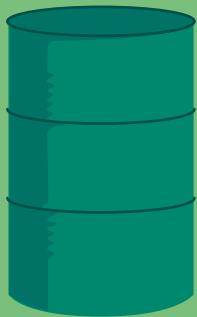


THE ENERGY CHARTER TREATY (ECT)

Assessing its geopolitical,
climate and financial impacts



OPENEXP

THE ENERGY CHARTER TREATY (ECT) IN NUTSHELLS

THE “RAISON D’ÊTRE” OF THE ECT IS NO LONGER THERE

The original objective of the ECT was quite rightly to overcome the political and economic divisions between Eastern and Western Europe as well as to strengthen Europe’s energy security. It was vital for Europe to secure the access to fossil fuels resources of the former Soviet regions by protecting the needed investment in these countries. However, the emergence of new global, regional and bilateral treaties and partnerships, since the entry into force of the ECT in 1998, questions the “raison d’être” of the ECT. This is particularly true as Europe’s energy security in a warming planet must be secured increasingly by endogenous energy savings and renewables and not by imported fossil fuels.

Almost 90% of the ECT signatories are members of the World Trade Organisation (WTO). Russia, with its extensive reserves of oil and natural gas, withdrew from the ECT in 2009 and swapped its provisional application of the ECT for WTO membership. Most of Eastern European countries are either members of the European Union or signatories of the Energy Community Treaty which aims at building an integrated and sustainable pan-European energy market by extending the EU energy acquis to neighbouring eastern countries. Furthermore, the over-protection of the economic interests of foreign investors by the ECT regime conflicts with the EU law which aims at protecting public interests and EU citizens who are expected to bear the cost of the long-term carbon neutrality target.

CLIMATE AND SUSTAINABILITY GOALS ARE THREATENED BY THE ECT PROTECTION OF FOSSIL FUELS INVESTMENTS

CO₂ emissions from fossil fuels investments are actually protected by the ECT. Since its entry into force in 1998, cumulative emissions protected by the ECT are estimated at 57 Gt CO₂ out of which 61% are committed CO₂ emissions from intra-ECT investment in fossil fuels. This is almost double of the remaining EU carbon budget, for the period 2018-2050, to limit the overshoot of the 1.5°C target. The continuation of investment protection of fossil fuels will further threaten global climate and sustainability goals. Arbitration tribunals under the ECT

regime encourage investors to shift onto taxpayers the financial risk that would result from investments in fossil fuels.

Various options can be considered for the modernisation of the ECT. Signatories of the Treaty could decide to not make any changes to the protection of fossil fuel investments under the ECT regime. In the no-ECT changes scenario, the “regulatory chill” effect of the ECT would discourage governments from aligning their regulations with the required climate targets under the Paris agreement leading to cumulative emissions of 148 Gt CO₂ protected by the Treaty by 2050. This is equivalent to almost five times the remaining EU carbon budget and 35% of the remaining global carbon budget over the period 2018-2050.

Another modernisation option could be to introduce the right for governments to regulate which would lower the costs for compensations due to regulatory changes, but fossil fuels will be kept in the list of energy materials and products protected by the ECT. Thus, investors can still challenge regulations and policy measures and claim huge compensations. The aim of this scenario is to foster trade among ECT signatories. In the trade scenario, cumulative CO₂ emissions protected by the ECT by 2050, would be 98 GtCO₂. This is more than three times of the remaining EU carbon budget and 23% of the remaining global carbon budget over the period 2018-2050. The no-ECT changes scenario and the trade scenario will both put climate and sustainability goals at risk as cumulative CO₂ emissions protected by the ECT would add to the already committed CO₂ emissions since its entry into force. The carbon neutrality target requires governments to consider ending investment protection for fossil fuels. In this scenario, foreign investment in the energy sector will have to align with the 1.5°C target and cumulative CO₂ emissions protected by the ECT by 2050 would be limited to those already committed since the entry into force of the ECT.

ARBITRATION TRIBUNALS UNDER THE ECT REGIME WILL INCREASE THE DECARBONISATION’S COST FOR THE TAXPAYER

The role of the ECT in attracting foreign investors is yet to be proven as shown by the Italian case. Since Italy’s

withdrawal from the ECT, foreign direct investments (FDIs) did not stop and average annual FDIs are around €3 billion. However, the use of taxpayers' money to compensate foreign investors, under the ECT regime for changes in regulations, has been demonstrated by the known 124 Investor-State-Dispute-Settlement (ISDS), under the ECT regime. ISDS cases in Italy and Russia occurred after their withdrawal as the investment protection under the ECT continues to apply twenty years after withdrawing. Furthermore, 70% of the known ISDS disputes under the ECT regime are intra-EU as intra-EU investments protected by the ECT represent 81% of total investments protected by the Treaty in signatory countries.

More than half of the total investments protected by the ECT are investments in fossil fuels. These investments are at risk of becoming stranded assets by 2050 and to increase the compensation costs governments would have to pay to investors for changes in regulation. Signatories of the ECT who have already adopted/announced their carbon neutrality target will have to allocate part of their public budget to compensate foreign investors for the "legitimate" expected revenues investors may lose due to adaptation of current regulations to the 1.5°C target. Based on the known compensation

for losses, governments may have to pay billions of Euros to investors as arbitral tribunals decisions are unpredictable and do not consider public interests when assessing investors' claims.

Investments in renewables represented one fifth of the total amount of investments protected by the ECT. However, ISDS cases related to renewables, which are mainly due to changes in feed-in-tariff in Spain, Italy and Czech Republic, represent so far more than 80% out of the known ECT ISDS cases. Most of ISDS renewable disputes under the ECT regime are intra-EU disputes. In theory, they should be settled under the EU law. However, as the ECT is considered a more favourable regime to investors, ISDS is the privileged option by investors to settle disputes.

