Arbitrating Climate Transition: Coal Phase-Out and International Investment Law

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In recent years, foreign investors in the coal sector have challenged host States' coal phase-out measures under international investment law, claiming that these measures violate their investment treaty obligations. This has led to criticism of international investment law as chilling climate action. This Article proposes to resolve the conflict through a contextual interpretation of foreign investors' legitimate expectations by taking into account the nature of climate transition.

The Article suggests that investment tribunals adopt this contextual interpretation of foreign investors' legitimate expectations when interpreting the indirect expropriation and fair and equitable treatment (FET) standards, and proposes a two-step approach: First, host States should comply with specific commitments made to foreign investors regarding their coal phase-out schemes; second, in the absence of such commitments, host States' phase-out measures should not be deemed a violation of investment treaty obligations unless they discriminate against foreign investors. The Article explains how this approach can be implemented in investment arbitration to achieve a balance between climate and investment interests.

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INTRODUCTION

Coal, the most carbon-intensive fossil fuel, remains the largest source of power worldwide and occupies 35 percent of the electricity mix.[1] By the end of 2023, eighty-four countries had committed to phasing out coal or refraining from developing new unabated coal power plants.[2] Collectively, these countries represent approximately 30 percent of the coal used for electricity generation.[3] Among these countries, thirty-seven have set coal phase-out targets with specific dates in their national plans, most are located in Europe, and 80 percent are advanced economies.[4]

Although phasing out coal is essential for climate change mitigation, it also poses challenges regarding the equitable distribution of transition costs among stakeholders.[5] In recent years, foreign investors in the coal sector have challenged countries' phase-out schemes through international investment law, alleging they have been subjected to unfair treatment prohibited by investment treaties. For example, in 2019, the U.S. mining company Westmoreland filed an

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1. INT'L ENERGY AGENCY, GLOBAL ENERGY REVIEW 19 (2025), https://iea.blob.core.windows.net/assets/5b169aa1-bc88-4c96-b828-aaa50406ba80/GlobalEnergyReview2025.pdf.

2. Carl Greenfield, *Coal*, INT'L ENERGY AGENCY, https://www.iea.org/energy-system/fossil-fuels/coal (choose "Tracking;" then choose "Policy") (last updated Mar. 26, 2024).

3. *Id.*

4. *Id.*

5. Thomas Spencer, et al., *The 1.5°C Target and Coal Sector Transition: At the Limits of Societal Feasibility*, 18 CLIMATE POL'Y 335, 339-40 (2018) (describing three groups of people that are likely to be made worse off as a result of substantive coal transition policy and thus need governmental compensation or adaptive assistance: (1) "workers currently employed in the coalmining sector"; (2) "communities or regions in which coalmining accounts for a large share of economic activity"; and (3) "owners of coal sector-specific assets, such as coal-mining companies").

international investment arbitration claim against Alberta, Canada's coal phase-out plan.[6] Westmoreland alleged that the phase-out plan violated Canada's obligations under the North American Free Trade Agreement (NAFTA), particularly the national treatment and fair and equitable treatment (FET) clauses.[7] Similarly, in 2021 two German multinational energy companies, RWE and Uniper, initiated separate arbitration proceedings against the Netherlands.[8] They claimed that the Dutch Coal Ban Law, which aims to phase out coal-fired power plants by 2030, breached the Energy Charter Treaty (ECT).[9] In 2023, the Swiss energy supplier Azienda Elettrica Ticinese brought an investment arbitration claim against Germany, alleging that the German Coal Ban Law violated investment protection clauses under the ECT.[10]

Investment arbitration cases involve foreign investors bringing claims against the host State for their investments.[11] The applicable laws are primarily international investment treaties between countries, which require that host States protect foreign investments within their territories and allow foreign investors to bring a claim against the host State before an international investment tribunal in case of treaty breaches.[12] Currently, there are over 2,600 investment treaties in force, with a significant portion signed in the 1990s and 2000s, many of which lack explicit provisions addressing environmental or climate concerns.[13]

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6. Westmoreland Mining Holdings, LLC v. Gov't of Can., ICSID Case No. UNCT/20/3, Final Award, ¶¶ 2-3, 5, 7 (Jan. 31, 2022) [hereinafter Westmoreland v. Canada Final Award], https://icsidfiles.worldbank.org/icsid/ICSIDBLOBS/OnlineAwards/C8473/DS17240_En.pdf.

