
STRIKING A LEGAL BALANCE: RECONCILING CLIMATE ACTION WITH INVESTOR PROTECTION IN INVESTMENT TREATIES

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ABSTRACT

The framework of international investment treaties that now exists is not well adapted to the goals of climate change. The "old generation" of international investment agreements, which were "climate neutral" or "climate blind," were signed prior to the broad climate action, which is what causes the tension.

This research highlights the need for reform by examining the barriers that prevent international investment agreements and investment arbitration from addressing climate change-related challenges. There are still numerous issues that need to be resolved with regard to international investment agreements, even though some states have started to modify them in light of climate change. To help mitigate climate change, the current system of international investment agreements needs to be changed to include investment arbitration provisions for climate change. The results suggest that states may update investment treaties using a model centred on climate change.

Keywords: Climate change; international investment agreements; investor-state dispute settlement; climate-oriented model investment treaty.

INTRODUCTION:

Today, there is a great deal of concern over global climate change, which the G20 has called "one of our greatest challenges".¹ Externality characterizes climate change, which affects the entire world over an extended period of time and across generations.² The Paris Agreement, which encourages climate finance and mitigates climate change globally, was agreed during the 21st United Nations Climate Change Conference in an effort to stop climate change from getting worse. "Holding the increase in the global average temperature well below 2 °C above preindustrial levels and pursuing efforts to limit the temperature increase to 1.5 °C above preindustrial levels" and "making finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development" are the objectives of climate change mitigation, according to Article 2 (1) of the Paris Agreement.³ Several international financial institutions, such as the World Bank and the Asian Development Bank (ADB), unveiled financing plans during the 28th Conference of the Parties to the United Nations

Framework Convention on Climate Change (COP28) with the aim of accelerating the global fight against climate change and encouraging more decisive action. For instance, to help developing nations better survive the harsh effects of climate change, the World Bank has committed to allocating 45% of its yearly loans for projects connected to climate change for the fiscal year that runs from July 1, 2024, to June 30, 2025. In addition, private investment—including foreign direct investment, or FDI—is a significant source of funding for climate change.⁴

Foreign investment has a wide definition, despite the fact that different national laws in different nations define it differently. Movable and immovable property, intellectual property rights, securities, money claims, commercial concessions, and other property rights are examples of what can be included in a foreign investment. Both domestic and international

¹ Daniel, B.; Jutta, B.; Lavanya, R. *International Climate Change Law*; Oxford University Press: Oxford, UK, 2017.

² Atanas, K.; Armin-D., R.; Georg, Z.; Edward, C. *Investment and Growth in the Time of Climate Change* Annual Economic Conference and Publication. Available online: <https://www.econstor.eu/bitstream/10419/90708/1/776716638.pdf> (accessed on 17 March 2024).

³ Paris Agreement, opened for signature Dec. 12, 2015, U.N. Doc. FCCC/CP/2015/L.9/Rev.1, Art. 2(1).

⁴ World Bank Group, Press Release, World Bank Group Doubles Down on Financial Ambition to Drive Climate Action and Build Resilience (Dec. 1, 2023), Accessed on 17 March 2024 Available at- <https://www.worldbank.org/en/news/press-release/2023/12/01/world-bank-group-doubles-down-onfinancial-ambition-to-drive-climate-action-and-build-resilience>.

legal frameworks can take into account the potential effects of foreign investments on climate change in their efforts to promote and safeguard foreign investment.

The majority of economies or nations implement laws or policies that control foreign investment. In addition to offering protection for overseas investments, these tools also direct and synchronize them with pertinent policy needs, guaranteeing that they more effectively advance policy goals. As an example, the European Commission started the "Invest EU program" in 2021 to encourage innovative ideas, sustainable investment, and the creation of jobs in Europe.⁵ As part of this program, being actively involved in mitigating climate change is one of the qualifying requirements for receiving Union financing, especially when it comes to infrastructure expenditures. The implementing partner is responsible for screening such investment projects that receive funding to ascertain whether they have an impact on the environment, climate, or society.

International investment agreements, or IIAs, have become one of the most important means of international legal protection and foreign investment promotion since Germany and Pakistan signed the first bilateral investment treaty (BIT) in 1959. International climate change law is developed in a different manner than IIAs. Issues related to climate change are not sufficiently addressed by the majority of current IIAs. The mechanisms for investor-state dispute settlement (ISDS), particularly the International Investment Arbitration system set up under IIAs, frequently fall short of striking a sufficient balance between safeguarding foreign investments and the host country governments' regulatory rights to address climate change. However, when climate change-related issues gain prominence, actions taken by a state to address them can give international investors the right to file an investment arbitration claim under IIAs. Numerous prior ISDS cases featured industries or initiatives relevant to climate change, according to statistical data [6]. These examples show the increasing tension between the investment regime and mitigating climate change, as well as the difficulties that arise when the two come together.