CARBON NEUTRALITY TARGET AND CLIMATE JUSTICE OBJECTIVE REQUIRE ENDING THE ECT ERA

The energy context has changed significantly since the ECT was negotiated. Efforts to decarbonise the global energy system need to be strengthened and accelerated and carbon neutrality target must be achieved earlier than 2050 given the climate urgency. Meeting global climate and sustainability goals requires a paradigm shift in policies and regulations in order to retire fossil fuels infrastructures at a global level. The "regulatory chill" effect of the ECT due to governments' fear of ISDS procedures and their costs may water down any new legislation aiming at the carbon neutrality objective or simply prevent ECT signatories to regulate.

Phasing-out investment protection for fossil fuels is, obviously, the only option ECT signatories should be considering if they aim to implement the Paris Climate Agreement. However, this is unlikely to happen as ISDS, the most contentious issue under the ECT regime, is not explicitly included in the items agreed for the discussion on the modernisation of the Treaty, nor is mentioned the phase-out of investment protection to fossil fuels under the ECT regime to ensure the carbon neutrality target will be met by ECT signatories.

The gap in the climate ambition among ECT signatories and the required unanimity vote, for any proposed amendment to the Treaty, of all ECT signatories make it unlikely that countries with carbon neutrality target succeed, after several years of negotiations, in phasing-out fossil fuels protection and ISDS mechanisms from the ECT regime. Entering into endless negotiations would increase cumulative carbon emissions protected by the ECT. The only option left for countries with carbon neutrality targets is to withdraw from the Treaty.

(1) At any time after five years from the date on which this Treaty has entered into force for a Contracting Party, that Contracting Party may give written notification to the Depository of its withdrawal from the Treaty.

(2) Any such withdrawal shall take effect upon the expiry of one year after the date of the receipt of the notification by the Depository, or on such later date as may be specified in the notification of withdrawal.

(3) The provisions of this Treaty shall continue to apply to investments made in the area of a Contracting Party by investors of other Contracting Parties or in other area of other Contracting Parties by investors of that Contracting Party as of the date that Contracting Party's withdrawal from the Treaty takes effect for a period of 20 years from such date.

(4) All protocols to which a Contracting Party is party shall cease to be in force for that Contracting Party on the effective date of its withdrawal from this Treaty.

ECT Article 47 on Withdrawal

UNDERSTANDING THE ENERGY CHARTER TREATY

The Energy Charter Treaty (ECT) is a multilateral agreement aiming at establishing a legal framework to promote long-term cooperation in the energy field. The ECT grants binding protection for foreign investors including Fair and Equitable Treatment (FTE) and most Favoured Nation Treatment (FNT) as well as compensation for losses and protection against expropriation, both direct and indirect ones. The ECT includes also binding provisions for free trade and freedom of transit of energy materials and products. However, ECT provisions related to environmental protection, renewables (except for electricity) and energy efficiency are not binding despite being the first and the only international agreement which considers energy efficiency as a considerable energy source.

Investments protected by ECT provisions are typically supply side investments including those related to the exploration, extraction, refining, production, storage, land transport, transmission, distribution, trade, marketing or sale of energy materials and products (nuclear energy, coal, natural gas, petroleum and petroleum products, electrical energy and other energy sources such as fuel wood and wood charcoal). Investments in energy demand reduction and distributed heat to multiple premises are not protected by ECT provisions and the same occurs for modern energy services such as demand/response.

The ECT subjects the host state to several broad obligations and allows foreign investments and investors to enforce these through binding international arbitration. Amicable settlement of a dispute between an investor and a host state is one of the options proposed by the ECT. However, if a dispute cannot be settled amicably within a period of three months, the investor (individuals, companies, holdings, financial institutions) can choose to submit the dispute either to the courts or administrative tribunals of the host country or to international arbitration for Investor-State Dispute Settlement (ISDS). Under the ECT regime, an investor is not obliged to resolve disputes through available domestic remedies before filing ISDS claims and it is presumed that the host state has given its consent to international arbitration by becoming ECT signatory even before knowing who the claimant might be.

Where two or more Contracting Parties have entered into a prior international agreement, or enter into a subsequent international agreement, whose terms in either case concern the subject matter of Part III (Investment promotion and protection) or V (Dispute Settlement) of this Treaty,

(1) Nothing in part III or V of this Treaty shall be construed to derogate from any provision of such terms of the other agreement or from any right to dispute resolution with respect thereto under that agreement; and

