



Council of the
European Union

Brussels, 2 July 2019
(OR. en)

10745/19
ADD 1

LIMITE

ENER 397
WTO 190
FDI 20

NOTE

From: General Secretariat of the Council

To: Permanent Representatives Committee/Council

No. Cion doc.: 9305/19
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Subject: Negotiating Directives for the Modernisation of the Energy Charter Treaty
- Adoption

The Annex contains the negotiating directives to the above Council Decision set out in doc. 10745/19.

**NEGOTIATING DIRECTIVES FOR THE MODERNISATION OF THE ENERGY
CHARTER TREATY**

Regarding the process of the negotiations:

The Union shall be represented by the Commission throughout the negotiations. In accordance with the principles of sincere cooperation and of unity of external representation as laid down in the Treaties, the Union and the Member States of the Union participating in the negotiations shall fully coordinate positions and act accordingly throughout the negotiations.

These directives are without prejudice to the division of competences between the Union and the Member States as laid down in the Treaties.

Member States which are Members of the ECT shall exercise their voting rights and express themselves in accordance with these directives and previously agreed EU positions.

Regarding the substance of the negotiations:

A. NATURE AND SCOPE OF THE AGREEMENT

The aim of the negotiations is to modernise the provisions of the Energy Charter Treaty (the 'ECT'), signed in Lisbon on 17 December 1994 by its signatories (including the European Union (EU) and its Member States¹) and result in an Agreement creating a Modernised ECT.

During the Ministerial Conference of the ECT in November 2018, the ECT Contracting Parties agreed on a list of items for modernisation².

¹ Italy withdrew from the ECT as of 1 January 2016.

² https://energycharter.org/fileadmin/DocumentsMedia/CCDECS/2018/CCDEC201818_-_STR_Modernisation_of_the_Energy_Charter_Treaty.pdf

B. PROPOSED CONTENT OF THE AGREEMENT

General Principles and Objectives

The objective of the Modernised ECT should be to facilitate investment in the energy sector in a sustainable way between the ECT Contracting Parties by creating a coherent and up-to-date legally binding framework that provides for legal certainty and ensures a high level of investment protection.

The Modernised ECT should aim at establishing clear rules on a broad number of investment-related issues. This in turn will allow the ECT Contracting Parties to strengthen their institutional capabilities, public policies and legislative frameworks in the energy sector.

The modernised ECT should clarify that the EU can require market participants from third countries operating within the internal market to comply with applicable Union and Member States' laws, including those concerning environmental and safety policy.

The Modernised ECT should reflect climate change and clean energy transition goals and contribute to the achievement of the objectives of the Paris Agreement.

Investment Protection

The negotiations should bring the ECT provisions on investment protection in line with the modern standards of recently concluded agreements by the EU and its Member States and adjust the ECT to new political and economic global changes (including in the energy sector).

The Investment Protection standards under the Modernised ECT should continue to aim at a high level of investment protection, with provisions affording legal certainty for investors and investments of Parties in each other's market.

The modernised ECT should provide clear definitions of covered investments and investors. The definition of investor should explicitly exclude investors and businesses that are lacking substantive business activities in their country of origin, in order to clarify that mailbox companies cannot bring disputes under the ECT.

The Modernised ECT should explicitly reaffirm the right of ECT Contracting Parties to take measures to achieve legitimate public policy objectives, such as the protection of health, safety, the environment or public morals, social or consumer protection ('right to regulate'). In line with the EU reformed approach on investment protection, it should be clarified that investment protection provisions cannot be interpreted as a commitment by the Parties not to change their laws, including in a manner that may negatively affect the investor's expectations of profits. It should include provisions on State aid in line with existing EU agreements.

