Climate and Investment Law Nexus Reimagined – Beyond ISDS, Obligations and Instruments to Avoid and to Defend

Marie-Claire Cordonier Segger, Markus Gehring, Ted Gleason and Matheus Garcia

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Executive Summary

This report explores the critical intersection between international investment agreements (IIAs) and climate action, emphasizing the need to reconcile investment protection with climate goals. While IIAs generally prioritize foreign direct investment protection, they risk hindering

ambitious climate policies through mechanisms like investor-state dispute settlement (ISDS). The report critiques broad ISDS clauses, vague investment definitions, and lengthy sunset clauses for their restrictive impacts on states' ability to regulate for climate resilience.

To realign IIAs with climate goals, the report advocates for targeted reforms, including incorporating climate-positive provisions, explicitly supporting renewable energy investments, and phasing out fossil fuel subsidies. Additionally, it highlights the role of robust legal frameworks in mobilizing climate finance, de-risking investments, and fostering international cooperation. The report stresses the importance of integrating environmental considerations across trade and investment frameworks, moving beyond limited Trade and Sustainable Development (TSD) chapters.

The report also examines innovative mechanisms like emissions trading system (ETS) linkages and supply-side crediting, which can address carbon leakage and enhance low-carbon investment. Through pragmatic reforms, IIAs can evolve to support the scale of investment required to achieve the Paris Agreement objectives and a just climate transition.

1. Introduction

The urgency of climate action has placed the intersection of energy transition, green investment, and international investment law at the forefront of global discourse.[1] As countries aim to meet the Paris Agreement goals,[2] the role of private funding in climate change mitigation and adaptation has become increasingly critical. This necessity underscores the importance of leveraging both domestic and international legal frameworks to attract foreign and domestic capital to critical sectors.

[1] United Nations Climate Change, "COP 28: What Was Achieved and What Happens Next?", https://unfccc.int/cop28/5-key-takeaways; Intergovernmental Panel on Climate Change (IPCC), 'Climate Change 2021: The Physical Science Basis'; International Energy Agency (IEA), 'Net Zero by 2050: A Roadmap for the Global Energy Sector'.

[2] See previous CISDL findings on this, Marie-Claire Cordonier Segger, Ilaria Espa, Marios Tokas, Javiera Caceres and Matheus Garcia, Interrelation between Paris Agreement and EU Free Trade Agreements' Commitments: In Search of a Sustainable Path (2024), https://www.cisdl.org/wp-content/uploads/2024/11/CISDL-Paris-Agreement-Paper-1.pdf

International Investment Agreements (IIAs) have sparked significant debate regarding their compatibility with climate ambitions.[3] Well-documented concerns concerning IIAs in the context of the fight against climate change highlight both the restrictive effects of such agreements on domestic climate policies and the risks posed by investor-state dispute settlement (ISDS) mechanisms.[4] At the same time, while IIAs have traditionally focused on investment protection, whether such agreements have the potential to facilitate investment in line with climate ambitions remains underexplored.[5] This report adopts a practical approach that focuses on examples of legal provisions found in IIAs. It explores the existing conflict between IIAs and climate change efforts, while identifying opportunities to reconcile IIAs with climate goals and proposing reforms to enable transformative climate finance while protecting legitimate investor interests. The report delves into contentious provisions, identifies synergies, and evaluates the broader legal landscape to chart a path toward climate-aligned investment frameworks.

2. Climate change and IIAs: Overview

The Paris Agreement, adopted during the 21st Conference of Parties to the United Nations Framework Convention on Climate Change (UNFCCC), represents a global commitment to combat climate change. Its primary goals include limiting the global temperature rise to "well below 2°C above pre-industrial levels", while striving to restrict it to 1.5°C. The agreement aims, among other objectives, to foster climate resilience and ensure that financial flows align with pathways toward low greenhouse gas (GHG) emissions and climate-resilient development.[6] Furthermore, the agreement sets forth additional key goals, including enhancing the capacity of countries to address the consequences of climate change and aligning financial investments with low GHG emissions and a climate-resilient trajectory.[7]

Despite these commitments under the Paris Agreement, IIAs that provide protection to investors in the fossil fuels industries, have the potential to stand in the way of transformative

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[3] See various inputs in the special issue: Sandrine Maljean-Dubois and others, 'International Investment Law and Climate Change: Introduction to the Special Issue' (2022) 23 The Journal of World Investment & Trade 737. Further: Joost Pauwelyn, 'Rational Design or Accidental Evolution? The Emergence of International Investment Law' in Zachary Douglas and others (eds), *The Foundations of International Investment Law* (Oxford University Press 2014).

[4] See:Climate Action Network Europe, 'Briefing on the Energy Charter Treaty' (Climate Action Network Europe Briefing, 2020). Further criticism: Kyla Tienhaara and Christian Downie, 'Risky Business? The Energy Charter Treaty, Renewable Energy, and Investor-State Disputes' (2018) 24 Global Governance 3, 451.

[5] PAGE, 'International Investment Agreements & Sustainable Development: Safeguarding Policy Prace & Mobilizing Investment for a Green Economy.' (United Nations Environment Programme 2018).

[6] UNFCCC, 'Adoption of the Paris Agreement' (2016) FCCC/CP/2015/10/Add.1- Annex at Art. 2(1), Preamble.

[7] Article 2.1(b)-(c) of the Paris Agreement.

climate policies, including in the context of climate financing. This section delves into the complex and often controversial relationship between IIAs and climate change. It begins by examining the primary concerns surrounding the compatibility of IIAs with ambitious climate goals, particularly the potential for these agreements to hinder policy space for environmental regulations and the risks posed by ISDS mechanisms. These concerns highlight the tension between traditional investment protection standards and the urgent need for transformative climate action. Thereafter, this section identifies the potential for increased symmetries between climate ambitions and reformed IIAs.

a) Conflicts of IIA commitments with climate ambitions

IIAs have regularly been criticized as favouring foreign direct investment protection over the promotion of climate-friendly policies.[8] Specifically, concerns persist about the potential for traditional investment protection standards to hinder governments from implementing climate-focused policies, including, *inter alia*, restrictions on fossil-fuel exploration, differential treatment of non-renewable versus renewable market actors, and the phasing out of fossil-fuel infrastructure.[9] An additional major point of criticism against IIAs concerns the capacity of oil and gas companies to sue investment host states for public interest regulatory measures linked to their climate change efforts through the ISDS system, as these firms have long been the most frequent claimants.[10] In light of the frequent use of the ISDS mechanism by fossil fuel investors, it has been considered to be contrary to the 'polluter-pay-principle' as in various cases major polluters have been rewarded, instead of being required to compensate for environmental damage caused.[11]

[8] Kyla Tienhaara, 'Regulatory Chill in a Warming World: The Threat to Climate Policy Posed by Investor-State Dispute Settlement' (2018) 7 Transnational Environmental Law 229; Ivar Alvik, 'The Justification of Privilege in International Investment Law: Preferential Treatment of Foreign Investors as a Problem of Legitimacy' (2020) 31 European Journal of International Law 289.

[9] Lise Johnson and others, 'Aligning Investment Treaties with Sustainable Development Goals Aligning Investment Treaties with Sustainable Development Goals' (2019) 58 Columbia Journal of Transnational Law 58; Nathal Lobel and Matteo Fermeglia, 'Investment Protection and Unburnable Carbon: Competing Commitments in International Investment and Climate Governance' (1.12.2018) 4 Diritto del Commercio Internazionale 945; Lise Johnson, 'International Investment Agreements and Climate Change: The Potential for Investor-State Conflicts and Possible Strategies for Minimizing It' (2009) 39 Envtl L Rep News & Analysis 11147; Vera Korzun, 'The Right to Regulate in Investor-State Arbitration: Slicing and Dicing Regulatory Carve-Outs' (2017) 50 Vanderbilt Journal of Transnational Law 355.

[10] Thomas Waelde and Abba Kolo, 'Environmental Regulation, Investment Protection and "Regulatory Taking" in International Law' (2001) 50 International & Comparative Law Quarterly 811; UNCTAD, 'Treaty-Based Investor-State Dispute Settlement Cases and Climate Action' (IIA Issues Note, 2022).

[11] Flavia Marisi, *Environmental Interests in Investment Arbitration: Challenges and Directions* (Kluwer Law International B V 2020).