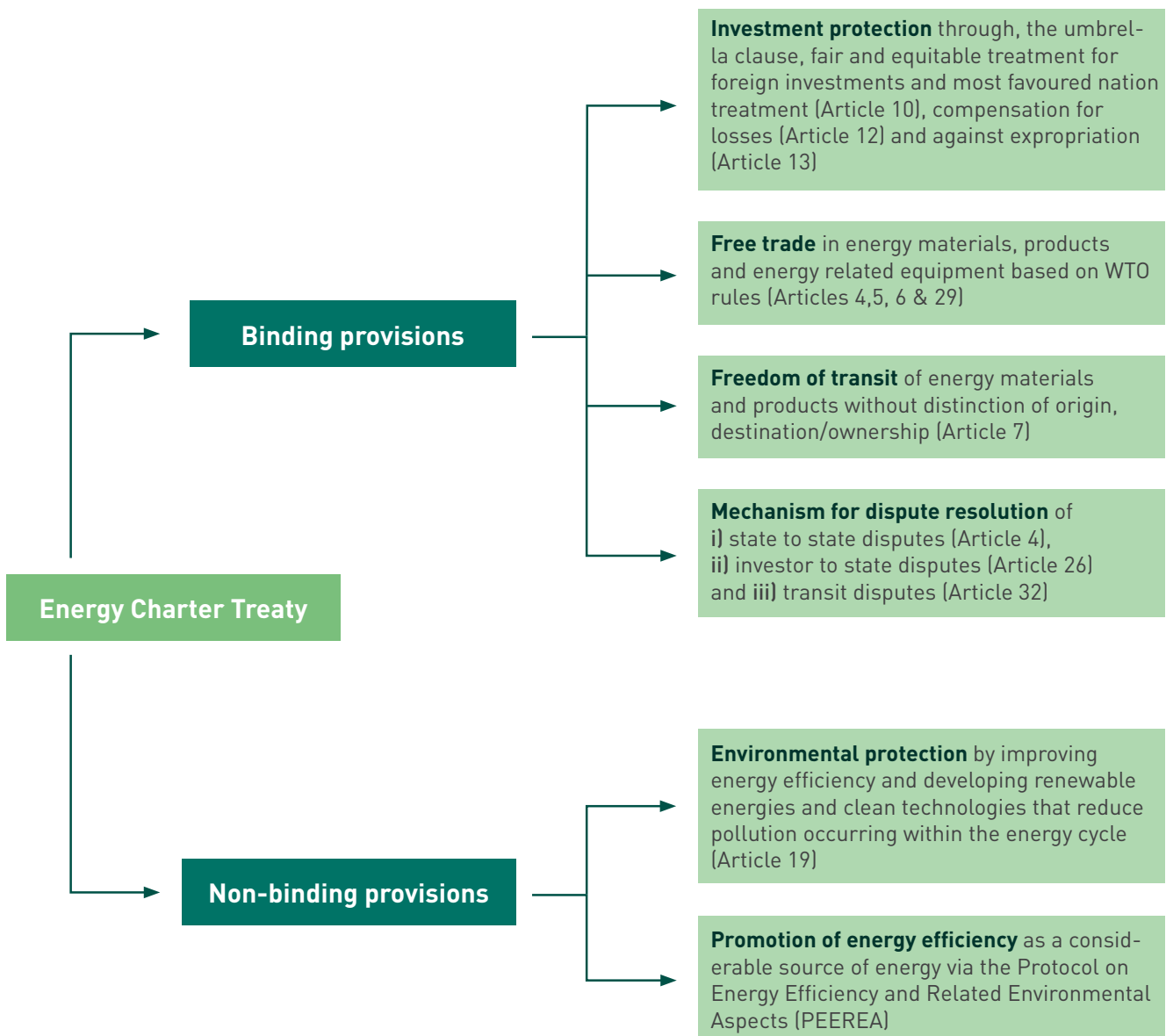
(2) Nothing in such terms of the other agreement shall be construed to derogate from any provision of Part III or Part V of this Treaty or from any right to dispute resolution with respect thereto under this Treaty.

Where any such provision is more favourable to the investor or investment

ECT Article 16 on relation to other agreements

Arbitration tribunals are composed of appointed paid private lawyers by the investor and the host state. Arbitrators can order remedies, usually in the form of monetary awards, to investors if they find that states have breached the obligations of the Treaty. Host states are legally bound to accept ISDS proceedings despite their lack of transparency and the absence of mechanisms to consider the rights and interests of other parties impacted by the investment. ECT signatories can withdraw from the Treaty to protect public interests, overcome ISDS threat to better regulation and limit ISDS damages on public budget. However, investment protection remains in effect for a further twenty years after effective withdrawal from the ECT which takes place one year after the notification of the withdrawal.

Overall, ECT obligations are on the host state only and not on the investor and ECT privileges and over-protects the economic rights/interests of foreign investors over the societal and economic interests of the host state and national stakeholders who have no rights under the system. The binding provisions of the ECT combined with ISDS mechanisms makes the Treaty the most favourable one to investors. De facto, investors prefer the enforcement of remedies ordered by private arbitrators especially with the emergence of third-party funding in international arbitration.



GEOPOLITICAL IMPACT OF THE ECT

The ECT aimed at introducing former socialist countries to the global trading system and to establishing a liberalised pan-European energy market by encouraging the flow of western investments in the energy sector in Eastern European and Central-Asian countries through binding investment protection provisions. Since its inception in 1994, the ECT has been signed by 53 countries and the European Union/Euratom. Among the early signatories of the treaty, four countries including Australia, Belarus, Norway and the Russian Federation have never ratified the Treaty.

After the entry into force of the Treaty in 1998, only ten new countries, including two of the EU (Poland and Malta), have signed the Treaty. The last wave of ECT signatories includes two Arab States, Jordan and Yemen. Nevertheless, these two countries are not among the major players in the energy field in the Middle East. The United States and Canada, who were involved in the three years negotiations of the Treaty in the nineties, have never signed it. Similarly, none of the emerging economies and major players in the global energy landscape are signatories of the Treaty. Importantly, the Russian Federation has withdrawn from the provisional application of the Treaty in 2009. Similarly, Italy withdrew from the Treaty in 2015. Both countries have been subject to disputes with investors on the basis of the ECT after their withdrawal. However, given that the European Union is signatory of the Treaty, it is likely that Italy's withdrawal from the Treaty is not as effective as it would have been for ECT signatories who are not members of the European Union.

Most of Eastern European countries are either Members of the European Union to which EU law and internal market regulations apply or signatories of the Energy Community Treaty which aims at creating an integrated and sustainable pan-European energy market based on EU energy acquis. Investments in the energy sector in these countries are, therefore, subject to EU law. Similarly, climate emergency and the carbon neutrality objective are shifting the debate on energy security from securing the access to fossil fuels to phasing-out hydrocarbons. From the global trade perspective, only six ECT signatories (Azerbaijan, Belarus, Bosnia and Herzegovina, Kosovo, Uzbekistan and Turkmenistan) are not yet WTO members. However, these six countries have long standing partnerships with the EU either through the Energy Community Treaty or the Eastern and Central-Asian partnerships.