7. *See id.* ¶ 94. For definitions of national treatment and the fair and equitable treatment (FET) standard, *see infra* Part III.B.1 and Part I.B, respectively.

8. *See* RWE AG v. Kingdom of the Netherlands, ICSID Case No. ARB/21/4, Claimants' Memorial, ¶¶ 6-19 (Dec. 18, 2021) [hereinafter RWE v. Netherlands], https://www.italaw.com/sites/default/files/case-documents/italaw170473.pdf; Uniper SE v. Kingdom of the Netherlands, ICSID Case No. ARB/21/22, Claimants' Memorial, ¶¶ 1-7, 41 (May 20, 2022) [hereinafter Uniper v. Netherlands].

9. *RWE v. Netherlands*, ICSID Case No. ARB/21/4, Claimants' Memorial, ¶¶ 17-18; *Uniper v. Netherlands*, ICSID Case No. ARB/21/22, Claimants' Memorial ¶¶ 32-33. The Energy Charter Treaty (ECT) is an international agreement that establishes a multilateral framework for energy cooperation among its member countries, promoting investments, trade, and the development of energy resources.

10. *Azienda Elettrica Ticinese v. Federal Republic of Germany*, ICSID Case No. ARB/23/47, Request for Arbitration, ¶ 52 (Sept. 29, 2023).

11. R. DOAK BISHOP ET AL., FOREIGN INVESTMENT DISPUTES: CASES, MATERIALS, AND COMMENTARY 2 (R. Doak Bishop et al. eds., 2nd ed. 2014).

12. Jeswald W. Salacuse, *The Treatification of International Investment Law*, 13 L. & BUS. REV. AM. 155, 155-56 (2007). Although the current climate-investment tension in investment arbitration primarily stems from investment treaties, future disputes may also originate from coal investment contracts. *See* Anatole Boute, *Phasing Out Coal Investment Contracts: Does Just Transition Finance Legitimize Unjust Compensation?*, ICSID REV. – FOREIGN INV. L. J. 1, 13-14 (2025).

13. U.N. CONF. ON TRADE & DEV., WORLD INVESTMENT REPORT 104-05 (2025), https://unctad.org/system/files/official-document/wir2025_en.pdf. For a mapping of environmental provisions in investment treaties, see *International Investment Agreement Navigator*, U.N. CONF. ON TRADE & DEV., https://investmentpolicy.unctad.org/international-investment-agreements (last visited

There have been increasing concerns about the adverse impacts of investor-state disputes on climate change mitigation efforts.[14] International organizations such as the Intergovernmental Panel on Climate Change have expressed concerns that investment agreements could impede climate mitigation efforts.[15] Similarly, the United Nations Environment Programme has labeled investment arbitration cases as "backlash cases," suggesting that the cases are against climate goals and could hinder both mitigation and adaptation measures.[16]

The international community and academic literature have made various proposals to reform investment treaties to protect States' right to regulate industries that contribute to climate change.[17] However, investment treaties often contain a sunset clause that permits foreign investors to benefit from treaty protection for five to twenty years after the treaty's termination, meaning that parties may be locked into treaties signed in a different climate context.[18] Moreover, although treaties can be amended, negotiations on amendments can be lengthy. With the looming threat of climate change requiring action on a shorter time scale, other solutions that do not require treaty amendment may prove more effective. One such alternative is treaty interpretation. Some scholars have proposed to incorporate climate concerns into the interpretation of the compensation standards.[19] This Article focuses on another aspect: How should

Jan. 11, 2025). For an empirical study of sustainable development provisions adopted in recent investment treaties, see U.N. CONF. ON TRADE & DEV., MAPPING SUSTAINABLE DEVELOPMENT AND INVESTMENT FACILITATION PROVISIONS IN IIAS CONCLUDED BY G20 MEMBERS AND INVITED COUNTRIES 6-14 (2024), https://unctad.org/system/files/official-document/unctad_oecd-2024-g20-iias_en.pdf.

