natural gas. These Russian plans were further facilitated by the change of guard in Athens. The 2015 leftist SYRIZA government¹²⁵ demonstrated a strong pro-Russian attitude, offering them more support than previous Greek governments. This was purportedly because TurkStream's Greek extension represented a chance for the party to indirectly defy EU austerity measures.¹²⁶

Besides SYRIZA's anti-Western rhetoric, there were also financial considerations behind the initially positive reception toward Russian proposals and presence in general, and regarding the gas sector in particular. Some of these considerations turned out to be broad miscalculations of the Greek financial crisis, most of which suggested an inevitable acquiescing to bail-out agreements with Western creditors. Greece hoped to see its gas debt erased, while securing a cut in gas prices – as well as receiving hundreds of millions in transit fees following the implementation of TurkStream.¹²⁷

The SYRIZA government turned against the EU common foreign policy and began routinely criticizing the sanctions levied against Russia in the wake of the Ukraine invasion. Moreover, the permanent representative of Greece in the EU blocked a key passage on sanctions – an action that prolonged the blacklisting of 132 individuals and 28 entities.¹²⁸ At the same time, the office of Prime Minister Alexis Tsipras issued an unprecedented statement – that the new Greek administration had, in fact, not approved a warning by EU heads of government regarding possible further sanctions against Russia.¹²⁹ The risk of

the Ukrainian crisis escalating into an internal EU political crisis thus heightened. EU sanctions against Russia were to expire in March of 2015, unless renewed by the unanimous decision of member states. This gave Greece effective veto power. While Greece provided last-minute support for the extension of these sanctions, the plan to expand their scope was abandoned by the EU. The following years saw such a recurring pattern of Greek policy towards EU-Russia relations. The Greek government's bargain was that of maintaining an ambiguous stance on sanctions in return for the promise of Russian financial aid. This, however, never materialized. At the same time, the Greek government relied on potential Russian investments in the construction of a large-scale gas pipeline and the prepayment of transit fees on the new infrastructure.

Russia's commitment to TurkStream's extension to Greece was linked to the Greek government's agreement for major Russian companies to participate in the tender for hydrocarbon exploration in 20 offshore blocks in the Ionian Sea, as well as south of the island of Crete. According to Greek, German and American press reports, Gazprom was considering providing up to EUR 5 billion as an advance for the extension of the TurkStream pipeline, which could hardly have come at a better time for Greece. In addition, there was the prospect of lowering the price of natural gas for Greece, as Russia had already done for Turkey.¹³⁰

Moscow was trying to replace Bulgaria with Greece as the main EU entry point of Russian gas transit, while keeping intact the main scheme for the supply of natural gas to Central and Eastern Europe. Greece was relatively confident that Brussels could be convinced to agree with the construction of the pipeline. The Greek and Russian governments reached an agreement that the Russian state-owned development bank Vneshekonombank (VEB) would finance and later own 50% of the joint venture, while the rest would be financed and owned by a Greek company.¹³¹ To implement TurkStream, the Greek government also decided to extend the Poseidon interconnector to the Greek-Turkish bor-

¹²⁵ As a declaration of his foreign policy intentions Tsipras had his first meetings with the Ambassadors of Russia and China in Athens even before his official inauguration.

¹²⁶ When in opposition, Syriza argued for the unilateral Greek exit from the EU sanctions against Russia.

¹²⁷ According to some publications the expected gains from the eventual price reduction were around EUR 100 million – Tagliapietra, S. and Zachmann, G., "Will natural gas cooperation with Russia save the Greek economy?". *Bruegel*. April 20, 2015.

¹²⁸ Traynor, I., "Greece delays EU agreement on Russia sanctions". *The Guardian*. January 29, 2015.

¹²⁹ Halligan, L., "Russia's sanctions hand the advantage straight back to debt-laden Athens". *The Telegraph*. January 31, 2015.

¹³⁰ Putin declared it quite clearly on December 1 2014 during his visit to Turkey: "As we expand our cooperation, we will lower the price for Turkey, as our strategic partner. The first step toward this is lowering the price by 6% from January 1, 2015, and then even more – perhaps by an equal amount, or maybe even greater. This will all depend on how we build our relationship with our partners in this area". President of Russia. "News conference following state visit to Turkey". December 1, 2014.

¹³¹ Mazneva, E. and Chrepa, E., "Russia Strengthens Greece Ties with Gas Link Deal to Europe". *Bloomberg*. June 19, 2015.

Figure 18. TurkStream map



Sources: BP, ENTSOG, GIE.

der all the way to the border town of Kipi in order to receive Russian gas.¹³²

Greece was facing an almost imminent default on its IMF obligations on June 30, 2015. The Greek government thus considered linking its support for the TurkStream project to a request for substantial loans, so as to avoid exiting the Eurozone. Such a request could have marked the beginning of a profound change in Greece's foreign policy orientation. In a series of exchanges, the Kremlin implied that Russia was willing to come to Greece's aid. However, in the end, no agreement was reached on the provision of direct financial assistance. This decision spelled the beginning of the end of the honeymoon period between Russia and Greece.

Greek-Russian relations cooled further with the deepening of Russian interference in Greece's effort to settle the name dispute with neighboring North Macedonia. The lowest point came on July 11, 2018 when the Greek government expelled two Russian diplomats and allegedly barred the entry of a third, citing national security concerns. Although this political meltdown never decisively led to the full freezing of bilateral relations, the damage was done – Russia gradually shifted its preferred route for expanding TurkStream back to the Bulgarian direction. In contrast to the case of South

Stream, Gazprom's TurkStream approach relies on a passive approach – this involved delivering the natural gas up to EU borders, and then leaving the subsequent transit to domestic gas network operators. This not only shifts the financial and regulatory burden to local companies, but also prevents EU scrutiny on competition requirements for new pipeline infrastructure.

Russia's decision for the TurkStream's European route to pass through Bulgaria rather than Greece was officially announced at the end of July 2019. The announcement came as the parliamentary elections in Greece earlier in July brought down the government of SYRIZA and restored Nea Demokratia back to power, signaling a potential worsening of political ties with Russia. For the past five years, the future trend of Russian economic influence in Greece had depended on Gazprom's choice of the new supply route to Europe. Once Gazprom stopped the transmission of gas through Ukraine on its Transbalkan pipeline, Russian exports of natural gas for Greece were redirected through TurkStream and Bulgaria along the existing transit infrastructure at the Bulgarian-Greek border crossing (Kulata-Sidirokastro).¹³³

¹³² The Poseidon Pipeline consists of two sections, with a total length of about 976 km. The Poseidon pipeline will extend for approx. 760 km following a west-bound route from Kipi to its landfall in the Thesprotia regional unit (Florovouni) and for approximately 216 km to the landfall in Italy and the receiving terminal in the Apulia region (Otranto). The underwater section in the Ionian Sea is to be used by EastMed pipeline, as well.

¹³³ ICGP has the capacity to export from Greece to Bulgaria 3 bcm/y of natural gas, but a potential later phase of the project could increase this capacity to 5 bcm/y and allow physical reverse flow capacity from Bulgaria to Greece. The ICGP has a crucial role to play in the Southern Corridor project and the EU attempts to diminish the dependence on Russian gas. Although it was planned to help Bulgaria reduce its almost complete reliance on Russian gas supplies, the probability of using it by Gazprom in reverse mode is quite real.

Box 9. Russian gas infrastructure projects – a sideshow?

At the start of 2016, while Gazprom was engaged in revitalizing the Poseidon project so as to transit natural gas to Italy, there was another development related to the Russian footprint in the Greek gas sector. The Greek government and Russian Sintez Group began discussing a deal to construct a gas interconnector between Greece and North Macedonia (then FYROM). Sintez had been eager to build the link in an attempt to increase its involvement in power generation as it was already operating a gas-fired plant near Skopje. In March 2017, Sintez, through a Greek-registered subsidiary, filed an application with the Greek Regulatory Authority for Energy (RAE) for a license to construct a natural gas interconnector between Greece and North Macedonia. Before applying, Lebedev, who headed Sintez, had signed a Memorandum of Understanding (MoU) on building the pipeline with the former Prime Minister of North Macedonia Gruevski. The main obstacle to Lebedev's plan was the fact that the state-owned gas network operator, DESFA, has developed its own project for a Thessaloniki-Skopje natural gas interconnector. At the end of 2018, the energy regulator of Greece gave the green light to both projects.

There had been assumptions that Sintez's interconnector had been planned in strategic anticipation of the TurkStream when it was still viable. Although logical, such an assumption does not seem plausible in retrospect due to the relatively minor capacity of the planned interconnector compared to that of TurkStream. Moreover, Sintez tried to acquire a gas distribution license for northern Greece but has so far failed to jump-start its projects. This is despite the fact that in 2017 the company received a retail gas permit that allowed its taking advantage of the ongoing gas market liberalization. Lebedev has also announced further grand investment intentions of up to EUR 5 billion in several other energy projects in Greece, including a giant offshore wind park estimated at around EUR 1 billion in the Aegean, and the construction of a gas pipeline from Libya to Crete and from there to the Peloponnese, linking up to the Greek national gas system. Although these projects seem unlikely to materialize in the near future, they may present an enormous potential opportunity to increase the Russian footprint in the Greek energy sector.

Sea ports

While Russia's quest to expand its influence by exploiting gaps in the Greek energy sector has been limited to the previous two decades, its attempts to acquire crucial pieces of Greek infrastructure are in line with their centuries-old quest for warm-water ports. Russian interest in Greek port infrastructure has been much more pronounced in northern Greece where Russian oligarchs have made direct attempts to acquire the most strategic marine outlets on the Aegean coast, including the port of Thessaloniki, Kavala and Alexandroupolis. These ports represent key ending points of land routes from Russia to commercial routes and the potential to secure a military presence in the Eastern Mediterranean.

Russian companies therefore saw potential investments in the northern Greek ports as a means to gain control over railway infrastructure.

The Thessaloniki port

A history of Russian attempts at the port

In 2012, Russian Railways (RZD) expressed interest in acquiring the Greek railway service operator TrainOse,¹³⁴ as well as the recently established rail-carriage maintenance company Rosco. The previous year, a Russian delegation had reviewed TrainOse's books to assess its value and the feasibility of a potential acquisition by one of Russia's largest state-owned companies.¹³⁵ Russian Railways, together with its CEO, Vladimir Yakunin – then a close ally of president Putin – linked the acquisition of TrainOse with the takeover of the Thessaloniki Port Authority (OLTH). The Greek government subsequently demanded EUR 100 million for the OLTH and another EUR 40 million for TrainOse and Rosco. However, Russian Railways needed a green

¹³⁴ With nearly 900 employees, TrainOse operates all 500 cargo and passenger routes on 2,500 km of railways.

¹³⁵ Deutsch. A., "Exclusive: European railway companies eye Greek network sale". *Reuters*. April 13, 2012.

light from the Kremlin to make an official offer. In a letter to President Putin, dated May 27, 2013, Yakunin asked for an approval of the deal that would include the takeover of a “big Greek infrastructure construction company” or the French Railway company.¹³⁶ Yakunin tried to convince Putin that after the company’s major investment in Serbian railways, the possible buyout of TrainOSE, combined with Thessaloniki port authority and Rosco, would not merely be a shrewd investment move, but would also strengthen Russia’s position in the Balkans.

In October 2013, RZD, in a consortium with the Greek infrastructure construction company GEK Terna, was among the 3 investors that advanced to the second phase of privatization tenders for both TrainOSE and for Rosco.¹³⁷ Six months later, the Greek Privatization Agency also officially opened the tender process for the sale of 67% of the shares in OLTH, which is licensed to operate the Port of Thessaloniki until 2051.¹³⁸ The same Russian-Greek consortium was among the 8 investors approved by the Agency to proceed to the second phase of the tender. However, the geopolitical situation changed following the annexation of Crimea and consequent imposition of US/EU sanctions. Moreover, the US Treasury placed the head of RZD under sanction, labelling him a “close confidant of Putin” who “regularly consults with Putin on issues regarding the Russian Railways company.” Meanwhile, the ongoing political turmoil amidst two consecutive Greek parliamentary elections led to the postponement of the ongoing privatization tenders.

When the international tender procedures were restarted in April 2016, the Russian Railways was still in the race – this time participating separately from the Russian-friendly GEK Terna, who was also submitting a bid. In May, on the eve of his visit, President Putin wrote in an article for the most widely-read Greek daily *Kathimerini* that “Russia could also help streamline the Greek transport infrastructure. We are referring to the participation of Russian business entities in the forthcoming Greek tenders for the purchase

of assets of railway companies and the Thessaloniki port facilities.”¹³⁹ This assertive stance reflected Russian commitment to the deepening of commercial ties with Greece. However, a month after the visit of the Russian president, neither RZD nor GEK Terna had submitted binding offers for TrainOSE. In the end, the sole offer for TrainOSE was made by Ferrovie Dello Stato Italiane, which was declared the winner with an offer of EUR 45 million. The eventual withdrawal of the Russian bid could have been due to strategic European Commission-directed changes to the binding conditions of the contract, which effectively blocked Russia’s participation. Approval of the contract by DG Competition of the European Commission was mandatory in light of previously-rendered aid to TrainOSE that amounted to EUR 700 million.

The Russian stake in port privatization

The same thing happened in March 2017 when the tender for the Thessaloniki port was closed without RZD submitting an offer. This time, however, Russia participated indirectly via Ivan Savvidis. His company, Belterra Investments, which is registered in Cyprus, joined a consortium together with Deutsche Invest Equity Partners GmbH and Terminal Link SAS. The latter is a French daughter company of CMA CGM, which was invited to join the consortium in the final days¹⁴⁰ for an obvious reason. As part of the China Merchants Holdings International (CMHI), it was the only one with experience in running ports from Hong Kong, the biggest port operator in the world. Deutsche Invest Equity Partners (DIEP) – a private equity investor with EUR 2 billion in assets under management in venture capital, growth and real estate with a focus on Germany, China and the United States¹⁴¹ – has five employees in total, which seems tailor-made to suit investment projects whose unclear ultimate beneficial owner is unclear. In 2012, DIEP explored the opportunity for buying out the fertilizer plant in Kavala on behalf of Russian oligarch Arkady Roteneberg, a close friend of Putin. It is possible that the fund was similarly assisting another Russian-led investment deal, although no evidence to the fact has emerged so far.

The consortium won a tender for the port privatization with an offer of EUR 231 million. It acquired 67% of the shares in December 2017, and the agreement for the sale

¹³⁶ Ю. Орлова, Е. Тимошинов, Н. Бархатова, „РЖД ищет путь в Грецию”. *Коммерсантъ* № 95, 05.06.2013, стр. 1.

¹³⁷ Hellenic Republic Asset Development Fund. “3 investment groups submitted Expression of Interest for TRAINOSE”. [Press Release], September 16, 2013.

¹³⁸ 25.73% of its 10 million shares are traded on the Athens stock exchange since August 2001 and are in the hands of small and medium-sized investors. At this point, the Privatization Agency will hold 7.22% of the shares, most probably with a sale option after their value rises or to transfer them to the Thessaloniki municipality.

¹³⁹ Putin, V., “Greece and Russia: cooperation for peace and prosperity”. *Ekathimerini*, May 26, 2016.

¹⁴⁰ Φλουδόπουλου, Χ., “Τρεις και επίσημως οι μνηστήρες για ΟΛΘ”. *Capital*. March 25, 2017.

¹⁴¹ Deutsche Invest Equity Partners GmbH.

was signed in late March, 2018. DIEP paid EUR 109 million (47%), Terminal Link SAS, EUR 78 million (33.5%) and Belterra Investments Ltd – EUR 45 million (19.5%). Consequently, the 13% direct Russian interest in the port does not approach majority control of the port. Yet, it is likely that Savvidis will try to increase his share by buying shares from the retail investors through intermediaries, as well as acquiring 7.27% in shares under control by the Privatization Agency, if made available. It is likely that Savvidis may also seek to acquire DIEP's share, seeing as, like most private equity investment funds, DIEP may consider selling its investment at a profit. The result could be full Russian control over the port, unless, of course, the funds that DIEP had invested were not of Russian origin to begin with.

Russian companies have also shown interest in the construction, financing, operation and maintenance of a logistics center in Gkonos – this is the site of a former army barracks, which is not far from the port itself and includes a railway connection. The investment, which is estimated at EUR 215 million, would be in an international freight hub capable of servicing all kinds of transport – maritime and inland – and providing warehouses suitable for storing containers, swap bodies, bulk dry goods and fresh products (in refrigerated buildings), etc. Initially, only two companies applied – Savvidis' Belterra and the Russia-friendly GEK Terna. In both cases, Russia would have gained considerable influence over the logistics center and thus indirectly over the port. This placed the Greek government under pressure from its Western partners who realized that the country's two biggest ports were under the partial control of China and Russia. The discussion of the public tender of the project coincided with the expulsion of two Russian diplomats, something unprecedented in the history of Russian-Greek bilateral relations.

