Modernisation of the Energy Charter Treaty

A Global Tragedy at a High Cost for Taxpayers

OPENEXP

"By the end of the coming decade we will be on one of two paths.

One is the path of surrender, where we have sleepwalked past the point of no return, jeopardizing the health and safety of everyone on this planet.

The other option is the path of hope.

A path where more fossil fuels remain where they should be – in the ground –

and where we are on the way to carbon neutrality by 2050."

António Guterres' remarks at the opening ceremony of the UN Climate Change Conference COP25, December 2019
United Nations' Secretary General

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Foreword

The global energy debate has changed drastically since the conception of the Energy Charter Treaty in the early nineties. At that time, energy security for energy import dependent countries, such as those in the European Union, was about ensuring access for continuous supply of fossil fuels.

Today, the world is facing a climate emergency. Energy transitions are underway - a shift towards decarbonized energy systems allowing countries to reach targets that result from climate accords. Reliable, affordable and clean energy for all is the goal.

I was proud to heed efforts to plot a critical path to achieving the Sustainable Development Goal on energy (SDG7) from 2016 through 2019. Its aim was to ensure that the goals of sustainable energy for all could be met by 2030 in the context of the PARIS Climate Agreement. This means that the energy access gap must be closed, that we need a revolution in efficiency in how we generate, transmit, distribute and use energy and that we would need to urgently decarbonize energy systems.

In achieving the SDGs developed countries have a dual responsibility. First, as the goals are universal, they must lead the way in achieving them. Secondly, they have a role in providing technical assistance, investment and funds to help lower income countries to leapfrog towards achieving the goals or to progress more rapidly. Policy coherence has become an important critique of development efforts. Countries subsidies of fossil fuels at home while giving aid to support nascent renewable energy markets abroad have been called out, not least by the UN Secretary-General in the run up to the Climate Action Summit in September 2019.

This report shows that there are continuing efforts to facilitate accession of developing countries to the Energy Charter Treaty whose purpose is to protect foreign investment in fossil fuels through an Investor-State-Dispute (ISDS) mechanism.

The accession of new countries, especially those with important fossil fuel reserves, means those countries at worst will be locked into a carbon intensive energy system that will prove an economic burden as well as having impacts on human health in decades to come. At best it provides only one part of a puzzle as countries will need to capture, use or store any emissions from fossil fuel use - and many commentators believe that the cost of this carbon intensive energy system is far more onerous than investing heavily in modern renewables, storage, green hydrogen and regional clean energy markets.

OpenExp's report on the modernisation of the Energy Charter Treaty (ECT) provides about important examination of another piece of the energy transition. It provides insights into the climate and financial impacts of the ECT.

In light of the increasing commitment to a Net zero economies by mid-century the report is an invitation to Contracting Parties to the ECT to consider carefully how the Treaty can adjust in order to contribute to that world.

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Acknowledgements

This analytical report was prepared by Yamina Saheb (OpenExp). It targets energy and trade policy makers and advisors involved in the ECT modernisation. The aim is to raise awareness about the potential climate and financial impacts of the ECT after more than two decades of its existence and the estimated impacts of the continuation of the binding protection of foreign investments in fossil fuels through the ISDS mechanism.

The report provides limited and concise explanations of the work performed and the data gathered. For the academic community, the content of this report will be included in a scientific article, which is under preparation. The scientific article should, therefore, be considered the most updated and accurate reference related to the results of this analytical work.

The report benefitted from valuable input provided by several experts including Katalin Bodis, Martin Dietrich Brauch, Mathilde Dupré, Rod Janssen, Adrian Joyce, Oliver Hailes, Masami Nakata, Heinz Ossenbrink and Kyla Tienhaara.

Cover page and layout by Bertrand Sadin

OpenExp is thankful to the European Climate Foundation for its financial support to this work.

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ISBN 978-2-9564721-7-9
EAN 9782956472179

January 2020

Executive summary

The ECT is a multilateral investment agreement solely dedicated to protecting foreign investments in energy supply through binding provisions. By January 2020, the Treaty has been ratified by 53 countries and the European Union/ Euratom. The ECT "*raison d'être*" became obsolete in 2009 with the withdrawal of Russia from its provisional application. Under the ECT regime, foreign investors can sue host States through arbitration tribunals, typically, composed of party-appointed private lawyers. Host States are legally bound to accept proceedings of these tribunals. However, in case foreign investors fail in meeting their contractual obligations, the host State is not protected by the ECT regime. The one-sided protection of the ECT regime made the Treaty an attractive tool to foreign investors. Nevertheless, the ECT failed in meeting its policy objectives. Contracting Parties launched, in 2009, a modernisation process to resuscitate the Treaty. Negotiations of the policy options to "*modernise*" the Treaty will take place during 2020.

The "modernisation" of the Energy Charter Treaty (ECT) is unlikely to lead to a fossil fuel-free and a climate friendly Treaty. In fact, despite being in an era of climate emergency, Contracting Parties active in the ECT modernisation did not propose to phase-out the binding protection of foreign investments in fossil fuels. The continuation, until 2050, of the binding protection of foreign investments in fossil fuels would end up with stranded fossil fuels assets amounting to €2.15 trillion. This is more than double the estimated investment needed to finance the European Green Deal in the next ten years. Crucially, the continuation of the binding protection of foreign investments in fossil fuels will potentially increase the cumulative carbon emissions protected by the ECT regime from at least 87 Gt by the end of 2019 to at least 216 Gt by the end of 2050. This is equivalent to more than one-third of the remaining global carbon budget to limit planet's warming to 1.5°C by the end of the century. The binding protection of carbon emissions qualifies the ECT for an "*ecocide*" Treaty given the scientific evidence available about the contribution of carbon emissions to the expected ecological disaster.

The continuation of the Investor-State-Dispute-Settlement (ISDS) mechanism under the ECT regime will, almost certainly, increase the cost of the energy transition for taxpayers in ECT signatories. The ISDS mechanism under the ECT regime is likely to continue in the "*modernised*" Treaty. Contracting Parties active in the modernisation of the ECT did not propose to end the use of arbitration tribunals for dispute settlement between foreign investors and host States. Ending, by 2020, all fossil fuels contracts protected by the ECT, since its entry into force, would potentially cost taxpayers €523.5 billion. The continuation of ISDS mechanism to protect fossil fuels, until 2050, under the ECT regime would potentially increase this cost to €1.3 trillion out of which 42% should be paid by EU taxpayers. This is slightly above the estimated investment needed to finance the European Green Deal over the next ten years. In the absence of provisions to end the ISDS mechanism under the ECT regime, investors will invest more in making their "*regulatory chill*" strategies highly effective. The "*right to regulate*" and other "*safeguards*" proposed by Contracting Parties are unlikely to limit the exploitation of investors and arbitrators of the ambiguities embedded in the ECT binding provisions.

The continuation of the "ecocide" ECT is a serious threat to the European Green Deal and to future carbon neutrality. The EU and its Member States cannot on one hand phase-out domestic investments in fossil fuels' operations, as confirmed by the EIB energy lending policy, and on the other

hand sign off on the continuation of the binding protection of foreign investments in fossil fuels under the ECT regime. The inconsistency between the EU domestic policies and its proposed policy options for the modernisation of the ECT puts at risk the ambition of the European Green Deal and its underlying goal to ensure EU global climate leadership. Making the ECT a fossil fuels-free Treaty is hardly achievable given the unanimity vote required to amend the Treaty and the contribution of fossil fuels' revenues to the economies of ECT signatories lacking a carbon neutrality target. The important gaps among ECT signatories in the progress made towards a fossil fuels-free energy system makes it unlikely that the negotiations would lead to a "*modernised*" Treaty contributing to the decarbonisation of the energy system and to a just energy transition.

A collective withdrawal of the EU and its Member States from the ECT could bring an end to the intra-EU disputes under the ECT regime and its survival clause without limiting cross-border investment flow in the EU. In fact, 67% of intra-ECT foreign direct investment in the EU are from investors hosted in EU countries. The EU and its Member States are facing, under the ECT regime, 88 ISDS cases out of which 83 are intra-EU disputes related to changes in incentives for electricity production from renewable energy sources. Total claimed amount for the 54 cases, for which information is available, is €15.9 billion. The arbitration industry has not so far agreed, and is unlikely to agree in the future, with the respondent States about the non-applicability of the ECT to intra-EU disputes. A collective withdrawal of the EU and its Member States could bring an end to intra-EU disputes under the ECT regime and its survival clause. Thus, cancelling the twenty years extension, after withdrawal, of the binding provisions of the ECT. Collaborating with Norway, Switzerland, Iceland and Liechtenstein to join the EU and its Member States' collective withdrawal from the ECT would be of paramount importance as these countries contribute at least 7% of foreign direct investments in the EU. Like in Achmea decision, national courts of Member States should seek a preliminary ruling from the European Court of Justice on the applicability of the ECT to intra-EU disputes.

The use of development funds to expand the geographical scope of the Energy Charter Treaty to the developing world raises moral and ethical questions. Expanding the ECT to the developing world will increase the global shares of carbon emissions protected by the ECT regime. Thus, jeopardising the Paris climate goal and its carbon neutrality objective. Carbon emissions do not stop at the administrative borders of the EU nor do the impacts of these emissions. Overall, the use of development funds to lock developing countries into the Energy Charter Treaty and its binding protection of foreign investments in fossil fuels through the ISDS mechanism is not aligned with the comprehensive strategy with Africa aimed for in the European Green Deal. EU financial and diplomatic instruments should no longer be used for making Africa the waste bin of the outdated European fossil fuels industry and the brain-dead ECT.

The climate emergency requires the development of a Treaty for the Non-Proliferation of Fossil Fuels to ensure effective implementation of carbon neutrality targets. Existing policies, such as those related to reducing energy demand and increasing the share of renewables in the energy mix, should be complemented with supply side policies targeting the end of the use of fossil fuels. Under the UNFCCC umbrella, the EU and its Member States could take a lead and join efforts with the most advanced countries in their carbon neutrality targets, to develop a Treaty for the Non-Proliferation of Fossil Fuels. Such a Treaty would require all countries to develop their roadmaps to gradually phase-out fossil fuels. Importantly, without such a Treaty, fossil fuels industry and its allies will not hesitate to use existing means and to invent new ones to delay climate action at a high cost for taxpayers.

Understanding the Energy Charter Treaty ■

The *"Raison d'être"* of the Energy Charter Treaty (ECT)

The ECT is a multilateral agreement solely dedicated to the energy sector. By January 2020, the Treaty has been ratified by 53 countries and the European Union/ Euratom. The Russian Federation, which was among the first signatories of the Treaty, but never ratified the agreement, withdrew completely in 2009 and Italy withdrew from the Treaty in 2015.

The ECT entered into force in 1998, with at least three major objectives to achieve:

1 - Contributing to energy geopolitics by overcoming the political divisions between Eastern and Western Europe through a European energy market and an energy forum for exchange of best practices.

2 - Contributing to energy security of energy dependent Western European countries by ensuring a continuous supply of fossil fuels from the East to the West.

3 - Contributing to overcoming the economic divisions between Eastern and Western Europe by ensuring a flow of Western investments in the energy sector in the East through binding protection.

However, after more than two decades of existence, the "*raison d'être*" of the ECT became obsolete and evidence suggests that the flow of investments in the energy sector is not driven by the ECT.

ECT contribution to energy geopolitics

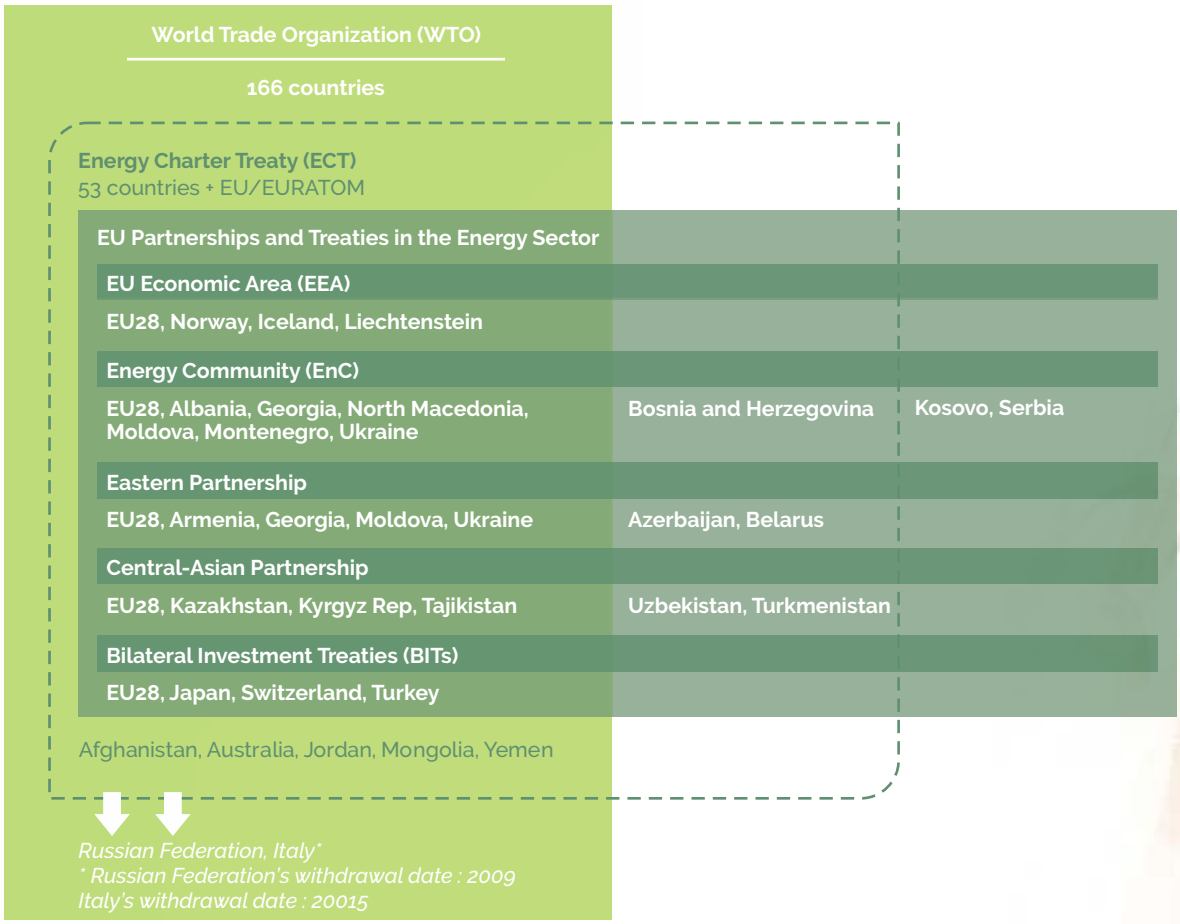
The purpose of the Energy Charter Treaty is *to "establish a legal framework in order to promote long-term cooperation in the energy field, based on complementarities and mutual benefits, in accordance with the objectives and principles of the Charter"* (Article 2 of the Treaty [1]). The Charter referred to in this Article is the political declaration, adopted in 1991, known as the European Energy Charter [1]. Its signature is required to become an ECT signatory.

Signatories of the European Energy Charter aim at *"improving security of energy supply and of maximising the efficiency of production, conversion, transport, distribution and use of energy, to enhance safety and to minimise environmental problems, on an acceptable economic basis"*. The objective is to create *"a broader European Energy market"* [1] which includes *"countries of Central and Eastern Europe"* [1] as well as Central-Asian countries. The aim was to overcome the political divisions between Eastern and Western Europe.

However, in the last two decades, new global/regional and bilateral treaties and partnerships emerged, making the geopolitical role of the ECT obsolete. This is particularly true since the withdrawal of Russia. ECT signatories are almost all members of the World Trade Organisation (WTO) which does not permit foreign investors to sue host States in international arbitration [2]. Azerbaijan, Belarus, Bosnia and Herzegovina, Uzbekistan and Turkmenistan are the only ECT signatories which are not yet members of the WTO. However, these countries have long standing partnerships with the EU either through the Energy Community (EnC) Treaty [3] or the Eastern and Central-Asian partnerships [4, 5] (Figure 1).

By January 2020, most Eastern European countries are either members of the EU or signatories of the EnC Treaty. The latter aims at building an integrated and sustainable pan-European energy market by extending the EU energy acquis to neighbouring Eastern countries [3]. Afghanistan, Australia, Mongolia, Jordan and Yemen are the only ECT signatories with whom the European Union (EU) does not have any other partnership. However, the contribution of these countries to the global energy dialogue in a warming planet is rather limited.

Figure 1. Overlaps between the ECT and other treaties and partnerships



Key point: Partnerships and treaties adopted since the ratification of the ECT, made the expected geopolitical role of the Treaty obsolete.