14. Kyla Tienhaara, *Regulatory Chill in a Warming World: the Threat to Climate Policy Posed by Investor-State Dispute Settlement*, 7 TRANSNAT'L ENVT'L L. 229 (2018).

15. INTERGOVERNMENTAL PANEL ON CLIMATE CHANGE, CLIMATE CHANGE 2022: MITIGATION OF CLIMATE CHANGE 1499 (2022), https://www.ipcc.ch/report/ar6/wg3/downloads/report/IPCC_AR6_WGIII_FullReport.pdf. The Intergovernmental Panel on Climate Change (IPCC) is an international organization established to assess scientific information related to climate change, its impacts, and potential adaptation and mitigation strategies. It provides policy makers with comprehensive reports based on the latest climate research. *See* INTERGOVERNMENTAL PANEL ON CLIMATE CHANGE, IPCC FACT SHEET – WHAT IS THE IPCC? 1 (2024).

16. U.N. ENV'T PROGRAMME, GLOBAL CLIMATE LITIGATION REPORT: 2023 STATUS REVIEW 70-71 (2023), https://wedocs.unep.org/rest/api/core/bitstreams/ddef44f2-b566-4a07-94ad-95c006749fcd/content.

17. *See, e.g.*, Joshua Paine & Elizabeth Sheargold, *A Climate Change Carve-Out for Investment Treaties*, 26 J. INT'L ECON. L. (2023); Sheng Zhang & Ni Li, *Addressing Climate Change Through International Investment Agreements: Obstacles and Reform Options*, 16 SUSTAINABILITY 1471 (2024); Ying Zhu, *A Quasi-Normative Conflict: Resolving the Tension Between Investment Treaties and Climate Action*, 33 REV. EUR. COMPAR. & INT'L ENVT'L L. (SPECIAL ISSUE) 183 (2024).

18. *See* Claudia Annacker, *Operation and Termination of Sunset Clauses in Bilateral Investment Treaties*, 10 NAT'L L. SCH. BUS. L. REV. 10, 12-13 (2024).

19. *See, e.g.*, Anatole Boute, *Investor Compensation for Oil and Gas Phase Out Decisions: Aligning Valuation Methods to Decarbonization*, 23 CLIMATE POL'Y 1087, 1096-97 (2023); Yawen Zheng, *Rethinking the 'Full Reparation' Standard in Energy Investment Arbitration: How to Take Climate Change into Account*, 27 J. INT'L ECON. L. 500, 515-16 (2024).

investment tribunals interpret the investment protection standards to strike a balance between investment and climate interests?

This Article contributes to the literature by proposing a contextual interpretation of the legitimate expectations of foreign investors in the coal sector. It challenges the conventional understanding of legitimate expectations as protecting investors from radical or fundamental regulatory changes. The Article argues that this approach overlooks the unique regulatory context of coal regulation during climate transition, where radical and fundamental regulatory changes are necessary to achieve climate goals. In the context of climate transition, coal investors should have reasonably anticipated these changes unless (1) the government explicitly provided assurances to the contrary or (2) the coal phase-out measures are implemented in a discriminatory manner. The Article suggests that this interpretation should be incorporated into tribunals' assessment of two core standards in investment treaties, FET and indirect expropriation, so as to carve out legitimate regulatory space in coal phase-out cases.

The Article proceeds as follows. Part I illustrates the emerging tension between coal phase-out measures and international investment law. Part II examines the climate transition risks foreign investors in the coal sector face, arguing that in the context of climate transition coal phase-out measures should be regarded as within the scope of foreign investors' legitimate expectations unless specific assurances to the contrary have been given or the measures are implemented in a discriminatory manner. Part III proposes that this contextual interpretation of legitimate expectations should be incorporated into the assessment of investment treaty standards.

