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ANNEX

ANNEX

to the

Recommendation for a Council Decision

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

ANNEX

NEGOTIATING DIRECTIVES FOR THE MODERNISATION OF THE ENERGY CHARTER TREATY

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 modernisation. The list covers the following topics: provisions related to investment protection standards and relevant definitions (such as definition of 'investment' and of 'investor'). Other ECT Contracting Parties expressed their wish to cover other topics such as pre-investment, transit, definitions of 'charter' and 'economic activity in the energy sector', Regional Economic Integration Organisation (REIO) and provisions related to dispute resolution. At the request of the Energy Charter Secretariat, the modernisation will also cover the deletion of obsolete provisions.

B. PROPOSED CONTENT OF THE AGREEMENT

General Principles and Objectives

The objective of the Modernised ECT should be to increase 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.

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 (also in the energy sector).

The Investment Protection standards under the Modernised ECT should 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 Investment Protection standards under the Modernised ECT should cover investments and investors of the ECT Contracting Parties. They should seek to include appropriate mechanisms to exclude businesses that do not have a sufficient connection to their country of origin.

The Modernised ECT should explicitly refer to the right of ECT Contracting Parties to take measures to achieve legitimate public policy objectives. It should include provisions on State aid in line with existing EU agreements.

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

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

- Right to regulate;
- Most favoured nation treatment provision, which under the ECT covers also national treatment;
- Clarification of 'most constant protection and security';
- Fair and equitable treatment and full 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;
- Transfers: allowing free transfers relating to an investment, together with appropriate exceptions and safeguards for financial difficulties or crises; and
- Denial of benefits.

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.

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 recently concluded 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 inclusion of the REIO provision in the ECT modernisation. Should, however, the REIO negotiations be pursued by the ECT Contracting Parties, their outcome should reflect the EU's understanding of REIO and its application with respect to the relationship between the EU and its Member States².

Pre-investment

The modernisation 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

² See Communication "Protection of intra-EU investment", COM (2018)547 final; and Council notes adopted by Foreign Affairs Council: State aid case SA.40348, Support for electricity generation from renewable energy sources, cogeneration and waste - Spain, Commission decision C(2017) 7384, recitals 160 to 163, and State aid case SA.40171 Promotion of electricity production from renewable energy sources - Czech Republic, Commission decision C(2016) 7827, recitals 143 to 148.

The transit chapter should be adapted to the requirements of integrated energy markets with third party access rights such as in the EU. 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.

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 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 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.