Source: The Energy Charter Treaty (ECT)- Assessing its geographical, climate and financial impacts [6]

ECT contribution to energy security in the EU

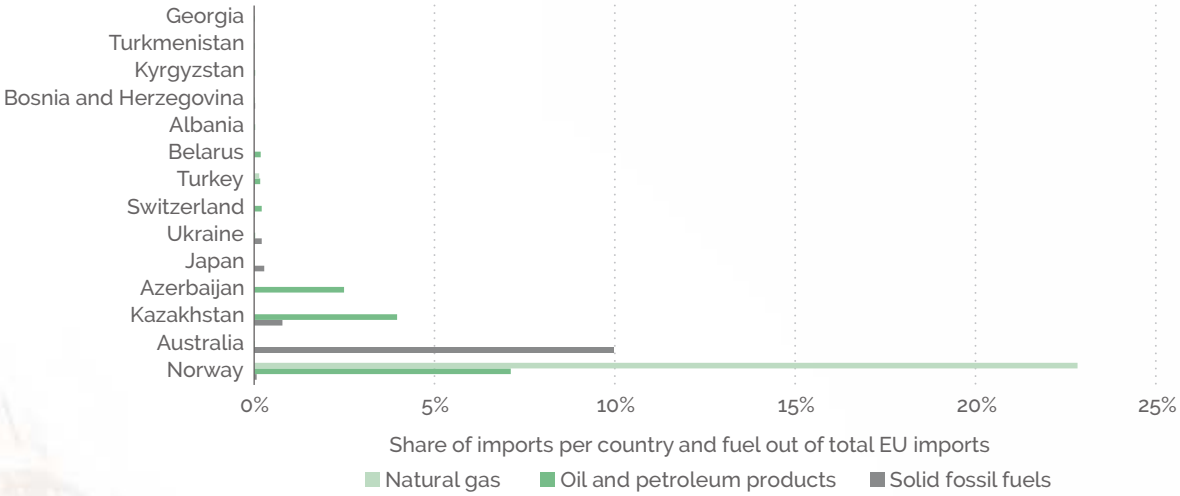
Strengthening the EU energy security by satisfying its hunger for fossil fuels was another objective of the initiators of the ECT. However, the contribution of ECT signatories to energy security in the EU has been, so far, rather limited. In fact, Russia, who is no longer an ECT signatory, remains the main fossil fuels supplier of the EU.

In 2018, ECT signatories contributed to total EU imports with 11% of solid fossil fuels, 14% of oil and petroleum products and 23% of natural gas. The same year, the EU imported from Russia 38% of its total imports of solid fossil fuels, 33% of its total natural gas imports while imports of oil and petroleum products from Russia were at 24%. Within the ECT constituency, Norway, which is also a member of the European Economic Area (EEA), is the main provider of natural gas and oil to the EU with 23%

and 7% out of total imports each. On the other hand, Australia contributed 10% to EU imports of solid fossil fuels (Figure 2).

Moreover, in a warming planet facing a climate emergency, the energy security debate has shifted from securing access to fossil fuels to saving the planet by phasing-out hydrocarbons and increasing the share of endogenous energy savings and renewables in the energy mix. This in turn, will reduce further the contribution to the EU energy security of fossil fuels exporting countries.

Figure 2. Contribution of ECT constituency to the EU supply of fossil fuels



Key point: Norway is the main ECT signatory contributing to Europe's supply of oil/ petroleum products and natural gas while Australia is the main ECT signatory contributing to Europe's supply of solid fossil fuels. .

Source: Based on Eurostat 2018 data

ECT contribution to the flow of energy investments from Western to Eastern countries

Over the period 2013-2019, the annual average Foreign Direct Investment (FDIs) in ECT signatories was at least at €87 billion out of which 62% were intra-ECT investments falling under the binding provisions of the ECT regime. However, extra-ECT FDIs are indirectly protected by the binding provisions of the Treaty as it is possible to adopt a nationality of an ECT signatory for convenience. It is worth noting that total FDIs might be higher, as at the time of writing, investment data for the identified 2018 and 2019 deals (energy contracts) in ECT signatories was still incomplete.

Importantly, EU Member States are the main recipients of FDIs in almost each of the economic activities in the energy sector as defined in the Nomenclature of Economic Activities in the European Community (NACE) (Table 1). In fact, investments in the EU, including intra-EU investments and those from investors hosted in countries that are members of the European Free Trade Area (EFTA), represented the highest shares of FDIs in all NACE economic activities except for manufacturing of coke oven products (Table 1). Furthermore, the attraction of non-EU/EFTA countries to FDIs is rather limited. This is particularly true for investors hosted outside the EU/ EFTA countries (Table 1), which suggests that the ECT failed in attracting FDIs in non-EU countries despite its binding investment provision.

Investments in fossil fuels represented at least 61% of total investments protected by the ECT while those in electricity production, trade and transmission represented 39% of total FDIs. The shares of

FDIs per country groupings and economic activities (Table 1) suggest that EU energy policies, especially internal energy market regulations, are the main driving factors for FDIs in EU Member States. Therefore, like in other sectors, FDIs decisions in the energy sector are, more likely, driven by national policies and country-level factors such as market size and per capita income, infrastructure and investment/energy policies [7].

Table 1. Shares of FDIs per NACE economic activities in the energy sector and country groupings

NACE economic activities in the energy sector	Intra-ECT out of total FDIs	Out of Intra-ECT FDIs					
		Intra-EU	EFTA in EU	Other ECT in EU/EFTA	EU/EFTA in EFTA	EU/EFTA in other ECT	non-EU/EFTA in other ECT
05 Mining of coal and lignite	87%	56%	0%	0%	0%	42%	2%
06(1) Extraction of crude petroleum	64%	55%	11%	16%	13%	2%	4%
06(2) Extraction of natural gas	55%	45%	16%	12%	19%	3%	5%
09(1) Support activities for petroleum and natural gas extraction	75%	58%	18%	5%	12%	0%	7%
19(1) Manufacture of coke oven products	6%	4%	0%	0%	0%	95%	1%
19(2) Manufacture of refined petroleum products	51%	60%	0%	4%	13%	23%	0%
35(11) Production of electricity	60%	87%	1%	7%	2%	2%	0%
35(12-13-14) Distribution, Transmission and Trade of electricity	69%	83%	0%	14%	1%	2%	0%
35(22-23) Distribution and Trade of gas	53%	83%	1%	10%	0%	3%	3%

Key point: EU Member States are the main recipients of FDIs protected under the ECT regime and EU investors are the most active ones in ECT signatories, but fossil fuels represent the highest shares of FDIs

Source: Based on ORBIS cross-border investment database for the period 2013-2019 [8]

ECT provisions

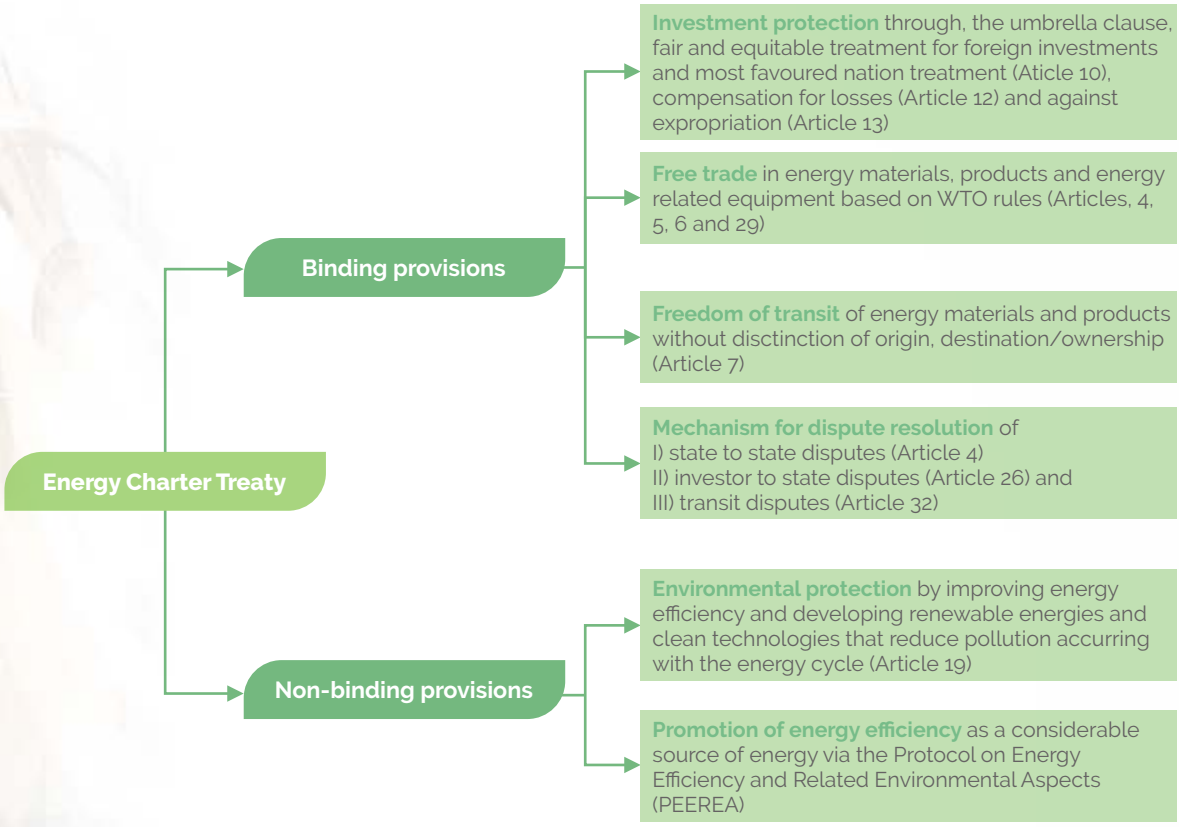
The ECT includes binding and non-binding provisions. Binding provisions are those related to investment protection, free trade, freedom of transit and mechanism for dispute resolution which distinguish between State-to-State disputes, investor to State disputes and those related to transit. Non-binding provisions are those related to environmental protection and the promotion of energy efficiency (Figure 3).

Investments protected by the ECT relate to economic activities which are defined in Article 1(5) of the Treaty [1]. These economic activities include "*the exploration, extraction, refining, production, storage, land transport, transmission, distribution, trade, marketing, or sale of Energy Materials and Products except […] those concerning the distribution of heat to multiple premises.*" [1]. Furthermore, Article 1(4) of the Treaty defines "*Energy Materials and products, based on the Harmonised System of the World Customs Organisation*

and the Combined Nomenclature of the European Communities, means the items included in Annexes EMI and EM II" [1].

Nuclear energy, coal, natural gas, petroleum and petroleum products, electrical energy, fuel wood and wood charcoal are the energy materials and products included in the annexes mentioned above. Renewable energy sources are not included in the list of energy materials and products. However, one of the illustrative economic activities in the energy sector considered in the understanding associated to Article 1(5) is the "*construction and operation of power generation facilities, including those powered by wind and other renewable energy sources*" [1]. Overall, the ECT regime protects foreign investments in energy supply only and without distinction between different fuels based on their environmental and human harm. However, investments in energy demand reduction, demand/response are not protected by ECT provisions despite being the only international agreement which considers energy savings as an energy source on it own. Distributed heat to multiple premises is also excluded from investment protection under the ECT regime.

Figure 3. Binding and non-binding provisions under the ECT regime



Key point: ECT binding obligations relate only to energy supply while provisions on environmental protection and energy demand reduction are non-binding

Source: The Energy Charter Treaty (ECT)- Assessing its geographical, climate and financial impacts [6]

Under the ECT regime, provisions on Investor-State-Dispute-Settlement (ISDS) allow foreign investors (companies, holdings, financial institutions and individuals) in the energy sector to allege Treaty violations by suing host States through ad hoc arbitration tribunals or institutional tribunals, such as the

International Centre for the Settlement of Investment Disputes (ICSID). These tribunals are composed of party-appointed private lawyers rather than career judges.

Amicable settlement of a dispute between an investor and a host State is one of the options proposed by the ECT. However, if a dispute cannot be settled amicably within a period of three months, the foreign investor can choose to submit the dispute either to the courts or administrative tribunals of the host country or to international arbitration for ISDS as described in the binding provisions included in Article 26 of the ECT [1] (Figure 3). Importantly, under the ECT regime, like under most investment treaties/agreements, an investor is not obliged to resolve disputes through available domestic remedies before filing ISDS claims.

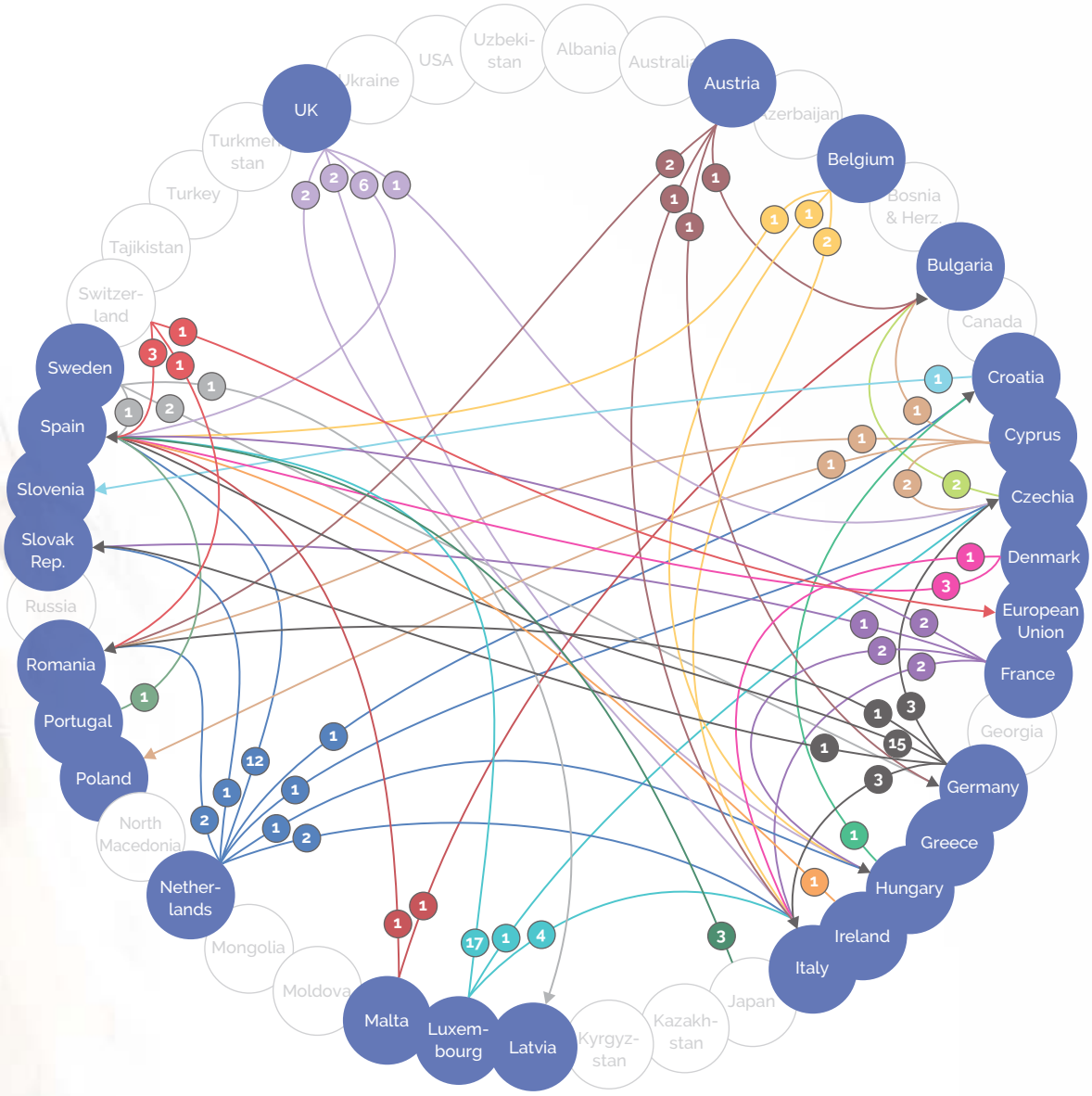
Moreover, it is presumed that the host State has given its consent to international arbitration by becoming an ECT signatory even before knowing who the claimant might be. Under the ECT regime, obligations are placed on the host States and not on the foreign investor. On one hand, host States are legally bound to accept ISDS proceedings based on claims brought against them by foreign investors. On the other hand, in the case a foreign investor fails in meeting its obligations under the local/national law, the host State must rely either on the national law, or on the terms of the investor-State investment contract, which a State entity such as a municipality might have signed with the investor, to achieve a settlement. The host State cannot use the ISDS mechanism under the ECT regime. Similarly, individuals and communities affected by the activities of a foreign investor cannot use the ISDS mechanism [9, 10]. Overall, the broad and one-sided binding investor protection provisions, the ISDS enforcement mechanism and the Treaty's wide geographical reach make the ECT a particularly attractive tool for foreign investors.

ECT impacts after more than two decades of existence

One of the major impacts of more than two decades of the existence of the ECT is the number of ISDS claims, their costs for taxpayers and the emergence of the arbitration industry in the energy sector. As of January 2020, the total number of publicly known ISDS claims under the ECT regime had reached 130. The actual number of disputes filled under the ECT regime might be much higher than the known 130 cases as the ECT regime does not require investors nor host States to make their ISDS cases publicly known.

To date, 29 ECT signatories are known to have been respondents to one or more ISDS claims brought by claimants based in 31 ECT signatories (Figure 4, 5). Spain is the most frequent respondent with 48 known ISDS claims (Box 1), followed by Italy with 12 known claims. 26 ISDS claims were brought by investors hosted in the Netherlands, while 24 claims were brought by investors hosted in Germany and 23 claims by investors hosted in Luxembourg.