I. COAL PHASE-OUT AND INTERNATIONAL INVESTMENT LAW

The international investment legal regime is primarily composed of investment treaties aimed at promoting and protecting foreign investments.[20] Over the past half-century, there has been a proliferation of international investment treaties.[21] According to the United Nations Conference on Trade and Development, as of 2025 there are more than 2,600 international investment agreements in force worldwide, mostly made through bilateral treaties.[22] These investment treaties contain similar provisions. They generally require host States to provide certain standards of protection to foreign investments in their

20. Jeswald W Salacuse, *The Emerging Global Regime for Investment*, 51 HARV. INT'L L. J. 427, 427-28 (2010).

21. *Id.* at 447-48.

22. U.N. CONF. ON TRADE & DEV., *supra* note 13, at 104-05. Bilateral treaties are treaties signed between two contracting parties, as compared to multilateral treaties, which have more than two parties.

territories, including national treatment,[23] most-favored nation treatment,[24] FET,[25] and compensation for expropriation.[26] In cases where host States violate these obligations, these treaties commonly contain the investor-state dispute settlement mechanism, which allows foreign investors to bring claims against host States in international arbitral tribunals.[27]

While investment treaties play an important role in protecting and promoting foreign investments, they have increasingly been criticized for their potential to "chill" the regulatory power of host States.[28] In recent decades, foreign investors have claimed that the environmental legislative, executive, or judicial actions of host States violate international investment treaties.[29] Most investment treaties have broad (and sometimes vague) language that can be read as precluding environmental regulation. Without specific clauses in these treaties delineating the scope of legitimate environmental regulation, tribunals have adopted different approaches to balancing investment and environmental protection.[30] In recent years, some States have reformed their investment treaties

23. The national treatment standard requires that the host State should accord the foreign investor in its territory no less favorable treatment than a domestic investor, if the two investors are in like circumstances. *See* Andrea K. Bjorklund, *The National Treatment Obligation*, *in* ARBITRATION UNDER INTERNATIONAL INVESTMENT AGREEMENTS: A GUIDE TO THE KEY ISSUES 532 (Katia Yannaca-Small ed., 2nd ed. 2018).

24. The most-favored nation treatment standard requires that the host State should accord the foreign investor in its territory no less favorable treatment than a third-country investor, if the two investors are in like circumstances. *See* Tony Cole, *The Boundaries of Most Favored Nation Treatment in International Investment Law*, 33 MICH. J. INT'L L. 537, 539 (2011).

25. The FET standard requires that the host State should accord fair and equitable treatment to the foreign investor. *See* Stephen Vasciannie, *The Fair and Equitable Treatment Standard in International Investment Law and Practice*, 70 BRIT. Y.B. INT'L L. 99, 101 (2000); Rudoff Dolzer, *Fair and Equitable Treatment: A Key Standard in Investment Treaties*, 39 INT'L L. 87, 89 (2005).

26. Generally, investment treaties require host States to pay compensation to foreign investors in cases of direct and indirect expropriation. *See* Steven R. Ratner, *Compensation for Expropriations in a World of Investment Treaties: Beyond the Lawful/Unlawful Distinction*, 111 AM. J. INT'L L. 7, 1 (2017).

27. BISHOP ET AL., *supra* note 11, at 576.

28. *See* Paine & Sheargold, *supra* note 17, at 288-89.

29. *See, e.g.*, Waste Mgmt., Inc. v. United Mexican States, ICSID Case No. ARB(AF)/00/3, Award, ¶¶ 40-42, 74 (Apr. 30, 2004), https://www.italaw.com/sites/default/files/case-documents/ita0900.pdf;); Unglaube v. Republic of Costa Rica, ICSID Case No. ARB/08/1 and ICSID Case No. ARB/09/20, Award, ¶¶ 37, 39 (May 16, 2012), https://www.italaw.com/sites/default/files/case-documents/ita1052.pdf; Clayton v. Gov't of Can., PCA Case No. 2009-04, Award on Jurisdiction and Liability, ¶¶ 11, 14 (Mar. 17, 2015), PCA Case Repository; Chevron Corp. v. Republic of Ecuador, PCA Case No. 2007-02/AA277, Partial Award on the Merits, ¶ 33 (Mar. 30, 2010), https://www.italaw.com/sites/default/files/case-documents/ita0151.pdf; Ole Kristian Fauchald, *International Investment Law and Environmental Protection*, 17 Y.B. INT'L ENVT'L L. 3 (2007); Ying Zhu, *A Bottom-Up Dilemma: International Investment Law and Environmental Governance*, 48 COLUMBIA J. ENVT'L L. 100 (2022).

