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MEMORANDUM FOR: DDI
D/SOVA
D/EURA

I obtained this critique of the SOVA/EURA pipeline paper informally. The DCI has a copy for background use. I hope the critique will not be sent formally to the DCI so that a full response will not be required. The new paper SOVA is doing at the DCI's request should serve policymakers' needs for a broader perspective. Other comments could best be handled at the working level.


Maurice Ernst
NIO/Economics

Date 1 September 1982

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**Items from CIA Study Not Included in Proposal
for Allied Control (Key to CIA Chart)**

Well-logging Equipment: left out of proposal due to limited impact on Soviets; U.S. not historic source of supply

Drill pipe and Tool Joints: not included due to wide number of non-Soviet suppliers outside Allied group who could undercut embargo; U.S. not historic source of supply

Other specialized drilling equipment: only moderate to minimal impact on Soviet production; availability outside Allied embargo (Austria, Finland)

Hydraulic pumps (oil): only moderate to minimal impact on Soviet production; low technology (counter balanced by high degree of U.S. control)

Casing and Tubing (gas): U.S. not historic source of supply; limited delay before Soviets could find alternative source of supply

Large Diameter pipe: for reasons stated in Tab A; U.S. not historic source of supply

Large diameter valves: as in pipe but greater degree of U.S. control through U.S. subsidiaries

Oil refining equipment: U.S. not historic source of supply; at present no Soviet demand; embargo would have no practical effect

In forming the proposed list of items for Allied control in the oil and gas equipment area, the main source of information was an Office of Technology Assessment, November, 1981 study on Soviet dependence on Western oil and gas equipment and technology.

The OTA study had several benefits for this purpose. The study is the most comprehensive source of information in the area and includes the greatest specificity as to actual Soviet imports, item by item, of Western oil and gas equipment and technology over the last seven years. The study also contains information on the relationship between European suppliers and their U.S. parents or licensors. Finally, data from the OTA study is unclassified and could be released in any forum.

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OIL AND GAS EQUIPMENT AND TECHNOLOGY

OBJECTIVE

Sufficient Western restraint on future transfers of oil and gas technologies to the USSR to warrant lifting of U.S. retroactive controls.

ANALYSIS

Until the Reagan Administration the United States had never developed a clear policy as to whether Soviet oil and gas production furthered or impeded Western interests. Even now the fact that the sanctions are tied to Poland reflects some ambivalence.

In the late 1970's, one of the arguments for approval of exports to the USSR of some mid-performance U.S. computers for oil exploration seismic data processing was the possible beneficial effect on the world oil market.

In 1978, the United States imposed controls on exports to the USSR of equipment and technology for exploration and production of oil and gas. But this action was designed as a "flexible tool of foreign policy" and all license applications were approved until revocation of the Dresser drill bit plant license in late 1980.

In March 1980, one of the escape clauses in the U.S. post-Afghanistan proposal to COCOM for a no-exceptions policy was "items that protect Western access to vital commodities or services" and the example given was a computer to regulate the flow of gas on the Orenburg pipeline.

In July 1981, the United States proposed at the Ottawa Summit a "prudent approach" to East-West economic relations, which pointed out the dangers of trade dependency relationships with the USSR. But the Europeans made clear at Ottawa their intent to proceed with the Siberian gas pipeline and the United States imposed no controls at that time which would affect that pipeline.

In addition to the vulnerability from dependence argument, United States officials have from time to time observed that Soviet hard currency earnings from sales of gas delivered through the pipeline would strengthen the USSR economically, permitting, inter alia, larger purchases of strategically significant high technology.

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After the imposition of martial law in Poland on December 13, 1981, U.S. controls were expanded on December 30 to cover transmission and refining for energy use and on June 22 to cover non-U.S. origin items from subsidiaries and products manufactured by licensees using previously transferred technology. These controls had a clear impact on the pipeline; but we have stated that they would be lifted if the three conditions for improvement in Poland stipulated in the NATO January 11 communique were met (lifting of martial law, freedom for political detainees, and resumption of dialogue with Solidarity and the church).

Our Allies have consistently resisted the imposition of controls on exports to the USSR for other than strategic security purposes.

In 1978 the United States asked France and others not to substitute for a computer we denied to TASS in reaction to the Shcharansky trial and the arrest and harrassment of a U.S. businessman and U.S. journalists. However, France proceeded to sell a more powerful computer to TASS, in spite of a U.S. objection in COCOM.

The only agreed Allied export control in response to Afghanistan was a COCOM no-exceptions policy with escape clauses, and even this was based on de facto observance rather than recorded agreement. In 1980, French and German firms replaced American steel mill and aluminum smelter exports to the USSR denied by U.S. post-Afghanistan sanctions, despite assurances from the French and German governments not to undermine U.S. measures. This public display of Allied disunity led to a major effort in NATO to develop an agreed contingency plan for export (and credit) controls in the event of Soviet military intervention in Poland.