ECT signatories and observers developed the International Energy Charter political declaration for the reasons and with the objectives described below:

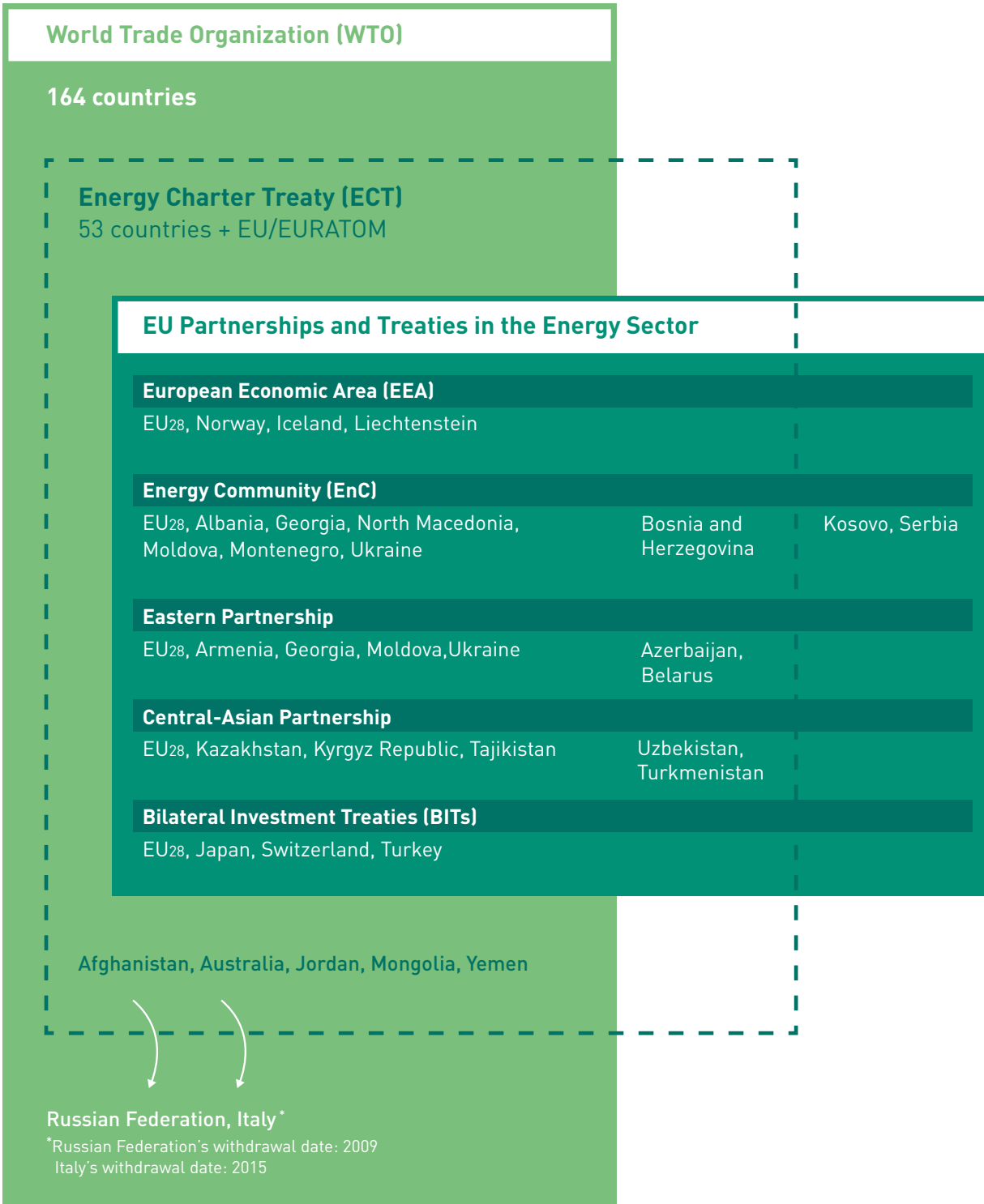
“Desirous to better reflect the new realities of the energy sector, especially the growing weight from developing countries, including emerging economies, and to serve the interests of the existing and potential participants of the Energy Charter constituency;

Recalling the objectives of the International Energy Charter:

- to support the Charter's policy of consolidation, expansion and outreach with the aim to facilitate the expansion of the geographical scope of the Energy Charter Treaty and process;
- to engage in a structured dialogue with non-signatories of the European Energy Charter in order to promote the principles of the Charter and its framework for cooperation on the global scale;
- to modernize the European Energy Charter as the basic political declaration of the Energy Charter process;
- to support active observership in the Energy Charter Conference, aiming at close political cooperation and early accession of observer countries to the Energy Charter Treaty;

Whereas the international Energy Charter is a declaration of political intention aiming at strengthening the energy cooperation between the signatories and does not bear any legally binding obligation “

International Energy Charter



ECT conflicts with the EU law/acquis and the WTO regime in terms of substance (energy materials and services covered) and dispute resolution in the energy sector. On one hand, the EU law refers to the EU Court of Justice/national courts for the resolution of disputes and WTO only permits state-to-state disputes. On the other hand, the ECT allows foreign investors (companies, holdings, financial institutions and individuals) to allege treaty violations by suing states through ad hoc arbitration tribunals composed of private lawyers.

Overall, the ECT “reason d’être” disappeared during its more than two decades of application. New treaties and partnerships, to which more than 90% of ECT signatories have adhered, have lowered, if not totally cancelled, the potential geopolitical impact of the ECT as foreseen by its initiators. The relevance of the Treaty for the global energy and trade governance in a warming planet, which needs to be fossil-fuel free, is today questionable. This is particularly true given the threat of legal proceedings, their costs for public budget and their “regulatory chill” effect on policies and measures which protect public interests.

INVESTMENTS PROTECTED BY THE ENERGY CHARTER TREATY

Contrary to the myth, the ECT is neither fuel nor technology neutral as it does not cover all economic activities in the energy sector. Investments protected by the ECT relate to economic activities of a detailed list of energy materials and products which includes nuclear energy, coal, natural gas, petroleum and petroleum products, electrical energy, and other energy sources such as fuel wood and wood charcoal. Renewable energy sources used for electricity production are also protected while distributed heat to multiple premises is explicitly excluded from ECT protection.

ECT provisions protect economic activities on the supply side only. These activities include those related to the exploration, extraction, refining, production, storage, land transport, transmission, distribution, trade, marketing or sale of energy materials and products. Economic activities and investments in measures to reduce energy demand and energy services essential for the delivery of a decarbonised energy systems are neither protected by the ECT nor are energy savings included in ECT list of energy materials and products.