30. *See* Kate Miles, *International Investment Law: Origins, Imperialism and Conceptualizing the Environment*, 21 COLO. ENVT'L. L. J. 1, 25 (2010); Jorge E Viñuales, *Foreign Investment and the Environment in International Law: Current Trends*, RESEARCH HANDBOOK ON ENVIRONMENT AND INVESTMENT LAW 27-28 (2019).

to preserve more environmental regulatory space.[31] Despite this trend, investment treaties that include environmental language only represent a small proportion of the total investment treaties in force, and the adoption of environmental language varies widely among countries.[32]

In the past few years, foreign investors have brought cases arguing that host States' actions to phase out fossil fuels violate investment protection obligations in investment treaties.[33] In these cases, foreign investors have claimed that the coal phase-out measures constitute violations of two key investment obligations present in most treaties: the indirect expropriation clause and the FET clause.[34] The following Subpart illustrates how, by their very nature, coal phase-out measures are vulnerable to arguments that they violate investment treaty obligations.

A. The Expropriatory Effect of Coal Phase-Out

There are two forms of expropriation: direct and indirect.[35] Direct expropriation occurs when a policy leads to a substantial deprivation of the investment's economic value; indirect expropriation occurs when a measure results in comparable economic impacts as direct expropriation but does not result in the transfer of property title.[36] By their very nature, coal phase-out measures are likely to have an expropriatory effect on the coal sector.

Under international investment law, a measure is considered to have an expropriatory effect if it results in a "substantial deprivation" of the foreign investments protected under investment treaties.[37] For instance, in *CME v. Czech Republic*, the tribunal found that indirect expropriation refers to the situation where the host State adopts "measures that do not involve an overt taking but that effectively neutralize the benefit of the property of the foreign owner."[38] In

31. Kathryn Gordon & Joachim Pohl, *Environmental Concerns in International Investment Agreements: A Survey*, OECD WORKING PAPERS ON INTERNATIONAL INVESTMENT, 2011/01, 5-6 (2011); Frank J Garcia et al., *Reforming the International Investment Regime: Lessons from International Trade Law*, 18 J. INT'L ECON. L. 861, 861 (2015).

32. Gordon & Pohl, *supra* note 31, at 31-32; Garcia et al., *supra* note 31, at 889.

33. *See, e.g.*, RWE v. Netherlands, *supra* note 8, ¶¶ 11, 18; Uniper v. Netherlands, *supra* note 8, ¶¶ 32-33; Westmoreland v. Canada Final Award, *supra* note 6, ¶¶ 5, 94.

34. *See* RWE v. Netherlands, *supra* note 8, ¶ 18; Uniper v. Netherlands, *supra* note 8, ¶¶ 33, 381; Westmoreland v. Canada Final Award, *supra* note 6, ¶ 94.

35. *See* RUDOLF DOLZER ET AL., PRINCIPLES OF INTERNATIONAL INVESTMENT LAW 153 (3rd ed. 2022).

36. *Id.* at 153, 157. For the controversy surrounding the definition of indirect expropriation, see generally L. Yves Fortier & Stephen L. Drymer, *Indirect Expropriation in the Law of International Investment: I Know it When I See it, or* Caveat Investor, 19 ICSID REV. – FOREIGN INV. L. J. 293 (2004).

37. Christian Riffel, *Indirect Expropriation and the Protection of Public Interests*, 71 INT'L & COMPAR. L. Q. 945, 947, 965 (2022).

