Kluwer Arbitration Blog

It’s Not Easy Being Green: ESG, Arbitration and the Future of Dispute Resolution

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Environmental, Social and Governance (“ESG”) considerations have evolved from idealistic frameworks into binding legal, financial and reputational imperatives and responsibilities. Increasingly, international arbitration must grapple with the complex and often competing, or at times contradictory, demands that ESG compliance places on states, corporations and dispute resolution mechanisms.

As set out below against an 80s soundtrack (a time of great music… and where the world was waking to the challenges of the future), as the landscape continues to shift, ESG has exposed both the potential and the limitations of arbitration as a tool of enforcement and transformation.

Everybody Wants to Rule the World: “*… nothing ever lasts forever*“

ESG: From Principles to Pressure Points

ESG is no longer just a reporting acronym. It is a recalibration of corporate identity, investment strategy and legal risk. This recalibration has implications at every stage of the business lifecycle: from supply chain contracts and due diligence to investment arbitration and enforcement. At its core, ESG is about creating enduring, responsible habits. But for these habits to take hold, early planning is essential. That includes budgeting for ESG initiatives, integrating them into contracts and anticipating disputes.

As the IBA Arbitration Committee’s 2023 *Report on ESG Obligations and Related Disputes* notes, this contractual embedding is essential for transforming ESG from being a soft commitment to an enforceable norm. The Report offers model clauses and practical guidance for incorporating ESG into commercial relationships, reflecting a growing recognition that ESG disputes are not only inevitable but evolving.

In the Air Tonight: “*If you told me you were drowning, I would not lend a hand*“

ESG Claims: Staying True to Principle in the Face of Reality

Bringing ESG-related claims, particularly against states, poses significant risks. Consider KELAG's ICSID arbitration against Romania over changes to renewable energy incentives. The Austrian renewables company faced not just a dispute over regulatory rollback but an existential question about its role, resilience, and ability to pursue long-term sustainability. The decision to proceed with arbitration requires weighing financial exposure, reputational risk, and the broader political context of intra-EU investment disputes.

Cases like KELAG's raise the question: are ESG initiatives genuine tools for accountability and change, or performative gestures vulnerable to retreat when the cost becomes real? The answer depends largely on the enforceability of ESG obligations and the robustness of dispute resolution mechanisms that uphold them.

ABBA: *"Take a Chance on me"*

Litigation Funding: ESG and the Risk Matrix

One emerging solution to the resource imbalance in ESG arbitration is litigation funding. Funders are increasingly assessing ESG claims not just as commercial opportunities but as vehicles for social impact, enhancing their role in enabling access to justice. However, ESG claims present unique challenges for funders: environmental harm is difficult to quantify; causation can be difficult if not impossible to prove; and evolving regulatory standards increase legal unpredictability and therefore increase the investment risk.

Nevertheless, funders are beginning to recalibrate expectations, including for e.g., accepting lower returns on some ESG-aligned claims to meet investor and reputational priorities and agendas. This marks a subtle but significant shift in the funding model, moving from a pure commercial calculus toward blended value metrics.

U2: *"I still haven't found what I'm looking for"*

Remedies and the Philosophical Limits of Arbitration

Traditional arbitration is designed around monetary compensation. But ESG disputes often involve harms that transcend financial value: ecological degradation, cultural loss, human rights violations, and intergenerational injustice. The question, then, is whether arbitration must and can evolve to offer new remedies, e.g. restorative outcomes, injunctive relief, or reputational redress.

So far, tribunals have been cautious. Most are bound by party agreement and the remedial limitations of commercial and investment law. But as ESG pressures mount, this cautionary approach may be subject to criticism and may no longer be acceptable to the broader public. This also extends to whether arbitral institutions, think tanks or other relevant institutions should take a more proactive stance on developing, promoting, or otherwise establishing equitable remedies, non-financial outcomes, and sustainability-focused procedures that better suit the circumstances of the particular case.

The *2025 ACICA Sustainability Protocol*, for example, offers effective suggestions and procedures.

It encourages environmentally conscious arbitration through practical tools: virtual hearings, carbon budgeting, and paperless proceedings. While largely voluntary, such initiatives signal a shift in institutional thinking from neutrality to proactive engagement with global challenges.

Mr. Mister: "*Take these broken wings*"

The Governance Gap and Erosion of Trust

Even as private actors embrace ESG, public institutions often lag behind. The sudden reversal of the EU's Corporate Sustainability Reporting Directive requirements in early 2025, despite years of corporate preparation and investment, undermined trust in the regulatory process. Companies that had invested heavily in compliance consider themselves penalised for early adoption.