The diplomatic fall-out between the two countries led to a change in the terms of the tender, including that of the firm's stipulated level of required experience. The new conditions excluded the participation of the Belterra company, which was registered in 2016 and hardly had any commercial activity. As a result, as the deadline of the tender approached, Belterra and GEK Terna did not submit a bid.¹⁴²

¹⁴² The tender procedure for the concession of the Thessaloniki Port Authority was criticized heavily including by the US Ambassador, Geoffrey Pyatt, for the lack of transparency and the obscure origin of the funds. The port of Thessaloniki is of strategic importance to the United States for a number of reasons, including supply lines for the US base Bondsteel in Kosovo.

Alexandroupolis and Kavala

In the future, Russian corporate interests could also be directed to the other two small strategic ports in northern Greece – the port of Alexandroupolis and the port of Kavala. The former has acquired geopolitical significance for its proximity to two gas pipelines which ship gas from a source alternative to Russia – the ITG (the Greece Turkey gas interconnector) and TAP – as well as its proximity to the planned floating LNG regasification terminal. Although it is a provincial port, Alexandroupolis is well connected to the Greek railway network, as well as to Bulgaria and Turkey. The port can also be used as an alternative route if Turkey were to shut down the Bosphorus Straits. The Greek privatization agency has included the Alexandroupolis port in its third privatization phase of 10 ports across Greece, and it is next in line for immediate development alongside the ports of Kavala, Igoumenitsa, Corfu and Volos. But this phase has been delayed and no tender has yet been opened.

Since Russia's advocacy for the construction of the Burgas-Alexandroupolis oil pipeline in the mid-1990s, the Russian government has tried to develop strong bonds with the local government and the population. Russian municipalities, including that of the Crimea's capital, Simferopol, have been signing cooperation agreements and joint organized vacation initiatives. A new wooden Russian church was built, with current plans for the construction of a Russian cathedral.¹⁴³ In these efforts, Russia is heavily dependent on the activities of the local Russian speaking population, which has its own organization "The Russian House". Many of them are the so called Russoponti – former citizens of the Soviet Union with real or alleged Greek roots.¹⁴⁴ The Russian diplomats expelled in 2018 were well known in the port of Alexandroupolis and their activity in the city was the reason behind their expulsion.¹⁴⁵

¹⁴³ The fact that a Russian detachment liberated the town from the Ottoman occupation in 1878 is widely popularized, including their contribution to the city planning and the church and graves that they had left behind.

¹⁴⁴ Until 2001, more than 150,000 of them emigrated to Greece. They were invited by the Greek government in an attempt to change the demographic composition of Western Thrace where a considerable number of Greek and Bulgarian Muslims, as well as Turks live. Most of the Russoponti settled in Thessaloniki and Athens while in Western Thrace they live mainly in Alexandroupolis. Pontian cultural associations formed to keep their Russian heritage alive and act as political lobby groups for the community have also attracted funding in Russia's drive for influence in Greece.

¹⁴⁵ Hope, K., "Russia meddles in Greek town to push back the west". *Financial Times*, July 14, 2018.

The other port of Kavala is also part of the EU-led Source to Sea (S2S) initiative to build new railway connections while modernizing the existing ones between northern Greece, the Bulgarian Black Sea, and the Danube river ports. Despite its smaller size, the port of Kavala is the deepest of the ports in Northern Greece. Its neighbor is ELFE Fertilizers – the largest producer and supplier of fertilizers in SEE. This company has attracted the attention of the Russian firm, Stroygazmontazh – the largest construction company for gas pipelines and electrical power supply lines in Russia.¹⁴⁶ Stroygazmontazh was founded and is owned by the Russian businessman Arkady Rotenberg, who is among the richest 100 people in Russia and on the US sanctions list. According to a senior official from the Kavala Port Authority, the Russian company insisted in acquiring the fertilizer plant because of its independent port facilities.

* * *

There is a need for more political resolve and coordination on the part of European governments to counter the malign Russian influence in Europe. This is even clearer in the case of Southern Europe where the economic crisis has left fragmented societies vulnerable to political extremism. Meanwhile, Russia has been able to exploit the region's changing orientation toward international relations, particularly the West. This has augmented its effective, extensive penetration into Europe's economy that started three decades before the 2014 Ukrainian crisis.

In the case of Greece, Russia has tried to nudge or derail the country away from the orbit of Euro-Atlantic institutions by taking advantage of the severe backlash from the Greek public against the harsh austerity measures imposed by the EU. By its skillful deployment of limited resources and effective channeling of its economic presence, Russia has managed to preserve its inroads over the oil, gas and partially the electricity sector in Greece. Moreover, Russian state-owned companies like Gazprom have worked with local oligarchic networks to perpetuate long-term, inflexible supply contracts and to foster gas infrastructure projects aiming to block or at least limit diversification. Through lucrative contracts and enabling political access to Russia, the Kremlin has tried

to win over economically powerful and politically influential Greek families.

In the process, Russia has indirectly gained a foothold in strategic domestic industries such as natural gas, electricity generation, airport and seaport infrastructure, tourism, real estate and media. While this has not translated into a large corporate footprint by way of total economic shares or enormous foreign direct investments, it has created channels to target and influence some decision-making processes. In particular, Russia's attempts to hinder the settling of Greece's name dispute with neighboring North Macedonia demonstrated its willingness to exploit avenues to disrupt and harm NATO and EU countries. While this specific attempt has failed to achieve its intended results, it has also shown Russia's capacity (and limitations) to draw on a range of hard and soft power instruments to appeal directly to the Greek society and put pressure on internal politics. These are risks that Greece and its allies in the EU and NATO need to understand, monitor, and tackle.

¹⁴⁶ It was formed in 2008 by the merger of five companies under the control of Gazprom after their privatization. It still works very closely with the Russian gas monopoly and does most of the construction of new pipelines for its projects.

CYPRUS: ENGULFING THE OFFSHORE

KEY FINDINGS

The analysis of investment and financial flows related to the Russian economic influence in Europe reveals that many corporate ownership network chains developed by Russian companies have either started, passed through or ended up in Cyprus. The Mediterranean island has become – to an even greater extent than traditional tax treaty jurisdictions in Northern Europe – an intermediary hub for Russian funds to enter the Eurozone by the back door. Russia has seized opportunities to increase its influence in Cyprus by taking advantage of the country's existing lax preferential tax regulatory framework, governance gaps and institutional weaknesses, as well as its general financial instability. The expansion of Russian economic influence on the island state has made it a platform for enabling capital flows into the European financial system, some of which have been identified as illicit. This influence has manifested in several ways:

- Russia is by far the **biggest foreign economic player in Cyprus**, with significant presence in strategic sectors of the local economy. The Russian direct corporate footprint, i.e. the share of Russian companies' turnover out of the total turnover in the Cypriot economy, increased to more than 20% in 2017. By the end of 2018, Russian companies had invested more than EUR 45.1 billion in Cyprus – this totaled 12.4% of the total foreign direct investment in the country, or around 230% of the country's GDP that year.
- Most of the Russian investments in Cyprus are in **large, strategic sectors** whose interests are often closely interlinked with government policy. This is in part due to the growing intersection between economics and politics in Russia.
- **Banking and corporate services** in Cyprus are the sectors most vulnerable to Russian capture. Russian oligarchs have taken large shares in several Cypriot banks. The Cypriot financial system has also facilitated money laundering and tax avoidance activities by Russian individuals.
- Cyprus serves as the **largest offshore hub for Russian funds flowing into the Eurozone**. In the last two decades, about one-third of Russian FDI – both inward and outward – were from or to Cyprus, respectively. A large share of these flows are a result of round-trip investments: Russian investments are disguised as FDI by initially investing capital in a Cypriot-registered subsidiary, and then transferring it back to the country of origin as inward FDI.
- An unintended consequence of the post-2013 bail-in has been an **erosion of the independence of the Central Bank of Cyprus** – this has opened new avenues that may risk facilitating further Russian influence in the country.
- An intricate fusion between political elites and corporate service providers in Cyprus has made its offshore industry attractive for Russian companies with close ties to the Kremlin. This fusion has allowed Russia to

develop an unvirtuous cycle of state capture in Cyprus. In this cycle, its investments leave an enormous economic footprint, creating a political dependence that then further enables the expansion of the economic relationship.

- Cypriot legal firms have been able to successfully channel Russian economic interests in Cyprus and facilitate their integration within the larger European economy. This is the result of persistent **governance deficits in the application of anti-money laundering standards**, as well as the much broader problem of **endemic conflict of interests** in the country's key regulatory institutions.
- The Cypriot **golden visa program** has provided a legal avenue for Russian oligarchs and influence-peddlers to receive EU citizenship. Russians have also captured a major share of the luxury real estate market in Cyprus, which has often been the result of their acquisition of a visa or resident status in Cyprus.

THE BACKGROUND

The economic links between Cyprus and Russia have deep and complex historical roots. Even before the creation of the Republic of Cyprus in 1960, Moscow defended the rights of the Greek Cypriot majority by supporting Greece's advocacy for Cyprus' self-determination at the United Nations in the early 1950s, despite the opposition of London and Washington.¹⁴⁷ After gaining independence in 1960, the first president of Cyprus, Archbishop Makarios III, was dependent on the support of AKEL – the Progressive Party of the Working People – which had maintained close ties to Moscow. Over time, these political ties translated into more personal ties, as the pro-communist political elite in Cyprus sent their children to be educated in the Soviet Union. It has been argued that during the Cold War, Cyprus' geostrategic value made it “an apple of discord within NATO and a golden opportunity for the Soviet Union to exploit the Western Alliance's tensions and conflicts.”¹⁴⁸ It is very likely that Russia, under President Putin, would strive to maintain a similar position, in order to strategically exploit divisions in Cyprus.

Since the 1980s to the present day, over 50 treaties, protocols, and memoranda of understanding have been signed between Russia and Cyprus, regarding manifold forms of cooperation.¹⁴⁹ As the Soviet Union dissolved in December 1991, Cyprus was among the few countries to which Russians could travel without a visa. In the 1990s, during Russia's turbulent transition from a command to a market economy, Cyprus was both an accessible and attractive destination for Russians to store their financial assets. Meanwhile, Cypriot banks, accountants, tax planners, investment managers and lawyers were more than happy to receive Russian money and business.¹⁵⁰ Since the 2000s, the Russian economic influence in Cyprus has steadily increased, making the island a new Russian foothold in the Eastern Mediterranean.¹⁵¹ Unlike many other European countries, Cyprus is not too dependent on Russia in terms of

energy – instead, it has become increasingly reliant on storing and investing further Russian capital.

In 2011, Russia provided a USD 3.5 billion emergency loan to the Mediterranean island that was facing an imminent default on its debt to international creditors, risking billions of Russian individual and corporate local bank savings. The subsequent banking crisis in 2013 strained relations between the two countries, seeing as Cyprus was forced by its international creditors to bail in Russian funds deposited in domestic banks to save the country's financial system. Seven years on, Russian capital had not left the island as expected, and Russian businesses continue to use Cyprus as a preferred destination to park their funds – not only because of the favorable and lax tax regime, but also their lax banking regulations and the notorious lack of transparency regarding ultimate beneficial ownership. Moreover, Cyprus is one of the most frequented destinations for Russian tourists, and 40,000 Russians live permanently on the island out of a total population of 800,000. Unsurprisingly, a local Russian political party sprang up in 2017.

In late 2017, the President of Cyprus, Nicos Anastasiades, and Vladimir Putin signed an action plan consisting of seven economic and trade agreements, among which was a deal to ease rules for financial transactions involving Russian state-owned banks. While Mr. Anastasiades had considered dragging Russia into the talks for reunification of the Southern and Northern parts of the island, Russia has been secretly working to undermine a deal between the Greek and Turkish Cypriots, in the interest of maintaining the status quo. This would benefit Russia's geostrategic objectives of keeping the Eastern Mediterranean gas reserves underground and stirring tensions within NATO. Russia has also taken advantage of the current situation by using Cyprus as a back door to the European financial system while catering to Turkish interests in the Eastern Mediterranean, in order to preserve its long-term energy deals with Ankara. The Kremlin also avails itself of the island's strategic location in the region, especially for its war in Syria, prompting US officials to insist that the Cypriot government discontinue the practice of allowing Russia's navy to use its ports.¹⁵²

¹⁴⁷ Melakopides, C. “On the ‘Special’ Nature of the Russia – Cyprus Relationship”, *Russia in Global Affairs*, June 22, 2017.

¹⁴⁸ Melakopides, C., “The ‘Pragmatic Idealism’ of Russia's Post-Cold War Policy towards Cyprus”. *The Cyprus Review* 24, no. 1 (2012), 78.

¹⁴⁹ Melakopides, “On the ‘Special’ Nature of the Russia – Cyprus Relationship”.

¹⁵⁰ Christensen, J., “The story of a tax haven: Cyprus,” Tax Justice Network, October 26, 2017.

¹⁵¹ Delanoe, I. “Cyprus, a Russian Foothold in the Changing Eastern Mediterranean”. *Middle East Review of International Affairs* 17, no. 2 (2013): 84-93.

¹⁵² Cyprus News Agency, “US Repeats Call for Cyprus to Halt Visits of Russian Navy Vessels,” *CyprusMail*, May 1, 2020.

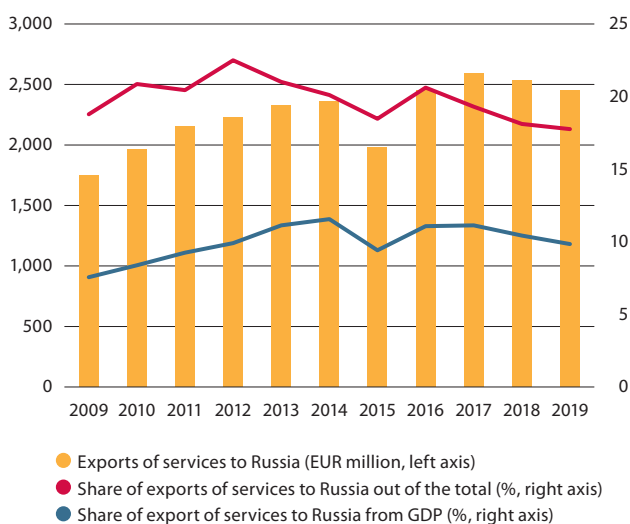
OVERVIEW OF THE RUSSIAN ECONOMIC FOOTPRINT

Trade dependence

Russia is by far the **biggest foreign player in Cyprus**, influencing large swathes of the island's economy. Unlike in many European countries whose energy sector has proven a visible and well-studied channel for Russian economic presence, the Russian footprint in Cyprus is concentrated in three other strategic sectors: banking and finance, real estate and tourism. Trade in financial and tourism services, in particular, has been the backbone of the bilateral economic relationship.

The export of services by Cypriot-registered companies to Russia – including the sale of hotel accommodation, financial brokerage, insurance and legal affairs management, among others – increased from around EUR 1.7 billion in 2009 to more than EUR 2.4 billion in 2019.¹⁵³ On average, the export of services to Russia has been around 20% of the total over the past decade with a peak of 22.5% in 2012 – a result of the island's status as Russia's main offshore financial hub. The consequent economic interaction between Russia-owned subsidiaries in both Cyprus and Russia shifts funds in both directions.

Figure 19. Cyprus export of services to Russia



Source: CSD calculations based on data from UNCTAD.

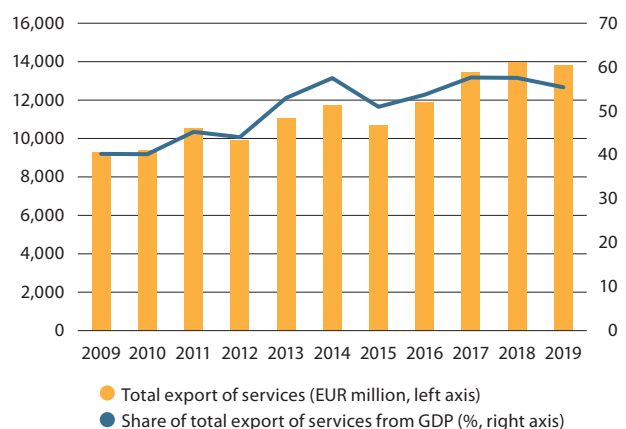
The services balance with Russia results in an enormous exposure for the small island's economy, as it comprises more than 10% of the country's annual

¹⁵³ The latest year for which statistics is available is 2019.

GDP. Any potential interruption in services trade with Russia would thus entail a macroeconomic shock that could easily trigger a balance of payments crisis.

The trade in goods between Cyprus and Russia is of secondary and much smaller importance – their total bilateral trade turnover was around EUR 200 million in 2017. Nevertheless, this amount was still four times that of 2008. The most important item in the Cypriot goods trade basket with Russia is the import of mineral fuels, namely oil derivatives – these add up to around half of all total goods imported in the past decade. Although Cyprus' domestic consumption of oil products is 100% dependent on imports, less than 5% of these come from Russia. In addition, Cyprus' close proximity to the Middle East allows for a more diversified oil import portfolio.¹⁵⁴

Figure 20. Cyprus dependence on export of services



Source: CSD calculations based on data from UNCTAD.

