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Proposal for a

REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

amending Regulation (EU) No 654/2014 of the European Parliament and of the Council concerning the exercise of the Union's rights for the application and enforcement of international trade rules

EXPLANATORY MEMORANDUM

1. CONTEXT OF THE PROPOSAL

• Reasons for and objectives of the proposal

The present proposal concerns an amendment of Regulation (EU) No 654/2014 of the European Parliament and of the Council of 15 May 2014 concerning the exercise of the Union's rights for the application and enforcement of international trade rules and amending Council Regulation (EC) No 3286/94 laying down Community procedures in the field of the common commercial policy in order to ensure the exercise of the Community's rights under international trade rules, in particular those established under the auspices of the World Trade Organization (the "Enforcement Regulation" or "Regulation")[1]. The objective of the amendment is the protection of the Union's interests under international trade agreements in situations when third countries adopt illegal measures and simultaneously block a dispute settlement process. The Regulation has not originally been designed to address such situations but current developments, namely blocking of dispute settlement under the World Trade Organization (WTO) Agreement, require that the Union act as quickly as possible to protect its interests.

The proposal is in line with the Union's priority to enforce effectively the Union's rights under international trade agreements. The Political Guidelines for the Commission set out that: "we must ensure that we can enforce our rights, including through the use of sanctions, if others block the resolution of a trade conflict"[2] and this language is echoed in the Mission Letter to the Commissioner for Trade.[3]

The proposed amendment extends the scope of the Enforcement Regulation to allow for action in a situation of dispute settlement procedures that are blocked. It is necessary to have this amendment adopted very quickly to ensure that the Union's rights are protected. To facilitate a speedy adoption by the co-legislators, no other changes are proposed.

– *Blockage of dispute settlement*

For more than two years, the WTO Dispute Settlement Body (DSB) has been unable to fill vacancies on the WTO Appellate Body. Due to the blockage of appointments there will only be one Appellate Body Member from 11 December 2019. Consequently, the Appellate Body will be unable to hear new appeals as from that date. WTO members will be able to avoid binding rulings and hence escape their international obligations by appealing panel reports. When a panel report is appealed but the Appellate Body cannot function, the dispute will be put into a legal void and will remain unresolved (this has been referred to as appealing "into the void"). This will mean that in those situations the WTO dispute settlement system will not be binding. Ultimately, the Union's economic interests will be compromised if international trade rules cannot be effectively enforced.

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1 Regulation (EU) No 654/2014 of the European Parliament and of the Council of 15 May 2014 concerning the exercise of the Union's rights for the application and enforcement of international trade rules and amending Council Regulation (EC) No 3286/94 laying down Community procedures in the field of the common commercial policy in order to ensure the exercise of the Community's rights under international trade rules, in particular those established under the auspices of the World Trade Organization (OJ L 189 27.6.2014, p. 50).

2 Political guidelines for the next European Commission 2019-2024. https://ec.europa.eu/commission/sites/beta-political/files/political-guidelines-next-commission_en.pdf

3 Mission Letter of 1 December 2019 from President von der Leyen to the Commissioner for Trade.

In the face of this emerging situation, the Union has been working intensively on two strands: i) making proposals to address the concerns raised by the WTO Member blocking the appointments and subsequent engagement with the WTO Membership[4], and ii) developing contingency measures in the form of an interim arrangement, which aims at replicating the WTO appellate mechanism until it is restored, through arbitration under Article 25 of the WTO Dispute Settlement Understanding (DSU)[5]. Such an interim appeal arrangement maintains appellate review and therefore produces not only a final ruling after the full completion of the WTO adjudicative process that is composed of two stages, but also a ruling which can be enforced under WTO rules. It is a stop-gap solution intended to function in the period before resumption of the operation of the Appellate Body. The interim arrangement is however not an automatic mechanism and will require the individual agreement of other WTO Members.

