

WTO and energy

60 years ago, when the rules of the GATT were negotiated, world energy demand was a fraction of what it is today and so were energy prices.¹ While energy has always been a crucial factor in geopolitics, at that time liberalising trade in energy was not a political priority. The industry was largely dominated by state run monopolies and thus governed by strict territorial allocation. International trade in energy resources and products was heavily concentrated, cartelised and controlled by a few multinational companies. This explains why the rules of the General Agreement on Tariffs and Trade (GATT), and now the World Trade Organization (WTO), do not deal with energy as a distinct sector.

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Also, no special agreement on trade in energy has emerged in any of the sectorial agreements that have been drawn up since the Kennedy Round. Yet since basic WTO rules are applicable to all forms of trade, they also apply to trade in energy goods and services.

- Certain features of the energy sector make it different from other industries in many ways.
- First, energy goods have peculiar physical characteristics, which influence means of storage,
- transportation and distribution. Then, particular challenges are associated with the existence
- of natural monopolies, as well as with the role of state-owned enterprises that dominate some
- national energy markets. Furthermore, in the Uruguay Round, WTO Members tried but did
- not manage to address effectively the practice of using dual energy prices and export
- restrictions.⁴ They also undertook very limited commitments to grant access to their energy
- markets to foreign service operators.

In recent years, energy topics have reappeared on the negotiations agenda. There are several reasons for this:

- Several energy-exporting countries have recently joined the WTO and others are currently negotiating their accession⁵, hence, a substantially larger amount of energy trade is now in the hands of WTO Members trade.
- Increasing energy needs have led to a growing interest in competition rules and export restriction practices.
- Progressive unbundling of vertically integrated state-owned entities offers a way for private operators to enter energy markets.
- The relationship of trade and the environment and the debate on sustainable development is strongly bound to energy. The correlations between trade, energy and climate change and the role of biofuels are also bringing attention to the trade in energy under multilateral trade regulation.

Energy has been discussed in the ongoing Doha negotiations. For the first time, Members have been discussing energy as a specific services sector.⁷ Energy issues motivate discussions on export taxes and export restrictions on raw materials. Another aspect of the ongoing round of negotiations is a balance between promotion of environmental goods and services and fossil fuel subsidies. Finally, the energy related negotiations in the current round are focusing on biofuels. When dealing with biofuels there is a need for a balance between climate change and energy security concerns, and their impact on agriculture in order to avoid creating new environmental problems.

B. The current status of energy in WTO Law (oil, gas, coal and electricity)

Traditionally, the energy industry has not distinguished between energy goods and energy-related services. This is because energy services were perceived as a value added to energy goods which could not be dealt with separately. Privatisation and liberalisation of the sector led to market reform which resulted in a conceptual separation of goods and services trade. Hence, the need for a clear legal framework to address this distinction emerged.

Oil and solid fuels such as coal clearly fall within the category of goods; they are easily stored and traded across borders. Crude oil is treated as a global commodity and has been traded internationally since the 1860s. Trade in crude oil represents the key link between the two poles of the industry: upstream and downstream, and crude oil prices give signals to both.⁸

The same applies to natural gas. It is traded across borders via pipelines and although it can be stored in its gaseous form, it is increasingly being liquefied for the purposes of transportation to remote regions and for storage.

It is commonly understood that under the WTO rules, production of energy goods comes within the scope of the General Agreement on Tariffs and Trade (GATT), while energyrelated services, including transmission and distribution, fall under the scope of the General Agreement on Trade in Services (GATS).

- *II. Electricity*

Modern society and production methods are inconceivable without electricity. It is a secondary energy source which results from the conversion of primary sources of energy, such as coal, natural gas, oil, nuclear power, wind and solar energy. Unlike oil and gas it is not a physical substance that can be stored easily. Electricity is a physical process which takes place throughout the cables that carry it and it has to be generated more or less at the same time as it is being used.

- Its value
- chain consists of four activities: *generation* which converts energy sources into electricity,
- *transmission* which occurs when electricity is transmitted over high voltage networks to major
- demand centres; *distribution* which is the process by which transmitted power flows to the
- final consumers such as factories and homes; and *supply* – the name given to the metering,
- billing and other services provided to the final consumers

The WTO law does not contain any specific provisions on electricity. Given the lack of disciplines on services under GATT 1947, electricity was defined as a good irrespective of its peculiar physical properties.