Although energy does not play a major role in the Russian economic footprint in Cyprus, it may become a future bone of contention. As US and European oil and gas companies get ready for large-scale exploration and production in the Eastern Mediterranean – specifically in the exclusive economic zone of Cyprus – they have met strong resistance from Turkey that has rejected any foreign presence in the marine territory controlled by the Northern Cypriot government. This could also provide Russia with a possible lever as it seeks to limit gas diversification efforts in the Eastern Mediterranean. Turkey has occupied a third of the island of Cyprus since 1974. As a consequence of this divided status, potential major oil and gas field developments hinge on the issue of Cypriot unification and the international recognition of its territorial waters.

¹⁵⁴ CSD calculations based on statistics from Eurostat.

Obstacles to energy diversification

For years, Russia has implicitly backed Turkish objection to oil and gas drilling in Cypriot waters – this has delayed the work on the giant Aphrodite natural gas field with estimated reserves of around 8 trillion cubic feet (around 235 billion cubic meters). This opposition could prevent or slow down the development of similar fields, such as the recently discovered Glaucus-1 well – the largest gas discovery near Cyprus so far. In addition, Turkish military vessels have regularly harassed exploration drilling ships in the region, heightening risks to potential financial commitment by investors.

These limitations imposed on the development of Cyprus' oil and gas capacity benefit Russian geopolitical interests in preventing the diversification of natural gas supply to the EU – in particular to Southeast Europe, which has been one of the regions most dependent on Russian gas supplies. This conflicts with European efforts toward building a Mediterranean natural gas hub. This hub would include a 1,900 km East Med gas pipeline linking gas resources in Israel, Cyprus and Egypt with continental Europe via Greece.

The current situation is creating additional tensions between Cyprus and Turkey while threatening to become a major security issue for the EU and NATO. In July 2019, Turkey's dispatching of two drilling ships to waters off the coast of Paphos heightened tensions regarding Turkish involvement in the Cypriot oil and gas sector. There have been, moreover, unconfirmed reports that the Turkish vessel *Fatih* discovered natural gas deposits totaling an estimated 170 billion cubic meters. On 15 July 2019, the EU, in solidarity with Cyprus, announced sanctions against Turkey. These included cutting EU funds, suspending negotiations on the *Comprehensive Air Transport Agreement*, and ceasing top-level talks on business and trade-related issues. Despite this, Ankara announced, following the EU decision, that it would continue its controversial drilling operations, in addition to sending two more ships to the area for more exploratory drilling. The exploration vessels were accompanied by the Turkish navy in order to ramp up pressure on existing U.S. and European oil and gas companies.¹⁵⁵

Russia has solidified its future involvement in energy exploration and development around Cyprus. The

strategy involved linking a potential gas revenue sharing agreement between Greek and Turkish Cypriots to the resolution of the Cypriot problem. While this prevents new East Med gas from becoming a potential future competitor to the Russian supply in Europe, it adds another layer of complexity to the Cypriot conflict.

Russia's investment back office

Strong investment ties between Russia and Cyprus point to the latter's excessive financial exposure to the Russian market. Russia is by far the biggest foreign investor in Cyprus – its inward FDI stock has more than doubled from EUR 15.9 billion in 2008 to over EUR 45.1 billion by the end of 2018.¹⁵⁶ This represents 12.4% of the total FDI stock in Cyprus, and over 230% of the island's nominal GDP. A comparison between the data from the Central Bank of Cyprus to that of the Russian central bank reveals that the degree of Cyprus' investment exposure to Russia is probably much higher. According to the Russian central bank, Russian FDI stock in Cyprus had reached EUR 189 billion by the end of September 2019 – an amount equivalent to 49.8% of combined Russian FDI abroad.

It is likely that the Russian central bank data more accurately reflects the situation on the ground. The Russian central bank data includes FDI for all companies with ultimate beneficial ownership in Russia. This may encompass equity and debt operations in Cyprus involving companies with non-Russian residence, but with Russian beneficial ownership.¹⁵⁷ In contrast, the Cypriot central bank data only reflects Russian investments that come from companies registered in Russia. For example, if a Russian subsidiary in the Netherlands reinvests profits from its activities in Cyprus, the Russian central bank would register this as Russian FDI flow into Cyprus. In contrast, the Cypriot central bank would count it as Dutch investment. Usually, central banks in the EU take into account foreign direct investments transiting through intermediaries operated by the subsidiaries of the main company, rather than originating from the ultimate beneficial owner.

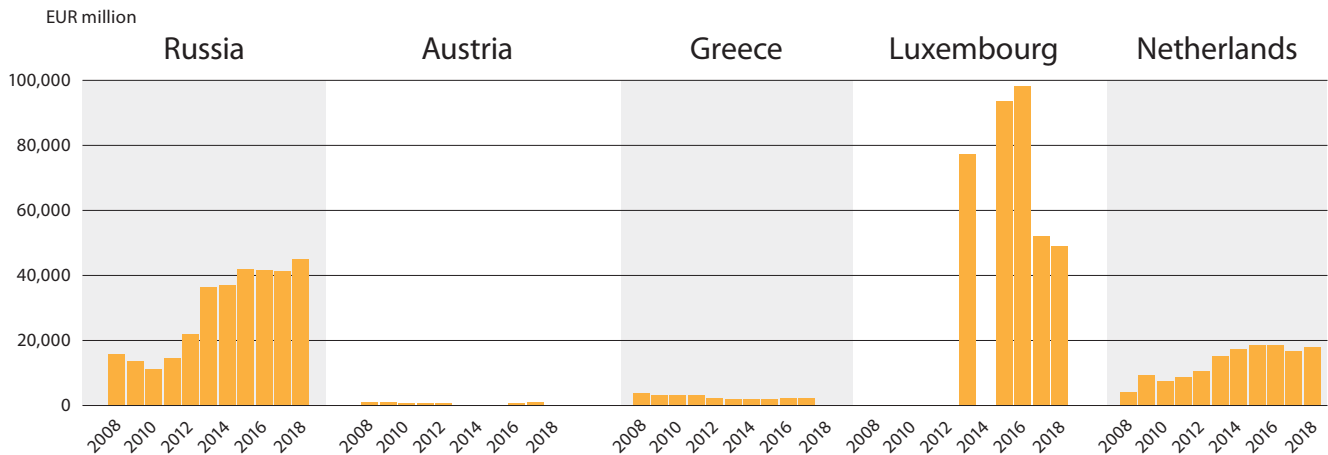
At present, Cyprus serves as the **largest offshore hub for Russian funds flowing into the Eurozone**. In the

¹⁵⁵ Johnson, K., "Turkey's Big Energy Grab". *Foreign Policy*, July 25, 2019.

¹⁵⁶ The latest available data from the Central Bank of Cyprus is from 2017.

¹⁵⁷ Methodology for measuring foreign direct investment used by the Russian central bank.

Figure 21. Cyprus inward FDI stocks from selected countries



Source: Central Bank of Cyprus.

last two decades, about one-third of Russian inward and outward FDI were from or to Cyprus, respectively.

A large share of these flows have been formed by **round-trip investment**, where Russian investments are disguised as FDI by first investing capital in a Cypriot-registered subsidiary and then transferring it back to the country of origin as inward FDI.¹⁵⁸ The main reasons for capital round-tripping via offshore jurisdictions, as in Cyprus, include tax avoidance and evasion, money laundering and the protection of assets vulnerable to nationalization and expropriation by the states where the capital originates.¹⁵⁹

Business experts in Cyprus note that the country's financial system effectively acts as a back office for Russian companies. Business is easier to conduct in Cyprus than in Russia in terms of rule of law, legal standards, banks, access to international professionals and so on. Consequently, most bookings are performed through Cyprus. Services that are exported from Russia to the EU are often first sold to a Cypriot (Russian controlled) company (at the lowest possible price), before they are re-sold on to their destination

(at market price). This exempts Russian exporters from paying the full amount of taxes imposed (on the majority) of their profits. In addition, many Russians have their wealth placed in Cypriot banks and financial institutions.¹⁶⁰

Russian shell entities, including those in Cyprus, are often layered in an intricate network that conceals the identity of the ultimate beneficial owners. Nominee and bearer shares can be used in tandem with shell entities to optimize concealment. Accountants, lawyers, as well as trust and company service providers facilitate and promote the abuse of shell entities by lawbreakers.¹⁶¹ However, following the financial crisis in 2013, Cypriot commercial banks have been prohibited by law to take shell companies as their clients. This has markedly decreased the potential to exploit Cyprus for such purposes.

It is likely that Russian companies also use offshore jurisdictions like Cyprus for tax avoidance and tax evasion purposes. However, it is unlikely that Russian investors utilize round-tripping schemes for gaining access to financial incentives allotted to foreign investors in Russia. This is because the country is better known for its restrictions, rather than its incentives to foreign investors.

This round-tripping investment pattern is clearly visible in the statistics reflecting Cypriot outward FDI

¹⁵⁸ IMF 2004. *Annotated Outline for the Revision of BPM5*. IMF, April 2004; Coe, N. M., Lai, K. P., & Wójcik, D., "Integrating finance into global production networks". *Regional Studies* 48, no. 5 (2014), 761-777; Ledyeva, S., Karhunen, P., Kosonen, R., & Whalley, J., "Offshore foreign direct investment, capital round-tripping, and corruption: Empirical analysis of Russian regions". *Economic Geography* 91, no. 3 (2015), 305-341.

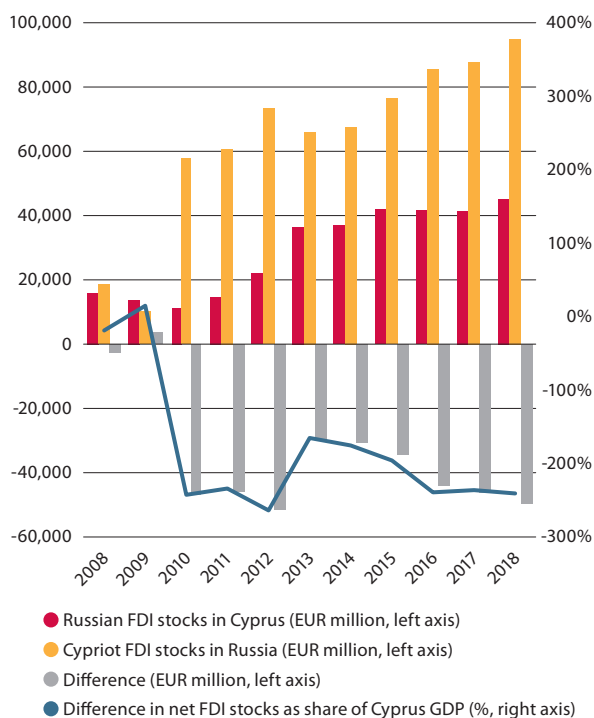
¹⁵⁹ Round-tripping is a specific case of pass-through funds that involves funds from an entity in one economy, i.e. host economy, being invested in an entity resident in a second economy, i.e. routing economy, then having them reinvested in an entity in the first economy (6.46, BPM6; 467, OECD benchmark definition of FDI 4-th edition).

¹⁶⁰ Christensen, "The story of a tax haven: Cyprus,".

¹⁶¹ Pacini, C., W. Hopwood, G. Young and J. Crain, "The role of shell entities in fraud and other financial crimes", *Managerial Auditing Journal* 34, no. 3 (2019): 247-267.

stock. This set of statistics closely approximate that of inward FDI (see Figure 22). With the exception of the 2010 – 2012 period preceding the banking crisis, inward and outward FDI stocks were more or less equal.

Figure 22. Round-tripping investment between Cyprus and Russia



Source: Central Bank of Cyprus.

Cyprus' enormous dependence on Russian FDI compounds the macroeconomic imbalance caused by the country's current account exposure. Even before the banking crisis in 2012, the European Commission had pointed to the emergence of a rapidly growing trade deficit, as well as persistently high current account deficits in Cyprus. These current account deficits were financed mainly through foreign direct investment inflows (including reinvested earnings and undistributed profits of firms with foreign shareholdings based in Cyprus). From 2010 to 2012, the massive outflow of Russian investment worth around EUR 75 billion deepened the impact of the severe banking crisis that followed. The Russian capital outflows caused a crunch in the sources of financing for domestic investment and dried up the operations of banking liquidity servicing companies. Following the crisis, inward FDI stocks have crept up again, rising by around a third from 2014 to 2018. However, the outflow of capital has accelerated. This signals, on one hand, the partial de-offshorization of Russian business capital, and on the

other, the growing use of Cyprus as an offshore-sink for capital movements coming from other more traditional tax jurisdictions such as the Netherlands, Switzerland and the British Virgin Islands. The Netherlands and the BVI, in particular, have been preferred destinations in which to register Russian company subsidiaries operating or investing within the European Economic Area and the Eurozone. Both countries have invested roughly EUR 36 billion in Cyprus over the last decade.

It is likely that most of the capital outflows to Russia at that time were related to large-scale oligarchic operations, rather than to the repatriation of funds owned by ordinary Russian citizens. As these companies were served by corporate service providers with ties to the political establishment and law firms, it is likely that they could have acquired insider information about the goings-on in the banking sector. Just before the banking crisis and subsequent imposition of the capital controls in March 2013, more than EUR 3.6 billion in (probably uninsured) deposits belonging to large Russian corporations (obscured behind a network of shell companies) were withdrawn in 5,323 transactions.¹⁶² These operations were preceded by an outflow of EUR 2.6 billion in January and February. The capital outflows, however, had begun much earlier in 2010, roughly around the time Russia provided a EUR 2.5 billion loan to Cyprus. In the next two years, around EUR 20 billion in Cypriot banking assets were withdrawn.¹⁶³

The repatriation of Russian-owned banking assets from Cyprus could have been additionally influenced by the Russian government strategy of "de-offshorization". This strategy aims to retrieve Russian capital back to special economic zones in Russia after the global economic crisis in 2009. The new legal framework for tax reporting pushed Russian investors using Cyprus as an offshore base to reinvest back in Russia, rather than recycling the capital back into the home country.¹⁶⁴ This is illustrated in Figure 22, which shows a surge of Cypriot FDI stock in Russia after the banking crisis in Cyprus.

¹⁶² Grey, S., Kambas, M., and Busvine, D., "Insight: Bank documents portray Cyprus as Russia's favorite haven," *Reuters*, May 16, 2013. The investigation points to some of the largest Russian companies owned by oligarchs with close ties to Kremlin moving hundreds of millions in deposits in the last months before the crisis erupted.

¹⁶³ Zhukov, Y. (2013). "Cyprus and Russia Did Not Just Break Up: Why Moscow Is Playing the Long Game on the Island of Aphrodite." *Foreign Affairs*, March 29, 2013.

¹⁶⁴ Aykut, D., Sanghi, A., & Kosmidou, G. (2017). *What to do when foreign direct investment is not direct or foreign: FDI round tripping*. Policy Research Working Paper 8046, The World Bank.

Box 10. The role of Russian banks in the banking crisis

The main reasons for the 2012 – 2013 crisis include Cypriot banks' excessive risk-taking in the period 2004 – 2010. The banks operated in a relatively lax regulatory environment that suited the country's ruling elite. This compromised financial industry service professionals, politically-connected law firms, property developers, as well as the Greek Orthodox Church that maintained significant business interests, including ownership of banks and other enterprises. Moreover, Cypriot banks offered deposit rates that were significantly higher than those of their European peers¹⁶⁵ – the spread for new deposits fluctuated around 2.0-2.5% p.a. in 2009. As a result, the banking sector doubled in size largely as a result of the inflow of money from high-risk jurisdictions including Russia, Ukraine, other former Soviet republics and the Middle East.

Laiki and Bank of Cyprus – the country's two largest banks – had been hosting the largest amount of Russian deposits. However, Cyprus lost access to the international financial markets a few months before the commencement of Greek debt restructuring – this was because markets could see that the government might find it difficult to bail out its oversize banking system given its large exposure to Greece. Despite this, Cyprus' left-wing government was reluctant to apply to Europe and the International Monetary Fund (IMF) for financial assistance. Instead, it managed to secure a EUR 2.5 billion bilateral loan from Russia. This allowed the government of Dimitris Christofias to postpone the inevitable until June 2012, when Fitch joined other credit rating agencies to downgrade Cyprus bonds to junk.¹⁶⁶ In June 2012, the government was forced to apply for a troika program in order to recapitalize Laiki and Bank of Cyprus.

Cyprus' economic adjustment program – reluctantly accepted by the new government – included very harsh terms that implicated the creditors of the island's two largest banks. Shareholders and bondholders in both banks were wiped out, leading to cries of foul play and public attacks on the whole continent by the Archbishop (in addition to losing control of the Hellenic Bank, the church suddenly saw its shares in Bank of Cyprus completely wiped out). Laiki was subsequently split into a good bank and a bad bank; uninsured depositors remained in the bad bank. The good part of Laiki was merged into Bank of Cyprus that was recapitalized through a bail-in of uninsured depositors. This protected the country's public finances, seeing as the government was spared around EUR 8 billion. This made sense from an economic, and arguably social, point of view – the poor, taxpayers, small savers and future generations were spared from the cost of the banks' failure. It also served to placate the opposition in Germany. The decision presented Angela Merkel as attempting to bail out rich Russians who had parked their "dirty" money in Cypriot banks with German taxpayers' money. In the end, indeed about EUR 4 billion of Russian deposits were bailed-in¹⁶⁷ but these were mainly done by the smaller depositors.¹⁶⁸

Cyprus remains a choice destination for Russian off-shore financing (the reasons why this is the case are discussed below). Although one would expect that the post-crisis restructuring of the Cypriot banking sector would make it less attractive as a haven for Russian capital, the facts say otherwise. Russian inward FDI stock in Cyprus dropped by around a third in 2014 before bouncing back to levels higher than before the crisis.

