

# Kluwer Arbitration Blog

## Climate Change or Change of Climate?

Mirko Camanna (Erasmus University Rotterdam) · Wednesday, May 15th, 2024

On 6 February 2024, the **Chartered Institute of Arbitrators (CiArb) European Branch/French Chapter** held a seminar at the **Paris office of Bird & Bird** moderated by **Jalal El Ahdab** (Bird&Bird) and **Alexandre Malan** (Belot Malan & Associés) on a crucial topic: Environmental, Social, and Governance (“ESG”) issues and their impact on international arbitration. The panel discussion featured **Pascale Accaoui Lorfing** (ESCP Business School/CREDIMI), **Yulia Levashova** (Nyenrode University), **Kirsten Odynski** (White & Case LLP), **Patrick Thieffry** (independent arbitrator).

This blog post summarizes the main arguments discussed by the speakers.

### Arbitrating Climate Change Disputes

Kirsten Odynski analysed the current landscape of climate change disputes, their relationship with arbitration, and future perspectives.

Generally, climate change disputes is a broad term covering a range of disputes arising from legal or factual issues relating to climate change (examples of litigation relating to climate change can be found [here](#)).

Focusing on arbitration, Odynski referred to the **2019 ICC Task Force Report on Climate-Related Disputes in Arbitration**. She noted the enduring relevance of the Report’s definition (**para. 2.1-2.3**), although further and new nuances need to be considered, especially regarding the **first two listed categories of climate change disputes** (para. 2.3). Climate change, environmental regulations, and legislation have impacted arbitration users, notably in the construction and energy sectors. For instance, should a dispute concerning delayed deliveries to a construction site caused by the **drought affecting the Panama Canal’s operations** be considered a climate change dispute?

Arbitration has several features that suit the resolution of climate change disputes: neutral forum, arbitrators with specialist expertise, procedural flexibility, confidentiality (though in tension with transparency), and ease of enforcement.

Regarding future perspectives, Odynski foresees an increase in climate-change arbitration and the impact of climate change on arbitration users, distinguishing:

- Investment arbitration, as evidenced by the potential implications of climate change and other environmental regulations on States' obligations under existing investment treaties (e.g., *RWE v. Netherlands*), and the increasing number of environmental obligations in investment treaties as a basis for States' counterclaims (e.g., **2019 Dutch Model BIT**; *Burlington v. Ecuador* for an example).
- Commercial arbitration, contracts typically containing arbitration clauses are increasingly incorporating ESG-related provisions (e.g., **standard construction forms**, supply chain agreements, credit facilities), increasing the likelihood of climate change-related contractual disputes. Odynski suggested to commercial arbitration institutions to categorize climate change disputes in their statistics to improve understanding of their nature and frequency.
- The increasing of greenwashing claims is unlikely to have a significant impact on international arbitration. As these types of claims are typically based on national consumer protection laws, they will mainly be dealt with by national courts and bodies. However, this may change with increasing regulation.

### Impact of the EU Due Diligence Legislation on International Arbitration

Yulia Levashova underlined the potential impacts of the **ongoing EU's Corporate Sustainability Due Diligence Directive** (CS3D) on foreign investors, commercial matters, and arbitrations. **The final compromise version of the Directive** was adopted on March 15, 2024, after delays due to disagreements among member States over its scope, leading to a substantial reduction in the CS3D's applicability.

Levashova underlined four CS3D's impact profiles:

- CS3D has an extraterritorial scope of application because it will apply directly to very large non-European companies investing in the European market. The European Commission will publish a list of non-EU companies falling within CS3D's scope in the near future. Moreover, CS3D will indirectly impact SMEs integrated into value chains, as those subject to CS3D must ensure compliance throughout their value chain. Companies must obtain contractual assurances from their direct (and, in some cases, indirect) business partners in order to comply with the obligation concerning the prevention and mitigation of adverse human rights or environmental impacts **(7(2)(b), 7(4), 8(3)(c), 8(5))**.
- EU companies subject to the CS3D investing in third countries must continuously incorporate due diligence ("DD") into their policies.
- The Directive (incorporated into national law) could be invoked in ISDS proceedings. Most investment treaties require that investments comply with the domestic law of the Host State to be considered lawful. An investor's lack of compliance with CS3D can potentially be a ground for an arbitral tribunal to decline jurisdiction (e.g., *Cortec Mining v. Kenya, para. 319*). A growing trend in ISDS involves **DD as a significant factor** in determining whether an investor's legitimate expectations merit protection under the fair-and-equitable-treatment (FET) standard (e.g., *Gaspar v. Costa Rica, para. 379*). Investors must demonstrate adequate DD efforts to prove the unforeseeability of the challenged regulatory measures (e.g., *Isolux v. Spain*). Nevertheless, the latter test remains ambiguous. In this regard, compliance with CS3D may serve as an indicator of whether HRDD measures were foreseeable to investors.
- CS3D will certainly affect commercial arbitration. The Directive relies heavily on companies' ability to control supply chain activities through commercial contracts. The inclusion of DD

clauses into contracts containing an arbitration agreement may lead to disputes over these clauses' interpretation and application. The interpretative challenges could arise from broadly formulated DD clauses, the third parties and their actions outside of the company's direct contractual relationship, and the assessment of damages.