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Further, the consistency of ISDS tribunals in interpreting and applying investment protection standards has been a major point of discontent,[12] both in general as well as when the cases refer to the protection of renewable energy investors. The capacity of ISDS tribunals to award private investors significantly high compensation constitutes another point of significant concern.[13] As an example, the highest arbitration award in history awarded a company $50bn USD in total damages against the Russian Federation.[14]

Moreover, IIAs have often been criticized as creating a 'chilling effect', which discourages Host States from introducing climate ambitious policies.[15] Additionally, many have casted doubt on whether IIAs promote foreign investment in any event; contesting the need to introduce such agreements.[16] Therefore, calls to abandon the international investment law regime as it is currently designed have gained prevalence in recent years.[17] Nevertheless, while some States have withdrawn and/or significantly reformed their participation in the international investment law regime,[18] it does not appear that there yet is a widespread appetite among states to fully disengage as IIAs continue to be regularly concluded.[19] At the same time, the form (e.g., as chapters of broader international economic agreements instead of standalone

[12] Jean-Michel Marcoux, 'Banning Oil and Gas Activities under International Investment Law: A Problem of Indeterminacy' (2024) 15 Journal of International Dispute Settlement 351; Lorenzo Cotula, 'International Investment Law and Climate Change: Reframing the ISDS Reform Agenda' (2023) 24 The Journal of World Investment & Trade 766. For an overview of the discussion: Wolfgang Alschner and Wolfgang Alschner, *Investment Arbitration and State-Driven Reform: New Treaties, Old Outcomes* (Oxford University Press 2022).

[13] Kyla Tienhaara and others, 'Investor-State Dispute Settlement: Obstructing a Just Energy Transition' (2023) 23 Climate Policy 1197.

[14] *Yukos Capital Limited v. Russian Federation*.

[15] Kyla Tienhaara, 'Regulatory Chill and the Threat of Arbitration: A View from Political Science' in Chester Brown and Kate Miles (eds), *Evolution in Investment Treaty Law and Arbitration* (Cambridge University Press 2011); Gus Van Harten and Dayna Nadine Scott, 'Investment Treaties and the Internal Vetting of Regulatory Proposals: A Case Study from Canada' (2016) 7 Journal of International Dispute Settlement 92.

Kyla Tienhaara, 'Regulatory Chill and the Threat of Arbitration: A View from Political Science' in Chester Brown and Kate Miles (eds), *Evolution in Investment Treaty Law and Arbitration* (Cambridge University Press 2011); Gus Van Harten and Dayna Nadine Scott, 'Investment Treaties and the Internal Vetting of Regulatory Proposals: A Case Study from Canada' [2016] Journal of International Dispute Settlement.

[16] Bonnitcha Jonathan and others, *The Political Economy of the Investment Treaty Regime*, vol 1 (Oxford University Press 2017); Emma Aisbett, 'Bilateral Investment Treaties and Foreign Direct Investment: Correlation Versus Causation' in Karl P Sauvant and Lisa E Sachs (eds), *The Effect of Treaties on Foreign Direct Investment: Bilateral Investment Treaties, Double Taxation Treaties, and Investment Flows* (Oxford University Press 2009).

[17] Overview: M Sornarajah, *Resistance and Change in the International Law on Foreign Investment* (Cambridge University Press 2015); Martti Koskenniemi, 'It's Not the Cases, It's the System: M. Sornarajah, Resistance and Change in the International Law on Foreign Investment. Cambridge: Cambridge University Press, 2015. Pp. Xx + 437. £80. ISBN 9781107096622.' (2017) 18 The Journal of World Investment & Trade 343.

[18] See for instance India (Prabhash Ranjan, 'India and International Investment Law: Preserving, Delegating, and Reclaiming Sovereignty' (2024) 23 India Review 115). Spain for instance, who experience also many ISDS claims has become increasingly more hostile towards international investment agreements, while US has similarly limited its support for ISDS clauses in the recent years.

[19] See further on policy trends: UNCTAD, World Investment Report 2024 (2024), Ch. I International Investment Trends.

BITs) and substance of IIAs has evolved in recent years. Many of these newer IIAs include provisions that attempt to address the past conflict between broad, unfettered protections for investors and the regulatory sovereignty of host states to pursue public interest measures (including those linked to climate ambitions). While arguments for states to exit the international investment law regime and the ISDS mechanism persist, a tipping point where a critical mass of states in fact heed such calls has not manifested. Thus, the next section will examine whether there exists room for increased synergies between IIAs and states climate goals under the Paris Agreement.

b) Room for Synergies between IIAs and climate ambitions?

While, as addressed in the preceding section, there is significant research critically examining the shortcomings of the international investment law regime, there also exists an important body of literature on the potential positive effects of IIAs in increasing investment and enhancing international cooperation.[20] For example, IIAs have been suggested to operate as important signals for markets indicating that a host state is willing to foster a stable and reliable environment that protects legitimate foreign investments.[21] It has also been argued that IIAs reduce the cost of investing by reducing the political risk associated with investing abroad.[22] Nevertheless, the empirical evidence supporting those suggestions has been scarce and heavily contested, as shown in the previous section.

States, though, have recognised in their NDCs the importance of investment and financing mobilization for climate transition.[23] The arguments raised in the previous paragraph

[20] Marie-Claire Cordonier Segger, 'Integrating Social and Environmental Considerations into Trade and Investment Agreements, for Sustainable Development' in Marie-Claire Cordonier Segger (ed), *Crafting Trade and Investment Accords for Sustainable Development: Athena's Treaties* (Oxford University Press 2021); Anatole Boute, 'Combating Climate Change Through Investment Arbitration' (2012) 35 Fordham International Law Journal 3, 613; Anatole Boute, 'The Potential Contribution of International Investment Protection Law to Combat Climate Change' (2009) 27 Journal of Energy & Natural Resources Law 333.
[21] Alan O Sykes, 'The Economic Structure of International Investment Agreements with Implications for Treaty Interpretation and Design' (2019) 113 American Journal of International Law 482, 482; Nathapornpan Piyaareekul Uttama, 'International Investment Agreements Provisions and Foreign Direct Investment Flows in the Regional Comprehensive Economic Partnership Region' (2021) 9 Economies 1, 28; Karl Sauvant and Lisa Sachs, 'The Effect of Treaties on Foreign Direct Investment: Bilateral Investment Treaties, Double Taxation Treaties and Investment Flows' [2009] Columbia Center on Sustainable Investment Books.
[22] Jeswald Salacuse, 'Of Handcuffs and Signals: Investment Treaties and Capital Flows to Developing Countries' (2017) 58 Harvard International Law Journal 127; Alan O Sykes, 'The Economic Structure of International Investment Agreements with Implications for Treaty Interpretation and Design' (2019) 113 American Journal of International Law 482; Eckhard Janeba, 'Regulatory Chill and the Effect of Investor State Dispute Settlements' (2019) 27 Review of International Economics 1172.
[23] Overview: Sirini Jeudy-Hugo and others, 'Considerations for Informing, Implementing, and Investing in the next Nationally Determined Contributions (NDCs)' (OECD/IEA Climate Change Expert Group Papers, 2024).

provide a perspective for examining how general international commitments affect international finance flows, and the potential role of IIAs, if reformed.[24]

Countries with different views on international investment law regime have recognized the role of investment in the pursuit of climate ambitions.[25] Countries traditionally in favor of IIAs, including ISDS, have long supported the positive synergies between the foreign investment and climate change transition.[26] This perspective has also extended to countries with more critical views of IIAs and ISDS.

Brazil, who is traditionally hostile towards IIAs with broad investment protection provisions and ISDS, in its 2024 NDC mentions the goal of "expanding financing, reducing the cost of credit and improving guarantee and insurance mechanisms for sustainable sectors, projects and practices, such as strengthening the Climate Fund by offering credit at more attractive rates and creating an exchange protection program for investments in ecological transformation".[27] In this context, Brazil has launched the Eco Invest Brasil Program, a specialized initiative designed to mobilize foreign private capital and promote sustainable investments in projects that drive ecological transformation. The program focuses on key areas such as technological densification, the bioeconomy, energy transition, the circular economy, green infrastructure, and climate adaptation. Its objectives include (i) fostering and encouraging investments in these transformative sectors, (ii) mobilizing sustainable foreign private capital to support the country's ecological goals, and (iii) enhancing the development, liquidity, and efficiency of Brazil's long-term foreign currency hedge market.[28]

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[24] This section should not be understood as proposing that old-generation IIAs could synergize positively *as such* with climate transition policies. Rather, the reader should read this section as a theoretical exercise on how the alleged positive effects of IIAs (*in abstracto*, i.e. with or without ISDS, broad protective standards or investor obligations) could co-exist constructively with climate change policies and ambitions.

[25] Countries traditionally in favor of IIAs, including ISDS, have long supported the positive synergies between the investment regime and climate change. See for EU an overview: Communication COM(2021) 66 final from the Commission of 18 February 2021 on Trade Policy Review - An Open, Sustainable and Assertive Trade Policy.

