

The Central Asian Countries and the Energy Sector: Economics, Politics and Legal Aspects

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Abstract

This paper is written with aim of investigating the importance of the natural resources within the Central Asian energy sector. The geopolitics position of the Central Asian Countries place them in the centre of conflicting powers; that is to say, on the one hand they are providing energy to Europe and USA, and on the other hand they are next to China, which has the highest and growing demand for energy consumption. In political arena, China accordingly seeks to prevent the independence of East Turkistan, which has historical links to Turkistan (West) in Russia. In this regard, we examine the energy policies and trade between states, and we particularly focus on the gas and oil pipelines from said countries to Europe. We also examine the demand from Caucasian and the Central Asian Countries by European, and Pacific Countries and, as well as, the USA. Correspondingly, we discuss the political conflicts upon the energy investments, and mainly concentrate on the investments in Central Asian and Commonwealth of Independent States ("CIS"), and the political risks and legal disputes relating to foreign energy investment and stability implications in this regard.

JEL codes: Q51, C78, Q43

1 Introduction:

Growing demand for energy in next decades has highlighted the resources of energy in various parts of the world. Demand for energy resources is going to increase in the future within China, India and other Emerging Economies such as Africa, the Middle East and Africa. (BP Energy Outlook, 2030). Importance of oil and gas supplying countries lead international securities concerns towards them. Since the fall of Soviet Union, there had been struggle of Russia to win back the regimes of the Central Asian Countries, such as Kazakhstan and Kirgizstan and Uzbekistan. Russia managed to assert her dominance over these countries due to the economic structure she had established in the past. Europe in the West, China and India in the East would be competing for Gas and Oil supplies from Russia and the Central Asian Countries and Azerbaijan. The importance of Central Asian energy sector is related to its geopolitical position finding themselves in the middle of conflicting political interests. On the one hand, the Central Asian Countries are providing energy to Europe and, on the other hand, they are closed to China with high growth rate which is expected to acquire the highest percentage of World's energy consumption.. However, Russia has economic and political power over the Central Asian Countries. Thus, the security of energy supply has become an important concern for European powers, since Russia cut off its gas supply to Ukraine for four days on Jan1, 2006 due to particular political reasons (Develi et al. 2010). A year later, Belarusian oil supply was also cut off by Russia. The long lasting cut-off was in 2009 that created the second Russian-Ukrainian Gas Crisis. Though European Union does not have a single definition of solidarity, the EU and its members are distinguished from other international organizations with their fundamental values (Turksen and Wojcik, 2012). The world gas consumption is projected to increase more than twice over the next three decades, rising from 23 to 28 percent of world total primary energy demand by 2030. This implies that gas production is exceeding coal production as number two energy source of the world. Furthermore, gas is potentially overtaking oil's share in many large industrialized economies. Energy security, especially in the Central Asia will become very important (Böckstiegel et al., 2012). We also observe that many Universities in UK and USA providing degrees in energy securities in the Department of International Relations and the Law Departments are dealing with various disputes (Olcott, 2004). Kazakhstan is argued to be in a better possession than Azerbaijan as she took lessons from the experience of Azerbaijan. Secondly, Kazakhstan has more diversified mineral resources than Azerbaijan. Azerbaijan will be able to export over 7 bn cm of gas annually. The capacity of the Hajibul-Mozdok pipeline connecting Azerbaijan and Russia will be total 7 bn cm annually. On January 2010 Azerbaijan started gas exports to Russia and Russia imported 799 mm cm of Azerbaijani gas in 2010. Since 2000 the following pipelines are under construction.

- a. Baku-Tbilisi-Ceyhan (BTC) went through Azerbaijan-Turkey-Georgia-Russia and Iran and carried oil, (Georgia is a just transit country, by tried to avoid Russia.
- b. Baku-Tbilisi-Erzurum (BTE) Carried Gas CPC carried oil Tengiz field from Kazakhstan has to go through Russia, since their fields are interlinked with Russian pipelines.
- d. Kazakhan-China pipeline to carry out western Kazakh oil to be refined in western China.
- e. Trans-Afghan pipeline.
- f. The Nabuco pipeline aims to carry gas to Europe. There are considerations to avoid crossing certain countries in order to ensure security. Both Russia and Georgia act as transit countries. The greatest threat to these