Accordingly, electrical energy qualifies as a good under WTO law and is, as such, subject to the rules of the GATT 1994. The same is true for the European Energy Charter and European Community law. Until the end of the 1980s, EC law hardly ever intervened in the organisation of electricity utilities. Although two of the three founding treaties of the EC were specifically directed at regulating energy, electricity was not dealt with explicitly by any of the three Treaties. Thus, for a long time, it remained uncertain whether the provisions of the EC Treaty applied to electricity. It was only in the 'Almelo' case in 1994¹⁵ that the European Court of Justice (ECJ) explicitly recognised that the rules on the free circulation of goods of the EC Treaty also applied to electricity.

III. WTO and other instruments of international energy law

- WTO law is only a minor fraction of international law addressing energy. A wide range of sources and instruments need to be taken into account. Also, it should be recalled that international trade in energy is mainly based upon contracts subject to international private law and commercial arbitration.

Energy issues around the world today are dealt with in a fragmented manner and some of the energy-specific agreements and institutions are described below.

1. Organisation for Economic Co-operation and Development (OECD)/International Energy Agency (IEA)

OECD is an international organisation, established in 1961, with 30 member countries and a budget of 342.9 million euros (as of 2008). The OECD's affiliate organisation, the IEA is a forum for coordinating the energy policies of 28 industrialised countries. The IEA, which addresses all types of energy sources has the following objectives: "improvement of the world energy supply and demand structure, more efficient use of energy, development of alternative energy sources to reduce dependence on any one source, assistance in the integration of environmental and energy policies and the promotion of cooperative relations between oilproducing and oil-consuming countries"

2. Energy Charter Treaty

The Energy Charter Treaty entered into force in 1998; however ratification by some Members is still pending. Several of the WTO Members engage in energy cooperation under this treaty. The ECT covers various issues related to investments and investor relations. The main elements of the ECT include: 'investment protection (e.g. by granting investors nondiscriminatory treatment – national treatment and most-favoured nation treatment – compensation in case of expropriation and other losses, free transfer of capital); trade in energy, energy products and energy related equipment, based on the WTO rules; freedom of energy transit; international dispute settlement, including investor-state arbitration and interstate arbitration; promotion of energy efficiency, and attempts to minimise the environmental impact of energy production and use'.

3. Organization of the Petroleum Exporting Countries

OPEC is a permanent intergovernmental organisation, currently consisting of twelve oil producing and exporting countries, spread across three continents: America, Asia and Africa. The main goal of OPEC is the coordination and unification of the petroleum policies of its Member Countries, working out ways and means of ensuring the stabilisation of prices in international oil markets with due regard being given to the interests of the producing nations and to the necessity of securing a steady income to the producing countries; an efficient, economic and regular supply of petroleum to consuming nations; and a fair return on capital to those investing in the petroleum industry. When OPEC was founded on 14 September 1960, none of its five founding members was a contracting party to the GATT.

This picture has been changing recently

- 4. Multilateral environmental agreements

Energy is also addressed by a number of multilateral environmental agreements (MEAs), in particular those relating to climate change, including the United Nations Framework Convention on Climate Change (UNFCCC) and its Kyoto Protocol. Anthropogenic climate change affects the energy sector and threatens the foundations of energy security systems.

At the same time, climate change mitigation measures catalyse energy efficiency and motivate energy sustainability policies. Recognising this fact, the climate regime avoided the approach adopted by a number of earlier MEAs which require parties to those agreements to use trade restrictive rules against non-parties to the agreements

- Regional Level: European Union (EU) and North American Free Trade Agreement (NAFTA)

The European Community (EC) has evolved since the European Coal and Steel Community (ECSC) Treaty of 1952 which covered an energy policy for coal. The ECSC did not address external relations. Indeed, the six initial member states were free to shape their relations with third countries. In 1957, two other fundamental treaties were signed: the Euratom and the European Economic Community. In 1967, the Merger Treaty allowed for the unification of the institutions of these Communities, covering all the main economic activities, including the rational use of natural resources. At an international level, the EC is active within the international organisations. Being a full member, alongside its Member States, of the WTO, the Energy Charter Treaty, and the Kyoto Protocol, the EC has attempted to establish the leadership in promoting international norms of energy trade.