In light of this, this study examines three different kinds of investment disputes pertaining to host governments' regulation of climate change issues, suggesting that the current IIA regime may serve as a roadblock to the implementation of climate policy. It also looks at the challenges

⁵ Elise-Nicoleta VÂLCU. "EU Invest Program"—Financing Union Mechanism of Member States for PostPandemic Economic Recovery. *Perspect. Law Public Adm.* 2022, 11, 252–259.

facing the IIAs today in tackling climate change and concludes with recommendations. The following inquiries are addressed in this study: First, what kinds of international investment arbitration cases are there now including climate change? Second, why is it so hard for the international investment arbitration system and existing IIAs to give host country governments protections when they implement climate change policies? What are the ways that their shortcomings manifest? Lastly, what improvements can IIAs make to make it easier to put climate-focused policies into action?

The report indicates that significant capital investments in the low-carbon sector are necessary for industrial transformation, upgrading, and technical innovation in order to achieve effective global climate governance. Cross-border investments from high-emission to low-emission sectors will be made easier and faster with the climate-oriented reform of IIAs. Consequently,

governments are able to accelerate the transition to low-carbon economies and enact climate measures without hindrance from IIAs. The results of this study have important policy ramifications for stakeholders, legislators, and government regulators. It proposes a model climate-oriented treaty that will act as a guide and pattern for all nations, particularly developing nations, when they amend or renegotiate their own IIAs.

OVERVIEW AND RATIONALE FOR CHANGE:

The framework for treating foreign direct investment (FDI) and foreign investors by host governments is made up of a network of bilateral investment treaties (BITs), investment chapters in free trade agreements (FTAs), and other treaties with investment provisions. Investment treaties provide investor-state dispute settlement (ISDS) procedures to compel foreign tribunals to uphold the substantive terms pertaining to the protection of investors and their capital. The system needs to be completely overhauled in order to enable climate aligned investment governance, ease the flow of climate investment, and gradually phase out climate-disruptive investment. As it stands, the regime stands in the way of accomplishing climate goals.

The expenses of states' lawful climate action, like phaseouts of fossil fuels and the regulation of other high-emission investments, are increased by investment treaties and arbitration.⁶ A foreign investor protected by an applicable treaty may, under the current investment regime,

⁶ Brauch, "Climate Action Needs Investment Governance"

demand monetary compensation from the host state for any policy measures that are thought to adversely harm the investor's investments in the host state. Investors are using ISDS more frequently to contest government policies pertaining to climate change and demand financial compensation. For example, investment treaties and arbitration may allow foreign investors whose interests are impacted to seek compensation for measures taken by nations that restrict petroleum activities, halt the development of fossil fuel infrastructure, or phase out fossil fired power generation.⁷ By transferring the public's obligation for high-emission investments from private enterprises, the investment regime safeguards the financial interests of high emission companies while simultaneously regulating them for the benefit of the public interest.

There are four methods to prevent climate change measures from violating an IIA:

1. by determining that the measure is not covered by the treaty as a whole;
2. by determining that the measure is not covered by a specific obligation;
3. by determining that the relevant treaty obligation has not been breached; or
4. by providing a valid reason for violating an obligation under an exception.

These exclusions can be classified into three categories: explicit requirements, broad exceptions stated in the treaty, and exceptions that are part of customary international law, such as those related to necessity and countermeasures.

In the first two scenarios, the treaty or obligation is not applicable, hence there is no requirement to ascertain whether there is a breach of obligation or if a violation may be justified under an exception. In the third scenario, both the treaty and the requirement are applicable, but there is no breach of the obligation. In the fourth scenario, both the treaty and obligation are applicable, and there is a breach of the obligation. However, there is an exemption that provides justification for the violation. Therefore, tribunals have the ability to determine if legitimate climate change rules are in line with the duties of states in international investment agreements (IIAs) at various stages of these treaties. One significant distinction between these techniques is that the complainant is responsible for providing evidence that the treaty and

⁷ Edward, G. Urbaser v Argentina: The Origins of a Host State Human Rights Counterclaim in ICSID Arbitration? Available online: <https://www.ejiltalk.org/urbaser-v-argentina-the-origins-of-a-host-state-humanrights-counterclaim-in-icsid-arbitration> (accessed on 22 March 2024)

obligation are applicable and that a violation has occurred, whereas the defending State is tasked with proving compliance with an exemption. Therefore, the arrangement of International Investment Agreements (IIAs) impacts the distribution of the responsibility to provide evidence.

