



Brussels, 14.5.2019
COM(2019) 231 final

Recommendation for a

COUNCIL DECISION

**authorising the entering into negotiations on the modernisation of
the Energy Charter Treaty**

EXPLANATORY MEMORANDUM

1. CONTEXT OF THE PROPOSAL

- **Reasons for and objectives of the proposal**

The Energy Charter Treaty ("ECT") is a plurilateral trade and investment agreement applicable to the energy sector. It was signed by the EU in December 1994 and entered into force for the EU in April 1998. To date the ECT has been acceded to by fifty-two states, as well as the EU and EURATOM. The EU Member States¹ represent roughly a half of the Energy Charter Conference membership as well as of the Contracting Parties to the ECT.

The ECT was originally set up as a framework for international cooperation between European countries and other industrialised countries with the aim of developing the energy potential of Central and Eastern European countries and of ensuring the security of energy supply for the EU.

The key provisions of the Treaty concern the protection of investment, trade in energy materials and products, transit and dispute settlement.

Since the 1990s (most of) the ECT provisions have not been revised. This became particularly problematic in the context of the ECT provisions on the protection of investment, which do not correspond to modern standards as reflected in the EU's reformed approach on investment protection. Those outdated provisions are no longer sustainable or adequate for the current challenges; yet it is today the most litigated investment agreement in the world².

In the view of growing legal and political concerns about the ECT, the Energy Charter Secretariat proposed a modernisation of the ECT. In preparation of the modernisation, the ECT Contracting Parties submitted ideas for topics: the EU's position was to modernise the investment protection standards; other Contracting Parties supported the inclusion of provisions such as transit, provisions related to dispute resolution, regional economic integration organisation ('REIO') or pre-investment. Taking advantage of the process, the Energy Charter Secretariat suggested addressing the issue of obsolete provisions.

The list of topics for modernisation was approved on 27 November 2018 by the Energy Charter Ministerial Conference and covers (mainly) investment protection provisions and related definitions, pre-investment protection, transit, REIO, provisions related to dispute resolution and obsolete ECT provisions.

- **Consistency with existing policy provisions in the policy area**

This recommendation (to enter the negotiations on the ECT modernisation) forms part of the EU reformed approach to investment as presented following the entry into force of the Lisbon Treaty³ and further developed in the 2015' Commission Communication on 'Trade for all'⁴.

¹ As of 1 January 2016 Italy has withdrawn from the Treaty; maintaining a status of Observer to the Energy Charter Conference. The voting rules provide that where the matter falls under EU/Euratom competence, the EU/Euratom have as many votes as they count members.

² UNCTAD has recorded a total of 121 investment disputes under the ECT. As arbitration can be kept confidential (no notification requirement or transparency obligation under the ECT), the actual number will likely be higher.

³ Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions 'Towards a comprehensive European international investment policy' (COM(2010)343 final).

Since then the EU reformed approach has been promoted in a number of recently concluded or negotiated EU investment agreements with third country partners⁵.

This approach should consequently be applied in the context of plurilateral relations, such as the ECT. The recommendation mainly entails the clarification and better definition of the standards of protection for investors and investments such as (non-exhaustive list):

- Most favoured nation treatment provision, including national treatment post-establishment;
- Right to regulate;
- Fair and equitable treatment, and full protection and security;
- Expropriation, covering direct and indirect expropriation, and appropriately defined to clarify the nature of indirect expropriation;
- Umbrella clause;
- Transfers: allowing free transfers relating to an investment, together with appropriate exceptions and safeguards for financial difficulties or crises;
- Denial of benefits.

Self-standing provisions on sustainable development and corporate social responsibility, in line with the commitments undertaken in the 'Trade for all' Communication and following the example of recently concluded EU investment agreements⁶ are proposed to be included.

Given the ongoing international initiatives on the reform of dispute settlement (ICSID and MIC), the modernisation of the relevant provisions of the ECT should only be conducted once those international initiatives deliver tangible results.

