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Energy Transition and the
International Trade and Investment Regime

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Glossary and Acronyms

The different kinds of trade deals

BIT – Bilateral Investment Treaty: an agreement between two countries that covers investment only. Treaties offer protection to investors from each party to the treaty when they are making investments in the other party's territory.

FTA – Free Trade Agreement: this can be a bilateral (between two countries) or plurilateral (between a number of countries) deal covering a wide range of issues. Chapters on trade in goods (such as border tariffs) are included in all agreements; the other issues covered vary between agreements but can include trade in services (like telecommunications, finance, health or water), access to government procurement markets, agreements relating to 'behind the border' regulation and many more. FTAs sometimes include investment protection chapters that offer the same protections as are found in BITs.

IIA – International Investment Agreement: this is a United Nations category referring to all treaties that contain investment protection provisions, including BITs and FTAs.

WTO – World Trade Organisation: the only forum where the aim is to agree trade deals that will apply to all 162 member states. A list of the key deals is below, with further explanation in chapter 3.

Specific trade deals discussed in this report:

WTO agreements:

DSM – Dispute Settlement Mechanism

EGA – Environmental Goods Agreement

GATS – General Agreement on Trade in Services

GATT – General Agreement on Trade in Tariffs

GPA – Government Procurement Agreement

SCM – Agreement on Subsidies and Countervailing Measures

TBT – Agreement on Technical Barriers to Trade

TRIMS – Agreement on Trade Related Investment Measures

Other agreements:

CETA – Comprehensive Economic and Trade Agreement: an FTA that has been concluded but not ratified between the EU and Canada.

ECT – Energy Charter Treaty: an agreement between 54 states covering trade and investment in the energy sectors.

EPA – Economic Partnership Agreements: FTAs that are at different stages of negotiation between the EU and 78 ACP countries.

IEC – International Energy Charter: a non-binding declaration of intent between 75 countries to expand liberalisation and geographic coverage of trade and investment rules in the energy sector.

NAFTA – North American Free Trade Agreement: an FTA between the US, Canada and Mexico.

TISA – Trade in Services Agreement: an FTA under negotiation between 23 parties including the EU, covering trade and investment in services.

TPP – Transpacific Partnership: an FTA that has been concluded but not ratified between 12 Pacific Rim countries.

TTIP – Transatlantic Trade and Investment Partnership – an FTA under negotiation between the EU and the US.

Other acronyms

ACP – African Caribbean and Pacific: group of 79 states. With the exception of Cuba, all are signatories to the Cotonou Agreement with the EU.

ASEAN – Association of South East Asian Nations: an economic, social and cultural grouping of ten member states.

COP – Conference of the Parties to the 1992 United Nations Framework Convention on Climate Change and the 9th session of the Meeting of the Parties to the 1997 Kyoto Protocol.

ECOWAS – Economic Community of West African States: a regional organisation promoting economic integration comprising 15 members.

IPCC – Intergovernmental Panel on Climate Change

ISDS – Investor-to-State Dispute Settlement: allows foreign investors to sue states at private international tribunals.

UNFCCC – United Nations Framework Convention on Climate Change

Executive Summary

The 2015 Paris climate agreement commits countries to keep any rise in the global temperature to below 2 degrees Celsius. Given that fossil fuel use is the single biggest source of CO₂ emissions, a radical transition in energy policy is necessary to achieve this goal. The clear and growing consensus is that three-quarters of all existing reserves of oil, gas and coal need to be left in the ground. However, countries signing the COP agreement have overlooked a very large elephant in the room: international trade and investment deals are a major barrier to the energy transition.¹

It is difficult to overestimate the importance of the energy sector to both climate change and the global economy. The high costs of exploration, production and distribution, combined with the potential profits to be made in the energy sector make it the single largest destination for foreign direct investment: figures for 2014 show that combined investment in coal, oil, natural gas and alternative and renewable energy accounted for US\$124 billion of the total global investment flows to all sectors of US\$649 billion.

Crucially, much of this investment is protected by international trade and investment agreements. In the vast majority of agreements, investors can seek to enforce broadly defined rights via an investor-to-state dispute settlement (ISDS) clause, described as “one of the most powerful legal mechanisms known to international law today.” ISDS allows companies to sue governments in private tribunals for financial compensation if they consider that a policy or its implementation has negatively affected the profitability of their investment. The average cost of defending a case is US\$8 million; if a government loses a case, the award against it can run to millions, if not billions of dollars. In stark contrast to the climate agreement, where it was deemed impossible to make commitments fully binding, ISDS provisions make commitments to investment protection both binding and enforceable by specifically named bodies equipped with all the necessary legal powers to do so.

The centrality of energy to the international trade and investment regime is demonstrated by the nature of the investment cases that have been brought in recent decades: half of all ISDS cases registered at the World Bank by the end of 2015 related to oil, mining, gas, electric power or other energy forms. Many of these cases have been brought under the Energy Charter Treaty (ECT): a trade and investment agreement that deals exclusively with the energy sector. The ECT has already been signed by fifty-four states, including the UK. There are also moves to expand the scope of trade and investment rules through the International Energy Charter (IEC).

The ECT covers issues such as foreign investment in energy, energy trade and the transportation of energy resources such as oil, coal and gas. The deal has been used to bring no less than eighty-nine of the total 696 ISDS known cases globally, making it the number one treaty for international investment disputes. Overwhelmingly, the findings of the tribunals hearing these cases support the proposition that companies should be compensated if their ‘legitimate expectations’ of a ‘stable business environment’ are undermined, including when a government moves to transition away from fossil fuel use and to support the development of renewable energy instead. In this way, ISDS serves to reverse completely the ‘polluter pays’ principle by requiring governments to pay companies to stop polluting.

Perhaps in recognition of this, there are some cosmetic provisions in the ECT that refer to energy sovereignty and environmental protection but they are remarkably weak compared to the unambiguous certainties of the sections on investor protection. For example, paragraphs in the environment chapter state that parties will merely “take account of”, “promote”, “have regard to”, “encourage” and “cooperate in” various aspects of environmental policy. These are aspirations rather than commitments, with no associated financial penalties and none of the enforceability or legal clout of the ISDS system.

At the same time as they were negotiating the climate deal, states agreed to further expand trade and investment protections for the energy sector. In 2015, sixty-nine countries signed the International Energy Charter (IEC). The IEC significantly increases the geographical coverage as compared with the ECT, by, for example, bringing the US

and China into the fold. It also aims to “remove all barriers to investment in the energy sector”, which could significantly increase liberalisation in the sector. Although the Charter itself is presented as non-binding, there is a clear intent to work towards a binding treaty. For its nod to climate change concerns, the IEC includes a commitment to promote energy pricing that “more fully” reflects environmental costs and benefits. Meanwhile, the list of stakeholders on its advisory panel includes the China National Petroleum Corporation, Gazprom, Shell, Dow Chemicals, BHP Billiton and BP. There is no parallel advisory panel on environmental or human rights issues.

Even if energy investors are not able to access protections under the ECT, or the IEC to come, they can look to the 2,318 Bilateral Investment Treaties (BITs) that are currently in force. They can increasingly also make use of a range of other protections against government policies they perceive as running counter to their interests, in the form of provisions contained in many of the world’s 267 Free Trade Agreements (FTAs). Investment protection chapters are also proposed for the pending ‘mega-regional’ agreements like the CETA (the EU-Canada FTA), the Trans-Pacific Partnership (TPP) and the Trans-Atlantic Trade and Investment Partnership (TTIP). If ratified, these deals would vastly increase the opportunities for foreign investors to access ISDS protections and impose significant limits on the ability of governments to implement policies in support of the energy transition.

A recent example demonstrates how these provisions can undermine measures that support the transition away from fossil fuels. In early January 2016 TransCanada Corporation filed a notice of intent to initiate a multibillion-dollar claim against the US under the North American Free Trade Agreement (NAFTA). The US government had denied a presidential permit for the extension of the Keystone XL cross-border oil pipeline. President Obama stressed that the project was at odds with climate change targets, commenting “if we’re going to prevent large parts of this Earth from becoming not only inhospitable but uninhabitable in our lifetimes, we’re going to have to keep some fossil fuels in the ground rather than burn them and release more dangerous pollution into the sky.” Despite this, TransCanada are claiming US\$15 billion in compensation. This would clearly be difficult to justify on any rational basis, as not one centimetre of pipeline extension had ever been built, nor, by its own admission, had the company incurred anywhere near US\$15 billion in costs. (Costs which could easily have been covered by paying for the private insurance to cover such losses that was already

widely available on international markets long before the advent of NAFTA). The only way they could come up with such a figure was to sue not for an actual loss, but for hypothetical expected revenues, something that the current international trade and investment regime considers part of companies’ ‘legitimate expectations’.

The precedents for many of the substantive rules contained in these deals are to be found in the World Trade Organisation (WTO) agreements. This includes the principle that all other policy measures must not unnecessarily restrict or create obstacles to international trade. The WTO has also established a set of rules on subsidies, public procurement, standards (including environmental standards) and the protection of international investment. In theory, WTO rules could be used to challenge the damaging subsidies that prop up the fossil fuels industry. In reality, not a single case against state subsidy of fossil fuels has ever been brought through the WTO. In stark contrast, countries are instead increasingly using WTO rules to challenge measures to support the renewable energy sector.

