The speech of the Secretary General Amb. André Mernier

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Mr Chairman, it is a great pleasure for me to participate in this conference today and to address the issue of energy security from the perspective of the Energy Charter. I am also very pleased for the opportunity to return to Moscow, where I served for four years as Ambassador of Belgium, in my new capacity as Secretary General of the Energy Charter Secretariat.

I would like to begin by welcoming the decision by the Russian Federation to put the issue of energy security at the heart of its agenda for its presidency of the G8. This timely decision recognises two essential considerations: firstly, the importance of energy to the wellbeing and prosperity of societies across the globe; secondly, the important role that the Russian Federation itself can play in promoting reliable and secure energy supply.

In my view, the aim of any discussion on energy security should be to find a balance of interest between producers, transit countries and consumers of energy. This balance of interest provides the basis for stable international cooperation, and this is the philosophy that lies at the heart of the Energy Charter process.

If we look at the global energy scene today, we can see a number of difficult challenges. We see the need for investment in new energy production and infrastructure in order to meet growing demand. We also see the importance of clear-cut rules on international energy flows, and transit flows in particular, to ensure that energy resources can be brought to international markets without interruption. We also have to tackle the issue of energy efficiency and the need to reduce the environmental impact of energy use.

These are common challenges, requiring common approaches. These are also the specific areas that are covered by the Energy Charter Treaty, a unique legal instrument which has been signed by Russia and by fifty other countries across Europe and Asia. In drafting the Treaty in the early 1990s, Russia and the other negotiating partners were concerned to reduce some specific risks that affect the energy sector, based on the shared belief that long-term security of supply - and security of demand for producing countries - can best be served by a binding multilateral framework for energy cooperation.

I would like to use this opportunity to consider how the Energy Charter addresses the issues of investment security and reliable cross-border flows. I hope along the way that I can dispel some misunderstandings and misconceptions about the Treaty and its application.

Investment projects in the energy sector are highly strategic and capital-intensive, frequently requiring the cooperation of a large number of commercial partners and - in the case of cross-border transportation projects - the consent and support of
multiple governments. This is a uniquely complex environment, in which risks have
to be assessed over a long-term horizon.

It is a major task to reduce these risks, as far as possible, by creating a stable and
transparent investment climate. The Energy Charter Treaty assists in this respect by
offering binding protection for energy investors against key non-commercial risks,
such as discriminatory treatment, direct or indirect expropriation, or breach of
individual investment contracts. By promoting transparency and sanctity of contract,
the Treaty provides a reliable interface between an investment project and the host
government. Moreover, by reducing risks the Treaty can also reduce the cost of
investment capital.

The Energy Charter Treaty does not dictate the structure of national energy markets
in its member states - there is no obligation to privatise or to unbundle vertically
integrated companies, and the Treaty is not a lever to force open access for foreign
investors to a country's oil and gas reserves. On the contrary, a fundamental
principle affirmed by the Treaty is national sovereignty over energy resources. Each
member country is free to decide how, and to what extent, its national energy
resources will be developed, and also the extent to which its energy sector will be
open to foreign investors.

Looking at this issue from a Russian perspective, it is important to remember that the
potential benefits of the Treaty are not limited to energy investment projects in
Russia itself. Russian energy companies are increasingly active in other countries
that are bound by the Charter Treaty, both in neighbouring regions such as those of
the Caspian region and Central Asia, and also in the main downstream markets. In
some of these countries, Russian investment raises political and strategic
sensitivities that can expose these investments to significant non-commercial risk.
The Treaty provides a clear and transparent legal mechanism for the protection of
these investments.

I would like to turn now to the issue of reliable cross-border flows. The recent dispute
between Russia and Ukraine demonstrated very clearly the link between questions
of energy transit and the overall agenda for energy security. Both Russia and
Ukraine are very important transit countries, and these events showed to me, and to
many other observers, the need for clear-cut international rules on energy transit that
can reduce the risk of future interruptions to supply.

In relation to the recent dispute, I should say immediately that it is not my role as
Secretary General to make judgements on specific issues arising between our
member states. In the event of a disagreement between member states on matters
covered by the Treaty, there are mechanisms within the Treaty for dispute resolution,
including a specific conciliation procedure for transit issues. I wrote to both the
Russian and Ukrainian authorities in the first days of January to recall the availability
of these mechanisms, but this possibility was overtaken by the swift conclusion of a
bilateral agreement. I should emphasise that bilateral agreements are always a
preferable solution to formal dispute settlement procedures.
Nonetheless, I would like to make some observations on why the Treaty and its principles are both relevant and useful in this case. As both Russia and Ukraine recognised during the dispute, the Energy Charter does include an obligation on transit countries not to interrupt or reduce existing transit flows. More broadly, it obliges member states to take all necessary measures facilitate energy transit, consistent with the principle of freedom of transit.

