

**APHRODITE'S GIFT:  
CAN CYPRIOT GAS POWER A NEW DIALOGUE?**

Europe Report N°216 – 2 April 2012

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## **APHRODITE'S GIFT: CAN CYPRIOT GAS POWER A NEW DIALOGUE?**

### **EXECUTIVE SUMMARY**

Eastern Mediterranean tensions have risen since late 2011, when Greek Cypriots unilaterally began drilling in their rich offshore hydrocarbon reserves and Turkey responded with tough criticism and threatening naval manoeuvres. Contested maritime boundaries and exploration of natural gas deposits off the divided island are the sources of the current dispute, but tensions also result from the slow-down of UN-mediated Cyprus reunification talks. A paradigm shift is needed. The gas can drive the communities further apart and increase discords, or it can provide an opportunity for officials from all sides, including Turkey, to sit down and reach agreements on the exploitation and transportation of this new find.

A year ago, when the Cyprus negotiations were already at an impasse, Crisis Group proposed six steps to build confidence and help establish an environment more conducive to an overall agreement. None of these were implemented; instead the talks dried up and trust between the parties eroded further. As we wrote in February 2011, neither Greek nor Turkish Cypriots can fulfil their potential on an island whose future is divided, uncertain, militarised and facing new economic difficulties. Turkey's European Union (EU) membership negotiations are at risk, and with Cyprus out of NATO and Turkey in, their disputes continue to hamstring EU-NATO cooperation. The start of offshore drilling in September 2011 has now put these threats into sharper focus.

In September 2011, the Republic of Cyprus, with the help of U.S.-based Noble Energy Inc., started offshore drilling south of the island and discovered significant gas reserves in the Aphrodite field, where drilling started. It is likely to find more and in February 2012, bidding for the remaining blocks was announced. It considers that it has a sovereign right to drill in its exclusive economic zone (EEZ), which it has delineated with Egypt, Lebanon and Israel, but not Turkey, Syria or Greece. Further complicating the situation, Noble Energy's operating company is 30 per cent owned by Israeli interests and the Aphrodite field is partly in Israel's EEZ. Turkey also now has frictions with both Cyprus and Israel, which have recently signed defence and cooperation agreements.

Turkey does not recognise the Republic of Cyprus, and contests its right to enter into EEZ agreements or to exploit unilaterally natural resources until there is a comprehensive settlement. It argues that the Greek Cypriot government does not represent the interests of Turkish Cypriots or a united island, refutes Greek Cypriot claims to exclusive sovereignty, saying sovereignty is being negotiated in the current talks, and evokes its status as a guarantor state under the 1960 Treaty of Guarantee to protect Turkish Cypriots' rights. Greek Cypriot drilling thus provoked a harsh reaction, with Ankara sending ships close to Greek Cypriot installations, signing maritime boundary agreements with the Turkish Cypriots, delineating the continental shelf between the Turkish coast and the north of the island, beginning its own gas prospecting off Cyprus, and announcing it will drill on land in the north on behalf of Turkish Cypriots.

The Republic of Cyprus has a sovereign right to explore and exploit inside its maritime zones, has an acute economic need for new revenues, and can justifiably complain about Turkey's actions and threats. Nevertheless, its unilateral start of exploration is a violation of the pledge to share natural resources, and undermines the already fragile reunification talks. Vague Greek Cypriot promises of sharing gas revenues in the future do not satisfy the Turkish Cypriot community. But the latter and Turkey, too, are acting provocatively and against the spirit of the talks by signing a continental shelf delimitation agreement, prospecting and drilling. Turkey, with its long coastline, has genuine concerns about losing its fair share of any eastern Mediterranean maritime zones as the Republic of Cyprus, and possibly Greece, establish EEZs; but Ankara needs to stop refusing offers of dialogue and engage with Greek Cypriots to defend its claims.

The Greek Cypriots say they will have to decide quickly on how to transport this new gas. Pumping the Cypriot gas to Turkey and on to the EU would be a much better option politically, and possibly economically. This is highly unlikely in the current circumstances, meaning Greek Cypriots may choose a more expensive liquefied natural gas (LNG) option, bypassing Turkey and Turkish Cypriots.

But the extra risks associated with the unresolved conflict will make any LNG development more expensive to finance and difficult to find markets for, Turkish threats will likely keep most major oil companies on the sidelines, there is not yet enough Cypriot gas to make an LNG plant truly profitable, and extra Israeli volumes seem unlikely. Energy executives say such circumstances will result in long delays.

The prospect of this costly tit-for-tat should make all re-commit to a comprehensive settlement to reunify the island, divided politically since Greek Cypriots seized control of the Republic of Cyprus in 1963 and militarily since a Turkish invasion in 1974 created a Turkish Cypriot zone on its northern third. Greek and Turkish Cypriots have agreed that natural resources and international agreements, including those delineating maritime boundaries, will be a federal competence in a reunited island. But progress over the next year in the UN-mediated talks seems unlikely. The UN, Turkey and Turkish Cypriots see a natural deadline when the Republic of Cyprus takes over the rotating EU presidency on 1 July 2012. Reaching substantive compromise is even more unlikely now that the Greek Cypriot political scene is indexed to the February 2013 presidential elections.

Even in the absence of an overall Cyprus settlement, the parties should re-examine the benefits of independent confidence-building moves, seek mutual advantage and avert a deepening of the crisis by taking these steps specific to the energy issue:

- The Greek Cypriot leadership should commit to share 20 per cent of any net revenue or gas from any offshore hydrocarbon resources with Turkish Cypriots, possibly distributed through a UN-supervised arrangement, as long as both parties remain formally committed to reunification. Turkish Cypriots should commit to share with the Greek Cypriots an inverse proportion of their hydrocarbon revenues from their ongoing onshore drilling activities.
- Greek Cypriots should agree with Turkish Cypriots to form a bi-communal, advisory ad hoc committee to discuss energy issues, and to plan potential domestic and industrial use of the gas throughout the island.
- Turkey and Turkish Cypriots should stop using threatening rhetoric and naval manoeuvres inside the island's EEZ, even if they dispute its limits; and formally commit not to interfere with, or to drill in, offshore hydrocarbon blocks that are in these waters, including the new Aphrodite field and areas west of Cyprus, pending an arrangement.

If the basic environment for dialogue is established:

- Turkey and the Republic of Cyprus should agree, possibly with third-party mediation, to discuss eastern Med-

iterranean energy issues, without prejudice to the UN-facilitated talks, or to any official recognition that will follow a settlement. They should study the feasibility of and consider possible cooperation on a gas export pipeline to Turkey, and onwards to Europe, with strong third-party arbitration clauses.

- Turkey, Cyprus and Greece should agree to take their claims for EEZs in the eastern Mediterranean to the International Court of Justice (ICJ) or an arbitral tribunal.

Cooperation on the exploitation of significant gas finds, which Greek and Turkish Cypriot leaders agree are a common heritage, can help build confidence without prejudicing the eventual outcome of comprehensive talks. If the sides continue engaging in unilateral actions, tensions will rise, accidents will become more likely, and Turks and Greek Cypriots will be on course for a head-on collision in the eastern Mediterranean.

**Nicosia/Istanbul/Brussels, 2 April 2012**

## APHRODITE'S GIFT: CAN CYPRIOT GAS POWER A NEW DIALOGUE?

### I. INTRODUCTION: REUNIFICATION TALKS STALL

Prospects for a comprehensive political settlement to reunify Cyprus' 1.1 million inhabitants, whether it is a federal model or a looser arrangement, are dimming every day.<sup>1</sup>

The last round of reunification talks since March 2008 has failed to produce tangible progress. This is despite four years of face-to-face meetings between the leaders of the two communities under UN auspices in which they deliberated over six official and one unofficial chapters.<sup>2</sup> All sides share the blame: the Greek Cypriot leadership for not pushing forward quickly in 2008 when pro-solution leaders were in power on both sides of the island; Greek Cypriot political parties for continuing to block compromise in talks; Turkish Cypriots for electing a hardline leader in 2010; Turkey for losing its EU path and interest in a Cyprus solution; and the EU for allowing Greek Cypriots' obstructive tactics against Turkey and for not keeping its 2004 promise to put an end to the Turkish Cypriot community's isolation.

After four decades of division, the two communities have said they want a bi-zonal, bi-communal federation but have failed to define its parameters.<sup>3</sup> Political jockeying ahead of the May 2013 Greek Cypriot presidential elections

makes compromise even more difficult. Almost nobody close to the talks voices the hope that they will advance in the near future. Turkish Cypriots are very explicit about their scepticism;<sup>4</sup> Greek Cypriots admit in private that the public is ready to discuss alternatives to reunification.<sup>5</sup> As a prominent Greek Cypriot observer muses, "We've got to the point in a chess game where the pieces can only move to a couple of places, and neither side can win".<sup>6</sup>

The leaders came together with the UN Secretary-General Ban Ki-moon five times since November 2010 in trilateral summits outside the island, twice in Geneva and three times in New York. Like the previous four, the last meeting at the Greentree estate in New York on 22-24 January 2012 disappointed.<sup>7</sup> No one wants to incur the stigma of

<sup>4</sup> "We're far from a solution. The Greek Cypriots won't sign anything. There is no point talking after 1 July [when they take over the EU Presidency]. After 40-50 years, there's nothing that hasn't been discussed. There's now a reality here [of two states]". Crisis Group interview, Derviş Eroğlu, president of the self-declared Turkish Republic of Northern Cyprus (TRNC), Nicosia, 23 February 2012. "We have tried mediation, arbitration, special representatives, working breakfasts, leaders' retreats, leaders from the right, left in every combination. This was the failure of the last method that we had left to try. After 40 years, if we can't establish a settlement like this, [we're stuck] ... this exhaustion should be declared by the UN". Crisis Group interview, Kudret Özersay, Turkish Cypriot chief negotiator, Nicosia, February 2012.

<sup>5</sup> A Greek Cypriot former official agrees that talks are at a standstill: "I can see very clearly that failure is coming. Christofias [president of the Republic of Cyprus] and Eroğlu can't make it. There is complete mistrust. ... We are going [toward] a two-state solution". Crisis Group interview, Nicos Rolandis, former Greek Cypriot foreign and commerce minister, Nicosia, 23 February 2012. A leading Greek Cypriot politician says nationalism is on the rise and the new generation believes in "ethnically pure areas". Crisis Group interview, Nicosia, February 2012.

<sup>6</sup> Crisis Group interview, Alexandros Lordos, Greek Cypriot polling expert, Nicosia, 22 February 2012.

<sup>7</sup> Before the summit, both sides admitted there had been almost no progress since a previous trilateral meeting in October 2011. Ban Ki-moon said they achieved "limited progress", and assigned his special adviser, Alexander Downer, to report back to him at the end of March 2012 focusing on three areas: property, governance and citizenship. Unlike previous trilateral meetings, Ban did not set a date for another summit. A senior internation-

<sup>1</sup> For previous Crisis Group reporting, see Europe Reports N°171, *The Cyprus Stalemate: What Next?*, 8 March 2006; N°190, *Cyprus: Reversing the Drift to Partition*, 10 January 2008; N°194, *Reunifying Cyprus: The Best Chance Yet*, 23 June 2008; N°201, *Cyprus: Reunification or Partition?*, 30 September 2010; N°210, *Cyprus: Bridging the Property Divide*, 9 December 2010; and Briefing N°61, *Cyprus: Six Steps toward a Settlement*, 22 February 2011.

<sup>2</sup> Chapters include governance and power-sharing, EU matters, the economy, property, territory, security and guarantees. Citizenship and settlers is the unofficial seventh area.

<sup>3</sup> Since the High Level Agreements of 1977 and 1979, the goal has been a federation. "The concept of the bi-zonal, bi-communal federation has lost its meaning not only between the two communities but also within each community; everyone understands different things from this phrase!" Crisis Group interview, Kudret Özersay, Turkish Cypriot chief negotiator, Nicosia, February 2012.

breaking off the talks, and they may stumble along in some form, but the UN has been giving signals of scaling back its mission and possibly winding down its involvement.<sup>8</sup>

For decades, a main obstacle to a settlement has been total lack of any state-to-state contacts, communication and trust between Turkey and the Republic of Cyprus. Ankara does not recognise the Republic of Cyprus, seeing its government as a Greek Cypriot monopoly, and has mostly refused to engage its officials, even unofficially. Dropping a condition to be received as the Republic of Cyprus' president in early 2011, Christofias told Turkish media, "I want to meet [Prime Minister] Erdoğan and [President] Gül, even if this is unofficial. I want to explain to them my vision for a settlement. Let's eat fish on the Bosphorus, without sidelining the Turkish Cypriots. We can solve Cyprus with Erdoğan".<sup>9</sup> He was rebuffed. Officials on either side do not believe the other genuinely wants a settlement to which it will stick.

Turkey's unwillingness to fulfil its 2005 EU Customs Union commitment (the Additional Protocol to the Ankara Agreement) to open its ports and airports to Republic of Cyprus vessels compounds this problem.<sup>10</sup> Now Turkey pledges it will not engage the Republic of Cyprus' EU presidency at all in the second half of 2012, even if Greek Cypriots open some of Turkey's blocked negotiating chap-

ters,<sup>11</sup> and a leading minister has even threatened to annex the north.<sup>12</sup>

Crisis Group suggested in February 2011 that the sides should take some confidence-building steps, together or separately, to build trust and address their counterparts' main concerns without prejudicing the outcome of an eventual settlement.<sup>13</sup> This included movement on the Additional Protocol, as well as breaking the isolation of Turkish Cypriots, whom the Republic of Cyprus blocks from any autonomous activities, from fielding their own teams in international competitions to trading directly with the EU (see Section V.A.2, below). Neither Ankara nor Nicosia expressed any interest in taking these steps separately and instead conditioned any movement on the other side's moving too, with Turkey for example stating that for it to implement the Additional Protocol, the Republic of Cyprus should allow international flights to land at Ercan airport in the north of the island.

The discovery of offshore natural gas deposits shows how time makes a sustainable, negotiated solution harder to reach. The window of opportunity is narrow – dialogue should start in the next twelve months, before Greek Cypriots are likely to commit to the exploitation and transportation of gas, bypassing Turkey and the Turkish Cypriots. Currently unable to even talk to Ankara, Greek Cypriots show little interest in contemplating cooperation on gas.<sup>14</sup>

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al official wonders if the process since 1977 is now dead, pointing out that while Turkish Cypriot leader Derviş Eroğlu has reneged on previous convergences, the Greek Cypriots do not seem to want a deal, either. Crisis Group interview, February 2012.  
<sup>8</sup> On 14 December 2011, Ban Ki-moon noted that the opportunity for further progress in negotiations was "very much limited". In a 4 January letter to the leaders he said talks had hit "an impasse", and warned again on 6 January that "we cannot go on this way, and considering that Cyprus is going to take the Presidency of the European Union from 1 July, there is not much time left". "Talks 'cannot go on this way'", *Cyprus Mail*, 8 January 2012.

<sup>9</sup> Interview, *Milliyet*, 7 January 2011.

<sup>10</sup> In December 2005, the EU Council blocked eight of Turkey's 35 negotiating chapters for this non-compliance, which remain frozen. In December 2009, Greek Cypriots unilaterally blocked six more. Taking into account chapters blocked by France because of its objection to Turkey's membership, and the ones currently open, Turkey has three difficult chapters it can negotiate on before its EU process comes to a standstill. In 2010, the European Commission and Belgian EU presidency failed in a new attempt to facilitate agreement between the Republic of Cyprus and Turkey on a phased opening of sea ports and airports. On the other hand, Turkish officials argue that Turkey "is in fact implementing the Customs Union, refusing that [its] implementation includes opening ports and airports". Crisis Group email correspondence, March 2012.