It is beyond doubt that climate change is one of the most urgent issues of our time. It is also almost universally accepted that in order to address climate change, states need to radically change their energy policy. As this report outlines, there exists a significant network of trade and investment agreements that govern the energy sector. Yet ahead of the UNFCCC COP21, the conference that led to the Paris Agreement, the EU’s trade policy committee issued a statement arguing that “the UNFCCC is not the appropriate forum to discuss trade measures” and that the EU should “continue to oppose discussion of trade measures under UNFCCC.”

As an essentially voluntary treaty with no meaningful enforcement mechanisms and no influence over crucial macroeconomic processes, the Paris Agreement looks like a feather in the path of the trade juggernaut. We urgently need to redesign international trade and investment rules to put them at the service of climate goals, and we need to do it now – saving the battle for another day will be too late.

¹ All references for this section can be found in the relevant sections of this report

Introduction

In March 2015, global carbon dioxide levels passed 400 parts per million (ppm), described by the Intergovernmental Panel on Climate Change (IPCC) as “the highest in history” and well beyond the 350ppm argued to be a safe level.² As a result of these unprecedentedly high levels of carbon in the atmosphere, weather patterns are changing, including increasingly extreme drought in some areas and rainfall in others, with serious implications for human, animal and plant life.³

The December 2015 United Nations Conference of the Parties (COP) 21 saw 195 countries commit to keeping the global temperature rise below two degrees Celsius and to work to limiting the increase to 1.5 degrees Celsius above pre-industrial levels. Parties to the agreement also committed to peak their CO₂ emissions “as soon as possible” and to eventually reduce them to a global limit of 40 gigatonnes.⁴

The IPCC has found that global increases in CO₂ emissions are due primarily to fossil fuel use, which has tripled since 1970 and accounts for around 57% of total emissions.⁵ As a result, there is broad agreement that in order to achieve climate change goals, global energy policy will need to change significantly: three quarters of the existing proven reserves of oil, gas and coal need to be left in the ground and there needs to be a transition to an energy system based on renewable sources such as wind, sun and water.⁶

There are, however, significant barriers to moving away from the status quo. The high costs of exploration, production and distribution plus the potential profits in the energy sector make it the single largest destination for foreign direct investment: figures for 2014 show that combined investment in coal, oil, natural gas and alternative and renewable energy accounted for US\$124 billion of the total global flows of US\$649 billion.⁷

Much of this investment is protected by international trade and investment deals. There are currently 2,318 Bilateral Investment Treaties (BITs) globally and a growing number of international trade

deals contain chapters on investment.⁸ The most significant of these deals is the Energy Charter Treaty (ECT), which entered into force in 1998 and covers trade in energy between fifty-four countries. As one commentator notes, “[t]he ECT...is the most extensive international agreement specifically regulating practically all energy issues.”⁹

One of the most controversial provisions of the ECT and other deals is the investor-to-state dispute settlement (ISDS) provision, which allows energy companies to sue countries if a policy or its implementation are considered to threaten the profitability of their investment. The energy sector is the subject of a significant number of disputes: half of all ISDS cases registered at the World Bank by the end of 2015 related to oil, mining, gas, electric power and other energy.¹⁰ The ECT has been used to bring no less than eighty-nine of the total 696 ISDS known cases globally, making it the number one treaty for investment disputes.

The reach of international trade and investment rules is not limited to the governance of international investment flows but also covers much of the world’s energy policy. So-called ‘mega-regional’ trade deals like the Transatlantic Trade and Investment Partnership (TTIP) and the Transpacific Partnership (TPP) seek to expand liberalisation in a number of ways that could limit governments’ ability to transition to sustainable energy use.

The precedent for these deals has been set by the WTO, which has established a number of principles that are used in most other deals. This includes the principle that all other policy measures must not unnecessarily restrict or create obstacles to international trade. The WTO has also established a set of rules on subsidies, public procurement, standards (including environmental standards) and the protection of international investment.

In contrast with climate agreements, all trade and investment agreements are both fully binding and enforceable. In the case of the WTO, this is via state-to-state dispute settlement. In an increasing number of bilateral and plurilateral trade and investment agreements, it is via investor-to-state dispute settlement (ISDS), whereby a company can sue a government at a private international tribunal for changes to policy that negatively impact on its perceived profitability.

This report explores the implications of the three major trade and investment architectures for the transition away from fossil fuels and towards renewable energy sources. It begins by outlining the agreement that has the most significant implications for energy policy: the Energy Charter Treaty (ECT) and its newly agreed complement, the International Energy Charter (IEC).¹¹ It then considers the network Bilateral Investment Treaties (BITs) and the major plurilateral and bilateral trade agreements currently under negotiation between the EU and its partners, and their implications for the evolution of energy-related trade and investment policy. Finally, it outlines the provisions of the WTO, and examines the capacity of the global multilateral trade and investment architecture to support climate change goals.

² IPCC (2014);

³ Adam Vaughan, 6th May 2015 *Global carbon dioxide levels break 400ppm milestone* The Guardian <http://www.theguardian.com/environment/2015/may/06/global-carbon-dioxide-levels-break-400ppm-milestone> accessed 15/04/16.

⁴ UNFCCC 12 December 2015 *Historic Paris Agreement on Climate Change: 195 Nations Set Path to Keep Temperature Rise Well Below 2 Degrees Celsius* <http://newsroom.unfccc.int/unfccc-newsroom/finale-cop21/> accessed 15/04/16

⁵ IPCC (2007), p.36; IPCC (2014) p.11 and p.45

⁶ ODI (2015) p.11. In 2009, as part of their commitment to changing energy policy, G20 leaders agreed to phase out 'inefficient' fossil fuel subsidies. However countries have been slow to implement this commitment: G20 countries provided US\$452 billion in subsidies in 2014. See G20 Leaders' Statement—The Pittsburgh Summit, Sept. 24 – 25, 2009, available at http://www.treasury.gov/resource-center/international/g7-g20/Documents/pittsburgh_summit_leaders_statement_250909.pdf accessed 19/03/16.

⁷ 2014 figures; amount allocated to energy excludes financial, communications, transportation or IT services associated with these sectors, including these sectors would significantly increase the final figure. Financial Times (2015) *The FDI Report 2015: Global Greenfield investment trends* <http://www.ftbsites.ft.com/forms/fDi/report2015/files/The-fDi-Report-2015.pdf> accessed 12/03/16

⁸ Information on these deals is available on UNCTAD's Investment Policy Hub <http://investmentpolicyhub.unctad.org/IIA> accessed 10/05/16

⁹ Nikos Lavranos, European Federation for Investment Law and Arbitration *To Include or Not to Include an Energy Chapter in TTIP?* December 2015 <http://kluwarbitrationblog.com/2015/12/30/to-include-or-not-to-include-an-energy-chapter-in-ttip/> accessed 10/05/16

¹⁰ According to the ICSID website, 213 cases were pending on 2 November 2015. 57 of them related to the oil, gas and mining sector, and 48 related to electric power and other energy. <https://icsid.worldbank.org/apps/ICSIDWEB/cases/Pages/AdvancedSearch.aspx> accessed 10/05/16 UNCTAD (2015), p.114

¹¹ One of the four 'main objectives' of the IEC is to "contribute to solid global energy governance by facilitating new accessions to the Energy Charter Treaty" - see International Energy Charter: Agreed text for adoption in The Hague at the Ministerial Conference on the International Energy Charter on 20 May 2015

Chapter 1

Investor Protections and Energy Transition

Key points:

- Investment agreements govern a growing proportion of global investment in the energy sector;
- Under these agreements, investors are offered sweeping protections that threaten to prevent action to move away from fossil fuels and towards renewable energy;
- None of the agreements have any binding commitments in respect of climate change.

The high costs of exploration, production and distribution and the potential profits in the energy sector make it the single largest destination for foreign direct investment: figures for 2014 show that combined investment in coal, oil, natural gas and alternative and renewable energy accounted for US\$124 billion of the total global flows of US\$649 billion.¹² A large network of trade and investment agreements governs this investment, with significant implications for transitioning away from fossil fuel use.