Investment agreements (IIAs) place three main obligations on governments regarding their treatment of foreign investors:

1. ensuring equal treatment between domestic and foreign investors (national treatment), as well as between foreign investors from different countries (most-favored-nation treatment);
2. establishing a minimum standard of fair and equitable treatment for foreign investors; and
3. requiring compensation to be paid in the event of expropriation. Nevertheless, certain government regulations are exempt from these duties.

This article will examine how environmental actions can either avoid being subject to the aforementioned responsibilities or be justified under specific exemptions. International investment flows play a crucial role in facilitating the global spread of climate change technology and expertise, in addition to the exchange of products and services through international trade. Therefore, it is crucial to establish appropriate motivations for foreign investors to share their most effective methods and technologies that might help combat and adapt to climate change. International Investment Agreements (IIAs) can mitigate regulatory and political risks faced by foreign investors, thereby reducing the cost of and providing incentives for foreign investment in clean energy or carbon mitigation technology. Therefore, it is crucial to effectively handle climate change measures in International Investment Agreements (IIAs) in order to protect regulatory autonomy and bolster the financial and technological capabilities of nations in combating climate change.

The legal framework of climate change and international investment law entails an intricate interaction between international agreements, treaties, and investment protection requirements. Below is a comprehensive summary of the main components:

1. The United Nations Framework Convention on Climate Change (UNFCCC): It is an

international treaty. The UNFCCC,⁸ ratified in 1992, is a fundamental global agreement that seeks to tackle climate change by stabilizing the levels of greenhouse gases in the atmosphere. The document outlines broad responsibilities for nations to address the issue of climate change by implementing measures to reduce its effects and adapt to its consequences.

2. The Kyoto Protocol: It established in 1997, is a global agreement within the UNFCCC that imposes mandatory carbon reduction goals on industrialized nations. The techniques of carbon trading and Clean Development Mechanism (CDM) were created to facilitate sustainable development and mitigate greenhouse gas emissions.
3. Paris Agreement: The Paris Agreement, ratified in 2015, expands on the UNFCCC and seeks to enhance the worldwide effort to address climate change.

The user did not provide any text. The document outlines the specific actions that a country will take to decrease the amount of greenhouse gases released into the atmosphere and improve its ability to withstand the effects of climate change. The ultimate objective is to restrict the increase in global temperatures to a level significantly lower than 2 degrees Celsius.

4. IIAs: International Investment Agreements: IIAs encompass Bilateral Investment Treaties (BITs), Free Trade Agreements (FTAs), and other agreements that regulate the movement of investments between nations. These agreements usually contain clauses regarding investment protection, which encompass principles of fair and equitable treatment, national treatment, and methods for resolving disputes between investors and states.

The convergence of climate change and investment law presents difficulties associated with regulatory chill, which refers to the concern that investor-state disputes may discourage countries from enacting essential environmental rules. The user did not provide any text. The adaptability of investment protection criteria, such as the fair and equitable treatment, may enable states to regulate in the public interest without breaching investment responsibilities. However, there is a need for clarification on the application of these standards to climate change initiatives. Striking a balance between investment protection and environmental goals is necessary to find a way to harmonize the goals of safeguarding investments with the imperative

⁸ United Nations Framework Convention on Climate Change, UNFCCC, <https://unfccc.int/> (last visited Apr. 21, 2024).

of effectively tackling climate change. Future agreements should include provisions for addressing disputes pertaining to climate initiatives and should integrate explicit references to social, environmental, and human rights factors.

The legal framework of climate change and international investment law requires managing intricate connections among environmental goals, investment safeguarding criteria, and the imperative for sustainable development. It is essential to strike a balance between these interests to ensure that investments contribute to climate action while also upholding environmental objectives and human rights.

INTERSECTION OF CLIMATE CHANGE AND INVESTMENT LAW:

The foreign investment law and climate change regulations have multiple points of intersection.

