



The Arbitration Review of the Americas

2024

**Climate policies and investment:
implications for disputes**

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Climate policies and investment: implications for disputes

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Summary

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IN SUMMARY

Climate-related claims look set to increase in both litigation and arbitration contexts, and legislative and regulatory changes are creating more grounds for claims. The energy transition is changing investment incentives and priorities, and this seems likely to lead to disputes.

DISCUSSION POINTS

- Climate change as a growing source of disputes
- Changing face of investment in the energy sector

REFERENCED IN THIS ARTICLE

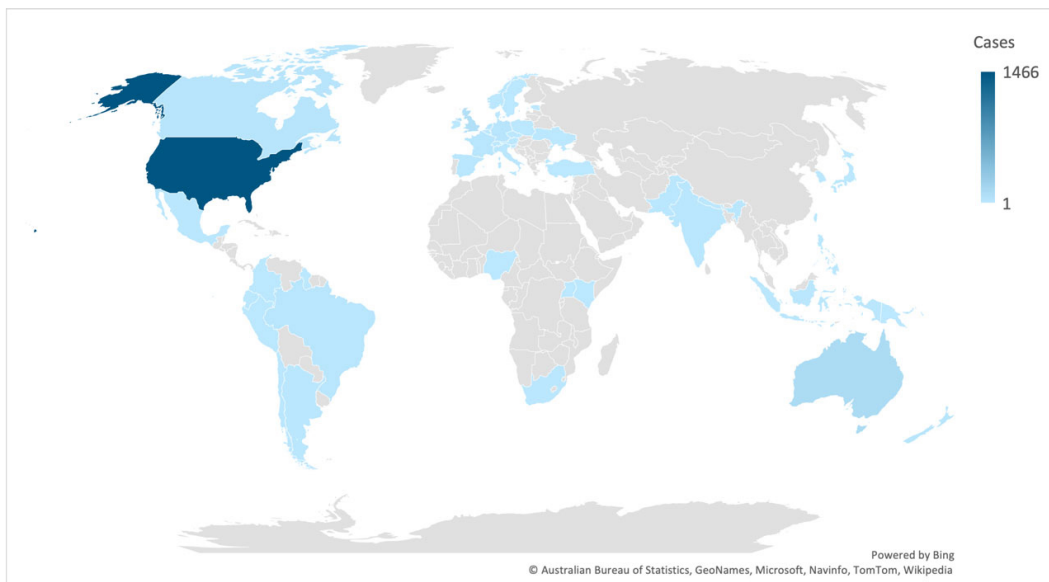
- UN Paris Agreement
- US Plan for Climate Change and Environmental Justice
- *Massachusetts v EPA*

INTRODUCTION

The transition to a low-carbon economy is not a new phenomenon, but one that has gained significant momentum in the past decade. Notably, since the signing of the Paris Agreement, governments around the world have taken steps to curb the effect of climate change through a variety of actions, such as setting date targets by which they would achieve 'net zero', phase out timelines of fossil fuels such as coal, introducing policies and laws to incentivise the development of low carbon generation assets. At the time of writing, according to available data, 94 per cent of countries globally have set out emission targets (including net zero, carbon neutrality, zero carbon, emission intensity, emission reduction and 1.5°C targets), and 10 per cent of those have included those targets in law.^[1]

Climate change is setting the scene and directing the actions taken by public bodies (eg, policymakers, governments, regulators) and private bodies (eg, energy majors, investment funds) alike. We have seen, as a result, significant changes to regulatory and policy frameworks, market dynamics and investment flows. It therefore follows that, over the past decade, climate change and the transition to net zero has become an increasingly prominent topic in dispute proceedings.

Figure 1. Total Climate Related Cases Around The World By Country (1986–April 2022)



Sources: CRA Analysis. Sabin Center 'US Climate Change Litigation' database and Grantham Research Institute 'Climate Change Laws of the World' database

In this article, we assess the trends behind the rise in climate change as a prominent topic in dispute proceedings. In particular we consider the trend in global investment away from fossil fuels and towards cleaner energy technologies, as well as growing policy and regulatory intervention to meet increasingly strict environmental targets set by governments around the world. These trends give way to some key considerations for disputes practitioners from growing climate issues in dispute proceedings. This includes their approach to legal issues, market analyses, asset valuation and damages calculations.