There is also a risk that dispute settlement concerning other international trade agreements of the Union, including bilateral and regional, particularly older agreements, can be stymied when a third country does not cooperate, as necessary, for dispute settlement to function. For example, the third country may fail to appoint an arbitrator and there is no fall-back mechanism foreseen for dispute settlement to nevertheless be able to proceed. In this situation, the Union's economic interests will be compromised and will require protection in the same manner as outlined above. This situation gains additional relevance in the light of the Union's increasing focus on enforcement. A greater use of dispute settlement under the Union's bilateral and regional free trade agreements is also expected as more of these agreements become applicable and provide for WTO plus obligations. Indeed the Union has recently initiated the first three such cases.

– *The Enforcement Regulation*

Following the Treaty of Lisbon, the European Parliament and the Council adopted the Enforcement Regulation as a common legislative framework for the enforcement of the Union's rights under international trade agreements, based on clear and predictable rules for action by the Commission. The co-legislators gave the Commission the power to adopt implementing acts in accordance with Article 291 of the Treaty on the Functioning of the European Union (TFEU), in a prompt manner, within the scope established by the Regulation and within the limits and in accordance with the criteria expressly set out.

Under the Regulation, the Commission may adopt the following types of commercial policy measures: customs duties, quantitative restrictions on imports or exports of goods, and measures in the area of public procurement. Such measures should be selected and designed on the basis of objective criteria, including the effectiveness of the measures in inducing compliance of third countries with international trade rules, their potential to provide relief to economic operators within the Union affected by the third countries' measures, and aim at minimising negative economic impacts on the Union, including with regard to essential raw materials.

The scope of the Regulation extends to the adoption, suspension, modification and termination of implementing acts with regard to:

[4] The process is led by Ambassador Walker of New Zealand, current Chairperson of the WTO Dispute Settlement Body.

[5] The initiative was endorsed by the Council of the European Union on 27 May 2019 and 15 July 2019. The European Parliament adopted a resolution supporting it on 28 November 2019.

(a) Enforcement of the Union's rights under binding multilateral and bilateral dispute settlement rules;

(b) Rebalancing measures under multilateral and bilateral safeguard rules; and

(c) Rebalancing measures in cases of modifications by a third country of its concessions under Article XXVIII of GATT 1994.

In particular with regard to the enforcement of the Union's rights under binding multilateral and bilateral dispute settlement the Commission has the power to introduce commercial policy measures in the case of an illegal measure maintained by a third country, notably to induce compliance by the third country in protection of the Union's interests. Such measures are however only possible on the basis of successful completion of dispute settlement procedures with regard to the third country's measure.

The Regulation does not therefore provide powers for situations in which the dispute settlement procedures do not function and therefore cannot be completed, such as the situations of blockage of dispute settlement mechanisms. The present proposal for an amendment of the Enforcement Regulation remedies this gap through an extension of the triggers for action under the Enforcement Regulation to such situations.

– *Policy considerations*

The main focus of the proposed amendment is to cater for situations where, after the Union has succeeded in obtaining a favourable ruling from a WTO dispute settlement panel, the process is blocked because the other party appeals a WTO panel report "into the void" and has not agreed to interim appeal arbitration under Article 25 of the WTO DSU. In such a situation, there will be no binding outcome of the dispute settlement process.

In addition, the proposed amendment caters for similar situations that may arise under other international trade agreements, in particular regional or bilateral agreements, when a third country does not cooperate, as necessary, for dispute settlement to function. For example, the third country may fail to appoint an arbitrator and there is no fall-back mechanism for arbitration provided to nevertheless be able to proceed.

The proposal covers the two situations together for reasons of coherence and efficiency. Both situations share the same root causes and bring the same negative consequences for the Union's economic interests. The common feature is that the Union should be able to enforce its rights, that this should be done to the utmost extent possible through independent adjudication. Where this is not possible and the other party is responsible for blocking the operation of binding independent adjudication, the Union should nevertheless be able to enforce its rights.

The present proposal ensures that the Union is equipped with the necessary tools to protect its economic interests, should that prove necessary. The course of action is a reflection of the Union's commitment to multilateralism and binding independent adjudication.

If the Union opted for not taking this action, the consequence in the situations of blocked dispute settlement described above would be that the Union could not protect its rights in a timely fashion. This could even create an incentive for third countries to thwart adjudication when the Union has rights under an international agreement, which the third country infringes.