38. CME Czech Republic B.V. v. Czech, Partial Award, United Nations Commission on International Trade Law [U.N. Comm'n on Int'l Trade L.], ¶ 604 (Sep. 13, 2001), https://www.italaw.com/sites/default/files/case-documents/ita0180.pdf.

Vivendi v. Argentina, the tribunal found that the measures Argentina adopted against the foreign investments amounted to an expropriation because their economic impact on foreign investments went beyond partial deprivation and rendered the concession accorded to the foreign investor valueless.[39] Ultimately, if the foreign investor can still generate significant profits from the investments, it does not meet the threshold of substantial deprivation and the governmental measure is not considered expropriatory.[40]

While international investment law does not prohibit expropriation by host States, it requires that an expropriatory measure must adhere to four conditions: The measure must serve a public purpose; be non-discriminatory; follow due process; and include "prompt, adequate, and effective compensation."[41] In other words, if a host State enacts a measure that has an expropriatory effect on foreign investors' property, regardless of whether it is motivated by public interest, the State is generally obliged to compensate the investor for the value lost.[42]

In investment arbitration cases, foreign investors have argued that the coal phase-out measures amounted to indirect expropriation that necessitates compensation for foreign investors, as the measures disrupt fundamental operations of the coal industry.[43] For instance, in *RWE v. Netherlands*, German energy company RWE, which invested in a coal-fired power plant in the Netherlands, brought an investment arbitration claim against the Netherlands's coal phase-out legislation.[44] The claimants argued that the Netherlands's Coal Ban Law constituted an indirect expropriation of their investments.[45] The claimants acknowledged that no formal expropriation had occurred, as the coal ban did not impact the ownership of the coal-powered plants.[46] However, they argued that the Coal Ban Law had an expropriatory effect on the plant by substantially depriving owners of the value of their investments.[47]

39. Compañiá de Aguas del Aconquija S.A. v. Argentine Republic, ICSID Case No. ARB/97/3, Award, ¶¶ 7.5.28, 7.5.34 (Aug. 20, 2007), https://www.italaw.com/sites/default/files/case-documents/ita0215.pdf.

40. This principle was upheld in *Merrill & Ring v. Canada*, where the tribunal found that Canada's export control measures did not constitute indirect expropriation given that the foreign investor could still operate the business profitably. Merrill & Ring Forestry L.P. v. Gov't of Can., ICSID Case No. UNCT/07/1, Award, ¶¶ 148, 152 (Mar. 31, 2010), https://www.italaw.com/sites/default/files/case-documents/ita0504.pdf.

41. Ratner, *supra* note 26, at 1; *see also* Patrick M. Norton, *A Law of the Future or a Law of the Past? Modern Tribunals and the International Law of Expropriation*, 85 AM. J. INT'L L. 474, 475-76, 479, 483 (1991).

42. Riffel, *supra* note 37, at 970-71.

43. *See, e.g.*, RWE v. Netherlands, ICSID Case No. ARB/21/4, Claimants' Memorial ¶ 18; Uniper v. Netherlands, *supra* note 8, ¶ 33.

44. RWE v. Netherlands, *supra* note 8, ¶¶ 7-19.

45. *Id.* ¶ 455.

46. *Id.* ¶ 456.

47. *Id.*

The claimants argued that the impact of the coal ban on the foreign investments went beyond a legitimate regulation.[48] To distinguish between a legitimate regulation and an indirect expropriation, the claimants referred to the criteria adopted by the *Continental Casualty v. Argentina* award, which took into account whether the "key feature[s]" and "basic, typical use" of the asset had been impeded.[49] The claimants argued that the Coal Ban Law impeded the "key feature[s]" and the "basic, typical use" of coal-fired plants by prohibiting the burning of coal for electricity generation.[50] Similarly, in *Uniper v. Netherlands*, Uniper claimed that the Netherlands's Coal Ban Law breached its obligations under the Energy Charter Treaty, the relevant international investment treaty.[51] In particular, the claimants argued that the Coal Ban Law constituted a substantial deprivation of the value and use of the investments, a result of the investments' loss of capacity to earn a commercial return.[52]

