Ambassadors, Distinguished Guests, I am delighted to be in Riyadh, and I would like to offer Ambassador Walther many thanks for his kind hospitality and for this invitation to deliver the 4th IEF Energy Lecture.

My intention today is to provide a perspective from the Energy Charter on issues of international energy security, and also to examine the role of the Energy Charter. Firstly, some observations on this debate:

1. Any ‘solution’ to the issue of international energy security that includes only part of the energy chain is only a partial solution. This applies both to upstream and to downstream. This is not a surprising message, but it is perhaps surprising how often it is not taken into account. The International Energy Forum is a very good venue to reinforce the need for strong dialogue on the overall balance between producers and consumers of energy, and for cooperation all along the energy value chain;

2. The reason why energy has risen up the international policy agenda is partly due to high prices, but also because there is a degree of unease about increased reliance on internationally traded energy, and a widespread sense of concern at the environmental impact of energy use. This in turn has focused attention on the ‘international rules of the game’ that apply to the energy sector, how they are implemented, and how they can be strengthened;

The debate has focused on two challenges in particular:

- Challenges stemming from the trade of energy through fixed infrastructure, with a particular concentration on the trade of natural gas through pipelines.
- Concerns about a mismatch between investment in additional capacity and energy infrastructure, on one hand, and growth in demand for energy on the other. This has reinforced the relevance of the Energy Charter as a foundation for international energy cooperation, since the Charter establishes some core disciplines protecting long-term investment and trade decisions, all along the energy value chain. The importance of the principles of the Charter was explicitly recognised by the G8 at the July 2006 Summit in St Petersburg.

The distinctive contribution of the Energy Charter is that these common principles find binding legal expression in the Treaty. I would like to examine the balance struck in the Treaty between the interests of different parties along the energy chain. There are three main elements: (i) sovereign rights over energy resources, (ii) benefits of open, transparent markets for energy (iii) principles of sustainable development.

A starting point for the Treaty is an explicit affirmation of sovereign rights over energy resources. It is for the resource owner to decide how its resources are to be
developed, at what speed, and also the extent to which foreign investors participate in this development. Since this is such an important point, and one on which the Treaty is sometimes misunderstood, I would like to refer to the Treaty’s Article 18:

This article starts with the recognition of state sovereignty and sovereign rights over energy resources, and then confirms that the Treaty does not affect in any way the rules of member states governing the system of property ownership of energy resources; it then continues:

“Each state continues to hold in particular the rights to decide the geographical areas … to be made available for exploration and development of its energy resources, the optimalisation of their recovery and the rate at which they may be depleted or otherwise exploited, to specify and enjoy any taxes, royalties and other payments payable by virtue of such exploration and exploitation, and to regulate the environmental and safety aspects of such exploration, development and reclamation… and to participate in such exploration and exploitation, inter alia, through direct participation by the government or through state enterprises.”

These are important provisions. They support the right of governments to control the rate of production and depletion of their energy resources. They also underline that a system of public ownership of oil and gas resources in the ground and after extraction is compatible with the Treaty – there is no obligation to privatise or to favour private ownership. Likewise, the Treaty does not require participating states to open up their resources to foreign investors.

What, then, does the Treaty provide?

The Treaty’s binding provisions come into play once a foreign investment has been carried out. At this stage, the investor is protected against the main non-commercial risks that can affect this investment, and in particular against the possibility of discriminatory treatment, expropriation, and the breach of individual investment contracts. In this way, once an investment has been made, countries within the Energy Charter are constrained in how they treat investors from other Energy Charter member states. These constraints are addressed with some important qualifications: expropriation, for example, is not prohibited, but – according to the Treaty – it must be accompanied by “prompt adequate and effective compensation”. However, these provisions are enforceable through the possibility for individual investors to take their host governments to international arbitration.

For investors, this protection is obviously attractive, since it offers the possibility to mitigate risk for large and complex investment projects. But what is the interest of producer states in submitting themselves to the discipline of international arbitration for their actions in relation to investors?