1.1 The Energy Charter Treaty

“The ECT – which has been signed by 54 states – is the most extensive international agreement specifically regulating practically all energy issues.” Nikos Lavranos, European Federation for Investment Law and Arbitration.¹³

The Energy Charter Treaty (ECT) governs a significant proportion of trade and investment in the energy sector. The treaty entered into force in 1998 and has fifty-four member countries, including the twenty-eight EU member states but excluding major oil producers such as the US and Saudi Arabia.¹⁴ It covers five broad areas: energy investment, energy trade, freedom of energy transit, environmental protections and dispute settlement.¹⁵

Its overarching aim is to “catalyse economic growth by means of measures to liberalise investment and

trade in energy.”¹⁶ In order to do this the treaty:

- Offers protection to foreign investors in energy;
- Promotes the progressive liberalization of international trade in energy;
- Facilitates the removal of technical, administrative and other barriers to trade in energy materials and products; and
- Has a long-term objective of transferring its provisions to the WTO, thereby giving them global reach.¹⁷

The provisions of the ECT offer significant protections to investors. The treaty contains a broad definition of ‘investment’, including property rights, shares and intellectual property.¹⁸ This means that investors with varying levels of ‘presence’ in a country – from investment in mining to owning shares – are able to use the treaty to protect their interests. The provisions of the ECT are considered to offer the potential for even broader interpretation than other pre-existing investor protection treaties, as the following example illustrates:

“Even a debt under an agreement for supply of equipment for a nuclear plant assigned to the claimant seems to have satisfied the test. The ECT may therefore be a more attractive option for parties who may struggle to show a qualifying ‘investment’ under one of the narrower [Bilateral Investment Treaties]” Report by law firm Norton Rose Fulbright on the Energy Charter Treaty at 20.¹⁹

The ECT offers investors sweeping rights, for example to treatment that is equal to that offered to domestic investors (National Treatment), treatment that is no less favourable than that afforded to investors from other countries (Most Favoured Nation treatment), as well as protection against expropriation.

Two of these provisions have proven particularly problematic in the international investment protection regime. The first is protection against ‘expropriation’ of investments; such clauses cover outright nationalisation but are also regularly interpreted to include any regulatory measure that is deemed to harm, affect or interfere with an investment to such

an extent that it has the effect of an expropriation. The second is the so-called 'fair and equitable treatment' (FET) provision, contained in the majority of treaties. This provides that foreign investors should receive treatment no less favourable than that offered to domestic investors and has tended to be interpreted very broadly. For example, in a case against Mexico taken under an agreement with Spain, the Tribunal outlined its interpretation of the FET provision as requiring:

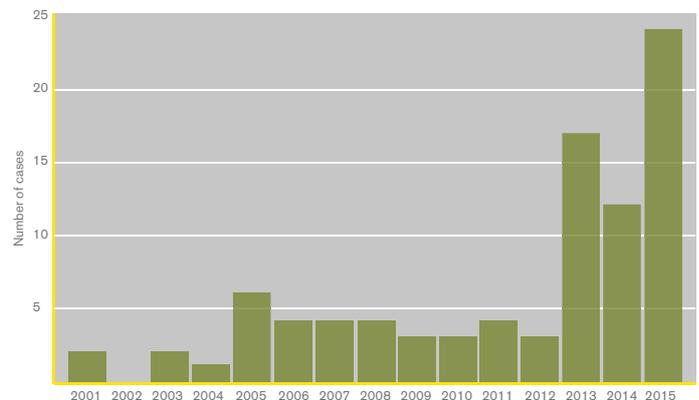
"The Contracting Parties to provide to international investments treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment. The foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor, so that it may know beforehand any and all rules and regulations that will govern its investments..."²⁰ The tribunal's definition continues for a further paragraph.

The ECT also bans local content requirements, which place conditions on foreign investors, for example to purchase a certain proportion of goods or undertake a certain proportion of their research and development locally (Article V, Energy Charter Treaty) and commits members to apply the principle of freedom of transit "without imposing any unreasonable delays, restrictions or charges" (Article VII). Bans on local content requirements have triggered a large number of cases that have challenged the development of renewable energy sectors in many countries (see Chapter 3, below for more on this). Taken together with strong investment protection provisions, the freedom of transit principle in particular is likely to place a serious restriction on countries' ability to reduce fossil fuel use.

In common with investment protections contained in other treaties, the provisions of the ECT are enforced via an investor-to-state dispute settlement (ISDS) clause. This has been described as "one of the most powerful legal mechanisms known to international law today."²¹ ISDS allows companies to sue governments in private tribunals for financial compensation if the company considers that a policy or its implementation has negatively affected the actual or potential profitability of their investment. The average cost of defending a case is US\$8 million and awards are generally in the millions, if not billions of dollars. The ISDS system therefore offers a significant advantage to foreign firms and to those who can afford the costly legal fees. By contrast, no similar system exists for domestic investors and smaller players in the energy sector are far less likely to bring a case. In this way, ISDS serves to reverse completely the 'polluter pays' principle by requiring governments to pay companies to stop polluting.²²

The energy sector is the subject of a significant number of ISDS disputes: half of all cases registered at the World Bank by the end of 2015 related to oil, mining, gas, electric power and other energy.²³ ECT has been used to bring no less than eighty-nine of the total 696 ISDS known cases globally, making it the number one treaty for investment disputes. In 2015, a third of all new ISDS cases brought to the World Bank's International Centre for the Settlement of Investment Disputes (ICSID) were brought under the ECT; by way of comparison, the 2,318 Bilateral Investment Treaties put together were responsible for 46% of the caseload, only 11% more than the ECT.²⁴

ECT cases by year



Germany weakens environmental legislation in response to ECT case

In 2007, Swedish company Vattenfall was granted a water permit to build a coal-fired power plant on the banks of the Elbe river. However, in response to significant public concern regarding the environmental impact of the plant, local authorities imposed strict environmental conditions to limit the utility's water usage, drawing on, among others, EU regulations to protect fish species. Vattenfall argued that these environmental measures were so strict that they made the plant uneconomical and therefore constituted an act of indirect expropriation under the ECT.

The case was settled in 2011: Germany issued a new permit that significantly lowered the environmental standards that had originally been imposed. The case is particularly worrying because it suggests that even measures taken to implement internationally agreed standards and targets are not immune to challenge, creating a significant block to regulation and policy-setting in respect of the energy sector.²⁵

Whilst the ECT contains an article on sovereignty over energy resources and a separate chapter on environmental protection, both are weak and contain only 'soft law' commitments. Paragraphs in the environment chapter state that parties will "take account of", "promote", "have regard to", "encourage" and "cooperate in" various aspects of environmental policy. Article 19 states only that "each Contracting Party shall *strive to minimize in an economically efficient manner* harmful Environmental Impacts" (emphasis added). It contains a commitment to the polluter pays principle but its implementation must be "without distorting Investment in the Energy Cycle or international trade." These commitments lack any of the significant legal clout of ISDS.²⁶

It is also technically possible for renewable energy companies to use the ECT to challenge policies that they consider to negatively affect their investments. When, in 2010, Spain removed measures a previous governments had put in place to promote renewable energies (caps on end user prices, feed in tariffs and other subsidies) in the face of a €4.5 billion payment deficit owed to utilities, a consortium of renewable energy companies put in claims under the ECT. However the first of the claims was rejected in January 2016, setting a precedent (if not necessarily a binding one), for remaining cases.²⁷ Even more drastically, when Italy was faced with a threat over similar measures to protect subsidies for renewables, its government withdrew from the ECT altogether.²⁸

1.2 The International Energy Charter – expanding investor protections in energy

This aspect of the international trade and investment regime is changing fast. In 2015 sixty-nine countries and international organisations signed the International Energy Charter (IEC).²⁹ The IEC is intended to expand on the ECT. While its provisions are currently not specific or binding, there is a clear intent to work towards a specific set of binding rules that would constitute "the premier instrument of global energy cooperation and governance."³⁰ If this were to happen, the IEC would signal a significant geographic expansion relative to the ECT, of specific protections for energy investors. Many more energy firms, from Chinese coal companies to US oil and gas corporations, would be empowered to challenge UK climate policies in private international tribunals.³¹

The IEC follows the ECT in providing only weak commitments to environmental protection, for example merely stating that the charter will take action in the field of energy efficiency and

environmental protection that will "imply" the "promotion" of a sustainable energy mix designed to "minimise negative environmental consequences in a cost-effective way" through the use of renewable energy sources and clean technologies, "including clean fossil fuel technologies."³² As with the ECT, all of the agreements, declarations and protocols on environmental protection referred to in the IEC annex are voluntary. The charter also makes no reference to the globally-agreed goal of reducing and phasing out the use of fossil fuels.

The weak commitment to implementing its environmental commitments is also apparent in respect of the stakeholders that are being consulted in the evolution of the charter. The IEC explicitly seeks to "strengthen the dialogue with the private sector on the main directions of the Charter Process, with a particular focus on risk mitigation and improvement of the business climate."³³ For this purpose it has established an advisory panel made up of private-sector representatives. At least twenty-seven of the panel's forty-seven members represent companies or associations with a significant stake in gas and oil production, including E.On, the China National Petroleum Corporation, Gazprom, Shell, Dow Chemicals, BHP Billiton and BP.³⁴ One of its members – the Bulgarian Energy Holding – runs the power station ranked in 2014 'the industrial facility causing the highest damage to health and the environment' by the European Environment Agency.³⁵ There is no parallel advisory panel on environmental or human rights issues.

