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The End Is Near: The European Commission's Proposed Coordinated Withdrawal from the ECT

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On 7 July 2023, the European Commission issued its [proposal for a Council decision on the withdrawal of the European Union from the Energy Charter Treaty \(ECT\)](#). The proposal comes more than 6 months after the Commission-sponsored ECT [modernization](#) package failed to be adopted and perhaps undermines any hope that a modernized ECT will be agreed any time soon. However, whilst it now seems highly likely that both the EU and its Member States will withdraw from the treaty (and refuse to agree to the modernized text), there remains at least 26 non-EU Contracting Parties to the ECT including States such as the UK, Japan, Switzerland, and Turkey. Even if the Commission does its best to try to neutralize the intra-EU effect of the ECT, it is difficult to see how, for the 20-year duration of the sunset clause, the EU and its Member States can avoid claims from ECT investors from the non-EU Contracting Parties. It seems perhaps that the end is not yet near for the ECT.

How Did We End Up Here?

Following the wave of ECT arbitration proceedings against various EU Member States including Spain, Italy, and Czech Republic in the mid-2010s, the European Commission started voicing its dissatisfaction with the ECT and calling for reform. The European Commission led the modernization process principally with the goal of aligning the ECT with the Paris Agreement. After fifteen rounds of negotiations, in June 2022 the Contracting Parties finally reached an [Agreement in Principle](#) which, among other reforms, includes significantly narrower standards of protection, more limited definitions of “investor” and “investment,” a mechanism for early dismissal of frivolous claims, and a provision on the right to regulate, including in relation to climate change mitigation and adaptation.

The Agreement also includes an optional carve-out under which the Contracting Parties can exclude fossil fuel investments made after August 2023 from ECT protection, while existing investments would be protected for only ten years after the modernized ECT entered into force. This mechanism would allow Contracting Parties to regularly review the list of protected investments under the treaty to adapt to the evolving science and technology as well as to their specific climate goals and energy needs. [Only the UK and the EU announced their intention to carve-out fossil fuel investments.](#)

Despite being significantly “greener” than most investment treaties currently in force, a few weeks before the Agreement in Principle was due to be adopted, several EU Member States announced their intention to withdraw from the ECT altogether.¹⁾ The European Parliament followed with the adoption of a [resolution](#) calling for the Commission to prepare the coordinated withdrawal of the EU and its Member States. The [Energy Charter Secretariat submitted a letter](#) in response, noting certain misunderstandings in the Parliament’s resolution and stressing that the EU should still support the adoption of the modernized ECT, even if it intends to withdraw afterwards.

As a result of this rebellion against the deal negotiated by the Commission, the vote on the modernized ECT was indefinitely postponed.

A few months later, [the Commission issued a “non-paper”](#) setting out the three options available: (i) a coordinated withdrawal by the EU and its Member States; (ii) the withdrawal by the EU, but allowing some Member States to remain Contracting Parties to the modernized ECT; and (iii) the adoption of the modernized ECT followed by a coordinated withdrawal by the EU Member States. Although expressly not the official position of the Commission, the non-paper made clear that the first option was considered the “most adequate option.”

The Commission’s Proposal and Its Consequences for the EU

Last week, [the Commission proposed to follow the first option in its “non-paper”](#): a coordinated withdrawal by the EU from the unmodernized ECT. The [Commission has withdrawn](#) its initial proposal that the EU and its Member States ratify the modernized ECT first, as it “did not gather the required majority among Member States” due to the abstention of Germany, Spain, the Netherlands, and France. Importantly, the proposal [refers to](#) the withdrawal of the Union and does not mention the withdrawal by individual EU Member States, as that process would be subject to the applicable domestic rules. Therefore, it remains to be seen whether all EU Member States will follow the coordinated withdrawal or whether some Member States (who have not expressed a public opinion on the issue yet) will be less willing or able to proceed with the withdrawal, for instance if the required approvals under domestic law are not obtained. To recall, four EU Member States did not sign the [Termination Agreement of all intra-EU BITs](#).

The proposed EU withdrawal will now be submitted to the Council of the EU, where it will need to be adopted by a qualified majority, after obtaining the European Parliament’s consent. Assuming it is approved, the EU (and its Member States) will then need to trigger the withdrawal process by submitting their written notifications to the ECT Depository. In December 2022, [Germany, France, and Poland already initiated the process](#) on their own initiative. The withdrawal would then take effect one year after the date of receipt of the notification by the Depository.

The biggest challenge to the EU’s withdrawal is the 20-year sunset clause in Article 47(3); it contradicts the purported reason for exiting the treaty in the first place, *i.e.*, removing protection for fossil fuel investments. Indeed, adopting the modernized ECT may be preferable to withdrawing altogether, given the sunset clause. In its proposal, the Commission has acknowledged the effect of the sunset clause, although it considers that it would not apply to intra-EU relations since “the ECT has never, does not and will never apply” within the EU ([see here](#)). [Multiple tribunals have rejected this position](#) so far, and Italy’s withdrawal from the ECT in 2016 has not prevented it from facing several ECT arbitrations, including from EU investors (*See, e.g., VC Holding II and others v. Italy*,

ICSID Case No. ARB/16/39; *Veolia Propreté SAS v. Italy*, ICSID Case No. ARB/18/20; *Encavis AG and others v. Italy*, ICSID Case No. ARB/20/39).

