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# Oil, Gas & Energy Law Intelligence

## A New Energy Charter: Myth or Reality? by A.V. Belyi and S. Nappert

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## **A New Energy Charter: Myth or Reality?**

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*23 April 2009*

Since the January 2009 gas crisis, top-level Russian officials have been suggesting that the Energy Charter Treaty should be reviewed. The Treaty was signed in 1994, but never ratified, by Russia. Russian gas giant Gazprom repeatedly invoked the Treaty's incompatibility with its own interests and often claimed that it should be amended. One of the main dilemmas for Gazprom has always been the question of transit: how to ensure a reliable gas transit through Belarus and Ukraine on the one hand, while preserving a monopoly on the gas transit from Central Asia on the other?<sup>1</sup>

The ECT transit provisions were unclear for Gazprom: issues concerned tariffs for transit, the dispute settlement mechanism, as well as the right of first refusal for long-term supply contracts. In order to clarify these and other issues, Russia and the EU started negotiating a Transit Protocol, which is still not adopted despite some nine years of off-and-on negotiations.

In the aftermath of the latest gas crisis in January 2009, the need for a gas transit regime became clear for all involved. At the same time, Gazprom experts and Russian political officials claimed the ECT to be next-to-useless for gas transit disputes. Gazprom consistently refused to use the conciliation dispute settlement mechanism provided in Article 7(7) of the ECT.<sup>2</sup>

In response, European capitals urged Moscow to ratify the ECT in order to enable Russia to defend its transit interests vis-à-vis Ukraine. It should be

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1 J. Stern, *Future of Russian gas and Gazprom*, OIES, 2004, pp. 179-183.

2 A. Belyi, and U. Klaus, Dispute Resolution Mechanisms in Energy Transit - Missed opportunities for Gazprom or false hopes in Europe?, *Journal of Energy and Natural Resources Law*, 2007, Vol 25 (3), pp. 7-26.

pointed out that Russia applies the Treaty provisionally (in accordance with the Article 45 of the Treaty) and hence arguably could invoke the dispute settlement mechanism.<sup>3</sup> Consequently, the reason for Russia's refusal of the ECT dispute settlement mechanism appears not to lie so much in its non-ratification of the ECT, as in its political unwillingness to accept an «EU-sponsored Treaty». Moreover, Ukraine never invoked the ECT transit dispute settlement mechanisms during the crisis. Consequently, it constituted a basis for a new proposal of the Energy Charter reforms.

A few weeks after the January crisis, President D. Medvedev proposed a «new Energy Charter». In his 1st March 2009 interview for the Spanish newspaper El País, President Medvedev pointed out that Europe needed a new Energy Charter, focused not only on consumers but also on producers and transit countries. On 20 April, President Medvedev tabled «an alternative» to the ECT, entitled Conceptual Approach to the New Legal Framework for Energy Cooperation.<sup>4</sup> Broadly-worded and in the form of a statement of principle at this stage, it includes many principles and practices which have been previously stated by the UN, the IEA and even the ECT itself: sovereignty over natural resources, ensuring non-discriminatory access to the markets, transparency, access to technologies, exchange of information etc.

In many terms, the Russian energy doctrine repeats positions previously defended by Moscow:

- the agreement should be universal and open to agreement by any country;
- the agreement should cover all energy sectors, including oil, gas, nuclear, renewables and power trade;
- it should not conflict with other international agreements; and
- it should aim at being an effective crisis management mechanism.

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3 On the effect of provisional application of the ECT, see S. Nappert, 'Russia and the Energy Charter Treaty: The Unplumbed Depths of Provisional Application', 2008, OGEL 3, <http://www.ogel.org>. There may be other strategic factors underpinning Russia's reluctance to rely on the ECT's dispute resolution provisions, notably a concern that invoking provisional application of the ECT in certain circumstances would be inconsistent with claiming overall that Russia will not ratify the ECT in its present form.

4 Also available at the OGEL Legal & Regulatory database, <http://www.ogel.org/legal-and-regulatory-detail.asp?key=3212>

Interestingly enough, the new conception introduces the idea of the non-discrimination at the pre-investment phase: «non-discriminatory investment promotion and protection, including *new investments* into all energy chains». The issue of pre-investment protection was already the subject of international negotiations in 1994, before ECT signature. Then, the text of Article 10 of the Treaty iterated a protection at the post-investment phase. Non-discrimination at the pre-investment phase re-emerged in 1998 when a Multilateral Investment Treaty was proposed. It was however aborted and the pre-investment phase issue became a subject of politically-agreed reciprocity rather than an impartial legal regime.<sup>5</sup> Russia reintroduced the issue ten years later but, unfortunately, the current proposal does not elaborate further on this topic.

Perhaps not surprisingly, transit provisions are the main focus of the Russian proposal. Indeed, since the beginning of the Energy Charter process, Russia has been suggesting that the ECT transit provisions needed clarification, hence the Transit Protocol negotiations, ongoing since 2000.

During those negotiations, Russia expressed concern about a possible mismatch between transit and supply agreements and therefore proposed a «right of first refusal» clause for transit contracts. In addition, Gazprom (as well as Naftogaz of Ukraine) often requested clarification of the conciliation dispute settlement mechanisms in Article 7(7). Mainly, the gas companies were worried about the provision allowing the conciliator to fix interim tariffs pending resolution of the dispute. This is mainly a political, and not only a legal, issue. Interestingly, the new Russian proposal appears to cast conciliation aside in transit disputes in favour of an UNCITRAL arbitration clause in the event of failure of diplomatic channels. It basically proposes to reform the dispute settlement mechanism of the Article 7(7).

The overall legal framework of the proposal, however, remains unclear: should the proposal be the subject of a particular EU-Russia agreement? Or

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<sup>5</sup> Detailed analysis of the EU-Russia energy investment reciprocity is proposed by A. Belyi, 'Reciprocity as a factor of the energy investment regimes in the EU-Russia energy relations', forthcoming July 2009 in *Journal for World Energy Law and Business*.

should it completely replace the ECT? Neither of these two options seems readily possible to implement.<sup>6</sup> A new EU-Russia agreement would require 29 separate ratifications, which would be hard to obtain in the current EU-Russia political climate. A «new ECT» is even harder to achieve. EU Member States will certainly resist an attempt to redefine the 1994 text. There is no doubt that Russian officials understand that opposition to the modification of the ECT will be met in Europe.

It may be that the 'new' proposal, rather than looking at practical implementation in the short term, represents Russia's willingness to portray itself as a constructive partner on the international energy scene, ready to participate in international norm creation. Politically, the proposal appears to aim at counter-balancing the EU's influence in the international energy regime and is a request that the interests of Russia, as a world leader in energy resources, be acknowledged and counted. It will be interesting to see how the EU and the ECT Secretariat, who is considering the quinquennial review of the ECT pursuant to its Article 34(7), respond to the Russian proposal.

*Moscow and London, 23 April 2009.*

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<sup>6</sup> A. Konoplyanik, 'A common Russia-EU energy space: the new EU-Russia partnership agreement, *acquis communautaires* and the Energy Charter', *Journal of Energy and Natural Resources Law*, 2009, Vol 27 (2), pp. 258-291.