CLIMATE CHANGE AS AN ISSUE IN DISPUTE PROCEEDINGS

There is no one definition for the term 'climate change disputes'. In fact, climate change as an issue in dispute resolution appears in a wide range of cases, from cases where parties are trying to influence government policy or affect behaviour of corporates, to cases where climate change is affecting commercial decisions (such as through policy changes).

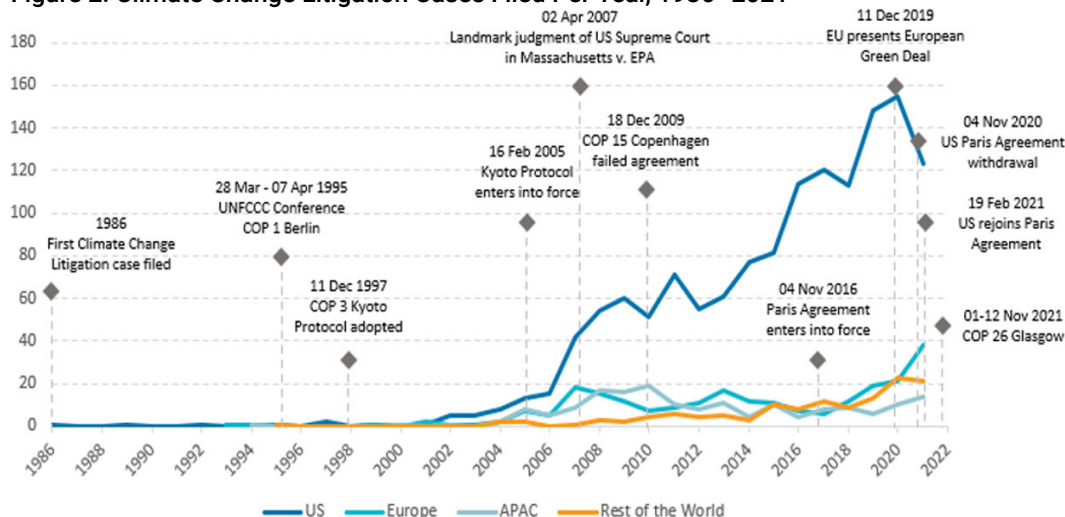
When referring to 'climate related disputes' we consider all dispute resolution mechanisms. We have sourced information from two primary data sources: the Sabin Center's US Climate Change Litigation database (for US based cases)^[2] and the Grantham Research Institute's Climate Change Laws of the World database (for non-US cases).^[3] (While these data sources are the most comprehensive resources available on the subject, they are not exhaustive.)

Following the first climate change litigation case in the US in 1986, a number of landmark environmental agreements and court judgments have sparked an increasing number of cases filed since the mid 2000s. The early 2000s saw a small number of claims against oil and gas companies for damage suffered as a result of extreme weather events; all, however, were unsuccessful due to jurisdiction and causation challenges in the cases.

Socioeconomic, regulatory and climate landscapes have changed globally, while over the past 20 years the number of climate change litigation cases filed each year has risen most prominently in the US. Between 2006 and 2015, 636 climate-related cases were filed in the

US. Most notable increases in case numbers may have been a result of events such as the landmark judgment of the US Supreme Court in the *Massachusetts v EPA* case in 2007,^[4] which established a regulatory mandate for measures to control greenhouse gas emissions in the United States. Cases in the period 2006–2015 were characterised by allegations of damage to legally protected interests caused by corporations' carbon emissions. Again, case issues revolved around the issues of causation and damage, and questions of standing and jurisdiction. An increase in climate change dispute activity was also caused by the failure of COP15 in Copenhagen in 2009 and the adoption of the Paris Agreement at COP 21 in 2015.

Figure 2. Climate Change Litigation Cases Filed Per Year, 1986–2021



Sources: CRA Analysis. Sabin Center 'US Climate Change Litigation' database and Grantham Research Institute 'Climate Change Laws of the World' database

In the period 2016–2020, 646 related cases were filed in the US, surpassing the total of the prior decade in half the time. With climate change now firmly on the global agenda, there is mounting pressure on policy and business leaders to take action and responsibility. In private climate litigation this period is characterised by claims of breach of human rights. The advancement of climate change science is beginning to allow claimants to quantify individual and historical emissions more accurately, forming better proof of causation arguments. The effect on the success of claims is not yet evident. There are, however, no signs of case numbers diminishing, and the Biden administration Plan for Climate Change and Environmental Justice is set to change the course of America's response to climate change.