The main reason is that it makes the positions and promises of the host government more credible. Where a host government is seen as providing reliable protection for property and for contract, this contributes to a reduction of political risk and to an environment of confidence for investors, thereby encouraging flows of capital and technology.
Without the external discipline of access to international arbitration, the Treaty would be little more than another statement of political intention. Now, eight years after it entered into force, the Treaty has a growing and positive record of facilitating the resolution of investment disputes, and has affirmed its status as a functioning instrument of international law.

On this point, it is extremely important to recall that the provisions of the Treaty are not only applicable to upstream markets. Political risk is not confined only to one part of the energy value chain, and companies from producer countries are increasingly active on downstream markets. Through the Treaty, these companies receive the same binding protection against non-commercial risk.

I would also like to say a few words about the Treaty provisions on trade and transit.

Firstly, I would like to address one argument that is sometimes heard: that membership in OPEC is not compatible with participation in the Energy Charter Treaty. This is an occasionally complex issue, but I would like to point out that the Energy Charter provisions on trade are drawn from those of the WTO, in the most part by direct reference to the WTO rules. Eight OPEC members have already acceded to the WTO on a mutually acceptable basis. This gives solid ground for the view, that I strongly hold, that there should be no obstacle to accession by an OPEC member country to the Energy Charter Treaty.

Secondly, it is worth remembering that there is no counterpart in the WTO system for the Energy Charter provisions on sovereignty over energy resources, on investment protection, and for the specific provisions relating to energy transit. In all of these areas, the Energy Charter provides a multilateral framework that is specifically designed for the energy sector.

Taking energy transit as an example, the point of departure for the Treaty is the well-established principle of ‘freedom of transit’, but the Treaty goes further than the WTO in developing a multilateral mechanism to ensure reliable cross-border flows. The Treaty deals with the specific challenges of energy transit bound to fixed infrastructure, and is accompanied by a unique conciliation procedure in case of transit disputes.

This is an area where producer countries have a significant interest, particularly in the context of possible pipeline routes for gas export from the Middle East. In a world where international energy trade continues to grow rapidly, a framework favouring de-politicised energy transportation and reliable energy flows across national borders has strategic significance. The application of international disciplines in this area plays a positive role in promoting the stability of energy trade and markets, an objective which is of course shared by producers and consumers in the International Energy Forum.

To summarise my message, Mr Chairman, I believe that there are strong reasons for a closer association between the countries in the Middle East and the Energy Charter process. The door is open, and this is a message that I also passed to the OPEC Secretary General in Vienna two weeks ago, and also in Qatar two days ago to the Deputy Prime Minister.
What does ‘closer association’ mean in practice. First and foremost, it means using the opportunities that already exist. Many of the countries in the Middle East already have observer status with the Energy Charter; the main benefit of this status is the possible to participate in an international energy policy forum in which producers, consumers and transit countries are represented. For example, I can imagine that the ongoing debate within the Energy Charter on international pricing mechanisms for oil and gas would be of great interest to countries in this region. I would urge your attention to a study prepared by the Energy Charter on this issue that will be published in March.

Closer association does not mean detailed prescriptions on how to reform national energy markets. However, it does mean is a shared commitment to the principles that provide the foundation of the Charter – strong energy cooperation, based on sovereignty over energy resources, sustainable development, and the operation of more open and transparent international energy markets.

Ultimately it can mean a binding commitment to the only set of international ‘rules of the game’ for the energy sector, through accession to the Treaty itself. This is a road that a number of current non-members are travelling. For example, the Energy Charter Conference responded positively in November last year to a request from Pakistan to accede to the Treaty, and in recent years China, Iran, ASEAN and, most recently, Afghanistan have also taken on the status of observers.

This shows that the Energy Charter is providing convincing answers to the challenges of international energy cooperation. The Treaty and the Charter process as a whole is responding to new developments on international energy markets, by working in partnership with other international organisations and with the energy industry - represented in our Industry Advisory Panel. I am convinced that, with the support of member countries, observers and other stakeholders, Energy Charter will continue to play an essential role in promoting international energy security.