The speech of the Secretary General Amb. André Mernier

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I would like to commend the interest from the World Energy Council in the issue of energy trade rules. I found the report by Lawrence Herman interesting and thorough, and it addresses an exhaustive range of issues related to energy trade.

With increasing reliance upon internationally traded energy, the rules and disciplines that apply to energy trade are of great strategic significance. Considerations of security of supply/demand and need of investment require predictability and transparency that could be achieved most effectively through a multilateral legal framework. At the same time energy markets and trade are constantly evolving, so it is a real challenge to negotiate multilateral rules for trade in energy.

I know from personal experience how difficult it is to negotiate binding international agreements. The room for negotiation is defined by the extent to which interests overlap; this room is not always very large. This is particularly true for the energy sector, at a time when both prices and the position of energy on the political agenda are very high and the interests of the players are more and more diverse.

Since negotiating new rules is likely to be difficult, let us therefore appreciate and value what we already have. To what extent can issues pertinent to energy trade be tackled through existing rules?

The WTO rules that govern international trade are fully applicable to trade in energy and energy products. Some might argue that these rules were not specifically designed to tackle energy issues, especially those that arise when cross-border energy trade is conducted through fixed infrastructure – pipelines and grids.

In considering this question, it is important to stress that the WTO provides a very effective and elaborate framework, including for the settlement of disputes. This system is flexible enough to address major issues in most sectors, including energy. Moreover, and here I agree with the conclusion of Lawrence Herman, if the Doha Round succeeds with its existing agenda, energy trade is likely to gain, for instance, from liberalized market access terms for energy equipment, possible liberalization of energy services, and new provisions on trade facilitation.

There are however some distinctive features of the energy sector, where more energy-specific rules may be needed.

The challenges are related to the fact that a significant part of international energy trade is linked to fixed infrastructure, built specifically for the purpose of carrying hydrocarbons or electricity. This link between energy trade and fixed infrastructure puts an additional premium on two issues: the framework for investment in highly capital-intensive infrastructure projects; and the conditions for access to these networks.

The WTO has already experience with negotiating specific rules for another network industry, the – telecommunications sector. Here too, international trade may involve transmission by wires, although – by way of contrast to electricity - the fixed grid is now contestable by wireless telecommunications. While I am sure some lessons from these negotiations could be learned, the energy sector has some differences, especially with respect to security of supply and environmental concerns.

In addition, the right of transit through the territory of other states has a significant impact on cross-border trade in energy. GATT Article V establishes a general rule of freedom of transit. But energy transit - when it is linked to fixed infrastructure - is very different from transit of other goods. In addition, many of the states where energy transit problems occur are not yet WTO members.

These issues, of specific relevance to energy trade, are addressed by the ECT. As this report recognises, the Energy Charter Treaty is 'unique as a stand-alone international agreement that is specific to the energy sector'. What is distinctive about the Energy Charter Treaty?

- First of all, it is the first multilateral investment protection treaty that contains binding provisions on the protection of investment in relation specifically to the energy sector. The report is completely correct in saying that the Treaty broke new ground in this area. The ECT protects foreign investors against the main non-commercial risks such as discriminatory treatment, direct or indirect expropriation, or the breach of individual investment contracts. The investment provisions are further strengthened by the dispute settlement provisions of the ECT, covering both state to state arbitration and investor-state dispute settlement. I would not agree with the point that, because there have been relatively few cases under the ECT, the "ECT investor-State provisions appear to be less than a boon to investors". I would not wish the number of arbitration cases to be a measure of the Treaty's relevance or effectiveness. Nonetheless, it is worth remembering that 18 disputes have been brought to arbitration under the ECT. This is a strong record. Moreover, I believe that the very existence of a functioning mechanism for the resolution of disputes provides persuasive encouragement for states to observe their obligations under the Treaty.
- Secondly, the ECT integrates WTO rules with respect to energy trade and extends them to non-WTO countries that are members of the ECT. This has proved to be a useful stepping stone for countries towards the WTO, and it retains value for our constituency since a significant volume of Eurasian energy trade and transit still takes place through countries that are not yet members of the WTO.
- With respect to the strategically important issue of transit, the ECT lays down the principle of freedom of energy transit and non-discrimination, on the basis of origin, destination, ownership or pricing of energy materials and products. The Report is again completely correct in saying that the Treaty's transit provisions are much more detailed and concrete than those in the GATT. For instance, in the event of a transit dispute, the ECT establishes the principle that transit flows should not be disrupted, and provides for a unique

conciliation procedure. Moreover, the ECT stipulates non-impediment for building new capacity, in case transit cannot be carried out through existing capacity. As many of you will know, we have also been engaged in strengthening these transit provisions through the negotiation of an additional Transit Protocol. We have reached a large measure of consensus on the text of this additional instrument. It has not yet been possible to agree the last 5%, underlining the point that I made at the start of these remarks – that reaching agreement on any new rules in the energy sector is a very significant challenge.

