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New Directions in International Investment Law: Towards Energy Transition

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The investor-State dispute settlement system (ISDS) is increasingly confronted with disputes related to climate-related measures. Consequently, this fora has been described as the new frontier in climate-change disputes, as tribunals are slowly becoming a *de facto* source of climate policy making that directly impacts the regulatory landscape. This blog post discusses the following issues: (i) whether the international investment arbitration system protects fossil fuels, and (ii) whether the international investment system can be used to foster investments in renewable energies.

Does The International Investment Arbitration System Protect Fossil Fuel Investments?

Both the latest IPCC Report and the International Energy Agency (IEA) Net- Zero by 2050 Report emphasized the need to reduce carbon emissions from fossil fuels to limit global temperature rise to a maximum of 1.5°celcius. Nonetheless, international investment treaties continue to protect investments in fossil fuels. The mere threat of an investment proceeding may forestall a State from taking climate change measures to limit fossil fuel exploitation, resulting in regulatory chill. On this basis, civil society and other that international investment law (and ISDS) conflict with the imperatives of the Paris Agreement.

Certain ISDS cases indicate that such criticisms may be correct. For example, in *Grenada Private Power & WRB Enterprises Inc v. Grenada*, Grenada sought to implement its Nationally Determined Contributions (NDCs) under the Paris Agreement, diverging from fossil-fuel energy to renewable energy. To accomplish this, Grenada enacted legislation that ended the monopoly of GRENLEC – a fossil fuel energy provider and the island's sole energy provider – over the energy sector. In response, GRENLEC swiftly commenced investment arbitration against Grenada. In the arbitration, Grenada made several policy arguments invoking, *inter alia*, its national interest in renewable energy development, the failure of GRENLEC to act as a good corporate citizen, and the energy cost savings for Grenadians that would be gained from renewable energy. In a unanimous decision, the Tribunal rejected these arguments stating: *"the task of the Tribunal is to determine whether the complex contractual arrangements between the Parties have been complied with and, if not, what remedy should be awarded."* (para. 8) The Tribunal ultimately found that Grenada's 2016 energy restructuring legislation violated the investment contract between Grenada and GRENLEC and ordered Grenada to repurchase shares in the investment vehicle.

Such a decision illustrates the capacity for ISDS awards to act as *de facto* tools of climate governance. The Tribunal's award prevented Grenada from ending GRENLEC's monopoly, and thus, limited the capacity of the island to reform its regulatory environment to foster investment in renewable energies to comply with its NDC commitments. In this regard, the award limited the capacity for Grenada to implement its energy transition policy, thereby exemplifying civil society's criticism that the international investment law system may undermine the capacity for States to adopt energy transition measures.

Can the International Investment System Foster Investments in Renewable Energy?

The nature of clean energy projects makes it critical that countries create a stable operating environment for investors. Clean energy projects are highly capital intensive, require long repayment periods, and are exposed to regulatory risks. Confronted with these risks, without investment protection, there are weak prospects for long-term return on renewable energy investments. Additionally, countries that do not provide a strong framework for the protection of renewable energy investments may find it challenging to attract foreign investors, compared to countries which offer a protective investment environment. Therefore, the international investment law system may foster investments in renewable energy because it grants foreign investors a sense of security over their investments.

Thus, international investment law may be used to encourage and protect investments in renewable energy and low-carbon technology, by creating a stable operating environment for investors. Post-COP 26, the IEA estimates that annual clean energy investments must more than triple by 2030 to around USD 4 trillion if States are to fulfill their decarbonization pledges. For emerging and developing economies, receiving trillions of dollars in private investment will be key to achieving decarbonization. Thus, many countries are designing incentive regimes to attract foreign investment in clean energy.

