

Q&A on the Climate Crisis and Investor-State Dispute Settlement (ISDS)

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Introduction

Investor-State Dispute Settlement provisions (ISDS) allow foreign investors, including fossil fuel companies and major polluters, to file international arbitration claims against governments when public policies or legislation affect their investments and profits. ISDS provisions are found in many treaties and trade agreements, and in contracts between investors and the governments of countries in which they are investing. Such provisions are increasingly being used to thwart action on climate change.

Fossil fuel companies are among those most frequently using ISDS claims to challenge governmental efforts to address climate change. According to one calculation, as of July 2025, there had been at least 349 investor-state disputes related to fossil fuel projects, with fossil fuel corporations receiving upwards of USD 82.8 billion through ISDS awards. A study released on November 12 found the current figure to be USD 86 billion. Given the secrecy of the system, in which the claim and award amount is not made public in many cases, these figures are likely to be conservative.

The use of ISDS claims to challenge or to penalize climate action puts states in a difficult situation in which fulfilling their legal obligation to take climate action could lead to devastating financial penalties. With investors often demanding enormous sums for speculative "lost future profits" and a process that is expensive, lacks transparency, limits public participation, and allows arbitrators to treat as irrelevant a state's reasons for taking action, the threat of ISDS claims has had a significant chilling effect on climate action. Reform of the ISDS system and the underlying investment treaties is thus critical.

This Q&A explains how ISDS and similar treaty clauses work, why they are particularly problematic in the context of challenges to governmental action to address climate change, and what might be done to address the issues they raise. It also explains how the July 2025 Advisory Opinion on climate change by the International Court of Justice (ICJ), reinforced by the May 2026 United Nations General Assembly (UNGA) Resolution affirming that decision, should fundamentally change the legal landscape for ISDS claims.

What is ISDS?

ISDS provisions give foreign investors the right to seek compensation or resolve disputes with the government of a country in which they have invested through international arbitration. Such provisions have been included in many investment treaties between national governments, in which each government commits to provide specified protections and benefits to investors from the other country or countries that are party to the agreement. They have also been included in free trade agreements that contain investment provisions, and in investor-state contracts.

Over 3,300 bilateral (between two countries) or multilateral (between multiple countries) investment treaties and free trade agreements with investment provisions have been entered into to date. Many of these agreements were put in place during periods when newly independent countries were seeking foreign investment to drive economic development, while multinational corporations and other foreign investors looking to invest in those countries wanted protections against expropriation or discriminatory treatment.

These treaties provide foreign investors with broad legal protections, including:

- entitlement to compensation in the event of direct or indirect expropriation;
- guarantees of “fair and equitable treatment” and “full protection and security;” and
- protections against “discrimination.”

Proponents of these arrangements argue that they depoliticize disputes between investors and states and promote investment flows that enhance economic development. However, they are frequently being interpreted and used in ways that give investor profits priority over the protection of the environment and the fight against climate change.

What’s the Problem With ISDS?

The protections granted to investors in investment treaties are often framed in vague terms, giving extensive discretion to courts and arbitrators for their

interpretation and application. As a result, investor protections in investment treaties have often been interpreted extremely broadly and in favor of the investor and have resulted in extremely large damage awards.

The protection against "indirect expropriation," which allows the investor to claim that changes in tax or other policies in the host state have fundamentally changed the investment environment and reduced the investor's profitability beyond its "legitimate" expectations, is particularly problematic. In all but the most recent treaties, that protection contains no exception for changes in laws, regulations, or policies intended to protect the environment or address climate change—both of which have become of much greater concern since the treaties were negotiated. As a result, investors have claimed that measures taken for those purposes have led to "indirect expropriation" and that they are therefore entitled to compensation for profits they arguably would have made had the changes not been made.

Regulatory, legal, and policy changes often affect businesses and are an accepted part of investment calculations. Yet in the context of treaty-based ISDS provisions, those changes can become the basis for legal claims. Moreover, the protections granted in such treaties are largely one-sided: most do not provide the host country with protection against, for example, environmental damage or the costs of externalities by the investor.

As a result, as discussed below, there is a growing international recognition—including in recent legal advisory opinions and UN special procedure communications—that many of these agreements and the ISDS mechanisms they include are fundamentally at odds with the urgent need for rights-respecting climate action. The government of Nigeria recently called for reform of the ISDS system, including the integration of public-interest considerations such as climate action, environmental protection, human rights obligations, community welfare and sustainable development, while other countries have called for exit from the system.