energy supplying countries comes from Russia. There are ethnic Russians in Caspian region and 40 per cent of the total population, especially in Kazakhstan, protects the Russian interest. On the other hand, the largest single investment is to Kazakhstan. Caspian Pipeline Consortium (CPC) is from the USA. Russia also needs great energy supplies for her domestic market and has strong interest in the region as she is also involved in oil explorations. The Chinese interest established ‘the Shanghai Five’ including Russia, Kazakhstan, Kyrgyzstan, Tajikistan, China to counter separatist activities. This land-line supply is important for China since they do not want to rely on the Middle East energy supply where USA has strong influences. The Chinese interest become greater as Russia is also interested in the oil field of Turkistan. The European countries also depend on Russian supply energy. However, Russia does not want any other competitor as a supplier to Europe. In return, the European Union has energy interest on Russia, which is the prime energy supplier to Europe. It can be argued that Russia and the EU are interdependent in energy. Since in the future European energy production is expected to decline, and their demand is also expected to rise substantially by 2030, European dependence on Russia will be greater. The argument that Russia relies on Europe to market her energy supply is a weak one, as Russia cut-off gas supply to Ukraine in 2009. Belarusian oil supply was also cut-off (Turksen & Wick, 2012). These examples are clear signs that Russia did and can in future use their economic power to exert their political dominance.

The rest of the paper is as follows: In Section 2, we explore the total demand for energy in the world by regions and expected possible energy production in different parts of the world. Furthermore, we concentrate on the most important energy suppliers to Europe, China, and India, namely the Central Asia and Russia. In section 3, we discuss the risk management for the energy generation and legal disputes between investors and invested countries in this regard. Furthermore, the risks of legal disputes between investors and the host states also certainly lead to the rise legal disputes between states, and recently emerging threats such as environmental and human rights issues.

2 World Energy Consumption and Production

2.1 Demand for Energy by Sectors

Energy experts had highlighted the repeat growth of demand for global energy in Developing Countries. The trend in demand for energy in China and Indian also brought about competition for the energy demand from the Central Asian Countries and Russia by European Union, which is rapidly growing in countries. The sustainable energy policies are desirable for satisfying billions of people in China and India. The long-term projections are also difficult due to uncertainties.

	1990	2030
Renewables*	0.4	6.3
Nuclear	5.6	6.0
Hydroelectric	6.0	6.8
Coal	27.3	27.7
Natural gas	21.8	25.9
Oil	38.9	27.2

*Renewable energy includes biofuels

Table 1 Share of Fuel 1990-2030

Table 1 reports the world total fuel shares in 1990 and estimated figure for 2030. The expectation is to increase the efficiency of fuel consumption and lead to usage of multi energy sources, rather than depending on only one source, coal and oil as it was in 20th century. In the future, there will be decline in demand for oil from 38.9 to 27 per cent and very small increase in demand for coal. The rest of the categories will be increasing as well. The renewable energy, which includes sun and wind energy will be increasing to 6.3 percent in 2030 from 0.4 percent in 1990. Nuclear will increase from 5.6 to 6.0 percent, and hydraulic will also increase from 6.0 to 6.6 percent.

The energy consumption is expected to become billion tons of oil equivalent by 2030. In absolute terms the order of the energy kinds according to the quantity are as follows: liquid, coal, gas, hydroelectric, nuclear power consumption. Especially coal and gas have the highest growth in energy demand due to China's demand for coal, as shown in the Table 2 reporting the regional distribution of the energy supply and demand in 1990, 2010 and 2030 projections. The Table 3 reports the changing (decreasing or increasing) of World Energy Demand and Supply by 2030 based on 2010 figures. The Asian Pacific energy demand is expected to increase 63 percent, while supply is expected to increase only 53 percent. In all the other regions supply increase is more than the demand. This shows how the Asian Pacific Countries rely on imported energy and highlights the importance of the Central Asian Countries as well as Russia in satisfying China's demand for energy.