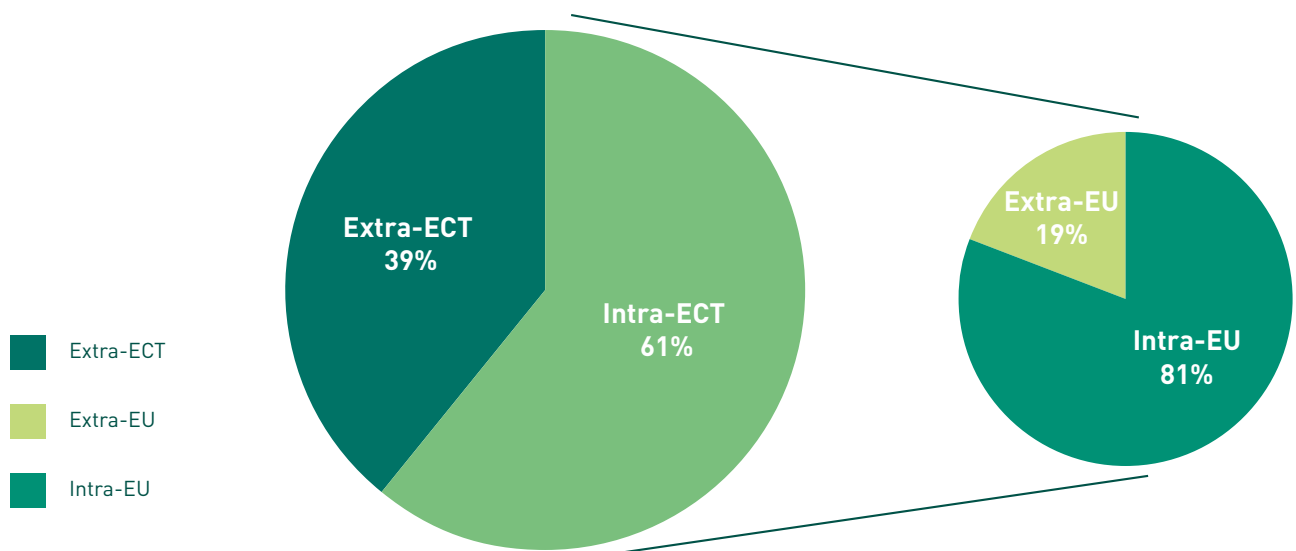
Average annual foreign direct investment (FDI) in the energy sector, which fall under ECT provisions, in ECT countries is estimated at €50 billion¹, out of which 61% are intra-ECT investments directly protected by ECT provisions. Within the intra-ECT investments, 81% are intra-EU investments which also fall under the EU law. Extra-ECT FDIs are indirectly protected as investors can adopt a nationality of an ECT signatory for convenience.

Economic activity in the energy sector means an economic activity concerning the exploration, extraction, refining, production, storage, land transport, transmission, distribution, trade, marketing, or sale of Energy Materials and Products except... those concerning the distribution of heat to multiple premises.

Energy Materials and Products means the items included in Annexes EM1 (Nuclear Energy, Coal, Natural gas, Petroleum Products, Electrical Energy)

ECT Article 1, point 5 and 4 on definitions and annex EM1

Share of FDIs in ECT signatories



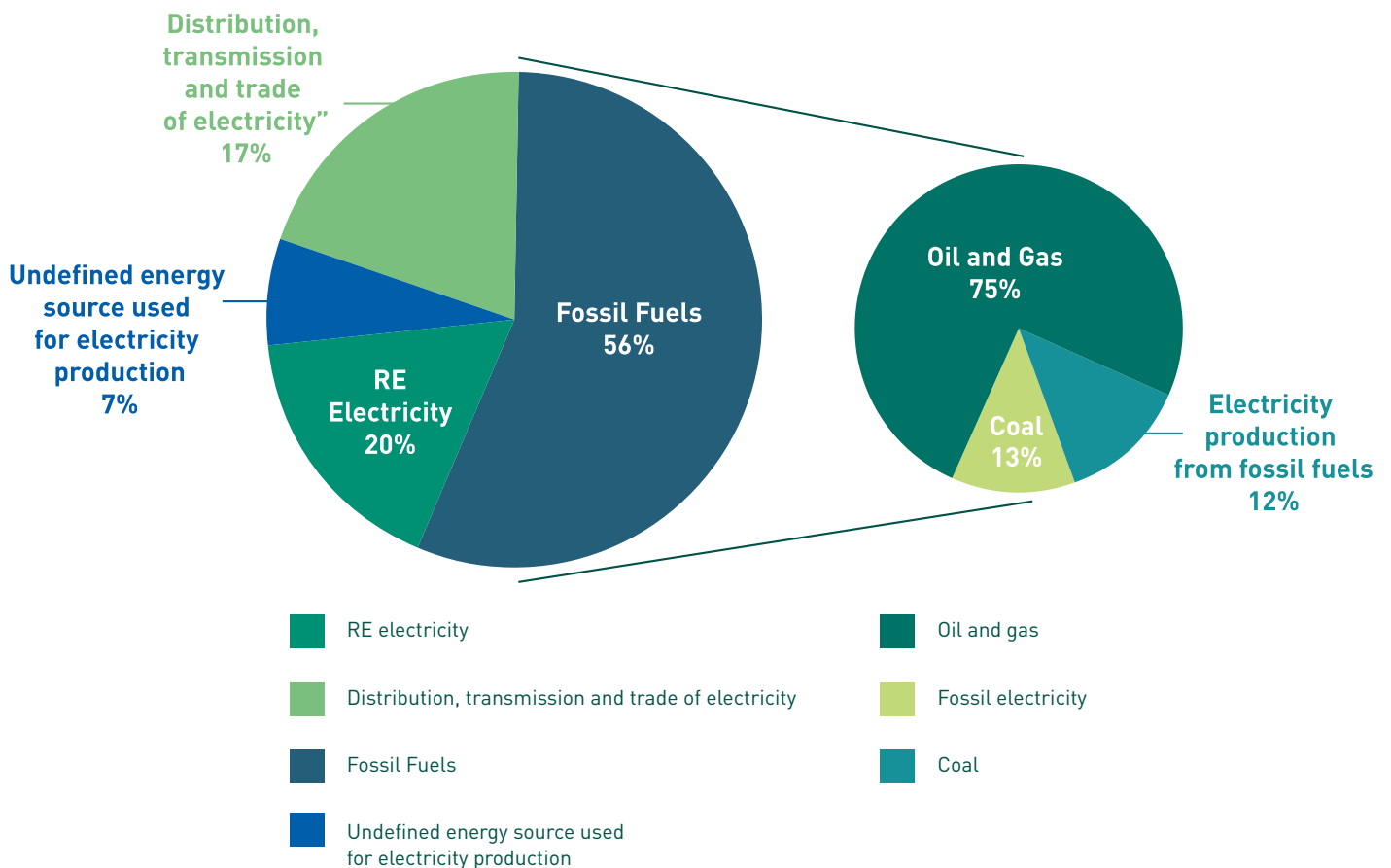
¹ Estimated using ORBIS Cross-border investment database