Example: The Energy Charter Treaty

A prime example of the risks posed by broadly interpreted ISDS provisions is the Energy Charter Treaty (ECT), a controversial 1994 multilateral treaty designed to protect foreign investments in energy.

The ECT includes comprehensive ISDS provisions allowing foreign investors to claim compensation through arbitration for "unfair" losses due to government regulation and has been the basis for numerous ISDS claims by fossil fuel companies. For example, in 2017, Rockhopper Explorations, an oil and gas company based in the United Kingdom (UK), sued the Italian government for damages after the government decided in 2015 to ban oil drilling within 12 miles of its shoreline to protect the environment and address public concerns—the kind of decision routinely made by governments around the world. Rockhopper, which had invested USD 29 million in the Ombrina Mare oil rig, for which it had hoped to obtain a production license, sought damages of up to USD 350 million dollars, seeking compensation not only for the money it had already invested, but also for what it asserted are the profits it would have made over the lifetime of the project. Rockhopper was able to file the claim even though Italy had withdrawn from the ECT in 2015, because the treaty contains a sunset provision legally binding the withdrawing country to the treaty for another 20 years. As a result, investors such as Rockhopper will be able to file claims against Italy under the treaty until 2035.

In 2022, the arbitration panel hearing the claim ordered the Italian government to pay Rockhopper more than USD 190,000,000 in damages—far exceeding the company's sunk costs. The decision was annulled in May 2025 on the grounds that the arbitrator chosen by Rockhopper had not disclosed that he had previously been criminally prosecuted in Italy in relation to his legal work. It is unclear whether Rockhopper will seek a new arbitration proceeding.

Other cases under the ECT have targeted coal restrictions and phase-outs in the UK, Germany, and the Netherlands, among others (see below). At least ten other individual countries, in addition to Italy, have now withdrawn from the ECT. However, as noted above, they all remain bound to the treaty for 20 years after withdrawal, so are still subject to claims for actions to protect the climate and reduce fossil fuel use.

In 2024, after several years of efforts to reform the treaty to ensure that it did not prevent countries from complying with their obligations under the Paris Agreement, the European Union announced its withdrawal from the treaty.

How Has the Arbitration Process Exacerbated the Problem?

Most ISDS provisions in investment treaties, free trade agreements, and government-investor contracts require that disputes be resolved by international arbitration rather than the national courts of one party's country.

International arbitration claims against governments are often brought at the International Centre for the Settlement of Investment Disputes (ICSID), which is headquartered in Washington, D.C. and is part of the World Bank. Other fora include the London Court of International Arbitration (LCIA), the International Chamber of Commerce (ICC), the Hong Kong International Arbitration Centre (HKIAC), and the UN Commission on International Trade Law (UNCITRAL). Each of these bodies operates under slightly different rules, and the treaty or contract generally specifies the body that will hear a particular claim.

Instead of being heard by a nationally appointed or elected judge, claims in arbitration are generally heard by either one or three arbitrators selected in accordance with the rules of the relevant arbitral body and/or in accordance with the parties' agreement. Many of those who work as arbitrators either do or did work for law firms that represent investors, which can raise concerns of pro-investor bias and conflicts of interest.

Unlike court proceedings, ISDS claims and documents are often kept confidential, hearings are often conducted behind closed doors, and both awards and negotiated settlements can be kept secret. Where the dispute involves an alleged conflict between the host government's laws and policies designed to protect the environment, climate, public health, or other important public policy issues, ISDS mechanisms give rise to several serious problems.

Limits on What is Considered by the Arbitrators

In many instances, ISDS arbitration panels have considered their sole focus to be the foreign investor's claim under the relevant investment treaty or contract and have considered irrelevant issues such as whether or not a challenged governmental action (or inaction) is consistent with domestic law, required for the state to fulfill its international human rights or environmental obligations, or was made in response to public opinion or changed circumstances.

The result is that relevant contextual factors, such as a government's rationale for adopting measures related to climate action, human rights, or environmental protection, are often disregarded. For example, arbitration tribunals have dismissed arguments by Colombia, Costa Rica, Ecuador, and El Salvador that their refusal to permit mines to open or continue operating was necessary to fulfil their obligation to safeguard the right to a healthy environment. Given the tension between a government's obligations to address climate change and the interests of investors, the failure to consider those obligations has led to outsize victories for those opposing the shift away from fossil fuels, among others.