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<sup>11</sup> "We will not sit at the table with Greek Cypriots even if they opened twenty chapters!" Turkish Foreign Minister Ahmet Davutoğlu quoted in *Sabah*, 8 March 2012.

<sup>12</sup> Outcomes envisaged by Turkey's Minister for EU Affairs Egemen Bağış included "Reunification under a deal that [the two] leaders could reach, creation of two independent states after an agreement between the two leaders if they are unable to reach a deal for reunification, or annexation of the TRNC to Turkey". Interview with *Kıbrıs*, 3 March 2012. "[Since] the government has remained silent and the minister did not denounce the option, we may assume that annexation is a policy option seriously being considered in Ankara". İhsan Dağ, "Annexing Cyprus", *Today's Zaman*, 12 March 2012. A Turkish official said, however, that "there is no change in Turkey's support to the ongoing comprehensive negotiation process aiming towards a bizonal, bicomunal federation, [and that] Turkey remains committed to the settlement aim before 1 July". Crisis Group email correspondence, March 2012.

<sup>13</sup> See Crisis Group Briefing, *Cyprus: Six Steps to a Settlement*, op. cit.

<sup>14</sup> Crisis Group interviews, international officials, Istanbul and Ankara, January 2012. "We called on Turkey to solve the Cyprus problem. Cooperation [on gas] cannot take place prior to a solution. Without [a solution], how can we commit ourselves to a country that does not recognise us, that does not abide by the Ankara [Additional] Protocol? Imagine that you live in a semi-detached house and you fight everyday with your neighbour, would you then go and use their kitchen? No, you can't do

## II. THE EASTERN MEDITERRANEAN GAS BONANZA

### A. GREEK CYPRIOTS GO IT ALONE

Cyprus faces severe economic difficulties like several other southern eurozone countries. Additionally, a massive explosion at a naval base in Mari in July 2011 destroyed their main power plant, caused widespread power outages and shocked Greek Cypriots.<sup>15</sup> Banks are exposed to the financial meltdown in Greece. The €5 billion they invested in Greek bonds have halved in value, and Greek Cypriot officials fear that the banks' exposure to Greek markets through business and private loans – at €22 billion, the equivalent of Greek Cypriots' entire annual economic output – is at risk.<sup>16</sup> Russia extended a much needed €2.5 billion loan in November 2011, with a favourable rate and terms, which covers Republic of Cyprus' borrowing needs for 2012. But there is no plan in place for 2013.<sup>17</sup> Rating agencies have steadily downgraded Cyprus's debt since 2011, with Standard & Poors and Moody's lowering it to junk status in 2012.

The economic crisis partially explains why Greek Cypriots were so euphoric when gas was discovered off their shores.<sup>18</sup> Apart from bringing lucrative export gains in several years' time, natural gas will help Cyprus meet its domestic energy needs; Greek Cypriots, using oil at their power plants, currently pay the highest price in Europe for

their electricity. These plants can easily be converted to burn gas.<sup>19</sup>

In September 2011 a medium-sized Texas-based American oil company, Noble Energy, began exploratory drilling in one of the thirteen Cypriot offshore research blocks encircling the southern half of the island (Block 12) in parallel to its operations in Israeli waters.<sup>20</sup> It subsequently announced that it had found between 5 and 8 trillion cubic feet (tcf), or between 142 and 227 billion cubic metres (bcm), in the Block's Aphrodite field, more than Cyprus can consume in a century.<sup>21</sup>

In February 2012 a second licencing round was announced for the remaining twelve blocks, including blocks which Turkey says overlap its continental shelf (see map 1) and areas where Turkish Cypriots gave Turks exploration licences (see map 2).<sup>22</sup> Interested bidders have until mid-May to submit their applications, and the licensing process is likely to last from six months to a year. Collection and evaluation of seismic data is set to start soon after, followed by exploratory drilling.<sup>23</sup>

During this process the Turkish Cypriots were not consulted. As an independent Turkish Cypriot energy expert explained: "By virtue of being inhabitants of this island, we are co-owners of these resources. We have all the rights owners have. We should decide where this gas goes, how the proceeds are used and so on. We have no idea right now what the Greek Cypriots are negotiating with Noble

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that". Crisis Group telephone interview, Greek Cypriot official, February 2012.

<sup>15</sup> 98 containers of confiscated explosives stored at the Evangelos Florakis Naval Base in Mari exploded in an accident on 11 July 2011, killing thirteen people and damaging hundreds of buildings including the island's largest power station which provided over half of its electricity, causing blackouts throughout the country. The Central Bank governor said the economy faces "a state of emergency" after the explosion whose estimated damages reach €2 billion, or almost 10 per cent of GDP. "Cyprus governor warns of emergency after blast", *Financial Times*, 20 July 2011.

<sup>16</sup> Crisis Group interview, senior Greek Cypriot official, Nicosia, February 2012. "There's no lending and the cost is high. Tourism is a bit better but the economy is not doing well, prospects are painful. The banking sector is very difficult. Non-performing loans are the real problem. If Greece does not recover, Cypriot banks will suffer a grave blow". Crisis Group interview, Greek Cypriot businessman, Nicosia, February 2012.

<sup>17</sup> "They have exhausted domestic borrowing". Crisis Group interview, European diplomat, February 2012.

<sup>18</sup> "The Cyprus ambassador is going about with dollar signs in his eyes". Crisis Group interview, German official, Berlin, January 2012. "The prevalent view is, 'how lucky we are'". Crisis Group interview, senior Greek Cypriot official, Nicosia, February 2012.

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<sup>19</sup> Electricity costs 1.2-1.5 times the EU average. "Energy price statistics", Eurostat, November 2011.

<sup>20</sup> It has been drilling in the eastern Mediterranean on Israel's behalf since 1998 and discovered the Leviathan field inside Israel's EEZ, which is the largest deep-water natural gas discovery of the last decade. The Levant basin in total is estimated to hold 122 trillion cubic feet (3,454 billion cubic metres) of undiscovered and technically recoverable natural gas and 1.7 billion barrels of oil. "Natural Gas Potential Assessed in Eastern Mediterranean", U.S. Department of the Interior, U.S. Geological Survey, 8 April 2010. These represent around 2 per cent of the world's proven gas reserves and 0.1 per cent of oil reserves.

<sup>21</sup> Noble Energy transferred 30 per cent of its rights in Block 12 to Israeli Delek Group, with Delek Drilling and Avner Oil Exploration having 15 per cent each, and now operates the well with a 70 per cent working interest.

<sup>22</sup> "Second round of licensing to be announced next week", *Cyprus Mail*, 7 February 2012; Crisis Group interviews, Nicosia, February 2012. The Greek Cypriot commerce minister said in November 2011 that several companies showed interest by purchasing seismic data.

<sup>23</sup> "We move very slowly. Look at the first licensing round in 2007. After four years, we have the results. If licensing goes well now, it will be completed in 2013, and then it's a matter of time for drilling to start". Crisis Group telephone interview, Greek Cypriot official, 13 February 2012.

Energy”.<sup>24</sup> They compare their right to natural resources with Greek Cypriots’ rights to their properties in the north independent of a settlement.<sup>25</sup>

Natural resources were a federal competence under the UN’s 2004 Annan Plan, as was entering into international agreements, including EEZs.<sup>26</sup> This was reaffirmed by the two community leaders in the current round of negotiations; a convergence paper on it was given to the UN.<sup>27</sup> A senior international official familiar with the talks regrets the current situation:

In the agreement [that the sides reached in bilateral talks], all royalties [from hydrocarbons] would go to the federal government. It’s a shame that so much was agreed, but no deal sealed . . . . If they were able to agree [on a comprehensive deal], it would make it easier to run the [property] compensation scheme and give more capacity to funding a settlement.<sup>28</sup>

Republic of Cyprus President Christofias has promised his “Turkish Cypriot compatriots that regardless of the circumstances, they will benefit from the possible discovery and extraction of hydrocarbons”,<sup>29</sup> an offer repeated by the former commerce, industry and tourism minister, Praxoula Antoniadou Kyriacou,<sup>30</sup> but Turkish Cypriots are not convinced.<sup>31</sup> Sharing the riches is deeply unpopular

among Greek Cypriots.<sup>32</sup> As a Greek Cypriot businessman told Crisis Group, “If the Turkish Cypriots return to the Republic of Cyprus, then they can share in it”.<sup>33</sup>

At the end of September 2011, Turkish Cypriots proposed a mutual and simultaneous suspension of all activities related to hydrocarbon reserves off Cyprus.<sup>34</sup> Turkish Prime Minister Erdoğan backed up the suggestion, saying “If the two sides renounce natural gas exploration, we will accept it”, even though it came two days after his country signed a hydrocarbon exploitation deal with the Turkish Cypriots.<sup>35</sup> The Turkish Cypriots also suggested creating a bi-communal ad hoc committee, with the UN’s participation, to take joint decisions on issuing licences, deals and management of revenues, including using the revenues to fund an eventual Cyprus settlement.<sup>36</sup> Turks and Turkish Cypriots say funds could be used to compensate Greek Cypriot properties in the north,<sup>37</sup> a sentiment echoed by the UN.<sup>38</sup> Some argue that the Greek Cypriots will bear the bulk of the investment burden, and that in order to benefit, Turkish Cypriots would also need to contribute financially.<sup>39</sup>

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implemented. The right way [to solve this] is to solve the Cyprus problem”. Crisis Group telephone interview, Özdil Nami, Turkish Cypriot politician in the opposition and former chief negotiator, 27 January 2012.

<sup>24</sup> “The commerce minister wanted to harness [gas revenues] to a solution. She immediately got named ‘minister of commerce and Turkey’. For the political class, it’s basically, ‘Gas is blue so it is Greek, of course. Here is something we can punish the Turks with, something we have in exchange for the properties [in the north] we can’t get back’”. Crisis Group interview, European diplomat, Nicosia, February 2012. “Greek Cypriots are not going to accept [joint management of gas with Turkish Cypriots]. They see it as an economic bonanza for a community buffeted by the euro crisis”. Crisis Group interview, senior international official, February 2012.

<sup>25</sup> Crisis Group interview, Nicosia, February 2012.

<sup>26</sup> “I told [Greek Cypriot president] Christofias, to his face, that if they started drilling, we would do things . . . [if they hadn’t started] we wouldn’t have done it”. Crisis Group interview, Derviş Eroğlu, president of the self-declared TRNC, Nicosia, 23 February 2012.

<sup>27</sup> “Turkey seeks simultaneous drilling halt”, *Hurriyet Daily News*, 25 September 2011.

<sup>28</sup> Foreign ministry of the self-declared TRNC, www.trncinfo.com.

<sup>29</sup> “We will make enough money to put cash into the property fund. The Turkish Cypriots will say ‘take our share’, and it will fund the property settlement”. Crisis Group interview, Turkish official, Ankara, November 2011.

<sup>30</sup> The UN is hopeful that gas revenues can fund a solution, particularly the property settlement. Crisis Group interview, international official, January 2012. As the UN Secretary-General’s special representative, Alexander Downer, put it: “A successful wedding needs a dowry”. “Natural gas can fund solution, Downer tells Security Council”, *Philoleftheros*, 14 November 2011.

<sup>31</sup> “First revenues from exports will go to financing the billions of dollars in loans that will go into launching this sector. The

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<sup>24</sup> Crisis Group telephone interview, 19 December 2011.

<sup>25</sup> See Crisis Group Report, *Cyprus: Bridging the Property Divide*, op. cit.

<sup>26</sup> Part IV, Article 14 of the Annan Plan on the competences of the federal government covers international agreements (14a) and natural resources (14e). When the plan was put to simultaneous referendum on both sides of the island, the Turkish Cypriots overwhelmingly voted in favour of reunification, with 76 per cent, while the Greek Cypriots voted against, with 65 per cent.

<sup>27</sup> Crisis Group interview, international official, January 2012; and Crisis Group telephone interview, Özdil Nami, Turkish Cypriot politician in the opposition and former chief negotiator, 27 January 2012.

<sup>28</sup> Crisis Group interview, February 2012.

<sup>29</sup> “Speech of the President of the Republic of Cyprus Mr. Demetris Christofias at the 66th session of the United Nations General Assembly in New York”, 22 September 2011, www.presidency.gov.cy.

<sup>30</sup> “Turkish Cypriots are citizens of Cyprus and as such can enjoy within the framework of a reunited homeland the benefits of any natural wealth that Cyprus has”. “Briefing on hydrocarbon exploration in Cyprus by Minister of Commerce, Industry and Tourism Praxoula Antoniadou”, provided by the ministry, February 2012.

<sup>31</sup> “We are not satisfied with [President] Christofias saying ‘we will share the revenues with Turkish Cypriots’. But it is hard for him to give a satisfying response because he does not recognise our state. Will he give money to Turkish Cypriot individuals, and if so, based on which criteria? There are Turkish Cypriots he does not recognise as citizens. This will cause division among our people and create domestic problems. His offer cannot be



According to the Turkish Cypriot leader, the Greek Cypriot reaction was negative: “They gave us back the envelope saying ‘this has nothing to do with talks’”.<sup>40</sup> The Greek Cypriots say that they have not formally rejected the proposals and have not yet responded.<sup>41</sup> They state that President’s Christofias’ pledge to share shows political commitment, but it is too early to discuss revenue-sharing schemes as actual revenues are still far from materialising.<sup>42</sup>

## **B. TURKEY ESCALATES TENSIONS**

The moment that Greek Cypriot leaders gave the green light for offshore drilling, Turkey responded it would do “whatever necessary” to defend Turkish and Turkish Cypriot rights.<sup>43</sup> Prime Minister Erdoğan denounced Cypriot and Israeli “oil exploration madness”,<sup>44</sup> and protested the “unilateral step of Greek Cypriots which is both irresponsible and provocative”.<sup>45</sup> Deputy Prime Minister Bülent Arınç warned, “Turkey will respond [to Greek Cypriot drilling]. This is not a bluff”.<sup>46</sup> After the February 2012 round of licensing, Turkey warned of an impending “crisis” and accused the Greek Cypriots of “taking on an adventure”.<sup>47</sup>

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residents in the south will have to pay for it through their electricity bills”. Gary Lakes, eastern Mediterranean editor, Middle East Economic Survey, presentation at “Cyprus Offshore Hydrocarbons: Wealth Distribution and Regional Politics” conference organised by Friedrich Ebert Foundation and PRIO Cyprus Center, Nicosia, 26 November 2011.

<sup>40</sup> Crisis Group interview, Derviş Eroğlu, president of the self-declared TRNC, Nicosia, 23 February 2012.

<sup>41</sup> A Greek Cypriot official confirms there has not been a response to the Turkish Cypriot proposals: “We must do planning first. We cannot move that quickly. We found out [the amount of reserves in Block 12] only in December. You know how slow the civil service works. It is very early to discuss [the details]. Why can’t we wait until a solution? [Managing the resources] will be a federal competence”. Crisis Group telephone interview, February 2012.

<sup>42</sup> Crisis Group telephone interview, Greek Cypriot official, February 2012.

<sup>43</sup> “Press release N°181 regarding the Greek Cypriot Administration’s gas exploration activities in the eastern Mediterranean”, 5 August 2011, [www.mfa.gov.tr](http://www.mfa.gov.tr).