COMMITTED CO₂ EMISSIONS PROTECTED BY THE ECT

Estimating committed CO₂ emissions protected by the ECT requires first assessing investments protected by the ECT per fuel. Over the period, 2013-2018, 56% of the protected investments under the ECT regime are investments in fossil fuels (oil, gas and coal combined), out of which three quarters are FDIs in oil and gas (extraction and support activities to extraction and distribution). The shares of FDIs in coal and in electricity production from fossil fuels are almost equal (13% out of total investments in fossil fuels). The share of ECT protected investments in renewables represented only 20% out of total FDIs followed by FDIs in electricity transmission, distribution and trade over the same period.

Committed CO₂ emissions protected by the ECT are estimated based on total fossil fuels investments in ECT signatories since the entry into force of the treaty in 1998. CO₂ emissions are calculated for the targeted opportunities to unlock future CO₂ emissions if alternative technologies are affordable². Cumulative CO₂ emissions protected by the ECT, over the period 1998-2018, are estimated at 57 Gt CO₂ out of which 61% are committed emissions from Intra-ECT investments in fossil fuels. This is almost double of the remaining³ EU carbon budget for the period 2018- 2050.

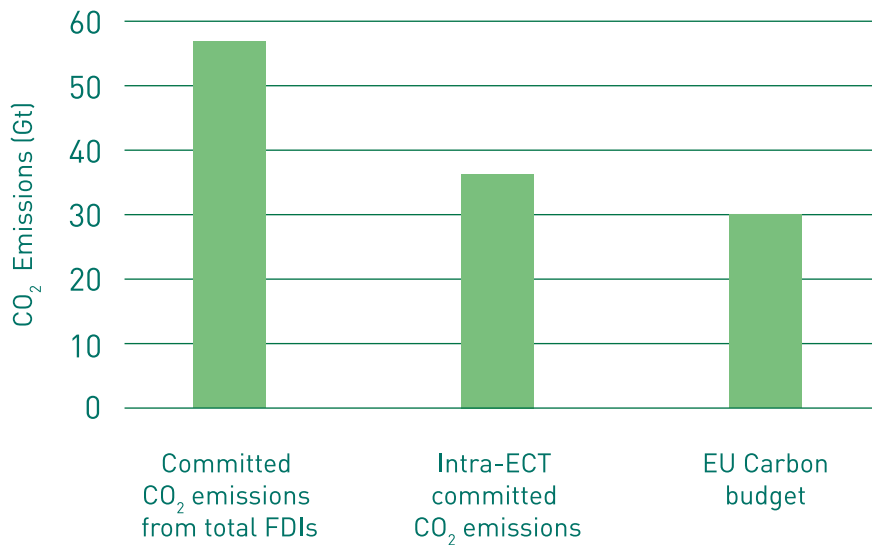
Share of FDIs per fuel



² The calculation methodology is based on the one described by Dan Tong in the article entitled "Committed emissions from existing energy infrastructure jeopardize the 1.5°C climate target (Nature, July 2019)". The assessment of the affordability of alternative technologies is based on Europe given its share of investment protected by ECT and the affordability level of alternative technologies due to EU energy and climate policies.

³ Remaining EU carbon budget are maximum cumulative GHG emissions allocated to the EU to avoid the overshoot of the 1.5°C target. The remaining EU carbon budget has been estimated using the methodology developed by Tim Jackson in his working paper entitled "Zero carbon sooner" (CUSP, July 2019).

ECT protected CO₂ emissions (1998-2018) compared to EU carbon budget (2018-2050)



DISPUTE SETTLEMENT REGIMES UNDER THE ENERGY CHARTER TREATY

Dispute settlement regimes under the ECT are unbalanced. For state-to-state disputes, the ECT requires its contracting parties to use diplomatic channels for a reasonable period of time before taking the dispute for arbitration. In the case of investor-state disputes, both parties are required to attempt amicable settlement. If the dispute is not amicably settled, the investor alone can decide to submit the dispute to a national tribunal or to seek international arbitration. Obligations subject to international arbitration relate mainly to the protection and treatment of investments, compensation and expropriation. Obligations related to competition, transit and the environment are not subject to international arbitration.

ECT is the most popular instrument used by investors to challenge governments by means of investment arbitration. The asymmetry of treatment between the foreign investor and the host country explains the attractiveness of arbitration procedures for foreign investors. On one hand, the foreign investor is the one

who chooses the dispute mechanism to be followed, and the contracting party, whose agreement in this respect is not required as it is considered given. By becoming ECT signatory, the host state is legally bound to accept investor's choice. On the other hand, if a foreign investor fails in meeting its obligations, the host state must rely either on the national law, or on the terms of the investor-state contract to achieve a settlement but cannot rely on the ECT. As of today, there are 124 known arbitration cases under the ECT regime out of which 82 are intra-EU disputes mainly related to changes in renewable energy subsidies schemes.