The 1981 NATO contingency plan called for a total export embargo (except pre-existing contracts) and a cutoff of all new government-supported credits. This plan was not invoked after December 13, 1981, because the Europeans considered that imposition of martial law in Poland was not a serious enough development to warrant such controls. The Europeans, acting through the EC, did agree with a U.S. proposal to expand the COCOM no-exceptions policy to cover exports to Poland; but they have protested U.S. objections in COCOM to Polish escape clause cases which are not supported by specific strategic rationale.

The only controls on exports to the USSR which our Allies have historically agreed to impose affect items on the COCOM list. Some equipment of significance to the oil and gas industry is already on the COCOM list, principally

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exploration equipment (such as magnetometers, gravity meters, computers, recording equipment, and hydrophones) and computerized pipeline control equipment. These items are on the COCOM list because of concerns other than oil and gas, for example computerized seismic equipment is used not only for oil exploration but also for anti-submarine warfare (ASW). The United States proposed in 1978 that COCOM tighten computer controls by adding a sub-item on special signal processing, which would more effectively restrict array transform processors (ATPs), which are used for both oil exploration and ASW. COCOM did not concur, primarily because the United States did not agree to liberalize controls on general purpose computers. We are trying again in 1982 to obtain tighter COCOM controls on ATPs, but other COCOM members may once again insist on liberalization of general purpose computers.

We will have an even more difficult time persuading the Allies to control oil and gas equipment which does not also have other uses of military concern.

The largest value item in Western exports of oil and gas equipment to the USSR is pipe, mostly from Germany, Japan, and Italy (about \$1 billion per year). In the 1960's, amidst much controversy, Germany eventually acceded to a U.S. proposal to ban pipe exports to the USSR. The USSR subsequently thanked the United States for this incentive to develop an indigenous Soviet pipe industry. The ban on Western pipe exports was shortlived. For many years, such exports have supplemented Soviet production. Pipe purchases are in bulk, with distribution made to a variety of Soviet projects.

FRG pipe sales to the Soviet Union for the West Siberian pipeline are contracted on an annual basis. This arrangement was developed partly as an FRG response to Soviet demands for lower interest rates. This reduced the size of the overall contract and allowed negotiations to be based on market terms and conditions closer to the actual time of delivery. The US-EC arrangement on steel exports to the United States is contingent on agreement by Mannesmann to reduce exports of pipe and tube to the United States. Given this history, European agreement to embargo pipe would be very difficult to achieve.

At least some of the European arguments for opposing controls on oil and gas equipment would be overcome if our proposal was limited to items with substantial impact on the USSR (other than pipe) and historically exported to the USSR largely by the United States.

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The following fit the above description:

I. Exploration

Magnetometers, gravity meters, and seismic equipment (including data processing hardware and software) - These items are already either on the COCOM list or in U.S. proposals to COCOM for revisions of that list. Therefore they need not be included in a new request for Allied controls.

II. Drilling

Offshore positioning equipment, tensioners, risers, and motion-compensating systems;

High-quality drill bits;

High pressure blow-out preventers with automatic controls;

III. Production

Deep submersible pumps;

Gas wellhead assemblies and down hole completion equipment;

IV. Gas pipeline

Pipelayers;

Compressors and turbines.

V. Gas processing equipment

Lists of significant Soviet purchases from the West of such equipment during the period 1975 to 1980 are attached. United States equipment and technology figured prominently in these sales, although in many cases the sales were not directly from the United States.

TALKING POINTS

- o IN 1981 WE COLLABORATED IN NATO TO DEVELOP A CONTINGENCY PLAN WHICH CALLED FOR A TOTAL EMBARGO ON EXPORTS TO THE USSR, EXCEPT PRE-EXISTING CONTRACTS (AND A CUTOFF OF ALL NEW GOVERNMENT-SUPPORTED CREDITS) IN THE EVENT OF SOVIET MILITARY INTERVENTION

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IN POLAND. AFTER THE IMPOSITION OF MARTIAL LAW IN POLAND ON DECEMBER 13, 1981, THIS PLAN WAS NOT INVOKED.

