EUROPEAN
COMMISSION

Brussels, 19.11.2019
COM(2019) 597 final

REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL

on the operation of Regulation (EU) No 912/2014 on the financial responsibility linked to investor-to-state dispute settlement under international agreements to which the European Union is party

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1. Introduction

On 23 July 2014, the European Parliament and the Council adopted Regulation (EU) No 912/2014 establishing a framework for managing financial responsibility linked to investor-to-State dispute settlement tribunals established by international agreements to which the European Union is party (the "Financial Responsibility Regulation" or "FRR"). The legal basis for the FRR is Article 207 TFEU concerning the common commercial policy, of which foreign direct investment is a component.

The Commission is the Union institution in charge of administering the Financial Responsibility Regulation. Within the Commission, the responsible service is the Directorate General for Trade; the Legal Service is in charge of representing the Union during the dispute settlement proceedings and the possible subsequent stages of the litigation.

The Financial Responsibility Regulation sets out criteria for the determination of the respondent status and the allocation of financial responsibility between the Union and the Member States for treatment which may result in awards for monetary compensation further to investor-to-State dispute settlement proceedings.

Generally, financial responsibility is allocated to the entity responsible for the treatment that gives rise to compensation. This entails that the Union bears financial responsibility where the treatment concerned is afforded by an institution, body, agency or office of the Union, while a Member States bears financial responsibility when the treatment concerned is afforded by it. However, when a Member States acts in a manner required by EU law, for example by transposing an EU directive, the Union bears the financial responsibility insofar as the treatment concerned is required by EU law.

Concerning the respondent status, the rule is that generally the party which bears financial responsibility also acts as the respondent in a dispute. However, there are specific circumstances where the Union acts as the respondent even when the Member State bears the financial responsibility. This is for instance the case when: a Member State prefers the Union to act as the respondent (for example in view of technical expertise required in the dispute); the case also involves treatment afforded by a Member State and such treatment is required by EU law; similar treatment is subject to WTO dispute settlement proceeding and it is necessary to ensure consistency of argumentation.

The Financial Responsibility Regulation sets out arrangements to ensure that when the Union acts as the respondent in cases concerning treatment afforded by a Member State, the Member State concerned and the Union work in close cooperation in the conduct of dispute settlement proceedings, in accordance with the duty of sincere cooperation enshrined in Article 4(3) of the Treaty on European Union. This includes taking into account the defence and protection of the interests of the Member State concerned, exchanging timely information and relevant documents, engaging in frequent consultations, and participating in the delegation to the proceedings.

The Financial Responsibility Regulation also lays down procedures for Member States and the Commission to enter into arrangements for the payment of costs of litigation and of awards granting monetary compensation, in order to ensure that the resources of the EU are not, even temporarily, unduly burdened. In particular, the Commission and the Member State concerned are required to enter into an arrangement for periodic payment of costs and for the payment of any compensation. If financial responsibility is not accepted by the Member State concerned, the Commission can address a decision to it requesting it to provide the relevant amounts to the budget of the Union, together with applicable interests.

Finally, the FRR establishes procedures and requirements for settling cases when settlements are in the interest of the Union. For cases that involve only the financial responsibility of the Union, it is the Commission that decides on the settlement. When a case concerns also treatment afforded by a Member State, settling a dispute either requires the agreement of the Member State, or it can be decided by the Commission provided it has no financial or budgetary implications for the Member State concerned.

Throughout the various stages of a dispute, the Financial Responsibility Regulation imposes information duties on the Commission vis-à-vis the European Parliament and the Council, for instance when it receives from a claimant a request for consultation or a notice of intention to initiate dispute settlement proceedings.

2. Current scope of application of the Financial Responsibility Regulation

The Financial Responsibility Regulation applies to investor-to-State dispute settlement proceedings conducted under agreements to which the EU is a party. At present, pending the ratification and entry into force of agreements which contain an investor-to-State dispute settlement mechanism, e.g. the bilateral agreements with Canada (CETA), Singapore and Vietnam, the FRR effectively applies only to investor-to-State dispute settlement cases initiated against the EU under the Energy Charter Treaty (ECT). The Union has been a Contracting Party of the ECT since its ratification in 1998.

3. Cases initiated against the Union under the Energy Charter Treaty

To date, there has been one investment dispute settlement proceeding initiated against the Union under the Energy Charter Treaty. In addition, there have been a few requests for consultations received by the Union pursuant to Article 26 of the ECT, which have not so far advanced to the stage of formal litigation. All these proceedings are described in more detail below.

a. Claims by Prosisa and Risteel Corporation on the Spanish renewables support scheme (2015)

In 2015, the Commission received two requests for consultation pursuant to Article 26 of the ECT, respectively from the Swiss company Prosisa AG and the Dutch company Risteel Corporation BV. The Commission informed the European Parliament and the Council in accordance with Articles 4 and 7 of the Financial Responsibility Regulation on 7 October 2015.

Both companies had made investments in the photovoltaic and wind sectors and in the production of renewable energy with biomass in the territory of Spain, and their claims related

to Spain's decision to amend the support scheme for renewable energy. The companies had also in parallel launched proceedings against Spain. They essentially argued that the Commission has violated the fair and equitable treatment standard enshrined in Article 10 of the ECT by intervening before arbitration tribunals constituted under the ECT and by arguing that the ECT did not apply in the relationships between an EU Member State and an investor from another EU Member State.

Consultations pursuant to Article 26(1) of the ECT took place on 1st December 2015 between the investors and the Commission. The Commission clarified that it considered there was no valid legal basis allowing the companies to proceed with their disputes against the Union.