- A key actor in these negotiations is the Russian Federation (a country which has played a far more constructive role in these discussions than is often appreciated). On the issue of Russia, I would not agree entirely with the opinion of the author when he states that 'Russia is not a party to the ECT, leaving a large gap in the fabric'. Well, the fabric is not in quite such poor shape as he thinks. Russia signed the Treaty and applies it on a provisional basis. While lawyers can argue about what this means in practice, it represents a considerable degree of commitment to the binding provisions of the Treaty.
- I would also differ with the characterisation in the report of the current ECT as a European Treaty. The challenges addressed by the ECT are broader than just Europe, and while the European Community was the founding father of the Energy Charter, it has always been a Euro-Asian initiative. This Euro-Asian characteristic is demonstrated by the strong role of Central Asian countries, and Japan and Mongolia in the process, and by the growing interest in the Charter process in Southern Asia.
- I would also like to mention what the ECT does not do – in order to correct some misconceptions that might exist: the ECT does not determine the structure of national energy markets, nor does it dictate national energy policies or oblige member countries to open up their energy sector to foreign investors. Each member state is free to decide how, and to what extent, its national and sovereign energy resources will be developed, and also the extent to which it will open its energy sector to foreign investments. Lastly, it does not impose mandatory third-party access to energy infrastructure.

You can argue about whether this framework is as complete as it could be, and whether article X could have been improved with some re-drafting, or whether provision Y really reflects the intentions of the negotiators, but it is – at the very least – a functioning instrument of international law.

The key issue to remember is the need for a balance between interests of different stakeholders. This is difficult to achieve. A necessary condition for reaching this consensus, and an area where the Charter process contributes, is the dialogue between different groups of players: consuming, producing, transit countries at all stages of economic development. From this point of view the ECT has a distinctive role – no other energy-related organisation provides common platform for the development and implementation of binding disciplines among these different groups of stakeholders.

But the aim of the report and of our discussion today is to “provide suggestions for a focused work program for WEC on legal rules applicable to international energy trade”. So, despite the challenges, what about the possibility for new disciplines for the energy sector? Here I would like to make the following, concluding remarks:

- A starting point must be to look at the principles and interests that are shared by countries along the energy value chain, including both producers and consumers. As well as the generalised principles of the international trading system, the St Petersburg and Heiligendamm G8 Conclusions are a good place to look. These are close in spirit and in substance to the principles underpinning the ECT – in fact they specifically endorse the Energy Charter principles as a basis for international energy cooperation.
- Efforts to regulate the international energy sector in the same way as any other internationally traded commodity are likely to face difficulties. Energy is different, because in the case of hydrocarbons we are dealing with finite non-renewable resources that are: a) vital to our modern way of life and b) under the sovereign control of a relatively small (and ever smaller) number of resource-owning countries.This means that there is an irreducible political and strategic component to international energy trade.
- The report rightly recognised that “in addressing trade-related rules in the energy sector, some politically sensitive areas are likely to be encountered, including questions of State sovereignty over natural resources.” The principle of sovereignty over energy resources is enshrined in the Energy Charter Treaty. Decisions on depletion policy, that is, on whether and how fast national resources are to be developed, are matters for resource-owning governments. International regulation is unlikely to succeed if it tries to encroach in a binding way on these national prerogatives. This was in fact the experience during the preceding rounds of trade negotiations. Resource-owning countries objected on several occasions to the creation of trade rules affecting ownership over natural resources. In the current WTO negotiations, more specifically, during services negotiations, a number of countries made it clear that the access to, and use of, natural resources as well as the right to regulate should remain outside the scope of negotiations.
- Nonetheless, there are undoubtedly issues that need clarification because they did not come into play when the existing international framework was negotiated. The report makes constructive and useful proposals as to the priority issues in the energy sector that need further clarification, and here the WEC can make a valuable contribution. One aspect is linked to environmental implications of energy use. What is the interface between trade rules and domestic policies on climate change and the environment? For instance, in the context of growing interest in the development of new sources of energy, a debate has emerged as to whether, in the trade system, a different sub-set of rules and disciplines should apply to renewable energies such as solar, wind and bioenergy. This debate has critical implications for renewable energy and climate change policies that are being developed in a large number of countries.

In my view, the WEC could make a valuable and practical contribution in analysing the interface between the existing rules for energy trade and some of the new challenges that we see on international energy markets. On behalf of the Energy Charter, I can only say that we would greatly welcome the opportunity for further dialogue with the WEC and its members on this topic.