[26] See for EU: Markus Gehring and Marios Tokas, 'Synergies and Approaches to Climate Change in International Investment Agreements: Comparative Analysis of Investment Liberalization and Investment Protection Provisions in European Union Agreements' (2022) 23 The Journal of World Investment & Trade 5–6, 778; Nicolò Andreotti, 'Is EU Investment Policy Fit for Promoting Sustainable Development? Insights from the EU-Angola SIFA' (2024) 2024 9 European Papers - A Journal on Law and Integration 229. For Western Balkans: Michail Dekastros and Marios Tokas, 'Promoting and Protecting Green Investment in Western Balkans: Existing Limitations and Future Opportunities in B. Beaumont et Al. (Eds.), Future of Investor-State Dispute Settlement ISDS' in Ben Beaumont and others (eds), *The Future of Investor-State Dispute Settlement* (Wolters Kluwer 2024).

[27] Brazil Second Nationally Determined Contribution, at 5. Available online: https://unfccc.int/sites/default/files/2024-11/Brazil_Second%20Nationally%20Determined%20Contribution%20%28NDC%29_November2024.pdf (accessed 18 Jan. 2025).

[28] Ministério da Fazenda, Eco Invest Brasil, Available online: https://www.gov.br/tesouronacional/pt-br/fomento-ao-investimento/eco-invest-brasil (accessed 18 Jan. 2024).

Indonesia, with a more moderate approach to IIAs, has similarly established the Environmental Fund Management Agency, tasked with managing and mobilizing environmental financing.[29] This agency is authorized to access climate finance from a wide range of sources, which includes foreign direct investment in addition to national and international channels, private and public funding, and bilateral and multilateral partnerships.[30] Further, Uruguay explicitly mentions that foreign direct investment is a necessity in order to implement its NDCs.[31] Finally, Guatemala, recognizing the need to mobilize international private financing, has updated key investment policies to attract investments in sectors critical for climate transition.[32]

Despite various implementation strategies in line with those discussed above, an important finance gap persists concerning the implementation of existing NDCs.[33] Recent research from the World Economic Forum (WEF) noted that Brazil alone will need an investment of $200 billion (BRL 1 Trillion) to reach its 2030 GHG reduction goals.[34] Thus, whereas states broadly recognize the importance of international investment in the pursuit of their climate ambitions, the extent to which IIAs are capable of contributing to rather than hindering these efforts remains unclear. The present report therefore works not only to clarify the negative impacts that IIAs may have on shaping reliable climate change policies, but also to examine various international commitments that could steer global investment towards a climate-friendly path. In other words, as radical change to the international investment law regime remains elusive, this report attempts to identify policies that must be avoided alongside policies that should be pursued in the current international law context.

3. IIA provisions that exemplify the conflict with climate-ambitious policies

The fragmented network of over 2,600 IIAs contains a wide variety of formulations concerning both substantive investment law mechanisms as well as different approaches to procedural

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[29] Cabinet Secretariat of the Republic of Indonesia, *Gov't Establishses Environmental Fund Management Agency*, Available online: https://setkab.go.id/en/govt-establishes-environmental-fund-management-agency/ (accessed 18 Jan. 2025)

[30] Enhanced NDC - Republic of Indonesia. Available online: https://unfccc.int/sites/default/files/NDC/2022-09/ENDC%20Indonesia.pdf (accessed 18 Jan. 2025).

[31] Uruguay Second NDC. Available online: https://unfccc.int/sites/default/files/NDC/2022-12/Uruguay%20Segunda%20CDN.pdf (accessed 18 Jan. 2025).

[32] Contribución Nacionalmente Determinada de Guatemala(Updated submission). Available online: https://unfccc.int/sites/default/files/2022-06/NDC%20-%20Guatemala%202021.pdf (Accessed 18 Jan. 2024).

[33] Jeudy-Hugo and others (n 20); Vera Songwe and others, 'Finance for Climate Action: Scaling up Investment for Climate and Development' (Report of the Independent High-Level Expert Group on Climate Finance, 2022).

[34] World Economic Forum, 'Finding Pathways, Financing Innovation: Tackling the Brazilian Transition Challenge' (White Paper, 2023).

issues in investor-state disputes.[35] This fragmentation renders the analysis of specific examples tricky. Nevertheless, the protective scope of IIAs, with legally binding investment protection obligations and a binding third-party dispute settlement system, has placed considerable restrains on states, from both financial and regulatory perspectives. Furthermore, the capacity of states to regulate may be put in jeopardy given the threat of a potential lawsuit by a foreign investor. In the field of climate change, such threats have been materialised in the form of proceedings against the decision of states to change the environmental regulatory field,[36] the change in subsidies provided in the energy sector[37] and the phase-out of fossil fuel energy production.[38] The present section will present three key examples of provisions that embody the conflict between investment protection in IIAs and ambitious climate policies, mainly broad ISDS and FET clauses, and lengthy sunset clauses.

a) Broad ISDS clauses

Almost all IIAs contain a clause providing for a private right of action for resolving disputes.[39] These ISDS clauses allow investors to challenge measures taken by the host states allegedly in breach of the IIA directly before investor-state tribunals.[40]

Broad ISDS provisions, which were often drafted prior to the impetus of the current pursuit of climate ambitions, seldom limit the type of claims that may be brought before an arbitral Tribunal.[41] In other words, under many IIAs as long as an investor and investment are covered by the relevant IIA, the investor has the right to instigate proceedings. Depending on the precise wording of the IIA, the foreign investor may avoid also all domestic proceedings concerning the challenged measures. For instance, Article 8 of the Zimbabwe-Czech Republic BIT (1999) provides consent to arbitrate for '[a]ny dispute which may arise between an investor

[35] UNCTAD, World Investment Report 2024 (2024), 65.

[36] See for instance *Vattenfall AB and others v Federal Republic of Germany*, ICSID Case No. ARB/12/12, where arose after Germany's decision to phase out nuclear energy following the Fukushima disaster in 2011. Swedish energy company Vattenfall, which had invested in German nuclear plants, claimed that the abrupt policy shift violated protections under the Energy Charter Treaty (ECT).

[37] See *Eiser Infrastructure Limited and Energía Solar Luxembourg S.à r.l. v. Kingdom of Spain*, ICSID Case No. ARB/13/36 which arose after Spain implemented substantial changes to its renewable energy support scheme, which had initially offered generous incentives to attract foreign investment in the solar energy sector.

[38] *RWE AG v Kingdom of the Netherlands*, ICSID Case No. ARB/21/4.

[39] UNCTAD, 'Investment Dispute Settlement Navigator, UNCTAD' (*Investment Policy Hub*, no date) Available online: https://investmentpolicy.unctad.org/investment-dispute-settlement (Accessed 18 Jan. 2024).

[40] Rudolf Dolzer and Christoph Schreuer, *Principles of International Investment Law* (Second edition, Oxford University Press 2012) 235–44; 'Investor-State Dispute Settlement: A Scoping Paper for the Investment Policy Community' (OECD Working Papers on International Investment, OECD Working Papers on International Investment, 31 December 2012) vol 2012/03.

[41] Vera Korzun, The Right to Regulate in Investor-State Arbitration: Slicing and Dicing Regulatory Carve-Outs (2016) SJD Dissertations. 8, 363.

of one Contracting Party and the other Contracting Party in connection with an investment in the territory of that other Contracting Party'.

Such broad ISDS clauses, together with a broad definition of covered investment, which can include concessions relating to the extraction or exploitation of natural resources as protected qualifying investments, expose states to potential ISDS lawsuits for measures taken in relation to climate change.[42] Arbitral Tribunals have been clear that they could not read limitations to ISDS clauses or definitions of investment and investors that have not been expressly included in the text of the treaty by the parties.[43] Thus, claims brought by fossil fuel companies against climate change measures cannot be dismissed by arbitral tribunals, unless the parties have explicitly provided for limitations. Even in cases where limitations have been introduced, though unrelated to climate change, tribunals have been hesitant to adopt an interpretation that would limit their jurisdiction.[44]

b) Broad investment protection clauses

As previously mentioned, broad clauses included in IIAs have been heavily criticized as states are faced with claims that they did not foresee.[45] The ambiguity of the treaty text is considered the primary reason for the inconsistency and reluctance of Tribunals to accept the relevance of non-economic objectives, such as climate change, in ISDS.[46]

For instance, the Angola-Japan BIT broad expropriation and FET clauses.

> Article 4. General Treatment
> Each Contracting Party shall in its Area accord to investments of investors of the other Contracting Party treatment in accordance with customary international law, including fair and equitable treatment and full protection and security.

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[42] Joshua Paine and Elizabeth Sheargold, 'A Climate Change Carve-Out for Investment Treaties' (2023) 26 Journal of International Economic Law 285.

[43] *Tokios Tokelės v Ukraine, Decision on Jurisdiction* No. ICSID Case No ARB/02/18 para 100.

