EUROPEAN COMMISSION

Brussels, 23.5.2013
COM(2013) 297 final

Recommendation for a

COUNCIL DECISION

authorising the Commission to open negotiations on an investment agreement between the European Union and the People's Republic of China

{SWD(2013) 184 final}
{SWD(2013) 185 final}

DECLASSIFIED PART

on 08 FEB 2016

EXPLANATORY MEMORANDUM

1. CONTEXT OF THE PROPOSAL

The Lisbon Treaty provides for the European Union to contribute to the progressive abolition of restrictions on foreign direct investment. Articles 3(1)(e), 206 and 207 of the Treaty on the Functioning of the European Union confer exclusive competence to the European Union in the field of foreign direct investment.

The Commission Communication[1] of 3 March 2010 "*A strategy for smart, sustainable and inclusive growth – Europe 2020*" emphasises the need to build strategic relationships with emerging economies. Trade and investment are a crucial component of the triple growth objective of the Europe 2020 Strategy. The Commission Communication[2] of 7 July 2010 "*Towards a comprehensive European international investment policy*" identifies China as a potential partner for an investment agreement, given the shortcomings of the current legal framework and climate for investment between the EU and China.

In April 2010 the European Commission President José Manuel Barroso and Chinese Premier Wen Jiabao agreed to look into ways of deepening and enhancing the EU-China bilateral investment relationship. European Trade Commissioner Karel De Gucht and the Chinese Minister for Trade, Chen Deming agreed at the EU-China Joint Committee in May 2010 to launch a Joint EU-China Investment Taskforce to study the options for enhancing bilateral investment and evaluate the desirability and feasibility of potential negotiations of an EU-China investment agreement.

At the EU-China Summit in February 2012 leaders emphasised that *"a rich in substance EU-China investment agreement would promote and facilitate investment in both directions. Negotiations towards this agreement would include all issues of interest to either side, without prejudice to the final outcome. They agreed to work towards the start of the negotiation as soon as possible."*

This statement echoes a basic mutual understanding that the negotiations will encompass all key issues of interest to either side – namely an acknowledgement that this agreement should deal with both investment protection as well as improved access to the market for investors from the EU and China.

The EU-China Summit in September 2012 "*reconfirmed both sides' commitment to launching negotiations of an EU-China Investment Agreement as soon as possible to promote and facilitate investment in both directions*".

2. RESULTS OF CONSULTATIONS WITH THE INTERESTED PARTIES AND IMPACT ASSESSMENTS

As a consequence of this mutual political intent and in order to guide next steps, the European Commission undertook an in depth impact assessment to analyse the underlying problems in the current EU-China investment relationship, the different options to address these and their respective impacts from an economic, social, labour, environmental, human rights and financial perspective.

1 Commission (2010) 2020 final
2 Commission (2010) 343 final.

Civil society, Member States and the European Parliament were consulted and informed of the reflections on an investment agreement and the draft negotiating directives in the framework of the impact assessment carried out by the European Commission.

China is the world's third largest economy and the biggest exporter, but also an increasingly important outward investor. EU-China trade has increased dramatically in recent years. China is now the EU's second trading partner behind the United States and the EU's biggest source of imports by far. International estimates predict China may be on track to become the world's biggest economy within the next 5-10 years. China's rise as a major global economy was boosted by its accession to the World Trade Organisation (WTO) in 2001, which integrated China into the multilateral trading system. WTO accession brought substantial reform and opening up of China's market in many respects but has not resulted in a sufficiently open investment environment.

China is regarded as one of the most strategic destinations for foreign direct investment (FDI) by European companies – both at present and for the future. This was confirmed by DG TRADE's public consultation in 2011 on the future of the EU-China investment relationship, as well as through other business surveys conducted.[3]

Yet while FDI between the EU and China has become a more visible factor of the bilateral relationship, there remains an important discrepancy between, on the one hand, the EU-China overall trade relationship, and investment on the other. Compared with those of other key trading partners such as the United States and particularly other emerging economies such as Brazil and India, EU-China FDI flows and stocks are clearly lagging behind in both directions.

Despite the growing attraction and strategic importance of China as an FDI destination, the lack of an open, predictable and secure environment negatively affects EU outward FDI flows to China. The result is not only an untapped potential, but also a growing imbalance, given the relative absence of barriers in the EU towards increasing Chinese inward investment. Market access limitations for EU investors in China are a major concern and exist at various administrative levels (national, regional, municipal) and in manifold forms (foreign ownership prohibitions and equity limitations, joint venture requirements, screening mechanisms, capital and licensing requirements to name but a few). These market access barriers increase the costs and/or prevent investing in China. Particularly SMEs which dispose of fewer resources are thereby prevented from entering China.

EU investors already established in China complain about discriminatory treatment in form of more burdensome administrative rules and requirements for foreign investors, insufficient protection of intellectual property rights and key technologies, subsidies to Chinese competitors and the conduct of state-owned enterprises (SOEs).

Chinese outward FDI has increased dramatically in the past years and also its investment into the EU is increasing. Yet, while the increases seem very large looking at the growth percentage (100 per cent increase from 2010 to 2011), having started from a very low base the total Chinese FDI into the EU remains comparatively low at a time when the EU is looking to attract even more FDI to counterbalance the economic crisis.

3 See public consultation; also reflected in: European Chamber of Commerce in China (EUCCC) (2011) *Business Confidence Surevy 2011*.

As regards protection of investors and their investments, a patchwork of agreements exists. China has concluded 25 Bilateral Investment Treaties (BITs) with 26 EU Member States. However, these BITs provide for widely discrepant levels of investment protection and post-establishment treatment while not addressing barriers to market access. China has been particularly interested in replacing this patchwork with a coherent EU level framework to increase certainty for Chinese investors in Europe.

On the basis of the analysis undertaken and given the strong calls received from stakeholders, the European Commission believes that there is a clear need to actively remedy the current shortcomings of the framework for EU-China investment relations through the negotiations of an ambitious investment agreement.

3. LEGAL ELEMENTS OF THE PROPOSAL

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ANNEX