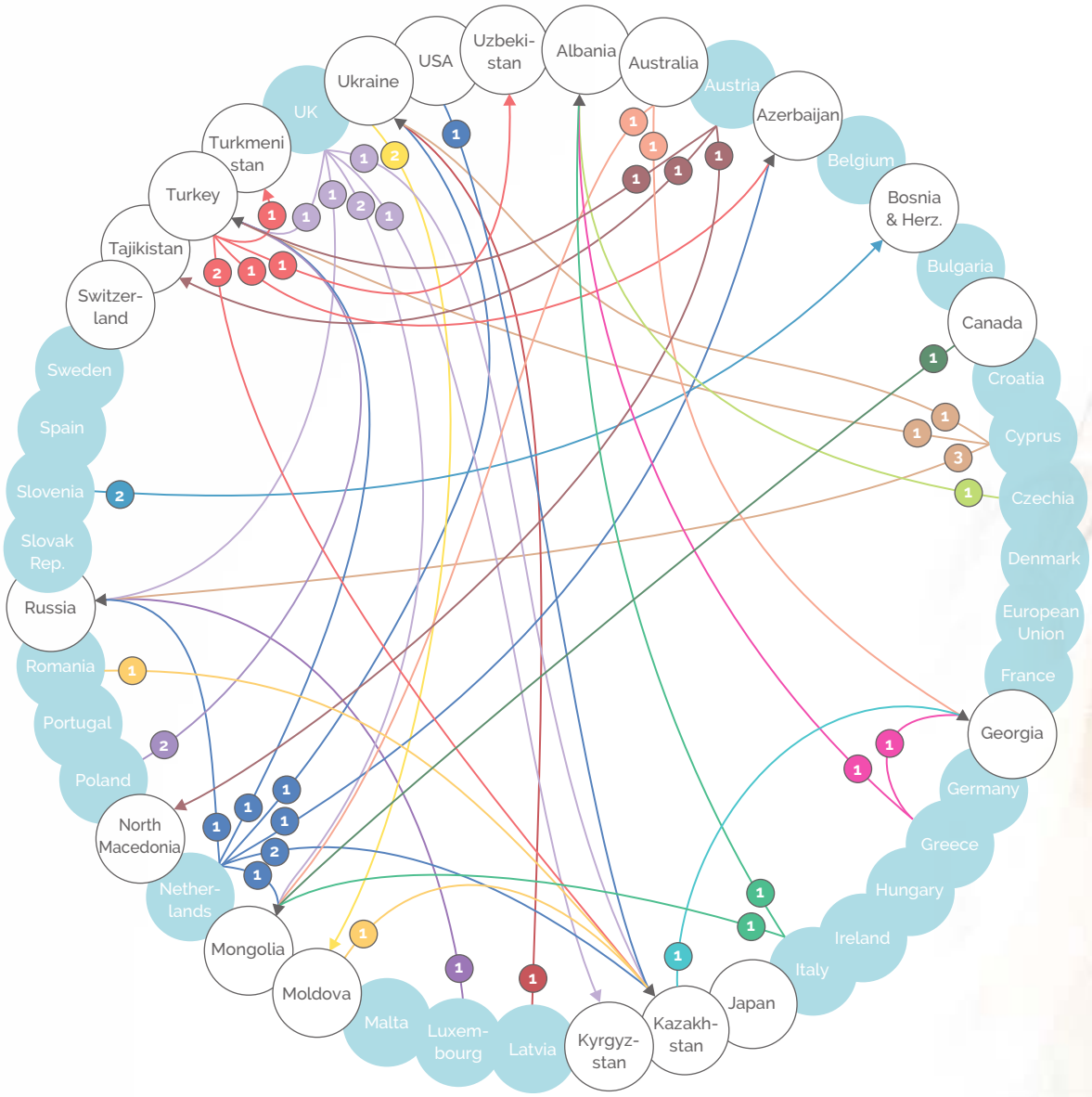
Figure 4. Respondent States and host States of ISDS claimants in the EU and its Member States



Key point: Spain is the most respondent State with 48 ISDS cases followed by Italy with 12 cases while the Netherlands is the host State for the highest number of claimants (26) followed by Germany and Luxembourg with 24 and 23 claimants respectively

Source: Based on data from UNCTAD Investment Policy Hub and List of ECT cases

Figure 5. Respondent States and host States of ISDS claimants in non-EU countries



Key point: ISDS claimants against non-EU countries are mainly hosted in non-EU countries

Source: Based on data from UNCTAD Investment Policy Hub and List of ECT cases

Box 1. The ISDS and the incentives vicious circle in Spain

Spain is the ECT signatory facing the highest number of ISDS claims which are all related to the governmental guarantee of rate of return of investment in renewable installations, which has changed after the investment has been made. As of January 2020, there are 48 known ISDS claims against Spain, out of which three involve non-EU investors from Japan and one from Switzerland. The amount claimed by investors for the 37 cases, for which information is publicly available, is €8.19 billion. The highest award being claimed against Spain is €1.9 billion from a transnational company which includes investors from Denmark, Germany, Ireland, Luxembourg, the Netherlands and the UK. The total amount to be paid by Spanish taxpayers is much higher as it will also include arbitration and legal costs which is estimated on average at €4.5 million. So far, arbitral tribunals rendered 11 cases in favour of investors, 2 in favour of the State and one case has been discontinued by the investor.

In response to the 48 known ISDS cases under the ECT regime against Spain, the government adopted, by the end of 2019, a new Royal decree [11] with the aim to end the vicious circle of changes in incentives leading to ISDS claims. The 2019 decree amends the Royal decree of 2013 [12] which has modified the feed-in-tariffs of the existing renewable power plants and lowered the rate of return of initial investment in renewable installations.

The new Spanish decree targets the regulatory period of 2020-2031 during which the rate of return of 7.398%, enjoyed during the regulatory period of 2014-2019, will be guaranteed by the government. This rate is higher than the 4.7% rate that would have been applicable for the period 2020-2025 based on the 2013 Royal decree. Furthermore, the decree extends the regulatory period until 2030. However, the new guarantee applies only to foreign investors that would agree to withdraw their ISDS claims against Spain by the end of September 2020 and to the investors in the process of enforcing their arbitral awards who would renounce all enforcement actions. Whether the 2019 Royal Decree would be more attractive to foreign investors than ISDS awards and would reduce the ISDS costs for taxpayers is yet to be shown.

The Spanish Royal decree raises the issue of the relationship between standards of protection for international investors and those that apply to domestic ones. The decree aims at promoting a Just Energy Transition. However, it enforces ISDS injustice by offering compensation to foreign investors using public money paid for by Spanish SMEs and individual investors which do not benefit from a similar treatment. Basically, domestic investors must pay for the privileged foreign investors because the country is trapped by the ECT. The decree may also encourage domestic investors to incorporate oversea in order to qualify for ECT protection.

It is worth noting that Spain is chairing the modernisation sub-group.

Status of arbitration in the 130 known ISDS cases

In 2019, foreign investors initiated seven publicly known ISDS cases under the ECT regime, which is equal to the number observed in the two previous years. Importantly, 2019 is the year where the first ISDS case against the EU has been filled by Nord Stream 2 AG, a subsidiary of the State-owned Russian company Gazprom

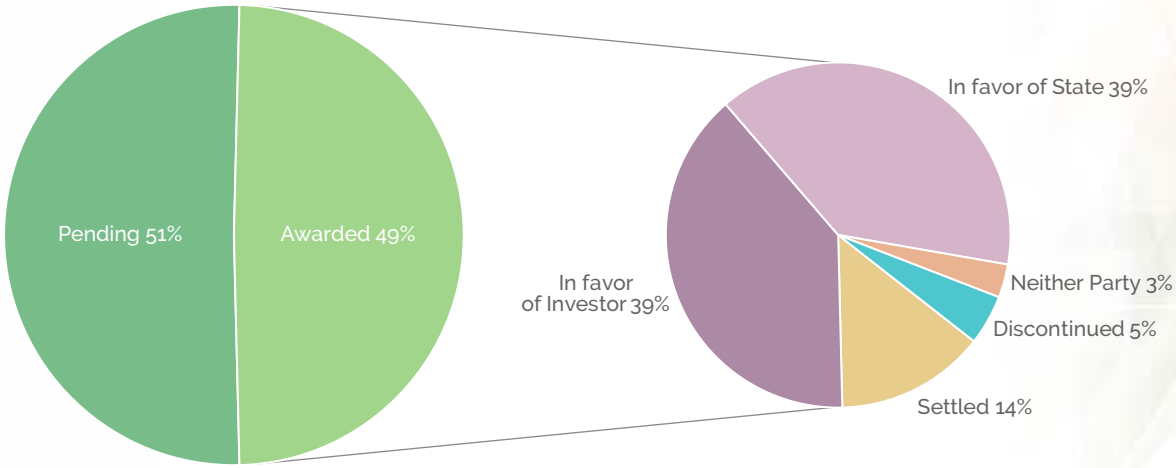
but headquartered in Switzerland. According to the information available, Gazprom considers the extension of the EU internal unbundling rules, under the 2019 recast of the EU Gas Directive [13], to third countries discriminatory and a breach of the Fair and Equitable Treatment (FTE) provisions under the ECT regime.

In 2019, the arbitral tribunals rendered at least three substantive ISDS decisions, which is equal to the number of decisions rendered in 2018. The three 2019 decisions were in favour of investors and are all related to changes in incentives in Spain. Claimants were from France, Germany and Luxembourg. The total amount claimed by these investors was €224 million and the total amount awarded was €115.7 million. The alleged breaches include Fair and Equitable Treatment (Article 10.1), indirect expropriation (Article 13), the umbrella clause (Article 10.1) and discriminatory measures (Article 10.1) of the Treaty [1].

The 2019 rendered claims were initiated in 2015, which is equivalent to four years of legal procedures and costs for the Spanish government. Furthermore, two out of the 2018 decisions were also related to changes in incentives in Spain and the claimants were based in Luxembourg and the Netherlands. The total amount claimed by investors was €498 million and the amount awarded was at least €176.5 million. The exact award is unknown as in one of the claims Spain must pay interest to the investor. The two claims rendered in 2018 were initiated in 2013 and 2014 respectively which is on average four and half years of legal procedures to be paid by the Spanish taxpayer in addition to the awards.

As of January 2020, slightly more than half of the 130 ECT ISDS cases are still pending while 5% have been discontinued by investors and 14% settled. In total, arbitral tribunals have rendered decisions on the merits on 52 ISDS cases. 25 decisions were in favour of the State, another 25 decisions were in favour of investor while 2 decisions were in favour of neither party (Figure 6). In the decisions holding the State liable, arbitral tribunals most frequently found breaches of the Fair and Equitable Treatment and expropriation provisions. Importantly, the cases rendered in favour of States do not necessarily mean zero cost for the taxpayer as the arbitration cost is usually shared between parties and the host State must pay for its own legal costs. The latter occurs also in the discounted and settled cases.

Figure 6. Status of arbitration of the 130 known ECT ISDS claims



Key point: Decisions in favour of State do not necessarily mean zero cost for taxpayers as usually the defendant has to pay for legal and arbitration fees

Source: Based on data from UNCTAD Investment Policy Hub and List of ECT cases

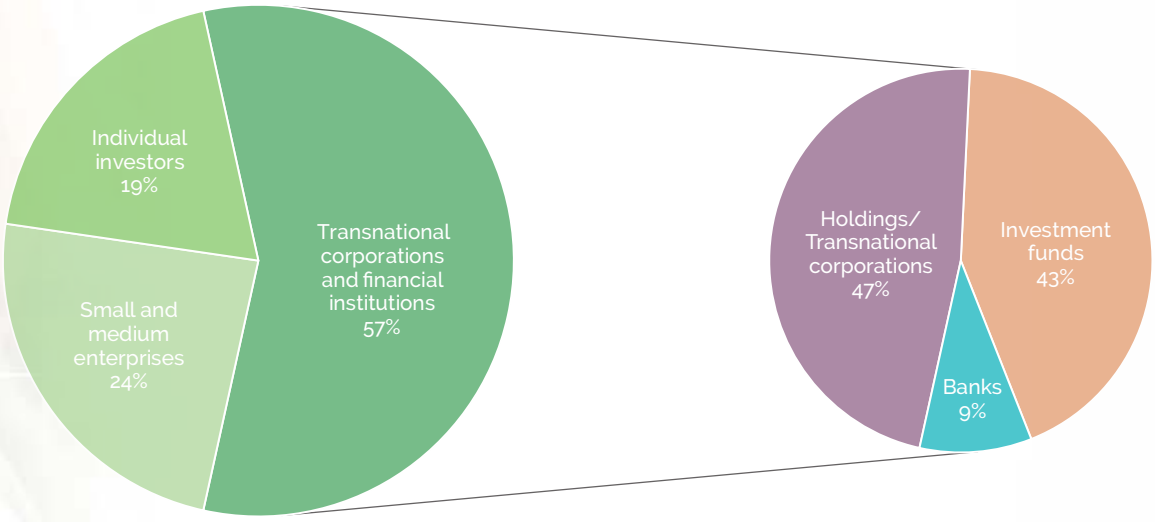
ISDS beneficiaries

More than half of the ISDS claims brought under the ECT regime were by transnational corporations and financial institutions out of which 47% were brought by holdings/transnational corporations and 43% by investment funds. This may explain the high number of investors hosted in the Netherlands or Luxembourg as these two countries offer advantageous tax incentives to foreign corporations. Thus, encouraging mailbox companies which are not prohibited under the ECT regime. ISDS claims brought by individual investors represented 19% out of the 130 known cases while Small and Medium Enterprises (SMEs) brought 24% out of the total (Figure 7).

As mentioned earlier, ISDS tribunals are typically composed of private lawyers appointed and paid by the investor and the host State. The increased number of ISDS claims, under the ECT regime, has led to the emergence of an arbitration industry in the energy sector composed of entrepreneurial arbitrators [10] who can order remedies, usually in the form of monetary awards, to investors if they find that States have breached the obligations of the Treaty. Under the ECT regime, there is a high contrast between the geographic origin of the arbitrators and the location of the respondent States. In fact, 15% of the appointed arbitrators are US-based, followed by the British, French and Canadian arbitrators with 12%, 10% and 6% respectively of appointed arbitrators while Spain is the main respondent State followed by Italy. It is worth noting that the United States (US) and Canada are not signatories of the ECT.

Arbitrators play an important role in the scope and the outcomes of ISDS proceedings which are based on their interpretation of the ECT provisions. The legitimacy of ISDS and the consistency of awards is increasingly criticised as arbitrators have a structural conflict of interest in deciding on whether they have jurisdiction to hear each ISDS dispute given the effects of a such decision on their lucrative business and costly fees [10]. Furthermore, arbitrators have multiple roles: they act as counsel for investors in some ISDS cases while they act as counsel for States in other cases [10].

Figure 7. Claimants per type of investor



Key point: More than half of the known ISDS ECT cases were brought by large transnational corporations and financial institutions

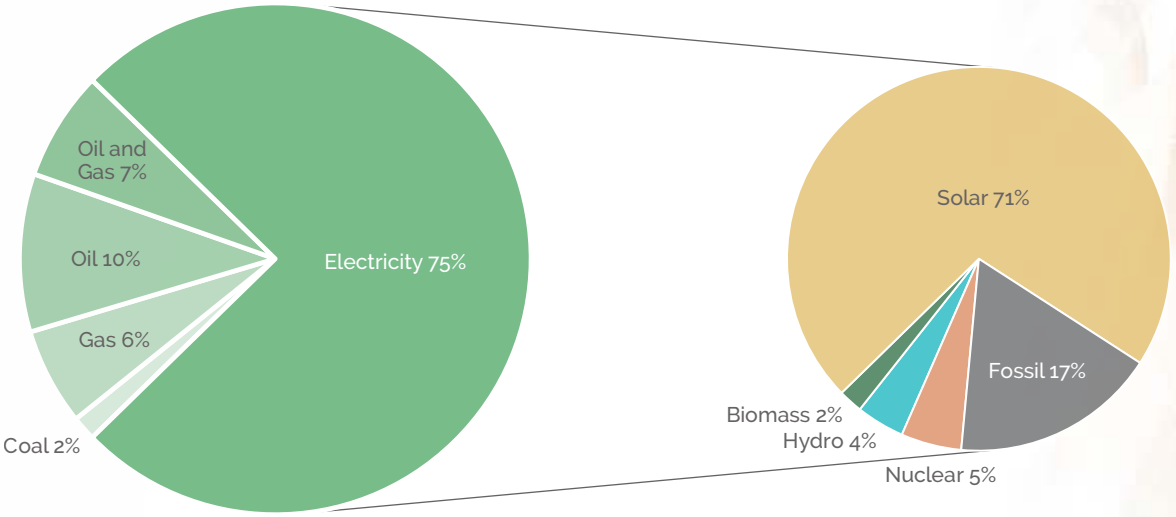
Source: Based on data from UNCTAD Investment Policy Hub and List of ECT cases

Another worrying development is the emergence of Third-Party Funding (TPF) of claims which pay for the high costs and high potential awards characteristic of arbitral awards in ISDS cases. TPF is a new industry composed of institutional investors who invest in litigation by providing finance in return for a stake in a legal claim and a contingency in the recovery. Funding arrangements usually involve investment funds which pay the legal fees on an interim basis and are paid back based on a contingency fee out of the award [10]. Research suggests that the emergence of the TPF industry contributes to the increase of the number of ISDS claims as it reduces the risk and cost of pursing a claim [14].

Energy products in the known 130 ISDS claims

The 130 known ISDS cases reflect well i) the list of energy materials and products protected by the ECT, ii) the energy mix of the signatory countries and iii) the progress made by these countries in shifting towards clean energy sources. Electricity deals are the most contentious ones with no distinction between different energy sources (Figure 8). In fact, three-quarters of the known ISDS cases are electricity related, out of which 71% relate to changes in incentives in renewables. The alleged breaches related to renewables are against EU countries while the alleged breaches related to the use of fossil fuels in the electricity sub-sector are against non-EU countries. Overall, ISDS cases per fuel reflect the different levels of commitment of ECT signatories towards a fossil fuel free energy transition.

Figure 8. ISDS claims per energy product (fuels as defined in the ECT)



Key point: Breaches alleged are mainly related to electricity deals with no distinction between energy sources

Source: Based on data from UNCTAD Investment Policy Hub and List of ECT cases

Intra-EU disputes

By January 2020, 83 out of the 130 known ISDS claims are intra-EU disputes mainly related to changes in energy subsidies. Based on the decisions rendered so far, EU Member States, facing the 83 intra-EU ISDS claims under the ECT regime, keep questioning the applicability of the ECT to intra-EU disputes (Annex I). However, arbitral tribunals held that the provision

of Article 1(3) of the Treaty [1] does not establish that EU Member States had transferred all their competence over energy investments to the EU nor did the EU Member States stopped being ECT Contracting Parties (except Italy who withdrew in 2015 yet faces the survival clause of twenty years of the application of the ECT binding provisions for investments made prior to the effective withdrawal of a signatory country).