[44] *Bear Creek Mining Corporation v Republic of Peru, Award* No. ICSID Case No ARB/14/21, para 316 ; The Tribunal in *Phoenix Action v The Czech Republic* did accept a limitation for breach of jus cogens, "[t]o take an extreme example, nobody would suggest that ICSID protection should be granted to investments made in violation of the most fundamental rules of protection of human rights, like investments made in pursuance of torture or genocide or in support of slavery or trafficking of human organ" (*Phoenix Action, Ltd v The Czech Republic, Award* No. CSID Case No ARB/06/5, para 78.

[45] Gehring and Tokas (n 26); Dekastros and Tokas (n 26).

[46] Enrique Boone Barrera, 'The Case for Removing the Fair and Equitable Treatment Standard from NAFTA' (CIGI Paper, Center for International Governance Innovation 27 April 2017); *Sempra Energy International v Argentine Republic, Award* No. ICSID Case No ARB/02/16 (28 September 2007).

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Such broad and vague clauses cause a sharp increase in litigation, even in cases where a states has exercised its right to regulate in a legitimate manner.[47] For instance, in *Tecmed v. Mexico*, a Spanish investor operating a hazardous waste landfill in Mexico invoked the Mexico–Spain BIT and challenged the Mexican authorities' refusal to renew its operating permit.[48] Without much elaboration, the tribunal referred to general principles recognized in international law, and held that FET:

> requires the Contracting Parties to provide to international investments treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment. The foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor.[49]

Such an interpretation of the FET introduces a high burden to states since even minor procedural or substantive errors or inconsistencies could amount to a breach of the FET standard.

Similarly, vague FET clauses allow arbitral tribunals to examine state measures for alleged 'creeping violation of [the] FET standard'.[50] In those instances, even though an individual government action by itself might not amount to a threshold that would breach the treaty obligation, when taking into consideration the 'cumulative effect' of multiple actions, together, they would amount to a breach of the FET standard.[51] This is exemplified in the *Bilcon v Canada* award. The dispute involved a proposal by American investors to operate a quarry and a marine terminal in the Canadian province of Nova Scotia, which was later rejected by the Canadian provincial and national governments on environmental grounds. The tribunal considered that even minor errors or mistakes coupled with certain investors' expectations, would amount to a breach of the FET standard.[52]

c) Lengthy sunset clause

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[47] Alison Giest, Interpreting Public Interest Provisions in International Investment Treaties, Chicago Journal of International Law Vol. 18 N. 1, Article 9 (2017) and Malcolm Langford and Daniel Behn, Managing Backlash: The Evolving Investment Treaty Arbitrator?, European Journal of International Law Vol. 29, Issue 2, (2018).

[48] *Tecnicas Medioambientales TECMED S.A. v. Mex.*, *Award,* ICSID Case No. ARB(AF)/00/2.

[49] Ibid., para. 154.

[50] *El Paso Energy Int'l Co. v. Arg*., ICSID Case No. ARB/03/15, Award, para. 518.

[51] Also see *The Rompetrol Group N.V. v Rom., Award,* ICSID Case No. ARB/06/3, para. 271.

[52] See: *Eco Oro Minerals Corp v Republic of Colombia, Decision on Jurisdiction, Liability and Directions on Quantum* No. ICSID Case No ARB/16/41..

Finally, the chilling effect on the regulatory capacity of IIAs also lies in the fact that lengthy sunset clauses have been put in place by various IIAs.[53] These clauses ensure that certain protections or obligations of the agreement remain in effect for a specified period even after the agreement is terminated.[54] The clause guarantees that investors from one contracting state will continue to enjoy the treaty's protections (e.g., FET, protection against expropriation) for their investments in the other contracting state for a defined period, typically ranging from 5 to 20 years, even if the treaty itself is terminated. For instance, the Economic Community of West African States (ECOWAS) Energy Protocol of 2003 (not in force) has a 20-year sunset clause. Article 42.3 provides:

> The provisions of this Protocol shall continue to apply to Investments made by Investors in the Area of a withdrawing Contracting Party for a period of 20 years from such date of withdrawal.

Many other IIAs, such as Bulgaria-China BIT (1989)[55] and China-Malaysia BIT (1988)[56] have a 15-year sunset clause.

Sunset clauses limit a State's ability to enact new policies or reform its investment framework, even in cases where such reforms are deemed necessary for the public interest.[57] Further, investors may use sunset clauses to bring claims under outdated treaties, potentially leading to costly disputes for the host state.[58] These impose significant burdens upon states that seek to exit from the existing IIA regime and introduce ambitious climate change policies, since any unilateral termination or withdrawal from IIA would still impose constraints on their capacity to regulate.[59]

4. Securing withdrawal or non-application of an IIA

[53] Tania Voon and Andrew D Mitchell, 'Denunciation, Termination and Survival: The Interplay of Treaty Law and International Investment Law' (2016) 31 ICSID Review - Foreign Investment Law Journal 413.

[54] *UP (formerly Le Chèque Déjeuner) and C.D Holding Internationale v Hungary, Award*, ICSID Case No. ARB/13/35 para. 265; *Mohamed Abdel Raouf Bahgat v. Egypt (I) , Decision on Jurisdiction*, PCA Case No. 2012-07 para. 313;

[55] Article 13.1 reads "4 . With respect to investments made prior to the date of termination of this agreement, the provisions of Article 1 to 12 shall continue to be effective for a further period of 15 years from such date of termination."

[56] Article 13(2) reads "(2) This Agreement shall remain in force for a period of 15 years, and shall continue in force, unless terminated in accordance with paragraph 3 of this Article. paragraph 3 of this Article."

[57] See for instance Antonios Kourotakis, Sunset Clauses in International Law and their Consequences for EU Law, Pg.

[58] See cases instigated: https://www.iareporter.com/articles/refinery-group-lodges-trio-of-ect-cases-against-the-european-union-denmark-and-germany/; https://www.iareporter.com/articles/japanese-investors-23-5-million-usd-ect-award-against-spain-comes-to-light/.

[59]See cases on ICSID Denunciation: *Venoklim Holding BV v Bolivarian Republic of Venezuela* , *Award,* ICSID Case No ARB/12/22, para. 62-63; *Rusoro Mining Ltd. v Bolivarian Republic of Venezuela*, *Award,* ICSID Case No. ARB(AF)/12/5.

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In response to the previous considerations, various states have proceeded with IIA reform. However, the process of reform is lengthy and arduous since states do not agree on the precise content and form of the reform.[60] For this reason, to remove the obstacles posed by the existing IIA regime to investment in line with climate ambitions, many states have opted to terminate or withdraw from IIAs.[61] However, such unilateral terminations have no effect on existing ISDS proceedings since the offer to arbitrate cannot be withdrawn unilaterally once an investor has initiated proceedings.[62] Once the agreement to arbitrate has been perfected through the acceptance by the investor of the offer to arbitrate included in the IIA, the consent cannot revoked.[63]

Further, as discussed above, a unilateral termination or withdrawal does not nullify an overly lengthy sunset clause.[64] Rather, the IIA parties need to mutually agree to neutralize such sunset clauses.[65] Such agreements could first take the form of a newly concluded IIA. Such instance, Australia agreed with Hong Kong[66] and Uruguay[67] to terminate older BITs with newer ones that fully replaced them. For instance, Article 40 of the Australia-Hong Kong BIT (2019) reads:

> 2. The Agreement between the Government of Australia and the Government of Hong Kong for the Promotion and Protection of Investments, done at Hong Kong on September 15, 1993 (IPPA) shall terminate on the date of entry into force of this Agreement. From that date, all provisions of the IPPA, including the provisions for termination contained in Article 14 (Entry into Force and Duration and Termination), and any rights or obligations arising from those provisions, shall cease to have effect.

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[60] José E Alvarez, 'ISDS Reform: The Long View' (2021) 36 ICSID Review - Foreign Investment Law Journal 253.

[61] Nathalie Bernasconi-Osterwalder, Sarah Brewin, Martin Dietrich Brauch and Suzy Nikièma, IISD Best Practices Series: Terminating a Bilateral Investment Treaty (2020), https://www.iisd.org/system/files/publications/terminating-treaty-bestpractices-en.pdf; Martin Dietrich Brauch, 'Should the European Union Fix, Leave or Kill the Energy Charter Treaty?' (SSRN Scholarly Paper, 2 January 2021).

[62] *Inceysa Vallisoletana S.L. v Republic of El Salvador, Award*, ICSID Case No. ARB/03/26, para. 167; *Compagnie d'Exploitation du Chemin de Fer Transgabonais v Gabonese Republic, Excerpts of Decision on Jurisdiction*, paras. 22-24; *Lanco International Inc. v The Argentine Republic Award on Jurisdiction*, ICSID Case No. ARB/97/6 para. 41.