- IT IS ARGUABLE THAT THE SITUATION IN POLAND MAY NOT BE SERIOUS ENOUGH TO WARRANT A TOTAL EMBARGO ON NEW CONTRACTS FOR EXPORT TO THE-USSR. HOWEVER, IT IS CERTAINLY SERIOUS ENOUGH TO WARRANT A CONCERTED ALLIED REACTION.
- INCREASED REPESSIVE ACTIONS OF THE POLISH GOVERNMENT IN PUTTING DOWN DEMONSTRATIONS MARKING THE FIRST ANNIVERSARY OF SOLIDARITY WITH LOSS OF LIFE AND MUCH SUFFERING EMPHASIZES THE NEED FOR A COMMON WESTERN RESPONSE OF DISAPPROVAL.
- A LIMITED YET SIGNIFICANT REACTION MIGHT BE A PROHIBITION OF EXPORTS TO THE USSR, OTHER THAN PRE-EXISTING CONTRACTS, OF KEY OIL AND GAS EQUIPMENT THE PRECISE LIST WOULD BE SUBJECT TO NEGOTIATION, AS WOULD THE DEFINITION OF PRE-EXISTING CONTRACTS. WE HAVE IN MIND ITEMS SUCH AS OFFSHORE DRILLING EQUIPMENT, HIGH QUALITY DRILL BITS, HIGH PRESSURE BLOW-OUT PREVENTERS, DEEP SUBMERSIBLE PUMPS, GAS WELLHEAD ASSEMBLIES AND DOWN HOLE COMPLETION EQUIPMENT, GAS PIPELINE COMPRESSORS AND TURBINES, AND GAS PROCESSING EQUIPMENT. THIS WOULD BE IN ADDITION TO COMPUTERS AND OTHER EQUIPMENT ALREADY ON THE COCOM LIST.

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- THE UNITED STATES HAS HISTORICALLY BEEN A MAJOR SUPPLIER OF THESE ITEMS, IN SOME INSTANCES THE SOLE SUPPLIER.
- WE SHOULD BE PREPARED TO REACH AGREEMENT NOT TO ENTER INTO CONTRACTS CONNECTED WITH THE SECOND STRAND OF THE SIBERIAN PIPELINE.

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Western Sales to the Soviet Union, 1975-1980,
Of Oil and Gas Equipment and Technology
Proposed for Allied Controls

The following two Tables record a sampling of Western exports of oil and gas equipment and technology to the Soviet Union during the period 1975 to 1980 in the areas proposed for new Allied controls. In key areas the United States is the sole supplier (submersible pumps) or the preferred supplier (gas turbine technology). Many European exports are from subsidiaries of U.S. firms and much of the technology that serves as a basis for European exports originated in the United States.

1/ Source - "Technology and Soviet Energy Availability, Office of Technology Assessment, Congress of the United States, November 1981. This document cites its source as the bi-monthly publication "Soviet Business and Trade". The OTA study states that U.S. industry representatives have indicated that information in this publication about their firms' activities is generally accurate but that OTA has made no attempt to validate total authenticity or completeness of the data.

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POINT-COUNTERPOINT PAPER

OIL AND GAS EQUIPMENT AND TECHNOLOGY

I. ISSUE

The Europeans will probably be reluctant to control exports beyond militarily critical COCOM items.

II. ESSENTIAL FACTS

The Europeans have not heretofore agreed to impose controls on exports to the USSR beyond items on the COCOM list. They are intent on proceeding with the pipeline.

III. TALKING POINTS

Criticism: Why do you propose controls on oil and gas equipment if you are unwilling to reimpose a grain embargo?

Response: The oil and gas equipment items we suggest be considered for control are items which could contribute significantly to Soviet ability to create conditions of political vulnerability. They are items for which there is a critical need in the USSR. They are items for which the United States has historically been a major supplier. On January 11, the North Atlantic Council agreed that "the Allies will maintain close consultations on the implementation of their resolve not to undermine the effect of each other's measures." Allied controls paralleling some of the U.S. measures would constitute a form of not undermining. A U.S. grain embargo is demonstrably of little effect unless other major grain suppliers cooperate. Even an effective grain embargo would not deny the USSR a critical need. Domestic grain supplies are adequate to feed the population on a diet with less meat.

Criticism: If we deny the Soviets help in developing their oil and gas resources now, won't that mean they will import energy from world markets and create tighter conditions for us in the future?

Response: Denial to the Soviets of the types of equipment we have in mind will not affect Soviet production for four to six years, because of the relatively long time lags in

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bringing these projects on line. Moreover, we believe it is highly unlikely the Soviets would expend the large amounts of hard currency necessary to import substantial energy supplies. Rather, they would restrict domestic consumption. The net impact on world energy supplies would therefore be small and would occur relatively far in the future. The cost to the Soviets, on the other hand, would be substantial and would be a clear demonstration to them of the consequences of their role in the repression in Poland.

Criticism: The purpose of establishing a supply relationship is to garner a continuing share of the oil and gas equipment market in the Soviet Union. Why should the Europeans and Japanese give up potentially valuable export markets?

Response: The value of the Soviet market for Western exports of oil and gas equipment ultimately depends on the possibility of increasing Soviet supplies to meet an increase in world energy demand. The same benefits could be derived from Western exports to Western nations for the development of non-Soviet sources of energy in response to an increase in energy demand. In addition, investment in Western energy production would have a beneficial multiplier effect for Western economies that would be foregone if the capital equipment were shipped to the Soviet Union.

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