To mitigate this risk, the Commission proposes the adoption of a “subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions” in accordance with Article 31(3)(a) of the Vienna Convention on the Law of Treaties (VCLT), by the EU and its Member States. Thus, the Commission **no longer appears to be pursuing** the adoption of an *inter se* modification agreement under Article 41(b) of the VCLT, perhaps given the challenges of that option which have been highlighted by tribunals and commentators (*see here and here*). However, a subsequent agreement on the interpretation of a treaty under Article 31(3)(a) of the VCLT must be agreed by all parties to the treaty (VILLIGER, Commentary on the 1969 Vienna Convention on the Law of Treaties, p. 429 (para. 16)). Therefore, such an agreement could not be adopted only by a subset of ECT Contracting Parties as the Commission proposes.

In any event, even this solution proposed by the Commission would **not** prevent investors from non-EU Contracting Parties (such as the UK, Turkey, Switzerland, or Japan) from bringing claims against the EU and its Member States during the sunset period. Indeed, as the Commission already anticipated in its non-paper last year, in order to avoid this the EU would need to enter into another agreement with non-EU Contracting Parties. However, **as the Commission admitted**, “no non-EU Contracting Party has indicated that they would be open to such a solution.”

For the EU and its Member States, **legal uncertainty will likely prevail** post-withdrawal given the ECT’s sunset clause and the risk that tribunals will not recognize the EU’s attempt to derogate from it. Adopting the modernized ECT prior to withdrawal would reduce such risk to some extent with respect to fossil fuel investments given the carve-out provision but the Commission appears to have considered and rejected this option.

What the Future Holds for the ECT

Shortly after the Commission’s proposed withdrawal was published, the Secretary General of the **ECT Secretariat issued a press release** expressing his “profound regret” and appealing to all EU Member States to support the modernized ECT, regardless of whether they intended to withdraw. Indeed, if the EU and its Member States follow a coordinated withdrawal, it will not be possible for the remaining Contracting Parties to adopt the modernized ECT in the near future. In its communication, **the Commission acknowledged** that “[w]ithout the participation of the EU and Euratom in such a vote, the voting quorum in the Conference is not met, and the modernization package cannot be adopted.”

Although it is unclear whether all the remaining Contracting Parties would adopt the modernized ECT further down the line (for instance, **Japan initially objected to the modernization of the ECT**, favoring the maintenance of the *status quo*), at this stage, it seems unlikely that the majority of the non-EU Contracting Parties will follow the EU’s withdrawal. For instance, **Switzerland indicated last year** that it may not follow the EU. The UK has also been a **strong supporter of the modernized ECT** and UK investors have significantly benefited from ECT protection. While the UK Government is also **facing some pressure at home**, remaining a party to a multilateral treaty like the ECT would seem consistent with the UK’s post-Brexit agenda, and would allow UK investors to maintain a significant level of protection that is **not found in the UK-EU Trade and Cooperation**

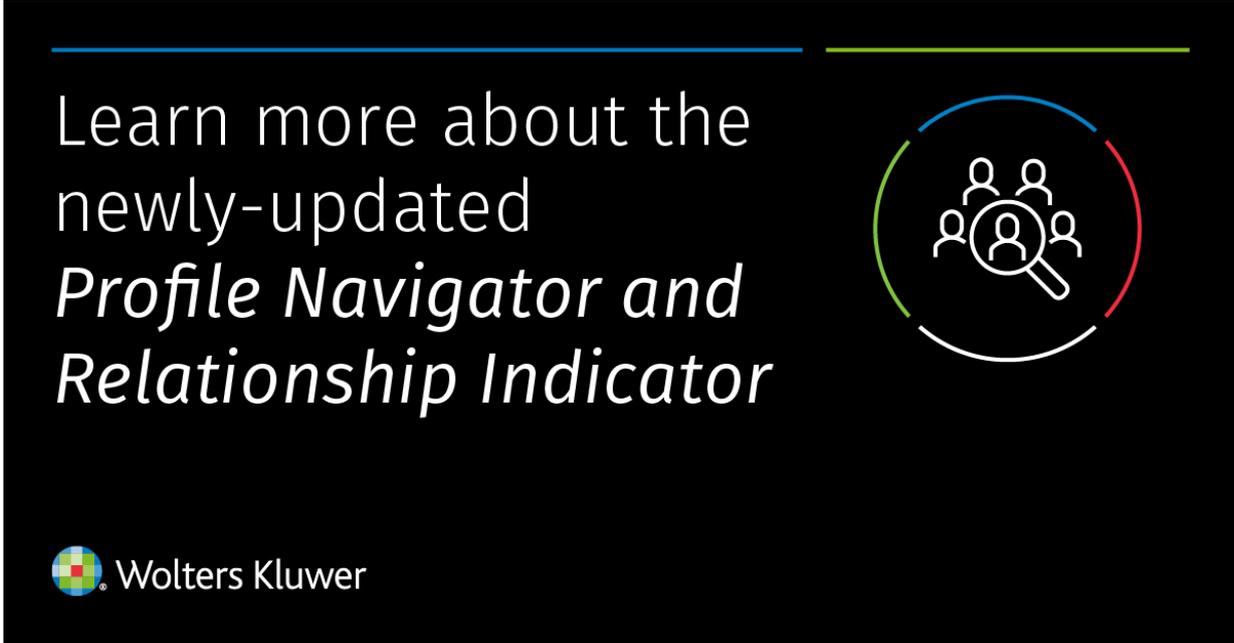
Agreement. Given that there is likely to be continuing protection for non-EU investments post-withdrawal, investors may also start to consider restructuring their investments via non-EU Contracting Parties (such as the UK or Switzerland) to ensure ECT protection.

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References

At that point Poland, Spain, the Netherlands, France, Slovenia, Germany, and Luxembourg ?1 announced their intention to withdraw. Since then, Belgium, Portugal, and Denmark made similar announcements.

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