[63] Arthur Lauvaux, 'Towards a Bumpy Ride into the Sunset: On the Mutual Termination of IIAs and Their Sunset Clauses' (2022) 38 Arbitration International 203; CH Schreuer, 'Consent to Arbitration (Updated 02/2007)' (2005) 2 TDM.

[64] Tania Voon and Andrew D Mitchell, 'Denunciation, Termination and Survival: The Interplay of Treaty Law and International Investment Law' (2016) 31 ICSID Review - Foreign Investment Law Journal 413.

[65] Lauvaux (n 63).

[66] See Australia-Hong Kong Investment Agreement (2019) which replaces the Australia-Hong Kong, China SAR BIT (1993).

[67] Australia-Uruguay BIT (2019) which replaces the Australia-Uruguay BIT (2001).

Second, the parties could mutually agree to terminate the BITs with an agreement to neutralize their sunset clauses. Notably, a majority of the EU pursued this approach when signed a Termination Agreement[68] – a multilateral treaty between 23 EU Members – to end their BITs and with them their respective sunset clauses. Article 2.2 reads "[f]or greater certainty, Sunset Clauses of Bilateral Investment Treaties listed in Annex A are terminated in accordance with paragraph 1 of this Article and shall not produce legal effects", thus ending sunset clauses of the intra-EU BITs that were in force at the time of the signing of the Termination Agreement. Additionally, Article 3 of the Agreement terminates the sunset clauses of previously terminated intra-EU BITs.[69] This approach was also observed in the case of the exchange of notes (note verbale) between Czech Republic and Denmark, Italy, Malta and Slovenia which outlined their mutual agreement to terminate their relevant BITs.[70] It should be noted though that it is debatable whether this approach may or not be extended to inter-se agreements of parties to a multilateral IIA.[71] International treaty law, as enshrined in the Vienna Convention of the Law of Treaties (VCLT), promotes the stability of treaty relations and imposes significant constraints on the capacity of states to introduce inter-se agreements in multilateral agreements.[72]

Nevertheless, most IIAs are bilateral in nature, thus, reducing the negotiation risks associated with a termination agreement. Still, to date, no claims have been based on a neutralized survival clause, and no arbitral tribunal has thus been confronted with the question of jurisdiction in such circumstances.[73] Thus, it is still uncertain whether arbitral tribunals will uphold or reject jurisdiction because of neutralization.

a) Provisions promoting climate finance in IIAs

[68] Agreement for the termination of Bilateral Investment Treaties between the Member States of the European Union (2019) https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:22020A0529(01).
[69] Article 3 reads "Sunset Clauses of Bilateral Investment Treaties listed in Annex B are terminated by this Agreement and shall not produce legal effects, in accordance with the terms set out in this Agreement."
[70] Italy (30 April 2009), Denmark (18 November 2009), and Malta (30 September 2010). Available online: https://investmentpolicy.unctad.org/international-investment-agreements.
[71] See overview for ECT: Marios Tokas, 'The Graduate: The E.U. and Its Member States' Exit from the Energy Charter Treaty' (2024) Online Perspectives Harvard International Law Journal.
[72] Article 41VCLT governs such agreements. See discourse on the matter: https://www.iisd.org/itn/en/2021/06/24/energy-charter-treaty-reform-why-withdrawal-is-an-option/#_ftnref23; and https://arbitrationblog.kluwerarbitration.com/2023/06/19/an-inter-se-modification-of-the-ect-to-exclude-intra-eu-arbitration-how-can-it-work/
[73] See Johannes Tropper, 'The Treaty to End All Investment Treaties: The Termination Agreement of Intra-EU BITs and Its Effect on Sunset Clauses' [2020] Völkerrechtsblog.

At this stage, the report focuses on IIA provisions that could potentially incentivize and synergize with the need to scale-up climate finance to reach the USD 1.3 trillion on green financing from private and public sources as agreed in the UNFCCC Conference of the parties in Baku in 2024.[74] Despite the various implementation strategies pursued by states around the world, studies have shown that clear finance targets and ambitious goals provide a reliable roadmap for private investors to look at as reference.[75] These goals should be sectoral-specific and align with general climate and economic strategies. Further, stability and predictability of policy and regulatory environment are critical, as well as accountable reporting and monitoring mechanisms.[76] For instance, Madagascar has clarified that all foreign direct investment should take into account climate risks and vulnerabilities.[77] It has set targets with regards to sanitary infrastructure (related to climate-sensitive diseases), investment in fair supply chains and water control. Similarly, Panama has provided its NDC implementation costs in order to prescribe the precise needs for private investments.[78] In the same vein, Antigua and Barbuda, and Belize have adopted a clear NDC implementation strategy that identifies key sectors where private investment is required.[79] Still, an immense financing gap remains in implementing existing NDCs.[80] By way of example, recent research from the WEF, noted that Brazil alone will need an investment of USD $200 billion (BRL 1 Trillion) to reach its 2030 GHG reduction goals.[81]

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[74] Overview of the New Collective Quantified Goal on Climate Finance here: https://unfccc.int/NCQG.

[75] Investor Group on Climate Change, 'Making NDCs Investable – the Investor Perspective' (Policy Brief, 2024); United Nations Development Programme, 'Steps Ahead: Leveraging Nationally Determined Contributions (NDCs) to Achieve Net-Zero, Emissions and Climate-Resilient Development, in Response to the Climate Emergency' (2022); United Nations Development Programme, 'Engaging Private Sector in NDC Implementation - Assessment of Private Sector Investment Potential in the Agriculture Sector' (NDC Private Sector Engagement Project, 2020)..

[76] Laia Barbarà, '5 Ways NDCs Can Become Private Climate Finance Catalysers' (Climate Action. WEF, 2024); Molly Caldwell and others, 'Paying for the Paris Agreement: A Primer on Government Options for Financing Nationally Determined Contributions' [2022] World Resources Institute; Emily McGlynn and others, 'Addressing Uncertainty and Bias in Land Use, Land Use Change, and Forestry Greenhouse Gas Inventories' (2022) 170 Climatic Change.

[77] NDC 2 Madagascar. Available online: https://unfccc.int/sites/default/files/NDC/2024-01/NDC%202%20MADAGASCAR.pdf (accessed 18 Jan 2025).

[78] Panama Second NDC. Available online: https://unfccc.int/sites/default/files/NDC/2024-06/Segunda%20Contribuci%C3%B3n%20Determinada%20a%20Nivel%20Nacional_CDN2.pdf (accessed 18 Jan 2025).

[79] See the projects online: https://ndcpartnership.org/news/advancing-ndc-implementation-antigua-barbuda-through-investment-planning-and-private-sector; https://ndcpartnership.org/news/lessons-belizes-ndc-investment-planning-integrated-approach-accessing-climate-finance (accessed 18 Jan 2025).

[80] Sirini Jeudy-Hugo and others, 'Considerations for Informing, Implementing, and Investing in the next Nationally Determined Contributions (NDCs)' (OECD/IEA Climate Change Expert Group Papers, 2024); Vera Songwe and others, 'Finance for Climate Action: Scaling up Investment for Climate and Development' (Report of the Independent High-Level Expert Group on Climate Finance, 2022).

[81] World Economic Forum, 'Finding Pathways, Financing Innovation: Tackling the Brazilian Transition Challenge' (White Paper, 2023). Similar gaps have been identified for India (IEA, World Energy Investment 2024 (2024) IEA, Paris) and for African countries (See Report by African Development Bank Group, Available

In the following sub-sections, this report will offer a few key emerging provisions in IIAs which create potentially positive synergies with NDC implementation and the promotion of private financing in line with climate ambitions, that could be included in future agreements.

b) Positive investment promotion commitments for renewable energy to support NDCs

One emerging approach is for IIA parties (whether a traditional BIT, or other treaty with investment provisions such as a regional FTA) to agree on positive commitments either on both sides or on one side (e.g. in North-South Agreements) related to the promotion of foreign investment in renewable energy to support NDCs. Investment promotion provisions could either include specific targets for foreign investment flows or provide assurances for financing of specifically identified projects. For instance, the EU-Singapore FTA provides in Article 12.11 that the parties "shall pay special attention to facilitating the removal of obstacles to trade or investment concerning climate-friendly goods and services, such as sustainable renewable energy goods and related services and energy-efficient products and services, including through the adoption of policy frameworks conducive to the deployment of best available technologies".[82] The formulation of obligations in this context goes beyond merely requiring parties "to pay special attention to" increasing these types of investment flows (e.g., "the parties shall facilitate"). This general commitment can be further operationalized and strengthened through specific binding commitments made in later institutional decisions, such as those by potential Joint Councils (such as the Board on Trade and Sustainable Development contemplated by Art. 12.15 of the EU-Singapore FTA).[83]

In case of stronger alignment, the parties could explicitly agree on specific financing targets. The recent European Free Trade Association (EFTA)-India Free Trade Agreement sets specific targets for foreign direct investment from EFTA countries to India within a 10-year (plus 5) period.[84] The parties have identified specific requirements with regards to the quality of those investments and their anticipated effects to the Indian economy.[85] The crucial part is that India is allowed to take temporary and proportionate remedial measures to rebalance the concessions given to the EFTA States, if the investment promotion targets are not met.[86] The

online:https://www.afdb.org/en/topics-and-sectors/sectors/climate-change/action-plan-climate-change?utm_source=chatgpt.com)

[82] Free trade Agreement between the European Union and the Republic of Singapore 2019 (OJ L 294) 3.