Working on the framework that already exists in the form of the Regulation would secure an ability of the Union to act expeditiously. Speed of action is vital. This course of action, as with the logic of the Regulation itself, is therefore preferable to envisaging an ordinary legislative procedure for the enactment of trade policy measures in each individual case in which a third country maintains a measure of the type that routinely goes to dispute settlement but blocks the adjudication procedure.

The commercial policy measures taken under the Regulation notably serve to induce a third country to terminate a breach of a trade agreement of the Union after the Union's successful recourse to dispute settlement. The proposed amendment creates a possibility for the Union to impose measures under the Regulation in particular to induce the termination of a breach also without full recourse to an adjudicative dispute settlement procedure where the third country prevents that recourse.

The envisaged measures would be compatible with the international obligations of the Union. general public international law allows, under certain conditions such as proportionality and prior notice, the imposition of countermeasures, i.e. of measures that would otherwise be contrary to the international obligations of an injured party vis-à-vis the country responsible for a breach of international law, and that are aimed at procuring cessation of the breach or reparation for it. This customary international law has been codified by the International Law Commission, a United Nations body, in its Draft Articles on Responsibility of States for Internationally Wrongful Acts[6]. In principle, a party taking countermeasures is not relieved from fulfilling its obligations under any applicable dispute settlement procedure[7]. Those provisions constitute lex specialis in relation to the provisions of general international law on countermeasures[8]. However, where the responsible party fails to cooperate in good faith in the dispute settlement procedures, thereby preventing the injured party from completing such procedures, the possibility to resort to countermeasures in accordance with the requirements of general public international law necessarily revives. The International Law Commission notes that the revival of that possibility arises when one Party "fails to implement the dispute settlement procedures in good faith" or "where a State party fails to cooperate in the establishment of the relevant tribunal".[9] These are the situations in which the current amendment would operate.

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

The proposal is in line with the Union's priority to enforce effectively the Union's rights under international trade agreements, in the interest of securing jobs and promoting growth in the Union. It adapts the existing common legislative framework to this new situation.

- **Consistency with other Union policies**

The proposal is in line with other Union policies and it reaffirms the Union's commitment to multilateralism and independent adjudication. The proposal is to amend the existing Enforcement Regulation which was already consistent with other Union policies.

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6 See International Law Commission, *Draft Articles on Responsibility of States for Internationally Wrongful Acts*, November 2001, General Assembly, Official Records, Fifty-fifth Session, Supplement No. 10 (A/56/10), chp.IV.E.1, Chapter II and, in particular, introductory commentary (1).

7 Ibid., Article 50.2(a).

8 Ibid, Article 55.

9 Ibid., Articles 52(3)(b) and 52(4) and commentaries (2), (8) and (9).

2. LEGAL BASIS, SUBSIDIARITY AND PROPORTIONALITY

• Legal basis

The main objective and content of the envisaged act relate to the common commercial policy because of the nature of the measures adopted and because of their purpose which is the enforcement of the Union's international trade agreements. Therefore, the substantive legal basis of the proposed amendment is Article 207 TFEU.

• Subsidiarity (for non-exclusive competence)

Not applicable. The common commercial policy is an area of Union's exclusive competence. The subsidiarity principle does not apply in areas of exclusive competence.

• Proportionality

The objective of swift protection of the Union's interests under international trade agreements in situations when third countries adopt illegal measures and simultaneously prevent a dispute settlement process is optimally achieved through the proposed amendment of the Enforcement Regulation. The amendment is limited to introducing two new triggers for the Union to act and does not go beyond what is necessary to achieve its objective. Also, the measures adopted under the Regulation must themselves be proportionate. For the cases where this does not follow from provisions of the international agreement in question, the amendment adds an explicit provision to that effect. This is in line with the requirement of general international law that countermeasures be proportionate.

• Choice of the instrument

The Commission considers this legislative amendment suitable because it amends an existing Regulation already adopted on the basis of Article 207 TFEU.

3. RESULTS OF CONSULTATIONS AND IMPACT ASSESSMENTS

• Ex-post evaluations/fitness checks of existing legislation

Not applicable.

• Stakeholder consultations

No public consultation has been carried out for this initiative. The proposed amendments would only insert new triggers for use of the Regulation with respect to the emergency arising in the WTO.