<sup>44</sup> Prime Minister Erdoğan’s statement to Turkish journalists in New York ahead of the UN General Assembly meeting, Anatolian Agency, 21 September 2011.

<sup>45</sup> “Statement by Prime Minister Erdoğan following the signing of continental shelf delimitation agreement between Turkey and the TRNC”, 21 September 2011, [www.mfa.gov.tr](http://www.mfa.gov.tr).

<sup>46</sup> “Sondaja sondajla yanıt gecikmeyecek” [Drilling will be met with drilling without delay], 20 September 2011, TRT Haber (Turkish state television station), [www.trthaber.com](http://www.trthaber.com).

<sup>47</sup> According to a Turkish official, a second round of licensing will “cause a crisis” because Turkey’s state oil company (Türkiye Petrolleri Anonim Ortaklığı, TPAO) also has licenses in some

A strongly worded Turkish foreign ministry statement on 15 February said that some of the blocks in the tender overlap Turkey’s continental shelf (see below Section III.B), and warned Turkey would not allow companies “under any circumstances ... to conduct unauthorised oil/natural gas exploration and exploitation activities in overlapping areas [with the Turkish continental shelf]” and “will take all necessary measures to protect its rights and interests”.<sup>48</sup> At the same time, Turkish officials admit these overlapping blocks to the west of Cyprus are not easy to exploit and seem unlikely to hold much gas.<sup>49</sup> They also represent a small part of the zone the Republic of Cyprus has put up for prospecting (see map 1).<sup>50</sup>

Since 2008, Greek Cypriots have complained of Turkish harassment in its maritime zones, where Turkey has carried out military exercises.<sup>51</sup> Over the past few months Turkey has sent ships close to Noble Energy installations, usually over the horizon some 10 nautical miles away, but on one occasion coming within 5 nautical miles.<sup>52</sup> Turkish diplomats say, “We are following a reactive policy. We are not going to shoot. Our reaction will be within international law. We don’t want to get physical”.<sup>53</sup> But other leaders maintain a tough line, stating that “all options are on the table; anything is possible”.<sup>54</sup> Greek Cypriots say Turkey’s “military provocations” have increased in recent months,<sup>55</sup> and complain of the “gunboat diplomacy”.<sup>56</sup>

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of those thirteen blocks. Crisis Group interview, Ankara, January 2012.

<sup>48</sup> Turkey also said: “These activities violate the Turkish Cypriots’ equal and inherent rights [and] contradict the letter and spirit of the current comprehensive settlement negotiations”. “Press release N°43 regarding the second international tender for offshore hydrocarbon exploration called by the Greek Cypriot Administration (GCA), 15 February 2012”, [www.mfa.gov.tr](http://www.mfa.gov.tr).

<sup>49</sup> Crisis Group interview, Turkish official, Ankara, January 2012.

<sup>50</sup> A Greek Cypriot official said he believed Turkey is adopting a harder line opposing Greek Cypriot exploitation of blocks to the west of Cyprus than those to the south east where the Aphrodite field lies. Crisis Group interview, Nicosia, February 2012.

<sup>51</sup> Between March and June 2007, Turkey carried out military exercises off the southern coast of Cyprus. It coincided with the first offshore licensing round and Greek Cypriots did not complain about these to not scare away investors.

<sup>52</sup> Crisis Group interview, energy expert with knowledge of the basin, Nicosia, February 2012.

<sup>53</sup> Crisis Group interview, Turkish official, Ankara, September 2011.

<sup>54</sup> Turkey’s Minister for EU Affairs Egemen Bağış said Turkey will do “whatever is necessary” to defend its rights in the area adding, “this is what we have the navy for. We have trained our marines for this; we have equipped the navy for this”. “Donanmalar bunun için var [This is what navies are for]”, *Zaman*, 2 September 2011.

<sup>55</sup> Greek Cypriot Foreign Minister Erato Kozakou-Marcoullis told Israeli Army Radio on 15 February that Turkey held nu-

Rising tensions increase the risk of costly, or even deadly, accidents.<sup>57</sup> While there have apparently been no shots fired so far, one international diplomat was more pessimistic than most:

It was 50-50 for a while [in late 2011] .... My very dark view is that this leads to a very ugly confrontation. Turks don't have to send F-16s [to achieve their goal of deterring international banks and businesses from working with Greek Cypriots].<sup>58</sup>

Turkey and Turkish Cypriots have taken other steps that have violated Cypriot sovereignty: signing an agreement with the Turkish Cypriots delineating their continental shelf in September 2011, and assigning exploration licenses for seven blocks, six of them offshore including in Greek Cypriot areas, and one onshore in Famagusta in the north.<sup>59</sup> Turkey's state oil company Türkiye Petrolleri Anonim Ortaklığı (TPAO) started implementing the deal and Turkey's veteran research vessel Piri Reis set sail in late September and conducted over a month of seismic studies in what Turkish Cypriots named "Block G" (see map 2), to the south east of Cyprus.<sup>60</sup>

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merous provocative military exercises in the eastern Mediterranean over the past few months. "Greek Cyprus accuses Turkey of bullying over gas find", *Today's Zaman*, 15 February 2012. In late September, Greek Cypriots claimed Turkish planes violated Nicosia flight information region (FIR). "Cyprus protests violation of Nicosia FIR by Turkish jets", *Famagusta Gazette*, 23 September 2011. But this is not something new, as Turkey never recognised Nicosia FIR. Crisis Group interview, Turkish official, Ankara, January 2012.

<sup>56</sup> President Christofias on 22 December said: "If Turkey does not change its gunboat diplomacy and stop playing the part of regional police officer, there will be consequences which will not be good – either for the whole region or the Turkish people and first and foremost for Turkish Cypriots". "President calls on Turkey to abandon its gunboat diplomacy", 28 December 2011, [www.mfa.gov.cy](http://www.mfa.gov.cy). Greek Cypriot Foreign Minister Kozakou-Marcoullis called Turkey "the neighborhood bully" on 25 January, and repeated that its "bullying behaviour" was "totally unacceptable" on 15 February. Speech by the foreign minister Erato Kozakou-Marcoullis at the London School of Economics, op. cit.; and "Greek Cyprus accuses Turkey of bullying over gas find", *Today's Zaman*, 15 February 2012.

<sup>57</sup> For instance, when a Noble Energy helicopter accidentally flew over a Turkish exercise, the Turks flew by close enough to photograph its tail number.

<sup>58</sup> Crisis Group interview, senior international official, February 2012.

<sup>59</sup> "Turkey will recover its expenses, but it's a partnership". Crisis Group interview, Derviş Eroğlu, president of the self-declared TRNC, Nicosia, 23 February 2012.

<sup>60</sup> After it broke down, Greek Cypriot media mocked Piri Reis for being a 33-year-old ship. But Turks say it has modern equipment inside and has collected good data. Crisis Group interview, Turkish energy official, Ankara, January 2012.

According to the Turkish energy minister, who says that his country is moving the focus of its prospecting activities from the Black Sea to the Mediterranean,<sup>61</sup> this is not a short term tit-for-tat but a strategic shift in Turkey's energy policy.<sup>62</sup> Turkish officials claim that they will carry out seismic research for two or three years "all over the place, including areas where Greek Cypriots claim EEZ".<sup>63</sup> TPAO increased the number of its leased research vessels in the Mediterranean from one (Piri Reis) to three in October 2011, renting two Norwegian ships to conduct explorations to the west of Cyprus' EEZ, including near the Greek island Kastelorizo (Meis in Turkish). Turks say they are now analysing prospects based on data from Block G and drilling will begin accordingly.<sup>64</sup> In November, Turkish Cypriots signed a production-sharing agreement with TPAO about hydrocarbon extraction.

Turkey started onshore exploration in Famagusta in north Cyprus at the end of March 2012 with a well called Türk Yurdu-1.<sup>65</sup> Turkish Cypriot leader Derviş Eroğlu expects to find enough oil or gas onshore or offshore to meet Turkish Cypriot energy needs through a power plant built with Turkish investments. He has even offered to sell to Greek Cypriots.<sup>66</sup> International officials are, however, more sceptical about the area's potential.<sup>67</sup>

The Turkish government says if Greek Cypriots do not accept Eroğlu's 24 September proposals to suspend drilling or set up a joint committee, TPAO will go to Cypriot waters south of the island to drill on behalf of Turkish Cypriots, including in the rich Aphrodite field:

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<sup>61</sup> "Petrolü artık Akdeniz'de arayacağız" [From now on, we will look for oil in the Mediterranean], *Sabah*, 6 October 2011. On 28 December, Turkish cabinet approved the purchase of a new seismic ship for TPAO, which says it will buy one in two months.

<sup>62</sup> TPAO also signed an agreement with Shell for offshore exploration off Antalya on 23 November, in uncontested parts of the Turkish continental shelf. Turks say the deal shows TPAO is capable of doing international tenders, so if Turkey finds gas or oil in the Mediterranean, it can hire foreign companies to do drilling on their behalf. Crisis Group interview, Turkish energy officials, Ankara, January 2012.

<sup>63</sup> Crisis Group interview, Turkish energy official, Ankara, January 2012.

<sup>64</sup> Crisis Group interview, Turkish energy official, Ankara, January 2012.

<sup>65</sup> Crisis Group interview, Turkish energy official, Ankara, January 2012; and *Today's Zaman*, 23 February 2012.

<sup>66</sup> TAK (Türk Ajans Kıbrıs) news agency, 27 November 2011.

<sup>67</sup> "It's symbolic. [The well is] on a hilltop near Famagusta. It's hard to imagine any gas there". Crisis Group interview, European diplomat, Nicosia, February 2012. "Nobody knows if there is any [hydrocarbons] there. It is more a gesture than anything else". Crisis Group interview, Western diplomat, Nicosia, February 2012.

We will put our straw down and take the gas, too. And then we'll say the same thing as the Greek Cypriots: We recognise your share, and we'll put it aside for you. We're very serious about this.<sup>68</sup>

The proposition of Turkish offshore drilling seems fanciful. Although Turks say they can bring drilling platforms from elsewhere in the Mediterranean near the island,<sup>69</sup> there may be technical difficulties to drilling offshore. Northern Cyprus and Turkey would have a hard time getting major petroleum companies interested in what is internationally recognised as Republic of Cyprus' maritime zones. Greek Cypriots think international criticism will stop Turkey from carrying out its drilling threat.<sup>70</sup> Any extraction from the Aphrodite field would cause a Turkish dispute with Israel, as it lies partly within its EEZ, and Cyprus and Israel will be sharing the revenue. If the Turks find hydrocarbons, the EU will never buy them.<sup>71</sup> Even some Turkish Cypriots are unsure of the benefits.<sup>72</sup> If Turkey is really committed to a revenue-sharing offer between Greek and Turkish Cypriots, it would logically have to hand over to Greek Cypriots an inverse proportion to that which the latter would give Turkish Cypriots. Since Greek Cypriots constitute three quarters of the population of the island, the economically unfeasible nature of this equation underlines how hard it will be for Turkey to make any profits from this endeavour.

Turkey acknowledges that hydrocarbon riches belong to the whole island and would not object to Greek Cypriots drilling in the north.<sup>73</sup> Turkish Energy Minister Yıldız said,

"Wherever there is a well, all of Cyprus has a right to it".<sup>74</sup> But the Greek Cypriots are not impressed.<sup>75</sup>

### C. INTERNATIONAL REACTIONS

The dispute is drawing in neighbouring states, and is of increasing concern to the EU and the U.S. Most publicly support the Republic of Cyprus' sovereignty, but are privately uneasy given the dispute's unresolved nature and their reluctance to actively confront regionally powerful Turkey.<sup>76</sup>

Greek Cypriots have conspicuously increased cooperation with Israel since they have a common commercial interest in neighbouring offshore gas fields. Both countries' current rift with Turkey seems to have pushed them closer, at least for now.<sup>77</sup> They signed agreements on defence cooperation and protection and exchange of classified information in January 2012, and on search and rescue missions in February 2012.<sup>78</sup> Israeli Prime Minister Benjamin Netanyahu paid a one-day visit to Cyprus on 16 February, the first by an Israeli head of government to the island. But Israeli support to Greek Cypriots may wane if it reconciles with Turkey.<sup>79</sup> Greek Cypriots are also wary of getting too close to Israel fearing that Arab states may retaliate by recognising the self-declared Turkish Republic of Northern Cyprus.<sup>80</sup>

The hydrocarbons dispute has worsened already sour relations between Turkey and Israel. Despite early concerns

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<sup>68</sup> Crisis Group interview, Turkish official, Ankara, November 2011.

<sup>69</sup> "The cost of drilling is estimated around \$250-\$300 million. TPAO can carry out international tenders for these. It can bring the drilling platform from İskenderun if needed". Crisis Group interview, Turkish official, Ankara, January 2012.

<sup>70</sup> "[The Republic of] Cyprus as a sovereign state has rights over its EEZ and over waters surrounding Cyprus. I don't see how Turks will come and start exploring in a sovereign state's EEZ". Crisis Group telephone interview, Greek Cypriot official, January 2012.

<sup>71</sup> Crisis Group interview, European official, January 2012.

<sup>72</sup> "What revenues will Turkish Cypriots get according to the continental shelf agreement [signed on 21 September] with Turkey? We don't know. 99 per cent of the Turkish Cypriot public doesn't know it, either. The arrangement is not public. The Turkish company will have to recover its investment. We'll get a proportion of profits, not revenues". Crisis Group interview, Özdil Nami, Turkish Cypriot politician in the opposition and former chief negotiator, Nicosia, February 2012.

<sup>73</sup> Crisis Group interview, Turkish official, Ankara, January 2012.

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<sup>74</sup> "Petrol ve doğalgaz için Akdeniz'de çalışmalar genişletiliyor" [Scope of work expanded in Mediterranean for oil and gas], TAK (Türk Ajans Kıbrıs) news agency, 27 November 2011.

<sup>75</sup> Crisis Group telephone interview, Greek Cypriot official, January 2012.

<sup>76</sup> Crisis Group interviews, Western and European diplomats, Nicosia, February 2012.

<sup>77</sup> Turkey's argument with Israel was mostly over Israeli policies toward Palestinians and also because of a Turkish-led international aid flotilla to Gaza unauthorised by Israel, which Israeli forces attacked on 30 May 2010, killing nine Turkish activists. See Crisis Group Europe Report N°208, *Turkey's Crises over Israel and Iran*, 8 September 2010. "Greek Cypriots feel very clever that they are siding with Israel. Some even think because Noble Energy is an American company the U.S. Sixth Fleet will be there, should anything happen". Crisis Group interview, international official, January 2012.

<sup>78</sup> "It was more symbolic than anything else. But they are fast-tracking the relationship". Crisis Group interview, Western diplomat, Nicosia, February 2012.

<sup>79</sup> "This is an example of Turkey pushing its rivals together. But if relations between Turkey and Israel improve, things [between Cyprus and Israel] may be different". Crisis Group telephone interview, Alexander Murinson, academic, 23 January 2012.