Following the major outflow of FDI in 2010 – 2012, round-tripping has been suppressed due to several concurrent changes in the economic and regulatory environment. One such change has been the introduction of new, much stricter anti-offshore legislation in Russia that came into force on 1 January 2015. The other reason has been the economic crisis in Russia. The crisis resulted from a confluence of factors, including

¹⁶⁵ The spread between average interest rates on new deposits in Cyprus and the rest of the euro area fluctuated around 2%.

¹⁶⁶ The loan was restructured in 2013, the year of severe banking crisis in Cyprus, under the current administration of President Nicos Anastasiades. The loan's repayment period was extended to 2021 and the interest rate was cut to 2.5% from 4.5%.

¹⁶⁷ See "Aid to Cyprus Could Benefit Russian Oligarchs", *Spiegel Online*, November 5, 2012. For a more general overview of these events see Demetriades, P. (2017). *A Diary of the Euro Crisis in Cyprus: Lessons for Bank Recovery and Resolution*, London: Palgrave-Macmillan.

¹⁶⁸ There were some notable exceptions. For example, the largest BoC shareholder, a Russian, is estimated to have lost EUR 400 – 500 million.

U.S./EU sanctions against Russia after the Ukraine invasion, the sharp decline of international oil and gas prices and the fall in corporate profits.

The crisis did not affect only cross-border investment flows with Cyprus, but also the overall investment climate in Russia. Total FDI flows into Russia fell almost three-fold from EUR 20 billion in 2014 to around EUR 7 billion in 2018. Last but not least, Cyprus' own financial crisis led to the repatriation of billions in Russian deposits from some of the country's largest banks. Between 2012 and 2019, Russian bank deposits in Cyprus declined by EUR 14.67 billion down to EUR 6.87 billion in the first quarter of 2019.¹⁶⁹

An offshore haven?

Cyprus's significant role in the offshorization of Russian capital flows raises the question as to why Russian entities seem to have shown a preference for Cyprus, among other countries which provide similar financial services (the British Virgin Islands, the Bahamas, Bermuda, Switzerland, and the Netherlands, among others). To answer this question, this analysis looks at several offshore jurisdictions with respect to the two main reasons for utilizing offshore financial centers (OFCs) – tax/regulatory arbitrage and secrecy arbitrage.¹⁷⁰

Tax and regulatory arbitrage

At first glance, low taxes are not Cyprus' main advantage in attracting Russian funds (Table 2). Basic corporate taxes in Cyprus are not much lower than in Russia. Hence, the routing of money via the offshore jurisdiction for the purposes of tax avoidance and evasion is ineffective – Cyprus cannot compete with such offshore jurisdictions as British Virgin Islands, Bahamas, Bermuda and the Cayman Islands. Rather, Cyprus competes mainly with other European countries, which are often considered OFCs – namely Swit-

zerland, the Netherlands and Luxembourg. Compared to them, Cyprus indeed has lower taxes, but the difference is not large enough to justify the associated transaction and regulatory costs.

What makes Cyprus attractive in terms of its tax regime is that while it is not officially an offshore zone, it nevertheless offers some of the lowest corporate tax rates in Europe (12.5%). In addition, its incorporation rules are quite flexible, as there is no minimum capital requirement and nominal ownership status. The concealment (at least to the public) of the true owners of assets is still widely practiced. By starting a company in Cyprus, the owner acquires an EU VAT number which allows the firm to legitimately conduct business all around Europe. Probably the most important factor is that until October 2014, Cyprus was not a signatory to the Multilateral Competent Authority Agreement that mandated the automatic exchange between the EU and national investigative authorities of financial information about suspicious accounts. This meant that bank account information linked to a Cypriot company would not be subject to cross-EU probes.

Apart from the EU status obtained by Cypriot companies, they gain from the maximum number of tax haven benefits offered in typical OFCs, including 0% withholding tax rate on dividends, accrued interest from cross-border debt operations, branch remittances and on royalties from patents. The preferential tax treatment of dividends and interest revenue. These factors are key for the Russian businesses that have set up shell companies (usually as holding firms) in Cyprus. Moreover, Russian majors, almost all of whom have close ties to the Kremlin, have registered subsidiaries in Cyprus for tax optimization purposes and for obfuscating corporate ownership.

As a result, Cyprus has *de facto* become a giant vault of these companies' profits from their business operations across Europe. Specifically, it plays a central role as the end destination or a sink-OFC¹⁷¹ for rerouted profits from other conduit tax jurisdictions, such as the Netherlands. Cyprus, predictably, is the biggest receiver of Russian funds, as well as the largest sink-OFC in Europe, together with Luxembourg. Mean-

¹⁶⁹ See Charalambous, A., "Further shrinking of Russian deposits in Cyprus banks", *In-Cyprus*, May 29, 2019.

¹⁷⁰ Tax/regulatory arbitrage enables firms to significantly decrease their tax burden by rerouting their profits via offshore jurisdictions with low or zero taxes. Secrecy arbitrage refers to the relative ease companies have in obfuscating the identity of the corporate ownership. This is important if the capital has an illegal origin (proceeds of corruption or illegal activities) or if the capital owner faces prosecution in his/her home country (For details see Ledyeva et al., op.cit. 2015).

¹⁷¹ The OFC Meter of the University of Amsterdam identifies two types of OFCs. Sink-OFC (such as Cyprus) is a jurisdiction in which a disproportional amount of value disappears from the economic system. Conduit-OFC (such as the Netherlands) is a jurisdiction through which a disproportional amount of value moves toward sink-OFCs.

Table 2. Cyprus corporate taxes compared with other offshore jurisdictions popular with Russian (round-trip) investors, 2018

Jurisdictions: Russia vs Offshore	Corporate tax	Capital gains tax rate	Branch tax rate	Withhold- ing tax: Dividends	Withhold- ing: Interest	Withholding: Royalties from patents, know-how, etc.	Withhold- ing: Branch remittance tax
Russia	0 / 15.5 / 20	0 / 15.5 / 20	15.5 / 20	0 / 13 / 15	15 / 20	20	0
Cyprus	12.5	20	12.5	0	0	0 / 5 / 10	0
British Virgin Islands	0	0	0	0	0	0	0
Bahamas	0	0	0	0	0	0	0
Bermuda	0	0	0	0	0	0	0
Cayman Islands	0	0	0	0	0	0	0
Seychelles*	33	0	33	15	0 – 33	15	0
Switzerland	12 – 24	No standard rates	12 – 24	35	0 – 35	0	0
Netherlands	25	25	25	15	0	0	0
Luxembourg	18	18	18	0 – 15	0 – 10	0	0

* Data for Seychelles is for 2017.

Source: *Worldwide Corporate Tax Guide of Ernst & Young, 2018.*

while, the Netherlands is the main conduit of funds between European countries and Cyprus.

Once in Cyprus, the holding company's two main incomes – including dividends sent from Russian subsidiaries across Europe or the profits from the sale of equity – are not taxable. In addition, onward payments to non-Cypriot residents are not subject to withholding taxes – this means that ultimately, profits can be returned tax-free to Russia due to the Russian participation exemption rule.¹⁷² Alternatively, in order to avoid the scrutiny of Russian tax authorities, they can be returned to a classic offshore haven such as the British Virgin Islands, using trusts as the shareholders of the company.

Regarding financial flows in the opposite direction, namely from Russia, the *Double Tax Treaty* between Russia and Cyprus allows Russian companies to invest in the EU via Cyprus at a lower tax cost. Financial

transfers from Russia to Cyprus thus avoid or enjoy much-reduced Russian withholding taxes (there is a 5% dividend withholding tax). Cypriot subsidiaries of Russian entities can then transfer funds to a third company in or outside the EU via a debt instrument. The interest accrued in these transactions then benefits from a reduced or even 0% withholding tax (Figure 23).

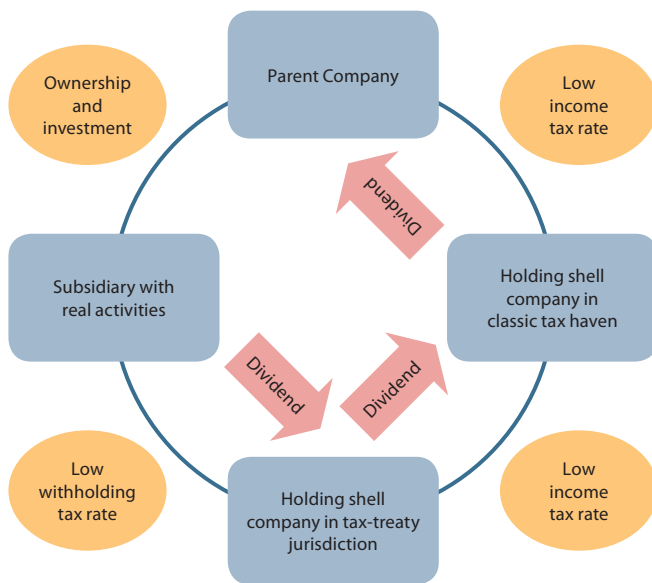
The preferential tax treatment of inward and outward financial flows from Russia to Cyprus comes as a direct result of the *Double Tax Treaty* between the two countries. The treaty, which dates back to 1998, is considered one of Russia's most enabling in terms of tax optimization. It was reinforced by a new protocol immediately after the banking crisis in 2013, enhancing the enabling environment with two critical provisions:

- The removing of Cyprus from the so-called "blacklist" of offshore jurisdictions, allowing Russian companies with subsidiaries in Cyprus to send dividends to apply for participation exemption;¹⁷³

¹⁷² A participation exemption rule relates to the cancellation of the taxation of a shareholder in a company on its dividends received and the potential capital gains arising from the sale of shares. The participation exemption aims to avoid the double taxation of both profits and accrued dividends allocated to shareholders, and is usually a major aspect of preferential double taxation treaties.

¹⁷³ To qualify for the participation exemption with regard to dividend income, a Russian company must hold a participation of at least 50% in the Cypriot company for at least 365 days in a calendar year. A foreign investee must not be a resident in a "blacklist" jurisdiction.

Figure 23. Tax avoidance scheme through tax-treaty jurisdictions and classic tax havens



Source: CSD based on PROFUNDO Case Study on Dutch Banks and Tax Avoidance.

- The introduction of a revised, stricter Exchange of Information article¹⁷⁴ – this would further promote transparency and information exchange in relation to taxation matters, to the benefit of Russian authorities.

The treaty's 2013 amendments did not eliminate the beneficial withholding tax rates for dividends (5% on investments above the qualifying threshold and 10% otherwise), interest (0%) and royalties (0%). However, in 2020, Russia forced Cyprus to amend the treaty to limit the withholding tax exemption only to corporate and eurobonds and to Russian regulated and publicly-listed companies. All other Russian-owned businesses registered in Cyprus will be subject to a higher 15% withholding tax. The amendments demonstrate Russia's leverage over Cyprus' policy-making but are unlikely to lead to substantial changes in corporate behavior.

Secrecy arbitrage

The level of financial secrecy is another reason for which the Cypriot financial system is attractive as a destination for round-tripping investments and the offshorization of Russian assets. It seems that Cyprus does not have more problems with the lack of transparency than its

competitors (Table 3). In fact, it seems to have a lower level of secrecy than many of its European counterparts, as well as Russia. However, a closer look at the regulatory framework and the practice for corporate ownership transparency in Cyprus may show why the island might be preferred by Russians compared to other places.

Beneficial shareholders in Cyprus very often keep their identities confidential through the use of nominee shareholders and directors on the Cypriot side of the corporate structure. The enormous Cypriot banking exposure to Russian entities can be explained by the attractiveness of the country's corporate ownership regulatory framework. Opening a bank account in Cyprus is easy and straightforward, and does not require the presence of the company's real owners. It suffices that a signed and notarized power of attorney is submitted by a local corporate service provider.¹⁷⁵ In order to register a company in Cyprus, only one shareholder and one director are required, with no restrictions on foreigners being managers of the entity.

Cyprus is among the set of offshore zones with the lowest secrecy scores (Table 3) – this is related to a number of legal and governance loopholes that allow the concealment of corporate information.¹⁷⁶ These loopholes have transformed Cyprus into a jurisdiction with significant financial secrecy opportunities.¹⁷⁷ The most important factors include:¹⁷⁸

- the right of companies with business activities not based in Cyprus, despite being registered in the country, not to keep accounting and financial records;
- the existence of unidentified owners through the use of bearer shares;
- the prevalent use of trusts to obfuscate the real ownership;
- unclear book-keeping rules for trusts.

Following the 2013 financial crisis, the European Stability Mechanism (ESM) commissioned a report re-

¹⁷⁵ Georgiades, Y., "Key Benefits of Company Formation in Cyprus", May 25, 2017.

¹⁷⁶ Which is more than can be said for the confidentiality of government information: "In late 2018 that hackers allegedly linked to the Chinese People's Liberation Army were able to download years' worth of EU diplomatic cables via an entry point in the Cyprus foreign ministry." Peel, M., "Moscow on the Med: Cyprus and Its Russians," *FT Magazine Life & Arts*, May 15, 2020.

¹⁷⁷ Tax Justice Network. (2018). *Narrative Report on Cyprus. Financial Secrecy Index 2018*.

¹⁷⁸ OECD (2012). *Global Forum on Transparency and Exchange of Information for Tax Purposes Peer Reviews: Cyprus 2012: Phase 1: Legal and Regulatory Framework*. Tech. rep. OECD Publishing.

¹⁷⁴ In line with Article 26 of the OECD Model Treaty for the exchange of information for tax purposes.

Table 3. Cyprus secrecy and anti-money laundering indices compared with other offshore jurisdictions, 2018

Offshore jurisdictions	Secrecy score	Financial secrecy index score	Financial secrecy index rank	Anti-money laundering index, score/ranking
Russia	64	361.15	29	5.83 / 47
Cyprus	61	404.44	24	5.01 / 80
British Virgin Islands	69	502.75	16	NA
Bahamas	84	429	19	NA
Bermuda	73	281.82	36	NA
Cayman Islands	72	1,267.68	3	NA
Seychelles	75	125.26	77	NA
Switzerland	76	1,589.57	1	5.33 / 64
Netherlands	66	598.8	14	4.9 / 88
Luxembourg	58	975.91	6	5.11 / 76
USA	60	1,298.47	2	NA

Note: The Financial Secrecy Index is a ranking of jurisdictions based on combining a qualitative measure (a secrecy score, based on 20 secrecy indicators) with a quantitative measure (the global weighting to give a sense of how large the offshore financial center is). The secrecy score and the weighting are arithmetically combined using special formula – the cube of a jurisdiction's secrecy score is multiplied by the cube root of its global scale weight, yielding the final score.

Source: Tax Justice Network; Basel AML index 2018.

garding the corporate ownership and money laundering loopholes in the Cypriot system. The assessment revealed glaring loopholes in the process of implementing anti-money laundering rules in six of Cyprus' largest banking institutions. These include the failure of banking officials to evaluate the business profile of the companies opening accounts and so assess the real corporate ownership.¹⁷⁹ The report concluded that on average, 10% of the customers surveyed were politically exposed persons (PEP), and more than half of the customers were assessed as high-risk.¹⁸⁰ In addition, less than a quarter of all companies had been regularly submitting annual financial reports. Moreover, 70% of the cases with complex corporate networks had nominal owners – in these cases, the true identities of beneficial owners were regularly left indeterminate by banks.

Despite the discovery of a number of suspicious transactions during the assessment, there have barely been any internal bank investigations for possible money-laundering. Ultimately, the findings have shown that regulatory institutions (e.g. the Central Bank of

Cyprus and the Financial Crimes Unit – MOKAS) have persistently failed to implement the provisions of the law. This has resulted in the failure to ensure adequate and timely exchanges of financial information related to possible money-laundering cases.

Over the next 5-6 years after the banking crisis, the Cypriot government tried to address the anti-money laundering deficits by introducing a number of legal changes ensuring transparency of incorporation, including that of the ultimate beneficial ownership of trusts. The conducting of customer due diligence, the raising of reporting standards and the operation of financial intelligence together aim to stem the widespread tax evasion and money-laundering practices plaguing the country's financial system. However, whether these will change the reality on the ground remains to be seen – what is pivotal in Cyprus is not the imposition of rules per se but their lax, non-existent or discretionary implementation.

¹⁷⁹ Moneyval and Deloitte. (2013). *Cyprus – Effective implementation of customer due diligence measures – level of implementation of preventive measures by financial institutions – summary report of main findings*.

¹⁸⁰ Ibid.

Box 11. Assessing Cyprus' financial secrecy

A more detailed analysis of the structure of the financial secrecy score might shed light on the relevant advantages of Cyprus such as more limited requirements for corporate and wealth ownership transparency, as well as for the disclosure of corporate accounts. The score consists of 20 subcomponents, which, weighted, produce a result measured in percentage with zero score indicating no secrecy and 100% indicating full secrecy. The figure below shows the 2018 scores of all subcomponents for Cyprus compared to that of the United States, the British Virgin Islands and Switzerland – the main non-EU and EU competitors of Cyprus for Russian offshore money.