INVESTMENT TRENDS AND THEIR DISPUTE IMPLICATIONS

During the past 10 years, investment behaviours have been affected by developments such as the affordability of clean technologies (through financing, and without relying on subsidy programmes), the emergence of new technologies, and increased policy and regulation to support net-zero targets. Further, important drivers from governments that affect investment activity include targeted incentives (eg, feed-in tariffs for particular technologies) and carbon pricing. The stability, tenure and competency of political leadership also affects the rate of change of policy. Simultaneously, policy decisions depend on the maturity of the technologies at the time of the decision and country-specific potential for their introduction.

Other interrelating forces include nascent technology's reliance on funding, the intermittent nature of most clean energy solutions setting climate concerns against energy security, and the effect of media coverage on environmental and policy issues in mobilising public pressure on government.

The need for specific expertise is increasing, questions of jurisdiction and causation are arising (who is to be held responsible?). We expect an increasing need for specific industry expertise for disputes practitioners to navigate questions of jurisdiction and causation but also issues of reasonable expectations and foreseeability as climate issues become embedded in disputes.

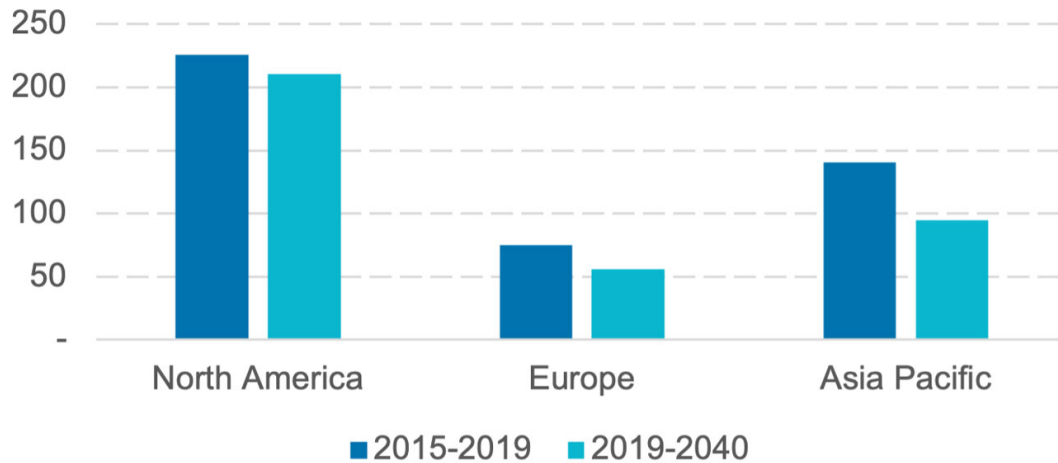
Declining Investment In Fossil Fuels Will Change Dispute Landscape

Energy capital flows over the past two years have been drastically reshaped due to the exceptional circumstances of the global pandemic and the growing momentum of ambitious green policies. The demand for, and consequently the investment in, oil, gas and coal has declined at a higher rate than previously forecast. The International Energy Agency (IEA) World Energy Investment 2021 report recorded a global fossil fuel supply investment drop of 26 per cent in 2020, followed by a 12 per cent rebound in 2021. Meanwhile global renewables supply investment increased 6.5 per cent in 2020 and 4 per cent in 2021.^[5] Legislative changes and net zero targets will lead to increasing closures or repurposing of facilities away from fossil fuels, which may lead to increased contract disputes in the areas of fair and equitable treatment, stranded assets or contract pricing benchmarks. However, fossil fuels have not reached their peak in some forecasts or regions, with some geographies such as Africa and Central and South America expecting to see increased investment in fossil fuel supply investment projects under the IEA Stated Policy Scenario.