Recently, some tribunals have taken into consideration a government's environmental motivations when considering investor claims. In July 2026, an ICSID tribunal rejected claims by two investors that Slovenia's decision to require environmental impact assessments for fracking operations, and a subsequent decision to ban fracking at the Petisovci oil and gas fields, violated its rights under the Energy Charter Treaty. United States (U.S.) based oil and gas company Ascent Resources and its subsidiary Ascent Slovenia had sought payment of EUR 598.7 million (USD 684 million) from Slovenia. The arbitral tribunal found that the decision by the Slovenia Environment Ministry was neither discriminatory nor arbitrary, and ordered the claimants to pay Slovenia three million euros in costs.

Lack of Community Participation

ISDS arbitrations largely exclude the participation of local communities, even those who have suffered or would suffer negative impacts from the project in dispute, or communities that supported or encouraged the government action at issue. Excluding stakeholder communities is fundamentally undemocratic, as the concerns of local communities are often the reason for governmental decisions on projects. While some tribunals have allowed written submissions by "non-parties" such as local communities or NGOs, the tribunals usually have complete discretion whether to accept such submissions and, even if they are accepted, what weight, if any, to give those filings.

Even if their filings are accepted, the "non-parties" generally have no access to other filings, and no ability to participate in or even observe the oral proceedings. Indeed, local communities may not even be informed about what has been decided in

arbitration, despite the impact they may have on their lives and livelihoods, or the environmental and rights costs that such decisions can entail.

Cost of Participation and Outsize Claims

The cost of participation in international arbitration is often significant and beyond the capacity of small, less wealthy nations. Legal fees alone can run into the millions of dollars—a heavy burden for lower-income countries. The mere threat of arbitration may cause some countries to give in to foreign investor demands, even if they are entirely unjustified, to avoid the cost of arbitration.

The financial imbalance is exacerbated by the fact that third parties, such as litigation finance firms, are often willing to underwrite the cost of the arbitration for the investor in exchange for a financial interest in any award. The involvement of third-party funders not only reduces the risk for investors and therefore encourages the filing of ISDS claims but may also impact decisions on whether or not to settle.

Moreover, the amounts sought in these claims are often enormous—sometimes many multiples of the host country's GDP. UNCTAD reports that at least 143 ISDS claims have been filed that seek USD 1 billion or more in damages. As of 2023, countries in the Americas had either "been ordered or agreed to pay investors USD 29.2 billion in awards and settlements."

Because at the outset of an ISDS process it will often be difficult for a state to predict how the tribunal will rule, and because decisions are often inconsistent, a country faced with an enormous claim will justifiably be very wary of the arbitration process. Particularly if the arbitration panel refuses to hear counterclaims, the foreign investor will have nothing at stake other than the cost of its lawyers and fees (which may be underwritten by a third party), while the host country will have those expenses plus the risk of massive liability. This risk will be exacerbated by the fact that there is generally no appeal from a tribunal's decision, even when a party believes there have been serious factual or legal errors either in the determination of liability or the calculation of damages.

How Have ISDS Claims Been Used to Stymie Climate and Environmental Action?

According to David Boyd, former UN Special Rapporteur on Human Rights and the Environment, "state measures vulnerable to the threat of ISDS claims include actions to enact, strengthen and implement climate and environmental laws, regulations, standards and policies. For example, refusing to grant oil and gas exploration permits, the phasing out of coal-fired power plants, denying permits for large mines, introducing fracking bans and strengthening laws to protect water supplies have all resulted in arbitration claims."

As noted above, fossil fuel companies are among those most frequently using ISDS claims to challenge climate action that they believe threatens their business. Below are a few public examples of recent ISDS cases based on governmental actions regarding fossil fuel projects.

- In 2023, U.S. company Ruby River Capital filed an initial claim for more than USD 20 billion against Canada under the North American Free Trade Agreement (NAFTA) legacy provisions of the US-Mexico Canada Trade Agreement (USMCA). The dispute arose from the decisions of the governments of Canada and Quebec not to permit the construction and operation of a liquified natural gas plant after environmental assessments concluded there were major environmental and climate change concerns that could not be mitigated. The arbitration process is still ongoing.

