

7th Asia Gas Partnership Summit 2012

Session III: Gas transportation and Distribution

The Energy Charter Treaty Provisions on Transit and Open Access Systems under Multiple Ownership

Speech by ECS Senior Adviser Patrick Larkin

Excellencies, Distinguished delegates, Ladies and Gentlemen,

It is a great honour to be here in New Delhi for this very prestigious and significant event, the 7th Asia Gas Partnership Summit 2012. I have travelled from Brussels, in Belgium, as the representative of the Energy Charter Secretariat. My role is Senior Adviser to the Secretary General, Ambassador Urban Rusnák, who took office on 1 January of this year.

I would first like to thank GAIL (India) and the Federation of Indian Chambers of Commerce and Industry (FICCI) for the invitation to the Energy Charter. The opportunity to speak and present at this conference is very much valued and appreciated. I would like also to express such thanks on behalf of the Secretary General, Amb. Rusnák, and his great regret that he is unable to be here himself.

I am aware that at previous Summits, there have been presentations on the Energy Charter by other of my colleagues, including the previous Secretary General, Amb. Mernier, in 2010. I, therefore, do not intend to spend too much time explaining again what the Energy Charter is.

I am however very pleased to say that India recently has been giving careful consideration to the Energy Charter. Back in Brussels, we in the Energy Charter Secretariat have been working in close cooperation with the Indian Embassy, on the question of India becoming an Observer to the Energy Charter Conference by signing the 1991 Energy Charter, about which I hope to explain later.

Today here in New Delhi, before the representative of major international oil and gas companies of the region, I have a great challenge. I hope to persuade you of the benefits of the Energy Charter, particularly of the potential benefits for the issues of transit and open access. I hope to discuss how the proposed TAPI project (*Turkmenistan-Pakistan-Afghanistan-India pipeline*), already mentioned in this session, might benefit from the international legal framework offered by the Energy Charter Treaty provisions on transit and open access.

I first need to briefly explain, or perhaps remind you, of what I mean precisely by (a) the Energy Charter and (b) the Energy Charter Treaty. The Energy Charter Treaty was developed on the basis of the 1991 Energy Charter. Whereas the Charter was drawn up as a declaration of political intent to promote energy cooperation, the Energy Charter Treaty is a legally-binding multilateral instrument and part of international law.

The legal framework of the Energy Charter Treaty provides some principles on the role of governments in facilitating international cooperation in the energy field and in addressing non-commercial risks. The Treaty provisions include common rules on investment promotion and protection, and on trade and transit.

The Energy Charter Treaty actually entered into force in 1998. It applies today in 46 countries of Eurasia, including the European Union and all its 27 member states, and also in Turkey, Ukraine, Japan, countries of the southern Caucasus, the Central Asian Republics, and most critically in the light of this discussion, Turkmenistan.

Turkmenistan has been a prominent member of the Energy Charter Treaty constituency from the early days. Turkmenistan was one of the first countries to sign the Treaty in 1994, and has been actively involved in all Charter activities ever since. The country participates in the decision-making processes, hosts Charter-related events and shares its valuable experience in the various Groups of the Charter Conference. Turkmenistan's involvement and commitment to the Treaty is very much appreciated. It is a long-standing and productive relationship which has proved to be mutually beneficial for Turkmenistan, the Energy Charter constituency as a whole, and the entire Energy Charter Process.

In common with all members of the Energy Charter Treaty, Turkmenistan has subscribed to certain core principles: national sovereignty over energy resources, respect for contract and property rights, stable and open frameworks for flows of energy, capital, technology and investment. All of this is inspired by an orientation towards market solutions, among them – non-discrimination, transparency, energy efficiency and sustainable development. The other countries of relevance to the TAPI project are of course Afghanistan and Pakistan.

Afghanistan has been an Observer to the Energy Charter Conference since signing the Energy Charter in 2006. The Energy Charter Secretariat and the government of Afghanistan cooperated in the preparation of the Accession Reports in 2007. In December 2007, the Energy Charter Conference approved those Accession Reports and invited the government of Afghanistan to accede to the Energy Charter Treaty and Related Documents. It is very much hoped that this process will be completed.

