Submission from Lise Johnson, Head of Investment Law and Policy, Columbia Center on Sustainable Investment, to the Committee on COP 26 and International Trade

# Investment Agreements' Actual and Potential Impacts on Climate Policy and the Goals of COP26

1. There are three important ways that investment agreements can affect climate policy, with respect to mitigation, adaptation, and financial flows. These are through:
a. Supporting Climate-Consistent Investment; Not Subsidizing Harmful Investment
b. Supporting Governance that Is Aligned with Climate Policy and a Just Transition
c. Supporting Cooperation on Climate Action

2. As described below, to date, investment treaties, including those concluded by the UK, have not been adequately designed to address any of those three areas.

## Supporting Climate-Consistent Investment; Not Subsidizing Harmful Investment

3. A climate-consistent investment agreement is one that supports investment so as to help it move away from carbon-intensive sectors and activities and into low- and zero-carbon sectors and activities, including those needed to support climate resilience and a just transition. This role is linked to one of the key rationales for investment treaties, namely, that they influence investment flows: The theory is that the agreements provide certain protections, analogous to risk insurance; and those protections, in turn, are thought to give investors the added confidence to commit capital to socially valuable economic activities.

4. But one key problem with treaties presently in force – those concluded by the UK as well as those concluded by other countries – is that the treaties protect *all* categories investments, irrespective of the impacts of those investments in the places where they are made (the "host countries"), the places where the investors are based or the money is from (the "home countries") or third countries. This means that investment treaties provide government-sponsored risk insurance for new fossil fuel investments and other projects incompatible with a just transition. Through investment treaties, as currently designed, governments are subsidizing any and all covered projects (with coverage being determined based on the nationality of the investor, not the characteristics of the investment) irrespective of their climate mitigation or adaptation impacts. That feature, alone, is inconsistent with states' commitments "to achieve, in accordance with the relevant provisions of the [UNFCCC], stabilization of greenhouse gas concentrations in the atmosphere at a level that would prevent dangerous anthropogenic interference with the climate system,"[1] and, more specifically, to "mak[e] finance flows consistent

with a pathway towards low greenhouse gas emissions and climate-resilient development."[2]

5. But investment treaties need not be such blunt instruments. They could permit – or even require – more discerning treatment, enabling states to distinguish between, for instance, those types of investments generating public goods and warranting public support, and those that undermine climate policy and are not eligible for the privileged treatment offered by investment treaties.

6. An additional key problem is that numerous studies conducted to date have shown that, while treaties may be effective tools for companies wishing to sue governments (discussed further in the next section), they have not actually been effective in terms of their influence on investors' decisions regarding whether or where to invest. In short, treaties have been designed on the premise that if investment receives the enhanced protections offered by the treaties, flows of such investment between the treaty parties will increase. But that pattern linking investment protection to investment flows is, after much analysis, not generally observable.[3] Such lackluster performance, however, need not be the case. The treaties could be designed to more strategically and nimbly overcome barriers to investment in those places, sectors, and activities, where investment is needed to meet UNFCCC and Paris Agreement Goals.

## Supporting Governance that Is Aligned with Climate Policy and a Just Transition

7. Investment treaties are also particularly relevant for climate policy in that they can affect governments' willingness and ability to adopt measures necessary for a transition away from fossil fuels and other carbon-intensive investments. And they can impact the cost of those measures, and who bears those costs, in ways that may prevent the transition, if achieved, from being a *just* transition.

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[1] UNFCCC Art. 2.

[2] Paris Agreement Art. 2(1)(c).

[3] See, e.g., Josef Brada, Zdenek Drabek and Ichiro Iwasaki, 'Does Investor Protection Increase Foreign Direct Investment? A Meta-Analysis' (2020) 35 Journal of Economic Surveys 1 https://doi: 10.1111/joes.12392; Lorenz Reiter and Christian Bellak, 'Effect of BITs on FDI: The Role of Publication Bias' in Julien Chaisse, Leïla Choukroune, and Sufian Jusoh (eds), *Handbook of International Investment Law and Policy* (Springer 2020) https://doi.org/10.1007/978-981-13-5744-2_123-1; Joachim Pohl, 'Societal Benefits and Costs of International Investment Agreements: A Critical Review of Aspects and Available Empirical Evidence' (OECD Working Papers on International Investment, No. 2018/01) https://doi.org/10.1787/e5f85c3d-en; 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* (OUP, 2009) (The working paper version is accessible here: <https://escholarship.org/uc/item/72m4m1r0>); Jason W. Yackee, 'Do Bilateral Investment Treaties Promote Foreign Direct Investment? Some Hints from Alternative Evidence' (University of Wisconsin Legal Studies Research Paper No. 1114, 2010) <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1594887>.