Secrecy score's subcomponents for Cyprus, United States, BVI and Switzerland, 2018

		Cyprus	USA	Switzerland	BVI
Ownership registration 	1. Banking secrecy	50	20	75	40
	2. Trusts and foundations register	38	50	100	50
	3. Recorded company ownership	100	100	100	75
	4. Other wealth ownership	100	100	88	50
	5. Limited partnership transparency	100	100	100	100
Legal entity transparency 	6. Public company ownership	100	100	100	100
	7. Public company accounts	100	100	100	100
	8. Country-by-country reporting	75	100	100	100
	9. Corporate tax disclosure	100	100	100	50
	10. Legal entity identifier	75	75	100	100
Integrity of tax and financial regulation 	11. Tax administration capacity	63	15	75	100
	12. Consistent personal income tax	100	0	75	75
	13. Avoids promoting tax evasion	40	40	100	100
	14. Tax court secrecy	50	25	75	100
	15. Harmful structures	50	50	75	75
	16. Public statistics	30	30	30	100
International standards and cooperation 	17. Anti-money laundering	29	37	38	33
	18. Automatic information exchange	19	100	77	25
	19. Bilateral treaties	0	28	0	0
	20. International legal cooperation	7	27	24	0

Source: Tax Justice Network.

From the graph, it can be seen that Cyprus' regulatory framework does not allow for much more financial secrecy in any subcomponent, compared to BVI and Switzerland. However, Cyprus allows for much greater secrecy than the British Virgin Islands in several important sub-dimensions including in other wealth ownership and corporate tax disclosure, as well as in banking secrecy, recorded company ownership and international legal cooperation. Moreover, Cyprus has maximum possible secrecy (100%) in seven subcomponents including:

Recorded company ownership. This indicator assesses whether a jurisdiction requires all available types of companies (not listed on a public stock exchange) to submit information and their relevant updates on beneficial/legal ownership to a governmental authority.

Other wealth ownership: This indicator assesses the ownership transparency of real estate and of valuable assets stored in free ports.

Limited partnership transparency. This indicator assesses: (i) whether a jurisdiction requires all types of limited partnerships to disclose their ownership online, and (ii) whether all limited partnerships are required to file annual accounts with a government authority.

Public company ownership. This indicator considers if a jurisdiction requires all available types of companies with limited liability to publish updated beneficial/legal ownership information through public records freely accessible online.

Public company accounts. This indicator considers whether a jurisdiction requires all available types of companies with limited liability to file their annual accounts with a governmental authority/administration, and to make them accessible online free of charge.

Corporate tax disclosure. This indicator assesses: (i) whether a jurisdiction ensures its own access to the CbCR (global country-by-country reports in compliance with OECD BEPS Action 13) of any relevant (with over 750-million-euro global consolidated turnover) foreign multinational enterprises with domestic operations, and (ii) whether all unilateral cross-border tax rulings are published online.

Consistent personal income tax: This indicator assesses whether personal income tax is levied at all in a jurisdiction, whether its laws provide laxity around citizenship and/or residency; and whether the personal income tax legislation is too narrow in scope, providing financial secrecy sinks for tax dodgers and criminals.

In summary, apart from providing expedient legal status for trusts and foundations, Cyprus seems to be especially attractive for its lack of transparency in ownership registration. In other words, Cypriot legislation provides good opportunities for maintaining **high secrecy of company ownership and its operations**.

Other factors have also enabled Cyprus to become an offshore hub specifically for Russian funds.

Firstly, mutual **cultural and historical links** may have been important in determining Cyprus' attractiveness. Immediately after the collapse of the Soviet Union, Cypriot law and accountancy firms – especially those with political connections – leveraged their already well-established links with the growing Russian oligarchic class in order to attract them as clients. They were persuaded that Cyprus could provide them with a safe haven for their accumulating wealth, which was often based on illicit activities or the siphoning of funds from newly-privatized companies.

Second, there have been **persistent governance deficits in Cyprus' key financial regulators** including their lack of independence, conflicts of interest and

limited capacity – politically-connected firms with the capacity to exploit such governance deficits were in a particularly strong positions to attract Russian business.

Finally, the existence of **special bilateral agreements between Russia and Cyprus** have transformed the island into a Russian “back office”. Currently, there are 23 bilateral inter-governmental agreements governing the economic relationship between Russia and Cyprus, most of them regarding rules on tax and financial reporting.

Russian corporate footprint

It is important to understand how Cyprus' structural economic vulnerabilities – coupled with the investment presence of Russia in the country – (may) augment Russian political influence, as well as the factors that amplify this. To this end, it is useful to assess the Russian corporate presence in Cyprus by identifying companies with direct, as well as indirect, links to Russian entities or political structures. The corporate footprint is based on the estimate of revenues, assets and employment figures of all Russian-owned or Russian-controlled com-

panies in Cyprus.¹⁸¹ The aggregate values of these three indicators are then compared with the total figures for the economy, allowing the approximation of the relative Russian corporate presence in the country. These three indicators have been identified in field research and expert analysis as the most telling indicators of vulnerability to Russian exploitation.¹⁸²

The penetration of Russian-controlled entities into the Cypriot economy, as well as their geographical and

sectorial distributions, was assessed using corporate registries and databases. In order to define “Russian ownership”, four scenarios have been considered (Table 4). The first scenario considers companies with Russian ultimate beneficial owners. The second and third scenarios consider companies with Russian controlling shareholders and Russian immediate parents, respectively. Finally, the fourth utilizes a more elaborate approach which includes multiple criteria regarding Russian presence in the company’s ownership.

Table 4. Criteria for the identification of Cypriot companies with Russian ownership

Scenario	Type of companies	Number	Percent of total
Cypriot companies	All companies in Cyprus registered in ORBIS corporate database with active status*	284,645	100
Scenario 1	Companies with Russian global ultimate owner, of which:	1,694	0.60
Scenario 1a	Companies with Russian global ultimate owner with direct share of >50%	1,092	0.55
Scenario 2	Controlling shareholder located in Russia	1,695	0.76
Scenario 3	Immediate parent located in Russia	1,228	0.43
Scenario 1-3	Number of companies that can be identified by at least one of the scenarios 1-3¹⁸³	1,714	0.60
Scenario 4	Companies with: (i) ultimate ownership (min. path of 50.01% shareholder) with subsidiaries located in Russia; or (ii) Shareholders with subsidiaries located in Russia, owned between 10% and 100%; or (iii) Shareholders with foreign subsidiaries located in Russia not ultimately owned but at least 51% owned; or (iv) Branches with headquarters located in Russia; (v) or Headquarters with branches located in Russia	6,944	2.44
Scenario 4a	Companies identified by scenario 4, but not identified by any of scenarios 1-3	6,598	2.32
Scenario 1-4	Number of companies that can be identified by at least one the scenarios 1-4	8,312 (1,714+6,598)	2.92

* Only companies with active status were considered in all scenarios.

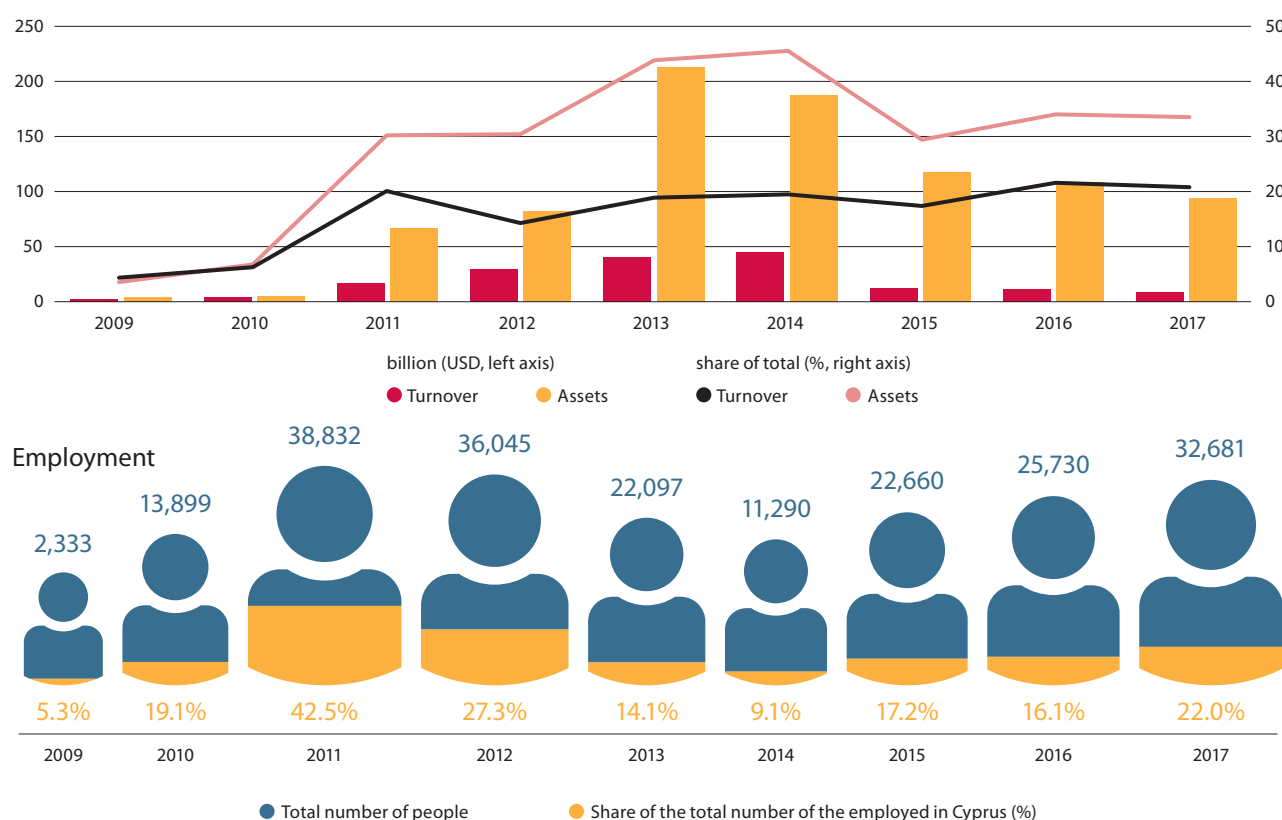
Source: CSD calculations based on corporate registers and databases.

¹⁸¹ “Direct” control means companies with a clearly identifiable final beneficial owner in Russia. “Indirect” control means companies which have between 5% and 100% of the equity controlled by a Russian owner at some point in the ownership chain. While we have detected also companies that are “ideal fronts”, i.e. they are completely detached from their final beneficiary owners, legally severing their link with their Russian patron, these have not been included in the present analysis, unless specifically noted. Understanding the mechanisms of such “ideal fronts” is important for comprehending the risk of Russian influence in a given country in its entirety.

¹⁸² Conley, H., Mina, J., Stefanov, R., and Vladimirov, M. (2016). *The Kremlin Playbook: Understanding Russian Influence in Central and Eastern Europe*; CSD (2018). *Russian Economic Footprint in the Western Balkans*.

¹⁸³ In each scenario, CSD identified the companies that belong solely in one of the scenarios, and have removed duplicates. In fact, it is very common for companies to be present in more than one scenario (e.g. a company that has Russian GUO, have Russian controlling shareholder and immediate parent). The companies that had missing information for one scenario but not for all were also included (e.g. GUO is not reported, but corporate shareholder is reported). Since there were a lot of companies that did not report information about shareholders or global ultimate owners, the numbers represented in the analysis are an underestimation of the true extent of the Russian corporate footprint in Cyprus.

Figure 24. Russian corporate footprint in Cyprus



Source: CSD calculations based on data from corporate databases.

If estimated solely as a proportion of the number of companies operating in Cyprus, the Russian corporate footprint, both direct and indirect, is relatively small – less than 3% of the total number of registered companies in the Cypriot economy (Table 4). However, in terms of the **size of these companies' revenues, assets and employment, the Russian corporate footprint is massive**. Russian companies have controlled, on average, 16% of the total business turnover in the island's economy since 2009. Since the 2013 banking crisis, its footprint further rose to reach around 21% at the end of 2017 (Figure 24).

Russian companies in Cyprus have generated cumulative revenues of around USD 170 billion (USD 17 billion on average per year) over the past decade – all this in an economy roughly the size of that of Bosnia and Herzegovina, but with a population four times smaller, i.e. just 850,000. In terms of corporate assets, Cyprus' exposure to Russian companies is even larger at an average of 28.6% of the total over the same period. In 2013/2014, the share of Russian controlled assets in Cyprus reached more than 45% of its total (USD 212 billion). This share has since declined to around a third in 2017. In nominal

terms, the assets of Russian companies have shrunk by half since the banking crisis in 2013.

This could have been the result of multiple confluent factors, including the outflow of FDI just before the crisis began, the bail-in of deposits that prompted Russian companies and individuals to withdraw their funds, and the Russian economic crisis after 2014 that led to falling revenues and assets, especially of energy and metal companies. The net income (after taxes) of Russian controlled companies has been on average around USD 2 billion, with a 2014 peak of USD 6.7 billion.

This means that close to 10% (and in some years, up to 30%) of the island's GDP was directly generated by Russian companies. In 2017, Russian companies employed 32,681 people directly, a figure that comprised around a fifth of the total number of employed persons in the Cypriot economy that year.¹⁸⁴ This marks a

¹⁸⁴ It should be noted that the financial and employment data for Russian companies is an underestimate, as for many of the companies identified to have a Russian ultimate beneficial ownership there is missing data for part of or the whole period under study. The data is derived from corporate registries and databases.

three-fold increase in the number of employees hired by Russian controlled firms since 2010.

A sectoral assessment of the Russian corporate footprint reveals that most Russian companies in Cyprus have been active in the country's non-manufacturing sectors. Not surprisingly, the sector¹⁸⁵ with the highest number of registered Russian-controlled companies is financial and insurance activities, followed by wholesale and retail trade, and professional, scientific and technical activities. In Cyprus, Russian-controlled companies make up 15% of all financial services firms and 8% of mining and quarrying firms. The concentration in these two sectors is easy to explain – Cyprus has become the biggest hub for Russian-owned offshore companies which depend on the activities of different financial, legal and other management consulting firms. Similarly, some of the largest Russian mining and metallurgical companies have their holding entities registered in Cyprus, a country with hardly a developed mining industry.

Assessing the Russian corporate footprint simply through its number of companies, however, skews the real picture: the Russian entities registered in Cyprus include some of the globally largest firms in their respective sectors, as well as the biggest investors in others. Looking at the concentration of revenues by sector further reveals that Russia is by far the biggest economic player in real estate, mining and quarrying, communications, financial and insurance activities, manufacturing, and even health. In these sectors, Russian-controlled companies accounted for more than 40% of the generated annual revenues. In particular sectors, like real estate, this share was close to 90%.

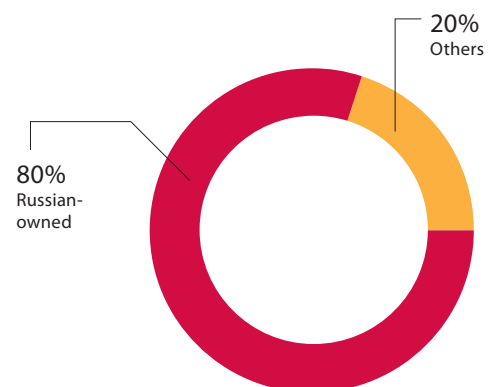
The Russian presence is most pronounced in the financial services and real estate sectors. Most Russian companies operate in trusts, funds and similar financial entities (82% of total assets) or are involved in all kinds of financial intermediation, except insurance and pension funding if measured by total assets. In activities of holding companies and fund management activities, the Russian presence is also quite significant. Looking at the financial services sector – the mainstay for Russia's management of its offshore empire in Cyprus – the Russian companies' footprint is around 10-12% in terms of the share of total revenues, and between 18% and 82% in terms of assets. For example, 82% of all companies operating trusts and funds are Russian-owned. This corroborates earlier observa-

tions that Russian shell companies conceal their ultimate beneficial ownership by placing their assets in trusts with nominal owners.

Hence, the true extent of Russia's infiltration of the Cypriot economy can, in some sectors, be qualified as complete control. This provides the Kremlin with seemingly unlimited possibilities for leverage, which judging by the number of special agreements signed between the two countries, it has not hesitated to exploit.

In addition, there is a need to account for the exertion of soft power, as well as the importance of Russian businesses, tourists and real estate owners in the Cypriot economy. The Cyprus-Russian business association estimates that their 300 registered Russian companies are worth 80% of the country's wealth.¹⁸⁶ In 2018, around a fifth (783 thousand visitors) of all tourist arrivals came from Russia (second only to UK travelers). These Russian tourists made up a quarter of all personal travel services exports – an indicator that Russia's footprint in the tourism industry totals around EUR 800 million per year.¹⁸⁷

Figure 25. Corporate wealth ownership in Cyprus



Source: Cyprus-Russian Business Association.