## **ESG & Force Majeure**

Pascale Accaoui Lorring addressed the relationship between ESG and *force majeure* (FM) clauses, advising how to draft clauses combining ESG and FM.

Firstly, the distinction between **FM** as a civil law concept and other concepts, such as *hardship*, *frustration of purpose*, *physical impossibility*, and *commercial impracticability* is fundamental.

After that, she underlined three potential relations between ESG issues and FM clauses:

- FM clauses with general definitions followed by a list of FM events, including ESG-related issues.
- FM clauses with a limited list of FM events but stating that other events could be included.
- FM clauses excluding climate-related issues.

In light of these considerations, she advised on drafting future clauses that combine ESG and FM. Drafting FM clauses related to ESG issues, parties should be aware of whether they wish to have defined criteria, either alone or in addition to a list of events, and whether these listed events, once occurring, are presumed to be FM events or whether they need to be proved (*e.g.*, the **2020 ICC Force Majeure Model Clause**). Concerning the obligations of the parties, careful attention should be paid to the notification and the contract's fate depending on the severity of the impossibility to perform (temporary, partial, or definite).

## **Procedural Challenges for Counsel and Arbitrators Facing ESG Clauses and Green Arbitrations**

Patrick Thieffry provided an insider view on the main challenges for counsels and arbitrators facing ESG clauses and green arbitration.

Since the **2019 Report of the ICC Taskforce on Arbitration of Climate Change-related Disputes**, new types of legal situations and an increasing number of traditional commercial disputes have become likely to have ESG aspects.

The potentially greatest challenge for arbitrators is the characterization of ESG-related substantive rules as **international public policy**. Considering ESG rules as overriding mandatory rules (*lois de police*) or as fundamental 'values' could result in applying a different law than that otherwise applicable or rejecting a foreign law that would have otherwise applied, or an award that would have applied such law. The lawmakers' intent regarding the mandatory character of such rules may be decisive. Similarly to cases involving corruption or money laundering. Arbitrators in such disputes would encounter dilemmas regarding to what steps to take.

Arbitration offers an alternative ‘non-state forum’ for companies considering extending arbitration offers to potentially affected parties with ESG-related claims, rather than facing burdensome multi-jurisdictional litigation, but also maintaining a sufficient level of perceived social acceptability.

Ongoing reforms (**revised ICSID Rules, UNCITRAL’s Working Group III**), offer future perspectives: mechanisms to dispose of manifestly unfounded claims early or require claimants to pay litigation costs; measures to enhance transparency through third-party information disclosure and to allow increased participation, as by incorporating *amicus curiae* in arbitration rules, allowing the formal involvement of affected persons as parties enabling mass arbitrations like in *Abaclat v. Argentina*, or pursuant to the **Bangladesh Accord post-Rana Plaza catastrophe**.

Finally, Thieffry was asked to shed light on the notion of ‘environment-friendly arbitrator,’ emphasizing the importance of upholding arbitral duties and procedural efficiency. Arbitrators should not decide the dispute on the basis of what is best for the environment, as this would be inconsistent with judicial duties. **Arbitrators with expertise in Environmental Law** may not exert such significant influence as may be expected on the tribunal and they may even raise suspicion of bias, depending on the circumstances. Finally, arbitrators aiming to limit the arbitral proceedings’ environmental footprint (*e.g.*, **Green Pledge**), should not compromise proceeding’s fairness and equality. Considering the adverse impact of information technologies’ intensive use, the problem of ascertaining proceeding’s footprint still remains.

## Conclusion

The seminar underlined the impact of climate change and ESG issues on business, commercial contracts, and investments, with implications for international arbitration. The number and types of arbitrations will increase, addressing problems such as legitimate expectations and interpretation of ESG clauses. Arbitrators would face new difficulties and duties.

The question remains: will climate change only create new issues within arbitration, or will it change the climate of arbitration?

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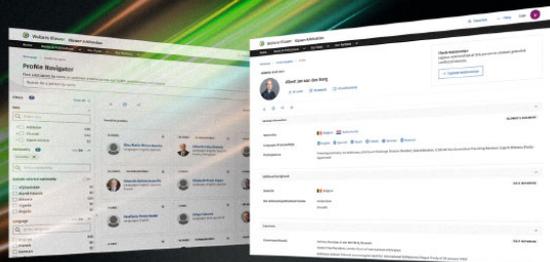
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