<sup>80</sup> Crisis Group interview, Alexandros Lordos, Greek Cypriot polling expert, Nicosia, 22 February 2012.

about Turkey's challenging Israeli drilling in the eastern Mediterranean, Turkish officials quickly airbrushed out Prime Minister Erdoğan's threatening statements on Israel's territorial waters.<sup>81</sup> Nervousness peaked after an unverified news report that Turkish warships shelled a strip of water dividing the Israeli Leviathan and Cypriot Aphrodite gas fields in December 2011, which a Turkish official dismissed as "ridiculous".<sup>82</sup>

Greece, a guarantor state to Cyprus,<sup>83</sup> has not played a role in this dispute as it does not want to aggravate its decades-old Aegean dispute with Turkey.<sup>84</sup> It is reluctant to declare EEZs or cause other controversy in the Mediterranean.<sup>85</sup> There has been talk of starting exploration for natural gas and building pipelines between Cyprus and Greece (see below Section IV.A), and an Israel-Cyprus-Greece power cable is under study.<sup>86</sup> Turkey and Greece deny any correlation between tensions in the eastern Mediterranean and the Aegean,<sup>87</sup> but as Athens scrambles to find new sources of income to deal with its financial crisis, some politicians are calling for it to also prepare for drilling.<sup>88</sup>

The UN is keeping the hydrocarbons issue out of the regular negotiations, saying it will be resolved after a settlement as both Cypriot leaders agreed, in a rare moment of convergence, that it is a federal competence.<sup>89</sup> The UN Sec-

retary-General's special adviser on the island, Alexander Downer, has said that the UN would consider mediating if asked.<sup>90</sup>

The U.S. is worried about the escalating tension,<sup>91</sup> even though chances that a clash will erupt are low.<sup>92</sup> Backing up the UN's thinking, the U.S. State Department said it would welcome a UN role in mediating some sort of revenue-sharing model.<sup>93</sup> The U.S. has supported Republic of Cyprus' sovereign rights to explore for energy in its maritime zones.<sup>94</sup> Apart from the presence of Noble Energy, the U.S. also worries about the developments adding to Israeli-Turkish tensions. U.S. officials express interest in supporting an export route through Turkey as a profitable confidence-building measure.<sup>95</sup>

Europeans are interested in the island as a potential alternative energy source, although the Aphrodite field is too small to significantly help diversification of energy supplies and the EU lacks a proactive policy on eastern Mediterranean gas.<sup>96</sup> An annual production of around 0.4 tcf

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<sup>81</sup> In an interview with Al Jazeera on 9 September, Prime Minister Erdoğan said Turkish warships would accompany Turkish aid vessels bringing humanitarian aid to Gaza, to ensure freedom of navigation, but Turkish officials make clear that they had no claims on the Israeli EEZ. "Erdoğan: Turkish navy to protect Gaza aid", 9 September 2011, Al Jazeera; and Crisis Group interview, Ankara, September 2011.

<sup>82</sup> Crisis Group interview, Ankara, January 2012.

<sup>83</sup> The UK, Greece and Turkey are all guarantors of the Cypriot state set up on independence in 1960, whose original bi-communal character collapsed politically in 1963-1964 and with de facto partition in 1974.

<sup>84</sup> See Crisis Group Europe Briefing N°64, *Turkey and Greece: Time to Settle the Aegean Dispute*, 19 July 2011.

<sup>85</sup> "Currently, and without prejudice to our relevant rights deriving from the Law of the Sea, we focus on the central difference [with Turkey], which remains the delimitation of the continental shelf". Crisis Group email correspondence, Greek official, 31 January 2012.

<sup>86</sup> The 2,000 megawatt cable, 287km long (via Crete) and costing €1.5 billion, could be built as early as 2016. "Israel, Cyprus, Greece sign electric cable deal", *Jerusalem Post*, 4 March 2012.

<sup>87</sup> Crisis Group email correspondence, Greek official, January 2012; and Crisis Group interview, Turkish official, January 2012.

<sup>88</sup> Poll-leading New Democracy Party leader Antonis Samaras said that Greece should follow Cyprus's example in declaring EEZs and hammer out a joint economic strategy for the exploitation of offshore mineral deposits. "ND Leader Eyes Aegean Drilling", *eKathimerini*, 21 February 2012.

<sup>89</sup> UN Good Offices Mission, [www.uncyprustalks.org](http://www.uncyprustalks.org), 27 September 2011.

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<sup>90</sup> "Remarks by SASG Downer following meeting of Cyprus Leaders", Republic of Cyprus Press and Information Office, 27 September 2011. This caused Greek Cypriot politicians to accuse him of suggesting UN arbitration. "Under-fire Downer says his words were lost in translation", *Cyprus Mail*, 29 September 2011.

<sup>91</sup> According to a source, Prime Minister Erdoğan told President Obama in September 2011 that Turkish ships would not interfere with Greek Cypriot drilling. "Turkey: Background and U.S. Relations", Congressional Research Service, 2 February 2012. "I'm worried about what's going on off the coast of Cyprus. We run terrible risks the drilling may become inflamed". Crisis Group interview, senior European official, October 2011. "Of course we are concerned any time [there is] armed aggression against a member state". Crisis Group interview, European official, January 2012.

<sup>92</sup> "There is a lot of posturing going on in eastern Mediterranean. We call Turkey's posturing a threat. Call a spade a spade. I see this playing out messily, but it won't come to blows". Crisis Group interview, European official, January 2012.

<sup>93</sup> "US supports revenue-sharing agreement in Cyprus for natural gas", *Today's Zaman*, 29 September 2011. According to Richard Morningstar, U.S. Special Envoy for Eurasian Energy, "any potential revenue from future oil and gas resources in Cyprus should be equitably shared between both communities". Speech cited by *Cyprus Mail*, "US urges east Med countries to work together on energy", 29 March 2012.

<sup>94</sup> "The United States supports Cyprus's right to explore for energy. Having a U.S. company involved in developing the energy resources of Cyprus is also positive. ... We continue to believe that the island's oil and gas resources, like all of its resources, should be equitably shared between both communities in the context of an overall settlement. And we don't believe that developing offshore energy resources need hinder [the] reunification talks". U.S. Department of State, Daily Press Briefing, 29 September 2011.

<sup>95</sup> Crisis Group interview, U.S. official, January 2012.

<sup>96</sup> Crisis Group interview, European diplomat, February 2012.

(10 bcm) expected from this field is a drop in the ocean of EU's consumption in 2010 of 18.4 tcf (522 bcm).<sup>97</sup> Nevertheless, Brussels, recognising Republic of Cyprus as the legitimate government of the island, fully backs its sovereign right to its EEZ,<sup>98</sup> and the EU Council's December 2011 conclusions criticised Turkey for its "threats" against a member state.<sup>99</sup> To appease tensions, Enlargement Commissioner Štefan Füle evoked international arbitration as a possible resolution mechanism for the dispute.<sup>100</sup> A traditional ally, Russia backed the Greek Cypriots saying that Turkey's threats were "not very wise".<sup>101</sup>

### III. THE LEGAL CONTEXT

Turkey and the Republic of Cyprus fundamentally disagree on their maritime boundaries. While Cyprus has been establishing EEZs with some of its neighbours since 2003, Turkey not only argues that it has no right to make such agreements, but also that Greek Cypriot claims encroach on its continental shelf, and that declaring EEZs is inappropriate in the relatively self-enclosed Mediterranean.<sup>102</sup>

If Turkey and Cyprus are willing to talk and frame this as a bilateral dispute, international law can provide some guidance, especially the 1982 United Nations Convention on the Law of the Sea (UNCLOS), even though Ankara has not signed it. International jurisprudence – decisions from the ICJ and arbitral tribunals, as well as the International Tribunal for the Law of the Sea (ITLOS), the judicial body established by UNCLOS – has often tried to strike a balance between equity and the median line principle of the 1958 Geneva Convention,<sup>103</sup> an area where Turkish and Greek Cypriots have differing views.

#### A. THE LAW OF THE SEA

UNCLOS gives all coastal states – irrespective of whether they are island-states or not – rights to maritime boundaries, including their EEZ and continental shelf up to 200 nautical miles off the coast.<sup>104</sup> The continental shelf and EEZ may relate to the same seabed and subsoil area, but the latter also includes the column of water above. An EEZ has to be declared in order to become effective.<sup>105</sup> A con-

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<sup>97</sup> "[Block 12] is not very important for the EU. Our saviour is Turkmenistan and Shah Deniz [a large natural gas field in the South Caspian Sea], which can only come through Turkey". Crisis Group interview, European official, January 2012.

<sup>98</sup> Crisis Group interview, European official, January 2012.

<sup>99</sup> The EU expressed "serious concern" and urged "the avoidance of any kind of threat or action directed against a Member State, or source of friction or actions, which could damage good neighbourly relations and the peaceful settlement of disputes", underlining that members have a sovereign right to enter into bilateral agreements, and explore and exploit their natural resources. "Council conclusions on enlargement and stabilisation and association process", paragraph 21, 9 December 2011.

<sup>100</sup> "Policy intervention on Turkey-Cyprus in the European Parliament", 27 September 2011, EU official website (europa.eu).

<sup>101</sup> Russian ambassador to Nicosia, Vyacheslav Shumskiy, in "Russian Gazprom eyes Cyprus gas reserves", *Famagusta Gazette*, 24 October 2011.

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<sup>102</sup> "Let's forget the EEZs, and find another way to share [the Mediterranean]". Crisis Group interview, Turkish official, Ankara, September 2011.

<sup>103</sup> The "median line" provision in continental shelf delimitations – still the starting point for determining EEZ boundaries – comes from the Article 6 (1) of the 1958 Geneva Convention on the Continental Shelf: "When the same continental shelf is adjacent to territories of two or more states with opposite coasts, the boundary will be determined by an agreement between them. In the absence of agreement, and unless another boundary line is justified by special circumstances, a median line will be used, every point of which is equidistant from the nearest points of the baselines from which the breadth of the territorial sea of each state is measured".

<sup>104</sup> Furthermore, Article 121 of UNCLOS says, "The territorial sea, the contiguous zone, the exclusive economic zone and the continental shelf of an island are determined in accordance with the provisions of this Convention applicable to other land territory", unless they cannot sustain human habitation or an economic life of their own.

<sup>105</sup> Article 56 of UNCLOS gives all coastal states up to 200 nautical miles EEZ from their baseline, in which they have sovereign rights for exploring and exploiting, conserving and managing living resources. UNCLOS expanded the 1958 Geneva Con-

tinental shelf, up to 200 nautical miles, is an inherent and exclusive right for the coastal state unless exercising this right affects another state's rights, in which case an agreement is needed.

Before a state can do exploration or exploitation up to 200 nautical miles off its coast, it has to delimit its EEZ and continental shelf with states with opposite or adjacent coasts.<sup>106</sup> States are also required under Article 74(3) and 83(3) to seek "an agreement in good faith" on practical arrangements for exploitation of natural resources in disputed areas pending delimitation, and to refrain from exploitation prior to such an agreement.<sup>107</sup> The ICJ and arbitral tribunals have imposed similar obligations of restraint pending delimitation, particularly suggesting drilling for exploitation may be prohibited.<sup>108</sup> UNCLOS emphasises cooperation between states, for example through the obligation under Article 283 to exchange views, by negotiation or other peaceful means, when a dispute arises. Similarly, Article 300 requires states to exercise their rights, jurisdiction and freedoms "in a manner which would not constitute an abuse of right". In a crowded sea like the eastern Mediterranean, no state can exercise jurisdiction over the full 200 nautical miles EEZ, and cooperation is essential.

UNCLOS and international jurisprudence spell out that the convention's rules are not absolute and that states should resolve conflicts over the attribution of rights and jurisdiction in the EEZ on the "basis of equity and in light of all relevant circumstances" (Article 59). Similarly, the ICJ ruled in the 1969 North Sea Continental Shelf case that delimitation of maritime boundaries in areas of over-

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vention's continental shelf provisions to cover both living and non-living resources, meaning states also have economic rights over hydrocarbons that are on their continental shelf.

<sup>106</sup> Article 74 and 83 of UNCLOS on delineation of EEZ and continental shelf respectively both say that delimitation shall be done by agreement, on the basis of international law, to achieve an "equitable solution".

<sup>107</sup> UNCLOS requires states to "make every effort to enter into provisional agreements of a practical nature", and not to "jeopardize or hamper the reaching of a final agreement" in the transitional period, thus limiting the states' right to unilateral exploitation of natural resources in disputed areas (Articles 74 and 83).

<sup>108</sup> In the 1976 Aegean Sea case, ICJ allowed Turkey and Greece to carry out seismic exploration for oil and gas, considering these activities did not risk physically damaging the seabed or subsoil, but prohibited drilling for production or exploitation. "Aegean Sea Continental Shelf (Greece v. Turkey)", Order of 11 September 1976, ICJ Reports, 1976. On exploratory drilling, the arbitral tribunal in "Guyana v. Suriname" found that Guyana violated its obligation under UNCLOS Article 83(3) by unilaterally engaging in exploratory drilling in disputed areas without Suriname's consent and that such drilling could cause permanent damage to the marine environment. "Guyana v. Suriname", Award of the Arbitral Tribunal, 17 September 2007.

lapping claims should be done by "agreement in accordance with equitable principles, and taking into account all the relevant circumstances".<sup>109</sup>

All of the above could hypothetically present the basis for a code of conduct between Turkey and Cyprus, but UNCLOS and case law only have limited applicability to the situation. Their disagreement over maritime boundaries to the west and south west of the island, namely in areas of overlapping claims, fall mainly within the context of international law of the sea. But Turkey's objections to the rest of Cypriot maritime areas, including Aphrodite, are not related to Turkish boundary claims but emanate from the political situation on the island and Turkey's non-recognition of the Republic of Cyprus and its advocacy for Turkish Cypriots' rights.

## **B. SOVEREIGN RIGHTS VS. EQUITABLE DISTRIBUTION**

The Republic of Cyprus ratified the 1958 Geneva Convention on the Continental Shelf in 1974, and the 1982 UNCLOS in 1988. Turkey has signed neither. Cyprus's EEZ agreements with Egypt, Israel and Lebanon are based on the median line principle. Greek Cypriot officials insist that UNCLOS has received such worldwide acceptance that it has become part of international customary law and is therefore binding on non-signatory states like Turkey.<sup>110</sup> While not all provisions of UNCLOS are reflective of customary international law, its EEZ provisions are.<sup>111</sup>

Turkey's objections to UNCLOS are not principally about its EEZ provisions in the Mediterranean, but are due to the 12 nautical mile territorial sea provision as it applies to Turkey's dispute with Greece in the Aegean Sea.<sup>112</sup>

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<sup>109</sup> "North Sea Continental Shelf (Federal Republic of Germany v. Denmark; Federal Republic of Germany v. Netherlands)", Judgment, ICJ Reports, 1986.

<sup>110</sup> Crisis Group interviews, Nicosia, February 2012.

<sup>111</sup> In its judgment on the continental shelf between Libya and Malta, the ICJ said it was "incontestable that ... the EEZ ... is shown by the practice of States to have become part of customary law". "Case concerning the Continental Shelf (Libyan Arab Jamahiriya v. Malta)". Judgment, ICJ Reports, 1985.

<sup>112</sup> Article 3 of UNCLOS defines a territorial sea as a belt of coastal waters extending at most 12 nautical miles from the state's low-water line, known as the baseline. It is the sovereign territory of the state, extending to the airspace above and seabed below. Turkey objects to this in the Aegean, arguing that if Greece applies it to its hundreds of islands, such an extension would allow Turkey only a narrow belt of territorial seas and would cut off its corridors to the high seas. See Crisis Group Briefing, *Turkey and Greece: Time to Settle the Aegean Dispute*, op. cit. Eastern Mediterranean countries Israel, Syria, Turkey have not signed UNCLOS while Lebanon, Egypt, Cyprus, Greece and Libya have.