What does this mean in practice? International energy flows through pipelines and grids have specific characteristics that set them apart from the usual case of goods travelling by road or by rail. For this reason, the Energy Charter member states took the decision to negotiate an additional legal instrument that would provide greater operational clarity on this key issue.

As many of you will be aware, the draft Energy Charter Transit Protocol remains to be finalised, although I feel that we have been making good progress on the outstanding issues in bilateral discussions between Russia and the European Union. I particularly welcome the fact that, following the meeting in Brussels between European Commissioner Piebalgs and Minister Khristenko at the end of February, we were able to hold constructive talks on this issue already again last Friday.

A finalised Transit Protocol would be beneficial because it would define, for the first time under international law, the obligation on owners or operators of networks to negotiate, in good faith, on access to available capacity for transit. It would also introduce more detailed provisions on the criteria used for setting transit tariffs.

It would not, however, introduce mandatory third party access to pipelines. This is a persistent misunderstanding about the Energy Charter Treaty, and so - for the avoidance of any doubt - I would just like to quote directly from an understanding that forms part of the Treaty itself: "The provisions of this Treaty do not oblige any Contracting Party to introduce mandatory third party access".

It would be highly appropriate, given the topics on the agenda for the G8, for the Transit Protocol to be finalised in the first half of 2006 - first at bilateral EU-Russia level and then with the agreement of all the Charter's member states. With political will on all sides, this is certainly a realistic goal, and this would already be a significant and lasting contribution to our common energy security.

However, conclusion of the Transit Protocol would not in itself be sufficient to allow the Treaty to reach its full potential as an instrument for energy cooperation. This is for the simple and well-known reason that the Russian Federation has not ratified the Treaty itself.

I should underline that the absence of ratification is not an obstacle to the practical and technical work of the Energy Charter Conference or of the Secretariat. Russia is a valued and active participant in Energy Charter activities, and our day-to-day cooperation is at a high level.

However, the fact that Russia applies the Treaty only on a provisional basis does have a number of disadvantages for the Energy Charter as a whole, and - I firmly believe - disadvantages for Russia itself.
The extent to which provisional application of the Energy Charter Treaty creates firm legal rights and obligations for Russia is not entirely clear under international law. Pending ratification, this question can be settled authoritatively only in the context of relevant cases brought to international arbitration. This uncertainty creates incremental risks - and costs - that are borne by energy investment projects within Russia and by Russian investments and energy flows in other Energy Charter countries. So when Russian companies approach the Secretariat and ask whether they can protect their interests under the Energy Charter Treaty, we can only provide a cautious response - reflecting the uncertainties of the situation.

Taking a broader view, the lack of ratification is perceived by Russia's partners in the Energy Charter as a lack of will to subscribe to the Treaty's rules. I appreciate the Russian position that - in practice - it complies with the Treaty, but this then begs the question that is now being asked: what are the obstacles that are hindering progress on ratification?

The last hearings in the State Duma on this issue took place in January 2001, and since that time many things have changed. The European Union has changed; Russia has changed - there is also a new Duma in place. Most importantly, however, the issue of energy security has an international profile and significance which has dramatically changed, and so has the relevance and importance of an instrument like the Energy Charter Treaty.

I have read the transcript of the 2001 Duma hearings, and while opinion was broadly favourable towards the Treaty, I well understand the concerns that were raised at this time. I feel that a number of these concerns were based on clear misunderstandings of the Treaty, and I have touched upon some of these misunderstandings already. However, there were also some substantial issues raised regarding the application of the Treaty's Article 7 on transit. This was the main reason why - at the end of the debate - the conclusion back in 2001 in relation to ratification was: 'not now, but later', and, in particular, once certain issues related to transit have been clarified or studied in more detail.

That was more than five years ago and - in the meantime - these outstanding questions have been taken up in the Charter process and in the negotiation of a Transit Protocol. That is why I am convinced that the moment defined as 'later' in 2001 is now within reach, and why I feel that 2006 is the right moment for a political signal from Russia that ratification is back on the agenda. As holders of the G8 presidency, and with energy security at the forefront of multilateral discussions, this would be a very visible and tangible demonstration of Russia's commitment to reliable energy supply, and to energy cooperation based on common principles and values.

Once again, Mr Chairman, I would like to thank you and the organisers of this Conference for the chance to participate in today's debate, and - as ever - I look forward to a productive and constructive dialogue.