Pakistan likewise has been an Observer to the Energy Charter Conference since signing the Energy Charter in 2005. The Energy Charter Secretariat and the government of Pakistan cooperated in the preparation of the Accession Reports in 2006. In November 2006, the Energy Charter Conference approved those Accession Reports and invited the government of Pakistan to accede to the Energy Charter Treaty and Related Documents. It is also hoped that this process will soon be completed.

There are many more countries in Asia and also in North Africa who are interested in joining the Treaty, or entering into closer cooperation. Among these are countries that are already actively engaged in Turkmenistan, such as China. China is an observer to the Energy Charter Conference, but has not at this point signed the Energy Charter political declaration.

Should India deem signature of the Energy Charter to be an appropriate step, it would be entitled to participate in activities of the Energy Charter, most relevantly in negotiations on Protocols and Declarations authorised by the Charter Conference. Furthermore, signature of the Charter would be very much welcomed as a step towards the eventual full involvement of India in the Energy Charter Process.

What does the Energy Charter offer? I will focus on two issues that are of particular importance in the context of TAPI: investment protection and energy transit.

It is clear that implementation of the ambitious TAPI project would require massive foreign investment. Turkmenistan has already taken steps to reach out to foreign partners and to

reform the energy sector and to improve regulation. The continuation of that policy, and not least its full membership of the Energy Charter increases its attractiveness for foreign investors.

The Energy Charter Treaty is designed to provide a reliable and stable interface between investment and the host government. Investors are of course concerned about the political and legal protection of their investments. That protection is one of the key provisions of the Energy Charter Treaty.

The Treaty protects foreign investors against non-commercial risks such as discriminatory treatment, direct or indirect expropriation, or the breach of individual investment contracts. The need for stability in the relationship between investors and host governments is particularly acute in the energy sector, where projects tend to be long-term and highly capital-intensive. The Energy Charter Treaty provides investors with the possibility to protect their rights by taking the host government to international arbitration. In practice this would be a last resort. What is significant is that the existence of these provisions increases mutual confidence and thus contributes to the overall favourable investment climate of the country. Investment protection is available to those companies that come from countries that are Contracting Parties of the Energy Charter Treaty (Contracting Parties means those states who have signed and ratified, or acceded to the Treaty).

The second set of the Treaty's provisions of particular relevance is on transit.

Transit is a major issue. It is so for China and the EU as energy consuming regions. It is at the core of the TAPI project.

Before the entry into force of the ECT in 1998, the international rules applicable to transit were those included in Article V of the GATT, which enshrines the principle of non-discrimination towards goods in transit. In the specific context of energy transit, those rules were further developed through the Energy Charter Treaty. The transit provisions of the Treaty build upon the non-discrimination principle embodied in Article V of GATT and develop that principle further in respect of fixed infrastructure such as pipelines and grids. The aim of these provisions, included in Article 7 of the Treaty, is to provide for a balance between the sovereign interests of States and the need for security and stability of transit.

Under those provisions of the Treaty, the Contracting Parties shall facilitate transit of energy consistent with the principle of freedom of transit. Contracting Parties' national provisions shall treat transit of energy no less favourably than energy originating in or destined for their own markets. Obstacles shall not be placed to the creation of new capacity in energy transport facilities, and established cross-border flows shall be secured. In the event of disputes over any matter arising from transit, the Treaty provides for a designated conciliation procedure. Furthermore, and importantly in view of the further development of infrastructure, the Contracting Parties commit themselves to encourage cooperation to modernise, develop and operate Energy Transport Facilities and to facilitate their interconnection and to mitigate the effects of interruptions in the supply.

The important new element in the Treaty is its explicit coverage of grid-bound energy transport and the enforceability of its provisions. A number of countries that previously did not participate in any international transit arrangements now have, through the ECT, access to a set of multilaterally accepted rules which can be used to protect their interests. Turkmenistan is a particular example because of its stated aim to diversify export routes.

Meanwhile energy consuming countries such as India and those of the European Union may achieve diversification of supply and enhanced energy security.

The Treaty definition of “transport facilities” through which transit takes place, includes inter alia “High-pressure gas transmission pipelines”.

Under the Treaty, measures to facilitate transit are to be taken without distinction as to origin, destination or ownership of energy, or discrimination as to pricing, and without imposing unreasonable delays, restrictions or charges. This means that countries may not refuse transit, or refuse to agree to the construction of a new pipeline or network capacity, solely on the basis of the origin, destination or ownership of the energy. The Treaty does not provide for mandatory third party access.