- In August 2025, a Singaporean investor in a Cumbrian coal mine filed an arbitration claim for compensation after a court in the UK quashed approval for the mine on the grounds that the government had not required an assessment of the emissions from the use of the coal to be produced by the mine before issuing its approval. The investors are relying on an ISDS provision in a 1975 bilateral investment treaty between the UK and Singapore, claiming that they were denied fair and equitable treatment, suffered indirect expropriation, and faced discrimination. The dispute is ongoing.

- In Germany, a Swiss public company, Azienda Elettrica Ticinese (AET), is demanding compensation in an international arbitration tribunal under the Energy Charter Treaty for Germany's accelerated coal phase-out plans. The company holds shares in a German coal-fired power plant that it argues will cease operations in 2031 due to the phase-out. AET is demanding compensation for its anticipated future profits from the power plant until 2053.

- In August 2026, ExxonMobil filed an ISDS claim against the European Commission under the Energy Charter Treaty, challenging mandatory carbon storage obligations outlined in the EU's Net Zero Industry Act. This law, adopted in May 2024, requires the construction of 50 million metric tons of annual CO_2 storage capacity by 2030. Despite having advocated for carbon capture and storage for years, ExxonMobil has challenged the law, in part because it requires oil and gas producers to pay for and build the capacity themselves, rather than relying on public subsidies.

Arbitration clauses in contracts between foreign investors and host states are also being used to seek compensation for alleged losses due to government action aimed at protection of the environment, the climate, and the health of its citizens. For example, a subsidiary of Australian company Energy Transition Minerals Ltd (ETM) filed an arbitration claim against the government of Greenland seeking approximately USD 11.5 billion in damages and interest—more than ten times Greenland's annual budget. ETM claimed it was entitled to damages stemming from Greenland's 2021 decision to ban any form of mining that releases radioactivity into the environment, a law designed to protect public health and fragile ecosystems from potential uranium and thorium contamination. The ban effectively prevented Greenland Minerals A/S (GMAS), a subsidiary of ETM, from obtaining an exploitation license to mine what the company describes as "one of the world's largest undeveloped rare-earth deposits." While in October 2025 the arbitrators ruled that the issue of whether GMAS was entitled to an exploitation license must first be heard in Greenland's courts, it confirmed that claims for breach of contract and damages may still proceed by arbitration after the Greenlandic court's decision.

How Has the Threat of ISDS Claims Suppressed Climate Action?

The fear of ISDS international arbitration claims, and the massive awards that can result from such claims, has had a serious chilling effect on climate action. The IPCC has acknowledged this phenomenon, observing that "international investment agreements may lead to "regulatory chill," which may cause countries to refrain from or delay the adoption of mitigation policies, such as phasing out fossil fuels.[1]

Some states, including Denmark, New Zealand, and France, have cited the fear of ISDS claims under existing treaties as a justification for scaling back climate ambition. For example, while facing no publicly known claims, Denmark's government chose to set its deadline to end fossil fuel exploration as 2050, rather than 2030 or 2040. The then-climate minister stated that the country made that decision because it would otherwise have had to pay "incredibly expensive" compensation to companies on top of lost revenue for the Treasury. Similarly, the government of Spain said in a submission to the UN special rapporteur on human rights and the environment that ISDS "serves to discourage States from promoting energy transition policies for fear of being sued by a foreign investor."

The government of Nigeria recently called for reform of the ISDS system, including the integration of public-interest considerations such as climate action, environmental protection, human rights obligations, community welfare, and sustainable development, while other countries have called for exit from the system.

How Frequent are ISDS Claims?

According to a report by the UN Conference on Trade and Development (UNCTAD), the number of treaty-based ISDS cases has more than doubled in the past ten years. As of 2024, more than 1,300 claims have been brought under investment treaties, with 60 new arbitrations initiated in 2023. About 70 percent of investor-state arbitrations in 2023 were brought under treaties signed in the 1990s or earlier. As some claims are kept confidential, this number is likely an undercount.

[1] IPCC, 2022, Climate Change 2022: Mitigation of Climate Change, Contribution of Working Group III to the Sixth Assessment Report of the Intergovernmental Panel on Climate Change, p. 1499, para. 14.5.1.3.

Most of the claims have been brought by investors from high-income countries against low to middle income countries. According to UNCTAD, 70 percent of the arbitrations initiated in 2023 were brought against developing countries, including least developed countries (Myanmar, Senegal, and the United Republic of Tanzania). About half of the claims were directed at countries in Latin America and the Caribbean. Developed-country claimants brought most—about 75 percent—of the 60 known cases in 2023.