1. Regulatory Takings and Regulatory Chill: Worries about the possibility of investor state arbitration resulting from regulatory takings can cause a decrease in regulatory activity, known as "regulatory chill." Host countries may abstain from enacting essential environmental rules out of concern for potential legal responsibility, so impeding endeavours to combat climate change.
2. Investment rule-making: The implementation of negative list procedures in international investment agreements (IIAs) has not had a deterrent effect on regulations, notwithstanding a rise in investment disputes in the past decade. T1 shows that the signatories of new generation IIAs have not been deterred from taking regulatory steps out of concern for potential conflicts.
3. Adaptability of Investment Standards: Certain scholars contend that the exception for police power and the adaptability of fair and equitable treatment standards in International Investment Agreements (IIAs) enable states to regulate in the public interest without incurring liability for harm to foreign investors, as long as the measures are impartial, appropriate, and do not excessively alter the regulatory framework. Nevertheless, this method may not offer unambiguous instructions for investment tribunals to ascertain the legitimacy of regulatory measures pertaining to climate change.
4. Harmonization of Objectives: It is necessary to harmonize the objectives of foreign investment legislation and climate change regulations in order to prevent the neglect of valid

environmental rules in favor of investment protection. Subsequent agreements to the Kyoto Protocol should have provisions for addressing private claims associated with Kyoto projects and incorporate explicit references to the social, environmental, and human rights concerns of State Parties.

The convergence of foreign investment law and climate change legislation presents intricate challenges concerning the deterrent effect on regulations, the establishment of investment rules, the adaptability of standards, and the harmonization of goals. It is important to make sure that investor protection and environmental aims are properly balanced and that reasonable regulatory actions are not unfairly limited.

CHALLENGES FACED BY THE CURRENT INTERNATIONAL INVESTMENT AGREEMENTS (IIAS) IN EFFECTIVELY DEALING WITH THE ISSUE OF CLIMATE CHANGE

The growing conflicts between International Investment Agreements (IIAs) and efforts to mitigate climate change.

Risks Associated with Investment Arbitration in the Face of Challenging Climate Measures

According to UNCTAD's figures, there are a total of 3300 IIAs worldwide, with the majority of them being finished between the 1980s and the 2010s.⁹ These "old-generation" International Investment Agreements (IIAs) were established before to the broad implementation of climate action and are considered to be either "climate neutral" or "climate blind". Investors have the ability to contest the climate policy of the countries they invest in by utilizing investment protection provisions, specifically the non-discrimination provisions, fair and equitable treatment (FET) provisions, and indirect expropriation provisions. These clauses are designed in a broad and ambiguous manner, allowing for potential challenges to be made.

The principle of non-discrimination laws prevents the unjust treatment of foreign investors in similar situations without a valid justification.¹⁰ The idea of "common but differentiated

⁹ UNCTAD. The International Investment Treaty Regime and Climate Action; United Nations Conference on Trade and Development: Geneva, Switzerland, 2022.

¹⁰ Munir, M. Expropriation of Alien Property and the Principle of Non-Discrimination in International Law of Foreign Investment: An Overview. *J. Transnatl. Law Policy* 1998, 8, 57–77.

responsibilities" is plainly violated by the need of non-discriminatory treatment, which is in opposition to the UNFCCC and the Paris Agreement.

Regarding the meaning of "in like circumstances," arbitral tribunals often only take into account investment projects that are in direct competition within the same market. They do not differentiate between investors based on their emission levels, whether high or low. Given this, foreign investors may raise concerns regarding the potential discriminatory nature of the host state's actions, particularly when it comes to providing incentives for low emission investments or withdrawing subsidies for high-emission ventures. In the power and energy industry, enterprises that have low carbon emissions, such as photovoltaic and wind power, will receive more favourable treatment compared to those that rely on coal power generation. This discrepancy may contradict the principle of non-discriminatory treatment. Moreover, differentiating investors based on their economic or business sectors may potentially infringe upon the non-discrimination mandate. In the case of *Occidental Exploration and Production Company v. Ecuador*, a tribunal concluded that the term "in like situations" cannot be narrowly interpreted as suggested by Ecuador. The tribunal argued that the purpose of the Non-Discrimination and National Treatment (NT) principle cannot be achieved by solely focusing on the specific sector in which a particular activity takes place.¹¹ In order to achieve the climate goals, states have incorporated businesses with large levels of emissions, such as power, steel, and building materials, into the carbon trading system and have imposed regulations on these industries. Foreign investors in high-emission industries may argue that the climate regulations of the host country are discriminatory when compared to investors in other sorts of businesses.

Furthermore, the majority of experts in international investment reform and the advancement of sustainable development in international economic law view the Fair and Equitable Treatment (FET) provision as the most prominent example of how international investment law hinders efforts to mitigate climate change and transition to a less carbon-intensive economy.¹² The major objective of the FET standard is to guarantee the stability of the investment environment in the country where the investment is made.¹³ However, when a host

¹¹ *Occidental Exploration and Production Company v. The Republic of Ecuador*, LCIA Case No. UN3467 (Final Award), adopted 1 July 2004, para 173. Available online: <https://www.italaw.com/sites/default/files/casedocuments/ita0571.pdf> (accessed on 20 March 2024).