If it is made binding, the International Energy Charter will significantly increase the extent to which the global energy sector is subject to investment protection rules and therefore the ability of companies to challenge government policy on fossil fuels. One of the main reasons for this is that the US is not currently a member of the Energy Charter Treaty and only has a small number of Bilateral Investment Treaties with European countries (see below).³⁶ It could also add to the number of overlapping but divergent approaches to ISDS already in existence: provisions within NAFTA, CETA, TTIP and the Energy Charter Treaty are unlikely to be harmonised. This leaves the prospect of companies 'treaty shopping' to secure the best protections for their investments.³⁷

1.3 Bilateral Investment Treaties – 2,000 ways for energy investors to maintain the status quo

Alongside agreements that are specific to the energy sector, there also exists a global network of 2,318 Bilateral Investment Treaties (BITs) that

establishes yet more company-friendly standards and protection mechanisms. The UK alone has more than one hundred such treaties. Protections under these treaties are defined in much the same way and with many of the same problems of broad scope and vague definition as the ECT. BITs contain very few limitations on the sectors or activities they cover. This means that a broad range of government activity that affects the energy sector, from decisions regarding a country's energy mix to permits for fracking or changes in subsidy regimes, is governed by these rules.³⁸

The purpose of BITs is often described as being to establish a minimum standard of treatment for investors operating outside of their home territories. However guidance for arbitrators is limited to vaguely-worded clauses in the treaties. Decisions on the admissibility of a case and which government actions contradict the terms of the BIT is at the discretion of arbitrators. There are already numerous examples of ISDS tribunals that have found that the investor's right to this treatment can obligate a government to compensate a foreign corporation for policy changes perceived by the company as arbitrary or thwarting its expectation of regulatory 'consistency'. For example, in an ISDS case that Occidental Petroleum launched against Ecuador, the tribunal concluded that "the stability of the legal and business framework is...an essential element" of this broad foreign investor right.³⁹

ISDS is a powerful tool for protecting investments, unparalleled in international public law.⁴⁰ Energy has become one of the sectors where this provision is most-used. Energy companies are already regularly using ISDS to protect their own interests by challenging government policy. This is causing significant policy chill in relation to climate change at precisely the time when the world's leaders have come together to announce formally that a change in policy is urgently needed.

¹² 2014 figures; amount allocated to energy excludes financial, communications, transportation or IT services associated with these sectors, including these services would significantly increase the final figure. Financial Times (2015) *The FDI Report 2015: Global Greenfield investment trends* <http://www.ftsites.com/forms/fDi/report2015/files/The-fDi-Report-2015.pdf> accessed 12/03/16

¹³ Nikos Lavranos, European Federation for Investment Law and Arbitration *To Include or Not to Include an Energy Chapter in TTIP?* December 2015 <http://kluwerarbitrationblog.com/2015/12/30/to-include-or-not-to-include-an-energy-chapter-in-ttip/> accessed 10/05/16

¹⁴ Russia had signed but not ratified the treaty and in 2009 announced that it planned to withdraw from the treaty and ceased applying its provisions following a case brought against it by Yukos Universal in which the tribunal made an award of US\$50 billion. The award has since been

overturned, in April 2016, by a court in the Netherlands, Yukos may seek to challenge this ruling.

¹⁵ Konoplyanik & Waelde (2006), p.528; Energy Charter Secretariat (2016), p.15.

¹⁶ Energy Charter Treaty (1998) Preamble, available at http://www.energycharter.org/fileadmin/DocumentsMedia/Legal/1994_ECT.pdf, accessed 25/02/16

¹⁷ *Ibid*

¹⁸ *Ibid*, p.8

¹⁹ Ruff et al (2014), p.3

²⁰ Findings of the tribunal in *Tecmed v. Mexico*, cited in Dolzer (2014) p9

²¹ Van Harten (2015), p.1

²² *Ibid* p.1

²³ According to the ICSID website 213 cases were pending on 2 November 2015. 57 of them related to the oil, gas and mining sector, and 48 related to electric power and other energy. <https://icsid.worldbank.org/apps/ICSIDWEB/cases/Pages/AdvancedSearch.aspx> UNCTAD (2015), p. 114,

²⁴ World Bank (2016) *The ICSID Caseload – Statistics (Issue 2016-1)* [https://icsid.worldbank.org/apps/ICSIDWEB/resources/Documents/ICSID%20Web%20Stats%202016-1%20\(English\)%20final.pdf](https://icsid.worldbank.org/apps/ICSIDWEB/resources/Documents/ICSID%20Web%20Stats%202016-1%20(English)%20final.pdf) accessed 26/02/16

²⁵ Bernasconi (2009) & Provost & Kennard (2015)

²⁶ UNCTAD (2000)

²⁷ Volciuc-Ionescu, 28th January 2016 *Energy Charter Treaty Claims: Spain wins first solar case arbitration* available at <http://www.lexology.com/library/detail.aspx?g=56483dbf-aa32-4f52-a415-1f52492ad218> accessed 03/06/16

²⁸ Fiorelli, Gaetano Iorio 6th May 2015 *Italy Withdraws from Energy Charter Treaty* available at <http://globalarbitrationnews.com/italy-withdraws-from-energy-charter-treaty-20150507/> accessed 03/06/16

²⁹ More information on the IEC here http://www.energycharter.org/fileadmin/DocumentsMedia/Legal/IEC_EN.pdf accessed 25/02/16

³⁰ *Ibid*

³¹ One of the four 'main objectives' of the IEC is to "contribute to solid global energy governance by facilitating new accessions to the Energy Charter Treaty" - see International Energy Charter: Agree text for adoption in The Hague at the Ministerial Conference on the International Energy Charter on 20 May 2015

³² *Ibid*

³³ IEC, Who We Are: Industry Advisory Panel <http://www.energycharter.org/who-we-are/industry-advisory-panel/> accessed 25/02/16

³⁴ The full list of members of the panel is available here http://www.energycharter.org/fileadmin/DocumentsMedia/IAP/IAP_Members_list.pdf accessed 25/02/16

³⁵ European Environment Agency (2014) *Industrial Facilities Causing the Highest Damage Costs to Health and the Environment* available at <http://www.eea.europa.eu/data-and-maps/daviz/industrial-facilities-causing-the-highest-damage#tab-daviz-tabular> accessed 08/05/16

³⁶ Beachy (2015)

³⁷ Nikos Lavranos, European Federation for Investment Law and Arbitration *To Include or Not to Include an Energy Chapter in TTIP?* December 2015 <http://kluwerarbitrationblog.com/2015/12/30/to-include-or-not-to-include-an-energy-chapter-in-ttip/> accessed 10/05/16

³⁸ Van Harten (2015)

³⁹ Beachy (2015), p.9

⁴⁰ Van Harten (2015)

Chapter 2

The Mega-Regionals – plurilateral treaties and government policy options in the energy sector

Key points:

- Governments are being pressured to treat climate and trade policies as if they have no effect on each other;
- A growing network of bilateral and plurilateral trade and investment agreements threaten to restrict governments' ability to phase out of fossil fuels and support renewable energies;
- Companies are already using these agreements to sue governments at private tribunals for policies intended to support the transition away from fossil fuels.

Countries are negotiating a growing number of bilateral and plurilateral trade and investment agreements whose scope is broader than that of the agreements described in chapter one. Whereas agreements covering the energy sector are limited to that particular sector and investment agreements deal exclusively with the protection of foreign investment, Free Trade Agreements (FTAs), including the so-called 'mega-regional' agreements, extend to almost all areas of government activity, from procurement to the establishment of regulations and standards, with huge implications for the energy transition.

Under the Lisbon Treaty of 2009, the EU took over full competence for trade and investment agreements. This meant that the UK had delegated negotiations on trade and investment to the EU. The UK decision to leave the EU means that this competence will be transferred back to the UK. At the time of writing and for the immediate future, it is not clear whether the UK will take part directly in any of the EU's existing or future deals. If the UK follows the model of Norway and Switzerland, it will negotiate its own deals independently. However certain aspects of the deals to which it is currently a party, in particular the ISDS provisions, will continue

to apply for up to twenty years after the UK exits the EU. Even if the UK is not automatically made a party to the deals, it may seek to join as a third party once they are concluded. It is therefore pertinent to consider EU FTAs like TTIP and CETA alongside deals like TISA for which there are relatively few obstacles to the UK joining in its own right.

The EU currently has eight full Free Trade Agreements (FTAs) in force, including with Mexico and Chile, and a further sixteen under negotiation with countries like the US and Japan.⁴¹ The deals vary considerably in scope: negotiations on the EU-US Transatlantic Trade and Investment Partnership Agreement (TTIP) cover a broad range of topics while Economic Partnership Agreements (EPAs) with African, Caribbean and Pacific (ACP) countries currently cover goods only.⁴² Negotiations are also at very different stages: those with the ASEAN (Association of South East Asian Nations) region and India have stalled; agreements with the ACP, Canada (CETA) and South Korea have been concluded but still need to be ratified.