For the adoption of any commercial policy measure under the regulation, the Commission is already under an obligation to carry out an information gathering exercise and follow an implementing act procedure in each individual case of application. Through the information gathering exercise the Commission will seek and obtain information and views from stakeholders regarding the Union's economic interests in specific sectors in which countermeasures might be contemplated. The Commission must take the input into account. The Committee established by Regulation (EU) 2015/1843[10] will assist the Commission in the

[10] Regulation (EU) 2015/1843 of the European Parliament and of the Council of 6 October 2015 laying down Union procedures in the field of the common commercial policy in order to ensure the exercise of the Union's rights under international trade rules, in particular those established under the auspices of the World Trade Organization (codification) (OJ L 272, 16.10.2015, p. 1).

application of the Enforcement Regulation. The Committee consists of representatives of the Union's Member States.

- **Collection and use of expertise**

Not applicable. Relevant details are provided below.

- **Impact assessment**

No impact assessment has been carried out for this initiative in view of the nature of the subject that is enforcement and implementation of rights under international trade agreements. The present proposal does not have a direct economic, social or environmental impact and the nature of the measures that may be adopted (on a case-by-case basis) does not in any case allow an ex-ante evaluation.

As explained above, for the adoption of any commercial policy measure, the Commission is already under an obligation to carry out an information gathering exercise and follow a procedure in each individual case of application. Through the information gathering exercise the Commission will seek and obtain information and views from stakeholders regarding the Union's economic interests in specific sectors.

The proposal renews the Commission's obligation to review the scope of the Regulation after a certain period of time. Therefore, the Commission will be able to examine the impact of the amendment accordingly.

Furthermore, the present proposal addresses an urgent situation and therefore requires rapid action.

- **Regulatory fitness and simplification**

Not applicable.

- **Fundamental rights**

Not applicable.

4. BUDGETARY IMPLICATIONS

None.

The proposed amendment provides a mechanism to enforce the Union's rights.

5. OTHER ELEMENTS

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

Not applicable.

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

The proposal is limited to the introduction of a limited number of amendments to the existing Enforcement Regulation.

The new provisions are as follows:

– In Article 3 (Scope), points (aa) and (bb) are added to allow the Union to take measures in the situations when a dispute settlement procedure cannot be pursued due to the non-cooperation of the other party, in a trade dispute under either the WTO Agreement or other regional or bilateral international trade agreements, respectively. As far as disputes under the WTO Agreement are concerned, this will require the Union having obtained a ruling from a WTO panel confirming the EU's right of action and absent agreement on an interim arrangement for appeal arbitration.

– In Article 4, point (bb) is added to set out the requirement that the Union's countermeasures in such situations not exceed the nullification or impairment caused by a measure of the third country. This is already in place in the existing framework by virtue of the respective rules of dispute settlement, and it is in line with the general public international law requirement that countermeasures be commensurate to the breach that they respond to.

– Article 10 is amended so as to renew the Commission's obligation to review the scope of the Regulation, including a review obligation with regard to the proposed amendment, after a period of five years.

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amending Regulation (EU) No 654/2014 of the European Parliament and of the Council concerning the exercise of the Union's rights for the application and enforcement of international trade rules

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 207(2) thereof,

Having regard to the proposal from the European Commission,

After transmission of the draft legislative act to the national parliaments,

Acting in accordance with the ordinary legislative procedure,

Whereas:

(1) Regulation (EU) No 654/2014 of the European Parliament and of the Council[11] establishes a common legislative framework for exercising the Union's rights under international trade agreements in certain specific situations.

(2) One of those situations relates to the dispute settlement mechanisms set up by the Agreement establishing the World Trade Organization ('WTO') and by other international trade agreements, including regional or bilateral agreements. Regulation (EU) No 654/2014 enables the Union to suspend obligations after dispute settlement proceedings are concluded.

(3) That Regulation however does not address a situation where the Union has a right of action in response to a measure maintained by a third country, but dispute settlement through adjudication is blocked or otherwise not available for reasons of non-cooperation of the third country having adopted that measure.