¹² Newcombe, A.P.; Paradell, L. *Law and Practice of Investment Treaties: Standards of Treatment*; Kluwer Law International: The Hague, The Netherlands, 2009.

¹³ Ying, Z. *Corporate Social Responsibility and International Investment Law: Tension and Reconciliation*. Nord. J. Commer. Law 2017, 90, 90–119

country implements climate policies, it may impact the reasonable expectations of foreign investors, who may perceive it as a violation of the fair and equitable treatment norm.¹⁴ An analysis of the instances reveals substantial variation in the legal criterion of fair and equitable treatment (FET).

In the case of Spain's modification and eventual cancellation of a feed-in-tariff renewable energy incentive scheme, there have been around 20 awards released so far. These awards show that the tribunal used inconsistent methods to interpret the legitimate expectation. Some tribunals have ruled in favor of investors, emphasizing that the host states cannot fundamentally alter the legal framework and business environment in which investors make their investments. Conversely, some tribunals have supported the host state's position, asserting that a violation of investors' legitimate expectations only occurs when the host state intentionally encourages and convinces investors to invest, and subsequently takes actions that fundamentally contradict the investors' expectations. Thus, this demonstrates that the

FET standard is ambiguous, and situations where host states attempt to fulfill their emission reduction obligations under climate change agreements, whether through legislation or administration, may lead investors of high-emission businesses to assert that these actions violate the FET standard in international investment agreements (IIAs). Therefore, host states may be compelled to forgo the essential system improvement to protect the public interest and implement climate-related actions due to the risk of arbitration and reimbursement for damages.¹⁵

Investors can use the indirect expropriation provision to challenge climate regulations implemented by host states. Practically, the tribunals have implemented three distinct and conflicting standards to assess whether the environmental actions taken by the host country amount to indirect expropriation: the "sole effects doctrine," the "proportionality test," and the "police powers doctrine".¹⁶ The extent to which the climate measures will be regarded indirect expropriation based on the aforementioned methodologies is uncertain and lacks clarity due to their various and somewhat inconsistent nature. Hence, both the content of International

¹⁴ Kyla, T. Investor-State Dispute Settlement in the Trans-Pacific Partnership Agreement. Available online: <https://www.pc.gov.au/inquiries/completed/trade-agreements/submissions/subdr067-attachment1.pdf> (accessed on 19 March 2024).

¹⁵ Meredith, W. Reconciling International Investment Law and Climate Change Policy: Potential Liability for Climate Measures Under the Trans-Pacific Partnership. *Sabin Cent. Clim. Change Law* 2015, 45, 10683–10698

¹⁶ Zhu, Y. Do Clarified Indirect Expropriation Clauses in International Investment Treaties Preserve Environmental Regulatory Space. *Harv. Int. Law J.* 2019, 60, 377–416.

Investment Agreements (IIAs) and the application of investment arbitration can potentially hinder the host state's capacity to enforce climate change measures due to the clauses about indirect expropriation. Foreign investors' interests will be impacted if the host country implements stringent climate protection measures to achieve climate objectives. These measures may include the establishment and enforcement of strict emission standards, the imposition of a carbon tax on high-emission activities, the prohibition of fossil fuel usage, or the denial of business licenses to high-emission companies. Foreign investors may choose to engage in international investment arbitration by alleging indirect expropriation when they perceive that these actions would result in the loss of their investment or impact their profitability.

The Unresolved Conflict between IIAs and Other Areas of International Law

The Paris Agreement enforces obligatory commitments on its participants to decrease the emissions of greenhouse gases. Consequently, the government must modify the legal structure in order to decrease investments that produce significant levels of emissions.

However, this could potentially subject the host state to the possibility of liability under the investor protection provisions of International Investment Agreements (IIAs). The cases of *S.D. Myers v. Canada* and *Santa Elena v. Costa Rica* both involve a disagreement between distinct treaty duties. Nevertheless, the tribunals in both instances ultimately determined that international responsibilities did not modify the legal essence of providing complete compensation for expropriation. The claimant in the case of *S. D. Myers v. Canada* contends that Canada's PCB laws violate the principles of national treatment, international minimum standard of treatment, performance criteria, and expropriation clauses as outlined in NAFTA, Canada stated that it was following the Basel Convention, which forbids the transfer of hazardous waste, including PCB regulations, to countries that are not part of the convention, such as the United States.¹⁷ The panel ultimately determined that there was no valid environmental justification for the restriction. The presence of conflicting treaty duties between NAFTA and the Basel Convention is evident in this issue. Furthermore, a dispute arose regarding the international commitments between the International Investment Agreements (IIAs) and the Convention Concerning the Protection of World Cultural and Natural Heritage