	1990	2010	2030
World Energy Demand	15907.5	18992.4	23849.7
world Energy Supply	14270.5	19739.5	26092.1
North America Demand	1747.2	2004.1	1915.3
North America Supply	2160.4	2424.4	2856.7
Asian Pacific Demand	1645.8	4063.0	6635.3
Asian Pacific Supply	1441.6	3766.4	5754.7
South & Central America	271.9	479.0	703.4
S&C America Supply	782.3	1458.4	2273.8
Africa Demand	182.9	278.1	2360.0
Africa Supply	440.5	650.4	1146.0
Middle East Demand	178.1	525.0	575.0
Middle East Supply	946.0	1603.3	2495.0
European & Eurasian Dem	2313.3	1949.0	2066.7
European and Eurasian Supply	5516.7	5406.0	5855.9

Table 2 Energy Demand and Supply by Region.s All energy is measured in million tons of oil equivalents.
Source: BP Energy Outlook

	Change of Energy Demand	Change of Energy Supply
North America	96	118
Asian Pacific	163	153
South America	147	156
Africa	157	176
Middle East	110	151
Europe& Eurasia	106	108

Table 3 Expected Change of Energy Demand and Supply for 2010-2030, by regions *Source: BP Energy Outlook*

2.2 Energy Consumption by Region

All energy is measured in million tons of oil equivalents. The natural gas is the second largest consumption after the liquid in North America. However, gas and renewable energy consumption will be increasing and liquid and coal consumption will be decreasing in future (Marşap et al. 2010). Demand for energy in the Asian Pacific region is mainly coal and gas. So, gas, from the Central Asia is a very important resource for the rapidly growing Chinese economy. Coal and gas are also increasing the energy demand in South and Central America. In Africa, the liquid energy consumption is ahead of coal consumption, which is different from the Asia Pasic Countries. However, gas consumption is expected to exceed the coal consumption. Petrol and gas consumption is also expected to increase in the Middle East. The most drastic structural change is expected to take place is in Europe and the Eurasian Countries, where both in absolute term and also in total share; petrol consumption is expected to reduce and gas is expected to increase. The share of renewable energy will also increase (BP Energy Outlook 2030).

2.3 Energy Production by Region

In 1990s, oil production was more than other energy production. Recently in 2010, gas exceeded oil and coal production. However, in shares of total production in the North American, oil and gas are expected to increase from 24 to 29 and from 28 to 34 percent respectively. In Asian Pacific, coal production will increase in absolute term but is expected to reduce from 70 to 60 percent in its share. This is due to the large size of China. Their demand is expected to be met by imports, mainly from Russia and the Central Asian Countries. The South and the Central America have been and is expected to increase its renewable energy production, which should be an example to the rest of the world for sustainable growth and environment. Therefore, the nuclear energy production is negligible. The order of energy importance in this region are the oil, hydroelectric and gas. The percentage of total production in biofuel and gas production are expected to increase in the total energy production and the renewable energy, which is also sustainable. In Africa oil, gas and coal production is expected to increase, but the share of oil production will reduce from 70 to 40 percent and gas production will increase

from 10 to 30 percent. In the Middle East, both gas and oil production is also to increase in total but in percentage there will not be any change. Oil will be 70 and gas will be 30 percent of their production. Europe and the Eurasian oil production will also be partly replaced by nuclear energy (BP Energy Outlook 2030). Table 2 also shows the supply of total energy by various regions. It is noticeable that the supply in Asian Pacific is less than the demand. The gap is expected to be supplied by Russia and the Central Asian countries. Turkistan already has commenced to provide gas via Turkistan-Uzbekistan- Kazakhstan-China gas pipelines (Alexander's gas and oil connections, 2012). Table 3 also shows the expected change in supply in various regions by 2030 based on 2010.

3 Threats and Legal Disputes on Energy Production

3.1 Foreign energy investments, political risk, emerging threats and investment stability: risk management of foreign investments through legal means

The energy produced from natural resources, whether in the form of oil, gas or coal, is the major source of the economic growth, and nation states are almost always the owner of these resources. As reported by the Organization of the Petroleum Exporting Countries (OPEC) oil, gas and solids (e.g. coal) are the most important sources of energy and will be same in the future as well. States, either directly or indirectly, play an important role in the regulation and operation of these resources as the economic welfare of a country is closely related with that. Although there is no single definition of an energy investment, for the purpose of this paper, the most suitable definition can be procured through the Energy Charter Treaty ("ECT") which states in Article 1(5) and 6 that *'the energy investments covers any investment involved in an economic activity in the energy sector in order to explore, extract, refine, product, store, transport, transmit, distribute, trade, marketing, or selling of energy materials and products'*.