Furthermore, arbitrators consider the term "Contracting Party in (Article 26) of the ECT [1] applicable at the same time to the State that ratified the ECT and the EU. Therefore, arbitrators keep concluding that being a national of an ECT Contracting Party as defined in Article 1(2) of the Treaty [1] means the claimants qualify as investors as defined in Article 1(3) of the ECT [1]. Overall, it is unlikely that the arbitration industry would agree with the respondent States about the non-applicability of the ECT to intra-EU disputes given the structural conflict of interest of arbitrators and the effects of a such decision on their lucrative business and costly fees. In fact, if arbitrators reject intra-EU disputes under the ECT regime, they will lose the opportunity of being appointed as arbitrators, thereby losing millions of Euros in fees as income.

Clarification about the applicability of the ECT to intra-EU disputes should be requested to the European Court of Justice (ECJ) by national court(s) of one or a coalition of the EU Member States facing one of the 83 intra-EU ISDS claims. This request is particularly important since, in 2018, ECJ ruled that ISDS clause in the Netherlands-Slovakia Bilateral Investment Treaty (BIT), ratified in 1991, is not compatible with the EU law. It is worth noting that the ECJ ruling confirmed the long-standing position of the EC about the inconsistency of the intra-EU BITs with EU law [9].

Furthermore, the ECJ ruling led EU Member States, in October 2019 *"to terminate their intra-EU bilateral investment treaties in a coordinated manner by means of a plurilateral treaty, unless bilateral terminations are considered mutually more expedient*" [15]. However, no decision has been taken regarding intra-EU disputes under the ECT regime. Instead, EU Member States agreed to discuss without undue delay the legal implications of the 2018 ECJ ruling on the applicability of the ECT regime to intra-EU disputes.

The lack of decision of EU Member States' reflects the disagreement between the countries about the applicability of the ECT regime to intra-EU disputes. In fact, 22 Member States have agreed, in January 2018, "*that the ISDS mechanism under the Energy Charter Treaty, if applicable to intra-EU relations, would be incompatible with EU law*" [16]. However, Finland, Luxembourg, Malta, Slovenia and Sweden, in a follow-up declaration, underlined "*the importance of allowing for due process and consider[ed] it would be inappropriate, in the absence of a specific judgment on this matter, to express views as regard the compatibility with the Union law of the intra-EU application of the Energy Charter Treaty*" [17]. Furthermore, Hungary in a separate declaration stated that "*the Achmea [2018] Judgment is silent on the investor-state arbitration clause in the Energy Charter Treaty and it does not concern any pending or prospective proceedings initiated under the ECT*" [18] and asked for further discussion.

It is worth noting that Sweden is the host State of the Stockholm Chamber of Commerce (SCC); an arbitration institution involved in at least 10 ISDS known claims under the ECT regime. Furthermore, Sweden, Luxembourg and Malta are host States of investors involved in 28 intra-EU ISDS claims under the ECT regime with a total claimed amount of €11 billion for the 20 cases, for which information is available (Table 2). This is equivalent to 69% of the total known amount claimed in the intra-EU ISDS cases. It is also worth noting that a State-owned Swedish company, claims from Germany a compensation of €6.5 billion over the phase-out of Nuclear

power plants and the implementation of EU environmental regulations. However, it is rather surprising for Finland to join this club as the country is not a host State nor a respondent of any of the known ISDS claims. Hungary is a host State of one investor and respondent in 4 claims. Slovenia is not a host State of any investor involved in intra-EU ISDS cases but respondent in one ISDS claim, in 2005, by a Croatian investor which claimed €24.5 million for a dispute over nuclear power plants.

Table 2. ISDS claimants in EU Member States non-signatories of the declaration to end intra-EU disputes under the ECT regime

Member State	Number of ISDS cases from claimants hosted in the country	Number of ISDS cases for which the claimed amount is known	Total known claimed amount by claimants hosted in the country
Sweden	4*	4*	€6.5 billion
Luxembourg	23*	16*	€4.6 billion
Malta	2	1	€42.8 million
Total	**28**	**20**	**€11 billion**

*One case, of €133.1 million, overlaps between Sweden and Luxembourg

Key point: Sweden, Luxembourg and to some extent Malta are host States of investors claiming 69% of the total known claimed €15.9 billion in intra-EU disputes under the ECT regime

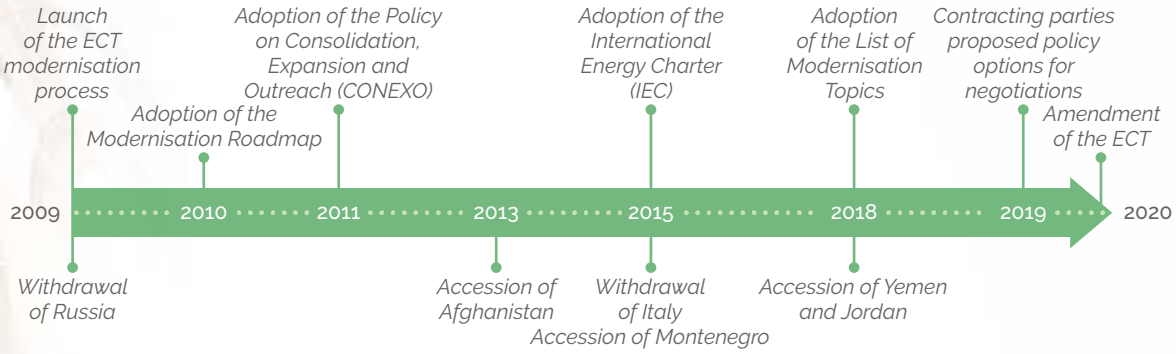
At this stage, arbitrators are rather silent regarding the historic agreement of EU Member States to end intra-EU BITs and how this decision will be implemented for the 9 ISDS cases under the ECT regime which also invoke intra-EU BITs. It is also unclear, if the ECJ is seized by national court(s) of one or a coalition of Member States, what its judgement would be in the case of the intra-EU ISDS disputes under the ECT regime. This is particularly true as Article 16 of the ECT [1], which relates to the relations of the Treaty to other agreements, stipulates "*that nothing in the other agreement shall be construed to derogate from any provision of Part III [Investment Promotion and Protection] or V [Dispute Settlement] of this Treaty [ECT] or from any right to dispute resolution with respect thereto under this Treaty [ECT], where any such provision is more favourable to the investor or investment*"[1].

Modernisation of the Energy Charter Treaty ■

The ECT modernisation process

The modernisation of the ECT is a multi-step and lengthy process (Figure 9) which started in 2009, the year Russia withdrew from the Treaty, with the recognition by the Energy Charter Conference, the governing body of the Charter, which is comprised of all ECT signatories, (hereinafter referred to as the Energy Charter Conference) "*that the Energy Charter Process must reflect new developments and challenges in international energy markets and respond to broader changes across its constituency*" [19]. The following year, a Strategy group was set "*to examine the possible options with regard the modernisation of the Energy Charter Process*" through "*consultations and negotiations on other Energy Charter Instruments required to deal with aspects of the Energy Charter Process, which may attract further expansion of its geographical scope*"[19].

Figure 9. ECT modernisation process



Key point: The ECT modernisation is a lengthy process of more than ten years with less than one year dedicated to discussing the policy options to be adopted

Source: Based on [19,21-28]

The finalisation of the modernisation process is planned for the end of 2020 when signatories of the Treaty are expected to conclude on the negotiations of the policy options on the table. However, contrary to the existing best practices in law-making such as the European Commission's better regulation guidelines [20], the proposed policy options for the modernisation of the ECT are not backed by the best available evidence nor by a comprehensive involvement of stakeholders. Moerover, a sound impact assessment which would have assessed the impact of each proposed policy option on different stakeholders has not been conducted despite being requested by Luxembourg in 2019 [21].

Similarly, the consultations, conducted during the lengthy modernisation process (Figure 9), were limited to observer countries of the Charter and industry representatives (mainly fossil fuels supply and petrochemical industries). Furthermore, the planned negotiations will take place behind closed doors and

only "*a short summary on [the] negotiations round will be made public without identifying the Delegations which made interventions*" [22]. Overall, more than ten years of governmental efforts were spent on the procedural and political aspects of the modernisation process against one year, with three meetings of four days each, planned for the discussions and negotiations of the policy options. The conference will take stock of the progress made by the end of 2020 [22]. ECT Contracting Parties decided that negotiations, "*including any subsequent amendment*" [22] will be concluded "*expeditiously*" [22], which suggests that the adoption of the "*modernised*" Treaty is expected for the end of 2020.

The implementation of the 2009 Energy Charter Conference's decision to modernise the Energy Charter Process went through four distinct phases

2010-2011: Modernisation roadmap and outreach policy

The first step in the ECT modernisation process was to develop a modernisation roadmap with seven identified areas to strengthen and/or to further develop. Identified areas include i) the promotion of the Energy Charter and the Energy Charter Treaty, ii) transit and cross-border trade, iii) emergency response, iv) investment promotion and protection, v) energy efficiency, vi) policy forum, interdependence, energy security; and vii) management, finance and legal affairs [23].

The approval of the modernisation roadmap by the Energy Charter Conference has led to the development and the adoption, the following year, of a Policy on Consolidation, Expansion and Outreach (hereinafter referred to as CONEXO) [24]. The CONEXO policy was articulated around three distinct pillars: *i) the consolidation of the ECT among its original signatories (Consolidation), ii) the attraction of key energy players, whose involvement would be beneficial to accede to the Treaty (Expansion)* and iii) *the promotion of the Energy Charter Treaty and Process at a global level (Outreach)* [24].

The consolidation pillar of the CONEXO policy aimed at the ratification of the Energy Charter Treaty by five countries, including Australia, Belarus, Iceland, Norway and the Russian Federation, who have signed the Treaty in early nineties but without ratifying it. The expansion pillar of the CONEXO policy targeted countries with the status of observers of the Energy Charter Conference. The Russian Federation re-confirmed, in 2018, its withdrawal, dated from 2009, from the provisional application of the ECT and Italy, who was one of the ECT Contracting Parties, withdrew in 2015. Furthermore, Afghanistan, Montenegro, Jordan and Yemen are the only four observer countries who joined the Energy Charter constituency respectively in 2013, 2015 and 2018 for both Jordan and Yemen while Iceland is the only "Consolidation" country which has ratified the Treaty in 2015.

It is worth noting that the remaining consolidation countries (Australia, Belarus and Norway) contribute to the budget of the Energy Charter Secretariat. However, the participation of these countries to the negotiations on the modernisation of the ECT is subject to their "*notification to the Secretariat of an official confirmation that a process of ratification of the ECT is ongoing at their domestic level or intended* "[22].

2012-2015: The International Energy Charter

The second step in the ECT modernisation process was the adoption, at the Ministerial Conference (the Hague II), of the International Energy Charter (IEC) in May 2015 [25] which complements the European Energy Charter, signed in 1991. The aim of the ECT signatories was to "*better reflect the new realities of the energy sector, especially the growing weight from developing countries, including emerging economies,*

and to serve the interests of the existing and potential participants of the Energy Charter constituency" [25].

The IEC is a political declaration which does not contain any legally binding obligation. However, its clear objective is to "*support the Charter's policy of Consolidation, Expansion and Outreach with the aim to facilitate the expansion of the geographical scope of the Energy Charter Treaty and Process*" [25] as well as *"to support active observership in the Energy Charter Conference, aiming at close political cooperation and early accession of observer countries to the Energy Charter Treaty"* [25]. The IEC has resulted in the increase of the number of observers of the Energy Charter Conference from 11 to 24 countries, 4 African regional organisations and 13 international organisations.

By January 2020, the IEC has been signed by 50 countries and the European Union/ Euratom, which is below the number of ECT signatories. However, IEC increased the number of observers. The newcomers to the Energy Charter Process are mainly developing countries with populations lacking access to energy but many of these countries have important fossil fuels reserves.

2017-2019: Modernisation topics and the proposed policy options

Following the internal discussions on the potential scope of the modernisation exercise, ECT signatories decided to consult with representatives from observer countries and industry (mainly energy supply and petrochemical industries) [26]. These two consultations were part of the six meetings where 25 modernisation topics (Table 3) were discussed and agreed [27]. The selection of the modernisation topics was based on recent decisions of the arbitral tribunals. The aim is to prevent the wide interpretations given by the arbitral tribunals to some of the ECT provisions and to provide for more policy space to the host States.

The next step was for Contracting Parties to propose policy options [21] to either clarify the existing provisions or to amend the Treaty by suggesting modifications to the current provisions. In the absence of an impact assessment, policy options proposed by Contracting Parties involved in the modernisation process (Figure 10), are based on individual experience gained by each Contracting Party from the implementation of the ECT, the new International Investment Agreements (IIAs) and BITs which entered into force after the ratification of the ECT.

Interestingly, despite more than ten years of governmental efforts on political and procedural aspects, the modernisation of the ECT does not seem to be of interest for at least 40% of the ECT constituency. Albania, Azerbaijan, the EU, Georgia, Japan, Kazakhstan, Luxembourg, Switzerland and Turkey are the only Contracting Parties who proposed policy options (Figure 10). However, Japan, who is co-chairing the modernisation sub-group, proposed, for each of the 25 identified modernisation topics, to not change existing ECT provisions [21].

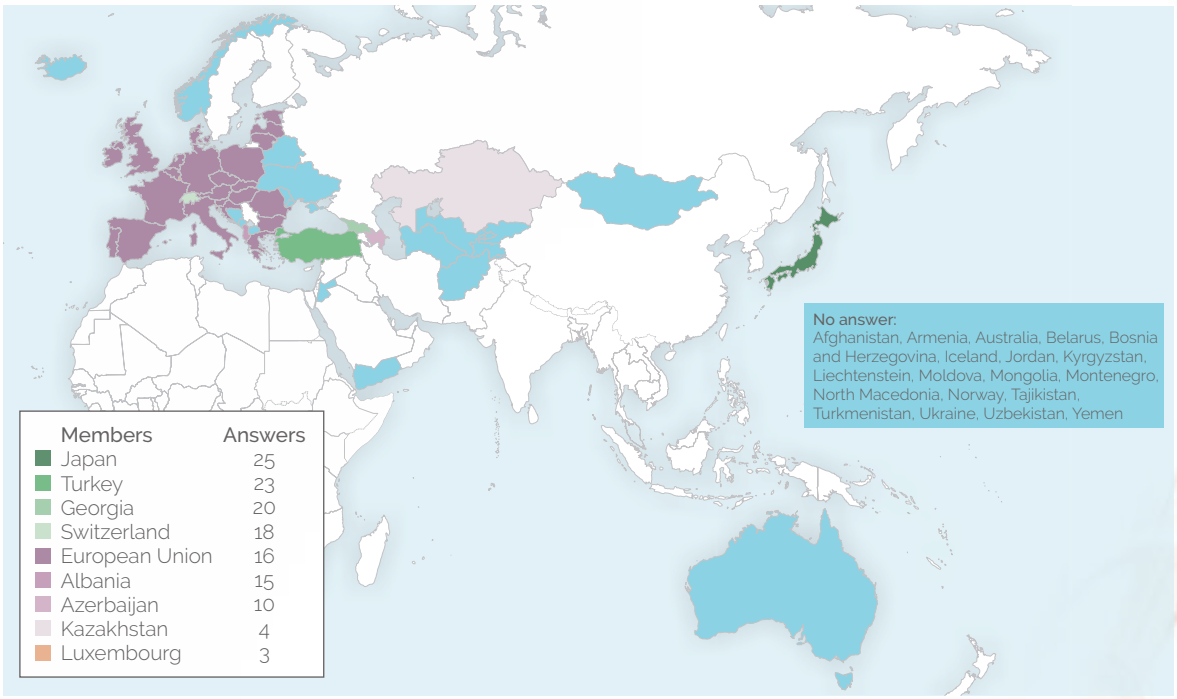
2020: Negotiation phase

The negotiation phase is planned to start in April 2020 and to end in October of the same year. ECT Contracting Parties agreed to conclude negotiations *"expeditiously"* [22], "*including any subsequent amendment*" [22]. Three negotiation rounds of four days each are planned during the year with the last negotiation round taking place in October. The decision to conclude "*expeditiously"* the negotiations "*including any subsequent amendment*" [22] suggests that amendments will be adopted at the 2020 Energy Charter Conference, scheduled on December 18th [28].

Planning to "*expeditiously*" conclude negotiations is rather unrealistic. In fact, according to Article 42 (2) of the ECT "*The text of any proposed amendment to this Treaty shall be communicated to the Contracting Parties by the Secretariat*

at least three months before the date on which it is proposed for adoption by the Charter Conference [1]." Technically, all amendments to the Treaty should, therefore, be submitted by Contracting Parties at the latest by September 17th as the 2020 Energy Charter Conference is planned for December 18th [28].

Figure 10. Contribution of ECT signatories to the 25 identified modernisation topics



Key point: 40% of the ECT constituency is not active in the modernisation process and Japan stands out by proposing to keep ECT provisions as they are for each of the 25 modernisation topics

Source: Based on [21]

Policy options on the negotiating table

The 25 modernisation topics, proposed by Contracting Parties for modernisation in 2018, include provisions spread across seven articles of the Treaty and suggests new provisions such as the right to regulate, transparency, sustainable development and corporate social responsibility. Overall, the provisions on the negotiating table can be grouped into five broad categories (Table 3):

1 - *The definitions* category which relates to provisions included in Article 1 of the Treaty.