Turkish officials say they would sign UNCLOS the day after the Aegean problem was resolved.<sup>113</sup> In fact Turkey already abides by EEZ principles in the Black Sea where it declared a 200-nautical mile EEZ in 1986 via an agreement with the Soviet Union, Bulgaria and Romania. It also uses UNCLOS's definition of a semi-enclosed sea when referring to the Mediterranean.<sup>114</sup>

Turkey challenges the legitimacy of Republic of Cyprus' EEZ agreements with Egypt, Lebanon and Israel based on two arguments. First, as the division of Cyprus continues, Turks argue the Greek Cypriot government does not represent the Turkish Cypriot population, and should have waited until the division was resolved before entering into such agreements.<sup>115</sup> They point out that Greek Cypriot unilateral drilling is hurting the reunification negotiations and undermine Turkish Cypriots' "equal and inherent" rights.<sup>116</sup>

Its second objection is about who should control what parts of the sea and seabed. In 2002, Turkey claimed rights to areas in the Cyprus-Egypt EEZ demarcation to the west of island (west of longitude of 32° 16' 18" E, see map 1), which it has registered with the UN.<sup>117</sup> It began actions that indirectly asserted a claim to a continental shelf in this area of the Mediterranean Sea.<sup>118</sup> It has not declared an EEZ but has signed a continental shelf agreement with the Turkish Cypriots in September 2011 to delineate between the Turkish coast and the north of the island (see

map 2).<sup>119</sup> Delimitation is not according to the median line but gives a slightly bigger share to Turkey.<sup>120</sup> Greek Cypriots condemned the agreement as an "unlawful act" with an "illegal entity".<sup>121</sup>

The Republic of Cyprus EEZ overlaps the area Turkey claims as its continental shelf in five of the thirteen offshore research blocks – namely 1, 4, 5, 6, and 7 (see map 1). Turkish state oil company TPAO has been given exploration licenses by the Turkish Cypriots in areas overlapping Cypriot Blocks 1, 2, 3, 8, 9, 12, 13 (see map 2).<sup>122</sup> Greek Cypriots complain that when these TPAO-licensed areas (see map 2) are taken together with the areas where Turkey claims continental shelf to the west, virtually the whole Cypriot continental shelf is usurped.<sup>123</sup>

Ankara on the other hand worries that should Greece ever declare an EEZ, it together with the Republic of Cyprus' zone would leave Turkey with a narrow EEZ hardly extending out from its long coastline (see map 3).<sup>124</sup> Ankara's problems with EEZs in the Mediterranean are also linked to the Aegean dispute, especially with regard to Kastelorizo (Meis), the easternmost Greek island in the Dodecanese.<sup>125</sup> At the moment, Greek officials think they have enough problems with Turkey in the Aegean Sea without bringing up possible EEZ boundaries in the Mediterranean.<sup>126</sup>

Turkey's EEZ claims limit Cyprus's maritime zones to only 12 nautical miles territorial waters to the west of the island (see map 1). Officially, Turkey maintains that Cyprus should be given limited maritime zones because of

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<sup>113</sup> Crisis Group interview, Ankara, April 2011.

<sup>114</sup> UNCLOS in Article 122 defines semi-enclosed sea as "a sea consisting entirely or primarily of the territorial seas and EEZs of two or more coastal states".

<sup>115</sup> "The Greek Cypriots hijacked the government in the 1960s, they hijacked sole membership of the EU, and now we're faced with a new *fait accompli*". Crisis Group interview, Turkish official, Ankara, September 2011. "The sovereignty issue is part of the negotiation process". Crisis Group interview, Turkish official, Ankara, January 2012.

<sup>116</sup> Crisis Group telephone interview. Turkish official, March 2012. "Greek Cypriot drilling is untimely. It's a slap in face of talks because there has been agreement that natural resources will be under the new federal government". Crisis Group interview, Turkish official, Ankara, September 2011. Turkey's Minister for EU Affairs Egemen Bağış said on 1 December 2011, "Gas is going nowhere if it's already there. Why the hurry? This is an open provocation [against] the UN-brokered peace efforts". *Hurriyet Daily News*, 2 December 2011.

<sup>117</sup> www.mfa.gov.tr.

<sup>118</sup> In March 2002, Turkey interrupted Norwegian vessel Northern Access, conducting geophysical research west of the island, warning it was on the Turkish continental shelf. In 2008, Turkish warships intersected research ships off the coast of Cyprus on 18, 19, 21 and 24 November 2008, which President Christofias reported to the UN on 25 November 2008. Ministry of Foreign Affairs of the Republic of Cyprus, www.mfa.gov.cy.

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<sup>119</sup> The deal cannot be registered at the UN, because the Turkish Cypriot state is not recognised, but it will be published in UN documents. Crisis Group interview, Turkish official, Ankara, January 2012.

<sup>120</sup> Crisis Group interview, Turkish official, Ankara, January 2012.

<sup>121</sup> Republic of Cyprus government spokesman Stefanos Stefanou, quoted in *Cyprus Mail*, 22 September 2011.

<sup>122</sup> Crisis Group interview, Turkish official, Ankara, January 2012.

<sup>123</sup> "The whole thing is now a 'disputed area'. They think they can create an area where no drilling can take place, to discourage investors". Crisis Group interview, Greek Cypriot official, Nicosia, February 2012.

<sup>124</sup> Turkey will lose 71,000 of its 145,000 sq km continental shelf to Greece and 33,000 sq km to Cyprus, and will be left with only 41,000 sq km in the eastern Mediterranean, if the Greek Cypriots and Greeks unite their EEZs. Prof. Dr. Sertaç Hami Başeren, "Doğu Akdeniz'de gerilim" [Tension in the eastern Mediterranean], Turkish Marine Research Association, www.tudav.org.tr.

<sup>125</sup> Turks argue that the Greek island Kastelorizo, located a mere 2km from Turkish coast and taking up only 12 sq km, cannot have any more maritime zones than 12 nautical mile territorial waters. Crisis Group interview, Turkish official, Ankara, January 2012.

<sup>126</sup> Crisis Group interview, Athens, April 2011.

its size and “island” status.<sup>127</sup> For instance, west of Cyprus, Turkey draws a hypothetical demarcation with Egypt along the median line between the two states’ coastlines, completely ignoring Cyprus.<sup>128</sup> Greek Cypriots argue that if one follows Turkey’s argument, the British Isles would not have a continental shelf, either.<sup>129</sup> Even Turkish officials admit 12 nautical miles is a starting position and see some limited room to negotiate.<sup>130</sup>

Moreover, even though Turkey says EEZs in eastern Mediterranean’s crowded neighbourhood should be determined through negotiations, based on equitable principles,<sup>131</sup> it refuses to engage in talks on this issue with the Republic of Cyprus.<sup>132</sup> This position, based on 1960s and 1970s zero-sum thinking, runs increasingly against the interests of Turkey and the neighbourhood.

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<sup>127</sup> There is case law to back up some limitations to islands’ maritime zones. See Crisis Group Briefing, *Turkey and Greece: Time to Settle the Aegean Dispute*, op. cit., p. 8 for a list of ICJ and arbitration rulings that awarded limited continental shelves to islands. Turkish officials particularly refer to the ICJ’s 3 July 1985 ruling between Malta and Libya, which adjusted the median line 18 nautical miles northward to give the latter a larger continental shelf. It found that the difference in their coastal lengths, with a one-to-eight proportion, was “so great as to justify the adjustment of the median line”. “Case concerning the Continental Shelf (Libyan Arab Jamahiriya v. Malta)”. Judgment, ICJ Reports, 1985. With its 1,542km coastline, the largest in the eastern Mediterranean, an ICJ judgment would likely award Turkey a larger share of continental shelf. Similarly, the ICJ took into consideration “factors calling for the adjustment or shifting of the provisional equidistance line in order to achieve an equitable result” in its 2009 judgment on “Maritime Delimitation in the Black Sea (Romania v. Ukraine)”. Between Greenland and Jan Mayen, ICJ said the disparity between coastal lengths (almost one-to-nine) constituted a special circumstance and moved the median line closer to Jan Mayen. “Maritime Delimitation in the Area between Greenland and Jan Mayen (Denmark v. Norway)”, Judgment, ICJ Reports, 1993.

<sup>128</sup> Crisis Group interview, Turkish official, January 2012.

<sup>129</sup> Speech by the foreign minister Erato Kozakou-Marcoullis at the London School of Economics, op. cit.

<sup>130</sup> Crisis Group interview, Turkish official, January 2012.

<sup>131</sup> To make this point clear, Turkey and Turkish Cypriots adjusted the median line in Turkey’s favour in their continental shelf agreement on 21 September.

<sup>132</sup> Turkey will only launch such talks with a federal government in Cyprus following a comprehensive settlement. Crisis Group telephone interview, Turkish official, March 2012.

#### IV. CASHING IN THE WINDFALL

The estimated value of 5 to 8 tcf (or 142 to 227 bcm) of gas<sup>133</sup> 6km under Aphrodite ranges from €30 billion to €100 billion.<sup>134</sup> Since the find borders Israel’s EEZ, the two sides must first agree on a unitisation deal, but most of the field is on the Cypriot side.<sup>135</sup> Before Greek Cypriots can decide what to do with the gas and how to share future revenues, they need to know how much there is, its value and location:

Hydrocarbons reservoirs [in Aphrodite] are 180km away from Cyprus. We have not decided what to do or how much to invest. There are lots of numbers going around. To be honest, it’s very early to say anything. Nobody knows exactly [what the value of the gas is]. Are we going to build a pipeline? Use ships? We must decide. But now the only pending issue is the second round of licensing in the remaining thirteen blocks. Then we will discuss how to go ahead.<sup>136</sup>

Most scenarios assume that the gas will first come by a 170-180km pipeline to Cyprus,<sup>137</sup> where part of it will be used for domestic consumption and the rest sent to world markets. This initial pipeline will cost around \$1 billion and take around two years to build.<sup>138</sup> Taking into account time needed for tenders and negotiations, it may take five

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<sup>133</sup> Roughly, the find translates into 10 bcm annual production for 20 to 30 years. Another way of expressing expected output is 1 billion cubic feet per day. Most of this gas will be available for export, since Cypriot consumption is roughly 150 million cubic feet per day, ie, 15 per cent of probable total output. Crisis Group interview, energy executive with knowledge of the basin, February 2012.

<sup>134</sup> Commerce Minister Antoniadou gave the figure of €100 billion; Foreign Minister Kozakou-Marcoullis added that this “can satisfy the electricity production needs of the country for 210 years”. Speech by the Foreign minister Erato Kozakou-Marcoullis at the London School of Economics, op. cit. Some energy experts cite a more conservative figure of €30 billion. “Finding gas is easy, now comes the hard part”, *Cyprus Mail*, 1 January 2012.

<sup>135</sup> Crisis Group interview, Praxoula Antoniadou Kyriacou, Greek Cypriot former commerce, tourism and industry minister, Nicosia, 23 February 2012.

<sup>136</sup> Crisis Group telephone interview, Greek Cypriot official, February 2012.

<sup>137</sup> A floating LNG platform is possible and being discussed, but would likely require the technology of a major petroleum company, most of whom are currently expected to avoid the political complications of Cyprus’s gas field. Crisis Group email correspondence, London-based oil expert, March 2012.

<sup>138</sup> Crisis Group interview, energy executive with knowledge of the basin, February 2012, Nicosia.



years to get the gas onshore, and ten years, perhaps even longer, until the state gets real income.<sup>139</sup>

## A. GAS EXPLOITATION

Greek Cypriots see gas as a solution to their economic problems (described in Section II.A).<sup>140</sup> Experts warn of “Dutch disease” – the dangers of handling a sudden influx of revenues for the economy and the state apparatus – and stress the need to establish rules before money starts flowing.<sup>141</sup> The initial euphoria among Greek Cypriots has given way to a calmer, more strategic approach.<sup>142</sup> Nevertheless, Greek Cypriots see gas as leverage in the UN negotiations, particularly with regard to what they perceive as Turkey’s lack of commitment.<sup>143</sup>

Tensions have negative commercial implications. Major international energy companies are reluctant to invest in disputed areas.<sup>144</sup> In September 2011, Prime Minister Erdoğan said Turkey would not “cause a crisis in the region”, but warned of sanctions against international energy companies, saying they would be banned from energy projects in Turkey.<sup>145</sup> Greek Cypriots say Turkey’s black-

listing threats have proved effective in the past,<sup>146</sup> but some argue that now that there have been significant discoveries, Turkey will be less effective in dissuading oil companies and banks from taking part in Cypriot projects, and would profit more from joining in than staying out.<sup>147</sup>

## B. GAS TRANSPORT

Greek Cypriots say that they will make a decision on whether to export gas via a pipeline or an LNG plant soon.<sup>148</sup> Noble Energy will carry out additional appraisal drilling in the Aphrodite field in the second half of 2012, which will take several months to a year, to gather more data before starting any development.<sup>149</sup> International petroleum executives believe that, in the absence of a Cypriot settlement, high financing costs and lack of a strong oil company’s participation may force delays in developing hydrocarbon reserves.<sup>150</sup>

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<sup>139</sup> Crisis Group interview, Gary Lakes, eastern Mediterranean editor, Middle East Economic Survey, Nicosia, 21 February 2012. An energy executive with close knowledge of the basin said it will take three to four years to start production and within five years, Greek Cypriots could be using the gas in power generation. Crisis Group interview, Nicosia, February 2012.

<sup>140</sup> A Greek Cypriot businessman points out that yields on long-term Cyprus bonds are lower than the short-term ones because of expectations of gas income. Crisis Group interview, Nicosia, February 2012.

<sup>141</sup> “We can’t do back of the envelope calculations for this”. Michael Sarris presentation, *op. cit.*

<sup>142</sup> Crisis Group interview, European diplomat, Nicosia, February 2012.

<sup>143</sup> President Christofias said Turkey “should direct the leader of the Turkish Cypriot community to show good will in the talks for finding a solution to the Cyprus problem [so that] the utilization of the natural resources of the country by the federal government will have a direct benefit for both communities”. “The President of the Republic met with the Prime Minister of Israel”, 16 February 2012, Republic of Cyprus Press and Information Office.

<sup>144</sup> “You need upwards of \$10 billion to invest in gas. No company does it alone, you need financing. Banks will look at stability and the risks. In the current circumstances [major international petroleum companies] don’t go there”. Crisis Group interview, Turkish energy official, Ankara, January 2012. “It costs a million dollars a day to run a rig, and they don’t want their rig to get bumped into!” Crisis Group interview, Western diplomat, Nicosia, February 2012.

<sup>145</sup> “We would like to caution international oil and natural gas companies that will undertake business with Greek Cypriots. Our Ministry of Energy is working to ban admission of these companies from energy projects in Turkey and impose a series

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of sanctions upon them”. “Statement by Prime Minister Erdoğan following the signing of continental shelf delimitation agreement between Turkey and the TRNC”, 21 September 2011, Turkish Prime Ministry website, [www.basbakanlik.gov.tr](http://www.basbakanlik.gov.tr).

<sup>146</sup> “There were only four bids on Block 12, and Noble Energy had a spare rig, so it could move immediately”. Crisis Group interview, senior Greek Cypriot official, Nicosia, February 2012. “I heard some [petroleum companies] are pulling out [of the second licensing round]. They do not want trouble. I don’t think any of the majors will come. Some mid-size companies may be interested”. Crisis Group interview, Nicosia, former Greek Cypriot foreign and commerce minister, Nicosia, 23 February 2012. A consortium of three international companies had reportedly pulled out of a bid they won for Blocks 6 and 11 in 2007 due to worries about Turkish retaliation because one of them cooperates with Turkey in Kirkuk. Crisis Group interview, Gary Lakes, eastern Mediterranean editor, Middle East Economic Survey, 26 November 2011.