The companies did not pursue further their claims against the EU.

b. Claims by Nord Stream 2 on the amendment of the Gas Directive (2019)

On 12 April 2019, Nord Stream 2 AG, a subsidiary of Gazprom incorporated in Switzerland, addressed a letter to the Commission seeking clarification on the application of the derogation regime contained in Directive (EU) 2019/692 of 17 April 2019 amending the Gas Directive 2009/73/EC ("Amending Gas Directive).[1] In the letter, Nord Stream 2 also provided notice to the Commission of an alleged breach of the ECT, and requested the EU to attempt to reach an amicable settlement in accordance with Article 26(1) of the ECT. In accordance with Article 4 of the Financial Responsibility Regulation, the Council and the European Parliament were informed of these developments on 13 May 2019.

Nord Stream 2 AG argued that it should be entitled to a derogation under the amended Gas Directive from the rules on unbundling, third party access and tariff regulation applicable pursuant to the Gas Directive, as such derogation would allow it to recover the investment made, thus respecting its legitimate expectations. It claimed that should it not be eligible for a derogation under the Amending Directive and no other steps be taken to put it in an equivalent position, this would amount to a breach of the EU's obligation under the ECT, in particular Articles 10 and 13 of the ECT. Nord Stream 2 AG also argued that it qualifies as an investor of a Contracting Party under the ECT being a company headquartered and having substantial business operations in Zug, Switzerland.

Consultations between the Commission and Nord Stream 2 took place on 25 June 2019. The European Commission reserved its position on whether it considers Nord Stream 2 to have standing to bring a claim under the ECT pending submission of concrete evidence by the investor of its business operations in Switzerland. It also informed the investor that it considers Directive 2019/692 to be non-discriminatory and in line with the EU's international obligations under the ECT. On the question of whether Nord Stream 2 would be eligible for a derogation, the Commission recalled the rules of the Amending Gas Directive, notably that the relevant Member States' authorities will decide on the granting of derogations based on national rules transposing the Directive and upon individual applications.

The Commission had further written exchanges with Nord Stream 2 on 8 July, 26 July and 6 August 2019. On 25 July 2019, Nord Stream 2 lodged an application for annulment of Directive (EU) 2019/692 before the General Court (Case T-526/19). On 26 September 2019,

[1] Directive (EU) 2019/692 of the European Parliament and of the Council of 17 April 2019 amending Directive 2009/73/EC concerning common rules for the internal market in natural gas, OJ L 117, 3.5.2019, p. 1.

Nord Stream 2 submitted a notice of arbitration against the Union pursuant to Article 26(2)(c) and 26(4)(b) of the ECT. The Commission informed the European Parliament and the Council in accordance with Articles 4 of the Financial Responsibility Regulation on 1 October 2019.

In the notice of arbitration, Nord Stream 2 AG alleges that Directive (EU) 2019/692 (the "Amending Directive") and the EU's action in connection with the Amending Directive breach the EU's obligations under the ECT, in particular Articles 10(1), 10(7) and 13 of the ECT.

c. Claims by UK investors on behalf of AS PNB Banka against regulatory requirements established by the European Central Bank (2019)

On 2 May 2019, the Commission received a letter, pursuant to Article 26(1) ECT, from Russian investors (with UK nationality) on behalf of the Latvian bank AS PNB Bank, in relation to certain decisions of the European Central Bank (ECB) which imposed regulatory requirements on the bank and allegedly impact on their investment in a wind power plant in Latvia, Winergy.

In particular, the investors claimed that a draft decision by the ECB of 17 May 2019 which imposed deadlines on AS PNB Bank to resolve its exposure to Winergy and to meet certain capital adequacy thresholds, led to the withdrawal of the bank's licence, and to the deprivation of their investments in Winergy. The investors argued that with its actions the Union was threatening the continued existence and security of their investments in Winergy in breach of the EU's obligations under Part III of the ECT, along with Latvia.

The European Parliament and the Council were informed of these allegations on 24 May 2019.

On 28 June 2019, the Commission addressed a letter to the investors setting out the view that they do not have standing to initiate proceedings against the EU under the ECT, the investors being EU nationals, and suggesting the withdrawal of the claims.

4. Transparency in investor-to-State dispute settlement proceedings against the Union

The European Commission is committed to ensuring the highest degree of transparency in investor-State dispute settlement proceedings initiated against the Union. In recent years, the Commission has radically reformed the Union's approach to investment dispute settlement through a number of initiatives. These include negotiating rules on transparency leading to the adoption of the UNCITRAL Transparency Rules in 2013, and the incorporation of such rules into the provisions of the Investment Court Systems established in the EU's bilateral agreements with Canada, Singapore, Vietnam and Mexico.

The Union has also been involved in the negotiation of the United Nations Convention on Transparency in Treaty-based Investor-State Arbitration ("Mauritius Convention", New York, 2014), which is a UN Convention providing for the application of the UNCITRAL Transparency Rules to the existing stock of over 3000 bilateral investment treaties. The Commission had sought to have the UNCITRAL Transparency rules applied to the ECT through the Mauritius Convention and has made a proposal for a Council decision authorising the signing of the Mauritius Convention by the EU in January 2015. However, so far the

Council has not agreed to the adoption of the Commission's proposal. This means that the transparency rules do not currently obligatorily apply to disputes under the ECT.

The Commission has nevertheless taken initiatives to ensure the fullest degree of transparency possible in the investors' claims that have so far been brought to its attention. It has published on DG TRADE's website the most recent exchanges between the investors and the Commission (https://ec.europa.eu/trade/policy/accessing-markets/dispute-settlement/investment-disputes/). If investors decide to submit their claims to arbitration, the Commission intends to continue applying transparency standards, by seeking agreement with the investors to publish submissions, and by organising open hearings.

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