2 - *The investment protection* category which relates to provisions included in Articles (10, 12, 13, 14 and 17) of the Treaty and the new provisions proposed by Contracting Parties to re-balance investment protection between host States and foreign investors such as the right to regulate.

3 - *The dispute settlement* category which includes new provisions proposed by the Contracting Parties.

4 - *The transit* category which relates to provisions included in Article 7 of the Treaty.

5 - *The miscellaneous category* which includes provisions that do not belong to any of the categories above and relate to either existing provisions or those to delete.

As mentioned earlier, not all ECT Contracting Parties are active in the modernisation of the Treaty (Figure 10 and Table 3). In fact, based on the number of suggested policy options, it is more likely that the negotiations will be steered mainly by Albania, Azerbaijan, the EU, Georgia, Japan, Kazakhstan, Luxembourg, Switzerland and Turkey. Japan stands out by proposing for each of the 25 identified modernisation topics to "*keep all ECT provisions as they are*"[21] and confirming that *"Contracting Parties retain the possibility to propose further options in the process of the modernisation of the ECT"* [21]. So far, the only two additional policy options proposed by Japan relate to pre-investment and denial of benefits. Negotiations on the pre-establishment will rather be challenging as Japan suggested to include provisions to protect the pre-establishment phase, while Turkey (the 2nd most active Contracting Party based on the number of responses) proposed to include provisions to explicitly exclude the pre-establishment phase from the ECT investment provisions and Georgia (ranked third based on the number of responses) as well as Albania suggested to keep the exclusion of the pre-establishment phase.

The EU and its Member States, where the ECT and the IEC were born, and which are the most challenged Contracting Parties by the provisions of the ECT, with 88 ISDS claims under the ECT regime, is the fifth most active Contracting Party based on the number of policy options proposed (Figure 10 and Table 3). Overall, EU responses are based on the negotiating directives [29] adopted by the European Council in mid-2019. However, it is unclear if Italy who withdrew as a Member State Contracting Party to the ECT is counted under the EU as a Contracting Party to the Treaty. Luxembourg is the only EU Member State that contributed with three policy options stressing the need to make the ECT Paris Climate Agreement [30] and Sustainable Development Goals [31] compliant.

Kazakhstan seems to be interested mainly by the provisions related to transit which raises questions about the potential geopolitical role of this country in a warming planet where fossil fuels will be phased-out. Consequently, transit of fossil fuels is not expected to be an issue in the 21st century. Surprisingly, Kazakhstan is also interested by the provisions related to the Regional Economic Integration Organisation (REIO) which are problematic mainly for the EU, the only REIO signatory of the ECT. However, the EU did not propose any policy option on REIO despite the objection of the EC and several Member States to the applicability of the ECT to intra-EU disputes.

Policy options proposed by Contracting Parties (Table 3) show that ECT modernisation has different meanings for ECT signatories which suggests challenging and lengthy negotiations. Importantly, three controversial aspects of the ECT are not on the negotiating table.

i) the end of Investor-State-Dispute-Settlement (ISDS),

ii) the phase-out of protection of foreign investments in unsustainable fuels (fossil and nuclear) and

iii) the end of intra-EU disputes.

Therefore, the potential outcomes of ECT modernisation, if any, will be rather marginal compared to the challenges raised in more than two decades of the existence of the ECT.

Table 3. Modernisation topics, their related articles in the ECT and proposed policy options by active contracting parties

Category	Modernisation topic	ECT related Articles	Number of ISDS cases where the Article was used	Rationale	Proposed policy option(s)	Countries interested by the issue	Instrument to use
Definitions	Definition of "Charter"	1(1)	At least in 5 ISDS cases	The International Energy Charter (IEC) is not included in the definition.	Include the IEC in Article 1(1).	Albania, the EU, Georgia, Switzerland, Turkey	Amendment
					No change	Japan	No change
	Definition of economic activity in the energy sector	1(5) and Annex EM	At least in 7 ISDS cases	The definition of economic activity in the energy sector is largely fossil fuels based which increases the risk of stranded fossil fuels assets and the share of carbon emissions protected by the ECT.	Extend the definition of economic activity to include new investment trends and technologies.	Albania, Azerbaijan, the EU, Luxembourg, Switzerland, Turkey	Amendment
					No change	Japan	No change
	Definition of investment	1(6)	At least in 32 ISDS cases	The definition of investment is very broad.	Require investment to fulfil specific characteristics and clear exclusion of certain types of assets.	Albania, Azerbaijan, the EU, Georgia, Switzerland, Turkey	Amendment
					No change	Japan	No change
	Definition of investor	1(7)	At least in 28 ISDS cases	Broad definition of an investor which leads to Treaty shopping.	■ Include additional criteria in the definition of investor. ■ Clarify the dual nationality. ■ Strengthen the denial of benefits clause.	Albania, Azerbaijan, the EU, Georgia, Switzerland, Turkey	Amendment
					No change	Japan	No change
Investment protection	Fair and Equitable Treatment (FTE)	10(1)	At least in 50 ISDS cases	■ Lack of clarity of the scope covered by FTE which leads to Treaty shopping and increases the risk of the use of the Treaty by shell companies. ■ Conflicts with the State's right to regulate in public interest.	Clarification of FET obligations.	Albania, Azerbaijan, the EU, Georgia, Switzerland, Turkey	Amendment
					No change	Japan	No change

Table 3. (continued)

Category	Modernisation topic	ECT related Articles	Number of ISDS cases where the Article was used	Rationale	Proposed policy option(s)	Countries interested by the issue	Instrument to use
Investment protection	Most constant protection and security	10(1)	At least in 21 ISDS cases	Some investors and arbitrators consider that both physical and legal protection of investors and investments fall under the scope of the most constant protection and security clause.	Clarify that most constant protection and security refers only to the physical security.	Albania, the EU, Georgia, Switzerland, Turkey	Amendment
					No change	Japan	No change
	Umbrella clause	10(1)	At least in 67 ISDS cases	State must respect any obligation it has assumed regarding a specific investment which means host States can be sued for any changes in their regulations. Thus, limiting the State's right to regulate.	Clarify/reduce the scope of the umbrella clause	Albania, the EU, Georgia, Switzerland, Turkey	Amendment
					No change	Japan	No change
	Pre-investment	From 10(1) to 10(6)	At least in 10 ISDS cases	Pre-establishment phase is implicitly not included in investment protection.	Keep the exclusion of the pre-establishment phase.	Albania, Georgia,	No change
					No change	Japan	No change
					Include provisions to protect the pre-establishment phase.		Amendment
					Include provisions to explicitly exclude pre-establishment phase.	Turkey	Amendment
	Most Favoured Nation (MFN) Clause	10(1), 10(2), 10(3) and 10(7)	At least in 33 ISDS cases	Confusing and ambiguous content leading to an abuse of the use of MFN clause by investors and arbitrators who consider the access to ISDS and the provisions related to investment itself under this clause.	Clarify that MFN does not include dispute settlement and excludes the use of provisions from other agreements.	Albania, Azerbaijan, the EU, Georgia, Switzerland, Turkey	Amendment
					No change	Japan	No change

Table 3. (continued)

Category	Modernisation topic	ECT related Articles	Number of ISDS cases where the Article was used	Rationale	Proposed policy option(s)	Countries interested by the issue	Instrument to use
Investment protection	Compensation of losses	12	At least in 3 ISDS cases	Undefined methodology to calculate compensation for losses.	No change	Georgia, Japan	No change
	Indirect expropriation	13 (1)	At least in 39 ISDS cases	Unclear definition of what makes States 'right to regulate in the public interest an expropriation.	Establish criteria to define expropriation (direct and indirect).	Albania, Azerbaijan, the EU, Georgia, Switzerland, Turkey	Amendment /Clarification
					No change	Japan	No change
	Transfers related to investments	14(1)	At least in 2 ISDS cases	State cannot impair transfer of funds.	Include a safeguard clause to adopt restrictive measures in the case of serious balance of payment, financial or monetary difficulties.	Azerbaijan, the EU Georgia, Switzerland, Turkey	Amendment
					No change	Japan	No change
	Denial of benefits	17 (1)	At least in 13 ISDS cases	The burden to show the claimant is a shell company or has adopted a nationality of convenience is put on the host State not on the investor.	Clear definition of substantive business and Georgia suggests extending the scope of the application of 17(1) to ISDS.	Albania, the EU, Georgia, Switzerland, Turkey	Amendment
					No change	Japan	No change
					Apply 17(1) to host country investors to avoid 'roundtripping'.		Amendment
	Right to regulate	No provisions	More than 2/3 of the known 130 ISDS cases	State's right to regulate is not expressly included in any particular provision of the ECT.	Include a new Article on the state's right to regulate.	Albania, Azerbaijan, the EU, Georgia, Luxembourg, Switzerland, Turkey	Amendment
					No change	Japan	No change

Table 3. (continued)

Category	Modernisation topic	ECT related Articles	Number of ISDS cases where the Article was used	Rationale	Proposed policy option(s)	Countries interested by the issue	Instrument to use
Investment protection	Sustainable Development and corporate social responsibility	No provisions	Rockhopper v IT, the announced Uniper vs NT and more ISDS cases are expected to come with the phase-out of fossil fuels in countries with carbon neutrality targets.	No provisions on sustainable development and corporate social responsibility.	Georgia & Switzerland: suggest making a reference to sustainable development in the preamble. Luxembourg: suggests a standalone Article. Turkey: suggests a declaration.	Azerbaijan, the EU, Georgia, Luxembourg, Switzerland, Turkey	Amendment /Declaration
					No change	Japan	No change
Dispute settlement	Frivolous claims	No provisions	At least in 21 ISDS cases	Initiation of claims without legal basis and evidence is possible under the ECT.	Include mechanism or procedure for early dismissal of frivolous and unmeritorious claims.	Albania, Georgia, Switzerland, Turkey	Amendment or New instrument
					No change	Japan	No change
	Transparency	No provisions	The 130 known ISDS cases and all the unknown ones	There is no obligation on the host State nor on the investor to make information on ISDS cases publicly available.	Include specific transparency regime but Georgia does not support straight incorporation of UNCITRAL rules on transparency.	Georgia, Switzerland, Turkey	Amendment
					No change	Japan	No change
	Security for costs	No provisions	Not identified	Concerns about the capacity of the respondent to cover adverse/arbitral costs.	Include specific provisions on security of cost to avoid frivolous claims.	Albania, Georgia, Switzerland, Turkey	Amendment or new Protocol
					No change	Japan	No change
	Third Party Funding (TPF)	No provisions	Not identified	Low level playing field when TPF gets involved in disputes as investors are not obliged to disclose their contracts with TPFs.	Obligation of compulsory disclosure of the TPF based on ICSID and UNCITRAL discussions.	Georgia, Switzerland, Turkey	New instrument
					No change	Japan	No change

Table 3. (continued)

Category	Modernisation topic	ECT related Articles	Number of ISDS cases where the Article was used	Rationale	Proposed policy option(s)	Countries interested by the issue	Instrument to use
Transit	Definition of Transit	7	Not identified	Swap operations, LNG, maritime transport and other new transit trends are not covered.	Revise the definition to include new transit trends, integrated energy markets with third party rights.	Azerbaijan, the EU, Kazakhstan, Turkey	Amendment
					No change	Japan	No change
	Definition and principles of tariff settings	7(1), 7(7) (f), 1(6), 10	Not identified	Lack of regulatory authorities in charge of setting transit tariffs may lead to abuse of dominant positions.	Define principles for tariff setting and introduce provisions to ensure the application of the agreed principles.	The EU, Kazakhstan, Turkey	Amendment
					No change	Japan	No change
	Access to infrastructure (including denial of access and available capacities)	7(5)	Not identified	Abuse of dominant positions.	Introduce an obligation to negotiate access conditions in good faith and clarify criteria for refusing access.	The EU, Kazakhstan, Turkey	Amendment
					No change	Japan	No change
Miscellaneous	Regional Economic Integration Organisation (REIO)	1(2), 1(3), 1(10)	The 83 intra-EU ISDS cases	Conflict between EU laws/ internal market regulation and ECT provisions.	Clarify legal relationship between REIO and its members under the ECT regime.	Kazakhstan, Turkey	Clarification
					No change	Japan	No change
	Obsolete provisions		Not identified	Several obsolete provisions are still included in the ECT.	Open to discuss provisions to remove from the ECT.	Albania, Georgia	Amendment
					No change	Japan	No change

Key point: Phasing-out fossil fuels' investment protection, ending ISDS and intra-EU disputes under the ECT regime are not among the modernisation options proposed by the active Contracting Parties (Albania, Azerbaijan, the EU, Georgia, Japan, Kazakhstan, Luxembourg, Switzerland and Turkey) in the ECT modernisation

Source: Based on [21] and data from UNCTAD Investment Policy Hub and List of ECT cases

Legal instruments to modernise the ECT

Clarifications, declarations, new instruments and amendments are the four options foreseen by the legislator to introduce changes to the ECT. Importantly, clarifications and declarations are non-binding while new instruments (i.e. Protocols) and amendments are binding to all Contracting Parties. In fact, Article 1(13-b) of the ECT stipulates that *"Energy Charter Declaration" or "Declaration" means a non-binding instrument"* [1]. On the other hand, new instruments such as Protocols are binding according to Article 1(13-a), which stipulates that *"Energy Charter Protocol" or "Protocol" means a treaty…"* [1]. Similarly, amendments are also binding to all Contracting Parties according to Article 42(4), which stipulates that amendments "*shall enter into force for any other Contracting Party…*" [1].

Voting rules represent the other major difference between the four options. On one hand, according to Article 36(4) of the ECT, declarations and Protocols require "*three-fourths majority of the Contracting Parties present and voting at the meeting of the Charter Conference…*" [1]. On the other hand, amendments require, according to Article 36(1) *"unanimity of the Contracting Parties present and voting at the meeting of the Charter Conference*" [1].

Despite the requirement to reach unanimity vote to adopt an amendment, amending some of the current provisions is the favoured option of the Contracting Parties active in the modernisation process (Albania, Azerbaijan, the EU, Georgia, Japan, Kazakhstan, Luxembourg, Switzerland and Turkey) (Table 3,4). However, as mentioned earlier, according to Article 42 (2), any amendment to the Treaty should be "*communicated to the Contracting Parties by the Secretariat at least three months before the date on which it is proposed for adoption by the Charter Conference* [1]." Therefore, Contracting Parties should submit their amendments, at the latest by September 17th as the 2020 Energy Charter Conference is planned for December 18th [28]. Achieving positive outcomes from the ECT negotiations is, therefore, rather challenging if not impossible.

Table 4. Legal instruments to introduce changes to the ECT

Instrument	Legal status	Voting rules	Modernisation topics for which the instrument was proposed	Contracting Parties who proposed the instrument
Clarification	Non-binding	Not defined	Indirect expropriation	Albania, Azerbaijan, the EU, Georgia, Switzerland, Turkey
			Regional Economic Integration Organisation	Kazakhstan
Declaration	Non-binding	Three-fourths majority	▪ Sustainable Development	Turkey
Protocols	Binding	Three-fourths majority	▪ Frivolous claims ▪ Security for costs ▪ Valuation of damage	Turkey
			▪ Third Party Funding	Georgia, Switzerland, Turkey
Amendments	Binding	Unanimity	23 modernisation topics	Albania, Azerbaijan, the EU, Georgia, Kazakhstan, Luxembourg, Switzerland, Turkey

Key point: ECT negotiations will be challenging as amendments, which require unanimity vote, represent the most favoured option of Contracting Parties

Potential impacts of ECT modernisation

Increasing the share of stranded fossil fuels' assets protected under the ECT regime

ECT signatories are all Parties to the Paris Climate Agreement which aims at *"Holding the increase in the global average temperature to well below 2°C above pre-industrial levels and pursuing efforts to limit the temperature increase to 1.5°C above pre-industrial levels, recognizing that this would significantly reduce the risks and impacts of climate change"* [30]. In 2020, Parties to the Paris Agreement are required to submit their updated Nationally Determined Contributions (NDCs) to the United Nations Framework Convention on Climate Change (UNFCCC) in which they are expected to align their climate ambition with the last scientific findings of the Intergovernmental Panel on Climate Change (IPCC) [32]. One of the major IPCC findings relates to the need to phase-out fossil fuels sooner than ever expected to avoid reaching the risky climate tipping points [32].

Luxembourg and Turkey made in their proposed policy options a clear reference to the Paris Climate Agreement [21]. However, making this reference is far from being enough, especially for EU countries. This is particularly true since the board of governors of the European Investment Bank (EIB), which is composed of Finance Ministers of the 28 EU Member States, approved revisions to the EIB energy lending policy in November 2019. In fact, the EIB energy lending policy stipulates that "*the Bank will phase out support to energy projects reliant on unabated fossil fuels*" by the end of 2021 [33]. Similarly, the EIB will invest outside the EU in projects with significant impact on decarbonising energy systems [33]. Phasing-out fossil fuels from the EIB portfolio inside and outside the EU is a real game-changer as the European bank is the biggest multilateral financial institution in the world.

Ironically, the week of the launch of the ECT modernisation was also the week of the launch of the European Green Deal which aims at making the EU the first carbon neutral region of the world by 2050 [34]. Being carbon neutral means Europe's energy mix will no longer include fossil fuels and action plans to gradually phase-out hydrocarbons will be developed by Member States and closely monitored by the European Commission (EC) and civil society.

Furthermore, in December 2019, EU leaders reached, an agreement on a unified EU classification system "taxonomy" to provide investors with a common language to identify economic activities which could be considered environmentally sustainable. The aim is to reduce "greenwashing" and to encourage private investment in a climate neutral economy. The proposed regulation [35] made it clear that investment in coal will not be considered environmentally sustainable and introduced the principle of "*do no significant harm*" to Europe's environmental objectives. Technical criteria to qualify for environmentally sustainable investment will be established by the EC in 2020 and enter into force by the end of 2021.