Canadian investors in the mining and oil and gas sectors have won 59 percent of their ISDS claims, averaging almost one billion dollars (USD 929 million) per award. The states that have settled or lost ISDS cases to Canadian investors are predominantly low-income states, including Bolivia, the Democratic Republic of Congo, Ecuador, Kyrgyzstan, Mongolia, Niger, Pakistan, Peru, and Venezuela.

As noted earlier, many investor claims never reach arbitration given the costs and risks involved. It is impossible to quantify the number of ISDS claims that have been threatened by foreign investors but not filed and that have successfully pressured states to weaken existing or withdraw proposed environmental and climate laws, regulations, taxes or other policies.

How Can States Reduce the Risk of ISDS Claims Against Climate Action Under Existing Treaties?

Where existing treaties contain ISDS provisions that would allow claims to be brought based on public policy initiatives designed to mitigate climate change or otherwise address environmental or public health issues, there are three possible ways to address the issue. States can seek to amend the treaty; issue interpretative statements regarding the intent of the treaty; or withdraw from it.[2]

[2] For a detailed review of possible actions, see Ladan Mehranvar, with Martin Dietrich Brauch, Achyuth Anil, Anna-Sophie Kloppe, Lucas Clover Alcolea, and Madeleine Songy, Breaking Free: Strategies for Governments on Terminating Investment Treaties and Removing ISDS Provisions. New York: Columbia Center on Sustainable Investment (CCSI), October 2024, https://ccsi.columbia.edu/sites/ccsi.columbia.edu/files/content/docs/publications/ccsi-breaking-free-investment-treaties.pdf.

Amendment

Existing treaties can, though mutual negotiation, be amended to more narrowly circumscribe and define the rights which investment treaties grant to foreign investors or to clarify the intent of the parties. For instance, when the U.S., Canada, and Mexico renegotiated the NAFTA and adopted its successor, referred to in Canada as the Canada-U.S.-Mexico Trade Agreement (CUSMA) and in the U.S. as the U.S.-Mexico-Canada Trade Agreement (USMCA) in 2021, the parties removed ISDS provisions for the U.S. and Canada, while limiting claims related to investments in Mexico to those for direct expropriation and discrimination. The treaty also specifically provides, in Article 1.3, that a party's obligations under the Agreement will not preclude it from taking measures to comply with its obligations under a specified list of multilateral environmental agreements, provided that the primary purpose of the measure is not to impose a disguised restriction on trade. Unfortunately, likely because the treaty was negotiated at a time when the U.S. was withdrawing from the Paris Agreement, the Paris Agreement is not among the agreements listed, although the agreement expressly allows for additional multilateral agreements and treaties to be added to the list.

Some other efforts at renegotiation and reform are underway, including efforts to revise the Energy Charter Treaty. Efforts were also made to remove ISDS provisions from the ASEAN-Australia-New Zealand Free Trade Agreement (AANZFTA) when it was upgraded in 2023, but those efforts were unsuccessful. However, the parties agreed to suspend ISDS claims for breach of the national treatment obligation for 30 months after entry into force of the upgrade, to allow time for a review of the ISDS provisions. That review is ongoing. Similarly, the OECD has also been discussing a proposal to exclude climate-related measures from ISDS, with a focus on measures related to reducing or stabilizing greenhouse gas emissions.

However, given the thousands of existing treaties, renegotiation is a daunting task that would take many years and much diplomatic energy. It is inconceivable that they could all be renegotiated quickly enough to meet states' needs to act quickly on climate change.

A more realistic and efficient alternative to amending the thousands of investment treaties would be the adoption, for example, by a group of countries of a multilateral instrument that amends all such treaties and free trade agreements. This would

include investment provisions that include an additional clause specifying that a party's obligations under the treaty will not preclude it from taking measures to comply with its obligations under a specified list of multilateral environmental and climate agreements, including the Paris Agreement. That instrument would then be open to signature (and ratification, if necessary, under domestic law) by all countries that are party to investment treaties and free trade agreements with those states. In this way, states could amend, via a single instrument, all pre-existing treaties between the parties that sign the new treaty.

Interpretative Statements

Some commentators have recommended the use of "interpretative statements," whereby governments endorse joint statements clarifying and defining their positions on contentious clauses in their existing investment treaties. Under international law, states have the right to constrain how international adjudicators interpret treaties, including after the treaties have been ratified. The Vienna Convention on the Law of Treaties requires tribunals to take such statements into account. State interpretative statements provide a viable way for governments to raise their concerns about existing treaties or clarify their intentions in those treaties, without going through the pains of terminations or renegotiations, and the ICJ advisory opinion provides important legal support for states to assert that investment treaty protections cannot be interpreted in a way that would require states to violate their binding climate and human rights obligations.