The nation states with rich natural resources, in general, lack the necessary capital and expertise needed for the development of such resources. Hence, they seek to attract foreign investors with the necessary capital and expertise to invest in their territories by offering investor friendly policies and royalties. Like the other forms of foreign direct investments, energy investments are also subject to both commercial and political risks. In summary, these are the risks of credit, completion, operation, production and sales, expert-dependency, transfer of profits, natural calamities, change of government and taking of assets (Chatterjee, 1996). Nevertheless, energy investments are much more vulnerable to political risks than any other investment type due to the special state sensitivity upon the natural resources and interrelating economic welfares. Another reason of the excessive vulnerability is concerned with the physical characteristic of the energy projects that are usually immobile and require creation of stationary infrastructures. This means that once the investment is made, the production facilities are practically incapable of being removed to another place.

Cameron (2010) explains the long-term instability of an energy investment on two bases, which are 'the obsolescing bargain' and 'the price cycle'. In respect to the former, the guarantees and encouragements offered to a foreign investor by a host state through formal agreements are in danger of being altered after the bulk some of investment is made. While a host state receives what it requires (i.e. capital, shares) once the investment is made, an investor needs longer periods to achieve a profitable return. Due to this reason, the contribution of risk moves from the capital-hungry host state to the investor after the early stages of the investment, since the host state might decide that the existing contractual terms are no longer sensible or up to date, and might accordingly force the amendment of contractual obligations. Other possible reasons are usually related to the change of governments or policies and complaints about the tariffs or pricing regimes of energy resources (e.g. gas, oil, electricity). All these unilateral and sovereign state acts usually result in reducing the investment value or loses in benefits and use of the investment, rather than the outright taking of assets through an expropriation or nationalization. On the other hand, 'the price cycle' is based on the macro-economic developments that are related to the international market conditions. In particular scenarios, the investor gains unexpected large sum of profits when the international price of the invested natural resource rises, and the host state usually seeks to acquire shares from investor's unexpected profits by increasing the tax tariffs or forcing a renegotiation over the existing contractual terms. The great example of this scenario can be seen through the experiences gained after the 2000s crisis; such as in Latin America and Central Asia.

The following part of the paper examines the foreign energy investments made particularly in Central Asian and Commonwealth of Independent States ("CIS") and the obstacles, i.e. political risk, environmental and human rights issues, standing on the way of investment stability. These states are distinctive in each other either by having significant domestic quantities of fossil fuels and energy sources (e.g. Russia, Kazakhstan, Turkmenistan and Azerbaijan) or having significant geographical position providing economic advantages growing from the transit of energy across their territories (e.g. Ukraine, Belarus and Moldova plays an important role for the transit oil and gas crossing from Russia to EU). On the other hand, some of the Central Asian States such as Kyrgyzstan and Uzbekistan nevertheless lack the geographical advantage as they sometimes referred to be landlocked and far from the larger markets which is also unattractive for foreign investors. In respect to the states around the Caspian Sea area, it is observed that the reserves of fossil fuels had to face a numerous of legal

and political barriers to be developed. The attitudes of foreign investors have proved that, although the incentives offered by host states to foreign investors influence the investors to invest, such incentives are not necessarily the only fact affecting them as the geographical position and a market-oriented legal framework of a host state might even be more effective than such incentives.

3.2 Types of International Energy Agreements (“IEAs”)

The types of investment contracts between the host states and foreign investors should be examined for a clear understanding of the disputes. These well-known investment contracts are namely the Oil/Gas Exploration and Production Agreements, Gas Sales and Transportation Agreements and Infrastructure Projects.

Particularly, Oil/Gas Exploration and Production Agreements comprise the Production Sharing Agreements (PSAs), the Licences/Concessions and the Risk Service Agreements. Although each of them is state-sanctioned and constitutes a completely different sort of governance, they can also be used in a hybrid manner. The PSAs are the most common IEA types within the whole international petroleum industry, and designed to provide a product sharing between an international oil company (IOC) and a host state or a national oil company (NOC). By signing this agreement, the foreign investor provides the capital and expertise (e.g. labour, skill, technology etc.) for the development of petroleum resources in the contracted region. Although all expenses and costs of the development belong to the investor, the host party holds the title of oil and gas. The PSAs also set the sharing scale between the contracting parties. On the other hand, Concessions grant specific mineral rights to foreign investors in respect to the exploration and exploitation. Conversely to the PSAs, these rights are exclusive, and investors own title of the produced oil and right to dispose. At the same time, investors are obliged to supply the oil to the state's local market. Moreover, IOCs are subject to income tax and royalty unless exempted by a contractual clause. As in PSAs, the licensee supplies the required equipment and installations for the development of the petroleum resources. Finally, by means of the risk service agreements, the host state or NOC hires the foreign investor for the exploration and development of services. Conversely to the concessions, although the investors provide the capital and expertise, the host parties do not offer any mineral or mining rights.