One Contracting Party wished to add 'pre-investment' to the list of topics for the negotiation. The EU recorded its reservation to avoid making pre-investment subject to dispute settlement. In general, the EU views that the reasons and circumstances that did not allow for a successful conclusion of a "Supplementary Treaty" in the past, remain. Against this backdrop, pre-investment is not a priority of the EU in this modernisation round which should focus on investment protection provisions. In addition, the ECT Secretariat expressed a wish to agree on the deletion of obsolete ECT provisions in the modernisation. While this is not the EU's priority, it may increase the readability of the ECT and it could therefore be considered to delete obsolete provisions.

The 'transit' chapter of the Treaty is not fully in line with the concept of liberalised energy markets in the EU. It should be adapted to the requirements of integrated energy markets with third party access rights. It should make clear that the concept of "transit" in the ECT does not contradict the principle of open access and unrestricted exchange of gas without territorial restrictions, with energy trading being based on virtual flows and not on the exchange of physical molecules, as applied in the EU.

⁴ See http://trade.ec.europa.eu/doclib/docs/2015/october/tradoc_153846.pdf.

⁵ E.g. EU-Canada Comprehensive Economic and Trade Agreement, EU-Singapore Investment Protection Agreement, EU-Vietnam Investment Protection Agreement or EU-Mexico Global Agreement.

⁶ EU-Canada Comprehensive Economic and Trade Agreement.

- **Consistency with other Union policies**

The recommendation is fully aligned with the Union investment policy, which is a part of the common commercial policy.

It is also linked to the energy policy of the Union; however better alignment of the ECT to sustainable development, including climate change and clean energy transition goals should be reflected, to the extent that these do not expand the scope of the ECT to carry out actions that are already dealt with in other fora.

2. LEGAL BASIS, SUBSIDIARITY AND PROPORTIONALITY

- **Legal basis**

Article 207(3) and 207(4), first subparagraph, Article 194(2) and Article 218(3) and (4) of the Treaty on the Functioning of the European Union (TFEU).

- **Subsidiarity (for non-exclusive competence)**

According to Article 5(3) of the TEU, the subsidiarity principle does not apply in areas of exclusive EU competence. The common commercial policy is listed among the areas of exclusive competence of the Union in Article 3 of the TFEU. This policy includes the negotiation of the trade and investment agreements pursuant to, inter alia, Article 207 TFEU.

- **Proportionality**

In line with the principle of proportionality, entering into the negotiations on the ECT modernisation is the only possible policy choice at this stage. Modernising the organisation in which the EU and its Member States are already members is the most suitable measure for achieving the objective of the proposal.

- **Choice of the instrument**

Decision of the Council of the European Union

3. RESULTS OF EX-POST EVALUATIONS, STAKEHOLDER CONSULTATIONS AND IMPACT ASSESSMENTS

- **Ex-post evaluations/fitness checks of existing legislation**

The need for the modernisation of the out-dated provisions of the ECT has been recognised by the ECT Contracting Parties (i.e. the EU, the EU Member States and other Contracting Parties). On 27 November 2018, the Energy Charter Conference adopted the Bucharest declaration stressing the importance of the ECT modernisation⁷ and approved a list of issues to be addressed⁸.

⁷ <https://energycharter.org/media/news/article/modernisation-of-the-energy-charter-treaty-discussed-during-the-celebration-of-the-20th-anniversary/>

⁸ https://energycharter.org/media/news/article/approved-topics-for-the-modernisation-of-the-energy-charter-treaty/?tx_news_pi1%5Bcontroller%5D=News&tx_news_pi1%5Baction%5D=detail&cHash=3da319e52a78fa54058bc2c08eccc214

- **Stakeholder consultations**

Stakeholder consultations on the EU reformed approach to investment were conducted in the context of entering into negotiations of investment treaties between the EU and its third countries partners, such as the Comprehensive Economic and Trade Agreement (CETA) between the EU and Canada.

In the context of the ECT itself, the decision on the list of topics for the modernisation was adopted following consultations with the industry and Observers and internal discussions during 2018 conducted by the Chair and Vice-Chair of the Subgroup on Modernisation⁹.

