

Session 40: International governance of energy trade: WTO and Energy Charter Treaty (ECT)

Sub-theme II: Trade in natural resources

Moderator

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Organized by

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Abstract

The distinctive features of energy raise the question of whether energy trade and investment can be effectively regulated by a general international legal framework or whether a more specialized framework is needed.

The aim of the session was to discuss ways of addressing challenges related to energy trade, taking into consideration the distinctive features of energy commodities. The session focused on the international regulation of energy trade by WTO Agreements and the Energy Charter Treaty (ECT), and provided an opportunity to discuss complementarities between the general WTO framework and the more specialized ECT framework, which is based on the WTO framework but contains additional rules relevant for the energy sector. The ECT is applicable for energy trade with and among ECT states that are still outside the WTO.

1. Presentations by the panellists

(a) H.E. Mr. André Mernier, Secretary General of the Energy Charter Secretariat

The present trends towards tighter supply to energy markets and the emergence of new consumers require a reliable framework for trade and investment in oil and gas.

The WTO rules that govern international trade are applicable to trade in energy and energy products. There is a perception that WTO rules entail a bias towards market access and do not sufficiently address the issues of export restrictions and investment protection, commonly regarded as the most crucial challenges in oil and gas trade. Trade-restrictive practices related to energy are mainly found on the exports side, and the multilateral trade rules were devised to address import barriers to a larger extent than export barriers.

The most important 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. The right of transit through the territory of other states has a significant impact on cross-border trade in energy.

These issues are of specific relevance to energy trade and are addressed by the ECT, the only energy-specific multilateral agreement that covers all major aspects of international energy turnover, including trade, transit, investment and energy efficiency. ECT binding provisions are strengthened by dispute settlement, covering both state-to-state arbitration and investor-state dispute settlement. The ECT provides useful value added to the existing general WTO framework, which covers a much larger constituency. The investment framework and more elaborate transit rules are features of the ECT that have not been negotiated in a detailed manner within the WTO. The cornerstone of the ECT is non-derogation from the WTO. The ECT incorporates WTO rules on energy trade and extends them to non-WTO ECT countries. The ECT and WTO frameworks complement each other, creating synergies without unnecessary duplications.

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 ECT. Decisions on depletion

policy are matters for resource-owning governments. International regulation is unlikely to succeed if it tries to encroach on these national prerogatives.

(b) Professor Gabrielle Marceau, Counsellor, Legal Division, WTO

WTO rules apply to trade in energy and include non-discrimination principles, such as national treatment and most-favoured nation (MFN) principles, and prohibition of quantitative restrictions under Article XI. There are numerous questions as to how exactly these general principles and rules can be applied to trade in natural resources and, in particular, to energy. Several WTO dispute issues have arisen on the application of existing general WTO rules and these could have ramifications for the energy trade.

The main goal of the WTO is to prohibit protectionism. In the energy trade, export restrictions represent a more important concern than import barriers.

Disciplines on state trading are important in the area of energy, given that the sector is dominated by large state-controlled enterprises. The General Agreement on Tariffs and Trade (GATT) Article XVII provides little guidance on the issue, as it only says that state trading enterprises (STEs) should behave commercially.

The energy sector is heavily subsidized, therefore the disciplines on subsidies are also very important. It is unclear how subsidies given to public enterprises should be dealt with compared to those given to private ones. Different rules apply to energy subsidies because some energy products are considered industrial and are regulated by the WTO Subsidies and Countervailing Measures (SCM) Agreement, while other energy products are considered to be governed by the Agreement on Agriculture.

Moreover, it is important to think about the ramifications of regional trade agreements (RTAs) for energy trade. How can RTAs allow for positive discrimination and rules on freedom of transit? It is unclear whether GATT Article XXIV can serve as justification for the violation of the freedom of transit enshrined in Article V.

With respect to the general system of preferences (GSP), the Appellate Body has said that preferences can be conditioned on criteria that are development-related. How can it be distinguished whether these criteria are development-related or linked to self-interest? For instance, can a donor give preferences to developing countries on the condition that they pursue certain energy-related policies?

Another difficulty lies in having rules on energy in accession protocols, meaning that members are treated differently depending on the terms of their accession. It is difficult to deal within the multilateral system with countries that have different obligations. It would be much better if the applicable rules were harmonized.

Finally, it is unclear how the WTO would deal with disputes between two WTO members who also participate in other agreements on energy, such as the ECT, which has more detailed rules on issues such as energy transit.

In conclusion, WTO members need to deal with these issues to make sure that rules are applied correctly and new rules created if needed. Civil and academic society also needs to reflect on these issues.

(c) Professor Thomas Cottier, Managing Director of the World Trade Institute and the Institute of European and International Economic Law

The issues related to energy trade have not been the focus of GATT and WTO debate because many oil-producing countries are not part of the organization. Studies indicate that the energy industry shows no real WTO awareness. One reason that the energy debate has recently received attention in the trade forum is due to the implications of energy production for climate change.

The reduction of greenhouse gases depends on the increased use of renewables and energy efficiency. This raises the question of how to create incentives in research on renewable energy and what the WTO should do about this. With respect to subsidies, 90 per cent of energy subsidies benefit non-renewable energy sources, but need to be reduced if climate change is to be mitigated. Existing WTO disciplines do not distinguish between subsidies for renewable and non-renewable energy sources. Should we review subsidies rules, reviving non-actionable subsidies and research and development subsidies?