The phase-out of fossil fuels' investment protection should have been proposed under the revision of Article 1(5) of the Treaty and its related annexes [1]. Albania, Azerbaijan, the EU, Luxembourg, Switzerland and Turkey are the six contracting parties who proposed policy options to amend Article 1(5) [21]. However, the proposed policy option is only about covering *"new investment trends and new technologies*" [21] while the phase-out of fossil fuels was not suggested by any of the Contracting Parties active in the ECT modernisation (Table 3) [21].

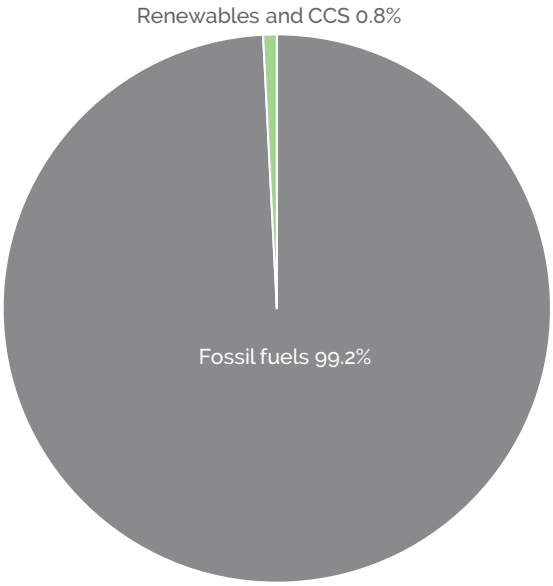
The EU went one step further in its narratives by suggesting to include "*a definition of the economic activity in the energy sector which allows addressing the challenges and*

opportunities of the transition to a safe and sustainable low-carbon, more digital and consumer-centric energy system". However, the policy option proposed by the EU does not include the definition referred to in its narratives (Table 3).

Basically, the EU and its Member States are phasing-out domestic investment in fossil fuels through the EIB energy lending policy, the Green Deal and the EU taxonomy for sustainable investment but plan to maintain protection of foreign investments in fossil fuels through the binding provisions of the ECT. Phasing-out fossil fuels from investment treaties is not a new idea. The Treaty for sustainable investment for climate change adaptation and mitigation [36] is an inspiring proposal to consider by the EU and its Member States to ensure the *"modernised"* ECT, if any, will be aligned with the Paris Climate Agreement [30] and the UN Sustainable Development Goals [31].

The continuation of fossil fuels' investment protection under the ECT regime will increase the share of stranded fossil fuels' assets protected by the Treaty. This is particularly true, as the fossil fuels industry continues to invest heavily in fossil fuels (Figure 11) and [37]. Overall, the need to phase-out fossil fuels infrastructures earlier increases the stranded capital which will not be recovered over the remaining operating time of the associated fossil fuels assets. Based on total FDIs in ECT signatories by January 2020 [8], stranded fossil fuels assets protected under the ECT regime, since its entry into force, are estimated at €870 billion. Importantly, in the absence of provisions to phase-out protection of foreign investments in fossil fuels, stranded assets under the ECT regime would reach at least €2.15 trillion by 2050. This is more than double the estimated investment need to finance the European Green Deal [38].

Figure 11. Oil and gas industry capital investment in 2019



Key point: Investment in clean energy solutions do not follow the announcements made by the fossil fuel industry since the signature of the Paris Agreement

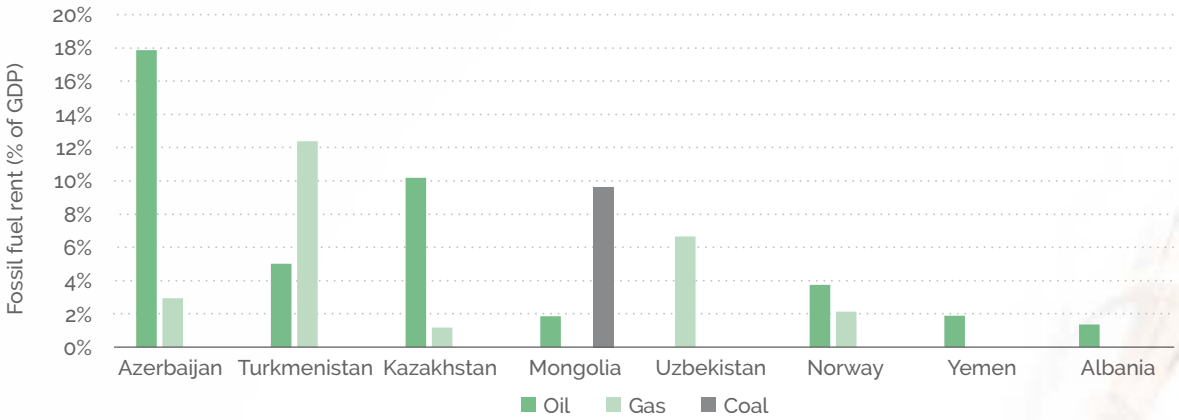
Source: Dr Evans from Carbon Brief based on IEA data [37]

The inconsistency between climate commitments of ECT signatories and their proposed policy options related to fossil fuels puts at risk the carbon neutrality target required for the implementation of the Paris Climate Agreement [30]. The EU and its Member States, which are the most advanced ECT signatories in setting their

carbon neutrality targets, cannot on one hand phase-out domestic investments in fossil fuels as confirmed by the EIB energy lending policy [33] and on the other hand sign off on the continuation of protection of foreign investments in fossil fuels under the ECT regime.

However, if the EU and its Member States would propose, during the negotiations, to phase-out fossil fuels' investment protection, this would require unanimity vote to amend the Treaty. It is unlikely that ECT signatories, with no carbon neutrality target, and making income out of fossil fuels (Figure 12), would vote for their phase-out from ECT investment protection. The important gaps among ECT signatories in the progress made towards a fossil fuels-free energy system make it unlikely that the negotiations would lead to a climate friendly "*modernised*" Treaty contributing to a just energy transition.

Figure 12. Fossil fuels' shares of GDP in ECT constituency



Key point: At least seven ECT signatories would, potentially, not vote to phase-out fossil fuels' investment protection from the Treaty

Source: World Bank 2017 data

Increasing the share of protected carbon emissions under the ECT regime

The binding provisions protecting foreign investments in fossil fuels under the ECT translate into binding protection of carbon emissions. Estimating CO_2 emissions protected by the ECT requires first estimating the amount of fossil fuels' investments protected by the ECT. Over the period 2013-2019, 61% of the protected investments under the ECT regime were investments in fossil fuels (extraction of coal and lignite, extraction of crude petroleum and natural gas, support activities for natural gas and oil extraction, manufacture of coke oven products, manufacture of refined petroleum products, distribution/trade of gas and fossil fuels electricity production).

CO_2 emissions are calculated for the targeted opportunities to unlock future CO_2 emissions if alternative technologies are affordable [39]. The assessment of the affordability of alternative technologies is based on the EU, given its share of FDIs. Cumulative emissions protected by the ECT, since its entry into force in 1998 until January 2020, are estimated at 87 Gt CO_2 out of which 62% are CO_2 emissions from intra-ECT investments in fossil fuels. Ironically, intra-EU cumulative emissions protected by the ECT are estimated at 30 Gt which is equal to the remaining EU carbon budget, to avoid the overshoot of the 1.5°C target, for the period 2018-2050 (Annex II). The continuation of investment protection of fossil fuels will, therefore, undoubtedly jeopardise Europe's carbon neutrality target and the Paris climate objectives.

Policy options proposed by Contracting Parties (Table 3) suggest three potential "*modernisation*" scenarios (Table 5):

1 - *No-change Scenario* based on the Japanese belief that "*it is not necessary to amend the current ECT provisions*" [21]. In this scenario, ISDS and protection of foreign investments in fossil fuels will continue as well as intra-EU disputes under the ECT regime (Table 5).

2 - *Trade Scenario* based on the various policy options for each modernisation topic proposed by Albania, Azerbaijan, the EU, Georgia, Kazakhstan, Luxembourg, Switzerland and Turkey (Table 3) [21]. Given the variety of the proposed options (Table 3) and the unanimity vote required to amend the Treaty, it is likely that Contracting Parties would vote for the lowest common denominator. In this scenario, the right to regulate would be introduced. However, protection of foreign investments in fossil fuels will not be phased-out and the ISDS under the ECT regime will continue to apply until hypothetical ISDS reforms would be agreed under the United Nations Commission on International Trade Law (UNCITRAL) and the World Bank's International Centre for Settlement of Investment Disputes (ICSID) (Box 2). Similarly, intra-EU disputes under the ECT regime will continue as Article 16 of the Treaty does not allow any derogation (Table 5).

3 - *1.5°C Target Scenario* which is based on policy options not included in the proposed ones by Contracting Parties active in the modernisation process (Table 3) [21]. In this scenario, phasing-out the protection of foreign investments in fossil fuels as well as ending ISDS and intra-EU disputes are considered. Such a scenario would allow the EU, Iceland, Norway and Switzerland, who have already agreed on a timeline to become carbon neutral, to ensure consistency between their climate policies, their domestic investment policies and their policies aiming at protecting, if needed, foreign investments in their territories (Table 5).

Potential future cumulative CO_2 emissions, which would be protected by the ECT under each of the three scenarios by 2050, are estimated by projecting FDIs in fossil fuels based on those for the period 2013-2019 and by assessing the announced climate and energy policies in signatory countries. Total cumulative emissions protected by the ECT since its entry into force and until 2050 result from the sum of the estimated emissions already protected by the ECT, since its entry into force (1998-2019), and the potential future cumulative ones for the period 2019-2050. In the Trade scenario, it is assumed that ISDS reforms under UNCITRAL and ICSID (Box 2) would at some point succeed in modernising ISDS mechanism and this would impact ECT provisions.

Importantly, the ECT cannot become a carbon neutral Treaty as foreign investments in fossil fuels and consequently in carbon emissions, over the last two decades, are already protected by the ECT. In fact, in the 1.5°C target scenario, which requires the phase-out of protection of foreign investments in fossil fuels, cumulative emissions protected by 2050 will be equal to those already protected by the ECT from its entry into force until 2019. This qualifies the ECT for an "*ecocide*" Treaty given the scientific evidence available about the contribution of past cumulative emissions to the expected ecological disaster. However, Contracting Parties could limit the "*ecocide*" effect of the ECT as there is a factor three between the no-change scenario and the 1.5°C target scenario (Table 5, Figure 13). It is worth noting that cumulative emissions by 2050 in the no-change scenario would be equivalent to more than one-third of the remaining global carbon budget for the period 2018-2050 to avoid the overshoot of the 1.5°C global warming (Annex II).

Table 5. Climate impact of ECT modernisation policy options

Criteria considered in each scenario	No-change Scenario	Trade Scenario	1.5°C target Scenario
Phase-out of fossil fuels	No	No	Yes
End of ISDS	No	No	Yes
End intra-EU ISDS under the ECT	No	No	Yes
Right to regulate	No	Yes*	Yes
Potential cumulative emissions protected by the ECT over the period 1998-2050 (Gt CO_2)	216	143	87

*Still investors can challenge policy measures and regulations such as those related to the phase-out of fossil fuels.

Key point: None of the policy options proposed by Contracting Parties is aligned with the 1.5°C target scenario

Source: Based on the proposed policy options included in [21]

Unfortunately, the voting rules, which require unanimity among Contracting Parties (Article 36) of the Treaty [1] and the high contribution of fossil fuels' revenues to the economies of some ECT signatories (Figure 12) are unlikely to lead to limiting the "*ecocide*" effect of the ECT. This is particularly true as phasing-out the protection of foreign investments in fossil fuels is not even one of the policy options on the negotiating table (Table 3).

Figure 13. Potential cumulative emissions protected by the ECT over the period 1998-2050 per modernisation scenario

Key point: The ECT cannot become a carbon neutral Treaty given the already protected emissions under the ECT regime. However, Contracting Parties could limit the "ecocide" effect of the Treaty by phasing-out investment protection of fossil fuels

Source: Based on the proposed policy options included in [21]

Increasing the ISDS financial burden on taxpayers

The EU, Georgia and Turkey made a reference in their proposed policy options to the on-going initiatives to reform ISDS at the multilateral level including the World Bank's International Centre for Settlement of Investment Disputes (ICSID) and the United Nations Commission on International Trade Law (UNCITRAL) Working Group III (Box 2). ISDS reforms introduced in the most recent BITs were also mentioned by the EU. The aim of all these reforms is to replace "*old ISDS*" mechanisms, such as those to which investors have access under the ECT regime, with modern ones which would address the identified concerns related to ISDS mechanism (Box 2).

Reforms under the ICSID are of high importance for the ECT regime as 65% of the known 130 ISDS cases were brought under ICSID procedural rules. The focus of ICSID is on Third Party Funding, the publication of awards, the initial procedures, the security for costs, the disqualification of arbitrators, the timing of awards and the expedited proceedings. A vote on the proposed amendments related to the focus areas of ICSID is expected to take place in 2020 [9].

Overall, the pending discussions and reforms at the UNCITRAL and ICSID levels are likely to have a direct impact on the application of ISDS provisions under the ECT regime. However, the timeframe of these parallel negotiations does not coincide with the "*expeditiously*" [22] nature of the ECT negotiations. Furthermore, achieving an agreement by the ECT constituency about the on-going ISDS reforms to consider under the "*modernised*" ECT regime is rather challenging given the variety of approaches of ECT signatories to the on-going ISDS reforms (Box 2).

Importantly, the EC impact assessment on multilateral reforms of ISDS [40] considered the option of renegotiating the ECT to align the dispute settlement provisions with the proposed EU permanent court regime. However, this option was considered "*burdensome in terms of time and resources*" [40] and has therefore been considered "*not feasible and not analysed in further details*" [40]. Similarly, the option of improving the ISDS under the ECT regime was also suggested by stakeholders involved in the impact assessment mentioned above. However, this option was also discarded as one of the proposed reforms by stakeholders was "*the exhaustion of domestic remedies which is not the EU's or Member States' traditional approach in investment*" [40].

More likely, the binding ISDS provisions under the ECT regime will continue. This would mean i) the arbitration industry will continue to encourage investors to shift onto taxpayers the financial risk of their investment in stranded fossil fuels assets, ii) the fear of ISDS procedures will increase the "*regulatory chill*" (see next section) and iii) taxpayers will be trapped in carbon at a high cost. Governments are accountable to their citizens for the use of public funds as well as for the design of the relevant policies to protect society. However, as shown by the known 130 ISDS claims, the high costs of ISDS proceedings, or the threat of such costs, will continue to play in favour of corporates and the arbitration industry as they are not the ones who have ratified the Paris Climate Agreement [30].

The costs of ISDS proceedings for the host States include the awards in the case the claim is won by the investor and the costs of legal and arbitral tribunal fees the respondent States must pay for defending against the alleged claims. The average cost of the former is estimated at €110 million while the average cost of the latter is estimated at €4.5 million. These estimates are based on the known ISDS cases which go beyond those related to the ECT regime [44].

Over the period 2013-2019, the average annual number of deals (contracts in the energy sector with foreign investors)

Box 2. ISDS reforms outside the ECT constituency

In recent years, concerns raised by ISDS mechanism have been analysed in various international fora [9, 10, 40]. Identified challenges related to ISDS mechanism include, but are not limited, to i) the lack of consistency, coherence, predictability of case-law and correctness of arbitral decisions by ISDS tribunals; ii) the lack of safeguards as to the arbitrators' independence, impartiality and legitimacy of decisions makers, iii) the lengthy and costly ISDS proceedings; iv) the lack of possibility to initiate a review of the proceedings and v) nationality planning of investors [9, 10, 40].

The on-going initiatives to reform ISDS at the multilateral level include those at the World Bank's International Centre for Settlement of Investment Disputes (ICSID) and those at the United Nations Commission on International Trade Law (UNCITRAL) Working Group III. In the context of the UNCITRAL Working Group III, the EU and its Member States are pursuing the option of establishing a permanent Multilateral Investment Court (MIC) composed of a first instance tribunal and an appeal tribunal to overcome the shortcomings of the ad-hoc international arbitration. Under MIC, private arbitrators appointed on a case-by-case and ad-hoc basis by parties will be replaced by tribunal members appointed by States Parties to MIC for pre-determined periods and will be assigned to specific cases on a rotational basis [9]. The aim is to guarantee the independence of MIC members, avoid conflict of interests, and to attract ethical and highly qualified lawyers. However, the German association of Judges issued an opinion in which it considers "the path envisaged by the European Commission to creating a multinational court that can create its own applicable law is the wrong one" [41].

In parallel to pursuing the establishment of an investment court at the multilateral level; the concept of a permanent Investment Court System (ICS) is already implemented by the EU in its newly signed bilateral treaties such as the Canada–EU Comprehensive Economic and Trade Agreement (CETA), signed in 2016, the EU–Singapore Investment Protection Agreement (IPA), signed in 2018 and the EU–Vietnam IPA which was agreed in 2018. The EC plan is to replace the newly established ICSs by a MIC when adopted. However, the European Association of Judges in its statement warned decision makers about the fact "the provisions for the election, time of office and remuneration for the judges of the ICS do not meet the minimum standards for judicial office as laid down in the European Magna Carta of Judges or other relevant international texts on the independence of judges » [42]. Moreover, the French Commission on Human Rights went one step further and proposed, during its assessment of CETA provisions, excluding sensitive fields such as social rights and environmental protection from the scope of ISDS [43].