<sup>147</sup> Crisis Group interview, Greek Cypriot official, Nicosia, February 2012. “The world is onto Turkey. The way it’s behaving doesn’t make people comfortable that it is a reliable gas supplier. Turkey cannot bully its way in, but it should deal itself in. Why doesn’t TPAO bid on one of the blocks? They could do that if [Turkey and Republic of Cyprus] had relations”. Crisis Group interview, eastern Mediterranean energy expert, Nicosia, February 2012.

<sup>148</sup> “If there’s a [Cyprus] settlement, all is possible and Turkey has a chance to be part of the new picture. Without a solution, there will be LNG. And we have to make a decision now; everything has to be decided in advance”. Crisis Group interview, Praxoula Antoniadou Kyriacou, Greek Cypriot former commerce, tourism and industry minister, Nicosia, 23 February 2011.

<sup>149</sup> Crisis Group interview, energy executive with knowledge of the basin, February 2012, Nicosia.

<sup>150</sup> Crisis Group interviews, March 2012.

## 1. Liquefied Natural Gas, or LNG

For now, the most widely-discussed export option is building an LNG facility on the southern coast of Cyprus, where gas, extracted from Cypriot blocks will be brought via a pipeline, processed and exported to world markets. Aphrodite has just enough gas to make an LNG plant viable by itself.<sup>151</sup> Noble Energy is clearly leaning toward the LNG option.<sup>152</sup> It takes on average eight to ten years before an LNG plant becomes operational, including three to four years of negotiations between the energy company and the government, then another four years for building the plant.<sup>153</sup>

The liquefaction plant would be at Vasilikos power station in Limassol,<sup>154</sup> while other options include having it in the sea (on what is known as a “floating LNG” platform), or in Israel. The investment may cost around \$10 billion.<sup>155</sup> Noble Energy and its main Israeli partner, Delek Group, have proposed an onshore facility with capacity to eventually produce 15 million tons of gas (0,7 tcf, or about 21 bcm) per year, which is larger than Egypt’s Damietta and Idku plants combined.<sup>156</sup>

LNG is by no means the perfect solution, however. Arguments in favour of it include market flexibility and shipment to Asia where gas prices are higher,<sup>157</sup> but Suez canal fees and new gas finds off east Africa and elsewhere will

reduce the prospects of Cypriot profit.<sup>158</sup> In addition to the major upfront cost, LNG shipments also cost significantly more than piped gas.<sup>159</sup> Furthermore, financiers of LNG investments may want to see twenty to 30 year up front commitments to buy if they are to break ground on a new project. For any LNG plant to be truly profitable, it would need double the amount of gas currently known to be in the Aphrodite field, and early Cypriot hopes of extra gas volumes from Israel are now seen as unlikely to materialise.<sup>160</sup> An international diplomat also warns it may be difficult for Cyprus to attract such a large investment in the current tense environment: “The company [that will build the LNG plant] has to find the money and insurance. Nobody is going to go near LNG [as long as Turkish threats persist]”.<sup>161</sup>

## 2. Pipeline options: Israel, Greece or Turkey?

Returns are quicker with a pipeline compared to an LNG investment, and if the pipeline is not too long, the initial costs are lower. Three possible routes have emerged. Following increased cooperation with Israel in energy and commercial areas, the one most widely discussed in Greek Cypriot media is sending the gas to Israel, even though this could create security problems.<sup>162</sup> Theoretically, Cypriot gas could relatively easily feed into the Arab Gas pipeline, which connects Egypt, Israel, Syria and Lebanon and is projected to be linked to Turkey in the future; but this is unlikely to happen soon given the high volatility in the region.

Secondly, Greek officials say a preliminary study into building an underwater pipeline between Greece and Cyprus has been conducted, and alternatives are being examined.<sup>163</sup> But Noble Energy says such a pipeline is not viable because of the distance from the field and seabed com-

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<sup>151</sup> 6-7 tcf (170-200 bcm) makes a plant viable. Crisis Group interviews, energy executive, senior international official, Nicosia, February 2012. But it is not enough to make much profit. “It is just enough for one train [liquefaction, purification facility inside the plant]. One train is dangerous because you have no safety net in the event of problems. The second, third and fourth trains [bring in the cash]”. Crisis Group interview, energy executive, Oslo, March 2012.

<sup>152</sup> Crisis Group interviews, diplomats and international experts, Nicosia, February 2012.

<sup>153</sup> Crisis Group interview, energy expert with knowledge of the basin, Nicosia, November 2011.

<sup>154</sup> If additional gas finds are made in the other twelve blocks, a bigger facility would be needed, but the real estate available at Vassilikos is limited. A receiving terminal would need to be built in Limassol, allowing ships to dock and transfer the gas. “Finding gas is easy”, *Cyprus Mail*, 1 January 2012.

<sup>155</sup> An energy executive with knowledge of the field gives the range as \$5-\$15 billion, a senior international official estimates \$10 billion. Crisis Group interviews, Nicosia, February 2012. Panos Papanastasiou, member of a small group of experts advising the government on natural gas issues, also said an LNG plant would cost \$10 billion. *Cyprus Mail*, 30 November 2011.

<sup>156</sup> Gary Lakes, eastern Mediterranean editor, Middle East Economic Survey, presentation at “Cyprus Offshore Hydrocarbons: Wealth Distribution and Regional Politics” conference, Nicosia, 26 November 2011.

<sup>157</sup> Crisis Group interview, Gary Lakes, eastern Mediterranean editor, Middle East Economic Survey, Nicosia, 21 February 2012.

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<sup>158</sup> Crisis Group interviews, international petroleum executives, March 2012.

<sup>159</sup> Crisis Group interview, Nicos Rolandis, former Greek Cypriot foreign and commerce minister, Nicosia, February 2012. “The LNG [option] is not easy because of its high cost”. Crisis Group telephone interview, executive from a major international petroleum company, March 2012.

<sup>160</sup> Crisis Group interviews, international petroleum executives, March 2012.

<sup>161</sup> Crisis Group interview, senior international official, February 2012.

<sup>162</sup> “In an ideal world, you send all the gas to Israel and connect it to the Arab pipeline. But of course that can’t happen because of the security situation. [The] Jordan pipeline gets bombed often”. Crisis Group interview, Gary Lakes, eastern Mediterranean editor, Middle East Economic Survey, Nicosia, 26 November 2011. The Arish-Ashkelon pipeline which brings Egyptian gas to Israel was attacked ten times in 2011.

<sup>163</sup> Crisis Group email correspondence, Greek official, 31 January 2012.

plexities.<sup>164</sup> It would take seven years just to make the pipe, which would be the longest and deepest in the world.<sup>165</sup>

The third option is a pipeline to Turkey and onwards transport to the EU. As a European diplomat explained to Crisis Group, “The simplest way to export is a pipeline to Turkey and joining Turkish networks. This would be 10 per cent of the cost of LNG”.<sup>166</sup> An executive from an international petroleum company agrees: “The technological challenges of laying a pipeline between Cyprus and Turkey can be dealt with, and this would be the clear economic solution”.<sup>167</sup> Turkish officials also support this view.<sup>168</sup> A former Greek Cypriot minister suggests exporting via Turkey to Greece, for instance, and an interconnector pipeline between the two countries already exists.<sup>169</sup> While economics matter, a Turkish energy executive argues, “It would be best for everybody to get this gas to Turkey. Economics is not the issue, the issue is political. This is a very good tool to bring peace, it can be a peace pipeline”.<sup>170</sup> Separately, Turkish officials have talked up the idea of Israeli gas being piped to Turkey.<sup>171</sup>

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<sup>164</sup> Noble Energy’s Cyprus country manager John Tomich said such a project would be immensely costly and “poses daunting logistical difficulties due to the geology between Cyprus and Greece because of the presence of trenches and faults in the seabed”. “Noble to drill second well after September”, *Cyprus Mail*, 27 January 2012.

<sup>165</sup> “There are three factories in the whole world that could make a thick enough pipe. It wouldn’t be good to do”. Crisis Group interview, energy executive with knowledge of the basin, Nicosia, February 2012.

<sup>166</sup> Crisis Group interview, European diplomat, Nicosia, February 2012. “The only way for that gas to go, for Israel too, is a pipeline to Turkey. There’s nowhere else for the gas to go except Turkey”. Crisis Group interview, U.S. official, Istanbul, January 2012.

<sup>167</sup> Crisis Group telephone interview, March 2012.

<sup>168</sup> A Turkish energy official says: “Piping this gas to Greece is the most difficult one [technically] among all options. With the Arab gas pipeline, the possibility of sabotage is high. The LNG alternative is not feasible as there is too much LNG in that region already. So, pipeline to Turkey is the only sensible alternative”. Crisis Group interview, Ankara, January 2012.

<sup>169</sup> Crisis Group interview, Nicos Rolandis, former Greek Cypriot foreign and commerce minister, Nicosia, 23 February 2012. An executive from a major international petroleum company said 5 bcm could easily be delivered to Greece through this existing pipeline infrastructure. Crisis Group telephone interview, March 2012.

<sup>170</sup> Crisis Group interview, Istanbul, December 2011.

<sup>171</sup> According to Turkish Energy Minister Taner Yıldız, absent Turkish-Israeli political problems, Turkey might speak of a partnership with Israel for gas export. “All the feasibility studies conducted are now pointing to Turkey [as the most suitable transportation route]”. “Israeli gas deal tied to resolution of Mavi Marmara dispute”, *Today’s Zaman*, 11 March 2012.

In addition to being a good export route to Europe, Turkey itself is also a convenient market for eastern Mediterranean gas with its high-growth levels<sup>172</sup> requiring sustainable energy supply. Currently, the country imports natural gas by pipeline from Russia, Iran and Azerbaijan, plus small amounts of LNG via ships from Nigeria and Algeria. If the price is right, Turkey can use Mediterranean Sea gas domestically, possibly increasing the share of gas in its energy consumption.<sup>173</sup> It spends \$50 billion a year on energy, as most of it needs to be imported.<sup>174</sup>

There are arguments against a pipeline to Turkey, which risks limiting the Cyprus gas market to Europe, and doubts that it is possible to use Turkey as a transit given its currently insufficient infrastructure.<sup>175</sup> Turkish officials assert that if the political will exists, the link to Europe can be expanded in two years.<sup>176</sup> Extensive discussions are already ongoing on how to pipe significant amounts of new Azeri gas from Turkey into the EU. Fixing the buyer may not necessarily be negative, as it would mean having a guaranteed market.<sup>177</sup> Plus, an energy executive says the “netback value”, ie, net returns, from a pipeline through Turkey to Europe would still be higher than shipping LNG to Asia.<sup>178</sup>

The most important problem is the political environment. The former Greek Cypriot commerce minister referred to

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<sup>172</sup> Turkey’s GDP grew 8.9 per cent in 2010, according to the Turkish Statistical Institute.

<sup>173</sup> Crisis Group interview, Turkish energy official, Ankara, January 2012. “I would keep some of the gas for my own activities at gas-powered plants. It would be cheaper than using Russian gas”. Crisis Group interview, top level Turkish energy executive, Istanbul, December 2011.

<sup>174</sup> According to a report issued by Turkish authorities in May 2011, Turkey produced 0,726 bcm, or a negligible 0,026 tcf, gas in 2010, compared with a BP figure for natural gas demand of 39 bcm, or 1.4 tcf. Turkey’s General Directorate of Petroleum Affairs, [www.pigm.gov.tr](http://www.pigm.gov.tr); and BP Statistical Review of World Energy June 2011, [www.bp.com](http://www.bp.com).

<sup>175</sup> “If you go via Turkey, you tie yourself to the EU market. Price of gas in the EU is half of that in Asia. It makes more sense from a financial perspective for Greek Cypriots to convert it to LNG and send it to Asia via ships, even though an LNG plant costs more initially. Another issue is that Turkey’s infrastructure to get the gas to Europe is not there yet”. Crisis Group interview, energy expert with knowledge of the basin, Nicosia, November 2011.

<sup>176</sup> “An infrastructure to export gas to Europe can be built in two years”. Crisis Group interview, top level Turkish energy executive, Istanbul, December 2011. “There are pipelines that are already built and will open soon. If there is political will, a pipeline to Europe can be done in two years”. Crisis Group interview, Turkish energy official, Ankara, January 2012.

<sup>177</sup> Crisis Group interview, Cyprus-based economist, December 2011.

<sup>178</sup> Crisis Group interview, December 2011.

plans for a pipeline project to Turkey,<sup>179</sup> but without a solution in Cyprus and improved relations, even talking about it generated negative publicity.<sup>180</sup> If the Greek Cypriots commit to an LNG facility, leaving Turkey and Turkish Cypriots out, it will further entrench hostilities and deepen the de facto partition of the island.<sup>181</sup> At the same time, Turkey has not yet expressed an open interest either in talking to Greek Cypriots or transporting this gas. Even if it did, such a discussion would need third-party mediation – by the UN, the U.S. or another neutral non-EU country – since the two parties do not talk to each other and since talks would involve extensive negotiations on prices, taxes, lengths of pipelines, legislation in both countries and revenue-sharing.<sup>182</sup>

## V. SHARING THE BOUNTY

The drift to partition on Cyprus is becoming irreversible. The reunification talks are stumbling and few believe this round can be revived over the next year. In the absence of a settlement, risks loom that may block Cyprus from benefiting from its new gas wealth.<sup>183</sup> At the same time, there is an appetite on the island for new ideas. Opportunities exist to avoid further instability and to optimise gas extraction and transport if each party takes both independent and coordinated steps to overcome psychological barriers and political impasses. In the absence of mutual agreement, Turkey will see no benefit from the new hydrocarbon-rich province at its back door and the Republic of Cyprus may experience higher costs and years of delays in monetising its reserves. More than ever, these two parties have interests to talk about the hydrocarbons, continental shelf and sea they share.

### A. INDEPENDENT STEPS

#### 1. Respecting mutual rights

At a time of high financial and energy needs, it is politically impossible for any Greek Cypriot leadership to leave the gas in the ground.<sup>184</sup> Even though revenues are not expected for several years, and as long as reunification is the formal goal,<sup>185</sup> the Greek Cypriots should commit to distributing at least 20 per cent of either the gas or profits from its sale to Turkish Cypriots.<sup>186</sup> Some Turkish Cypriots

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<sup>179</sup> “Rum sürprizi” [Greek Cypriot surprise], *Sabah*, 19 Dec 2011. A pipeline project bringing Russian gas to the Mediterranean via Turkey was envisaged in a report titled “The day after: Commercial opportunities following a solution to the Cyprus problem”, co-authored by Praxoula Anroniadou Kyriacou, Fiona Mullen and Özlem Oğuz. Peace Research Institute Oslo (PRIO) Cyprus Center, 1/2008.

<sup>180</sup> Some Greek Cypriots say Turkey would need to sign UNCLOS first. Crisis Group interview, Alexandros Lordos, Greek Cypriot polling expert, Nicosia, 22 February 2012.

<sup>181</sup> “The natural market [for this gas] is Europe. Trying to base the gas production on the basis of hostility [to Turkey] will be disastrous . . . . The future lies in peaceful productive cooperation. We need visionary leaders who will dare to resolve problems of the past and move ahead into the future for the benefit of the peoples of the eastern Mediterranean and those of our wider European family”. Crisis Group interview, Praxoula Anroniadou Kyriacou, Greek Cypriot former commerce, tourism and industry minister, Nicosia, 23 February 2012.