The development of renewable sources of energy means there would be an increase of cross-border trade over long distances. This raises the question of security of transport and transit. Should we move towards special rules on transit or enhance existing WTO rules?

For dealing with energy trade at a multilateral level, are special rules or general rules more effective? There are strong arguments in favour of special rules. Energy requires an integrated approach:

- All forms of energy should, in principle, be subject to the same rules and conditions of competition.
- The production and transmission of energy is a complex operation, often involving both goods and services.
- It also entails technology and is affected by intellectual property rights.
- The sector shows a high level of governmental involvement, necessitating coherent rules on competition and government procurement.

Recourse to a framework convention implies that its provisions may refer to pertinent provisions of other agreements of the WTO. These may also incorporate provisions of agreements outside the scope of the WTO, as the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) did for the Paris and Berne Conventions on industrial property and copyright. Alternatively, they could allow references to other provisions without incorporating them, for example to the ECT, to a future and revised UNFCCC, or to the Kyoto Protocol. Both reference and incorporation allow the building of a comprehensive and coherent agreement on energy within the WTO subject to binding dispute settlement.

(d) Professor Peter Cameron, Director of the Centre for Energy, Petroleum and Mineral Law and Policy; Professor of International Energy Law at the University of Dundee

Energy is different from other products: in the case of hydrocarbons we are dealing with finite non-renewable resources. These resources have historically been of strategic significance for all states, although in different ways, depending on whether a particular state is a net importer or exporter of energy. Policies on resource depletion have traditionally been viewed as sovereign matters of resource-owning countries. The principle of sovereignty over natural resources is expressed in Article 18 of the ECT.

The principal challenge linked to energy trade is the one of reconciling different interests between consuming and producing states. For consumers, availability of energy supplies is important. Energy supply security is a significant challenge for areas like China, the EU and the United States. On the supply side, resource nationalism has been associated with the development of energy resources.

The second challenge relates to the growing role of the state in the energy sector. This phenomenon is evident in the rise of national energy companies. Ninety per cent of the world's oil reserves and 70 per cent of production are controlled by governments. A similar percentage of government involvement is observed in infrastructure systems. These systems are said to be highly inefficient (with exceptions of companies like Statoil). It is important for states to rely on international frameworks. The ECT has been particularly relevant to disputes between investors and states.

The third challenge is linked to the dynamic character of energy. This is illustrated by new discoveries in the Arctic and Brazil and the development of new technologies for energy exploration and development. Consequently, more countries are involved in exploitation and extraction of energy.

The final challenge is linked to the sustainability of energy production and use, linked to oil spills, adverse effects on climate change, violations of human rights, transparency and corruption.

How is one to respond to these challenges? The non-legal role of international organizations has potential to set out common ground for dialogue. The WTO's *World Trade Report 2010* on trade in natural resources and organization of this session are both developments in the right direction. International organizations should contribute more to the debate. Cooperation between the WTO and ECT is desirable.

2. Questions and comments by the audience

Most of the discussion centred around the question of the feasibility of negotiating effective international legally binding disciplines on energy. Most commentators questioned the incentives for producing countries to adhere to such disciplines.

Whereas the WTO fosters market access, energy trade barriers are linked to difficulties in access to supplies. Energy-producing countries therefore have much more leverage than consuming countries.

Several comments cast doubt on the feasibility of reaching consensus on energy-specific rules within the multilateral framework, given the differences in the interests of consuming and producing countries. However, it was pointed out that there are already energy-producing countries in the WTO, and some proposals in the current negotiations have addressed issues related to energy. Among these were issues related to transit, energy services and liberalization of environmental goods and services.

As to the question of incentives for the energy-producing countries, it was pointed out that up to 75 per cent of the export earnings of some energy-producing states come from energy exports, which leads to the conclusion of a certain dependence of producing states on supplying external markets.

Regarding the possibility of negotiating more specific multilateral rules on energy, it was pointed out that, during previous rounds of trade negotiations, consensus had seemed to be impossible on a number of issues, and yet agreements were finally reached. A proposition was made to integrate the ECT disciplines into the WTO framework in the form of a plurilateral agreement.

Issues of interest for many energy-producing countries include technology. Moreover many energy companies from energy-producing states are becoming more interested in investing abroad. The perception of investment rules by producing states may be changing. Since, with the development of renewable energy sources, demand on fossil fuels may decline, the position of energy-producing countries may also change.

The development of renewable energy sources has faced difficulties due to extensive subsidies for fossil fuels. However, many subsidies for renewable energy, such as feed-in tariffs, are inefficient and insufficient. More support should be given to the research and development of new low-carbon technologies.

3. Conclusions

Energy trade is different from trade in manufactured products. In addressing trade-related rules in the energy sector, politically sensitive areas are likely to be encountered, including questions about state sovereignty over natural resources. Despite clear interdependence, the interests of energy-consuming and -producing countries differ significantly and this makes the negotiation of international binding rules covering energy very difficult.

While rules contained in WTO Agreements cover trade in energy products, they are not designed to tackle problems that arise in the field of energy trade. While the WTO protects market access, problems in energy trade are related to access to supplies rather than market access. Investment, and possibly competition rules, are needed. While the WTO does not have an investment framework, the ECT provides additional value added. The investment framework and transit rules are valuable features of the ECT that have not been negotiated in a detailed manner within the WTO. The ECT incorporates WTO rules with respect to energy trade and extends them to non-WTO countries that are members of the ECT. Cooperation between the two organizations should be fostered.