[83] Markus Gehring and others, *Evaluating Post-Treaty Options in EU FTAs for Promoting More Ambitious Sustainability Commitments* (Centre for International Sustainable Development Law 2024).

[84] Article 7.1 EFTA-India Free Trade Agreement.

[85] Article 7.3 EFTA-India Free Trade Agreement.

[86] Article 7.8, EFTA-India Free Trade Agreement.

parties, thus, could opt for a renewable energy promotion target with specific goals, timelines and potential repercussions in case of non-fulfilment.

An additional approach consists of the parties agreeing on a list of investment financing projects that would primarily be financed by private parties and, in case of failure, by the government of the developed State. For instance, the EU-Kenya Economic Partnership Agreement (EPA) introduces a resource mobilization commitment, with the objective of supporting "the efforts of [East African Communities] Partners States in pursuing alternative sources of funding to support regional integration and the development strategies".[87] The EPA includes an elaborate Annex on Development Investment projects. Specifically, the EU commits to funding or finding alternative sources for the listed investment projects., such as financing the construction of the Rusizi IV hydro power plant in Rwanda and Burundi (500 mil USD). The Annex includes clear development benchmarks, targets and indicators, including the increase of renewable energy production in the short, medium and long term (3, 5 and 10 years respectively).

Provisions and annexes such as those included in EU-Kenya EPA should be linked with planned investments in the NDCs or finance essential infrastructure that will mobilize further investment. The parties could opt to schedule precise financing projects that are mentioned in the relevant NDCs.

In sum, IIAs can play a pivotal role in promoting foreign investment in renewable energy by including positive commitments tailored to support NDCs. These commitments could range from general obligations to facilitate investment in climate-friendly goods and services, to specific financing targets and timelines, or even targeted projects. By adopting flexible mechanisms such as institutional follow-ups, specific investment goals, and resource mobilization commitments, the Parties can ensure alignment with relevant climate objectives. Linking these provisions to planned investments in NDCs and critical infrastructure further enhances their effectiveness, fostering both environmental and economic progress.

c) Securing policy space for promoting and protecting green investments

Even when states conclude reformed versions of IIAs, where substantive IIA standards are present, states must ensure that they have the policy space to promote and protect investments in line with climate ambitions in order to mitigate regulatory chill as described in previous

[87] Research Mobilization: Article 101.2 of the EU-Kenya Agreement.

sections.[88] While a broader discussion of preserving the right to regulate in the international investment law regime is beyond the scope of this report, various emerging approaches that have the potential to work towards this objective in the context of investment in line with climate ambitions warrant specific mention.

One approach to encouraging investment in renewable energy is through subsidies provided to companies engaged in such initiatives. However, subsidies could be perceived as discriminatory under IIAs,[89] or potentially breaching other substantive standards.[90] To address this concern, states can incorporate explicit provisions within their IIAs to exempt specific investors or investments, such as those related to renewable energy, from the treaty's scope. This allows host States to retain greater discretion in exercising their regulatory authority in this area. For instance, Article 14 of the Investment Protection chapter of the Draft EU-Mexico Free Trade Agreement (FTA) clarifies:

> 2. For greater certainty, nothing in this Section shall be construed as preventing a Party from discontinuing the granting of a subsidy[original footnote 15] or requesting its reimbursement, where such action has been ordered by a competent court, administrative tribunal or other competent authority, or as requiring that Party to compensate the investor therefor.
> 3. For greater certainty, a Party's decision not to issue, renew or maintain a subsidy or grant
> (a) in the absence of any specific commitment under law or contract to issue, renew, or maintain that subsidy or grant; or
> (b) in accordance with any terms or conditions attached to the issuance, renewal or maintenance of the subsidy or grant, or
> (c) in accordance with paragraph 2;
> does not constitute a breach of the provisions of this Section.[91]

States may further explicitly allow for differentiation between investments that contribute to climate ambitions and those do not, as well as those which hinder such ambitions.[92] By doing so, States retain the regulatory space to adopt policies that discourage certain investments and encourage others. Some IIAs have included an explicit clarification in

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[88] See further: Ted Gleason and Catharine Titi, 'The Right to Regulate' (Academic Forum on ISDS Concept Paper, 2022).

[89] It was claimed in *Sergei Paushok, CJSC Golden East Company and CJSC Vostokneftegaz Company v The Government of Mongolia*; *United Parcel Service of America Inc. v Government of Canada*, ICSID Case No. UNCT/02/1.

[90] See: *SolEs Badajoz GmbH v Kingdom of Spain, Award*, ICSID Case No. ARB/15/38, para 308; *Eurus Energy Holdings Corporation v Kingdom of Spain*, Decision on Jurisdiction and Liability, ICSID Case No. ARB/16/4; *Sevilla Beheer B.V. and others v Kingdom of Spain*, Decision on Jurisdiction, Liability and the Principles of Quantum, ICSID Case No. ARB/16/27.

[91] *Draft EU-Mexico Agreement-Agreement in principle of 21.04.2018.*

[92] Gehring and Tokas (n 26).

the text of their IIAs that the ‘likeness’ test in non-discrimination provisions encompasses an examination of, among other things, the investment’s effects on the local community or the environment. For instance, Article 12 of the AfCFTA Investment Protocol states:

> 2. In assessing "in like circumstances" an overall examination is required on a case by-case basis, of all the circumstances of an investment, including, among others:
>
> a. its effects on third persons and the local community;
>
> b. its effects on the local, regional or national environment, the health of the populations, or on the global commons;
>
> c. the sector in which the investor is active; d. the aim of the measure in question; e. the regulatory process generally applied in relation to a measure in question; and
>
> f. any other factor directly relating to the investment or investor in relation to the measure in question.

By doing so, States hope to avoid discrimination claims arising out of the preferential treatment of climate-friendly investments. Such clauses may refer to carbon intensity as a criterion of likeness in order to be able to afford better competitive and investment conditions for investments in less carbon-intense industries. For example, Article 17 of the COMESA Investment Agreement explicitly mentions that the effects on the environment are to be taken into account for determining like circumstances.

In summary, to ensure the promotion and protection of investments in line with climate ambitions within the framework of IIAs, states must preserve sufficient policy space to support sustainable initiatives. This can potentially be achieved by *inter alia* incorporating explicit exemptions for discrete categories of investments, clarifying the scope of subsidies, and refining the interpretation of non-discrimination provisions to account for environmental impact. By embedding such safeguards, states maintain their regulatory autonomy to pursue measures encouraging investments that sustainably support climate change efforts.

d) Investment regulation and fossil fuel subsidies

An additional approach that could be implemented by states to avoid stranding scarce public spending in an industry that will be rendered obsolete by the need to address the climate emergency is to commit to international cooperation in exploring options for swapping subsidies away from fossil fuels and into renewable energy. Currently, only a few international

agreements provide positive commitments to reducing such fossil fuel subsidies.[93] For example, the UK-New Zealand FTA, which include investment protection and promotion standards without ISDS clauses, introduces binding commitments on both parties to eliminate harmful fossil fuels. Article 22.8, titled 'Fossil Fuels Subsidy Reform and Transition to Clean Energy', notes that the parties should take steps to eliminate harmful fossil fuel subsidies, unless there is a legitimate public policy objective. It further requires that parties end unabated coal-fired electricity generation in their territories as part of a clean energy transition and end new direct financial support and international aid funding to fossil fuel energy non-parties, with limited exceptions.