Very few countries have gone down this route, possibly due to the sheer number of treaties for which such statements would need to be issued, or to a lack of understanding of the role that such statements could play. Some commentators have therefore suggested plurilateral arrangements facilitated by an existing international organization, such as UNCITRAL or the OECD, along the lines suggested above for multilateral amendments. That body could map out common ground among potential signatory states and, on the basis of this mapping exercise, produce a series of interpretative statements on contentious provisions and issues, with associated commentary. Governments could then, in turn, opt into some or all of these statements on an individual basis during meetings facilitated by the secretariat.

Interpretative statements are, however, less effective than full amendments. One drawback is lack of certainty as to whether arbitral panels will give full weight to mutual interpretative statements. On the other hand, because the constitutions or domestic laws of some countries, including the U.S., require domestic approval for ratification that are time-consuming and politically challenging, one benefit of a mutual interpretative statement is that it is unlikely it would require ratification and thus can be implemented more quickly than an amendment.

Withdrawal or Cancellation

Some countries have chosen to withdraw from treaties containing broad ISDS provisions. For example, as discussed above, the EU and eleven individual countries have withdrawn from the controversial Energy Charter Treaty.

However, when one party withdraws from a treaty, "survival" or "sunset" clauses may keep protections in place for years and sometimes decades after termination, meaning this option has limited near-term effect in shielding states from controversial claims. As discussed above, the ECT contains a "sunset provision" legally binding the withdrawing country to the treaty for another 20 years.

It is possible for both parties to mutually agree to terminate that treaty. In such a case, they can also agree to terminate the sunset or survival clauses. In any case where this is possible, however, it will likely also be possible to keep all of the mutually beneficial parts of the agreement in place and amend the agreement to remove the threat of ISDS claims that would undermine the parties' ability to achieve legitimate public policy goals.

In 2018, the Court of Justice of the European Union (CJEU) ruled in the *Achmea* case that arbitration clauses in intra-EU investment treaties are inconsistent with the Treaty of the Functioning of the European Union because the use of such private tribunals violates the autonomy of the EU judicial system. In response, EU member states signed a plurilateral agreement to officially terminate all intra-EU BITs and their respective ISDS mechanisms and sunset clauses. However, EU member states continue to be party to many such treaties with non-EU countries, and companies from EU member states regularly file ISDS claims against non-EU countries.

Moreover, companies continue to try to circumvent the ruling by filing claims in the name of non-EU subsidiaries. For example, as noted above, in August 2026, ExxonMobil filed an ISDS claim against the European Commission, challenging mandatory carbon storage obligations outlines in the EU's Net Zero Industry Act. The action, brought under the Energy Charter Treaty, included as a plaintiff a UK-based subsidiary, in order to bypass the EU restrictions on intro-EU arbitrations.

What About New Investment Treaties and Contracts?

When negotiating new investment treaties and contracts, it is critical that states ensure that they contain explicit clauses excluding non-discriminatory climate-related measures and bona fide environmental and public health initiatives from state conduct that can give rise to claims for compensation. It may also be desirable to include clauses that limit damages for speculative or anticipated profits. While some recent treaties have taken steps in this direction by including exceptions for certain types of government action, few, if any, contain clear exceptions for environmental or climate-related measures.

Working Group III of the UN Commission on International Trade Law (UNCITRAL) has been working on ISDS reform proposals since 2017, but much of its work has focused on codes of conduct, procedural changes to arbitration tribunals, and draft language to be included in new ISDS provisions. It is also working on a draft statute to create a permanent tribunal for international investment disputes and a permanent appellate tribunal for such disputes.

While these initiatives may have merit, the easiest measure for states to take when negotiating new treaty obligations is to make sure that national efforts to mitigate climate change and protect the environment and human rights are clearly removed from the bases on which an ISDS arbitration panel can award damages.