The lack of consistency, coherence and predictability of arbitral tribunals raise concerns about the 69 pending ECT cases, and the potential upcoming ones, as this international investment 'regime', unlike the WTO system, has no appellate mechanism to provide guidance on interpretation. Spain and Italy have the highest number of pending ISDS cases with 37 and 9 respectively. Given that the ECT regime continues to apply 20 years

after the effective withdrawal of a country party, investors sued Italy after its effective withdrawal from the ECT regime.

ECT provisions related to arbitration procedures is one of the areas of conflicts with the EU law. The European Commission has been trying to internalise conflict resolution of intra-EU ECT disputes in the Court of Justice of the European Union (CJEU). There is a disagreement as to whether such disputes are in breach of the Achmea⁴ ruling of the CJEU. However, at this stage, it is unclear if the CJEU ruling in the case of Achmea could succeed in making ECT claims null and void in international arbitration and to proceed under European laws and national or European courts. In fact, under the ECT regime, contracting parties cannot derogate from any provisions of the Treaty, including the provisions on

dispute resolution, that is most favourable to investors and investment. An investment tribunal constituted under the ECT would therefore apply the ECT rules.

Another area of conflict with EU law relates to the expected legal changes which will inevitably occur to ensure Europe will meet its carbon neutrality target. One of the Italian pending disputes relates to the decision of the national court to not renew the oil exploration license in the South of Italy due to its environmental impacts. Similarly, the French law on phasing-out exploration licenses was watered down due to the threat by a Canadian company under the ECT regime.

(1) Disputes between a Contracting Party and an Investor of another Contracting Party relating to an investment of the latter in the area of the former, which concern an alleged breach or an obligation of the former under Part III (Investment Promotion and Protection) shall, if possible be settled amicably.

(2) If such disputes cannot be settled according to the provisions of paragraph (1) within a period of three months from the date on which either party to the dispute requested amicable settlement, the investor party to the dispute may choose to submit it for resolution:

- a. To the courts or administrative tribunals of the Contracting party party to the dispute;**
- b. In accordance with any applicable previously agreed dispute settlement procedure;**
- or**
- c. In accordance with the following paragraphs of this article.**

(3) Subject only to paragraphs (b) and (c), each Contracting Party hereby gives its unconditional consent to the submission of a dispute to international arbitration or conciliation in accordance with the provisions of this article.

ECT Article 26 on Settlement of Disputes between an investor and a Contracting Party

⁴ In the Achmea case, the CJEU ruled that the arbitration clause contained in the Netherlands-Slovak Republic Bilateral Investment Treaty (BIT) has an adverse effect on the autonomy of the EU law and is therefore incompatible with EU law.

GOVERNANCE OF THE ECT

Governance of the ECT consists of the Energy Charter Conference and its subsidiary bodies. The former is the governing board of the Charter. Accordingly, ECT signatories which are considered Contracting Parties take decisions at the annual meeting of the Conference. The latter is composed of several groups including the Strategy Group, the Advisory Legal Panel, the Budget Committee and the Implementation Group. The aim of these groups is to support the Conference decisions in specific areas of expertise.

The Conference is supported by a Secretariat which deals with daily business and facilitates discussions at different meetings. An Industry Advisory Panel (IAP) and a Legal Advisory Committee (LAC) composed of experts from the energy industry and legal affairs have been established to provide advice to the conference in their respective areas of expertise. However, energy and law experts from civil society are not members of any of the Conference advisory groups.

Since 2014, the Chairmanship of the Conference changes on a yearly basis. Countries who have volunteered to chair the Conference include Kazakhstan in 2014, Georgia in 2015, Japan in 2016, Turkmenistan in 2017 and Romania in 2018. Albania is the 2019 Chair,

while Azerbaijan will be the Chair in 2020, Armenia in 2021 and Mongolia in 2022. Unfortunately, ECT signatories leading in global climate and energy discussions and with carbon neutrality target did not chair the Conference recently nor they did announce their interests in the Chairmanship of the Conference for the upcoming years. The only exception is Japan who chaired the ECT conference in 2016 and the G20 in 2018. However, Japan is among the advanced economies and ECT signatories without a carbon neutrality target. The lack of climate ambition of Conference Chairmanships may explain the lack of climate leadership of the Conference.

Status of carbon neutrality targets in ECT signatories (source: Climate Home News)

Norway	2030	In law
Sweden	2045	
United Kingdom	2050	
France	2050	
Finland	2035	In policy document
Iceland	2040	
Denmark	2050	
Portugal	2050	
EU28	2050	
Germany	2050	
Spain	2050	Announced
The Netherlands	2050	
Ireland	2050	
Switzerland	2050	

Afghanistan

Albania

Armenia

Australia

Azerbaijan

Belarus

Bosnia & Herzegovina

Georgia

Japan

Jordan

Kazakhstan

Kyrgyzstan

Liechtenstein

Moldova

Mongolia

Montenegro

North Macedonia

Tajikistan

Turkey

Turkmenistan

Ukraine

Uzbekistan

Yemen

Unknown

CHALLENGES OF REFORMING THE ENERGY CHARTER TREATY

After two decades of the ECT regime, it became clear that achieving societal goals such as climate and social justice will be challenging for signatory countries if the Treaty regime, as it was designed in the 1990's, continues to apply. One option would have been to reform the treaty towards a model that is not primarily about investment protection, but instead sets out a framework to ensure a low-carbon transition through investment and to support host countries and their citizens in this transition. This is particularly needed given that the current regime's centrepiece is ISDS to ensure the enforcement of rules that are not designed to promote climate and societal goals and do not set out any obligations for companies.

Unfortunately, reforming the Treaty to ensure it would contribute to meeting signatories' climate targets and UN sustainable development goals (SDGs) is unlikely to happen as the list of items agreed for the discussion on modernisation options does not include the phase-out of fossil fuels and the adoption of any amendment to the Treaty would require unanimity vote of the contracting parties present and voting at the ECT governing board meeting, which occurs just before the end of the calendar year.