In addition to IIAs, the recently concluded Agreement on Climate Change, Trade, and Sustainability (ACCTS), signed by Costa Rica, Iceland, New Zealand, and Switzerland, marks the first international accord to contain specific prohibitions on fossil fuel subsidies.[94] The ACCTS establishes commitments for participating States to implement a minimum net pricing framework for fossil fuels, incorporating carbon pricing, certain energy taxes, and subsidies under the "Standardised Carbon Rate Measurement" (SCRM). It bans all types of coal subsidies while allowing parties to identify subsidies they intend to retain, subject to a standstill agreement prohibiting expansion and a commitment to their gradual reduction.[95]

The inclusion of explicit commitments to phase out fossil fuel subsidies and promote renewable energy within international agreements such as the ACCTS and the UK-New Zealand FTA sets a critical precedent for aligning investment and trade policies with climate objectives. These agreements demonstrate that international cooperation can be effectively leveraged to transition away from fossil fuels, redirect public spending towards sustainable energy, and embed environmental obligations within broader economic frameworks. To address the urgency of the climate crisis, states should either join the ACCTS or adopt similar provisions in trade and investment agreements, ensuring that environmental sustainability is integral to global economic policies.

e) Positive environmental commitments in IIAs

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[93] Marios Tokas, 'Highest Priority Trade Provisions Related to Sustainable Development and Climate Change: Streamlining Climate Change Commitments in Horizontal Chapters of EU-Americas FTAs' (2023) 50 Legal Issues of Economic Integration 263.

[94] See Chapter 4 of the ACCTS and IISD, Agreement on Climate Change, Trade and Sustainability: A landmark pact for trade and sustainability (2024) https://www.iisd.org/articles/deep-dive/agreement-climate-change-trade-and-sustainability-landmark-pact-trade-and (accessed 18 Jan. 2025)

[95] Article 4.5.1 ACCTS.

New-generation international agreements with investment protection provisions have started to include positive commitments of states on environmental protection. International trade agreements, including those with investment liberalization obligations, include commitments of States to effectively implement multilateral environmental treaties, including the Paris Agreements and the NDCs,[96] and prohibiting lowering the level of protection in terms of environmental obligations in order to incentivize foreign investment (non-regression obligations).[97]

In case of pure investment protection agreements, the Nigeria-Morocco BIT and the African Continental Free Trade Agreement (AfCFTA) Investment Protocol have incorporated investment and environment protection clauses within the agreement.[98] Such clauses provide guarantees to preserve the levels of labour, social and environmental protection, notwithstanding investment promotion.[99] Such clauses should operate to inform the interpretation of all relevant investment protection standards and reaffirm the applicability of police powers doctrine.[100]

5. Ensuring public and private finance for climate change in international accords

The present section provides an overview of the critical role of public and private finance in achieving climate goals and underscores the necessity of aligning IIAs and trade frameworks with climate objectives. As the global climate finance gap remains a significant barrier to meeting the targets of the Paris Agreement, this section explores legal and policy mechanisms to mobilize and de-risk investments, particularly in developing countries. By examining the interplay between international and domestic laws, emissions trading systems (ETS), and innovative financing strategies, the section aims to identify pathways for fostering a robust and inclusive financial architecture that supports climate resilience and low-carbon transitions.

These actions are particularly important given the recent advisory opinion by the International Tribunal for the Law of the Sea (ITLOS) marks a pivotal moment in the intersection of climate change and international law, particularly regarding the obligations of states under the United

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[96] See special issue: Marie-Claire Cordonier Segger and others, '"Trade and Sustainability in EU-Americas Trade Relations"' (2023) 50 Legal Issues of Economic Integration.
[97] Andrew D Mitchell and James Munro, 'An International Law Principle of Non-Regression from Environmental Protections' (2023) 72 International & Comparative Law Quarterly 35.
[98] See Articles 13 and 15 Nigeria-Morocco BIT and Articles 25-26 of the AfCFTA Investment Protocol
[99] See for instance Article 10 Colombia - United Arab Emirates BIT (2017).
[100] Jorge Vinuales, *Foreign Investment and the Environment in International Law* (Cambridge University Press 2012) 363–65.

Nations Convention on the Law of the Sea (UNCLOS). For the first time, an international judicial body has clarified that states have a legal duty to mitigate climate change impacts on the marine environment, reinforcing the interpretation that greenhouse gas (GHG) emissions qualify as marine pollution under UNCLOS. This opinion strengthens the legal basis for holding states accountable for failing to reduce emissions and provides a framework for future climate litigation and policy-making. By emphasizing the binding nature of environmental obligations, ITLOS not only reinforces global efforts to protect ocean ecosystems but also sets a precedent that could influence other international courts and tribunals in shaping climate governance.

a) Summary of proposals for IIAs and ISDS

To address the challenges posed by IIAs and ISDS mechanisms in advancing climate goals, it is essential to avoid broad ISDS clauses and vague investment definitions that enable claims against legitimate climate measures, overly long sunset clauses that restrict regulatory space post-termination, and unrestricted FET clauses that prioritize investor expectations over public interest regulations. Recognizing the ‘spaghetti bowl’ of thousands of IIAs with inconsistent provisions, we have proposed realistic clauses that should necessarily be added to ensure climate-aligned BITs, clarifying, though, that many of these clauses remain untested in practice. While reforms are essential for long-term alignment with climate goals, their direct impact on scaling climate finance at the level required for the NCQG will likely be limited, necessitating complementary strategies beyond IIAs.

b) Key recommendations for Trade and Investment provisions in international accords

The necessity to stimulate private finance in line with climate ambitions points towards the inclusion of bilateral avenues such as Clean Trade and Investment Partnerships (CTIPS) that actively incentivize green investments, such as commitments to renewable energy targets, mechanisms to mobilize private capital for climate projects, and safeguards to protect regulatory space for climate policies. In trade agreements, climate ambition should not be confined to Trade and Sustainable Development (TSD) chapters;[101] instead, treaties should integrate climate-positive provisions throughout, including tariff preferences for environmental goods, targeted subsidy provisions, climate-aligned government procurement rules, and

[101] Tokas (n 93).

intellectual property frameworks that facilitate green technology transfer.[102] Further exploration is required to develop comprehensive and actionable strategies for embedding these provisions effectively into trade and investment frameworks.

A key aspect to evaluate is the impact of prohibiting local content requirements in trade and investment agreements on building domestic political support for climate change initiatives. The WTO Trade-Related Investment Measures (TRIMs) Agreement imposes national treatment obligations[103] and prohibits investment measures that mandate local content requirements, including those implemented through subsidies, taxes, or other incentives.[104] These restrictions have significant implications for the effectiveness and political feasibility of domestic climate change policies.[105] Notably, the TRIMs Agreement has restricted states from introducing subsidies or granting preferential treatment to industries that utilize local renewable energy sources.[106] Although the general exceptions under Article XX of the GATT 1994 provide some flexibility,[107] invoking these exceptions can prove to be an onerous process for states.

Under IIAs, such measures are similarly prohibited by the so-called 'performance requirements' clauses. Few IIAs, though, such as the Canada - Guinea Bilateral Investment Treaty (2015) clarify that performance requirements regarding the use of a technology to meet generally applicable environmental requirements are not inconsistent with the relevant prohibition of performance requirements.[108] Hence, countries may impose performance requirements with regards to the environmental impact of investment projects. This approach should be extended to other investment and trade accords.

c) Unilateral trade and investment measures and climate change

[102] See further: CISDL, Highest Priority Trade Challenges Related to Climate Change: EU and Americas Economic Law Relations (2022). Available online: https://www.cisdl.org/wp-content/uploads/2022/11/EU-Americas-Synthesis-Report-Nov-2022.pdf.
[103] Article 2 of the *Agreement on Trade-Related Investment Measures (TRIMS)*, 1994.
[104] See the Annex of TRIMS.
[105] Panel Report, *Indonesia – Certain Measures Affecting the Automobile Industry*, para. 14.73.
[106] See: Panel Report, *Canada - Certain Measures Affecting the Renewable Energy Generation Sector, Canada - Measures Relating to the Feed-In Tariff Program* and Panel Report, *India - Certain Measures Relating to Solar Cells and Solar Modules.*
[107] Panel Report, *India - Certain Measures Relating to Solar Cells and Solar Modules,* 7.1888.
[108] Article 9.2.

Carbon pricing mechanisms, including ETS and carbon taxes, have gained prominence as effective tools to internalize the social cost of carbon emissions and drive investment in low-emission technologies.[109] By April 2023, 73 such systems were operational, covering 23% of global greenhouse gas (GHG) emissions.[110] Countries without carbon pricing should explore these mechanisms as viable policy options, while those with existing systems should collaborate on measures like Border Carbon Adjustments (BCAs) to prevent carbon leakage and offshoring.[111] Responses to the EU's Carbon Border Adjustment Mechanism (CBAM) have varied; China's muted reaction reflects its cooperation with the EU on emissions trading, enhancing its access to European markets. [112] Countries like Turkey, Morocco, and the Western Balkans view CBAM as a catalyst for decarbonization to align with EU market standards.[113]

Brazil provides an interesting case study concerning CBAM-aligned carbon pricing strategies, in light of the recently concluded EU-Mercosur FTA and its hosting of the next UNFCCC Conference of the Parties. For Brazil, adopting a CBAM-aligned carbon pricing strategy, such as an emissions cap or carbon tax announced at events like the Belém summit, would require embedding social externalities into economic frameworks. This could position Brazil competitively in global markets while incentivizing climate finance and green investment.