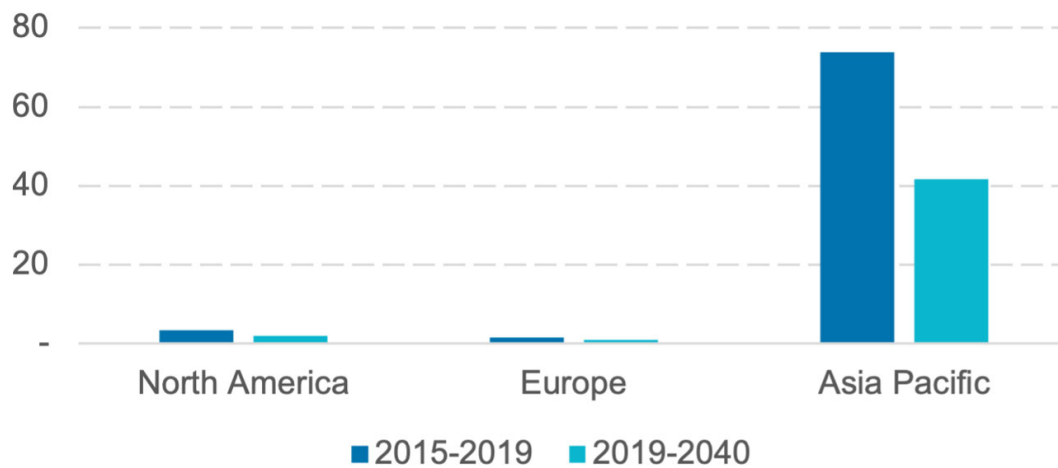
Projects that undermine the Paris Agreement goals possess lower investment incentives, and some investment bodies are planning to cease or restrict fossil fuel funding in the relatively near future. For example, the UK's largest pension fund, the National Employment Savings Trust, began fossil fuel divestment in July 2020 with a new investment policy to be net-zero by 2050.^[6] Other measures against high emissions, such as carbon pricing, are also making investments less attractive. As seen in Figure 3, average annual investment in fossil fuel supply is set to decline in North America, Europe and the Asia-Pacific regions in the coming decades. As investment moves away from fossil fuels, new value-creating opportunities are promised in renewables where technologies are maturing.

Figure 3. Average Annual Fuel Supply Investment (2019 \$bn)