<sup>182</sup> Crisis Group interview, Turkish energy official, Ankara, January 2012.

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<sup>183</sup> “They won’t be able to exploit gas while Turkey’s objections are in place”. Crisis Group interview, international official, Istanbul, December 2011. The former Greek Cypriot foreign and commerce minister, Nicos Rolandis, argues that unless Greek Cypriots find a way to share the revenues with Turkish Cypriots, they may not be able to proceed with the exploitation of their hydrocarbon wealth, which may be worth \$400-\$500 billion or 0.5% of the world reserves, before it is “cannibalised” by their neighbours. “Christofias (rise and fall) and offshore oil & gas”, 15 September 2011 (provided by the author).

<sup>184</sup> Crisis Group interview, senior international official, February 2012.

<sup>185</sup> A two-state solution or loose confederation is increasingly discussed on both sides of Cyprus. Crisis Group interviews, Nicosia, February 2012.

<sup>186</sup> This interim figure is based on relative populations and would be to underline initial Greek Cypriot commitment; any final figure would be subject to negotiation or a final settlement. A 2011 census in the north, viewed as reliable by the UN, showed that there are 300,000 residents of the Turkish Cypriot zone. Since there are officially 800,000 residents of the Greek Cypriot government zone, residents of north Cyprus now represent 27 per cent of the island’s population. On the basis of ethnicity, population expert Mete Hatay estimates the relative number of residents who qualify as Turkish Cypriots according to Greek Cypriot rules as 140,000, while there are 630,000 ethnic Greek

and Greek Cypriots have proposed the idea of using an escrow account, and debated whether the money should be available immediately, after a settlement or for a set number of years.<sup>187</sup> Naturally, Turkish Cypriots should also declare their readiness to share any possible net revenues from their onshore hydrocarbon project in an inverse proportion to what the Greek Cypriots pay them.

Any funds or gas should be made available to the Turkish Cypriot administration, as the future constituent state or federated entity of a united Cyprus, or if this appears to imply recognition, Greek Cypriots could send the funds to a UN-supervised mechanism. Neutral third-party supervision would be desirable to avoid disputes. If either side were to choose formally not to pursue reunification, however, any such sharing of resources would naturally cease. According to the Greek Cypriot politician who scored the diplomatic coup of signing the Egypt-Cyprus EEZ, the first such deal in the eastern Mediterranean:

[Sharing the gas up front] would entail a protection of our self-respect and our sovereignty (which are now in danger), the avoidance of any military adventure and a constructive gesture to the other community which might prove conducive to the solution of the Cyprus problem. We would also be enabled to proceed without delay and without any hindrance with the exploitation of our hydrocarbon wealth ... before it is cannibalized by our neighbours .... "When elephants fight it is the grass below their feet that suffers". In our case, between Israel, Turkey, [Lebanon] and Cyprus, we are unfortunately the grass.<sup>188</sup>

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Cypriots in the south, making the Turkish Cypriot-Greek Cypriot ratio 22-78 per cent. Crisis Group interview, Nicosia, February 2012. The last island-wide census in 1960 found that Turkish Cypriots constituted 18 per cent of the population. See [http://ec.europa.eu/languages/documents/cy\\_en.pdf](http://ec.europa.eu/languages/documents/cy_en.pdf).

<sup>187</sup> "If the UN Security Council members had said 'we will set up an escrow account under UN auspices and will not release funds to Cyprus until a settlement', we would have a solution to the Cyprus problem in a few months". Crisis Group telephone interview, Özdil Nami, Turkish Cypriot politician in the opposition and former chief negotiator, 27 January 2012. "[We should] put aside money in an escrow account according to a formula agreed with the Turkish Cypriots. ... Redistribution of wealth will be very difficult without a solution". Michael Sarris, presentation, op. cit. "I put forward a plan, which I repeated many times during the past five years. ... The plan would provide that out of the net income of the Republic of Cyprus from oil and gas reserves, a percentage to be agreed would be deposited in an escrow account in favour of the Turkish Cypriots, payable either upon solution of the Cyprus problem or at a fixed time to be agreed, whichever happens earlier". Nicos Rolandis, former Greek Cypriot foreign and commerce minister, "Christofias (rise and fall) and offshore oil & gas", 15 September 2011 (provided by the author).

<sup>188</sup> Ibid.

Greek Cypriots have an interest in remedying their future federation partners' predicament now to show that it is not only Turkey that is looking out for their interests, and to remove Ankara's justification for drilling in Cypriot waters. Turkish Cypriots should reassure their Greek Cypriot neighbours, the original owners of some two thirds of what is now the Turkish Cypriot zone,<sup>189</sup> that their property claims in the north will be remedied in line with European Court of Human Rights standards.<sup>190</sup>

At the same time, Turkey and Turkish Cypriots should formally commit not to interfere with, or to drill in, the Aphrodite field or other offshore hydrocarbon blocks in Greek Cypriot waters. Both sides should also give assurances that they are not planning activities in waters west of Cyprus disputed between Turkey and the Republic of Cyprus, pending talks on a joint arrangement, or, as suggested below, a broader Turkey-Cyprus-Greece EEZ settlement after application to the ICJ or an arbitral tribunal.

## 2. Building confidence

Turkey should open its airports and ports to Greek Cypriot vessels, as it has committed to do under its 2005 Customs Union agreement with the EU (the Additional Protocol to the Ankara Agreement). This would be the minimum for starting talks on using Turkey as a possible transport route for eastern Mediterranean gas, as it would be absurd to expect Greek Cypriot officials to allow Cypriot gas to travel to Turkey when their ships and planes cannot. Such a step would also relaunch Turkey's EU membership process, since it would automatically open fourteen negotiating chapters.

For its part, the Republic of Cyprus can strengthen this confidence-building environment by permitting Turkish Cypriots to trade directly with the EU, as the EU Council promised before the Republic of Cyprus joined the EU in 2004.<sup>191</sup> Such Turkish Cypriot trade through the port of

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<sup>189</sup> Greek Cypriots say they owned 78 per cent of private land; Turkish Cypriots argue it amounts to about 60 per cent of the total Turkish Cypriot zone. See Crisis Group Europe Report N°210, *Cyprus: Bridging the Property Divide*, 9 December 2010, op. cit., p. 2.

<sup>190</sup> This is currently done through an Immovable Property Commission (IPC), but its mandate is short-term, even though the Turkish Cypriot leadership keeps extending it.

<sup>191</sup> See Crisis Group Briefing, *Cyprus: Six Steps toward a Settlement*, op. cit., p. 7 and p. 10. Direct Trade was a 2004 European Commission proposal to allow Turkish Cypriots to export to the EU directly at preferential customs rates, instead of being forced to go through Greek Cypriot ports or pay external EU duties. Alternatively, Greek Cypriots could declare Famagusta port open, under Turkish Cypriot management, for preferential trade with the EU and under supervision of EU officers.

Famagusta and other exit points could easily be monitored by EU officials through an extension of existing regulations.

These two steps could be simultaneous or independent. As Crisis Group has frequently underlined, this would open the way to a good degree of normalisation without sacrificing any of the parties' fundamental positions on the Cyprus settlement.

## B. STEPS TO AN AGREEMENT

If the parties agree to a dialogue on how to most effectively exploit the eastern Mediterranean's resources, they should resolve their disputes over maritime boundaries and utilisation of the gas. As Greek Cypriots and Turks have no formal relationship and have had almost no direct talks for nearly four decades, it is likely that complex negotiations on a gas process would require mediation by the U.S., the UN, or a neutral state or small group of neutral countries. Depending on the issue to be discussed, third parties would mediate between Nicosia (involving both sides of the island), Ankara, and Athens<sup>192</sup> on the following issues.

### 1. Energy issues

Greek Cypriots and Turkish Cypriots could form an ad hoc advisory committee to discuss gas exploitation and domestic consumption. It could join a number of technical committees of experts set up in 2008, who continue to do good work coordinating issues related to police and crime, health, environment and cultural/religious sites.

Similarly, officials from Turkey and the Republic of Cyprus should agree to carry out exploratory talks on eastern Mediterranean energy issues, without demanding that a deal be reached on reunifying the island first, without prejudice to the UN-facilitated talks and to any eventual mutual official recognition that will follow a settlement. The Republic of Cyprus should be prepared to discuss possible cooperation on a gas export pipeline through Turkey to Greece and onwards to Europe, or for sale to Turkish markets, and Ankara should be prepared to discuss the commercial and government guarantees it would give to any contract, with strong third-party arbitration clauses.

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<sup>192</sup> The Greek involvement is necessary both from a Cyprus problem perspective, as a guarantor state, and also because Greece would need to take part in a Mediterranean EEZ delimitation with Turkey.

### 2. Exclusive economic zones (EEZs)

Turkey, Cyprus and Greece should agree to take their claims for EEZs in the eastern Mediterranean to the ICJ, an arbitral tribunal or the International Tribunal for the Law of the Sea (ITLOS).<sup>193</sup> In private, Turkey has seen adjudication as a valid option for others, at least, pointing out to Egypt that it ended up with a smaller EEZ by doing a bilateral agreement with the Republic of Cyprus and should have taken the issue to ICJ.<sup>194</sup> It would be even better if the parties could agree on this matter among themselves, but this seems most unlikely. In and around Cyprus, the various sides have tried and failed to impose their own unilateral settlements for decades, and, given the limited time available to find an inclusive framework to exploit Cypriot gas, a neutrally adjudicated compromise is now needed.

More than 50 meetings between Turkey and Greece have failed to reach a deal on how to divide the Aegean Sea, despite good relations and a decade of strong normalisation and expanding trade. Part of the problem is historical and psychological, and part is about maritime delimitations, with Turkey and Greece disagreeing on the boundaries of both Aegean islands and between the Aegean and the Mediterranean seas, stoking Turkish fears that it will be deprived of fair maritime zones.<sup>195</sup>

Pending a ruling on delimitation to solve their underlying disputes, the parties can still cooperate with a working agreement to manage resources. One way to do this is through a joint development mechanism, a model that has backing in international adjudication,<sup>196</sup> where the sides

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<sup>193</sup> Even though Turkey is not a signatory to UNCLOS, it can resort to the dispute resolution methods listed in the convention by agreement. Article 74, which addresses EEZ delineation between states with opposite or adjacent coasts, points to Part XV for settlement of disputes, including conciliation and binding adjudication by ITLOS, the ICJ or an arbitral tribunal pursuant to the procedures of Annex VII. Conciliation may be conducted by agreement between states, and being a signatory to UNCLOS is not a prerequisite for the jurisdiction of ITLOS, the ICJ, or an arbitral tribunal.

<sup>194</sup> "Egypt lost 14,500 sq km by doing a bilateral EEZ delimitation [with Cyprus], instead of doing one with us. We told them they should have gone to the ICJ". Crisis Group interview, Turkish official, January 2012.

<sup>195</sup> See Crisis Group Briefing, *Turkey and Greece: Time to Settle the Aegean Dispute*, op. cit.

<sup>196</sup> There is no fixed terminology to refer to legal arrangements under which states agree to develop and exploit resources jointly in maritime areas subject to overlapping claims of sovereignty. The terms "joint development agreement", "joint exploration agreement" and "joint management agreement" are commonly used. The ICJ has endorsed this mechanism for resolving disputes over natural resources, although both ICJ and arbitral tribunals have stopped short of imposing joint exploitations in

must agree on how the revenues will be divided, what geographic areas will be covered, who will carry out the exploration, and so on. International mediation will increase chances of success. Such an arrangement would lead to closer relations and understanding between the parties, pooling of expertise, financial resources and technological assets.

### 3. Pipelines

If ongoing studies find a pipeline to Turkey to be an economically compelling and safe gas export route, then Turkey and the Republic of Cyprus should try to reach an agreement on commercial terms. The gas could be sold in the Turkish market and, in initial limited quantities at least, be passed on through the interconnector pipeline to Greece.<sup>197</sup>

Until a settlement, Republic of Cyprus and the commercial operators should have the right to decide how the gas is developed and where it goes. The upfront cost of such an option will be far less than the more independent LNG option, and its longer-term security could be even stronger.

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their judgments. An example is the North Sea continental shelf case where the ICJ said an agreement for joint exploitation was particularly appropriate to preserve the unity of the deposit. "Decision of 20 February 1969 in the North Sea Continental Shelf case [between Federal Republic of Germany, Denmark and Netherlands]", ICJ Reports, 1969.

<sup>197</sup> The existing Turkish pipeline infrastructure could without much modification pass on to Greece about 5 bcm (0.2 tcf) per year, about half of Aphrodite's expected production. Crisis Group telephone interview, international oil executive, March 2012.

## VI. CONCLUSION

Resolving differences over maritime boundaries and satisfying all parties' legitimate concerns over the new hydrocarbon riches would benefit all sides in the long term. Greek Cypriots should avoid unilaterally going after short-term gains when their long-term security is overshadowed by Turkish occupation troops and the frozen conflict. While the gas finds could be the locomotive for reunification, unilateral developments will make a jointly negotiated settlement even more difficult, further raise tensions and hurt hopes of future security and stability around the island. Turkish Cypriots, as long as reunification is the goal, must be assured in advance of a fair share of any income. On the other hand, a feasible plan to make Turkey the export route may convince Ankara of its interest in cooperating with Greek Cypriots, who should not condition any talks with Turkey on reaching a settlement first.

For Greek Cypriots to overcome decades of fearful hostility and consider cooperation, however, Turkey will have to reach out rather than threaten. Its current stance is that of an assertive power making legally indefensible claims on another, far weaker sovereign state's rights. In addition to damaging its international image and uniting regional rivals like Cyprus, Israel and Greece together against it, failure to solve the Cypriot conflict keeps Turkey's EU membership negotiations in the deep freeze. Ankara's refusal to engage Republic of Cyprus officials is part of the dead-end policy of the past. Agreeing to discuss Cypriot offshore reserves may not only be profitable, but it could also open the path for greater normalisation on the island.

