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ENERGY CHARTER TREATY HINDERS FOSSIL FUEL PHASE OUT

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KEY MESSAGES

1. The Energy Charter Treaty (1994) negotiated mostly by European countries encourages investments in fossil fuel (FF) by protecting such investments.
2. ECT protection includes enabling foreign investors to sue states where they operate, in the public and environmental interest, if they decide to phase out FF.
3. Such protection includes that even after withdrawing from the ECT, countries are still liable for breaches of the ECT for 20 years.
4. Such protection appears to be stronger than other obligations under EU and public international law. Proposed revisions may not address the above problems.
5. Inviting developing countries to join the ECT affects them negatively as they have had no influence on the content.
6. Such invitations are based on unverified claims about the potential impact of the ECT on attracting investments, reducing energy prices, and energy poverty for developing countries.

INTRODUCTION

The Energy Charter Treaty (ECT) (1994) is a multilateral investment treaty protecting investment in the energy sector. The ECT secretariat has invited countries beyond the current 53 Contracting Parties to join the ECT (see Table 1). Yet even as new countries are invited to join, the EU officially withdrew from the ECT in 2024. The question is: does the ECT stand in the way of a fossil fuel phase out?

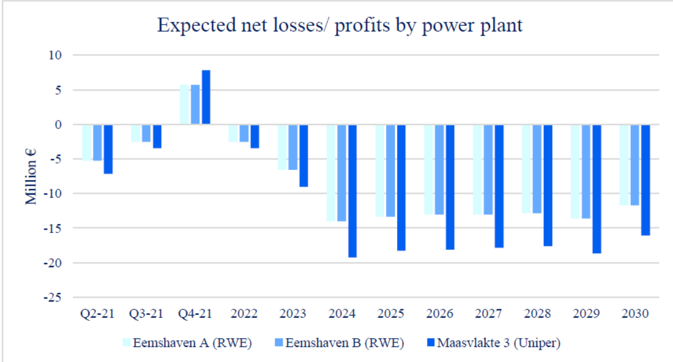
THE ENERGY CHARTER TREATY CONTINUES TO PROTECT FF INVESTMENTS

The ECT, negotiated to protect western European countries' access to fossil fuels (FF) in the republics of the former Soviet Union and eastern Europe, continues to be used to pressure states to postpone the energy transition by protecting existing FF projects and permits for new FF projects. It also leads to further investment in FF exploration.

THE ECT ENABLES FOREIGN INVESTORS TO SUE STATES WHEN THESE STATES DECIDE TO RESTRICT OR PHASE OUT FF

FF investors are protected under the ECT. When states adopt climate or environmental policies that restrict or end the exploration of FF or prematurely end a contract with an FF investor, they may be obliged to pay compensation to the FF investor that goes above and beyond the compensation under ordinary law, e.g. including compensation for potential future revenues (Fig. 1).

Fig. 1. Expected losses by 2030 (by power plant)



Source: Brown, 2021 & Verbeek, 2021

The case in point is Rockhopper, in which a UK investor received USD 250 million in compensation from Italy for banning offshore drilling (Arcuri, 2023). Additionally, two fossil fuel companies (RWE and Uniper) sued the Dutch Government for banning the use of coal for electricity generation by 2030. However, the case by Uniper was ended as part of a bail-out package in which Germany took majority ownership of Uniper and the case by RWE was suspended. On July 27, 2023, the German Federal Court decided that the claim by RWE is inadmissible because it was incompatible with EU law.

Table 1. Countries in the ECT accession process

Regions	Country
Sub-Saharan Africa	Benin, Burkina Faso, **Burundi**, Chad, Gambia, **Eswatini**, Kenya, Mali, **Mauritania**, Morocco, Niger, Nigeria, Rwanda, Senegal, Tanzania, **Uganda**
Asia	Bangladesh, Cambodia, China, South-Korea, **Pakistan**
Latin America	Chile, Colombia, Guatemala, Panama
Middle East & North Africa	Iran, Iraq, **Jordan**, Morocco, Palestine, United Arab Emirates
Europe	Serbia

NB. Countries in bold are in advanced stages of accession

The prospect of and actual cases under the ECT have been identified to deter governments from restricting or phasing out FF (regulatory chill; see, e.g., Tienhaara, 2018). The number of publicly known energy arbitration cases is rising (Fig. 2). Moreover, investors are preparing to restructure their businesses to be able to sue under the ECT, e.g. by suing from a non-EU state to avoid the incompatibility with EU law (Kahale III, 2020; Eckes & Ankersmit, 2022). The broad and vague definitions of 'investor' and 'investment' in the ECT enable investors to disguise as foreign investors and sue their home states from shell companies in another contracting state. E.g. 23/24 'Dutch' claimant investors are letterbox companies (TNI, 2018; Fig 3).