By means of Gas Sales and Transportation Agreements, the foreign investor guarantees the supply of service, and the host state shares the development risks. They have around twenty-five years of duration and cover long-term sale and purchase between producers and buyers. As the duration is very long, the contractors usually seek to include special provisions for the review of terms in regular intervals or after an unexpected policy change in the market. Conversely to the international oil industry, renegotiations of terms are usually conducted in a moderate manner due to the willingness of parties to continue their contractual relationship. Since the natural gas is transported either through pipelines or as liquefied (the LNG form), the state-owned/controlled companies (e.g. Gazprom) usually provide the pipeline networks. This imposes a special political character upon such agreement types that are so called the ‘state-to-state’ agreement. Conversely to the oil industry, the gas market also lacks internationally recognized trading price. Therefore, the contracting parties usually seek to negotiate the price of gas according to a specific formula provided under separate agreements.

Finally, infrastructure projects are usually being designed for the infrastructure of electricity, water, telecommunications and transport through the grant of concessions by a host state or municipality. Among all other investment types that were explained above, the infrastructure investments are considerably the most vulnerable ones to the political risks. Examples were present in 1990s where the host states were changing their policy in the electricity sector. During these years, many legal mechanisms were developed in order to challenge this risk, for example through ‘power purchase agreements’, ‘build-own-operate’ and ‘build-own-transfer’ approaches.

3.3 Today's ‘Political Risk’: Indirect Expropriation

The term ‘political risk’ covers broad range of risks including wars, takings, unilateral change of contractual terms, currency transfers and sabotages. However, the risk of takings comes above all as it is the most frequently experienced unilateral state action. Taking over of foreign investments by host states are divided into three categories, which are the expropriation, nationalization and confiscation. Confiscation refers to ‘the seizure of private property by the government without compensation to the owner, often as a consequence of conviction for crime, or because possession or use of the property was contrary to law’ (Garner, 2004). Regarding the other two taking types, Ingram's view suggests that an expropriation occurs when one or several properties within a single area of economic activity are taken, whereas nationalization occurs when a government takes all properties within the area (Ingram, 1974). Moreover, expropriation can either be outright or indirect. In this context, an outright expropriation occurs when the foreign investor completely loses the legal title and benefits of the investment; whereas under an indirect expropriation the investor holds the legal title of the property but the measures taken by the host state deprives the owner of the substantial benefits or use of the property. These measures are commonly seen where a state adopts a new legislative regime, which usually ends up with a revocation of license, increase on the formerly agreed tax rates, forced renegotiations of contractual terms etc. As a result of such measures, the foreign investor, who previously relied upon the favourable legislative regime of

the host state before investing such sum of capital, faces the economical disadvantages which in most scenarios results with holding the formal title of the investment while losing the possession and control of it. In modern times, it is observed that states are more reluctant to perform an outright expropriation as it adversely affects states' international reputation and reduces the possibility of future foreign investments in their territories.

The sections below reflect the examples of indirect expropriation experienced in Central Asian Countries.

Russia:

In the early 1990s, Russian government president Yeltsin was keen to attract foreign investors into the development of oil and gas sector. In those years, the government issued a Presidential Decree awarding of Production Sharing Agreements ("PSA") which in following years even committed a law on PSAs. The PSAs were only the legal guarantees besides Foreign Investment Law adopted in 1991 and other investor-friendly legislative regimes causing the rise of foreign investments, such as the Presidential Decree transforming Gazprom into a joint stock company in 1992. Nevertheless, following the election of Vladimir Putin in 2000 as President, the new Russian government adopted a restrictive approach with respect to foreign investments within the oil and gas industry. Particularly the 2003 Energy Strategy of the Russian Federation clearly stated that "Regardless of whose property the natural resources and in particular the mineral resources might be, the state has the right to regulate the process of their development and use" (Putin, 2006). Putin's 2003 Energy Strategy was officially transformed into a government decree. This was followed by the nationalization of the major Russian oil company, Yukos; enhancement of Gazprom's control over strategic development of the country's gas supply in East Siberia and the Russian Far East; though later ratified, attempts to refuse ratification of the Energy Charter Treaty which offers protective standards to foreign investors whose home-state is a member of the treaty. Following the new Russian regime, foreign investors encouraged by the state authorities to renegotiate their existing investment contracts by alleging the failures to perform contractual or license obligations or environmental abuses. The great examples can be seen through the renegotiations of Sakhalin I, Sakhalin II and Kharyaga PSA. However, it should be noted that unlike many other host states which performed unilateral actions by means of measures taken following the 2000s crises, none of the Russian pressures of renegotiations lead to the initiation of arbitral proceedings.