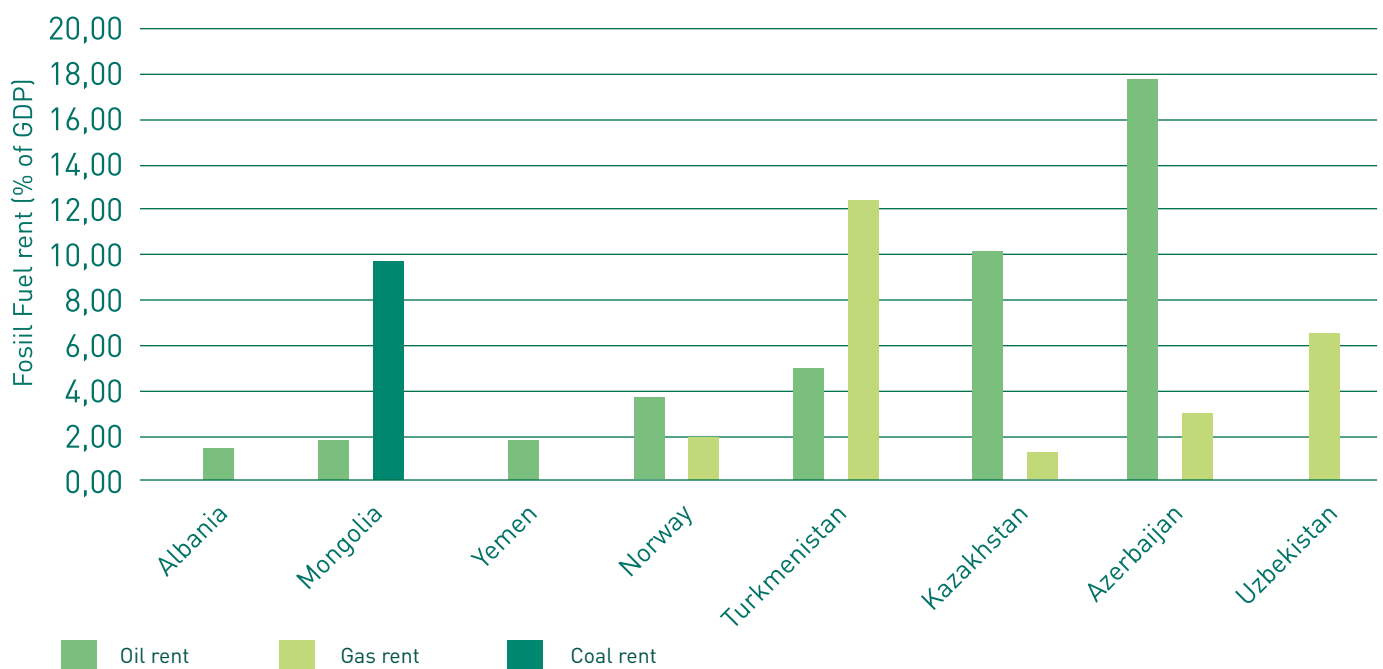
Ending investment protection to fossil fuels would be a considerable threat to investors in fossil fuels who will use various means to influence the vote of host states with fossil fuels reserves as well as those hosting fossil fuel corporations. It is more likely that these countries will not vote for ending investment protection to fossil fuels as this would lower their revenues. This is particularly true for countries with fossil fuels revenues above 1% of their Gross Domestic Product (GDP).

Unanimity of the Contracting Parties present and voting at the meeting of the Charter Conference where such matters fall to be decided shall be required for decisions by the Charter Conference to:

- (a) Adopt amendments to this Treaty
- (b)
- (c)
- (d) Approve modifications to Annexes EM
- (e) Approve technical changes to the annexes of this Treaty

ECT Article 36 on Voting rules

ECT signatories with fossil fuels rent above 1% of GDP in 2017 (Source World Bank)



ECT MODERNISATION SCENARIOS

In 2018, the Energy Charter Conference approved a list of topics for discussion on the modernisation of the ECT, after internal discussions and external consultations with industry. However, civil society representatives were not consulted. Topics included for ECT modernisation include a narrow set of investment protection issues such as definitions to traditional investment protection standards and third-party funding. Neither, the most contentious issue, ISDS, is explicitly mentioned nor is the phase-out of investment protection to fossil fuels required to ensure the carbon neutrality target will be met by ECT signatories. Similarly, the modernisation of the ECT does not include the modernisation of its governance.

The 2019 ECT Conference plans to announce the start of negotiations on the potential policy options. ECT signatories were invited to submit their policy options for each of the identified item for modernisation. Based on the information publicly available, policy options proposed by ECT signatories have been grouped in three different scenarios: no-ECT changes, Trade and 1.5°C target scenario.

ECT modernisation scenarios	No-ECT change scenario	Trade scenario	1.5°C target scenario
Right to regulate	No	Yes*	Yes
Phase-out of fossil fuels	No	No	Yes
End of ISDS	No	No	Yes
Cumulative emissions protected by ECT by 2050 (Gt CO ₂)	148	98	57

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

Cumulative CO₂ emissions, which would be protected by the ECT under each of the three scenarios by 2050, are estimated by projecting FDIs in fossil fuels based on those for the period 2013-2018 and climate and energy policies in signatory countries. There is almost a factor three in the cumulative emissions that would be protected by the ECT between the no-ECT changes scenario and the 1.5°C target scenario. Importantly, the Trade scenario, which includes the modernisation options proposed by countries who have either announced or already put in law their carbon neutrality target, is also a scenario which will increase the carbon lock-in effect due to the ECT regime.

ECT signatories have the opportunity to limit cumulative CO₂ emissions protected by the ECT to those committed since the entry into force of the Treaty in 1998 until today by ending at the 2019 Conference, protection of fossil fuels FDIs. This would make the Conference a player in the global climate governance. Unfortunately, given the gap in climate ambition between ECT signatories, the role of fossil fuels for some economies and the voting rules under the ECT regime, the 1.5°C target scenario is unlikely to be the selected one. For consistency, countries with carbon neutrality commitment should, therefore, withdraw collectively from the ECT.

Potential ECT protected cumulative CO₂ emissions per modernisation scenario compared to EU carbon budget



**Comments and questions are welcome
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