ISDS has indeed been used to protect investments in renewables. The Energy Charter Secretariat reports that 60 % of ISDS filed under the ECT have been to protect investments in renewables. UNCTAD Dispute Navigator shows that foreign investors have initiated at minimum 35 arbitrations in , Italy and the Czech Republic over the rollback of incentive regimes. In at least 18 of the arbitrations against Spain investors have been successful. The saga of arbitrations against Spain show that, despite the lack of uniformity in these rulings, some tribunals do favor stability and certainty in the legal frameworks of renewable energy cases. In arbitration cases against Italy, at least 3 awards have been rendered in favor of the investor. Given the success of ISDS in protecting renewables, it would be inappropriate to generalize the international investment law system as inimical to the energy transition.

ISDS being invoked to protect renewables shows no sign of abatement. In 2021, investors initiated arbitrations against Currently, there are many investment arbitration scenarios confronting Mexico because of the Electricity Industry Law 2021, which reverses incentives initially granted to renewables.

New Trends in IIAs Can Incentivize Investments in Renewable Energy

International investment arbitration is changing with the introduction of new generations IIAs containing carve-outs, a state's right to regulate and the obligation of investors to protect the environment and respect human rights. These novel provisions in new generation IIAs are welcome considering that, historically, environmental provisions were not a feature of most IIAs. OECD research shows that since 2008, 89% of newly concluded IIAs contain references to environmental matters. This development highlights the growing concern of States to balance their environmental policies with the commitments made to foreign investors.

New generation IIAs such as the Netherlands Model BIT, Morocco- Nigeria BIT or the Singapore-Indonesian BIT, contain progressive features recognizing an explicit right to regulate and investors' environmental obligations. For instance, Article 11 of the Singapore – Indonesia BIT expressly grants the host State the right to regulate for environmental objectives. Similarly, Article 8 (2) of the Morocco- Nigeria BIT provides that investors have the obligation not circumvent international environmental law duties. Such language in new generation IIAs rebalances the States' environmental policy against the investors' economic interests by expressly protecting the State's environmental concerns in activities conducted by foreign investors.

Additionally, new generation IIAs, for example, Article 6.6 of the Netherlands Model BIT, incentivize foreign investment that aligns with the imperatives of the Paris Agreement. This provision reminds the Parties they are not free to opt-out of their obligations under the Paris Agreement, but what is more, they reaffirm their commitments within the scope and application of international investment law.. In this regard, in sectors difficult to decarbonize, investments should consider carbon set-offs, and where available, carbon capture and storage technologies. The strength of language in new generation IIAs is that, if drafted accurately, they are capable of limit new fossil-fuel investments and encourage renewable energy investments aligned with the Paris Agreement.

Another benefit and incentive from new generations IIAs, is that investors in renewable energy can structure their investment to take advantage of investment protection. For example, new generation IIA containing an environmental non-regression provision may potentially safeguard an investor from a state derogating environmental standards and incentives existing at the time when the renewable energy investment was made. For instance, Article 1114(2) of NAFTA first introduced a non-regression clause in an IIA, providing that parties shall not induce investment by relaxing measures of general application introduced to protect, among others, the environment in their territories. Similarly, Article 24.4.3 of the USMCA provides that parties recognize that it is inappropriate to encourage trade or investment by relaxing environmental law protection. This is particularly useful for renewable energy investments, which are capital intensive and immovable, such as photovoltaic plants or wind energy project, that require predictable investment environments. As noted before, despite the lack of uniformity in the rulings, the Spanish Saga Cases, are again, proof that international investment law fosters a stable legal framework where investors are entitled to have a legitimate expectation of legal certainty at the initial time of investment and throughout the life of the investment.

Conclusion

The foregoing analysis has examined how IIAs and ISDS create a predictable and secure operating environment for foreign investors, including guaranteeing a fair and equitable standard of treatment and protection against indirect expropriation. Despite this, the global energy transition has many questions including whether ISDS protects fossil fuel investments and whether it is subject to fostering investments in renewable energies. The new trends in ISDS are likely to foster investment in renewables. Thus, the future of IIA suggests that tribunals can become a tool of global climate governance, serving as a *de facto* source of climate policy that impacts the internal regulatory landscape of host countries.

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