It has to date been very rare for a specific energy chapter to be included in FTAs. The US has included it only once, in NAFTA's Chapter 6.⁴³ The EU has included energy related provisions in some of its agreements, in particular the EU-Ukraine Association Agreement (recently rejected in a referendum in the Netherlands, which could mean that the deal will collapse) and the Deep and Comprehensive Free Trade Area agreements with Moldova and Georgia.⁴⁴ However it has failed to secure full energy chapters in the EU-Singapore FTA (although this deal contains a specific chapter covering non-tariff barriers to trade and investment in renewable energy generation), CETA (the EU-Canada deal) and the EU-South Korea FTA.⁴⁵ Where energy has been covered by trade agreements, the provisions tend to fall into four limited categories: to clarify that generally applicable rules on trade in goods apply to trade in energy goods; to narrow some of the exceptions that could otherwise be utilised under the WTO agreements to restrict imports or exports of energy products; to create a more explicit definition

Mega regionals that could threaten climate change goals

Transatlantic Trade and Investment Partnership (TTIP)

A deal between the EU and the US which, if agreed, would cover nearly half of the world's GDP and one third of the world's trade.⁴⁸ Because border tariffs between the two parties are already relatively low, the focus is on so-called 'behind the border measures' or 'non-tariff barriers' to trade.⁴⁹ These measures include regulations and standards, many of which have implications for countries' ability to address climate change. The negotiating partners also envisage the inclusion of an investment protection chapter that would increase the likelihood that governments will be sued for measures taken to support the phase out of fossil fuels. The EU admits that every scenario it envisages for TTIP leads to an increase in CO₂ emissions.⁵⁰

Comprehensive Economic and Trade Agreement (CETA) & Trans-Pacific Partnership (TPP)

CETA is a deal between the EU and Canada that was concluded in 2014 and is slated for ratification in 2016. TPP was negotiated between 11 Pacific Rim countries, agreed in 2015 and due for ratification in 2016. Both deals contain investment protection chapters and provisions on public procurement that prohibit local content requirements and could therefore hinder the development of the renewable energy sector in partner countries. The TPP requires the US Department of Energy to automatically approve all exports of liquefied natural gas to participating countries.⁵¹

Trade in Services Agreement (TISA)

TISA is being negotiated between twenty-two parties, including the US, Mexico, Australia and the EU, covering around 70% of international trade in services. Leaked documents show that negotiators plan to include a chapter on measures affecting trade in energy related services. Proposals for the chapter include agreeing the principle of 'technological neutrality', such that regulation would no longer be able to distinguish between sources of energy – this would mean that countries would not be able to offer incentives to investment in one energy sector without offering them to all sectors, hindering the development of renewable energies.⁵²

of freedom of transit as applied to energy products; and to create a streamlined dispute resolution procedure to address issues of interrupting transit of energy goods.⁴⁶

The EU and the US have different positions regarding the inclusion of an energy chapter in TTIP; the outcome of these negotiations could set a significant global precedent for the relationship between trade rules and the energy sector. Transatlantic trade in non-crude oil and gas products has for some time been very high: mineral fuels, petroleum and petroleum products are consistently in the top five exports into each other's markets.⁴⁷ At the time of the NAFTA negotiations, the US was concerned that it did not have access to a sufficiently reliable energy supply, so was a proponent of the inclusion of an energy chapter. More recently, however, these concerns have abated in response to the dramatic rise in US production of gas and oil (the US is now the world's largest producer of liquid fuels and the largest gross exporter of refined products). As a consequence, in December 2015 the US ended its forty-year ban on exports of crude oil and gas. In the context of TTIP, it now argues that a standalone chapter on energy will not be needed and that the issues will be addressed in the other chapters of the deal.⁵³

The EU's energy situation is very different. Its major priority is to reduce its high dependency on imports of Russian oil and gas.⁵⁴ One of the ways that it is seeking to do this is to increase the coverage of energy within trade and investment rules globally. In its 2015 strategy paper it states that "access to energy and raw materials is critical for the EU's competitiveness" and as a result for the first time states explicitly that it is "committed to proposing an energy and raw materials chapter in each trade agreement" (this paper was released after the conclusion of the deals mentioned above).⁵⁵ It believes that an energy chapter in TTIP could help to address these issues by serving as "a model for subsequent negotiations involving third countries" and sending "a powerful signal to other countries that trade in raw materials and energy can be and will be subject to global governance."⁵⁶ The EU has also set its sights on 'tackling' specific elements of the global energy industry that it considers to be problematic, including local content requirements.⁵⁷

The EU produced a proposal for a TTIP energy chapter very early in the negotiations. Whilst these have not been officially published, a version was leaked in September 2013.⁵⁸ The chapter aims at facilitating the export of "coal, crude oil, oil products, natural gas, whether liquefied or not, and electrical energy" from the US to Europe.⁵⁹ Fracked US shale gas and tar-sands oil from Canada transiting

through the US would be included in this mix. The subsequent provisions include: the removal of export restrictions, including the automatic granting of export licenses for energy goods; the removal of trading and export monopolies; the elimination of local content requirements and a ban on any requirement to share intellectual property. The initial EU Position Paper on Raw Materials and Energy further suggests that local content requirements for renewable energy subsidies should be restricted.⁶⁰

These proposals are much more extensive than the energy-specific trade provisions in the EU's previous bilateral agreements.⁶¹ The provisions on export restrictions and export licenses would lead to increased investment in fossil fuel infrastructure and increased business interest in maintaining production and trade in fossil fuels. This is very likely to drive up the cost of transitioning away from fossil fuel dependency: the International Energy Agency estimates that if energy investments continue to favour emissions-intensive infrastructure up to 2020, the investment required up to 2035 to achieve low-carbon objectives would increase from US\$1.5 trillion to US\$5 trillion.⁶² As evidenced by the cases being taken to the WTO (see chapter 3) the elimination of local content requirements can undermine state support for renewable energy programmes. Finally, placing limits on the sharing of technology could further hamper the expansion of the renewable energy sector.

Even without a specific energy chapter, other provisions in both EU and US deals can be applied to the energy sector. The final text of CETA has been available since March 2016 and provides an example of how important energy-related provisions can be included in chapters that do not explicitly cover energy:

- CETA's procurement chapter prohibits local content requirements for contracts over a certain value. The provincial government of Ontario has estimated that the thresholds defined by CETA will increase coverage to 80% of the value of all government procurement – much more than under WTO provisions. This could threaten the province's 'Green Energy Act' because the Act requires significant local content in solar and wind projects in order for energy producers to benefit from generous feed-in-tariff rates. The province has already been required to amend its local content requirements in response to a WTO ruling (see chapter 3).⁶³
- The chapter on domestic regulation obliges parties to ensure their licensing requirements (which could include environmental permissions and approvals) are "as simple as possible and

do not unduly complicate... the pursuit of any... economic activity." This places a significant burden of proof on governments to demonstrate that any environmental measure does not 'unnecessarily' hinder trade.

- The rules on subsidies are not covered by the general exceptions that would normally shelter "market correcting" subsidies such as those for renewable energy.⁶⁴ In other words, the deal contains nothing to ensure that subsidies to support renewable energy – not even those to support new industries that might struggle to compete with existing non-renewable competitors – are protected from challenges by foreign investors or governments.
- Finally, the chapter on trade and sustainable development contains no binding commitments, instead the parties aim to 'enhance coordination', 'promote dialogue' and 'enhance enforcement' of environmental and labour goals. There is no specific mention of sectors such as mining, energy and transportation and no reference to the need to phase out the use of fossil fuels.⁶⁵

Similarly, irrespective of whether or not an energy chapter is included in TTIP, ISDS provisions would in principle apply to the energy sector. This has a number of implications. It would significantly increase the exposure of EU countries to potential cases from the US – the US currently only has treaties containing ISDS provisions with nine of the twenty eight EU member states, under TTIP, ISDS provisions would apply to all states.⁶⁶ This in turn increases the potential for US companies to challenge policies aimed at phasing out fossil fuels or supporting the renewables sector. Indeed, this is already occurring under existing treaties; for example, in March 2015 an ISDS tribunal ruled against Canada for denying a mining project that was rejected by an environmental review panel.⁶⁷ As with investment agreements, the question of the business's 'reasonable expectations' was key to the tribunal's findings. It suggested that the environmental review panel's decision was "arbitrary" and contrary to "reasonable expectations," and that this violated US mining firm Bilcon's right to a "minimum standard of treatment."⁶⁸

The European Commission claims that "preventing dangerous climate change is a key priority" and that it is "working hard to cut its greenhouse gas emissions substantially while encouraging other nations and regions to do likewise."⁶⁹ It has set targets to reduce greenhouse gas emissions by 20 per cent by 2020 and 40 per cent by 2030 against 1990 levels. Yet in the case of TTIP, the European Commission's own impact assessment states that its preferred outcome from the negotiations (an

Lone Pine Resources and TransCanada challenge energy policy

Some of the most prominent energy-related cases include:

- Lone Pine Resources is seeking damages of US\$118.9 million against Canada under NAFTA in response to Quebec’s moratorium on fracking. The moratorium was passed in response to a number of reports which found that fracking would lead to significant adverse environmental impacts in the St. Lawrence river. The company claims that the revocation of fracking licenses constitutes an expropriation of its investment and has called the restriction an “arbitrary, capricious, and illegal revocation” of the firm’s “valuable right to mine for oil and gas.” Lone Pine asserts that the decision to not allow fracking under the province’s largest waterway has “no cognizable public purpose.” It has further argued that the moratorium violates the NAFTA guarantee of a “minimum standard of treatment” because it “violated Lone Pine’s legitimate expectation of a stable business and legal environment.”⁷¹
- In early January 2016 TransCanada Corporation filed a notice of intent to initiate a multibillion-dollar claim against the US under the North American Free Trade Agreement (NAFTA). The US government denied a Presidential Permit for the Keystone XL cross-border oil pipeline, stating that they believed it would not make a significant contribution to economic growth, to job creation or to the reduction of energy prices. In a speech announcing the decision, Obama also stressed that the project was at odds with climate change targets: “if we’re going to prevent large parts of this Earth from becoming not only inhospitable but uninhabitable in our lifetimes, we’re going to have to keep some fossil fuels in the ground rather than burn them and release more dangerous pollution into the sky.”⁷²