¹⁷ *S. D. Myers v. Canada*, NAFTA, NAFTA (Partial Award), Adopted 13 November 2000, paras 130–144, 146–160, 195. Available online: <https://www.italaw.com/sites/default/files/case-documents/ita0747.pdf> (accessed on 19 March 2024).

in the case of *Santa Elena v. Costa Rica*. Costa Rica seized the land of a foreign investor in order to protect a distinct ecological location, as mandated by the Convention Concerning the Protection of the World Cultural and Natural Heritage. Costa Rica asserted its worldwide duty to safeguard the environment. Nevertheless, the tribunal declined to take into account the environmental responsibilities of nature reserves and determined that regardless of the commendable and advantageous nature of a governmental action for society as a whole, it would still be considered expropriation and need compensation.¹⁸

POTENTIAL REFORMS FOR INTERNATIONAL INVESTMENT AGREEMENTS (IIAS):

Climate change has gained significant attention from investment treaty policymakers in recent years. In recent treaty practice, governments have started including explicit climate elements in their International Investment Agreements (IIAs) in order to bring the IIA regime in line with their climate goals.

Increasingly, a larger number of International Investment Agreements (IIAs) have incorporated obligations to carry out the Paris Agreement and the United Nations Framework Convention on Climate Change (UNFCCC), which involve adhering to nationally determined contributions (NDCs) or domestic objectives for reducing emissions in the updated set of IIAs. As an illustration, the European Union (EU) endeavours to incorporate ambitious climate-related clauses and adherence to international conventions on climate change, such as the Paris Agreement, as a crucial component of its trade and investment agreements. However, these attempts do not effectively tackle the underlying deficiency of IIAs. For instance, the majority of International Investment Agreements (IIAs) only reassert their dedication to combat climate change or promote the elimination of barriers to trade or investment in products and services that are specifically related to mitigating climate change. These rules seem to essentially restrict their role to making recommendations and political commitments, rather than imposing legally binding responsibilities on host states or investors. However, in contrast to investment protection clauses that have a legally enforceable nature, these declaratory provisions are considered "soft law" due to their nonbinding language and lack of an effective enforcement mechanism. In addition, the majority of International Investment Agreements (IIAs) do not

¹⁸ *Santa Elena v. Costa Rica*, ICSID Case No. ARB/96/1 (Final Award), Adopted 17 February 2000, Para 71. Available online: <https://www.italaw.com/sites/default/files/case-documents/italaw6340.pdf> (accessed on 19 March 2024).

have proactive measures for promoting and facilitating low-carbon investment, which hinders their ability to effectively support such investments. Several governments, including the European Union (EU), support the use of state-state dispute settlement (SSDS) methods to resolve issues related to sustainable development or climate change. Instead of using sanctions or financial penalties, the SSDS system, demonstrated by the dispute settlement mechanism in the "Investment and Sustainable Development" chapter of the Comprehensive Agreement on Investment,¹⁹ relies on international cooperation, dialogue, and other soft power mechanisms. Consequently, the symbolic significance of the agreement may be more significant than its practical significance in aligning international investment agreements (IIAs) with urgent climate initiatives.

Both historical and contemporary International Investment Agreements (IIAs) clearly lack proactive elements aimed at effectively strengthening climate action. The current trend of expanding the policy space for host governments and allocating responsibilities to international investors and their home nations seems slow and weak. In order to enhance the effectiveness of IIAs in promoting climate change activities, it is necessary to incorporate the notion of sustainable development into reform efforts, with a focus on achieving collective progress while acknowledging diversity. IIAs should undergo reconstruction in order to effectively address the varied demands and interests of different states. In addition, host states will have the ability to uphold their authority levels while also adhering to their promise to liberalize investments. This essential component guarantees that the IIA regime does not impede governments from making efforts to take measures to alleviate climate change. Additionally, it enables a rapid shift towards environmentally-friendly investments. Furthermore, it involves achieving a harmonious equilibrium that promotes ecological accountability while ensuring that a country can make resolute and prompt decisions. A climate-oriented model investment treaty, which incorporates current treaty practice and relevant policy reports, would be a compelling choice for nations worldwide to modernize their investment treaties and effectively tackle the intricate challenges linked to climate change. This is due to the fragmented provisions of existing IIAs and the inconsistent positions adopted by different nations. The essential elements of the model treaty that can be added to dealt with climate change and international investment treaties can be pointed as follows-

¹⁹ Popa Tache, C.E. The EU-China road to the Comprehensive Agreement on Investment. *Jurid. Trib.-Trib. Jurid.* 2022, 12, 476-494

A. Non Discrimination provision:

Classifying the term "in like circumstances" in non-discrimination rules such as National Treatment (NT) and Most-Favored Nation (MFN) can assist in preserving the regulatory flexibility of host governments. One can differentiate between rules and protections that specifically apply to high-emission investments (such as the fossil fuel business) and low-emission investments (such as the renewable energy industry).