8. This is because the investment treaties concluded by the UK (like investment treaties concluded by other countries in recent decades) tend to (1) impose vaguely worded obligations on states regarding their treatment of foreign investment, and (2) include provisions permitting investors to sue the states in which they have invested through international arbitration, alleging breach of those obligations and seeking damages for the breach. These investor-state arbitration provisions, often called investor-state dispute settlement or "ISDS" provisions are exceptional in international law due to the powers they grant private actors to (1) sue governments for harm without first exhausting domestic remedies, and (2) seek large damage amounts largely unavailable under other areas of international (or even domestic) law. [4] ISDS decisions have interpreted and/or applied treaty obligations in ways that the treaty parties consider to be broader and more exacting than envisioned or proper,[5] and that have resulted in undue regulatory chill.[6]

9. The threats to climate policy are real: As we have seen, covered investors have already used investment treaties to challenge climate measures and other restrictions on extraction and use of fossil fuels. Known cases include *RWE v. Netherlands*, ICSID Case No. ARB/21/4; *Uniper v. Neth*erlands, ICSID Case No. ARB/21/22; *Westmoreland v. Canada*, ICSID Case No. UNCT/20/3; *Rockhopper v. Italy*, ICSID Case No. ARB/17/14; *TransCanada v. United States*, ICSID Case No. ARB/16/21, and *Lone Pine v. Canada*, ICSID Case No. UNCT/15/2. There are other cases that have been threatened, or that have been initiated, but are not public.[7]

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[4] See OECD, Investor-State Dispute Settlement: Public consultation: 16 May – 9 July 2012 (OECD), pp. 23-26, Annexes II and IV, https://www.oecd.org/investment/internationalinvestmentagreements/50291642.pdf.

[5] See, e.g., *Mesa Power v. Canada*, PCA Case No. 2012-17, Second Submission of the United States of America (June 12, 2015); *Mesa Power v. Canada*, PCA Case No. 2012-17, Second Submission of Mexico Pursuant to NAFTA Article 1128 (June 12, 2015); *Mesa Power v. Canada*, PCA Case No. 2012-17, Submission of the Government of Canada, Observations on the Award on Jurisdiction and Merits (May 14, 2015).

[6] United States Trade Representative Robert E. Lighthizer, Testimony before House Ways and Means Committee (21 March 2018). Ambassador Lighthizer stated in testimony before members of the US Congress:

> We've had situations where real regulation which should be in place which is bipartisan, in everybody's interest, has not been put in place because of fears of ISDS ... Why should a foreign national be able to come in and not have the rights of Americans in the American court system but have more rights than Americans have in the American court system? It strikes me as something that at least we ought to be skeptical of and analyze. So a U.S. person goes into a court system, goes through the system and they're stuck with what they get. A foreign national can do that and then at the end of the day say 'I want three guys in London to say we're going to overrule the entire US system.'

[7] For instance, after dropping its first suit against the United States for stopping development of the Keystone XL Pipeline, TransCanada has announced it is bringing a second ISDS claim challenging the permit denial. However, there are not yet (as of the time of writing) publicly available filings evidencing the formal launch of the claim. See, TC Energy, News Release: TC Energy commences NAFTA claim following revocation of Keystone XL Presidential Permit (2 July 2021) https://www.tcenergy.com/announcements/2021-07-02-tc-energy-commences-nafta-claim-following-revocation-of-keystone-xl-presidential-permit/.

10. Even if ultimately unsuccessful on the merits, such actions increase the costs of, and uncertainty around, climate policy. It is reasonable to assume that, as government action in response to the climate crisis expands and accelerates, more claims under investment treaties will follow.

11. In addition to concerns about potential claims against the UK, there is a deep concern about UK investors using these treaties to thwart climate action abroad, as climate change is a global issue. Emissions do not stop at the border. Additionally, the lawsuits can place added budgetary strain on countries supported by the UK's development assistance, potentially undermining the UK's long-term efforts in and partnerships with those countries.[8]

12. Thus, it is crucial to ensure that both the investment protections in investment treaties and the ISDS mechanism used to interpret and apply those protections are not exploited so as to frustrate climate action, or shift the implementation of climate measures in ways inconsistent with the polluter pays principle. In addition, it is crucial to review investment treaties and treaty policy to ensure that their provisions on intellectual property and on performance requirements do not and will not prevent the (1) transfers of technology needed – and agreed to[9] – to achieve climate objectives; and (2) industrial policies crucial for ensuring that there is domestic political buy-in for, strategic design of, and beneficial economic spillovers from climate policy.

## Supporting Cooperation on Climate Action

13. As instruments of international cooperation – instruments used to raise floors, address collective action problems, and tackle challenges that no one country can solve, or solve as well, alone – treaties have a crucial and enduring role to play. It is important to ensure that instruments of international economic law and policy, such as investment treaties, are designed to buttress, not block, other related areas of international law and policy, such as climate law and policy. At present, investment treaties concluded by the UK (following the general practice) contain little in terms of cooperative mechanisms or institutions aimed at supporting beneficial investment flows, improving investment governance, or enhancing cross-border efforts to address transnational challenges.

[8] For a paper outlining and assessing countries' exposure to ISDS claims for climate measures, see Kyla Tienhaara and Lorenzo Cotula, 'Raising the Cost of Climate Action? Investor-state dispute settlement and compensation for stranded fossil fuel assets' (IIED 2020).
[9] UNFCCC Art. 4, paras. 1(c), 3, and 5, among others.