It is likely that future investment projects will further increase tourist flows. For example, Europe's biggest casino resort is due to open in Cyprus in 2021 and is expected to attract about 330,000 new visitors.¹⁸⁸ In 2010, tourism represented 14.3% of Cyprus' GDP in –

¹⁸⁵ Based on the NACE rev. 2 industrial classification.

¹⁸⁶ Smith, H., "Welcome to Limassolgrad: the city getting rich on Russian money". *The Guardian*, February 17, 2018.

¹⁸⁷ CSD calculations based on statistics from the Cypriot national statistical institute and the United Nations Conference on Trade and Development (UNCTAD).

¹⁸⁸ Smith, "Welcome to Limassolgrad: the city getting rich on Russian money".

a share that has continuously increased to 23.3% in 2017.¹⁸⁹ In 2017, more than half of the Cypriot tourism sector's contribution to GDP was indirect, and the sector employed 22.7% of the total workforce in 2017, or 85,000 jobs.¹⁹⁰ In light of all this, dependence on Russian tourism is a major vulnerability for Cyprus.

In addition, the financial, insurance and legal consultancy – one of the most strategically important business sectors in Cyprus – is heavily dependent on its Russian

clientele. Russia receives more than 12% of Cyprus' total exports of financial services, excluding the abundance of domestic business generated by Russia-owned firms already registered in Cyprus. Finally, Russian investments are critical for the construction and hospitality businesses – the burgeoning number of new residential complexes in Cyprus, especially on the southern coast of the island, depend on wealthy Russians willing to buy high-end properties.

Table 5. Top Russian companies in Cyprus by revenues (2010 – 2018) and by ties to the Kremlin

Company name	Core sector	Main owner	Relevant details	Potential ties to the Kremlin
METALLO-INVEST CYPRUS LIMITED	Non-specialized wholesale trade	Metalloinvest LLC (100%)	Metalloinvest is a Russian mining and metallurgy company specializing in the manufacture of steel. Alisher Usmanov is the major beneficiary of USM Holdings (48%), alongside other major beneficiaries – namely the companies of Andrei Skoch and Farhad Moshiri, who own 30% and 10%, respectively.	Alisher Usmanov, a Russian oligarch, ally of the Kremlin and president Putin.
ROS AGRO PLC	Manufacture of machinery for food, beverage and tobacco processing	Family business (71.8%)	Vadim Moshkovich is chairman of the agro-industrial firm Rusagro, a big manufacturer of pork and sugar (whose real time net worth, as of 17.06.2019, is 2.2 billion USD).	Vadim Moshkovich is a former member of the Federation Council (Russia), the Upper Chamber of the Russian Parliament
FLONTRANO TRADING LIMITED	Wholesale of solid, liquid and gaseous fuels and related products	100% owner is Russian citizen, Nikolai Bukhantsov.		Not found
LUKOIL MID-EAST LIMITED	Support activities for petroleum and natural gas extraction	Russian oil company LUKOIL	The main owner of LUKOIL is Vagit Alekperov, a Russian billionaire, whose net worth is USD 21 billion (Forbes, 2019). Third richest person in Russia in 2019.	Lukoil is one of the 13 Russian companies on the OFAC's Sectoral Sanctions Identifications List (SSI) announced in response to Russia's 2014 annexation of Crimea.
TMK STEEL HOLDING LIMITED	Non-specialized wholesale trade	The GUO is Dmitriy Pumpyansky (100%)	Dmitriy Pumpyansky, Russian billionaire, whose real time net worth is USD 2.4 billion (Forbes). He is the owner and chairman of OAO TMK, a Russian global manufacturer of steel pipes for the oil and gas industry.	No direct ties found but TMK has been accused on a number of occasions for having received inflated Gazprom contracts, as well as for its participation in some of the largest civil infrastructure contracts during the preparation of the Sochi Olympics in 2014 and the World Cup in 2018.

¹⁸⁹ Knoema, "Cyprus – Contribution of travel and tourism to GDP as a share of GDP".

¹⁹⁰ According to a 2018 World Travel and Tourism Council study.

Table 5. Top Russian companies in Cyprus by revenues (2010 – 2018) and by ties to the Kremlin (continued)

Company name	Core sector	Main owner	Relevant details	Potential ties to the Kremlin
ROSNEFT INDUSTRIAL HOLDINGS LIMITED	Activities of holding companies	The GUO is the Russian government with 100% ownership	Ownership tree includes Federal Agency for State property management and state companies Rosneftegas and Rosneft.	State-owned company with significant political engagement abroad.
FESCO OCEAN MANAGEMENT LIMITED	Other transportation support activities	The GUO is Far Eastern Shipping Company PLC. (Russia; 100%) with ultimate owner Ziyavudin Magomedov	Ziyavudin Magomedov, Russian billionaire and the main owner of the privately-held investment company Summa Group. In March 2018, he was arrested and charged with “racketeering and embezzlement of state funds”. ¹⁹¹	Ziyavudin Magomedov is believed to be part of the inner circle of former Russian President and Prime Minister Medvedev and has received many large contracts ahead of the 2018 World Cup.
DIGIMAX LIMITED	Non-specialized wholesale trade	100% owned by Russian company DOMUS	The owners are 14 Russian individuals.	No clear links
FINVISION HOLDINGS LIMITED	Other financial service activities, except insurance and pension funding	The GUO is Artem Avertisyan.	The company specializes in providing a wide range of financial products and services. Avertisyan has been battling for control over the Bank Vostochny, which is owned by the private equity investor Michael Calvey. Calvey is under house arrest on trumped-up embezzlement charges.	Artem Avertisyan, is the chairman of Russia’s “Leaders’ Club,” a Kremlin-sponsored group of entrepreneurs whose purpose is to improve the country’s investment climate. He is also the director of new business for the Agency for Strategic Initiatives, an organization, headed by Putin, that sponsors investment projects. ¹⁹²
SCFMANAGEMENT SERVICES (CYPRUS) LTD	Business and other management consultancy activities	100% owned by the Russian government via Sovcomflot	Sovcomflot is Russia’s largest shipping company, and one of the global leaders in the maritime transportation of hydrocarbons, as well as in servicing offshore exploration and production.	State owned company.
ABH FINANCIAL LIMITED	Commercial bank	ABH HOLDINGS SA is GUO (97.4% ownership). The Luxembourg-based offshore company owning the holding has three main owners including Mikhail Fridman (36.47%), German Khan (23.27%), Alexei Kuzmichev (18.12%) and Pyotr Aven (13.76%)	Mikhail Fridman, Russian business magnate (net worth USD 15.6 billion) is one of the richest men in Russia.	Mikhail Fridman’s Alfa Group has developed enormous business presence in the telecommunications, oil and gas and financial sectors. The corporate group owns Russia’s largest private bank and has sold a majority stake in one of Russia’s largest oil companies, TNK-BP, for USD 14 billion to Rosneft. Alfa Bank has reportedly also facilitated a communication backchannel between the Kremlin and U.S. President Trump.

Source: CSD calculations based on corporate databases.

¹⁹¹ Nikolskaya, P. and Tetrault-Farber, G., “Russian tycoon Magomedov arrested on embezzlement charges”. *Reuters*. March 31, 2018.

¹⁹² Knight, A. “The Price of Doing Business in Russia: Prison”. *New York Review of Books*. March 4, 2019.

GOVERNANCE DEFICITS IN VULNERABLE ECONOMIC SECTORS

As the corporate footprint assessment has affirmed, Russia is by far the biggest foreign economic player in Cyprus, with significant presence in strategic sectors of the local economy. While Russian corporate presence is not unwanted per se, the Kremlin has increasingly used Russian capital to further its economic and political interests.¹⁹³ Three interrelated factors – namely the economic crisis in Europe and in Russia, the push for de-offshorization of Russian companies, and the rising assertiveness and control of the Kremlin over Russian businesses – have made it increasingly easier for corporates to be pressured into advancing Russian political interests.

Another influence channel often used by the Kremlin is **domestic corporate networks** with significant influence over parties, businesses, and government institutions. These act as intermediaries, boosting Moscow's interests where necessary.¹⁹⁴ This is possible in light of the concentration of Russian investments in large, strategic sectors, whose interests are often closely interlinked with government policy. It is also a result of the ever-increasing intersection between business and politics in Russia.

It is difficult to distinguish business enterprises from the Russian interference in domestic politics. Powerful local economic groups have often sought Russian corporate links in order to secure capital and political backing – this would allow the acquisition of assets and the investment in large projects. It seems a win-win outcome for both Russian and local private interests – the former find a way to move their funds out of Russia and the latter acquire financial resources that would not be available otherwise. In this way, domestic interests can help their Russian partners exploit known governance deficits. Such means include passing laws that sustain monopolistic market structures, evading tax payments, ensuring non-transparent public procurement and privatization procedures, as well as clinching mergers and acquisitions which allow for slush funds to be easily hidden and redirected towards side investments or political activities. In ex-

change, Russia can help domestic networks to engage in rent-seeking with the national governments.

This analysis discusses the weak spots and internal vulnerabilities in Cyprus' economic sectors where the impact of Russian direct or indirect footprint has been the strongest. These deficits arise from the combination of economic dependencies and bad governance (including corruption and state capture).¹⁹⁵ They contribute not only to a long-term corrosion of institutional resilience, but also to the long-term permeation of malign Russian influence into the Cypriot – and, by extension – European policy-making processes.

Banking and finance

Banking and corporate services in Cyprus are the most vulnerable sectors to Russian capture.¹⁹⁶ The FDI flows between Russia and Cyprus are disproportionately large considering the size of the Cypriot economy – as such, the importance of Russian business for the two sectors is so large that it can easily influence the decisions of government institutions. On the forefront of this business are law and accountancy firms, which offer a one-stop shop for rich Russians. They offer a comprehensive range of company services, including company registration, secretarial and nominee services, opening and managing bank accounts, escrow agent services, bookkeeping and accounting, incorporation of international investment schemes (hedge funds, venture capital and mutual funds), provisions of corporate trustees, liaising with fund managers for the operation of investment accounts, liquidation of companies, insolvency, bankruptcy and reorganization, including re-domiciliation. In addition, law firms offer international tax planning services, including “tax optimization”, trust law and immigration law. This also includes handling applications under the Cypriot Citizenship by Investment Scheme.

The Cypriot law and accountancy firms most successful in attracting Russian business are those with political connections. Implicitly, if not otherwise stated, they offer protection from Cypriot tax and AML authorities, providing “reassurance” to corrupt Russian businessmen and politicians seeking to launder illicit

¹⁹³ Shentov, O., Stefanov, R., and Vladimirov, M. (2019). *The Russian Economic Grip on Central and Eastern Europe*.

¹⁹⁴ Conley, H., Ruy, D., Stefanov, R., and Vladimirov, M. (2019). *The Kremlin Playbook 2: The Enablers*.

¹⁹⁵ For an in-depth methodological review and a pilot of state capture monitoring see Stoyanov, A., Gerganov, A. and Yalamov, T. (2019). *State Capture Assessment Diagnostics*.

¹⁹⁶ Ibid.

Box 12. Russian stakes in Cypriot banks

Russian influence in the banking system has also been facilitated through the Russian Commercial Bank (RCB). RCB is a former Beirut branch of the Soviet Moscow Narodny Bank. It was involved in financing Soviet foreign policy operations in the Middle East, and was accredited in Cyprus in 1995 as a subsidiary of Russian VTB, which now owns 46% of its share capital. RCB has thus served as a conduit of Russian influence. Its board includes several important Cypriot political figures, namely the former foreign minister Erato Markoulli, the former Attorney General Petros Clerides, the former Ambassador to Russia Sotirios Zackheos, and the Nobel prize-winner economist and London School of Economics professor, Christopher Pissarides. The presence of such high-profile individuals on the bank's board helps placate public opinion about the bank – it also provides a model to other politicians, diplomats and academics to aspire to such well-paid positions in the future.

The Panama Papers investigation revealed that RCB played a key role in providing enormous unsecured loans worth USD 650 million between 2009 and 2012 to a British Virgin Islands shell company (Sandalwood Continental Ltd.). The firm was set up by the Panama law firm, Mossack Fonseca, and was used to siphon funds to a series of other shell companies buying up luxury property.¹⁹⁷ Some of these funds were traced back directly to personal friends of President Putin or to directors of state-owned banks and other financial institutions. Since 2014, RCB has become much more active in financing Cypriot enterprises, not least because it has been directly supervised by the Single Supervisory Mechanism in Frankfurt. As a result, the bank is now among the 122 systemically significant banks in the EU, a status that has helped it to expand its customer base in Cyprus.

RCB's successful expansion of its operations in Cyprus can also be credited to the presence of weak banks plagued by a high volume of non-performing loans. RCB was thus in a unique position to take advantage of the 2013 crisis, before which it had hardly operated in the local market. Since 2016, it has joined forces with the European Investment Bank (EIB) and the Cyprus government in the financing of small and medium sized enterprises (SMEs). RCB's expansion into the local market is bound to help the bank amplify Russian influence within Cyprus.

proceeds through Cyprus. It is no coincidence that some of the highest profile cases of money laundering through Cyprus used law firms with strong political connections. A more benign explanation for the success of politically-connected Cypriot firms is that they have a comparative advantage in networking with politically-exposed businessmen in Russia. In any case, Cyprus has become attractive to Russian politicians and the Kremlin's corporate stooges (see Table 5).

Russian entities have also maintained a significant footprint in Cyprus's banking system for more than a decade now. At the peak of the Russian corporate influence in Cyprus in 2013, estimates showed that USD 31 billion of Russian funds were stashed in Cypriot accounts: USD 19 billion from businesses and individuals, USD 12 billion from banks. Moreover by the end of 2012, Russian banks had USD 40 billion

in cross-border loans to Cypriot companies with ties to Moscow.¹⁹⁸ It is clear that Cypriot banks have not only been used as an investment tool/asset storage, but have also facilitated transactions resembling money laundering activities.

Russian interests in the Cypriot banking sector increased after the financial crisis. Its resolution via the intermediation of the European Commission and the IMF created the opportunity for wealthy Russians not only to hold bank deposits, but also to own bank equity. In 2013, the EU's bailout strategy entrenched Russia's position in the Cypriot financial system when, in a so-called "bail-in" strategy, it forced savers – Russian and otherwise – to convert 47.5% of all deposits above EUR 100,000 into bank shares. As intended, the bail-in of uninsured depositors protected the country's public

¹⁹⁷ Harding, L., "Revealed: the \$2bn offshore trail that leads to Vladimir Putin". *The Guardian*. April 3, 2016.

¹⁹⁸ Young, E. "Russian money in Cyprus: Why is there so much?" *BBC*. March 18, 2013; "Russia risks billions of dollars if Cyprus defaults – Moody's". *Reuters*. March 13, 2013.

finances – there was no longer a need for a government bailout funded by public money.

However, the bail-in of uninsured depositors also resulted in an unpredictable transfer of bank ownership in the saved/bailed-in institutions. The Bank of Cyprus, for instance, is the largest financial institution in the country with assets worth close to EUR 21 billion. In their case, the ten largest new shareholders were politically exposed Russian oligarchs including Viktor Vekselberg and Vladimir Strzhalkovsky (former KGB agent and a close ally of the Russian President Putin). As a result of the 2013 bail-in, the Bank of Cyprus acquired six Russian members on the Board of Directors, including Strzhalkovsky¹⁹⁹ as the Vice-President as well as Anjelica Anshakova, Dmitry Chichikashvily, Erishan Kurazov, Igor Lojevsky and Anton Smetanin. The Cypriot central bank also came under direct political pressure to approve all of them as fit and proper for their respective positions.²⁰⁰ As of late 2019, Vekselberg's Renova company was the largest individual shareholder (9.9%), followed by legacy Cyprus Popular Bank, 84% of which is owned by the Cypriot Government. The bank's non-executive director is Maksim Goldman, former director of strategic projects and deputy chief legal officer of Renova.²⁰¹

Risks of conflicts of interest on the board of the Central Bank of Cyprus

The risk of regulatory capture by interest groups that benefit from the “special relationship” between Cyprus and Russia is significant. For example, nearly all recent appointments to the Cypriot Central Bank's board are individuals who have risks of conflicts of interest, in that they previously served in the banking and/or corporate services sector heavily dependent on Russian money or in that they did not have the required prior experience.

Overall, the 2013 crisis resulted in an increased Russian influence on the Cypriot banking system,²⁰² initially through the bail-in that converted uninsured deposits

into equity, and then through legislative changes that enabled the Anastasiades government to tighten its grip on the banking system. These changes included amendments to:

- the composition of the Resolution Authority that enabled the government to appoint the board members to the country's largest bank in 2013;
- the governance structure of the central bank that diminished its independence, allowing the government to exercise greater influence on central bank decisions.

The expansion of Russian business presence in Cyprus has been deterred somewhat by the introduction of stricter AML/CFT standards in December 2013. These include nearly all of the enhanced provisions of the 4th EU AML Directive, as part of the bail-out agreement with Europe and the IMF. These standards were further strengthened in April 2016, with the introduction of a revised framework with additional restrictive provisions regarding the operation of [high risk] professional intermediaries. The reliance on such individuals is limited to the outset of establishing a business relationship – banks are now expected to deal directly with the customer in operating the account.