Adopting this strategy would offer rationales for nations to handle fossil fuel investments in distinct ways and dissuade them from enhancing their own fossil fuel industries. States have the option to create a "illustrative list of the application of non-discriminatory treatment" which outlines specific instances that need to be considered when evaluating "in like circumstances". This includes considering the effect of investment on greenhouse gas emissions. The bilateral investment agreement between Nigeria and Morocco, signed in 2016, includes a provision in Article 6 (3) stating that treating foreign investors differently from domestic investors due to measures taken by the host country to address climate change and meet international emission reduction obligations is not considered a "like circumstance." Therefore, this differential treatment does not violate the requirement of non-discrimination.

B. FET Provision:

Precise interpretation of the FET provisions by directly mentioning the minimum treatment standard in the agreements or by collaboratively creating a legally enforceable interpretative declaration. When considering situations where a violation of fair and equitable treatment (FET) may occur, Article 4.3.3 of the UNCTAD Investment Policy Framework for Sustainable Development can be consulted. This article specifically states that acts carried out in good faith and regulatory measures that are essential for the host country to achieve public policy goals, such as addressing climate change, are not covered by the FET provisions. Additional elucidation of the term "legitimate expectations" can be found in the EU-Canada CETA. According to this agreement, the concept of "legitimate expectations" only encompasses obligations pertaining to the physical security of investors or investments. It does not include any assurances of legal or regulatory stability.

C. Indirect Expropriation Provisions:

According to the provisions outlined in Annex 8-A of the EU-Canada CETA, we can provide

a description of indirect expropriation. To ascertain the occurrence of indirect expropriation, a thorough examination based on factual evidence must be carried out on a case-by-case basis, considering factors such as the economic consequences, duration, legitimate expectations, and objective. It also does not include actions that aim to safeguard legitimate public welfare goals, such as environmental protection, human rights, preservation of life and health, and goodwill efforts to attain climate targets. Alternatively, climate change-related policies can be incorporated within the IIAs as a specific exemption to indirect expropriation. The draft text agreed upon by the European Commission and the German Federal Government regarding the indirect expropriation provision in the CETA reaffirms that nondiscriminatory measures implemented by a contracting party to combat climate change or address its consequences are not considered indirect expropriation, unless the impact of these measures is perceived as undeniably unreasonable in relation to their purpose. The Agreement in Principle on the Modernisation of the Energy Charter Treaty also contains similar wording. By adopting this strategy, future investment treaties might include a specific and clear exception for climate change policies. This exception would exclude climate measures implemented by states that are parties to the UNFCCC and Paris Agreement, and are aimed at achieving emission reduction targets, from being considered as indirect expropriation.

D. Provisions regarding the right to regulate:

These rules give host governments the right to take action on climate change in order to secure the validity of associated actions. Article 1 of the "investment and environment" subsection of the CAI explicitly acknowledges the host state's authority to regulate. It recognizes the right of each party to determine its sustainable development policies and priorities, establish its own levels of domestic labor and environmental protection, and make changes to its laws and policies in line with its multilateral commitments in the areas of labor and environment. The 2021 Canada Model Foreign Investment Promotion and Protection Agreement of Canada restates the right of the contracting party to regulate within its territory in order to achieve legitimate policy goals. These goals include protecting the environment, addressing climate change, ensuring social or consumer protection, promoting and protecting health and safety, safeguarding the rights of Indigenous peoples, promoting gender equality, and preserving cultural diversity. The EU-UK Trade and Cooperation Agreement and the UK-Japan Comprehensive Economic Partnership Agreement have similar terminology. These clauses will validate government measures to address climate change and more effectively meet the

government's responsibility to decrease emissions.