Moreover, the gradual nature of a coal phase-out scheme does not completely exempt the host State's responsibility under indirect expropriation clauses, as the economic effect of the phase-out measure on coal sector investors can be determined on a cumulative basis.[53] In *Generation Ukraine v. Ukraine*, for example, the tribunal stated that "creeping expropriation" refers to a situation where "a series of acts attributable to the State over a period of time culminate in the expropriatory taking of such property."[54] In *Biwater v. Argentina*, the tribunal also noted that the expropriatory effect will be assessed on a cumulative basis.[55]

Accordingly, even if the phase-out of coal is implemented gradually, it can still constitute a creeping indirect expropriation that necessitates compensation to foreign investors. As the foreign investors in *RWE v. Netherlands* claimed, the existence of the transition period does not mean that the expropriation has not already occurred.[56] The claimants argued that even though the Coal Ban Law's prohibition on coal firing does not go into full effect until 2030, it still constitutes a substantial deprivation of the asset's value.[57] The claimants argued that the Netherlands had deprived both the value and the use of their investments and the

48. *See* RWE v. Netherlands, ICSID Case No. ARB/21/4, Claimants' Memorial ¶¶ 486-87.

49. *Id.*

50. *Id.* ¶ 487.

51. Uniper v. Netherlands, ICSID Case No. ARB/21/22, Claimants' Memorial ¶ 33.

52. *Id.* ¶¶ 388-9, 405.

53. *See* Sanja Djajic & Petar Djundic, *Creeping Expropriation—In Search for a More Comprehensive Approach*, 2 Y.B. ON INT'L ARB. 239, 243 (2012).

54. Generation Ukraine, Inc. v. Ukraine, ICSID Case No. ARB/00/9, Award, ¶ 20.22 (Sept. 26, 2003), https://www.italaw.com/sites/default/files/case-documents/ita0358.pdf (emphasis omitted).

55. Biwater Gauff (Tanzania) Ltd. v. United Republic of Tanzania, ICSID Case No. ARB/05/22, Award, ¶ 456 (July 24, 2008), https://www.italaw.com/sites/default/files/case-documents/ita0095.pdf.

56. RWE v. Netherlands, *supra* note 8, ¶ 466.

57. *Id.* ¶ 467.

ten-year transition period did not constitute sufficient compensation.[58] Similarly, in *Uniper v. Netherlands*, the claimants argued that the Coal Ban Law amounted to an indirect expropriation of their investments, since it forced the claimants to shut down the coal-powered plant twenty-six years earlier than its forty-year lifetime without providing adequate compensation.[59] The claimants specifically drew comparisons to previous jurisprudence where tribunals determined that the revocation of licenses, which allowed foreign investors a longer operational period before shutdown compared to the *Uniper* case, still amounted to an indirect expropriation.[60]

The differentiation between the host State's legitimate exercise of climate regulatory authority, where compensation is not required, and indirect expropriation, where the host State must compensate the foreign investor, is not always clear-cut.[61] The coal phase-out measures, while serving legitimate climate objectives, encounter challenges in being justified under the indirect expropriation clause. Generally, the existence of a public purpose does not, by itself, excuse the expropriatory nature of a regulatory measure.[62] In the existing jurisprudence, investment tribunals have adopted different approaches regarding whether the intent of a measure will be considered in determining whether there has been an expropriation.[63]

Some tribunals have followed the sole effect doctrine, which assesses indirect expropriation solely based on the economic impacts of the challenged measure. For instance, the tribunal in *Santa Elena v. Costa Rica* noted that:

> Expropriatory environmental measures—no matter how laudable and beneficial to society as a whole—are, in this respect, similar to any other expropriatory measures that a state may take in order to implement its policies: where property is expropriated, even for environmental purposes, whether domestic or international, the state's obligation to pay compensation remains.[64]

In recent investment disputes arising from phase-out measures, foreign investors have relied upon this approach to argue that despite being implemented for legitimate climate objectives, the phase-out measures still amount to indirect expropriation. In *RWE v. Netherlands*, the claimants argued that a climate

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58. *Id.* ¶ 473.