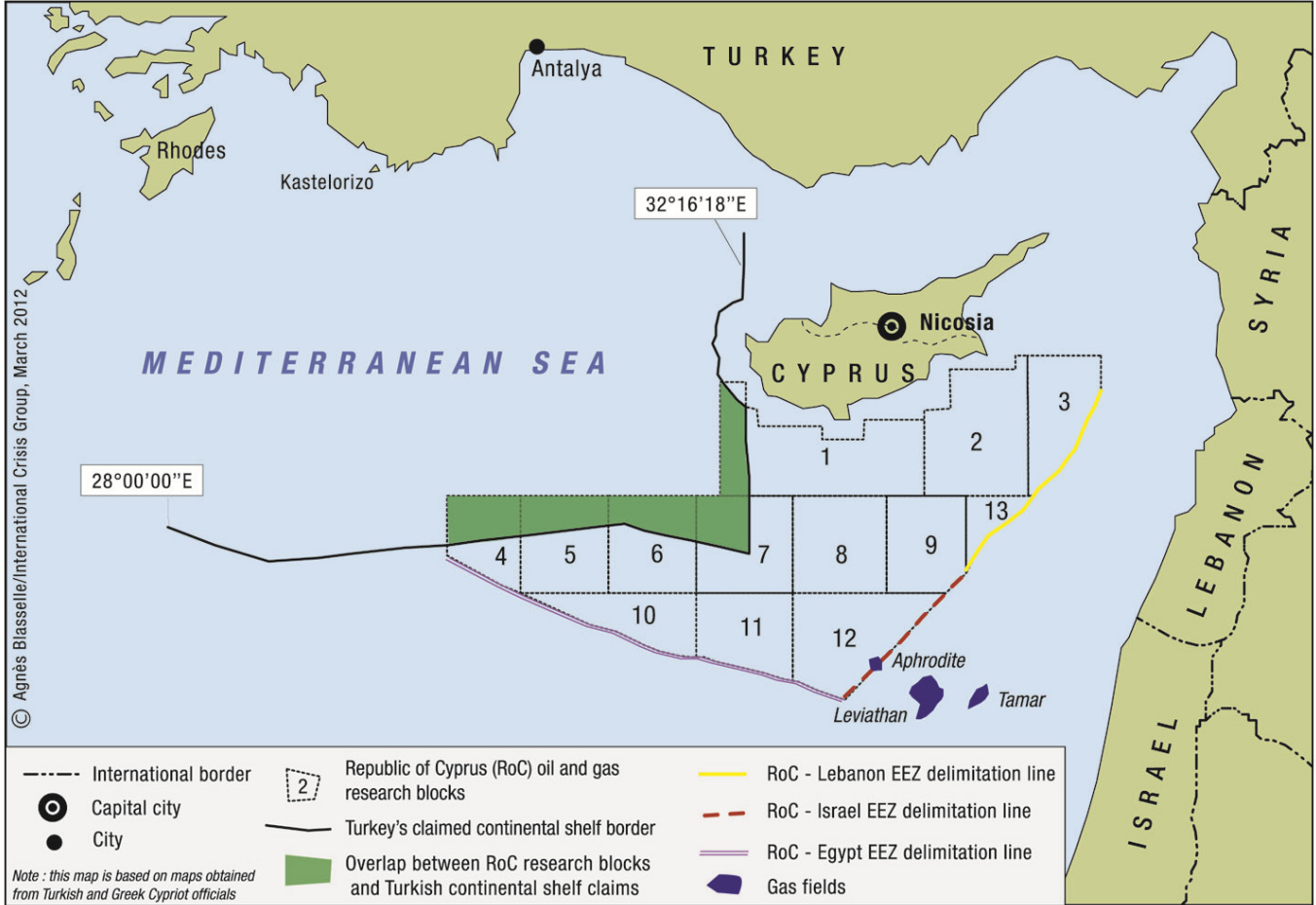
Turkey says it is looking out for the interests of Turkish Cypriots, but it is not possible in the current status quo for the latter to fully benefit from the development of hydrocarbon riches in the south and substantiate a claim. On a broader scale, without a negotiated settlement, they will continue facing Greek Cypriot opposition to their efforts for international recognition and their zone will be further absorbed into Turkey.

The challenge to reach a breakthrough is great as both sides need to overcome generations of lack of communication and misinformation – and avoid any accidental escalation. Using gas riches as an incentive to establish contacts and communication would help build confidence, would not prejudice the eventual outcome of talks, and does not have to address the complex issues of status or recognition before a settlement. It is nonetheless worth remembering that it is such a settlement, and not the gas, that will one day provide the real economic bonanza for all the inhabitants of Cyprus.

**Nicosia/Istanbul/Brussels, 2 April 2012**

APPENDIX A

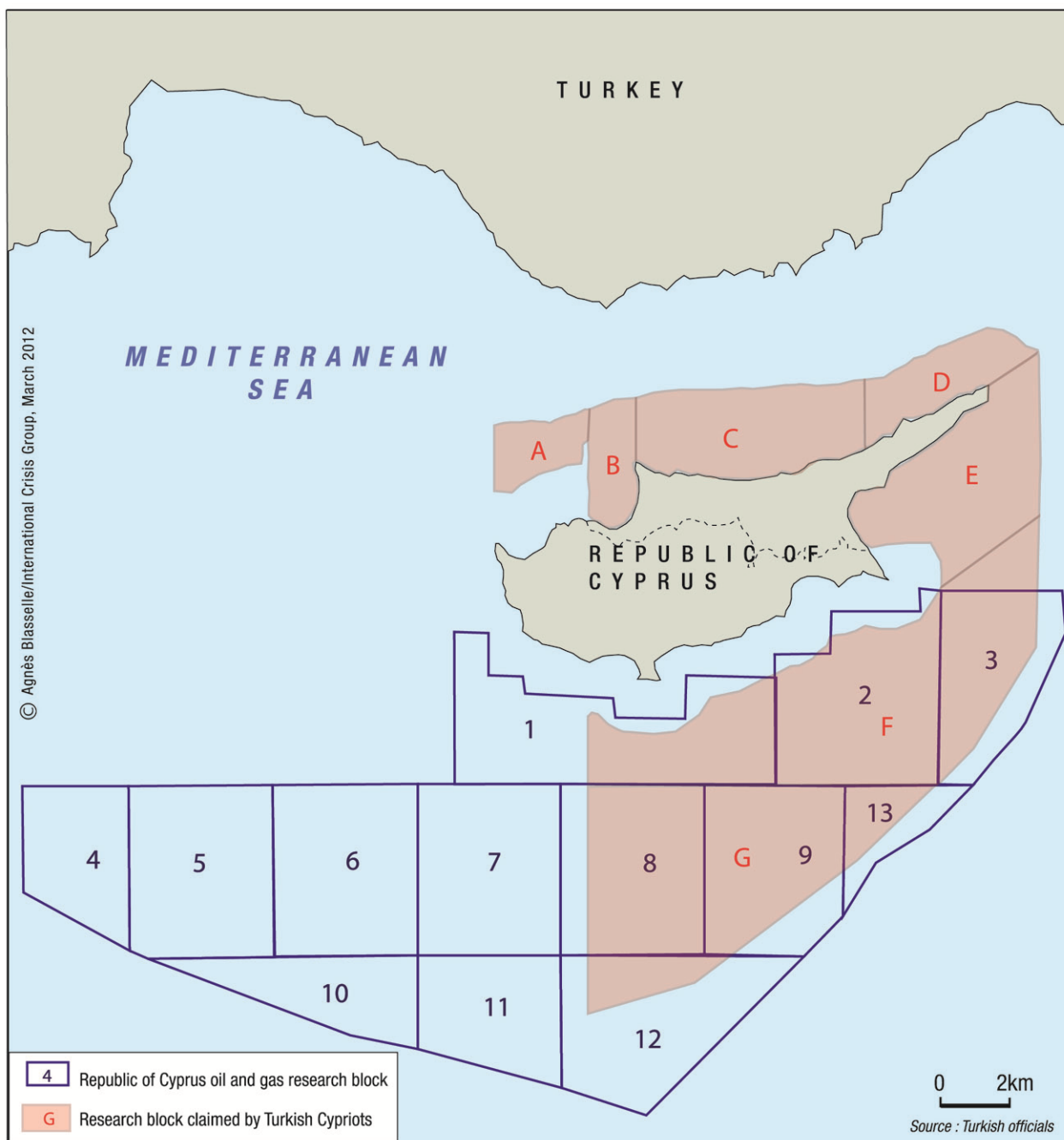
MAP 1: THE REPUBLIC OF CYPRUS EEZ DELIMITATIONS AND HYDROCARBON RESEARCH BLOCKS, AND TURKEY'S CONTINENTAL SHELF CLAIMS





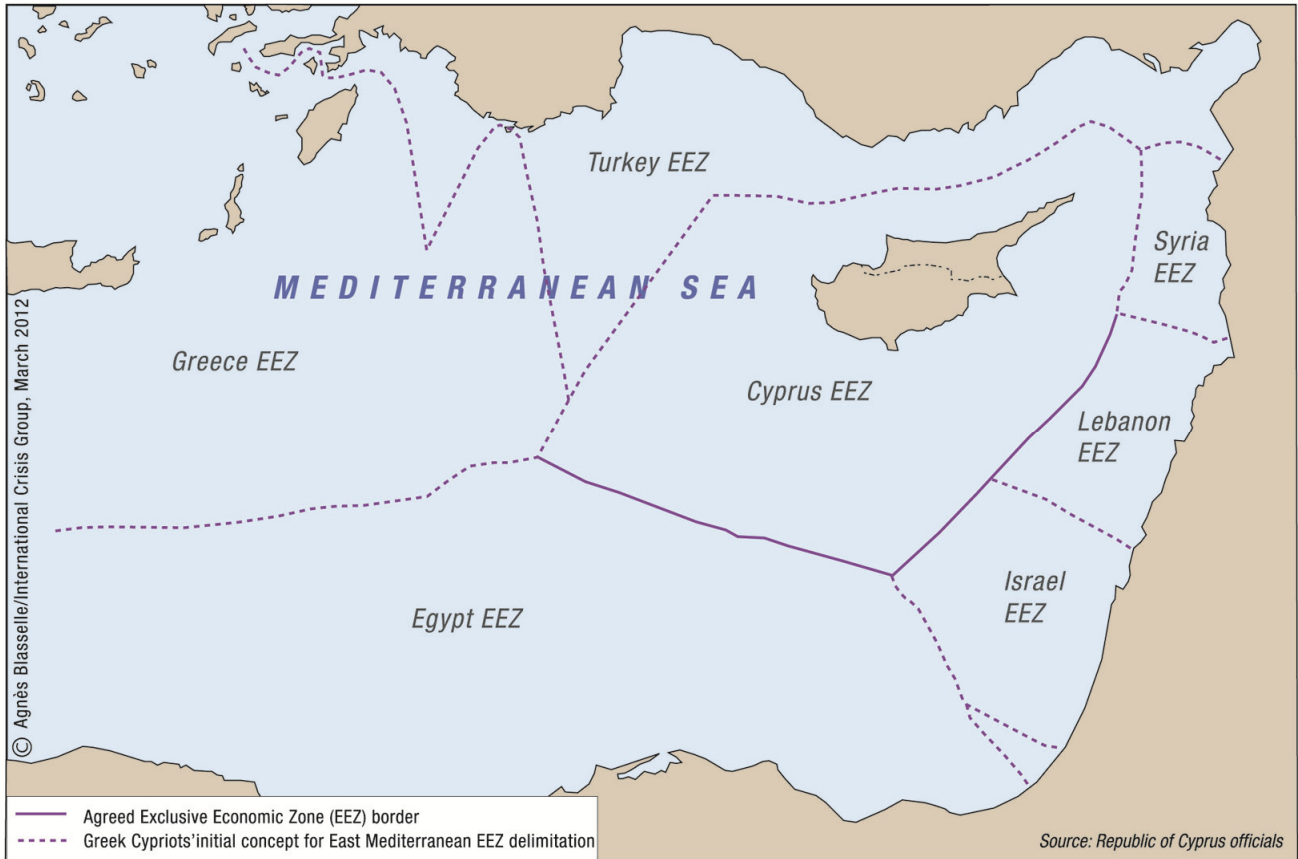
## APPENDIX B

### MAP 2: THE TURKISH CYPRIOTS' CLAIMED HYDROCARBON RESEARCH BLOCKS



### APPENDIX C

**MAP 3: THE INITIAL GREEK CYPRIOT CONCEPT FOR EAST MEDITERRANEAN EEZ DELIMITATION**



## APPENDIX D

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- Tackling Azerbaijan's IDP Burden*, Europe Briefing N°67, 27 February 2012.

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- Cyprus: Reunification or Partition?*, Europe Report N°201, 30 September 2009 (also available in Greek and Turkish).
- Cyprus: Bridging the Property Divide*, Europe Report N°210, 9 December 2010 (also available in Greek and Turkish).
- Cyprus: Six Steps toward a Settlement*, Europe Briefing N°61, 22 February 2011 (also available in Greek and Turkish).

#### *Turkey*

- Turkey and Armenia: Opening Minds, Openings Borders*, Europe Report N°199, 14 April 2009 (also available in Turkish).
- Turkey and the Middle East: Ambitions and Constraints*, Europe Report N°203, 7 April 2010 (also available in Turkish).
- Turkey's Crises over Israel and Iran*, Europe Report N°208, 8 September 2010 (also available in Turkish).
- Turkey and Greece: Time to Settle the Aegean Dispute*, Europe Briefing N°64,

- 19 July 2011 (also available in Turkish and Greek).
- Turkey: Ending the PKK Insurgency*, Europe Report N°213, 20 September 2011 (also available in Turkish).

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<b>Neil &amp; Sandra DeFeo Family Foundation</b>	<b>Faisel Khan</b>	<b>Michael L. Riordan</b>	<b>Stelios S. Zavvos</b>
<b>Equinox Partners</b>	<b>Zelmira Koch Polk</b>	<b>Shell</b>	
<b>Fares I. Fares</b>	<b>Elliott Kulick</b>	<b>Statoil</b>	
<b>Neemat Frem</b>	<b>Liquidnet</b>		
	<b>Jean Manas &amp; Rebecca Haile</b>		

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## SENIOR ADVISERS

Former Board Members who maintain an association with Crisis Group, and whose advice and support are called on (to the extent consistent with any other office they may be holding at the time).

<b>Martti Ahtisaari</b> Chairman Emeritus	<b>Mong Joon Chung</b>	<b>Timothy Ong</b>	<b>Grigory Yavlinski</b>
<b>George Mitchell</b> Chairman Emeritus	<b>Pat Cox</b>	<b>Olara Otunnu</b>	<b>Uta Zapf</b>
<b>HRH Prince Turki al-Faisal</b>	<b>Gianfranco Dell'Alba</b>	<b>Lord (Christopher) Patten</b>	<b>Ernesto Zedillo</b>
<b>Hushang Ansary</b>	<b>Jacques Delors</b>	<b>Shimon Peres</b>	
<b>Óscar Arias</b>	<b>Alain Destexhe</b>	<b>Victor Pinchuk</b>	
<b>Ersin Arıođlu</b>	<b>Mou-Shih Ding</b>	<b>Surin Pitsuwan</b>	
<b>Richard Armitage</b>	<b>Gernot Erler</b>	<b>Cyril Ramaphosa</b>	
<b>Diego Arria</b>	<b>Marika Fahlén</b>	<b>Fidel V. Ramos</b>	
<b>Zainab Bangura</b>	<b>Stanley Fischer</b>	<b>George Robertson</b>	
<b>Shlomo Ben-Ami</b>	<b>Malcolm Fraser</b>	<b>Michel Rocard</b>	
<b>Christoph Bertram</b>	<b>I.K. Gujral</b>	<b>Volker Rüehe</b>	
<b>Alan Blinken</b>	<b>Max Jakobson</b>	<b>Mohamed Sahnoun</b>	
<b>Lakhdar Brahimi</b>	<b>James V. Kimsey</b>	<b>Salim A. Salim</b>	
<b>Zbigniew Brzezinski</b>	<b>Aleksander Kwasniewski</b>	<b>Douglas Schoen</b>	
<b>Kim Campbell</b>	<b>Todung Mulya Lubis</b>	<b>Christian Schwarz-Schilling</b>	
<b>Jorge Castañeda</b>	<b>Allan J. MacEachen</b>	<b>Michael Sohlman</b>	
<b>Naresh Chandra</b>	<b>Graça Machel</b>	<b>Thorvald Stoltenberg</b>	
<b>Eugene Chien</b>	<b>Nobuo Matsunaga</b>	<b>Leo Tindemans</b>	
<b>Joaquim Alberto Chissano</b>	<b>Barbara McDougall</b>	<b>Ed van Thijn</b>	
<b>Victor Chu</b>	<b>Matthew McHugh</b>	<b>Simone Veil</b>	
	<b>Miklós Németh</b>	<b>Shirley Williams</b>	
	<b>Christine Ockrent</b>		