The Modernised ECT should include appropriate standards of protection for investors and investments, in line with EU law and the EU's reformed approach on investment protection, in particular (and in a non-exhaustive manner):

- Most favoured nation treatment provision, which under the ECT covers also national treatment;
- Fair and equitable treatment and full protection and security ('most constant protection and security'), which are appropriately circumscribed for interpretation purposes;
- Expropriation, covering direct and indirect expropriation, and appropriately defined to clarify the nature of indirect expropriation;
- Umbrella clause: to clarify the scope of the umbrella clause, which includes 'specific' or 'written' commitments and covers only breaches of contractual obligations that occur in the exercise of governmental authority;

- Transfers: allowing free transfers relating to an investment, together with appropriate exceptions and safeguards for financial difficulties or crises; and
- Denial of benefits: allowing the denying Party to adopt or maintain measures which are related to the maintenance of international peace and security (including the protection of human rights) and which prohibit transactions with that investor or covered investment.

The EU shall engage on the dispute settlement topics that have been identified in the list of items for modernization (frivolous claims, transparency, security for costs, valuation of damages and third party funding) in line with the EU approach in its investment protection agreements and the position taken by the EU in UNCITRAL WG III and ICSID, to ensure that this approach is reflected in the Modernized ECT.

In any event, the EU should strive to ensure that ongoing multilateral reforms of investor-to-state dispute settlement, such as those within UNCITRAL WG III and ICSID, will be applied to the ECT. This includes striving to ensure that a future Multilateral Investment Court applies to the ECT.

The European Union may engage in negotiations on all topics related to the list of items for modernisation, in line with these negotiation directives and the EU approach in its investment protection agreements. It shall also ensure that any rule or commitment agreed upon by the European Union should be in line with the EU legal framework.

Sustainable development and Corporate Social Responsibility ('CSR')

The Modernised ECT should include provisions on sustainable development, including on climate change and clean energy transition in line with the Paris Agreement and recently concluded EU agreements and EU positions in ongoing negotiations. It should also contribute to the promotion of human rights and international labour standards, including through provisions on transparency and corporate social responsibility/responsible business conduct.

Regional economic integration organisation ('REIO')

The EU does not support the amendment of the REIO provision in the ECT modernisation process. Should, however, the negotiations cover also the REIO provision, the EU should ensure that the aim of the provision in the Modernised ECT remains that of providing that none of the ECT provisions should be construed so as to oblige any Party to the ECT which is a party to an Economic Integration Agreement ('EIA') to extend to another Party of the ECT which is not a party to that EIA any preferential treatment applicable between the parties of the EIA.

Pre-investment

The EU does not support the inclusion of pre-investment in the ECT modernisation, which should focus on investment protection provisions. Should, however, the negotiations cover also pre-investment, the EU should oppose making pre-investment provisions subject to dispute settlement.

Transit

The provisions of the transit chapter should be clarified to better take into account the requirements of integrated energy markets with third party access rights such as in the EU.

In relation to gas, it should make clear that the concept of “transit” in the Energy Charter 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 by the EU. Any rule or commitment agreed upon by the European Union should be in line with the EU legal framework and EU international commitments, notably in relation to third-party access and tariffs for infrastructure use.

Definition of “Charter”

The definition is relevant for several key provisions of the ECT. In 2015, the International Energy Charter was adopted in order to update the original 1991 European Energy Charter. The ECT Contracting Parties were unable to agree whether the reference to the Charter in the ECT could be understood to also referring to the International Energy Charter. The EU was in favour of such an interpretation. Therefore, the Modernised ECT should include the 2015 International Energy Charter inside the definition of the ‘Charter’.

Definition of “economic activity in the energy sector”

Investments covered by the ECT must be associated with ‘economic activity in the energy sector’. Such economic activity is associated with products and materials that are largely fossil fuels-related (listed in Annex EMI of the ECT). The definition may not cover new trends in investment, in particular with regard to renewable energy nor the energy efficiency tools and on-going digitalisation of the energy sector. Therefore, the Modernised ECT should include a definition of the ‘economic activity in the energy sector’ which allows addressing the challenges and opportunities of the transition to a safe and sustainable low-carbon, more digital and consumer-centric energy system.

Deletion of obsolete provisions

The ECT Secretariat requested to use the modernisation process to address the issue of obsolete ECT provisions. 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.