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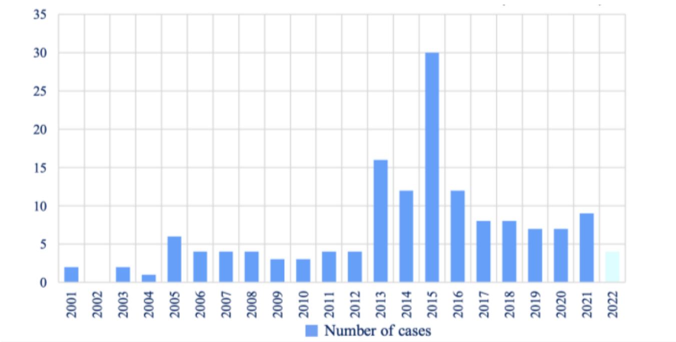
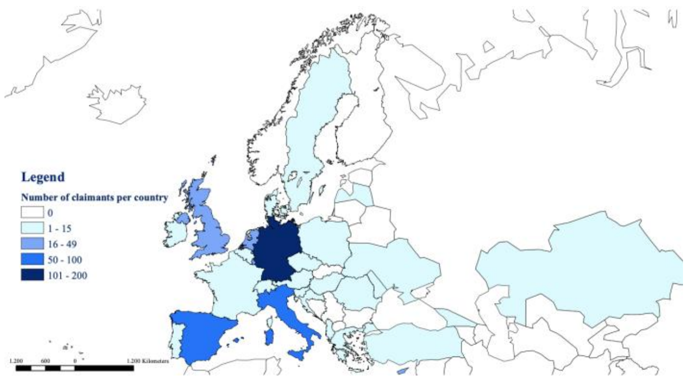
Fig. 2. Rising arbitration cases under the ECT



Source: IEC, 2022

Fig. 3 No. of arbitration cases by claimant nationality



Source: IEC, 2022

A contracting state can therefore effectively be sued from any investor around the world, increasing the scope of the risk. There are currently 150 known arbitration cases under the ECT (IEC, 2022), and this number is therefore expected to rise.

SUCH PROTECTION INCLUDES A SUNSET CLAUSE

A country that withdraws from the ECT can still be held liable for breaches of the ECT for 20 years thereafter, further hindering the achievement of the Paris Agreement goals. With the EU's withdraw in 2024, the sunset clause means EU investment remain protected until 2044.

SUCH PROTECTION APPEARS TO BE STRONGER THAN OTHER OBLIGATIONS UNDER EU AND PUBLIC INTERNATIONAL LAW. PROPOSED REVISIONS MAY NOT ADDRESS THE ABOVE PROBLEMS

The ECT's environmental provisions are weak in comparison to the protections of the investor. The European Court of Justice judgement that intra-EU cases under the ECT are incompatible with EU-law, yet such cases continued (Saheb, 2022). Protections under investment law appear to be stronger than the requirements under the Paris Agreement on Climate Change and EU law. Furthermore, if ECT protection is more favorable to investors than EU-law, the ECT prevails. These tensions likely contributed to the EU's withdrawal. All investor-state-dispute-settlement cases under the ECT amount to USD 35B which is more than Africa's annual costs for climate adaptation under the Paris Agreement (ADB, 2011) and more than the annual investment required to provide energy access to everyone worldwide that currently lacks access (TNI, 2018).

INVITING DEVELOPING COUNTRIES TO JOIN THE ECT EXPOSES THEM TO ARBITRATION RISKS AND THEY HAVE HAD NO INFLUENCE ON THE CONTENT OF THE ECT

Many developing countries have been invited to join the ECT. However, they have no influence over the already negotiated clauses protecting the investor under the ECT. Accession on these terms can undermine recent attempts to improve the transparency and independence of dispute settlement. Expansion of the geographical scope of the ECT would increase the protected FF investments, further locking countries into FF dependent futures and exposing them to the risk of high awards.

SUCH INVITATIONS ARE BASED ON UNVERIFIED CLAIMS ABOUT WHETHER THE ECT HELPS IN ATTRACTING INVESTMENTS, REDUCING ENERGY PRICES AND POVERTY FOR DEVELOPING COUNTRIES

The ECT is supposedly attractive because it could ensure energy investment and reduce the price of energy. But if such investment goes to FF enterprises, it may lead to higher local and global pollution and create a legal structure in which FF enterprise can claim large amounts of compensation from the developing countries enact environmental or social policies. Further, it could worsen energy poverty as the ECT also allows investors to sue states for restraining energy profits and lowering energy prices.

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