(4) The WTO Dispute Settlement Body has been unable to fill the outstanding vacancies on the Appellate Body. The Appellate Body is no longer able to fulfil its function from the moment when there are fewer than three Appellate Body Members left. Until this situation is resolved and in order to preserve the essential principles and features of the WTO dispute settlement system and the Union's procedural rights in ongoing and future disputes, the Union has sought to agree interim arrangements for appeal arbitration pursuant to Article 25 of the WTO Understanding on Rules and Procedures Governing the Settlement of Disputes ("WTO Dispute Settlement Understanding"). This approach has been endorsed by the Council of the European Union on 27 May 2019 and 15 July 2019 and supported in a resolution of the European Parliament on 28

[11] Regulation (EU) No 654/2014 of the European Parliament and of the Council of 15 May 2014 concerning the exercise of the Union's rights for the application and enforcement of international trade rules and amending Council Regulation (EC) No 3286/94 laying down Community procedures in the field of the common commercial policy in order to ensure the exercise of the Community's rights under international trade rules, in particular those established under the auspices of the World Trade Organization (OJ L 189 27.6.2014, p. 50).

November 2019. If a WTO Member refuses to enter into such an arrangement, and files an appeal to a non-functioning Appellate Body, the resolution of the dispute is effectively blocked.

(5) In the same vein, a similar situation may arise under other international trade agreements, in particular regional or bilateral agreements, where a third country does not cooperate, as necessary, for the dispute settlement to function, for example by failing to appoint an arbitrator and where there is no mechanism foreseen to secure the functioning of dispute settlement in this situation.

(6) In the face of blockage of dispute settlement, the Union will be unable to enforce international trade agreements. Therefore, it is appropriate to extend the scope of Regulation (EU) No 654/2014 to such situations.

(7) To this end, the Union should be able to expeditiously suspend obligations under international trade agreements, including regional or bilateral agreements, when effective recourse to a binding dispute settlement mechanism is not possible because the third country has rendered it impossible for the Union to do so.

(8) It is also appropriate to set out that where measures are taken to restrict the trade with a third country in the situations at stake, such measures should be commensurate to the nullification or impairment of the Union's commercial interests caused by the measures of that third country, in line with the Union's obligations under international law.

(9) Finally, the review clause of Regulation (EU) No 654/2014 should be renewed for another five-year period and should cover the application of the proposed amendment.

(10) Regulation (EU) No 654/2014 should therefore be amended accordingly,

HAVE ADOPTED THIS REGULATION:

Article 1

Regulation (EU) No 654/2014 is amended as follows:

(1) Article 3 is amended as follows:

(a) the following point (aa) is inserted:

"(aa) following the circulation of a WTO panel report upholding, in whole or in part, the claims brought by the European Union, if an appeal under Article 17 of the WTO Dispute Settlement Understanding cannot be completed and if the third country has not agreed to interim appeal arbitration under Article 25 of the WTO Dispute Settlement Understanding;"

(b) the following point (bb) is inserted:

"(bb) in trade disputes relating to other international trade agreements, including regional or bilateral agreements, if adjudication is not possible because the third country is not taking the steps that are necessary for a dispute settlement procedure to function;"

(2) In Article 4 (2), the following point (bb) is inserted:

"(bb) where measures are taken to restrict the trade with a third country in situations under Article 3(aa) or Article 3(bb), such measures shall be commensurate to

the nullification or impairment of the Union's commercial interests caused by the measures of that third country;"

(3) Article 10 is amended as follows:

(a) paragraph 1 is replaced by the following:

"By 1 March 2025 at the latest, the Commission shall review the scope of this Regulation, taking into account in particular the amendments to the scope having effect from [date of entry into force of this amending Regulation], the commercial policy measures that may be adopted, as well as its implementation, and shall report its findings to the European Parliament and the Council."

(b) paragraph 2 is amended as follows:

(i) in the first subparagraph of paragraph 2 the first sentence is replaced by the following:

"In acting pursuant to paragraph 1, the Commission shall undertake a review aimed at envisaging under this Regulation additional commercial policy measures suspending concessions or other obligations in the field of trade in services".

(ii) the second subparagraph is deleted.

Article 2

This Regulation shall enter into force on the […] day following that of its publication in the *Official Journal of the European Union*.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels,

For the European Parliament	*For the Council*
The President	*The President*