This regulatory framework was tightened further in July 2017 and April 2018 when the *EU Directive 2015/849 on the Prevention of the Use of the Financial System for the Purposes of Money Laundering or Terrorist Financing* was transposed into domestic law. The subsequent amendment, *Directive (2018/843)*, was published on June 19, 2018 but has not yet been transposed into Cypriot law. The directive, which intends to further harmonize AML standards across the EU, includes harmonization of enhanced customer due diligence for non-EU countries that the European Commission considers high-risk. It requires member states to apply additional measures where appropriate.

The directive also requires enhanced cooperation among European financial intelligence units and the exchange of information without impediment – this includes access to information on virtual currencies. Additionally, it aims to enhance access to information on beneficial ownership across the EU and to improve transparency of the ownership of companies and trusts. As such, it is particularly relevant in fighting money laundering rooted in Russian sources.

In 2016, the CBC imposed fines on various Cypriot banks for failing to comply with the provisions of

¹⁹⁹ See “Russians, including Putin ally, join bailed-in Bank of Cyprus board”, *Reuters*, September 10, 2013.

²⁰⁰ President Anastasiades himself publicly criticized the central bank for alleged delays in completing the fit and proper checks; see Demetriades, *A Diary of the Euro Crisis in Cyprus: Lessons for Bank Recovery and Resolution*.

²⁰¹ *Bank of Cyprus, Who We Are*.

²⁰² Kirchgaessner, S. and Farolfi, S., “FBI investigates Russian-linked Cyprus bank accused of money laundering”. *The Guardian*. December 24, 2017.

Box 13. Compromised Central Bank independence

One unintended consequence of the bail-in was an erosion of the independence of the Central Bank of Cyprus, and resulting opportunities to proliferate Russian influence in Cyprus. Legislative amendments to the governance structure of the central bank shifted powers from the Governor to the Board, which the Cypriot government controls through direct appointments. These amendments were voted in by the Parliament, notwithstanding an ECB legal opinion warning against their enactment.²⁰³ Eventually, they resulted in the resignation of the then CBC Governor Demetriades – a blow to central bank independence in Europe. Demetriades' successor, Chrystalla Giorghadji, was the choice of President Anastasiades. During her tenure, the Cypriot government was able to exercise unhindered influence on the banking system. Within months of her appointment, Viktor Vekselberg emerged as the largest shareholder of Bank of Cyprus, having bought out the stakes of other Russians. At more or less the same time, Wilbur Ross, the US Treasury Secretary, led a group of western investors to invest EUR 1 billion in the Bank. Josef Ackerman, former Deutsche Bank CEO, also served as non-executive director of Renova, Vekselberg's holding company in Switzerland. He became the bank's new Chairman, taking over from Chassapis.²⁰⁴ During Ackerman's term, the Bank of Cyprus sold its Russian and Ukrainian subsidiaries to the Alfa Group empire owned by the oligarch Mikhail Fridman. Fridman controls, through his Cypriot-registered ABH Holdings, one of the largest Russian funds: LetterOne. LetterOne is exemplary of the corporate reach of such groups in Europe in its ownership of the largest Italian telecommunications company WindTre, as well as its operation of the Amsterdam Trade Bank.

money laundering laws. Specifically, Hellenic Bank was fined EUR 1.1 million, Jordan Kuwait Bank (Cyprus branch) EUR 1.2 million, and Privatbank (Cyprus branch) EUR 1.5 million. The central bank also took various actions to close down FBME (Cyprus branch), following special measures taken by the US Treasury over concerns that the bank was of "primary money laundering concern."²⁰⁵

Stricter AML/CFT standards – as well as a more effective enforcement of these standards by the central bank – have reduced banks' appetites for Russian business.²⁰⁶ According to statistics published by the Central Bank of Cyprus, non-resident, out-of-the-EU deposits declined almost three-fold since the banking crisis from EUR 20.88 billion to EUR 6.67 billion in January 2020.

However, despite Cyprus' seeming will to apply the AML/CFT standards, concerns remain that enforcement may be limited to smaller, foreign-owned banks. Bigger local banks, especially Bank of Cyprus, possess political clout that makes them "too big to regulate" –

this had been the case leading up to the 2012 – 2013 crisis.²⁰⁷

High-profile scandals have raised serious questions about Bank of Cyprus. These relate, in particular, to the continuation of Paul Manafort's money laundering in 2014 and 2015, despite the initial 2012 reported closure of his account at Laiki, where the bank was absorbed by the Bank of Cyprus following suspicions of money laundering.²⁰⁸ In a similar vein, the November 2018 central bank circular on shell companies – hailed as an important step in the fight against financial crime – differs significantly from the draft circular published in June 2018. The main difference is that it introduces discretion as to the definition of a shell company, allowing credit institutions to use their own risk-based approach to decide on the businesses with which to engage. Such discretion may allow shell companies to sustain a business relationship with a bank as long as the bank itself can provide justification for that relationship. While it has raised the cost of operating a shell company, the circular has not addressed the problem of the concealment of the identities of the ultimate beneficial owners. This is a service

²⁰³ European Central Bank. *Opinion of the European Central Bank on Changes to the Governance of the Central Bank of Cyprus*. June 5, 2013.

²⁰⁴ Ackerman stepped down in May 2019 and was replaced by Takis Arapoglou, a Greek national, former CEO of National Bank of Greece.

²⁰⁵ Alexandrou, F. and Orphanides, S. "Sources: Cypriot Police Raid Bank in Money Laundering Probe". OCCRP. May 31, 2019.

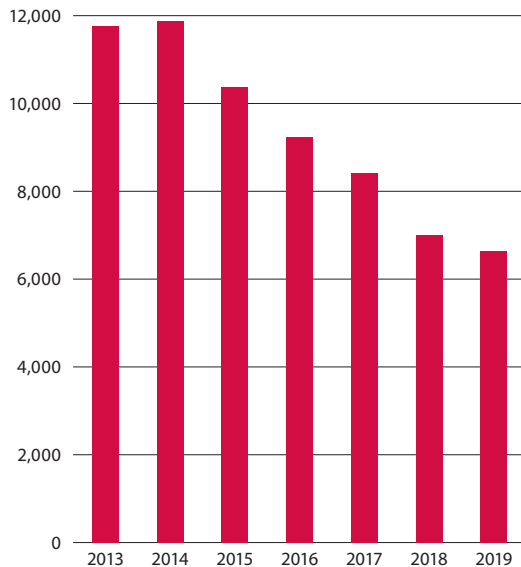
²⁰⁶ See for example, Tugwell, P. and Georgiou, G., "Cyprus no longer Mediterranean haven for Russian business". *Bloomberg*. January 10, 2019.

²⁰⁷ See for example, Rettman, A. (2018). "Cyprus: Russia's EU weak link?" *EU Observer*. September 25, 2018. For details on how some banks became too big to regulate in the build-up to the 2012 – 2013 crisis see Demetriades, *A Diary of the Euro Crisis in Cyprus: Lessons for Bank Recovery and Resolution*.

²⁰⁸ See, for example, Demetriades, P., "US Trial Sheds Light on Murky Cyprus-Russia Links". *EU Observer*. August 15, 2018.

which some banks – those that enjoy political backing and are less likely to be fined – can continue to offer.

Figure 26. Total deposits of non-EU residents in Cypriot banks, EUR million



Source: Central Bank of Cyprus.

Political capture of the offshore business and its regulators

Another reason for which Cyprus has become such an attractive destination for operating shell companies has been a **highly developed corporate service providers (CSP) industry**. CSPs make up a large section of the economy, with a current estimation of 4,000 lawyers practicing on an island of only 850,000 residents.²⁰⁹ Cyprus's tax system continues to provide incentives for Russians to set up companies on the island. This is compounded by the poor implementation of regulations and restrictions on the establishment of shell companies. However, it is the intricate fusion between political and corporate elites in Cyprus that has made the offshore industry in Cyprus so attractive for politically-exposed Russian companies. This fusion has allowed Russia to develop an unvirtuous cycle of state capture in Cyprus, in which its investments leave an enormous economic footprint, creating political dependence – this further enables the expansion of the economic relationship.

The perpetuation of this vicious cycle owes also to President Anastasiades' (in office since March 2013)

²⁰⁹ Orphanides, S. (2019). "The Curious Case of Dr. K and Mr. Chrysostomides". OCCRP. June 28, 2019.

role in sustaining and further developing the country's exposure to Russian offshore financing. His immediate family has benefited from the "special relationship" with Russia. Although the President himself proclaims publicly that he has nothing to do with the law firm that bears his name (Nicos Chr. Anastasiades & partners), his daughters Elsa and Ino Anastasiades are two of the four partners.²¹⁰ The firm has represented leading Russian oligarchs, including Vladimir Strzhalkovsky, mentioned above. The firm is also among the few approved by the government as official agents for the Citizenship by Investment Scheme (more widely known as golden visas).²¹¹

During his first term in office (2013 – 2018), Anastasiades visited Russia three times. He was the only EU head of state to attend the 70th anniversary celebrations of the end of WWII, which were boycotted by all the other EU leaders following Russia's aggression in Ukraine. During his visit to Moscow in 2017, Anastasiades called for a relaxation of the sanctions against Russia.²¹² The powers that Anastasiades possesses as head of state, in combination with his family's financial interests, make the Republic of Cyprus vulnerable to capture by Russian and other interests.^{213,214}

The President's law firm has also been connected to a network of shell companies used in various dubious financial operations between 2006 – 2013. These

²¹⁰ For more details see: <http://anastalaw.com/our-firm>

²¹¹ Anastasiades' daughters are nominee directors of a company that owns Bashkir Soda, the largest chemical plant in Russia that produces chemicals for both civilian and military use. The president's office described this as "standard [business] practice". Specifically, they stated: "The president's daughters are active lawyers. In this professional capacity, and according to common practice, they may act as nominees on behalf of clients of their law firm who happen to have shares or any other interest in various firms," such as Bashkir Soda, it said. Rettman, A. Cyprus: Russia's EU weak link?. *Euobserver*. 25 September 2018.

²¹² He was quoted as saying: "We should all work to create conditions that will pave the way for full re-establishment and further deepening of EU-Russian relations". CyprusMail, "Our View: Anastasiades' Russia trip left the impression he was eager to please Putin," October 26, 2017.

²¹³ In 2013, the IMF presented Anastasiades with the details of the bank bailout bill. He proposed taxing small savers (including those below the threshold of EUR 100,000 guaranteed by deposit insurance schemes), in order to protect large depositors, many of whom were Russian oligarchs. In the end, the Cypriot parliament rejected the government's proposal and Anastasiades was offered an ultimatum of accepting the bail-in proposed by the IMF or no bailout, which would have meant Cyprus leaving the Eurozone and the EU. Anastasiades' response was to send his finance minister Michael Sarris to Moscow to plead for a new loan. The Kremlin's response was a negative one, notwithstanding the burden of EUR 4 billion born by Russian oligarchs.

²¹⁴ See Demetriades, *A Diary of the Euro Crisis in Cyprus: Lessons for Bank Recovery and Resolution*.

Box 14. Enabling law firms

Nicos Chr. Anastasiades is not the only Cypriot law firm that has political connections at the highest level. Tassos Papadopoulos, who served as President of Cyprus during the 2003 – 2008 period, established his own legal firm after his term ended. Papadopoulos' law firm was the external counsel of Laiki Bank until it was taken over by the Greek tycoon Andreas Vgenopoulos in 2005. Papadopoulos set an important precedent for other Cypriot lawyer-politicians: in the late 1980s and early 1990s, he helped Yugoslavia's President Slobodan Milosevic break UN sanctions through Laiki Bank, described by the *Financial Times* as the "defiant bank that helped finance two wars".²¹⁵ According to media reports, the bank broke UN sanctions with the then CBC Governor's (Afxentis Afxentiou) blessing.²¹⁶ The amounts involved, according to media reports, were around USD 4 billion.²¹⁷ The wealth of the family has helped his son become leader of the Democratic Party, as well as an aspiring presidential candidate.

Christodoulos Vassiliades & Co. LLC is probably the law firm that has had the closest ties to the Kremlin. Its owner and founder, Christodoulos Vassiliades, is also a director of the Cyprus branch of Sberbank. The firm's presence in several offshore destinations, as well as in Moscow and London, places it in a strong position to attract politically-exposed Russians seeking to set up complex corporate structures involving several jurisdictions. Following the bail-in of uninsured depositors at Bank of Cyprus in 2013, Vassiliades emerged with a proxy share of 8.37% of the bank's capital. His vote was crucial in electing six Russian nationals to the board of the Bank of Cyprus soon after it exited resolution.

are known as "Troika Laundromat" and amount to USD 4.6 billion.²¹⁸ Behind many of the transactions has been the Russian billionaire Alexander Abramov, a former scientist who made money exporting metal and coal in the 1990s, and is now the chairman of Evraz – a major international steel producer with headquarters in London. Abramov was awarded a Cypriot EU passport in July 2010 "in exchange for his service to the Republic of Cyprus".²¹⁹ His application for citizenship was handled by Anastasiades' law firm.

²¹⁵ As quoted in Charambous, L., "Who really ran Laiki Bank into the ground?" *CyprusMail*. November 17, 2013.

²¹⁶ Charambous, L., "This was a farce, not an inquiry". *CyprusMail*. September 1, 2013.

²¹⁷ Howden, D., "Cypriot leader's law firm 'broke Milosevic sanctions'". *Independent*. April 17, 2003.

²¹⁸ OCCRP and IRPY, "Bank Records Link President of Cyprus to 'Troika Laundromat'". August 14, 2019.

²¹⁹ Ibid. The shell companies that are at the heart of the OCCRP allegations include Batherm Ventures Ltd, a company registered in the British Virgin Islands, whose director is Stathis Lemis, a managing partner of the Anastasiades law firm, and Matias Co Ltd, a subsidiary of Batherm. During 2007 – 2008 Batherm transferred USD 96 million in eight instalments to Delco Networks S.A., another British Virgin Islands company, that is one of 75 companies that make up the Troika Laundromat. In 2008, Delco purchased 70,000 shares in Russian energy giant Rosneft from International Media Overseas – a company linked to Sergei Roldugin. Delco also helped shift USD 2.2 million stolen from the Russian government in the 2007 Magnitsky affair. Batherm and Matias jointly agreed to purchase Energostroyinvest-Holding, Russia's largest builder of electrical networks and thermal power plants at USD 220 million – a price well below the company's estimated value of USD 2 billion just four years later. This was paid to Gotland Industrial Inc – one of the three core companies of the Troika Laundromat.

Other high-profile transactions facilitated by the law firm are linked to the cellist Sergei Roldugin, a friend of (and widely considered a proxy holder of wealth for) Russian President Vladimir Putin. It is believed that many of their operations were handled by the Bank of Cyprus. So far the Cypriot government has not investigated the allegations, claiming that no Cypriot banks had been involved.

The main reasons why Cypriot legal firms have been able to successfully channel Russian economic interests in Cyprus and to facilitate their integration within the larger European economy are the persistent governance deficits in the application of anti-money laundering (AML) standards and the much broader problem regarding endemic conflict of interests in the country's key regulatory institutions.²²⁰ As noted above, the Central Bank of Cyprus, which serves as the country's AML supervisor in relation to banks, has been and continues to be plagued by conflict of interest risks on its board of directors. The board not only approves AML policy but also determines the resources that are used for enforcement through its con-

²²⁰ The 2018 GRECO compliance report on corruption prevention in respect of members of parliament, judges and prosecutors concludes that Cyprus has implemented satisfactorily only two of sixteen recommendations contained in the Fourth Round Evaluation Report. Of the remaining fourteen recommendations, eight have been partly implemented and six have not been implemented. In a nutshell, conflicts of interest in Cyprus are endemic, notwithstanding some limited progress in addressing them.

Box 15. Paul Manafort

Another high-profile case is that of Paul Manafort, who was convicted in the US of tax fraud and money laundering. Manafort's trial shed light on how the money laundering was carried out. This was accomplished mostly through his Cyprus bank account managed by his lawyer (named in the case as "Dr K" – a firm that belongs to an eminent Cypriot politician and former justice minister, who, according to US press reports, was recommended to Manafort by Oleg Deripaska). Manafort was generating tens of millions of dollars of income from his political activities in Ukraine while avoiding paying taxes by disguising his income as alleged "loans". In the process, he was using "nominee offshore corporate entities" and "foreign accounts". Twelve out of the fifteen foreign entities were incorporated in Cyprus and were set up during August 2007 to March 2012. The Party of Regions – a pro-Russia political party in Ukraine – retained Manafort in 2006. Dr "K" was advising Laiki bank.

Source: Orphanides, S. (2019). *"The Curious Case of Dr. K and Mr. Chrysostomides"*. OCCRP, 28 June 2019.

trol of the central bank's budget. Unlike the governor, the board has limited autonomy from the government, and comprises of, by and large, conflicted individuals with long service in the commercial banking or financial services of the country.²²¹ The conflicts within the country's AML regulator combine with conflicts of interest in politics and law enforcement to create fertile conditions for Russian capture in Cyprus. These conditions allow politically-connected law firms to promote their clients' interests without impediment. The financial crimes unit of MOKAS has twice investigated the activities of Anastasiades and his law firm, including his ties to the Troika scandal, and has in both cases cleared him of all charges – most recently at the end of December 2019.²²² Over the last decade, MOKAS has proven highly ineffective in countering money-laundering, especially cases related to high-profile Russian business entities or individuals.