Implementation of NAFTA began on 1 January 1994. The objective of the agreement was to remove trade barriers between the United States, Canada and Mexico. NAFTA covers various issues related to energy trade, including investment, cross-border services, measures related to trade in energy services, limitations and barriers and measures related to investments in the territories of the parties as well as cross-border trade

IV. Role of government procurement

- Government procurement (GP) is the purchase by a government of the goods and services needed to perform its functions. It is an area of international trade that was previously carved out of the non-discrimination obligations. The Agreement on Government Procurement (GPA) imposes the national treatment and most-favoured nation (MFN) obligations, but it binds only those WTO Members that subscribe to it. Energy efficient GP was identified by the IPCC as a possible policy tool to address climate change. Accordingly, countries began implementing 'green' public procurement as a part of their policy package for climate change.
- In terms of its size, government procurement represents up to 18% of the gross domestic product (GDP) in the OECD countries and, in the EU for instance, it amounts to 10–25% of GDP.³¹ This percentage may well be higher in the case of developing countries. GP apparently plays a major role in promoting the use of environmentally friendly products and
- motivates the market for climate-friendly technology

V. Unresolved and controversial issues

- The interface of trade and climate change mitigation and adaptation is at the heart of contemporary legal developments in energy law. This was the subject of the World Trade Forum Conference in 2007 at which the different angles were extensively addressed. Yet, the challenges of climate change are merely the tip of the iceberg of unresolved and controversial issues relating to the status of energy in international law. The picture is one of fragmentation with multiple instruments involved. The bulk of regulation comes under domestic law and the role of regional and global law in addressing energy and secure production and supplies has remained unclear and unsettled. Doctrines of multilayered governance have hardly been applied to the sector.

- The fundamental divide between goods and services does not offer an appropriate basis for
- addressing and regulating energy in an integrated manner in domestic and international law.
- Electricity is a case in point. It is traditionally treated as a good, but in fact, by its nature and
- its dependence upon grids, it is much more like a service, or perhaps a mixture of both. There
- is no clear perception of defining energy in terms of goods and services, and services relating
- to energy are not properly defined under GATS.

Different and competing forms of energy are therefore subject to strongly divergent international rules, depending on whether they qualify as a good or a service. The same applies to the operation of trade remedies, in particular because of the absence of disciplines on subsidies in services. Moreover, existing disciplines on subsidies in goods may not be suitable to address a distinction between renewable and non-renewable energy under GATT and the Agreement on Subsidies and Countervailing Measures (ASCM). The Agreement on

Agriculture again offers different disciplines. It thus makes a fundamental difference whether a product is classified as an industrial or an agricultural product.

- There are also unresolved and basic issues related to competition policy and thus about the
- relationship of WTO law and OPEC as a producer organisation. The crucial question is
- whether oil exporters, when they join the WTO, will still be able to support oil prices through
- the regulation of oil production, or whether they could face challenges on the basis of
- GATT/WTO rules and provisions.³² This leads to the question of whether additional WTO
- rules on competition are required to properly address the relationship between trade and
- production in the energy sector.

The international trading in energy resources and its associated services has always posed special problems, and classification of energy services has been one of the topics of debate among various interest groups. The energy sector has traditionally been dominated by state owned companies or has been under the direct control of the national government. This situation has resulted in endless negotiations on the classification of energy services and neither the WTO's 'Services Sectoral Classification List' (W/120)³⁶ nor the United Nations Provisional Central Product Classification (UNCPC)³⁷ lists energy services as separate categories. Clarifying classification issues is an important precondition to successful negotiations on energy.

- Currently, some of the energy-related products and services are listed under different
- headings. One is 'transportation of fuel' described in the CPC as 'transportation via pipeline
- of crude or refined petroleum and petroleum products and of natural gas'.³⁸ This comes under the broad category of transport services, which is not strictly appropriate. Transportation of
- energy-related products and services requires very specific and technically complicated
- procedures. Concerns regarding safety and security are always associated with it. Classifying
- the energy services sector under a separate category would simplify the process for regulation
- of transmission and transportation of energy products and services.

- The upstream activities for oil and gas fall under the category of 'Other Business Services'. It
- is 'services incidental to mining' described as 'services rendered on a fee or contract basis at
- oil and gas fields, e.g. drilling services, derrick building, repair and dismantling services, oil
- and gas well casings cementing services'³⁹. At the same time, the services essential to the
- energy industry such as oil and gas field exploration and geological surveying services are not
- covered by this category, but are classified as 'Geological, geophysical and other scientific
- prospecting services',⁴⁰ under 'Engineering related scientific and technical consulting
- services'.⁴¹ Such a classification does not provide a clear view or complete information in one
- place and may therefore lead to confusion in commitments.

- The third energy-specific entry relates to: ‘Services Incidental to Energy Distribution’⁴², listed under ‘Other Business Services’ category. It refers to ‘transmission and distribution services on a fee or contract basis of electricity, gaseous fuels and steam and hot water to household, industrial, commercial and other users