This type of regulatory flip-flopping contributes to what can be described as "compliance fatigue." When ESG frameworks appear unstable or politicised, the incentive to take them seriously diminishes. Parties begin to question the utility of compliance if regulators, or entire jurisdictions, backtrack and fail to hold all market participants to the same standard. In this vacuum, litigation and arbitration step in not only as dispute resolution mechanisms but as instruments of accountability. Is it really the role of the courts and tribunals to be the vanguards of social and environmental change? Surely that is the task of parliament and intra- and international institutions.

In addition, this shift comes with its own risks. Litigation is slow, costly, piecemeal, and lacks the legitimacy of the democratic legislative process. Without clear regulatory anchors, arbitral decisions risk inconsistency or overreach. The law lags behind the ESG agenda: Courts and tribunals are increasingly being called upon to push the envelope and enable or even force change in the face of a statutory limbo or vacuum.

Queen: "*Under Pressure*"

Insurance and the Challenge of Known Risks

Insurance traditionally functions as a hedge against unforeseen events. But ESG-related harms, such as climate damage or corporate breaches, are increasingly predictable. As environmental data proliferates and supply chain visibility improves, insurers may begin to limit coverage for what they consider "known risks."

This would place a greater onus on corporations to prevent, monitor, and mitigate ESG-related exposures themselves. ESG exclusions are already appearing in some policies. The result may be a new insurance landscape where liability for ESG harm is borne more directly by market actors. *Caveat emptor*: the risks are growing, but knowledge of the same by relevant stakeholders, in particular insured parties, may not be in step with such developments.

For arbitration, or the avoidance of the same, this trend reinforces the need for clear ESG drafting, comprehensive due diligence, and robust dispute avoidance procedures. If insurance coverage fails, contracts must carry the burden of risk allocation, and tribunals must be prepared to enforce them.

Toto: "*Hold the line*"

Contractual Governance as a Compliance Strategy

Given the instability of state-led frameworks, private arrangements through contracts are emerging as the most reliable way to ensure ESG accountability. Parties can and should define ESG standards contractually, drawing on international instruments like the UN Guiding Principles on Business and Human Rights (UNGPs) or the OECD Guidelines for Multinational Enterprises on Responsible Business Conduct.

The IBA's model ESG clauses offer a starting point by defining obligations, setting enforcement mechanisms, and outlining appropriate remedies. These clauses are not merely technical, they are normative tools that transform sustainability from aspiration to obligation.

Contractual governance also reinforces procedural fairness. When parties have jointly defined their ESG commitments, tribunals are better equipped to assess breaches and award remedies. This reinforces legitimacy and predictability in an otherwise unsettled landscape.

Simple Minds: "*Don't you forget about me*"

Dialogue, Learning From the Past, and Going Forward

Ultimately, the success of ESG integration depends on transparency and dialogue. Regulatory mandates are important, but collaboration between governments, investors, civil society, and institutions is essential to engender lasting impact. ESG cannot be imposed top-down. It must be co-created: a rising tide raises all ships.

Timing is also crucial. ESG transformation is a long game, but the legal and financial costs of delay are mounting. Arbitration has a role to play, not just in adjudicating disputes, but in shaping the standards against which compliance is judged. This opens the door to a potential new issue of whether ESG arbitrations, and the standards established in each case, may become influential, guiding, or otherwise create binding case law to ensure consistency, predictability, and supportive references in an otherwise developing legal landscape. Practitioners would do well to consider whether the confidentiality of such ESG arbitrations should and could be foregone, in light of the overriding interest of the broader public to be privy to the case law developing under the auspices of such ESG arbitrations.

What is needed now is leadership from governments and institutions, arbitral institutions, and stakeholders, including funders, corporations, and lawyers. Sustainability is not easy, but it is achievable through preparation, creativity, and shared commitment.

Europe: "*It's the Final Countdown*"… or are we in for a "*Thriller*"? (Michael Jackson)

Conclusion

The intersection between ESG and arbitration presents both a challenge and an opportunity. Dispute resolution frameworks must evolve to reflect the complexity of ESG-related harm, while maintaining fairness, legitimacy, and enforceability. Arbitration is not yet fully equipped to resolve every ESG dispute. But with the right contractual tools, procedural reforms, and collaborative ethos, it can become a cornerstone of the global sustainability transition.

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