- **Collection and use of expertise**

The ECT modernisation is a process based on the experience gained by the ECT Contracting Parties in the implementation of the ECT over the last 20 years. Building on that experience the ECT Contracting Parties carry out their assessment of the ECT provisions and their relevance for energy markets today.

- **Impact assessment**

The objective of the ECT modernisation will be to bring the investment protection provisions in line with the standards developed along the lines of the reformed investment policy approach that the EU has adopted and applied since 2010¹⁰ (e.g. modern definition of the Right to Regulate, a clarification of the concepts of Fair and Equitable Treatment and of indirect expropriation etc.). These standards already form part of several EU agreements and the EU also obliges Member States to apply them when being authorised to negotiate any new Bilateral Investment Agreements. As such the ECT modernisation is a logical step in pursuing the EU's reformed approach on investment protection. The impact should be in line with the one of the EU reformed approach. The modernisation is expected to minimise the number of possible investor claims against legitimate public policy measures of the Contracting Parties.

- **Regulatory fitness and simplification**

Investors (including SMEs) and Member States will benefit from the updating of the investment protection standards in line with the modern international trends and the EU standards.

- **Fundamental rights**

The human rights aspects should be addressed as a part of negotiations, in particular in relation to topics such as sustainable development or right to regulate.

4. BUDGETARY IMPLICATIONS

The ECT modernisation has no impact on the budget of the EU.

⁹ https://energycharter.org/media/news/article/approved-topics-for-the-modernisation-of-the-energy-charter-treaty/?tx_news_pi1%5Bcontroller%5D=News&tx_news_pi1%5Baction%5D=detail&cHash=3da319e52a78fa54058bc2c08eccc214

¹⁰ COM(2010)343 final, quoted above.

5. OTHER ELEMENTS

- **Implementation plans and monitoring, evaluation and reporting arrangements**

In the spirit of its commitments regarding better implementation made in the 2015 Commission Communication 'Trade for all', the Commission will ex-post evaluate the result and effects of the ECT modernisation.

- **Explanatory documents (for directives)**

Not applicable.

- **Detailed explanation of the specific provisions of the proposal**

Not applicable.

- **Procedural aspects**

The Commission will negotiate for the EU.

In accordance with Article 218(4) TFEU, it is suggested that the Council of the European Union designates the Trade Policy (Services and Investment) Committee and the Energy Working Party as the committees in consultation with which the negotiations must be conducted.

The European Parliament will be informed at all stages of the procedure, in line with Article 218(10) TFEU.

The Commission welcomes the fact that the Members of the Council of the European Union are increasingly engaging at an early stage with their parliaments on trade negotiations in line with their institutional practices. It encourages the Members of the Council of the European Union to do the same with regard to this Recommendation for a Council decision having due regard to Council Decision 2013/488/EU on the security rules for protecting EU classified information.

The Commission will inform the ECT Contracting Parties of the EU's internal rules on transparency and access by the Council of the European Union and the European Parliament to negotiating documents.

The Commission makes this Recommendation and its Annex public immediately after its adoption.

The Commission recommends that the negotiating directives be made public immediately after their adoption.

Recommendation for a

COUNCIL DECISION

**authorising the entering into negotiations on the modernisation of
the Energy Charter Treaty**

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 194(2), Article 207(3) and the first subparagraph of Article 207(4), in conjunction with Article 218(3) and (4) thereof,

Having regard to the recommendation from the European Commission,

WHEREAS participation of the European Union in the negotiations on the modernisation of the Energy Charter Treaty should be ensured,

HAS ADOPTED THIS DECISION:

Article 1

The Commission is authorised to enter on behalf of the Union into negotiations on the modernisation of the Energy Charter Treaty.

Article 2

The negotiating directives are set out in the Annex.

Article 3

The negotiations shall be conducted in consultation with the Trade Policy Committee (Services and Investment) and the Energy Working Party.

Article 4

This Decision and its Annex will be made public immediately after their adoption.

Article 5

This Decision is addressed to the Commission.

Done at Brussels,

*For the Council
The President*