Kazakhstan:

Similar to the Russian attempts in 1990s, Kazakhstan had also initiated various range of legal guarantees for investment stability which were respected for many years. Foreign Investment Law, Tax Code, Petroleum Law and Subsoil Law were some examples of incentives offered by the state in 1990s. Behind its favourable legislative regime, unlikely to Russia, it was really willing to sign and ratify the ETC, and to conclude bilateral investment agreements (BITs) with foreign investor's host states (Cameron, 2010). However, together with the adoption of the "Kazakhstan 2030" in 1997 which was aimed to establish a long-term development programme extending national interests, the state reverted its investor-friendly legislative policy into a more nationalist approach. In this regard, the establishment of the vertically integrated state oil and gas company (Kazmunaigaz/KMG) by a Decree in 2002 is an example of the aim of protecting the state interest in such projects. The series of unilateral state measures were more apparent following the legislative changes in 2003. Firstly, the Foreign Investment Law and Tax Code were replaced by restrictive approaches. In 2005, the Suboil Law and Law on Petroleum were both amended in a significant amount and a new law on PSAs limiting such agreements to offshore territory was also introduced. All these measures had affected the guarantees previously offered to the foreign investors and this ended up with a growing number of disputes between the state authorities and investors with regards to the conduct of their operations. In contrast to the Russian approach of renegotiations, it was observed that Kazakhstan conducted more coercive renegotiations together with the adoption of restrictive unilateral actions and the use of environmental law by the state to impose pressure on investors during these negotiations. It is argued that the previous incentives offered by Kazakhstan to foreign investors were much more effective than the ones which Russia had offered (Cameron, 2010). Consequently this causes the legitimate expectation of foreign investors to be more effective than the foreign investors in Russia, thus results with a growing number of legal challenges both before local courts and arbitral tribunals. The most well-known of these disputes is the Kashagan dispute. By alleging the environmental violations in 2007, Kazakh state authorities threatened to revoke the license held by a foreign consortium for a very large offshore oil field at Kashagan in the north Caspian Sea. The consortium was led by the Italian company Agip and included Shell, ExxonMobil, ConocoPhillips Total, Inpex (Japan) and KazMunaigaz (KMKG) and the Kazakh National Oil Company ("NOC"). The dispute was concerned with the allegations that the death of large numbers of rare seals was caused by the project in concern. Following the challenges, in 2003, the British Gas decided to sell its interest in this project to two Chinese companies. Besides to the environmental concerns, there were other concerns with the project such as delays in the commencing date and the production. In 2007, Agip informed the government that the project would not be commenced until 2010 and the cost of first phase amounted to 19 billion USD. The government refused to accept this new plan and budget for the project and required a discussion over the contractual terms. Moreover, it was alleged by the state that the delays caused to a change to the terms of the 1997 PSA and they were allowed to receive more favorable terms and an increase of profit from

10 percent to 40. The state unilaterally decided that the negotiations shall be concluded in 2 months following its commencement in August. From the analysis of the reports, it was observed that the characteristics of these negotiations were quite coercive in nature and marked a considerable success for the host state. Consequently, a new operator entity called North Caspian Operating Company was established and the Agip lost its role as operator. However, none of the investors chose to file a case neither through contract-based dispute nor treaty-based dispute (in other words investment arbitration) despite the fact that Kazakhstan ratified the ECT, concluded various BITs between home states of these foreign investors and moreover offered range of stabilization guarantees which investors relied before investing in this country.

3.4 Emerging threats: Environmental and Human Rights issues

In addition to the political risk which is inherent to the foreign investments, the recent disputes had truly proved that the stability of energy investments is also being affected by the environmental and human rights issues.