ISDS Claims and Obligations Under International Law

The July 2025 unanimous Advisory Opinion on states' obligations in relation to climate change by the ICJ represents a watershed moment that should fundamentally reshape the legal landscape in which ISDS claims must be assessed. The opinion makes clear that states have a duty under international law to prevent

climate harm, to protect the climate system, and to protect the human rights of present and future generations. The ICJ established that the 1.5° limit under the Paris Agreement is legally binding and the failure to take appropriate measures to prevent foreseeable harm—including through fossil fuel production and consumption, new exploration licenses, subsidies, or inadequate regulation—can constitute an internationally wrongful act attributable to the state.

Critically, in the context of ISDS claims, the Court underscored that states must regulate non-state actors within their jurisdiction, especially fossil fuel companies whose activities drive climate breakdown, and that fossil fuel consumption, subsidies and licensing decisions may lead to legal responsibility under international law. This obligation clearly applies not only to domestic companies, but also to foreign-owned energy companies that might seek to use ISDS provisions in contracts or investment treaties to challenge such action.

ICJ judge Sarah Cleveland specifically addressed the implications for investment treaties in her separate declaration, clarifying that "the interpretation of investment instruments must be informed by states' obligations in respect of climate change under international law, including the stringent due diligence standard to which states are bound in implementing such obligations." She also cited the IPCC's recognition that ISDS can deter climate regulation—the so-called "regulatory chill"—as a reason that investment treaties should not be interpreted in isolation from international climate law. This declaration by a serving ICJ judge is an invitation to further develop the legal understanding that ISDS does not, and should not, operate in a vacuum that ignores science, the facts of the climate crisis, and international law, including customary international law obliging states to protect the climate system and the human rights of present and future generations. Led by Vanuatu and other Pacific island nations, in May 2026 the UN General Assembly reinforced this new legal framework through resolution A/80/l.65, with 141 votes in favor, only 8 against, and 28 abstentions.

Similarly, the Inter-American Court of Human Rights, in its 2025 Advisory Opinion 32/25, found that states must take all necessary measures to reduce risks stemming from both the degradation of the global climate system and the exposure and vulnerability of people and communities to the resulting harms. To fulfill that obligation, states must require companies to conduct human rights and climate due diligence across their value chains, mandate public disclosure of emissions, enforce

emission reduction actions, require alignment with national climate targets, and address greenwashing and undue political influence. The court specifically addressed ISDS provisions, noting that “States should revise their trade and investment agreements, as well as Investor-State Dispute Systems, to guarantee that they neither limit nor restrict efforts in the area of climate change and human rights.”

While neither of the advisory opinions is legally binding, the laws, including customary international law, that they interpret, are binding, and the opinions of the highest international court and the regional court for Latin America should be given heavy weight.

The legal implications of the ICJ decision for ISDS claims were spelled out in detail by Lukas Schaugg at the International Institute for Sustainable Development (IISD) in a March 2026 briefing. He identified three key dimensions:

1. On legitimate expectations: the most commonly used basis for ISDS claims is the fair and equitable treatment (FET) standard, invoked in over 80% of ISDS cases. The ICJ's findings establish that compliance with international law requires progressively stricter environmental regulation. Investors therefore cannot expect states to maintain regulatory frameworks that violate binding international obligations, including by issuing or extending fossil fuel exploration or production licenses in breach of their climate duties.

2. On direct and indirect expropriation claims: in light of the ICJ advisory opinion, arbitration tribunals should be much more willing to find that climate-justified regulatory measures, such as drilling bans or fossil fuel phase-outs, do not constitute compensable expropriation, since the state was legally obliged to take such measures under international law.

3. On proportionality: the stringent due diligence standard articulated by the ICJ means that environmental measures should more readily be justified as proportionate. Tribunals typically examine whether a measure pursues a legitimate public policy aim, whether it is rationally connected to that aim, and whether it represents the least restrictive means available. The ICJ's determination that phasing out fossil fuels is a legal duty, not merely a policy

preference, means that climate measures will much more easily satisfy all these criteria.

States can and should adopt key provisions from the ICJ advisory opinion, Judge Cleveland's declaration, and the Inter-American Court of Human Rights (IACtHR) advisory opinion 32/25 as part of their legal defense in ISDS proceedings. International law practitioners and scholars can add weight to this effort by utilizing the amicus curiae mechanisms in trade tribunals to highlight the implications of such cases for states' binding international climate and human rights obligations.

Among other things, states should push for restrictions on forward-looking damage awards in ISDS cases, which often rely on speculative projections of future revenues from fossil fuel assets whose value is in structural decline. The ICJ's determination that states are obliged to phase out fossil fuels makes such speculative claims for future profits from fossil fuel operations particularly difficult to justify.