Oil & Gas



Coal

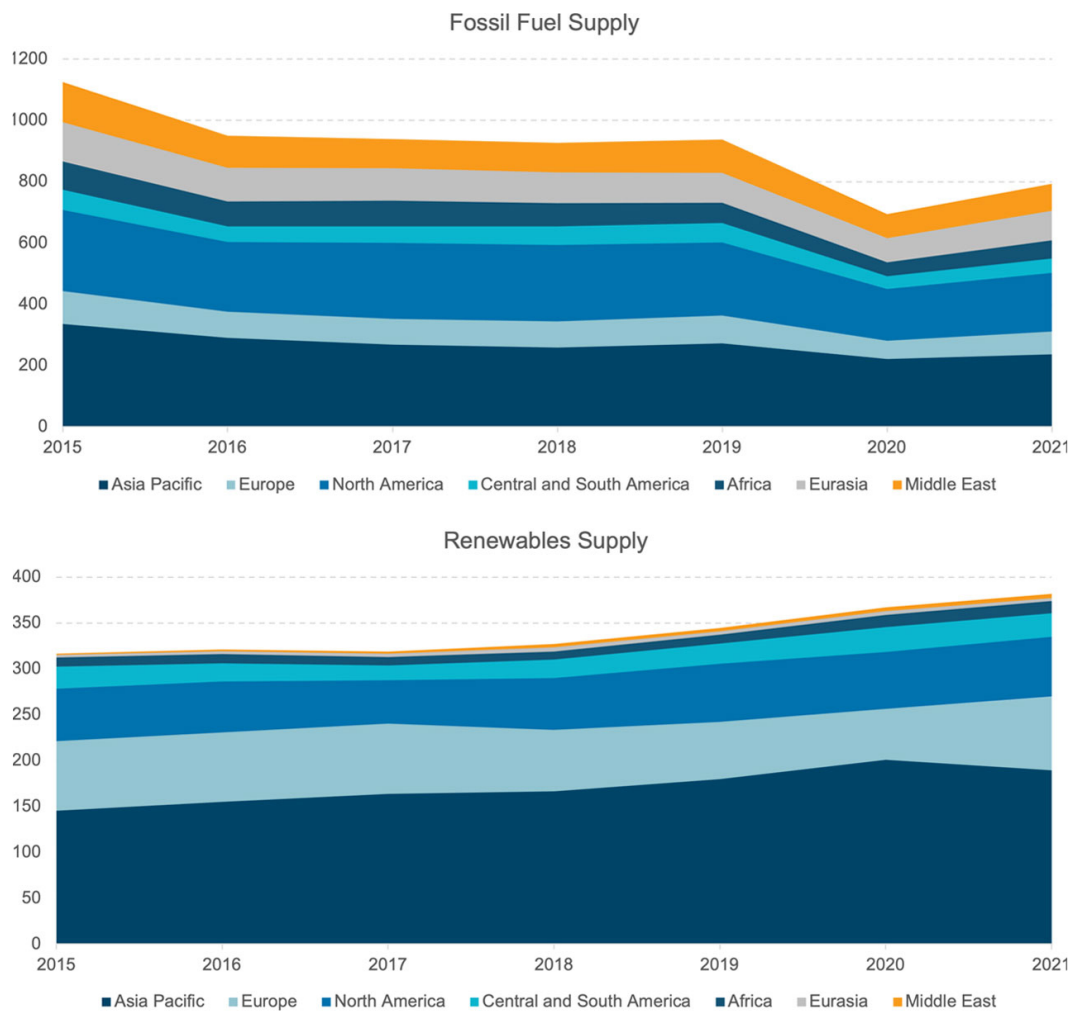


Sources: CRA Analysis of IEA World Energy Outlook 2019 (Stated Policies Scenario) and IEA World Energy Investment 2021 data

Despite diminished global demand and investment in fossil fuels owing to the pandemic and wider climate change agenda, global renewables investment is reported to have grown 4 per cent in 2021 relative to 2020, according to the IEA World Energy Investment 2021 report.^[7]

A positive historical trend in renewables investment has been developing and is set to continue as shown in Figure 4, owing to increased research and investment opportunities in low carbon industries, decreasing costs of renewable technologies and government subsidy schemes supporting the uptake of green electricity systems.

Figure 4. Historical Supply Investment (2019 \$bn)