At the EU Member State level, the recently signed BITs include reformed ISDS based on the EU investment approach [9]. However, ECT signatories who are also members of the Commonwealth of Independent States (CIS) did not make any major ISDS policy shifts. On the contrary, Armenia, Belarus, Kazakhstan and Kyrgyzstan have signed and ratified, in 2014, the Treaty on the Eurasian Economic Union which includes a largely unreformed ISDS mechanism [9]. It is worth noting that Russia is also a signatory of the Eurasian Economic Union. On the other hand, Japan has adopted some procedural reform features in some of its newly signed treaties [9].

protected by the ECT is estimated at 407 deals out of which 54% are fossil-fuels related deals [8]. Ending all fossil fuels deals protected by the ECT, since its entry into force, would potentially cost taxpayers on average additional €523.5 billion out of which €503 billion are the awards, if investors won, and €20.5 billion the potential costs of legal and arbitration fees.

The continuation of the ISDS mechanism under the ECT regime until 2050 will increase this cost to €1.3 trillion out of which 42% will be paid by EU taxpayers. This is slightly above the estimated investment need to finance the European Green Deal [38]. It is likely that the cost of the continuation of ISDS mechanism under the ECT regime will be higher than the estimates above as changes in incentives related to electricity production from renewable energy sources will also continue to raise the appetite of investors and the arbitration industry.

Increasing the "regulatory chill" effect through ISDS threat

"*Regulatory chill*" occurs when governments either water-down, cancel or delay regulations designed in the public interest because of the fear of ISDS procedures, the difficulty in predicting their outcomes and their related costs. The climate emergency and the continuation of the ECT increase the risk of "*regulatory chill*" effect through the ISDS threat. In fact, setting a carbon neutrality target will inevitably mean governments will have to urgently enact and enforce regulations to end the exploration of fossil fuels and to plan for an earlier retirement of existing fossil fuels infrastructures. In other words, the fossil fuel industry is, for the first time, facing an existential threat unless climate policies and regulations are delayed, watered-down or cancelled.

"Importantly, fossil fuel corporations do not have to win any ISDS cases for this strategy to be effective; they only have to be willing to launch them" [45] or to remind governments of the ISDS provisions included in the Treaties they have ratified years ago. The latter was the case of the French law on ending the exploration of fossil fuels. ISDS threat under the ECT regime from a Canadian company has contributed to watering-down requirements included in the draft law [46]. Similarly, Germany faced two ISDS cases under the ECT regime from a State-owned Swedish company over the implementation of environmental regulations and the phase-out of nuclear power plants.

In 2017, Italy was sued under the ECT regime by a British company because of the implementation of the ban of new fossil fuels' operations close to the coast. It is worth noting that Italy withdrew from the ECT in 2015. However, according to Article 47(3) of the ECT, "*the provisions of this Treaty … continue to apply as of the date when the Contracting Party's withdrawal from the Treaty takes effect for a period of 20 years from such date.*"[1] More recently, the Dutch government has been under ISDS threat from a German company because of the law aiming at phasing out, by 2030, the use of coal for electricity production in the Netherlands.

The lack of transparency under the ECT regime suggests that there might be many unknown cases of "*regulatory chill*". It is likely that investors will try to institutionalise the "*regulatory chill*" in EU Member States to avoid the domino effect of ambitious climate policies. This is particularly true given the low understanding of the ECT and its impacts by government officials and the active lobbying of arbitrators and investors in various international fora to keep the status-quo. Without ending ISDS under the ECT regime, it is unlikely that the proposed "*right to regulate*" and other "*safeguards*" would limit the abuse of investors and arbitrators of the ambiguities raised by the binding provisions of the ECT.

Investors are likely to invest more in making their "*regulatory chill*" strategies more effective and arbitrators will help them in launching new lengthy and

costly ISDS proceedings. Unfortunately, the most advanced countries in setting carbon neutrality targets will have to allocate part of their public budget to compensate foreign investors for their losses of "*legitimate*" expected revenues. Overall the continuation of the ECT and its binding protection of foreign investments in fossil fuels through ISDS will increase the cost of the energy transition and may even make it unaffordable for taxpayers.

Locking the developing world in carbon emissions at a high cost

Enlarging the constituency of the ECT beyond its traditional Eurasian countries and convincing key energy players to accede and to ratify the Treaty is one of the objectives of the modernisation process [23]. The CONEXO policy is one of the pillars of the modernisation roadmap [23,24] and its implementation is supported by three instruments including i) the International Energy Charter (IEC), ii) the Knowledge Centre, and iii) the Energy Investment Risk Assessment (EIRA) annual publication.

1 - The International Energy Charter is "*the instrument that facilitates familiarisation of the ECT, the signing of [the IEC] grants the status of observer to the Energy Charter Conference*" since 2015 [47]. Importantly, the 2021 vision of the International Energy Charter considers that *"the (modernised) Energy Charter Treaty can become an indispensable tool for securing private investment necessary for successful global low carbon transition"* [48] and "*the International Energy Charter with (a modernised) ECT will remain a niche organisation, standing for 'protecting investment for the global energy transition' [48].* As mentioned previously, the IEC has attracted newcomers from the developing world to the ECT constituency out of which many are host of fossil fuels reserves.

2 - The knowledge centre was "*established in 2013 with the objective to bring a higher visibility of the ECT*" [49] through forums and seminars with observer countries. Since its inception, the knowledge centre provided several training programmes with a special focus on investor-state-arbitration and contracts/deals in the fossil fuels industry. Furthermore, the knowledge centre developed special cooperation programmes with key energy players such as China, Iran and Nigeria [47]. A Joint Research Centre was established in 2017 with the China Electricity Council, an International Energy Charter Conference was organised in Teheran in 2018 as well as a National Energy Summit targeting countries from Western Africa was organised in Abuja the same year [48].

3 - The Energy Investment Risk Assessment (EIRA) annual publication was launched in 2018 with the aim to assist governments in identifying and eliminating investment risks in regulatory and legal frameworks. So far, the publication attracted 38 countries out of which 15 are newcomers from the developing world. ECT signatories participating to EIRA are mainly middle or low-income countries. The assessment of investment risks is conducted using four indicators scored based on a questionnaire filled by government officials and national experts. However, the only question which would allow assessing progress in the energy transition, out of the 67 questions included in EIRA, is the one related to the Paris Climate Agreement [30]. Interestingly, the maximum score a country could get for being a Party to the Paris Agreement is 50 out of 100 while the inclusion of arbitration in countries' investment laws is scored 100 [50].

Acceding to the ECT is a lengthy process which requires going through several steps (Annex III) and takes on average seven years [47]. By January 2020, at least 18 countries are in the process of acceding to the ECT. The most advanced ones

include Burundi, Eswatini, Mauritania and Pakistan and the least advanced ones include Cambodia, Colombia, Guatemala, Nigeria, Panama, Senegal and The Gambia (Figure 14). It is worth noting that these countries are among the ones targeted by the EIRA publication and that some of these countries are highly ranked in terms of fossil fuel reserves (i.e. Nigeria ranks 12th in the world in terms of proven oil and gas reserves).

Figure 14. Status of accession countries to the ECT

Countries formerly invited by the Energy Charter Conference to accede to the ECT
Burundi, Eswatini, Mauritania, Pakistan

Countries working on their internal approval of the three accession reports
Bangladesh, Chad, China, Morocco, Niger, Serbia, Uganda

Countries developing their three accession reports
Cambodia, Colombia, Guatemala, Nigeria, Panama, The Gambia

Key point: Several developing countries at a high risk to be trapped by the ECT regime

Source: Based on [47, 60-63]

Importantly, the accession process is supported by voluntary contributions from ECT signatories. In fact, "*some African countries (Chad, Mauritania, Mozambique, Nigeria, Tanzania and Swaziland) have benefited from the EU Technical Assistance Facility (TAF) for the SE4All [Sustainable Energy for All] initiative. Such assistance was strictly limited to the secondment of civil servants to the ECS [Energy Charter Secretariat] in Brussels for a period of three months, followed by a meeting with stakeholders and national authorities to seek further engagement in the ECT accession process*" [48].

Furthermore, the EU is currently providing, under its 11th development fund, support to the accession of Western African countries to the ECT [51]. However, it is unclear how Western African countries could accede to the ECT given the cautious approach of the region towards ISDS [9]. In fact, the Supplementary Investment Act to the Treaty of the Economic Community of West African States (ECOWAS) does not grant foreign investors ISDS [52]. Instead it requires foreign investors to use national remedies. It is worth noting that the EU support for the expansion policy was decided by the Council of the European Union, back in 2011, when "*promoting the benefit of joining the ECT as full member*" [53] was considered by EU leaders as an instrument to strengthen EU cooperation with third countries.

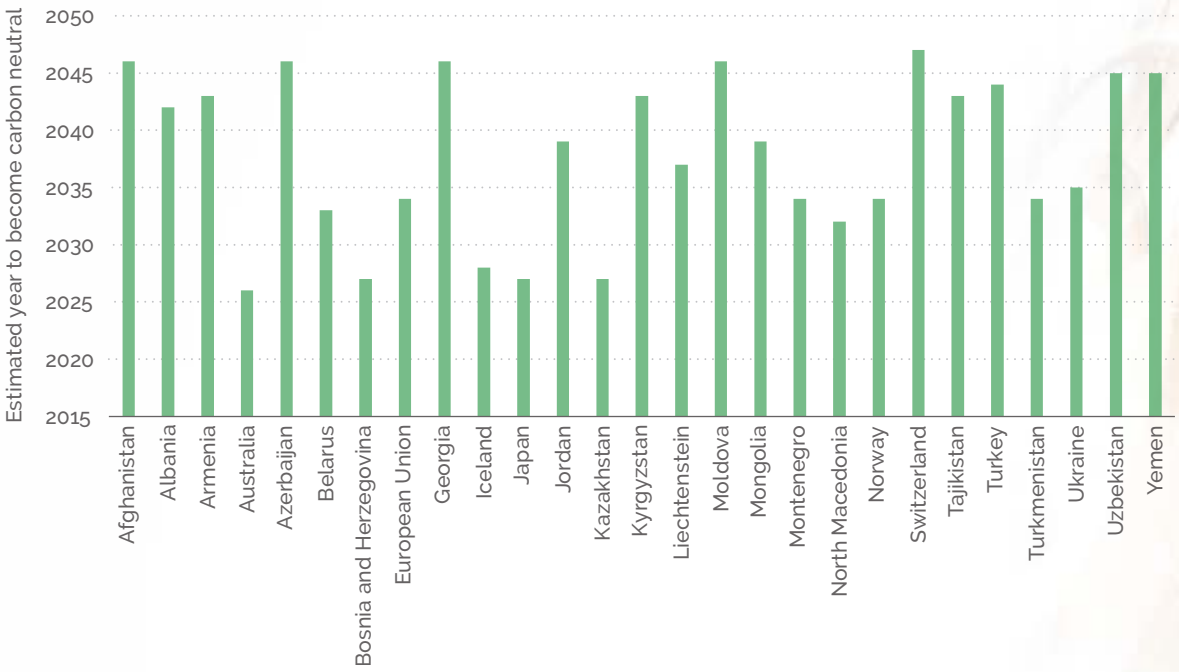
Similarly, Japan supported expansion efforts in Africa and South East Asia through the Tokyo International Conference on African Development (TICAD) [54]. Moreover, the ECT constituency also provides diplomatic support to the expansion policy through the Energy Charter Liaisons Embassies (ECLE) such as the Dutch embassy in Morocco, the Slovak embassy in Montenegro, the Turkish embassies in Pakistan and Tunisia [54] as well as the External Action Service of the European Union.

Overall, using development funds and diplomatic channels to attract developing countries to the ECT process raises moral and ethical questions given the binding provisions to protect foreign investments in fossil fossils, the ISDS mechanism under the ECT regime and the potential continuation of both in the "*modernised*" Treaty, if any.

Into the future ■

By ratifying the Paris Climate Agreement [30], governments signed on becoming carbon neutral before 2050 (Figure 15) in order to avoid the overshoot of the 1.5°C target of global warming by the end of the century (Annex II). Carbon neutrality means that exploration of fossil fuels could no longer be undertaken, and important shares of the proven fossil fuels reserves shall become unburnable fuels [32]. However, by January 2020, only few governments have set a carbon neutrality target but without necessarily linking this target to the need to phase-out the use of fossil fuels sooner than ever thought. Early estimates showed that at least a third of oil reserves and half of gas reserves as well as more than 80% of coal reserves should remain in the ground between now and 2050 [55]. However, the proportion of unburnable fossil fuels reserves may be even higher given the current rate of emissions [56].

Figure 15. Estimated year for ECT signatories to become carbon neutral, at their current emissions levels, and to avoid the overshoot of the 1.5°C target of global warming



Key point: All ECT signatories must become carbon neutral before 2050 to avoid the overshoot of the 1.5°C target of global warming by the end of the century

Source: Carbon neutrality: Earlier than ever thought (OpenExp, forthcoming)

Unfortunately, as shown in the previous sections, phasing-out the binding protection provisions for foreign investments in fossil fuels under the ECT regime is not on the agenda of ECT modernisation. The "*modernised*" ECT would, therefore, lead to protecting, by 2050, at least the equivalent of more than one-third of the remaining global carbon budget between 2018 and 2050 (Annex II). It is crystal clear that phasing-out fossil fuels' investment protection is a considerable threat to the fossil fuels industry and investors. ECT beneficiaries will, therefore, not hesitate to

use the powerful ISDS mechanism, which will also continue with the *"modernised"* ECT, to threaten governments with the objective of either watering-down, cancelling or delaying climate action.

The ISDS threat against the Dutch decision to phase-out the use of coal for power generation by 2030 is a good illustration of the up-coming ISDS cases in the most advanced countries in setting their carbon neutrality timeframe. Governments will have to choose between locking their populations into carbon or paying high compensations to fossil fuels industry and investors. Ending the existing fossil fuels deals by 2020 would potentially cost at least €523.5 billion and the continuation of ISDS and fossil fuels' investment protection would increase this cost to at least €1.3 trillion by 2050. This is more than the EU investment plan for the Green Deal for the next ten years [38].

Making the ECT a climate friendly instrument, which would contribute to the transition from fossil fuel-based economies to fossil-free economies, is hardly achievable given the contribution of fossil fuels revenues to the economies of some of the ECT Contracting Parties (Figure 12) and the unanimity vote required to amend the Treaty. Withdrawing from the ECT is, therefore, the only option left especially for the EU and its Member States. In fact, around 80% of intra-ECT FDIs in EU countries are either from investors hosted in the EU or in EFTA countries. As shown earlier, the ECT cannot be the instrument driving cross-border flow of investment in the energy sector in the EU. Most likely FDIs in the EU are driven by EU laws and internal energy market regulations.

Ending the intra-EU disputes is, also unlikely, to be achieved under the ECT regime as the Treaty does not allow any derogation. However, by withdrawing collectively from the ECT, EU Member States could agree on ending the intra-EU disputes, as they did with ending disputes under EU-BITs. The cost of the five ISDS cases from non-EU countries would be much lower than the potential cost of the 88 known ISDS cases against the EU and its Member States. Working with EFTA countries to join the collective EU withdrawal is of paramount importance. This could further lower the ISDS costs as two cases are from investors hosted in Switzerland.

Similarly, governments' fear of the survival clause, which extends the lifetime of ECT provisions for twenty years more after withdrawing from the Treaty, can be addressed only if EU countries withdraw collectively from the ECT. After withdrawing, EU Member States could agree between themselves, as they did for the intra-EU BITs, to also cancel the survival clause related to the ECT regime. Overall, the EU and its Member States can no longer afford to be ECT signatories as the Treaty is a serious threat to Europe's long-term decarbonisation strategy and will challenge the implementation of the European Green Deal and its financing. This is particularly true when considering the costs of the potential ISDS claims which will result from the gradual phase-out of fossil fuels in Europe.

The global climate emergency requires a new approach to the energy sector which would combine existing policies (reducing energy demand and increasing the share of renewables in the energy mix) with supply side policies targeting the end of the use of fossil fuels. The EU should take a lead and join efforts with the most advanced countries in their carbon neutrality targets, to develop a Treaty on the Non-Proliferation of Fossil Fuels [57]. Developing such a Treaty, under the UNFCCC umbrella, would be a viable instrument to ensure large shares of the remaining fossil fuels' reserves will effectively be left in the ground as required by the 1.5°C target.

