Transiters Protection under ECT: Fact or Fiction?

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Importance of Transit in ECT Context

The Goals behind the ECT

- Liberalization of investment and trade in energy
- Implementation of “full national treatment” and “most favored nation” principles
- Avoidance of discrimination in international trade
- Removal of technical, administrative and other barriers in energy trade
- Potential GATT membership and harmonization of rules
- Support of the existing competition rules

What is the importance of ECT transit provisions in this context?
Transit as Means to Support Int’l Trade

- Primary purpose of the transit provision – fostering of trade in energy (similarly to GATT, WTO rules etc., mind ECT Article 4)

- Article 7 imposes some typical rules:
  - “non-discrimination” principle in respect of availability of transit facilities and pricing (1);
  - “national treatment” of Energy Materials and Products in Transit (3);
  - “no new obstacles” obligation (4)

- The original purpose of the transit provision appears to be trade-oriented
New Challenges to ECT

- Recent events demonstrated that energy relations in Europe bring challenges other than trade concerns.
- The most feared events – interruptions of supply/transit, potential consequences are beyond being measured in money – *energy security* is at stake:
  - industrial aspects
  - social aspects
  - political aspects
- *Energy supply/transit is a multi-billion-dollar business, the problems are magnified*
  - Europe-Ukraine-Russia relations in gas trade – the brightest example
The Gas Trade Relations Structure

- Familiar structure of the gas trade:

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Supplier → Transiter → Consumer
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Russian Federation/Gazprom → Ukraine/Naftogaz → European Consumers
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Gas Relations Triangle

- Because there are several levels of relations, this structure is a triangle:
Several mechanisms that provide for security in gas supplies to Europe on different levels:

- **Supplier’s security:**
  - Supply contract with its European counterparties;
  - Transit contract with the transiter

- **Consumers’ security:**
  - Supply contract with its Russian supplier
  - ECT provisions calling for non-interruption of transit

- **Transiter’s security:**
  - Is there a security for the transiter?
ECT Article 7: Risks for Transiters


How does it distribute risks? Let’s take a look at transiters’ rights and obligations under Article 7:

**Obligations:**

- Take necessary measures to facilitate transit;
- Avoid discrimination in access to transit facilities and pricing;
- Ensure no less favorable treatment than for materials or products for its own purposes;
- Avoid placing additional obstacles for transit;
- Secure established flows of Energy Materials to, from or between other Contracting Parties
- Not to interrupt the flow of Energy Materials in the event of a dispute, including a pricing dispute
What are the transiters’ rights under Article 7?

- Apply for the conciliator’s decision in case of a dispute;
- Not much else.

The transiters are vulnerable to virtually any irregularities in energy supply/transit relations, especially when all of the parties involved are not subject to the same legal provisions.
What Happens when Crisis Strikes?

Several crises in gas supply/transit during the past years: 2006, 2009

Origin of crisis: Russia-Ukraine supply contract.

Historically, there was a balance between the price for Russian gas and transit fee charged by Ukraine for transit – pricing disputes.
What Happens when Crisis Strikes? Cont’d

What are Ukraine’s options?

- It may not impose increased transit tariff – there are other transitters, it means renegotiation of terms with them;

- It may not cut off the gas transit – it would mean liability under the ECT;

- It (probably) may apply for the conciliator’s decision, but it is not efficient – **no such applications**

- It must ensure uninterrupted transit flow, no matter what
What Happens when Crisis Strikes? Cont’d

Further aggravation: Supplier can cut off gas for Ukraine (for commercial, political, other reasons)

- It has happened at least twice (2006, 2009) – during the winter period
- Causes economic and social distress in Ukraine
- Causes uncertainty as to the volumes of transited gas (claims of unauthorized taking, difficulties in gas accounting)
- Undermines Ukraine’s technical possibility to maintain transit: deficit of fuel gas
- Creates significant difficulties for operation of the gas transporting system that potentially can disrupt transit (necessity to facilitate reverse flow)
What Happens when Crisis Strikes? Cont’d

- In such situation Ukraine is potentially open to claims from:
  - **Russia/Gazprom** – under the transit contract;
  - **European consumers/states** – under the ECT provisions
- Ukraine’s defenses in such situations are not obvious.
- **ECT: energy security of the energy consumers dominates security of the transit countries.**
- After Russia’s formal withdrawal from the ECT, situation for Ukraine is all but hopeless.
ECT and Transit: Solving the Problem

- Difficulties with ECT transit provisions are acknowledged – Draft Transit Protocol under consideration, and questions still remain:
  - Prohibition of unauthorized taking of transited materials;
  - Transit tariffs determination – how liberal is this?
  - Supply of energy materials to the transiter – what are the consequences of failure to do so?
- It all may prove to be meaningless if the supplier (Russia) is not bound by these provisions
ECT and Transit: Solving the Problem.

Conclusions

- Russian President declared the need to replace the ECT with a “better” instrument. **Perhaps not such a bad idea for Ukraine?**

- The new legal framework should complete the “triangular” supplier-transiter-consumer structure: **supply and transit contract must be legally “merged”**

- East-West energy supply is a trilateral process, and **all three parties involved must be inter-connected** via respective rights and obligations

- **Transiter must build its relations with a consumer.** The scope of actual responsibility before the consumer is greater than before the supplier – purchase of gas at Ukraine/Russia border
Questions? Comments?

Thank You!