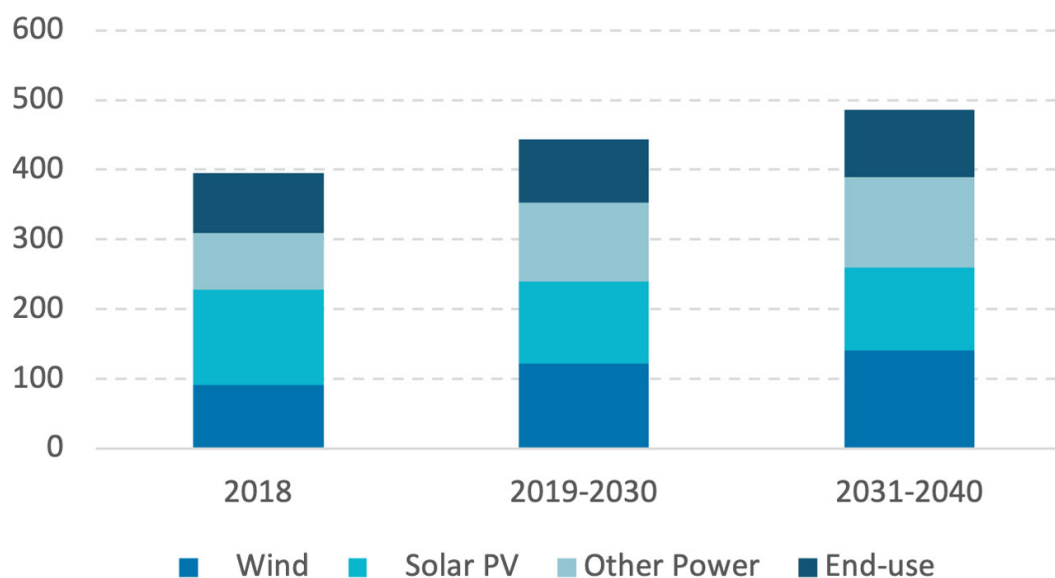


Sources: CRA Analysis of IEA World Energy Investment 2021 data

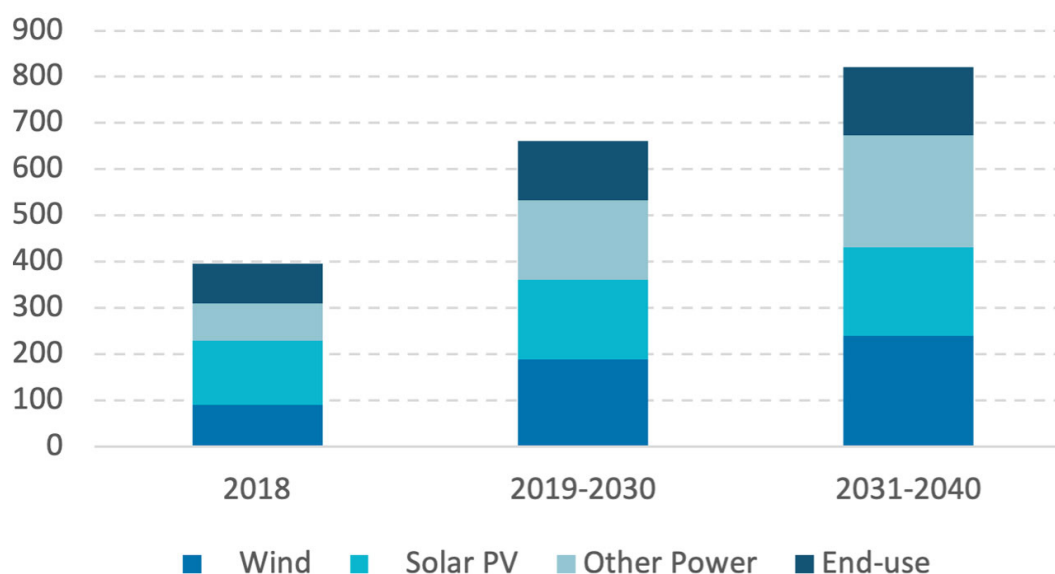
In this context, the intersection of new environmental standards with industrial activities has given rise to disputes in which performance versus standards is a central topic. These disputes often touch on the topic of 'greenwashing' and often require specialised expertise to adjudicate. In addition, nascent technologies which may rely on policies regulating their trade and marketing (eg, hydrogen and synthetic fuels) could encounter route-to-market issues resulting in disputes against regulatory bodies.

Figure 5. Global Renewables Average Annual Supply Investment (\$2019 Bn)

Stated Policies Scenario



Sustainable Development Scenario



Sources: CRA Analysis of IEA World Energy Outlook 2019

As has already been seen, disputes in this area have focused on the discontinuation of incentive schemes, whereby investors claim violation of fair and equitable treatment and of reasonable expectations. For example, the Spanish Promotion Plan for Renewable Energy (2000) included a feed-in tariff allowing solar plant owners to sell electricity at a higher rate for the first 25 years. However, in 2008 the government began to reduce the incentives due to a tariff deficit. By 2012 it had largely eliminated incentives for new photovoltaics. This led to many disputes, where investors made claims under the Energy Charter Treaty (ECT) relating to the solar subsidies that had been cut. Spain sought to resolve the issue by approving a Royal decree law (17/2019) in November 2019 to adapt remuneration parameters for the electricity system. This gave two options to investors involved in pursuing claims, either to drop the claim and receive a 7.39 per cent rate of return for 2020–2031 or to continue

with the claim and forfeit the new incentive and have their rate of return drop to 7.09 per cent, subject to review every six years.^[8] Investors who have renounced their claims include Element Holdings BV, Stadtwerke München, RREEF and Masdar, whose claims total around €3 billion.^[9] We are likely to see continued contract and sub-contract disputes concerning large scale projects involving multiple actors and jurisdictions, as well as multiple legal regimes.