TransCanada are citing national and most-favoured nation treatment, treatment in line with international law and expropriation as grounds for the case. They are claiming more than US\$15 billion in costs and damages and argue that they have invested billions of dollars in preparatory work under the “reasonable expectation” that a permit would be granted. Estimates suggest that TransCanada’s total investment to date is only US\$2.4 billion; the rest of the claim is to cover ‘loss of expected revenues’.⁷³

agreement that covers as many sectors as possible and achieves maximum liberalisation) will add an additional 11 million metric tons per year of CO₂ to the atmosphere.⁷⁰ Whilst the Commission suggests that this increase is small, at 0.07 per cent of the current annual rate, it also acknowledges that “every scenario” for a possible agreement will increase trade and the use of resources for production and that this creates “dangers for both natural resources and the preservation of biodiversity.” Despite this, the EU’s trade policy committee issued a statement ahead of the UNFCCC COP21, arguing that “the UNFCCC is not the appropriate forum to discuss trade measures” and that the EU should “continue to oppose discussion of trade measures under UNFCCC.”⁷⁴

The US is also pursuing policies in tandem that are fundamentally at odds with each other. The US submission to the UNFCCC states that it aims to reduce its greenhouse gas emissions by 26-28 per cent below its 2005 level in 2025.⁷⁵ Yet in 2015 the Obama administration sought special provisions to allow it to ‘fast-track’ trade negotiations so that the input of Congress is limited to a ‘yes or no’

vote. In order to secure Congress’s approval for this move, the administration agreed to introduce the ‘Bi-partisan Congressional Trade Priorities and Accountability Act of 2015’ which will specifically ensure that “trade agreements do not require changes to US law or obligate the United States with respect to global warming or climate change.”⁷⁶

Climate and trade policies are currently being developed in such a way that they directly contradict each other. The proposed mega-regional trade deals, if implemented, could add significantly to the ‘free trade’ rules already standing in the way of achieving the phase out of fossil fuels and transition to renewable energy sources necessary to enable the Paris Agreement to be fulfilled. These new plurilateral deals cover most of the world’s trade, threaten to further lock in fossil fuel use and infrastructure, and offer only very weak exemptions for countries introducing climate-friendly regulation, while at the same time offering very strong enforcement mechanisms for companies seeking to protect their interests in industries responsible for significant greenhouse gas emissions.

- ⁴¹ These figures exclude Association Agreements because they do not contain significant trade liberalisation; “in force” refers only those deals that have been ratified; those that have been concluded but not ratified are included in the number classed as ‘under negotiation’.
- ⁴² EPAs contain a ‘rendez-vous’ clause that commits partners to negotiate on issues such as investment and competition policy at a future date.
- ⁴³ NAFTA Chapter 6, available at <http://www.sice.oas.org/trade/nafta/chap-06.asp> accessed 21/03/16.
- ⁴⁴ BBC, April 2016 *Netherlands Rejects EU-Ukraine Partnership Deal* <http://www.bbc.co.uk/news/world-europe-35976086> accessed 11/05/16 The EU-Ukraine Association Agreement would have established a Deep and Comprehensive Free Trade Area (DCFTA) http://eeas.europa.eu/ukraine/docs/association_agreement_ukraine_2014_en.pdf accessed 30/04/16 Chapter 11 dealt with energy issues. Details on the other agreements can be accessed here: http://ec.europa.eu/trade/policy/countries-and-regions/agreements/index_en.htm accessed 11/05/16
- ⁴⁵ Text of the Comprehensive Economic and Trade Agreement (CETA) between Canada and the European Union available here: http://trade.ec.europa.eu/doclib/docs/2014/september/tradoc_152806.pdf; EU-Singapore Free Trade Agreement: Chapter 7 on non-tariff barriers to trade and investment in renewable energy generation but not on the full range of energy services and goods, see <http://trade.ec.europa.eu/doclib/press/index.cfm?id=961>; EU-Korea Free Trade Agreement documents http://trade.ec.europa.eu/doclib/cfm/doclib_section.cfm?sec=130 all accessed 21/03/16
- ⁴⁶ Benes, Keith (2015), p.11
- ⁴⁷ Eurostat (2013) Main Exports to the US (SITC level 2), EU-28 [http://ec.europa.eu/eurostat/statistics-explained/index.php/File:Main_exports_to_the_US_\(SITC_level_2\),_EU-28,_2013.png](http://ec.europa.eu/eurostat/statistics-explained/index.php/File:Main_exports_to_the_US_(SITC_level_2),_EU-28,_2013.png) accessed 31/03/16; Directorate-General for Trade (2015) *European Union, Trade in goods with USA* Brussels: European Commission http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc_113465.pdf accessed 31/03/16
- ⁴⁸ De Ville & Siles-Brugge (2016), p.39
- ⁴⁹ Priority areas for the negotiations include: increasing liberalisation in public procurement and services and introducing investment protection. Regulatory cooperation is also a priority, envisaged as ‘mutual recognition’ of standards, which means that standards on both sides of the Atlantic would be recognised as equivalent and therefore more easily traded within each party’s market.
- ⁵⁰ European Commission, March 2013 *Impact Assessment Report on the Future of EU-US Trade Relations* Section 5.8.2, p49 available at http://trade.ec.europa.eu/doclib/docs/2013/march/tradoc_150759.pdf accessed 20/03/16
- ⁵¹ Sinclair et al (2014) & Soloman & Beachy (2015)
- ⁵² Wikileaks (2015) *Expert Analysis on Energy Related Services (ERS) Annex Proposal: Questions and Answers* <https://wikileaks.org/tisa/Analysis-TiSA-Annex-on-Energy-related-Services-QA/page-3.html> accessed 16/04/16
- ⁵³ Benes, Keith (2015), p.7
- ⁵⁴ *Ibid*, p.8
- ⁵⁵ European Commission (2015). Previous strategies noted the importance of energy and raw materials to the EU economy but stopped short of calling for a separate energy chapter in trade deals, see for example European Commission (2010).
- ⁵⁶ European Commission, July 2013)
- ⁵⁷ European Commission (2015)
- ⁵⁸ European Commission (July 2013)
- ⁵⁹ *Ibid* Article A ‘Principles’, p2.
- ⁶⁰ European Commission (July 2013)
- ⁶¹ Benes, Keith (2015) p.15
- ⁶² International Energy Agency (2013) *Redrawing the Energy-Climate Map* Paris: IEA
- ⁶³ Sinclair et al. (2014) p.26
- ⁶⁴ Aaron Cosbey (2014) *Inside CETA: Unpacking the EU-Canada free trade deal* available at <http://www.ictsd.org/bridges-news/biores/news/inside-ceta-unpacking-the-eu-canada-free-trade-deal> accessed 31/03/16
- ⁶⁵ Sinclair et al. (2014), p.108
- ⁶⁶ Beachy (2016) finds that TPP and TTIP together would “grant broad foreign investor rights to more than 1,000 U.S. subsidiaries of over 100 foreign fossil fuel corporations - more than the total number of fossil fuel firms that have such rights under all 56 existing U.S. trade and investment pacts combined” p3.
- ⁶⁷ Other cases include: Shell Nigeria Ultra Deep Limited v. Federal Republic of Nigeria <http://www.italaw.com/cases/3320>, BP America Production Company, Pan American Sur SRL, Pan American Fuegoina, SRL and Pan American Continental SRL v. The Argentine Republic <http://www.italaw.com/cases/172>, Dow AgroSciences LLC v. Canada <http://www.italaw.com/cases/3407>, Mobil Investments Canada Inc. and Murphy Oil Corporation v. Canada <http://www.italaw.com/cases/1225>, Chevron Corporation and Texaco Petroleum Corporation v. Ecuador <http://www.italaw.com/cases/257>, and Occidental Petroleum Corporation and Occidental Exploration and Production Company v. Ecuador <http://www.italaw.com/cases/767>. The targets of recent ISDS cases include a fracking moratorium in Quebec, new coal-fired power plant standards and a nuclear energy phase-out in Germany, a court order to pay for pollution in Ecuador’s Amazon rainforest, a requirement to remediate toxic metal smelter emissions in Peru, and an environmental panel’s decision to reject a mining project in Canada. For summaries of these and other ISDS cases affecting environmental protections, see Solomon and Beachy (2015) & Public Citizen (2015) *Case Studies: Investor-State Attacks on Public Interest Policies* <http://www.citizen.org/documents/egregious-investor-state-attacks-case-studies.pdf> accessed 11/05/16.
- ⁶⁸ Beachy (2015), p.9
- ⁶⁹ European Commission *EU Action on climate* available at <http://ec.europa.eu/clima/policies/brief/eu> accessed 20/03/16
- ⁷⁰ European Commission, March 2013 *Impact Assessment Report on the Future of EU-US Trade Relations* Section 5.8.2, p49 http://trade.ec.europa.eu/doclib/docs/2013/march/tradoc_150759.pdf accessed 20/03/16
- ⁷¹ *Ibid*
- ⁷² President Obama, 6th November 2015 *Statement by the President on the Keystone XL Pipeline* <https://www.whitehouse.gov/the-press-office/2015/11/06/statement-president-keystone-xl-pipeline> accessed 06/04/16
- ⁷³ Democracy Now, January 2016 *TransCanada Sues the U.S. for \$15B for Rejecting Keystone XL. Will This Be the New Normal Under TPP?* available at http://www.democracynow.org/2016/1/7/transcanada_sues_the_us_for_15b accessed 11/05/16
- ⁷⁴ Trade Policy Committee, November 2015 *UNFCCC and Trade-related issues and intellectual property* – leaked document available at http://www.globaljustice.org.uk/sites/default/files/files/resources/trade_and_climate_trade_policy_committee.pdf.
- ⁷⁵ UNFCCC (2015) *US Cover Note INDC and Accompanying Information* available at <http://www4.unfccc.int/submissions/INDC/Published%20Documents/United%20States%20of%20America/1/U.S.%20Cover%20Note%20INDC%20and%20Accompanying%20Information.pdf> accessed 18/04/16.
- ⁷⁶ United States Congress House Rules Committee, June 2015 *Amendment to the Senate Amendment to H.R. 644: Trade Facilitation and Trade Enforcement Act of 2015* p251 Washington: US Congress available at <https://www.congress.gov/bill/114th-congress/house-bill/644/text> accessed 03/06/16