Annex I

Decisions rendered by arbitral tribunals on ECT intra-EU disputes

Table A-I. Arbitral tribunals' decisions on ECT intra-EU disputes

Disputes	Year of the decision	Arbitral tribunal's decision on the application of the ECT to intra-EU disputes
Vattenfall v. Germany	2011	*the "EU as a REIO "is a Contracting Party to the ECT in its own right" and "the term "Contracting Party" in Article 26 should be understood as including both any State that signs and ratifies the ECT, and the EU, which has signed and ratified the ECT" and "Article 1(3) does not establish that the ECT is not applicable among EU Member States: [t]he mere mention in Article 1(3) that EU Member States have "transferred competence over certain matters" to the EU does not convey that there is no application of the provisions of the ECT between EU Member States"*
Charanne v. Spain*	2016	*"although the EU is a Contracting Party of the ECT, the States that compose it have not ceased to be Contracting Parties as well. Both the EU, as its Member States, may have legal standing as Respondent in an action based on the ECT"*
Isolux v. Spain	2016	*"the fact that the "territory" of the EU, according to Article 1.10 of the ECT, covers the territories of the Netherlands and the Kingdom of Spain does not prevent each of them also maintaining a "territory" in the sense of the ECT"*
RREEF v. Spain	2016	*"It has been made aware by the Parties of awards given in cases with similarities with the present case. While according them due attention, the Tribunal has formed its own opinion on the legal issues before it and has applied the applicable legal rules in light of the particular circumstances of the present case without feeling bound by any of the decisions of previous tribunals"*
Blusun v. Italy	2016	*"The mere fact that the EU is party to the ECT does not mean that the EU Member States did not have competence to enter into inter se obligations in the Treaty. Instead, the ECT seems to contemplate that there would be overlapping competences. The term 'regional economic integration organization' (or REIO) is defined in Article 1(3) of the ECT to mean an 'organization constituted by states to which they have transferred competence over certain matters a number of which are governed by the ECT, including the authority to take decisions binding on them in respect of those matters.' The Area of the REIO is also defined by Article 1(10) with reference to EU law. But nothing in Article 1, nor any other provision in the ECT, suggests that the EU Member States had then transferred exclusive competence for all matters of investment and dispute resolution to the EU" and "if the Member States thought they did not have competence over the inter se obligations in the ECT, this would have been made explicit by including a declaration of competence to set out the internal division of competence between the EC and its Member States, as has been done in many other treaties with mixed membership. Nothing in the text of the ECT supports the implication of such a declaration of competence" and* *"EU Member States and the EU are all Contracting Parties. Prima facie at least, a treaty applies equally between its parties. It would take an express provision or very clear understanding between the negotiating parties to achieve any other result."*
Eiser v. Spain	2017	*"the claimants in these cases are qualified investors under the ECT since they are nationals of the States that satisfy the definition of a "Contacting Party" as set out in Article 1(2)" as "[t]he definition of a "Regional Economic Integration Organization" ("REIO") in Article 1(3) does indeed contemplate that a REIO's member can transfer competence over some matters to the Organization. However, this does not establish that EEC member countries had transferred competence over energy investments and their protection to the EEC when they signed the ECT in 1994, as Respondent apparently contends, or that this position was communicated to and accepted by other ECT parties"*

Table A-I. (continued)

Disputes	Year of the decision	Arbitral tribunal's decision on the application of the ECT to intra-EU disputes
Novenergia v. Spain	2018	*"[t]he ECT tribunals in other previous similar cases against the Respondent, namely Charanne, Isolux, RREEF, and Eiser, all followed the same approach and dismissed the jurisdictional objection of the Respondent on the same above grounds. This Tribunal finds no reason to depart from such a stable case law in resolving the present dispute, which involves similar, if not identical, legal issues"*
Antin v. Spain	2018	*"[t]he definition of a "Regional Economic Integration Organization" ("REIO") in Article 1(3) does indeed contemplate that a REIO's member can transfer competence over some matters to the Organization. However, this does not establish that EEC member countries had transferred competence over energy investments and their protection to the EEC when they signed the ECT in 1994, as Respondent apparently contends, or that this position was communicated to and accepted by other ECT parties" and* *"[t]he simultaneous existence of Spain, the Netherlands and Luxembourg as Contracting Parties to the ECT, together with the EU, where each would have obligations under the Treaty, results from their separate ratifications of the Treaty".*
Greentech v. Spain	2018	*"it is not aware of a single award that has found "intra-EU" disputes to be excluded from the scope of Article 26(1) ECT. By contrast, the Claimants led the Tribunal to eighteen awards in which jurisdiction over intra-EU investment treaty disputes has been upheld […] As the foregoing discussion has demonstrated, the Tribunal finds no reason to depart from these awards, in particular those arising from cases involving similar or identical issues" and* *"The Tribunal is cognizant of the fact that the ECT tribunals in Charanne, Isolux, Eiser, Novenergia and Masdar have also considered the disputed measures. The Tribunal is not bound by any of those decisions and must reach its own decision on the claims at issue in this arbitration. That said, the awards are clearly relevant to the Tribunal's analysis of the factual issue of whether or not Spain abrogated the RD 661/2007 support scheme, as well as the legal question of whether, if such an abrogation occurred, this amounts to a violation of the Claimants' legitimate expectations"*
Masdar v. Spain	2018	*the "EU as a REIO "is a Contracting Party to the ECT in its own right"*
Rockhopper v. Italy	2019 Decision rendered is only the intra-EU jurisdictional objection of the respondent	*"While there is no system of binding precedent in the field of investor-state dispute resolution, the Tribunal does consider it of assistance to see the reasoning adopted by other tribunals in relation to intra-EU jurisdiction and the ECT" and "if the Member States thought they did not have competence over the inter se obligations in the ECT, this would have been made explicit by including a declaration of competence to set out the internal division of competence between the EC and its Member States, as has been done in many other treaties with mixed membership. Nothing in the text of the ECT supports the implication of such a declaration of competence" and* *"EU Member States and the EU are all Contracting Parties. Prima facie at least, a treaty applies equally between its parties. It would take an express provision or very clear understanding between the negotiating parties to achieve any other result."*
CEF v. Italy	2019	*"if the Member States thought they did not have competence over the inter se obligations in the ECT, this would have been made explicit by including a declaration of competence to set out the internal division of competence between the EC and its Member States, as has been done in many other treaties with mixed membership. Nothing in the text of the ECT supports the implication of such a declaration of competence" and* *"EU Member States and the EU are all Contracting Parties. Prima facie at least, a treaty applies equally between its parties. It would take an express provision or very clear understanding between the negotiating parties to achieve any other result."*

Table A-I. (continued)

Disputes	Year of the decision	Arbitral tribunal's decision on the application of the ECT to intra-EU disputes
9Ren v. Spain	2019	*"that this is confirmed by the European Communities' Statement under Article 26(3)(b)(ii) of the ECT as a Contracting Party to the ECT"*
Eskosol v. Italy	2019	*"As for Article 1(3), this does refer to States having "transferred competence" to a REIO "over certain matters," and the word "transfer" in its natural and ordinary meaning is capable of denoting the conveyance of exclusive (and not simply concurrent) powers. The effect of such a reading would be that for the "certain matters" over which the transferee (the REIO) gains authority, the transferor (the States) concomitantly cedes all residual authority. This notion of a transfer of exclusive competence is consistent with Article 1(3)'s reference to the REIO thereby obtaining "authority to take decisions binding on [the States] in respect of those matters"* *"However, the Treaty does not stipulate that the obligations of the States-Contracting Parties to the ECT and members of a REIO-Contracting Party under Parts III and V in their entirety are transferred to the REIO:* *The fact remains, however, that Article 1(3) alludes only in the abstract to "certain matters" where such an exclusive transfer may occur, without elucidation as to which matters those may be. In particular, nothing in this Article remotely suggests a shared understanding, as of the date the ECT entered into force, that either the entirety of Part III's substantive obligations, or the entirety of Part V's procedural obligations with respect to dispute settlement, were the contemplated subjects of such an exclusive transfer. If such a wholesale transfer of exclusive competence for major parts of the ECT, among a large group of the ECT's original Contracting Parties, already had been completed or was directly contemplated as of the ECT's entry into force, one would expect that this major development would have been expressly referenced somewhere" and* *"The inclusion of REIOs in definition of a "Contracting Party" does not mean the States-parties to a REIO are curtailed of their obligations under the ECT: [T]here is no doubt that this expands the universe of ECT Contracting Parties by enabling REIOs (and not just States) to ratify the treaty, but nothing in its language suggests a concomitant intent to curtail the obligations of States which choose to become Contracting Parties in their own right"*
NextEra v. Spain	2019	*"A good faith interpretation of the terms of the ECT leads to the conclusion that a REIO such as the EU, may have standing under the ECT in arbitration proceedings" and* *"The fact that the EU is a Contracting Party to the ECT did not deprive the EU Member States of their competence to enter into obligations under the ECT at the time of its conclusion. Therefore, in absence of a disconnection clause and a revision of the ECT by the Contracting Parties, the Tribunal cannot conclude that presence of the EU as REIO consenting to the provisions of the ECT would supersede the consent given by each EU Member State individually to the ECT. Rather, a good faith interpretation of the terms of the ECT leads to the conclusion that a REIO, such as the EU, may have standing under the ECT in arbitration proceedings. However, concluding that Contracting Parties, taken individually, lack standing when the investment operation remains in the European Area would go beyond the terms of the Treaty"*

Key point: Arbitrators continue to reject EU Member State's arguments against the use of the ECT for intra-EU disputes

Source: Based on available ISDS proceedings available at UNCTAD Investment Policy Hub and List of ECT cases

Annex II

Carbon neutrality

The timeframe for carbon neutrality is estimated based on the remaining global carbon budget, the projections of the population in each ECT signatory country by 2050 and the last know domestic carbon emissions without those related to land use [58] (Table A-II). The remaining global carbon budget is the amount of carbon that can be emitted into the atmosphere from 2017 until the end of this century and measured in Gt (giga-tonnes) of carbon dioxide.

For the purpose of this report, the remaining global carbon budget considered is the one provided in the last IPCC report [32] which would give us a 50% chance of remaining within the 1.5˚C global warming target. The available global carbon budget under these conditions is 580 Gt CO_2 [32]. This budget is being depleted by current emissions of 38 Gt CO_2 per year. If emissions were to stay at this level, the global carbon budget will be exhausted in fifteen years.

The estimated time left for ECT signatories to become carbon neutral would be much shorter if the global carbon budget considered was the one that would give us a 66% chance of remaining within the 1.5˚C global limit. The timeframe would shorten further if all emissions (including those related to aviation of embodied emissions in goods) were considered.

Table A-II. Remaining carbon budget between 2017 and 2050 in selected ECT Contracting Parties based on their current emissions and the remaining carbon budget per capita

Country	Population in 2050 (millions)	Reference year for carbon emissions	Carbon emissions (Millions of tonnes of CO2) in the reference year	Remaining carbon budget (Millions of tonnes of CO2) between 2017 and 2050
Afghanistan	65	2013	9.9	3 855
Albania	2	2009	5.9	144
Armenia	3	2010	4.5	168
Australia	33	2017	417	1 956
Azerbaijan	11	2013	39	659
Belarus	9	2017	63	515
Bosnia and Herzegovina	3	2014	22	160
EU28	524	2017	3 515	31 230
Georgia	4	2013	9	210
Iceland	0.38	2017	3.6	22
Japan	106	2017	1 188	6 306
Jordan	13	2006	23	771
Kazakhstan	24	2017	283	1 432
Kyrgyzstan	9	2010	6	544
Liechtenstein	0.04	2017	0.2	2
Moldova	3	2013	8	200
Mongolia	4	2006	10	265
Montenegro	1	2011	3	35
North Macedonia	2	2009	9	111
Norway	7	2017	44	393

Key point: The remaining carbon budget is very limited for all ECT signatories

Source: Based on UN population, UNFCCC data and Carbon neutrality: earlier than ever thought (OpenExp, forthcoming)

Annex III

ECT accession process

Acceding to the ECT is a lengthy process which requires several steps including [59]:

1 - Developing three reports on i) the harmonisation of laws and regulations of the country with the provisions of the ECT, ii) investment climate and exceptions to national treatment and iii) energy efficiency policies. Those reports are developed by officials from the targeted countries for accession seconded to the Secretariat with contributions from the latter.

2 - Approving the three reports by the government aiming at acceding to the ECT and expressing its readiness to sign or ratify the ECT and to comply with its related obligations.

3 - Presentation, to the Energy Charter Conference, of the three accession reports and the expression of interest of the government to sign or ratify the ECT.

4 - Invitation, by the Energy Charter Conference, to the acceding State to proceed with the accession under specific accession terms and conditions.

5 - Confirmation, to the Energy Charter Conference, by the acceding State of its intention to accede to the Treaty and its fulfilment of the specific terms and conditions.

6 - Proceeding by the acceding State with national ratifications of the ECT.

7 - Depositing the accession instruments with the Government of Portugal.

8 - Entry into force of the Treaty on the ninetieth day after the date of deposit of the accession instruments.

By January 2020, at least 18 countries are in the process to accede to the ECT. However, these countries are at different stages of the accession process [Table A-III].

Table A-III. Accession status of ECT observer countries from the most to the least advanced ones

Observer Country	Accession status
Pakistan	Invited by the Conference in 2006 to accede to the ECT [60]
Burundi	Invited by the Conference in 2016 to accede to the ECT [61]
Mauritania	Invited by the Conference in 2016 to accede to the ECT [62]
Eswatini	Invited by the Conference in 2018 to accede to the ECT [63]
Chad	Working on the internal approval of the three accession reports since 2017 [47]
China	Working on the internal approval of the three accession reports since 2018 [47]
Bangladesh	Working on the internal approval of the three accession reports since 2017 [47]
Morocco	Working on the internal approval of the three accession reports since 2015 [47]
Niger	Working on the internal approval of the three accession reports since 2017 [47]
Serbia	Working on the internal approval of the three accession reports since 2012 [47]
Uganda	Working on the internal approval of the three accession reports since 2012 [47]
The Gambia	Developing their accession reports [47]
Nigeria	Developing their accession reports [47]
Panama	Developing their accession reports [47]
Senegal	Developing their accession reports [47]
Cambodia	Developing their accession reports [47]
Colombia	Developing their accession reports [47]
Guatemala	Developing their accession reports [47]

Key point: African and Latin American countries are the main targets of ECT expansion policy

Glossary

Ecocide is the extensive damage to, destruction of or loss of ecosystem(s) of a given territory because of human activity such as the exploration, exploitation, production and use of fossil fuels resources.

Fair and Equitable Treatment provides a yardstick by which relations between foreign direct investors and Governments of capital-importing countries may be assessed. It also acts as a signal from capital-importing countries, for it indicates, at the very least, a State's willingness to accommodate foreign capital on terms that considers the interests of the investor in fairness and equity [UNCTAD].

Most Favoured Nation treatment means that a host State treats investors from one foreign country no less favourably than investors from any other foreign country. The most-favoured-nation standard gives investors a guarantee against certain forms of discrimination by host countries. This clause is considered crucial for the establishment of equality of competitive opportunities between investors from different foreign countries. While most-favoured-nation treatment is generally more than the minimum standard required under customary international law, it does not go so far as to put the foreign investor on an equal footing with domestic investors in the host country [UNCTAD].

Stranded assets referred to in this report is stranded capital invested in fossil fuels projects which will not recover the capital invested in them during their operating time as it will be shorten due to climate emergency.

Umbrella Clause requires a host State to respect any obligation that it has assumed regarding a specific investment (i.e investment deal). By doing so, the umbrella clause allows bringing under the umbrella of the ECT all contractual obligations of the host State. Policy changes which may affect the contractual obligations are considered as a breach of these obligations and consequently of the ECT [ECT]

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List of acronyms

BIT	Bilateral Investment Treaty
CETA	Comprehensive Economic and Trade Agreement
CIS	Commonwealth of Independent States
CONEXO	Consolidation, Expansion and Outreach
EC	European Commission
ECJ	European Court of Justice
ECT	Energy Charter Treaty
ECOWAS	Economic Community of West African States
EFTA	European Free Trade Area
EEA	European Economic Area
EIB	European Investment Bank
EIRA	Energy Investment Risk Assessment
EnC	Energy Community
EU	European Union
FDI	Foreign Direct Investment
GHG	Greenhouse gas
GDP	Gross Domestic Product
Gt	Giga tonnes
ICS	Investment Court System
ICSID	International Centre for Settlement of Investment Disputes
IEA	International Energy Agency
IEC	International Energy Charter
IIA	International Investment Agreements
IPCC	Intergovernmental Panel on Climate Change
IPA	Investment Protection Agreement
ISDS	Investor-State-Dispute-Settlement
MIC	Multilateral Investment Court
NACE	Nomenclature of economic Activities in the European Community
NDC	Nationally Determined Contributions
REIO	Regional Economic Integration Organisation
SCC	Stockholm Chamber of Commerce
TICAD	Tokyo International Conference on African Development
TPF	Third Party Funding
UNCITRAL	United Nations Commission on International Trade Law
UNFCCC	United Nations Framework Convention on Climate Change
US	United States
WTO	World Trade Organisation

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Modernisation of the **Energy Charter Treaty**

A Global Tragedy at a High Cost for Taxpayers

The Energy Charter Treaty (ECT) is a multilateral investment agreement solely dedicated to protecting foreign investments in energy supply. By January 2020, the Treaty has been ratified by 53 countries and the European Union/Euratom. Under the ECT regime, foreign investors can sue host States through arbitration tribunals, typically, composed of party-appointed private lawyers.

After more than two decades of existence, the ECT failed in meeting its policy objectives and the "*raison d'être*" of the Treaty became obsolete. Contracting Parties launched, in 2009, the year Russia withdrew from the provisional application of the ECT, a modernisation process of the Treaty. Negotiations of the policy options to "*modernise*" the ECT will take place in 2020.

However, the "*modernisation*" of the Energy Charter Treaty (ECT) is unlikely to lead to a fossil fuel-free and a climate friendly Treaty. In fact, phasing-out protection of foreign investments in fossil fuels is not on the negotiating table. The continuation of investment protection of foreign investments under the ECT regime will potentially lead to 216 Gt of carbon protected by the Treaty by the end of 2050. This is equivalent to more than one-third of the remaining global carbon budget to limit planet's warming to 1.5°C by the end of the century. Similarly, the "*modernisation*" of the Treaty will not end the Investor-State-Dispute-Settlement (ISDS) mechanism under the ECT regime. Thus, leading, by 2050, to a potential cost for taxpayers of €1.3 trillion out of which 42% should be paid by EU taxpayers.

The EU and its Member States cannot on one hand phase-out the use of public finance for domestic investments in fossil fuels, through the EIB energy lending policy, and on the other hand sign off on the continuation of protection of foreign investments in fossil fuels, through the continuation of the ECT. For consistency with the European Green Deal and its ambition of making the EU a global climate leader, the EU and its Member States should withdraw collectively from the ECT.

Moreover, under the UNFCCC umbrella, the EU and its Member States could take a lead and join efforts with the most advanced countries in their carbon neutrality targets, to develop a Treaty for the Non-Proliferation of Fossil Fuels. Such a Treaty would require all countries to develop their roadmaps to gradually phase-out fossil fuels and will avoid locking the world, especially developing countries, in carbon at high cost for taxpayers.

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