Rights-based litigation is also expanding, which has been evident particularly since the landmark *Urgenda* ruling in December 2019 in favour of a Dutch environmental group.^[10] It was the first case globally where a court ordered a state to limit greenhouse gas emissions for reasons other than statutory mandates, in this case on the basis of articles 2 and 8 of the European Convention on Human Rights. It shows a clear path for the pursuit of climate litigation to protect human rights; however, the success of such claims is heavily dependent on jurisdiction. A possible end to the protection of fossil fuel investments in the ECT could change the types of cases seen in European countries. The EU and most member states are signatories to the ECT, which provides a legal framework to protect foreign investments and trade in the energy industry. However, in October 2020 the European Parliament adopted an amendment to a proposal that shall 'end protection of investments in fossil fuels in the context of the modernisation of the Energy Charter Treaty'.^[11] If successful, this would remove the ability for fossil fuel companies to sue states over climate action, consequently changing the number of disputes and the types of claims we expect to see in the future. In 2019, a bill was passed in the Netherlands to ban the use of coal in power generation by 2030; this triggered a lawsuit in 2021 whereby German utility RWE evoked the ECT against the Netherlands for the implementation of phasing out coal power plants.^[12] There is mounting tension as EU member states face a choice between protecting citizens against climate change through their justice systems by imposing pressure on the fossil fuel industry, or allowing the ECT investor–state dispute settlement (ISDS) mechanism to continue forcing governments to pay out large sums in settlement claims.

CONCLUSIONS

Evolving policy landscapes could have a domino effect on investment and disputes. Changes in investment trends look set to lead to an increased number of climate-related disputes, be they commercial disputes related to incentives or citizens' constitutional claims. But politically unstable countries with changing incentive schemes will deter investors.

There is a need for transparency in disputes with an underlying climate related issue, owing in no small part to public interest. A growing proportion of claims will be initiated by third parties, and there may be constitutional objections where governments are accused failing to take sufficient action. Although international arbitration provides flexibility and specific expertise and has been a preferred dispute resolution method for states and investors, its inherent lack of transparency could be problematic.

Endnotes

- 1 <https://zerotracker.net/>. [^ Back to section](#)

- 2 Sabin Center, The US Climate Change Litigation database. The Sabin Center adopts two criteria that must be satisfied for a case to fall within the scope of the database. First, cases must generally be brought before judicial bodies and second, climate change law, policy or science must be a material issue of law or fact in the case. Historically, the term 'cases' in the US database included more than judicial actions and proceedings. Other types of 'cases' formerly contained in the database included quasi-judicial administrative proceedings, rulemaking petitions, requests for reconsideration of regulations, notices of intent to sue and subpoenas. Since 2018, these other types of cases have not been added to the US database, and approximately 100 older such cases were removed from the database in November 2021. Further information regarding the criteria for case inclusion may be found here: <http://climatecasechart.com/about/> (Accessed July 2022). [^ Back to section](#)

- 3 Grantham Institute, Climate Change Laws of the World (CCLW) database. The Grantham Institute adopts a narrower definition of climate litigation, which focuses on 'judicial cases and targeted adjudications involving climate change presented to administrative entities and a few international bodies. In the CCLW database the case-files contain one or more of the following keywords: climate change, global warming, global change, greenhouse gas, sea level rise.' Grantham Institute 'Global Trends in Climate Change Litigation: 2020 Snapshot', July 2020, p. 5. [^ Back to section](#)

- 4 *Massachusetts v EPA*, 549 US 497 (2007). [^ Back to section](#)

- 5 <https://www.iea.org/reports/world-energy-investment-2021>. [^ Back to section](#)

- 6 <https://www.nestpensions.org.uk/schemeweb/nest/nestcorporation/news-press-and-policy/press-releases/Nest-going-net-zero-to-support-green-recovery.html>. [^ Back to section](#)

- 7 <https://www.iea.org/data-and-statistics/charts/key-estimated-energy-demand-co2-emissions-and-investment-indicators-2020-relative-to-2019>. [^ Back to section](#)

- 8 <https://www.miteco.gob.es/es/prensa/ultimas-noticias/el-consejo-de-ministro-s-aprueba-un-real-decreto-ley-para-dar-certidumbre-al-marco-retributivo-de-las-energ%C3%ADas-renovables-e-impulsar-una-transici%C3%B3n-ecol%C3%B3gica>. [^ Back to section](#)

- 9 <https://www.simmons-simmons.com/en/publications/ckhaj1g2c150d0965puipnu8j/will-more-renewables-investors-renounce-claims-against-spain->. [^ Back to section](#)

- 10 <http://climatecasechart.com/non-us-case/urgenda-foundation-v-kingdom-of-the-netherlands/>. [^ Back to section](#)

- 11 https://www.europarl.europa.eu/doceo/document/TA-9-2020-0253_EN.html
Amendment 143 on article 8a. [^ Back to section](#)

- 12 <https://icsid.worldbank.org/cases/case-database/case-detail?CaseNo=ARB/21/4>. ^
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