Chapter 3

WTO rules OK? Setting the parameters of environmental protection

Key WTO rules that impact on Energy Policy

General Agreement on Tariffs and Trade (GATT)

GATT binds WTO members to eliminate or reduce tariff rates (border taxes) and non-tariff measures applicable to trade in goods (manufactured and agricultural). Countries submit national schedules detailing the levels of liberalisation to which they have committed. Rules on non-tariff measures have a broad scope and include a number of measures that are relevant to energy policy, for example disciplines on subsidies and transport delays or restrictions.

General Agreement on Trade in Services (GATS)

GATS applies to trade in all services except those “supplied in the exercise of government authority”⁷⁷, broadly accepted to mean any public service that is provided on non-market terms. This means that any public service including energy that has been (partially) privatised or for which a charge is made is subject to GATS rules. There is no specific category for energy services in GATS but in practice they fall under a number of existing categories, including for example ‘cross-border services’ which could include pipeline and maritime transport, and ‘commercial presence’ which could be applied to foreign investment in oilfield services or distribution of gasoline.

Technical Barriers To Trade (TBT)

TBT specifies that technical regulations and standards must not “create unnecessary obstacles to international trade.”⁷⁸ It covers mandatory labelling schemes and minimum standards that relate to the end-use performance of a product. It contains two basic obligations for WTO Member States: first, a

provision prohibiting discrimination against and between foreign products; and second, the so-called ‘necessity’ requirement which obliges WTO members not to adopt standards that are “more trade-restrictive than necessary” for achieving ‘legitimate objectives’.⁷⁹ The latter requirement creates a significant burden of proof for governments seeking to introduce new regulation to the energy sector.⁸⁰

Agreement on Trade Related Investment Measures (TRIMS)

TRIMS applies GATT rules to investment measures that might have a trade-restrictive or distorting effect on trade in goods. It contains an ‘illustrative list’ of measures that are considered to be incompatible with the agreement, which in fact covers only local content requirements and quantitative restrictions (such as limits on the quantity of goods that can be imported for use in a production process).⁸¹ The deal’s scope has been elaborated through case law at the WTO’s dispute settlement mechanism. Forty-one challenges have been brought under this agreement, many of which relate to local content provisions in renewable energy programmes.⁸² TRIMS is more limited in scope than BITs because it applies to trade in goods only.

Agreement on Subsidies and Countervailing Measures (SCM)

Under the SCM, a subsidy is defined as a financial contribution and/or a benefit conferred by a government upon its domestic industries so that a given sector can develop with (temporarily) lower production costs and improve its competitiveness. A subsidy can take the form of loan guarantees, fiscal incentives such as tax credits, provision of goods and services other than general infrastructure, or direct payments to a funding mechanism.⁸³ Several specific kinds of subsidies are banned, including those that are linked to export performance or the use of domestic over imported products.⁸⁴

Government Procurement Agreement (GPA)

The GPA has been negotiated under the auspices of the WTO, although currently only 45 WTO members are signatories. It covers government purchasing of goods, services and construction work estimated to be worth US\$1.7 trillion annually.⁸⁵ The GPA follows other WTO agreements in both specifying that tenders for procurement must not create unnecessary obstacles to international trade and including an exception for “technical specifications to promote the conservation of natural resources or to protect the environment.”⁸⁶ Environmental exceptions have belatedly been introduced into the agreement, which means that there is no evidence yet as to whether they are effective in allowing governments to use procurement spending to promote climate-friendly practice.

Environmental Goods Agreement (EGA)

Negotiations towards the Environmental Goods Agreement were launched in July 2014 with the participation of 44 countries (including the 28 countries of the EU). The negotiations aim to reduce or eliminate tariff and non-tariff barriers to trade in environmental goods and services. However the negotiations quickly ran into difficulties when negotiators attempted to agree on a definition of an ‘environmental good’.⁸⁷ A key issue appears to have been that a number of goods, for example turbines, can be used for a variety of purposes not necessarily limited to those that are environmentally friendly.⁸⁸

Dispute Settlement Mechanism

The above agreements are enforceable via the dispute settlement mechanism. A ruling against a state is legally binding and can: require it to alter its policy or practice to bring it into compliance with WTO agreements; lead to a demand for compensation (generally in the form of offering a trade preference to the complainant); or (usually as the last resort) lead to trade retaliation from the complainant.⁸⁹



Key points:

- The WTO has proven itself unable to discipline environmentally harmful fossil fuel subsidies;
- WTO definitions of what classes as a subsidy have skewed the trade system in favour of the fossil fuel industry and away from the renewables industry;
- WTO rules contain no explicit exemptions for environmental subsidies; its dispute settlement system is frequently being used against renewable energy programmes.



The WTO is an intergovernmental organisation of 162 member states. It administers a set of international agreements covering trade in goods, services and intellectual property. The WTO agreements contain general rules, such as Most Favoured Nation treatment, which specifies that one member state should receive equal treatment to that accorded to all other partner states with which the state has a trade deal and National Treatment, which states that foreign entities should receive equal treatment with domestic ones. Agreements are enforced via a dispute settlement mechanism which allows a member state to bring a complaint against another member state if it believes the latter’s actions are inconsistent with WTO disciplines.

While there are no energy-specific provisions in the WTO agreements, general WTO provisions apply to trade in energy goods and services in the same way that they apply to other sectors. Most important among these are the provisions that preclude the setting of standards that are “more trade restrictive than necessary to fulfil a legitimate objective” or that have “the effect of creating unnecessary obstacles to international trade.”⁹⁰

Whilst the definition of ‘legitimate objective’ in the TBT (above) potentially allows some scope for climate-friendly changes to energy policy, the burden of proof on governments is extremely high. Similarly, to qualify as exempted under GATT, a measure must meet three separate tests. First, it must fall into one of a number of specific categories, which include: the fulfilment of national security requirements, the prevention of deceptive practices and the protection of human health or safety, animal or plant life or health or the environment. Second, a state must be able to demonstrate that the measure does not constitute “a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail” and finally that it is not a “disguised restriction on international trade.”⁹¹

In theory, WTO rules on subsidies and its dispute resolution mechanism could offer a way of challenging and reducing fossil fuels subsidies. However WTO members have been reluctant to explicitly include energy and fossil fuel subsidies in WTO agreements. This is primarily because countries fear sparking a global political rift that could jeopardise their national energy security or international trade prospects. For this reason, although energy subsidies are subject to the general rules under the SCM Agreement (see the Subsidies and Countervailing Measures section of the box above), not a single case has been brought against fossil fuel subsidies.⁹² Furthermore, the subsidy definition of the SCM agreement would be limited to the actual financial contributions (of around US\$775 billion) and would not cover the full extent of subsidies, calculated by the IMF to be US\$1.9 trillion when factors such as traffic congestion, road damage, accidents and pollution-related public health problems are taken into account.⁹³ Attempts to factor these subsidies into costs for fossil fuel industries, for example via a carbon or polluters' tax, could see countries challenged under the WTO's dispute settlement mechanism.⁹⁴

One of the only areas in which there has been serious discussion of applying WTO rules to fossil fuel subsidies relates to dual pricing schemes. Under dual pricing schemes, governments set a lower price for domestic consumption of fossil fuels than the price charged for exported fuel. This is problematic for two reasons: from an environmental perspective, it encourages greater consumption of fossil fuels by lowering the price that consumers pay; from a trade perspective, it can provide some companies or countries with cheaper energy inputs relative to the prices paid by competitors. Governments have periodically argued that these schemes are therefore either prohibited or at least actionable under WTO rules. However, in order to be found incompatible with WTO rules, the subsidies would have to be shown to be either linked to increased exports or to the use of domestic products over imported ones. Since dual pricing applies on an economy-wide basis, fossil fuel subsidies avoid both challenges.⁹⁵ This situation led former deputy-general Pascal Lamy to conclude that:

“The discussion on the reform of fossil-fuel subsidies has largely bypassed the WTO.”