E. Dispute resolution mechanisms:

The reform of ISDS under UNCITRAL should consider the functional compatibility of ISDS with climate goals to prevent any negative impact on their efforts and international commitments to address climate change as outlined in the Paris Agreement. To accomplish this objective, several measures can be implemented: Initially, these measures can involve setting a jurisdiction threshold to exclude climate measures taken by the host state to fulfill its international obligations under the Paris Agreement from the application of ISDS. Additionally, the focus should be on achieving countries' independent emission reduction contributions and sustainable development goals through the ISDS mechanism. Thus, the availability of ISDS will be limited to conscientious investors who adhere to global climate commitments. Furthermore, it is advisable to select arbitrators who possess expertise in public international law, particularly individuals who have a track record in environmental, human rights, or climate public welfare initiatives. As an illustration, Article 3, paragraph 9, subparagraph 4 of the preliminary investment chapter of the Transatlantic Trade and Investment Partnership Agreement explicitly stipulates that the judges in the proposed investment court must possess expertise in the area of public international law. Furthermore, the tribunals will permit non-governmental organizations to present climate protection opinions as "Amicus Curiae". When dealing with investment conflicts related to climate change, it is crucial to take into account technical matters, such as the cause-and-effect relationship between greenhouse gas emissions and the resulting harm. Given their involvement, it is imperative to engage climate specialists to participate in the arbitration process in order to elucidate the causal connection. The tribunal has the option to consider written arguments that are provided by parties who are not involved in the dispute. Additionally, the host state can implement a counterclaims system. Due to the adaptable and diverse nature of investment arbitration processes, counterclaim offers an opportunity to hold foreign investors accountable for violations of climate change-related commitments, including those arising from local legislation. Two recent instances, *Urbaser SA v. Argentina* and *Perenco v Ecuador*,²⁰ have involved state counterclaims against investors for alleged violations of environmental commitments under the host state's domestic law. Both tribunals ruled in favor of the counterclaims in both instances. In investment arbitration, a host

²⁰ Edward, G. *Urbaser v Argentina: The Origins of a Host State Human Rights Counterclaim in ICSID Arbitration?* Available online: <https://www.ejiltalk.org/urbaser-v-argentina-the-origins-of-a-host-state-humanrights-counterclaim-in-icsid-arbitration> (accessed on 26 March 2024).

state has the potential to file a counterclaim against an investor if their actions have led to a breach of climate change obligations, such as failing to meet emission reduction goals. Finally, during the process of determining the amount of compensation for damages, if the case involves the climate change actions taken by the government of the country where the dispute is taking place, a limit can be established for the claims made by high carbon emission companies. This is done to prevent the tribunal from granting the host country an excessively large compensation package.

It is important to also contemplate the inclusion of a mediation mechanism in the resolution of conflicts related to climate change. The International Chamber of Commerce (ICC) released a paper titled "Resolving Climate Change Related Disputes through Arbitration and Alternative Dispute Resolution." This report acknowledges mediation processes as a viable method for resolving conflicts with the agreement of all parties involved.²¹ This not only conforms to the Singapore mediation convention and facilitates the prompt and timely resolution of conflicts, but it also guarantees the expeditious implementation of settlement agreements and fosters the sustained advancement of global investments.

CONCLUSION:

International investment law is not an autonomous legal system [64]. It is closely connected to other areas of law, especially those that deal with climate change. By participating in international investment treaties, a state exposes itself to arbitral rulings that might greatly affect its responsibilities under climate agreements.

The need to address climate change has increased the need of reforming International Investment Agreements (IIAs). The current framework of International Investment Agreements (IIAs) can impede climate change mitigation efforts, as highlighted in this paper. A significant problem arises from the utilization of investment arbitration by foreign investors to contest climate legislation. The introduction of global climate governance and the reform of international investment dispute settlements have led to a new phase for IIAs. This phase is characterized by coordination, unification, and mutual support. The goal is to assist countries in achieving their greenhouse gas emission reduction targets and to ensure that IIAs and climate

²¹ Resolving Climate Change Related Disputes through Arbitration and ADR. Available online: <https://iccwbo.org/content/uploads/sites/3/2019/11/icc-arbitration-adr-commission-report-on-resolving-climatechange-related-disputes-englishversion.pdf> (accessed on 25 March 2024).

change treaties, such as the Paris Agreement, are mutually supportive. This will not only create a stable investment environment for climate-friendly investments but also contribute to a systematic reform of international investment law towards sustainable development.

There is a growing body of research indicating that International Investment Agreements (IIAs) can play a role in reducing the impact of climate change. It is feasible to include clauses regarding climate change and the environment in International Investment Agreements (IIAs).²² This paper conducts a comprehensive analysis of the arguments connected to climate change in investment arbitration, based on a thorough survey of existing literature and experience. It also recommends for reforms in international investment agreements (IIAs) that are focused on addressing climate change. A climate-oriented model investment treaty can effectively support a transition towards sustainability and actively address the issue of climate change. In order to accomplish these goals, the framework outlined in this study might be viewed as a roadmap.

²² Gehring, M.; Stephenson, S.; Cordonier Segger, M.-C. Sustainability Impact Assessments as Inputs and as Interpretative Aids in International Investment Law. *J. World Invest. Trade* 2017, 18, 163–199. [CrossRef]

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