The ICJ advisory opinion and the supporting UNGA resolution also provide a strong legal and political case for states to insist that all new investment treaties explicitly exclude lawful climate measures from the scope of ISDS claims.

Businesses also have an obligation to ensure that their operations do not cause human rights and environmental harms. Using ISDS provisions to thwart state action intended to protect the climate system and the environment is inconsistent with those obligations and carries serious reputational and other risks. Similarly, financial institutions should adopt policies that exclude companies using or threatening ISDS claims to block climate action from those eligible for investment or financing as part of their climate and human rights commitments.

Recommendations

To States

When negotiating new investment agreements or treaties

- Ensure that all new investment treaties and trade agreements explicitly exclude from claims for compensation acts taken to mitigate climate change and protect the environment and human rights.

- Limit the ability to claim damages for future or speculative profit. This is especially important in the fossil fuel sector, where the ICJ has confirmed that phase-out is a legal obligation, making claims for speculative future profits particularly difficult to justify.
- If including an international arbitration clause in the treaty or agreement:
    - specify that the arbitrators can and should consider the reasons behind governmental action when assessing fault, including a state's obligations under international climate and human rights law.
    - require that all affected parties are notified of the dispute and provide a meaningful and substantive avenue for participation of all affected parties, including local communities and the public.
    - prohibit third party funding for any arbitration under the agreement or treaty.
    - specify that arbitrators need not be members of a specific arbitration body and that, for cases related to decisions allegedly made on environmental or climate grounds, at least one arbitrator should have a background in environmental law and/or climate change.
    - require that arbitrators can and should consider the reasons behind governmental action when assessing responsibility, including states' binding climate and human rights obligations under the ICJ, IACtHR, and International Tribunal for the Law of the Sea (ITLOS) advisory opinion.

With respect to existing treaties and agreements

- Issue interpretive statements, individually and jointly with treaty partners, making clear that investment treaty protections are to be interpreted in harmony with states' binding international climate and human rights obligations as confirmed by the ICJ.
- Where possible, work with the other party/parties to the agreement to amend the treaty or agreement to:
    - explicitly exclude from claims for compensation acts taken to mitigate climate change and protect the environment and human rights.
    - limit the ability to claim damages for future or speculative profit.
    - delete any sunset clauses.
- Where such bilateral (or multilateral for multilateral treaties) agreement is not achievable, work with like-minded countries to draft a multilateral instrument that amends all BITs and free trade agreements, as discussed above, and is open to signature (and ratification, if necessary, under domestic law) by all countries that are party to BITs and free trade agreements.

- Use the ICJ advisory opinion and UNGA resolution A/80/l.65 proactively as part of legal defenses in all pending and future ISDS proceedings relating to climate and environmental measures.

To ICSID and Other International Arbitral Fora

- For arbitrations between investors and state parties, amend your procedures to:
    - specify that the arbitrators can and should consider the reasons behind governmental action when assessing responsibility, including states' binding climate and human rights obligations under the ICJ, IACtHR, and ITLOS advisory opinions.
    - provide an avenue for participation of all affected parties, including local communities and taxpayers.
    - prohibit third party funding for any arbitration under the agreement or treaty.
    - specify that the arbitrators need not be members of a specific arbitration body, and that, for cases related to decisions allegedly made on environmental or climate grounds, at least one arbitrator should have a background in environmental law and/or climate change.
    - limit the ability to claim damages for future or speculative profit.
    - include a right to appeal any arbitral award and set up a neutral body to hear such appeals.

To Investors

- Companies invested in countries where ISDS provisions are available should refrain from using such provisions to seek damages for action taken to protect against climate change and protect human rights. Using ISDS provisions to challenge states' lawful measures to protect the climate system and human rights of present and future generations is inconsistent with companies' own obligations to ensure that their operations do not cause human rights and environmental harms.

To Financial Institutions

- Take a public position against the use of ISDS claims to challenge climate action.
- Exclude companies that have used or threatened ISDS claims to challenge climate action from those eligible for investment and/or financing.

- Recognize that companies that try to block climate policy through ISDS create long-term financial risk, both due to the physical consequences of the climate crisis and due to the legal risks arising from the ICJ's confirmation that states are legally obliged to protect the climate system and the human rights of present and future generations, and to phase out fossil fuels as the main driver of the crisis.



An industrial oil refinery emits smoke into the atmosphere. Photo: Michael Pointner/Unsplash.