Article 7 of the Energy Charter Treaty already represents the most detailed set of multilateral legal obligations in existence dealing specifically with energy transit flows. Nonetheless, following the Treaty’s entering into force in 1998, a consensus emerged among Energy Charter member governments that the Treaty’s existing rules in this area needed to be further strengthened and developed.

Negotiations on a Transit Protocol have already been underway for a number of years. These negotiations have focused on particular issues such as utilisation of available capacity for transit, common principles for tariffs and non-discriminatory rules for expansion and creation of new capacity as well as technical standards.

However, it is not a secret that the negotiations on the proposed Protocol have had great difficulties. Such difficulties were mainly rooted in the different regulatory regimes in place in the European Union, a major player in the ECT constituency as opposed to some countries in the eastern part of the constituency, such as Russian and Kazakhstan. One solution therefore might be a less ambitious document with a lower level of detail agreed by a broader constituency. At the moment consideration is being given to a reset of negotiations which might cover cross border aspects as well as focussing on electricity.

Secretary General Rusnák has stated that it is now the right time to make every effort to pursue such a Protocol, and to address these important transit challenges. The Secretary General argues that the Charter has taken the correct approach in balancing the interests of producer, consumer and transit states under a single legal framework. If a reliable common framework were in place at this stage, there would be no need for expensive bypass pipelines. He has emphasised that the Energy Charter is available as a multilateral framework to address emergency situations with regard to energy supply.

A very important point in the context of TAPI is that those countries who have Observer Status to the Conference, achieved by signing the 1991 Energy Charter have the entitlement to participate in negotiations on Energy Charter Protocols and Declarations authorised by the Charter Conference. Turkmenistan is already fully entitled to do so as are both Afghanistan and Pakistan as Observers to the Conference.

Transit arrangements for the TAPI project are vital. Each of Turkmenistan, Afghanistan, Pakistan, and India, should it decide to sign the Charter, now have a great opportunity to participate in those Protocol negotiations. Moreover new ideas from new players would be welcome.

Given the type of energy projects being envisaged in India and in South Asia, the Energy Charter Secretariat is ready and willing to share the experience gained from long years of close cooperation with our member states.

There is one final issue of relevance that I would like to touch on. That is the proposed Modernisation of the Energy Charter.

The constituency of the Energy Charter is located mostly on the Eurasian continent, at least at this point in time. Here, the Russian Federation and the European Union are the major players. There is an important synergy between the EU and Russia, which is longstanding, stable and profoundly beneficial on both economic and political levels. The European Union has other gas suppliers, such as Norway and Algeria, maybe Iraq in the future. Russia also has export markets other than Europe, such as China and the North-East Asia region. However, none of those markets is mature enough to absorb significant volumes comparable to those of the European Union.

Russia has clearly indicated its desire to modernise the existing Energy Charter. In December 2010 the Russian delegation presented a “Draft Convention on Ensuring International Energy Security”. This Russian proposal was carefully analysed and enabled us to be clearer as to what Russia has in mind by way of change, though it remains to be seen how it will be achieved. The suggestions were consistent with the intention of other ECT member states to recognise the changes, which had come about in the energy sector, reflected just a month earlier in the Road Map for Modernisation as adopted by the Energy Charter Conference. Furthermore, the member states agreed that the Energy Charter was the appropriate tool with which to make progress on this issue.

An important and relevant component of the Road Map for Modernisation is work on a new strategy for expansion. India’s engagement with the Charter would do much to enhance the standing of the Charter. It would be for the mutual benefit of India and the existing constituency.

Modernisation is the most important endeavour of the Energy Charter for the immediate future. The Treaty signatories now have an excellent opportunity to discuss the substance of the Modernisation process and its implementation. Moreover, in the Energy Charter Secretariat this process is also open for observer countries. This is a point of particular relevance for India as it gives consideration to signing the Charter.

There is a clear road map for the way forward, and an important task to be completed. Active participation of the Energy Charter constituency will result in a positive outcome of this exercise. The ECT would thus become attractive to an even greater number of countries. This would be part of the public service that the Energy Charter Secretariat can provide to strengthen common energy policy.

In short I argue that India now has a very significant opportunity to participate in this important exercise and to shape the future direction of the Energy Charter and perhaps even the direction of global energy governance. That is in addition to benefits that involvement with the Energy Charter might bring to the important TAPI project.