These concerns were not only brought forward by those states, which are reluctant to offer a broad application of 'freezing' provisions into IEAs, but also by the civil society organizations (CSOs) and international lending institutions which have taken initiatives to influence the conducts of companies. Accordingly, the impacts of CSOs are already apparent in the structure of various concessions. Moreover, it is seen that their activities even extend to the submission of amicus curiae briefs in arbitral tribunals, as in *Vivendi v Argentina arbitration case*. On the other hand, some initiatives by the international lending institutions such as The World Bank Group's Extractive Industries Review Reports and Environmental, Health, and Safety Guidelines (the EHS Guidelines); the Organization for Economic Cooperation and Development's (OECD's) Recommendation on Common Approaches on Environment and Officially Supported Export Credits; and the Equator Principles which had been adopted by seventy-two financial institutions in twenty-seven countries were also very important in this regard.

It is comprehensible that the welfare of societies must be protected, but the stabilization guarantees offered to foreign investors are reasonably disturbed while acquiring a balance between the interests of investors and societies. This concern especially becomes prominent in high-profile energy investments, such as Liquefied Natural Gas (LNG) projects which involve in very long-term goals and needs, since the investors of these projects seek to receive more extensive and reliable guarantees on the investment stability before investing such large sum of capitals. Yet, the sources of law regarding the social and environmental protections are mainly based on the weak principles. These are particularly the indirect interrelation of energy investment law with rules derived from international law and the 'soft law' norms comprised through a large number of influential standards and guidelines that have a non-binding character. However, the increasing pressure of third parties on non-economical concerns, which are already present in the recent energy project examples, have indeed raised 'a new source of uncertainties and parameters' in respect to the investment stability 'which are very difficult to identify with any precision at the present time' (Cameron 2010).

As stated above, the host states are keen to allege environmental issues as a reason of forced contract renegotiations. In addition to them, the current practice proves that the human rights concerns receive a number of debates which mostly related on whether the contractual stabilization instruments can restrict the activities of host states while safeguarding the interests of their societies. The present circumstances show that the scale of oppositions on the issues of human rights can be really strong, and with the involvement of third parties (particularly the CSOs or NOGs) amendments may be required in the contents of investment contracts. In this respect, the events encircling the conclusion of the BCT Cross-border Oil Pipeline Project are the great examples of the crucial interest in the relationship of stabilization clauses and human rights. The BCT project was exempted from the application of new laws through the stabilization clause included in the HGA, for a forty-year period, including the laws for protection of the environment and human rights. At the same time, the host states ensured that the investors would be financially compensated for any unilateral legislative changes. However, these exemptions induced the growth of criticism by NOGs who argue that the stringent nature of those stabilization clauses had restricted the host states power (in particular Turkey, Azerbaijan and Georgia) to enforce the obligations under international human rights law. Consequently, the contracts were adapted to cover a 'Human Rights Undertaking' and Environmental Code of Practice which have the effect of avoiding any adverse impacts of stabilization clauses on the human rights protection. After the BTC project, modification of pre-existing investment agreements aiming to limit the scope of stabilization clauses were also seen in other industries, such as The Mittal Steel investment in Liberia.

4 Conclusion

In the first two sections of this paper, we investigated the world's energy consumption and production by focusing particularly in the Central Asian Countries. The high growth countries such as China and India are relying on oil and gas energy production in the Central Asian Countries. In the future, the world economy will depend on the stability and sustainability of energy supply, which requires the risk management on the energy

sector. However, there are legal and environmental disputes that may threaten energy security. In section 3, we have focused more on the aspects of the foreign energy investments and their sensitive nature that is significantly vulnerable to the political risks called 'indirect expropriation'. In addition to this risk, we further examined the emerging threats such as environmental and human rights issues, which are expected to play more important role in the future years for foreign investors, while pursuing the stability of their investments.

It is nevertheless apparent that, once a host state decides to expropriate a foreign investment, either directly or indirectly due to the legislative policy changes, there is not possibility to prevent such actions due to the principle of state sovereignty. The Central Asian experiences showed that the foreign investors in most countries had faced forced renegotiations of the royalties and incentives afforded to them prior to investing in those countries. Although such forced renegotiations did not end up with arbitral claims as in Latin America experiences, it would not be wrong to conclude that the stability of foreign investments will remain to be under the risk of unilateral policy changes, which might always be resulted with indirect expropriation and disputes in this regard.

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