Since 2013, the Cypriot government in power has shown favor to the sectors that benefit most from Russian business – corporate and banking services. The government has, for example, appointed individuals from the commercial financial services sector, including banking and accountancy firms, to the CBC board. Consequently, several current and past board members have played a key role in enabling and amplifying Russian economic influence in Cyprus. The appointment of individuals with conflicts of interest to the board of CBC indicates governance deficits in the process of appointments to

public bodies. Whereas many parliamentary democracies require the approval of the legislature for such appointments, such approval is not required in Cyprus. In Cyprus, the executive, chaired by the President of the Republic, makes such appointments on the recommendation of the Finance Ministry.

The power of the President to make appointments throughout the public sector (as well as to appoint and dismiss ministers and other state officials, including the Chief of Police) is, in fact, excessive. There are historical reasons for this to do with the Constitution of 1960 that was initially designed to create checks and balances between the powers of the Greek and Turkish Cypriot communities. However, the departure of all Turkish Cypriots from public office in 1963 has meant a lack of real checks and balances on the executive powers of the president. These disproportionate powers have, in fact, disincentivized successive presidents to make genuine efforts to solve the "Cyprus problem".

Moreover, EU membership has resulted in constitutional amendments that protect the independence of the central bank governor, who, can no longer be dismissed by the President. However, the appointment process of CBC board members has not changed significantly, allowing the President to exert pressure on the governor through the board. A further de-facto reduction of government influence on the CBC was the implementation of the Single Supervisory Mechanism at the ECB in 2014, which means that the major systemic banks are now supervised directly from Frankfurt. Nevertheless, AML/CFT regulation and supervision continue to be in the hands of EU member states. Consequently, the governance deficits arising from unchecked conflicts of interest result in the un-

²²¹ The CBC has a special section called Anti-Money Laundering/CTF and non-SSM Functions. Total number of staff is 15 but very few actually work in that area, notwithstanding past recommendations from the IMF to increase AML staff capacity.

²²² Andreou, E., "Anastasiades and law firm cleared by MOKAS in Troika Laundromat allegations", *CyprusMail*, December 20, 2019.

Box 16. Privatbank

Cyprus was also implicated in one of Ukraine's biggest financial scandals, according to the former chairwoman of Ukraine's central bank Valeria Hontareva. Specifically, OCCRP reports that the Cyprus branch of Privatbank facilitated the alleged theft of at least USD 5.5 billion of public money, an amount equivalent to one third of bank deposits in the Ukraine (or 5% of its GDP). The bank accounts of various Cypriot offshore companies were used to perform large scale fraudulent transactions – these allowed the bank's two oligarch owners, Ihor Kolomoisky and Hennadiy Boholiubov, to carry out the fraud using bogus contracts. The fraud remained undetected as the Cypriot branch was treated as a domestic branch – Ukrainian officials therefore were unable to detect that cash transferred to Cyprus was leaving the country.

Source: Stack, G. (2019). *"Oligarchs Weaponized Cyprus Branch of Ukraine's Largest Bank to Send \$5.5 Billion Abroad"*. OCCRP. 19 April 2019.

Box 17. The Klyuev group

The case of Bill Browder, co-founder of Hermitage Capital, provides a good example to illustrate the various mechanisms at play of how Cyprus serves Russia's interests. Hermitage is an investment firm that used to be the largest foreign portfolio investor in Russia, before exposing corruption in Russia and becoming one of Mr. Putin's biggest enemies outside Russia. Hermitage Capital fell victim to large-scale frauds by the transnational criminal organization known as the "Klyuev group" belonging to convicted criminal Dmitry Klyuev. According to an affidavit issued by Browder's lawyer in Cyprus, Klyuev had maintained an account at the Bank of Cyprus and had bought and sold properties in Paphos at a profit. As a result, USD 30 million of stolen funds were laundered through companies and banks in Cyprus. However, the Cypriot authorities did little to investigate Browder's complaints and chose instead to cooperate with the Russian prosecutor's service investigating Bill Browder's activities in Russia.

Source: Rosca, M. (2019). *"Activist financier targets Cyprus over Russian dirty cash"*. Politico. 26 July 2019.

der-resourcing of AML bodies and a weaker will to prosecute the key culprits, who tend to be very well politically connected. The central bank's AML section would thus often target less significant AML cases. It may even be encouraged to pursue individuals without political backing to use as scapegoats – this would show that Cyprus is serious in its fight against money laundering.

Both the US Department of State and the Council of Europe's anti-money laundering watchdog, Moneyval, have acknowledged the improvements made by Cypriot authorities to counter money-laundering activities, although severe weaknesses remain.²²³ The most pronounced governance deficits are related to the lack of supervision of the corporate service providers sector, which serve as gatekeepers of information

about the true ownership of companies and bank accounts. Despite attempts by the CBC and the MOSAK to streamline transparency procedures, formal assessments of corporate risks, as well as basic information regarding approximately 30% of registered companies are largely missing.²²⁴ Growing risks remain in the real estate market, the casino industry and the money transfer businesses, which have all been used for money-laundering operations, including by a large number of Russian entities.

Real estate and the investment-for-citizenship scheme

One factor contributing to the Russia-related boom in real estate investment may be the notorious golden visa scheme. Investment in real estate has not only

²²³ Christou, J., "EU report highlights Cyprus' vulnerability to money laundering". *CyprusMail*, February, 12, 2020.

²²⁴ Ibid.

Box 18. Danske Estonian

Cyprus was also implicated in the USD 200 billion Danske Estonian branch scandal, which is Europe's biggest ever money-laundering scandal. The Danske internal investigation revealed that around 9% of the suspicious transactions, or approximately USD 18 billion, were funneled through shell companies registered in Cyprus. As yet, it is not known which or how many Cypriot banks were involved in the Danske scandal, which took place during 2007 – 2015.

Source: In-Cyprus. (2019). “*Danske Bank scandal the answer to Cyprus’ critics*”. 26 March 2019.

become financially wise, but also a legally beneficial practice for Russian citizens doing business in Cyprus. The strongest incentive for wealthy Russians to purchase property in Cyprus has been the 2002 introduction of an investment-for-citizenship program by the government that aimed to increase foreign investment. This money-for-passports program gives the opportunity for foreigners to become Cypriot (and hence EU) citizens in a matter of 6 months if they invest at least EUR 2 million in property or EUR 2.5 million in companies or government bonds.

Procedurally, the investment-for-citizenship scheme of Cyprus is one of the fastest citizenship programs in the world. An application takes about 6 months to be approved; for minor children, only 3 weeks. Another benefit of the program is that the spouse or partner of the investor has the right to apply for the citizenship alongside the investor. The parents of the main applicant can be added to the same application under the condition of an additional investment of EUR 500,000 in residential property. The properties acquired may then be rented out through the developers, and are advertised with possible rental returns of 4-7%. The submission fee is EUR 2,000 per individual, the certificate issuance fee is EUR 5,000 and legal fees are usually covered by the developer. These figures indicate that the “approved real estate” is sold with very large profit margins, allowing developers to pay hefty commissions to law firms that do the work. By mid-2017, Cyprus had granted citizenship to 3,322 individuals under the program, 34.3% of whom are of Russian origin.²²⁵

The citizenship program has attracted USD 4.4 billion in investment over the last four years, creating a construction boom that many Cypriot economists (including Cyprus’ independent Fiscal Council) have described as “unsustainable,” a “source of Dutch dis-

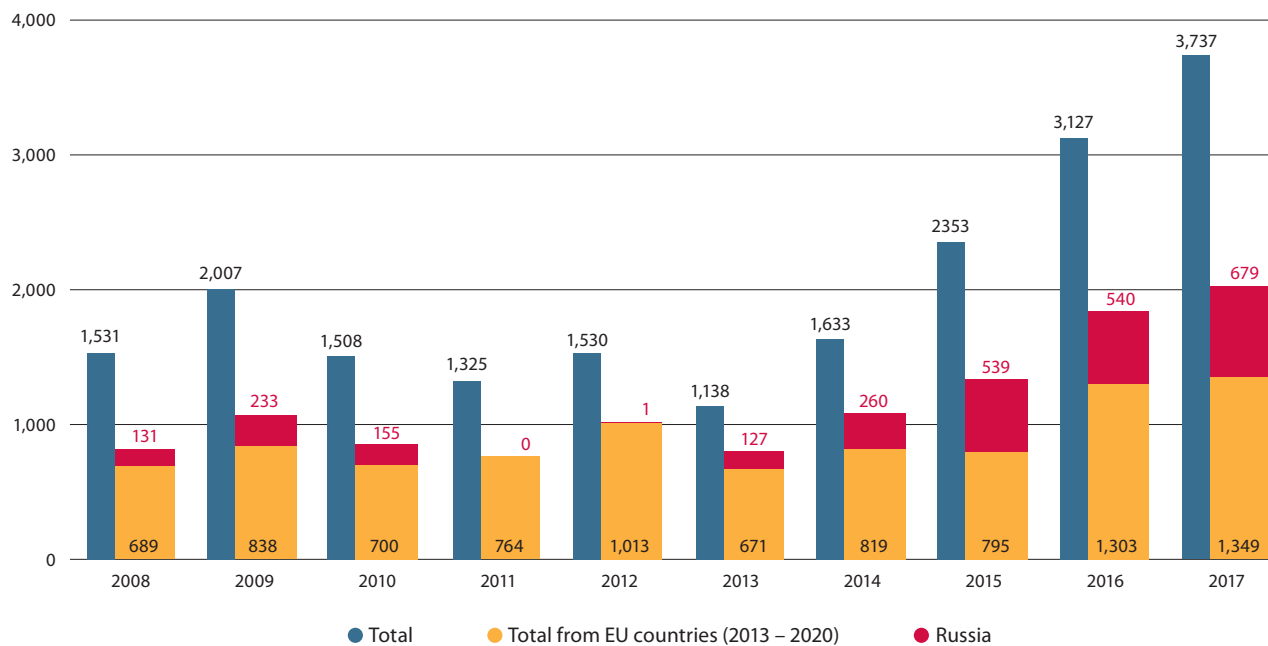
ease,” a “distortion of resources” and a “bubble.”²²⁶ There have also been complaints criticizing the high-rise buildings in Limassol as environmentally unfriendly. It has also sparked outcry by Cypriot citizens that the scheme has pushed rents to unaffordable levels, benefiting the few at the expense of the many – particularly the younger demographic. Following pressure from the EU, however, the program is becoming stricter and more expensive. It will also require applicants to be in possession of a Schengen visa.

The schemes grant many privileges to wealthy Russians. First, Cypriot citizenship automatically hands them all the rights and privileges EU citizenship provides – namely the right to free movement of goods and capital. This also includes free travel and work within the EU, and the benefit of visa-free travel to 159 countries worldwide. A Cypriot citizenship also yields tax benefits as Cypriot local authorities are no longer obliged to report the new citizen’s investment revenues to the Russian tax authorities. In addition, the Cypriot citizenship makes round-trip investments more flexible and harder to track. One major loophole of the scheme, however, allows investors to give up their business interests in Cyprus years after acquiring their citizenship, while still retaining the advantage of EU mobility. This defeats the main aim of the program advocated by the government – that is, to attract and cultivate long-term foreign investment in Cyprus.²²⁷

²²⁶ Farolfi, S., Pegg, D., and Orphanides, S., “Cyprus ‘selling’ EU citizenship to super rich of Russia and Ukraine,” *The Guardian*, September 17, 2017.

²²⁷ One notable example is the granting of citizenship to the Russian oligarch Oleg Deripaska. Despite the controversies surrounding Mr. Deripaska, his application to the program was approved in 2017. Another possible red flag is the naturalization of the founders of the Ukrainian PrivatBank, Hennadiy Boholiubov and Ihor Kolomoisky who along with Russian oligarch Olegskiy Martynov were the three members of the bank’s Supervisory Board before the nationalization of PrivatBank.

²²⁵ Russia-Cyprus Business Association, EY Cyprus.

Figure 27. Acquisition of Cypriot citizenship by former citizenship, number of persons

Source: Eurostat.

Cyprus has been heavily criticized by the European Commission for the laxity of the scheme, which may attract high-risk individuals, including money launderers and criminals who seek to protect proceeds from corruption or fraud.²²⁸ Moreover, the scheme is operated by law, accountancy and consultancy firms (many of which have political connections) who act as agents for individuals wishing to apply for citizenship.

* * *

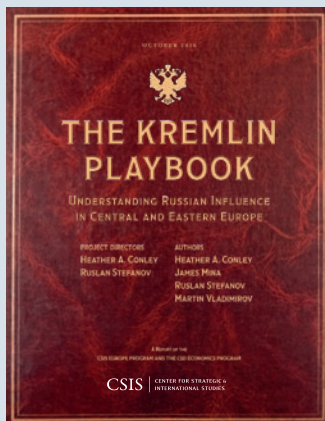
The assessment of the Russian economic footprint in Cyprus has revealed it to be the European country most vulnerable to Russian influence – economically and, to an extent, politically. Besides being the largest foreign economic player controlling directly or indirectly around a third of the Cypriot economy, Russia has also developed mechanisms to translate its economic presence into political leverage via state capture networks whose influence extends to the President himself. In addition, Russian businesses have transformed the Cypriot financial sector into their accounting and legal back-office. By utilizing politically well-connected consultants and lawyers, Russian companies have exploited governance gaps

in financial and corporate ownership regulations in order to:

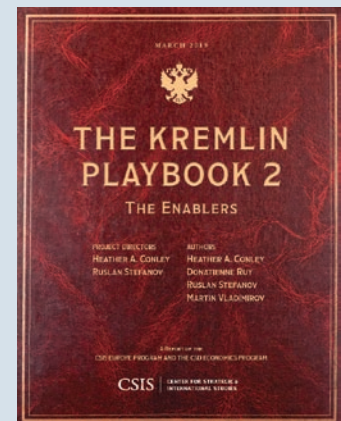
- enable round-tripping investment operations – these allow funds to pass through European banks and flow back to Russia or Europe while hiding their purpose and yielding no real economic activity;
- avoid and evade taxation, and obfuscate the ultimate beneficial ownership of assets globally;
- launder proceeds from illicit activities, including bribery, organized crime and public funds embezzlement;
- execute schemes for reallocating funds to Russian-influenced political activities and media propaganda in Europe;
- create special purpose vehicles, mostly used for big investments or mergers, to finance acquisitions while hiding beneficial ownership.

Cyprus has thus become a **key enabler of the Russian economic and political influence in all of Europe**. Russian-owned Cypriot entities have facilitated the deep penetration of Russian companies in European finance and trade. They have also been used to reallocate and store corporate profits from Russian economic activities in the EU. In turn, Cypriot state capture networks have benefitted from their relationship with Russian companies through rent seeking. They have used their access to Russian capital to transform the Mediterranean island into one of the most important offshore hubs in Europe.

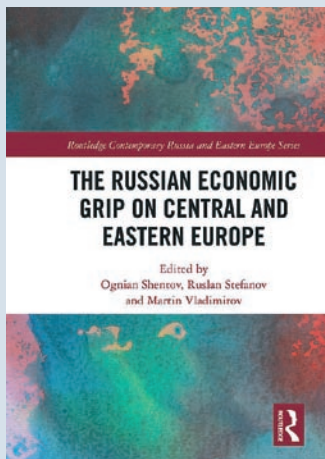
²²⁸ See: *Investor Citizenship and Residence Schemes in the European Union*. Report from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions. Brussels, 23.1.2019 COM(2019) 12 final.



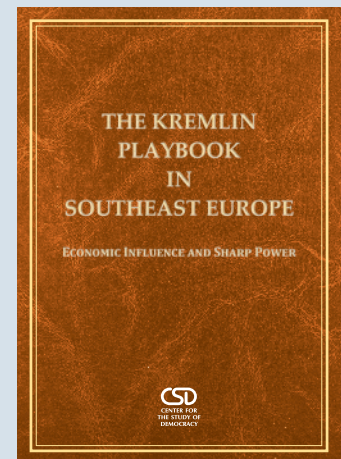
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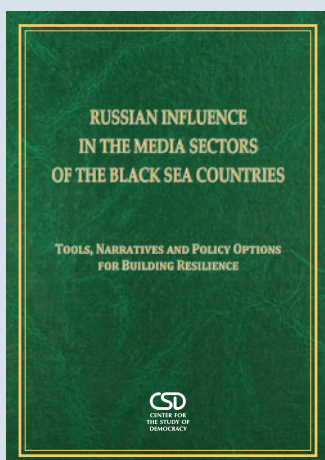
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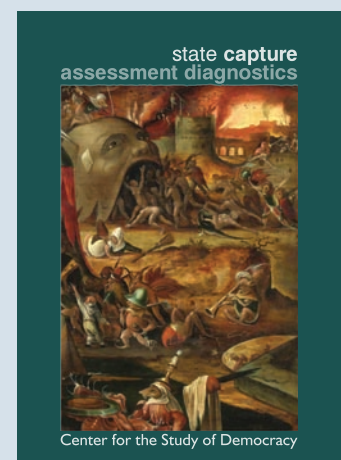
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