Pascal Lamy, Director-General, WTO, April 2013.⁹⁶

In stark contrast to the approach to fossil fuel subsidies, countries are increasingly bringing cases to the WTO regarding renewable energy programmes. The WTO SCM agreement used to contain an exemption, Article 8.2(c), for subsidies for industrial policies favouring renewable energy, in order to allow firms to adjust to increases in costs of production caused by new environmental regulations. In 2000, however, this exemption was not renewed, opening the sector up to challenge.⁹⁷ Programmes including ones in Canada, India, the US, China, Italy and Greece have all been challenged under the WTO's DSM. The WTO has already ruled that India and Canada are in breach of their obligations under GATT and TRIMS and the state of Ontario was forced to amend local content requirements in its feed-in tariff system as a result of the challenge.⁹⁸

This has led to a situation that, in the view of report by a leading Washington think tank, means that:

“China and other countries are today being straightjacketed by the subsidies-are-bad ideology. The global battle against climate change is thus being fought with a depleted arsenal. Countries that have the financial means to do so should be allowed to deploy industrial policy to promote clean energy and green technologies.”

Mattoo & Subramanian, Center for Global Development.⁹⁹

Challenges to these renewable energy programmes are generally based on the fact that they include local content requirements, all forms of which are explicitly prohibited in WTO rules. Proponents of the WTO have argued that they therefore do not represent a challenge to the development of renewable energy per se.¹⁰⁰ However there are a number of reasons why governments choose to include local content requirements in their renewable energy programmes. Most important is the fact that the programmes involve considerable sums of public money. This means that the programmes would be difficult to justify politically if they did not incorporate some measures to guarantee benefits to the local or national economy.¹⁰¹

The overwhelming weight of evidence is that the WTO system of rules constitutes a significant hurdle that governments will have to overcome if they are to meet their climate commitments, and may delay or

prevent the introduction of policies aimed at realising the Paris Agreement. The institution is ill equipped to deal with the political and economic realities that governments face in phasing out fossil fuels and developing their renewable sectors. As a result, countries have been unable or unwilling to use WTO rules to tackle fossil fuel subsidies. The WTO, and the international trade and investment system it has helped to shape, has clearly demonstrated that it is not up to the task of supporting the energy transition that is so urgently needed.

⁷⁷ See WTO *The General Agreement on Trade in Services (GATS): objectives, coverage and disciplines* available at https://www.wto.org/english/tratop_e/serv_e/gatsqa_e.htm#3 accessed 02/06/16

⁷⁸ See WTO *Agreement on Technical Barriers to Trade* available at https://www.wto.org/english/docs_e/legal_e/17-tbt_e.htm accessed 02/06/16

⁷⁹ Bernasconi-Osterwalder & Norpoth (2009), p.11

⁸⁰ *Ibid*

⁸¹ WTO *Agreement on Trade-Related Investment Measures (TRIMs)* available at https://www.wto.org/english/tratop_e/trims_e.htm accessed 19/03/16

⁸² WTO *Disputes by agreement* available at https://www.wto.org/english/tratop_e/dispu_e/dispu_agreements_index_e.htm?id=A25 accessed 03/06/16

⁸³ Assuncao & Xiang Zhang (2002)

⁸⁴ WTO *Agreement on Subsidies and Countervailing Measures* available at http://www.wto.org/english/docs_e/legal_e/24-scm.pdf Article 25; see also Lang et al. (2010)

⁸⁵ Marc Steiner (1 December 2015) *The WTO Government Procurement Agreement: Assessing the Scope for Green Procurement* Geneva: ICTSD, available at <http://www.ictsd.org/bridges-news/biores/news/the-wto-government-procurement-agreement-assessing-the-scope-for-green> accessed 18/04/16.

⁸⁶ WTO (2012) *Revised Agreement on Government Procurement* Geneva: WTO, available at https://www.wto.org/english/docs_e/legal_e/rev-gpr-94_01_e.pdf accessed 18/04/16

⁸⁷ WTO *Eliminating trade barriers on environmental goods and services* available at https://www.wto.org/english/tratop_e/envir_e/envir_neg_serv_e.htm accessed 18/04/16

⁸⁸ Mahesh & Brewer, 22nd November 2012 *APEC's environmental goods initiative: How climate-friendly is it?* available at <http://www.ictsd.org/bridges-news/biores/news/apecs-environmental-goods-initiative-how-climate-friendly-is-it> accessed 03/06/16

⁸⁹ WTO *Dispute Settlement Mechanism* available at https://www.wto.org/english/tratop_e/dispu_e/dispu_e.htm accessed 11/05/16

⁹⁰ Bernasconi-Osterwalder & Norpoth (2009), p.11

⁹¹ WTO *WTO rules and environmental policies: GATT exceptions* available at https://www.wto.org/english/tratop_e/envir_e/envt_rules_exceptions_e.htm accessed 26/03/16

⁹² Asmelash (2014): 261

⁹³ International Fossil Fuel Subsidies, available at <http://priceofoil.org/fossil-fuelsubsidies/international/> accessed 26/03/16

⁹⁴ Asmelash (2014): 265

⁹⁵ Meyer (2013)

⁹⁶ Pascal Lamy, Director-General WTO, 29th April 2013 *Remarks to the Workshop on the Role of Intergovernmental Agreements in Energy Policy* available at https://www.wto.org/english/news_e/sppl_e/sppl279_e.htm accessed 03/06/16

⁹⁷ Assuncao & Xiang Zhang (2002), p.274

⁹⁸ See for example 'Reports of the Appellate Body, Canada – Certain Measures Affecting the Renewable Energy Generation Sector – Canada – Measures Relating to the Feed-In Tariff Program', available at https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds412_e.htm accessed 11/05/16

⁹⁹ Mattoo & Subramanian (2013)

¹⁰⁰ See for example Prabhash Ranjan and Deepak Raju (March 2016) *What the WTO Panel did not Decide on Solar Panels* Financial Express, available at <http://www.financialexpress.com/article/fe-columnist/what-the-wto-panel-did-not-decide-on-solar-panels/226070/> and Pradeep Mehta and Smriti Bahety (March 2016) *India's Solar Panel Dispute: A Need to Look Within The Wire* available at <http://thewire.in/2016/03/15/indias-solar-panel-dispute-a-need-to-look-within-24787/> both accessed 20/03/16.

¹⁰¹ Assuncao and Xiang Zhang (2002)

Conclusion

Taken together, investor protections - such as those contained in the ECT, the new IEC and BITs - free trade agreements such as the new megaregionals, and the existing fossil fuel friendly rules of the WTO, have together created an international trade and investment regime that is undermining efforts to realise the Paris Agreement's vision of a transition away from fossil fuels and towards renewable energy. The increased liberalisation inherent in these deals threatens to restrict governments' ability to introduce urgently-needed reforms in the energy sector.

Of particular concern is the Energy Charter Treaty which to date has received much less attention than some of the other agreements. Specifically covering the energy sector, with sweeping protections for investors and paying no more than lip service to environmental concerns, this agreement could be a major roadblock to achieving transition in the energy sector. Even more alarming are the attempts, in the form of the IEC – an agreement negotiated in the same year as COP21 but which is bound by no environmental rules – to secure greater geographical coverage and deeper liberalisation.

TTIP also poses a particularly significant threat. As currently envisaged, it would cover a wide range of sectors and greatly expand the possibilities for companies to challenge, via the ISDS system, government efforts to transition to sustainable energy.

As with the other mega-regional deals, TTIP is being negotiated in isolation from climate negotiations, leading to serious contradictions between the two. The new mega-regional deals cover most of the world's trade, threaten to further lock in fossil fuel use and infrastructure, and offer only very weak exemptions for countries introducing climate-friendly regulation.

The playing field between the environment and trade and investor protection is already far from level. Enforcement mechanisms mean that countries can face significant financial cost to any deviation from trade rules. There are no similar rules or enforcement mechanisms for the COP21 agreement. Unless this imbalance is redressed, the current system will continue to work to the detriment of climate change goals, not to their benefit.

The words of the Paris Agreement left no doubt that climate change is one of the most urgent challenges we face. The overwhelming evidence outlined in this report is that the current international trade and investment system is threatening to make it impossible to achieve the climate change goals contained within it. Fundamental reform of the international trade and investment regime, including the very basis of the system in the form of the WTO, will be needed if there is to be any hope of preventing the worst excesses of climate change.

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We believe that everyone has the right to feed their families, make a decent living and protect their environment. But the rich and powerful are pursuing trade policies that put profits before the needs of people and the planet. To end poverty and protect the environment we need trade justice, not free trade.

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