The recently concluded EU-Mercosur FTA demonstrates how climate ambition is directly linked with trade competitiveness.[114] The parties agreed that unilateral environmental measures, which could include CBAM,[115] could trigger a rebalancing procedure that leads to suspension of concessions in order to avoid negative trade effects.[116] On the other hand,

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[109] CCSI, Event Highlights: Carbon Border Adjustments in the EU, the U.S., and Beyond: Economic, Legal, Political, and GHG Accounting Aspects, CCSI Past Event on November 19, 2021, https://ccsi.columbia.edu/content/event-highlights-carbon-border-adjustmentseu-us-and-beyond

[110] World Bank, State and Trends of Carbon Pricing 2023 (World Bank, 2023), http://hdl.handle.net/10986/39796.

[111] Aaron Cosbey and others, 'Developing Guidance for Implementing Border Carbon Adjustments: Lessons, Cautions, and Research Needs from the Literature' (2019) 13 Review of Environmental Economics and Policy 3.

[112] Christopher Kardish et al, 'The EU Carbon Border Adjustment Mechanism (CBAM) and China: Unpacking Options on Policy Design, Potential Responses and Possible Impacts' (Adelphi, 2021).

[113] Pieter Pauw and others, 'The CBAM Effect: How the World is Responding to the EU's New Climate Stick' (Clingendael Alert, Netherlands Instittue of International Relations 05.2022); Sonja Risteska and others, 'The EU's Carbon Border Adjustment Mechanism: Challenges and Opportunities for the Western Balkan Countries' (01.2022).

[114] Not yet ratified.

[115] Seems to be disputed between the parties. See report by Veblen Institute, Available online: https://www.veblen-institute.org/Key-Insights-into-the-Final-EU-Mercosur-Agreement.html.

[116] Further on such measures: Marios Tokas, 'Rebalancing Trade and Sustainability Scales Via FTA Reviews' (*IISD:SDG Knowledge Hub*, 20 June 2022) <https://sdg.iisd.org/commentary/generation-2030/rebalancing-trade-and-sustainability-scales-via-fta-reviews/>.

however, Clean Trade and Investment Partnerships (CTIP) can also provide a different avenue – via a bilateral approach – to fill the gaps on the shortcomings of the recently announced version of the EU-Mercosur FTA. Further exploration is needed to assess the feasibility and implications of such a move.

d) International and domestic laws and policies to de-risk climate investments in developing countries

While the present report has examined the relevance of IIAs on climate financing and investment, climate finance aligned with global ambitions can thrive without relying on these instruments. De-risking climate investments in developing countries further requires robust legal and regulatory frameworks that attract and sustain climate finance from both public and private sectors.[117] National frameworks should encompass mechanisms such as in-country climate funds, domestic financial regulations, and corporate taxation legislation to create an environment conducive to climate investments. Achieving "legal readiness" involves integrating mutually supportive financial mechanisms and regulatory modalities tailored to local contexts, addressing mitigation and adaptation needs within urgent timeframes. Regulatory mapping and reform, supported by financial and technical capacity-building, are crucial for this process. Multilateral financial institutions (MFIs) also play a pivotal role in providing the necessary support for such reforms, ensuring sustained investor engagement and fostering systemic transformation.[118]

Globally, implementing the Paris Agreement's objectives demands mobilizing climate finance through coherent jurisdictional legal architectures that align national and international regulatory efforts.[119] While corporate disclosure regulations have been a focal point, they are insufficient alone to drive systemic change or mainstream finance in line with climate ambitions. A pluralistic regulatory approach—integrating financial mechanisms and facilitative modalities—is necessary to achieve the broader objectives of the Paris

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[117] Megan Bowman, 'Turning Promises into Action: "Legal Readiness for Climate Finance" and Implementing the Paris Agreement' (2022) 16 Carbon & Climate Law Review 41.
[118] Megan Bowman and Webster Emily, 'Legal Creativity and Private Financing to Implement the Paris Agreement in the United Kingdom' in *Routledge Handbook of Climate Law and Governance* (Routledge 2024).
[119] Megan Bowman, 'Sustainable Finance and Implementing the Paris Agreement: The Key Role of Jurisdictional Legal and Regulatory Architecture' in René Smits (ed), *Sustainable Finance and Climate Change* (Edward Elgar Publishing 2024).

Agreement.[120] International cooperation among states is vital for aligning investment governance with climate goals, including addressing intellectual property, technology transfer, and data governance. Establishing independent advisory bodies to oversee the implementation of climate-aligned investment policies could further strengthen global-to-local frameworks, ensuring a comprehensive and actionable approach to climate finance governance.

e) International and domestic laws and policies or mechanisms for linking ETS even if they have different scopes and ambitions

Another critical element with regards to global climate action and climate financing is he development and integration of ETS, which offer market-based solutions to reduce greenhouse gas emissions and mobilize resources for decarbonization efforts.

Linking ETS across jurisdictions with differing scopes and ambitions presents both challenges and opportunities for achieving more harmonized global carbon pricing.[121] In the absence of a binding multilateral agreement, reconciling national and regional carbon pricing mechanisms is essential to maintain consistent pricing pressures and prevent competitive distortions in global markets.[122] Innovations like supply-side crediting mechanisms can complement existing climate policies by incentivizing non-extraction of fossil fuels, creating revenue streams for low-carbon technologies, and addressing socioeconomic impacts of the energy transition.[123] Such mechanisms can help overcome entrenched political economy barriers to climate ambition by making carbon pricing more politically viable and enabling broader stakeholder buy-in for decarbonization efforts.[124]

Successful ETS linkages require robust accounting frameworks, as outlined in Article 6 of the Paris Agreement, to ensure transparency, credibility, and fungibility of carbon units across jurisdictions.[125] While minimum harmonized rules can facilitate linkages, mechanisms

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[120] Michael A Mehling and others, 'Linking Heterogeneous Climate Policies (Consistent with the Paris Agreement).' (2019) 8 Environmental Law 647.

[121] Alice Pirlot, 'Carbon Border Adjustment Measures: A Straightforward Multi-Purpose Climate Change Instrument?' (2022) 34 Journal of Environmental Law 1, 25.

[122] Samuel Kortum and David Weisbach, 'The Design of Border Adjustments for Carbon Prices' (2017) 70 National Tax Journal 421; Susanne Dröge and Simone Cooper, 'Tackling Leakage in a World of Unequal Carbon Prices: A Study for the Greens/EFA Group' (05.2010).

[123]Michael A Mehling, 'Supply-Side Crediting for Accelerated Decarbonization: A Political Economy Perspective' [2023] Cambridge Working Papers in Economics.

[124] Goran Dominioni and Alessandro Monti, Internalizing Climate Externalities from Internationally Traded Goods: Challenges and Way Forward for Border Carbon Adjustment Mechanisms (SSRN, March 2023).

[125] Mehling and others (n 118).

such as qualitative and quantitative restrictions are essential to address environmental integrity and governance concerns. In regions like Asia and the Pacific, political and institutional barriers—such as fears over sovereignty loss and lack of trust between partners—remain significant challenges.[126] Early stakeholder engagement, transparent policymaking, and rigorous environmental and economic impact assessments are critical to building mutual trust and fostering long-term cooperative carbon market linkages. These efforts can support the development of a more integrated and equitable global carbon market that drives meaningful climate action.[127]

6. Conclusion

Reforming IIAs to align with climate priorities is essential for addressing the twin imperatives of investment protection and environmental sustainability. Targeted provisions supporting renewable energy, phasing out fossil fuel subsidies, and safeguarding states' regulatory space are crucial for fostering climate-aligned investments. Beyond these reforms, integrating climate-positive measures across trade and investment agreements can help address global finance gaps and mobilize resources for the transition to a low-carbon economy.

Through innovative mechanisms like ETS linkages, supply-side crediting, and collaborative governance frameworks, IIAs can be repositioned as instruments of climate ambition rather than barriers. This transformation requires sustained international cooperation, rigorous legal and policy reforms, and alignment with global sustainability goals. Ultimately, the integration of climate and investment law offers a pathway to achieving the scale and equity needed to meet the Paris Agreement objectives and ensure a just transition for all.

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[126] Michael A Mehling, 'Theories and Practices of Cross-Border Carbon Market Linkages: Implications for Asia and the Pacific' [2024] ADB Background Paper.

[127] Michael A Mehling and others, 'The Form and Substance of International Cooperation on Border Carbon Adjustments' (2022) 116 American Journal of International Law 213.