59. Uniper v. Netherlands, *supra* note 8, ¶¶ 381-82, 392.

60. *Id.* ¶ 393.

61. *See* Fortier & Drymer, *supra* note 36, at 293-94; Ying Zhu, *Do Clarified Indirect Expropriation Clauses in International Investment Treaties Preserve Environmental Regulatory Space?*, 60 HARV. INT'L L. J. 377, 378 (2019).

62. Riffel, *supra* note 37, at 970-71.

63. *See* Ben Mostafa, *The Sole Effects Doctrine, Police Powers and Indirect Expropriation Under International Law*, 15 AUSTL. INT'L L. J. 267, 280-81 (2008).

64. Compañía del Desarrollo de Santa Elena, S.A. v. Republic of Costa Rica, ICSID Case No. ARB/96/1, Award of the Tribunal, ¶ 72 (Feb. 17, 2000), 15 ICSID Rev. 169 (2000).

regulatory measure does not, by itself, exempt the host State of its obligation under an investment treaty.[65] The claimants stated that:

> The Coal Ban Law amounts to an indirect expropriation as it deprives Claimants of the use and value of their investments. And although the Coal Ban Law serves a public purpose, has been enacted after public consultation and is non-discriminatory (at least insofar as all operators–which are all foreign investors–are treated equally bad) and still only fulfils three out of four criteria for a lawful expropriation, Respondent has not paid any compensation, even though it offered insufficient non-monetary compensation.[66]

In this case, the claimants argued that the public purpose underlying the measure is irrelevant for determining whether a policy constitutes an expropriation since public purpose is a condition for a *lawful* expropriation.[67] The claimants argued that:

> It would take compliance with the requirements for a lawful expropriation—non-discrimination, due process and a public purpose—as evidence for the absence of an expropriation. That a measure serves a public purpose cannot mean that it does not amount to an expropriation. If every measure adopted for a public purpose was exempt from expropriation, then there would be no expropriation.[68]

Different from the sole effect doctrine, other investment tribunals have adopted the police powers doctrine, which considers the public policy objectives underlying the challenged measure when assessing the existence of indirect expropriation.[69] For instance, in *Feldman v. Mexico*, the tribunal stated that:

> [G]overnments must be free to act in the broader public interest through protection of the environment, new or modified tax regimes, the granting or withdrawal of governmental subsidies, reductions or increases in tariff levels, imposition of zoning restrictions and the like. *Reasonable governmental regulation of this type cannot be achieved if any business that is adversely affected may seek compensation, and it is safe to say that customary international law recognizes this.*[70]

However, what is a "reasonable governmental regulation" remains unclear. In the context of climate transition, even if the investment tribunal adopts a

65. RWE v. Netherlands, *supra* note 8, ¶ 478.

66. *Id.* ¶ 480.

67. *Id.* ¶ 483.

68. *Id.*

69. The investment tribunals have adopted various approaches regarding the police powers doctrine, including a broad definition of police power that includes any non-discriminatory regulation for a public purpose, a more limited definition that encompasses certain public purposes, and a narrow definition that requires the necessity of the regulatory measure to achieve the public purpose. *See* Mostafa, *supra* note 63, at 272-78.

70. Marvin Feldman v. Mexico, ICSID Case No. ARB(AF)/99/1, Award of the Tribunal, ¶ 103 (Dec. 16, 2002) (emphasis added).

police powers doctrine, the host State still faces challenges in proving that the phase-out measure is "reasonable" to achieve emission reduction objectives due to the global nature of the climate change. For instance, in *Uniper v. Netherlands*, the claimants raised the carbon leakage concern that "a coal phase out would actually stimulate more emissions from power stations in other European countries."[71] The claimants stated that "[t]his is because the closure of Dutch coal plants would prompt the import of more electricity from other European countries, which would stimulate more electricity production and more emissions by fossil-fueled power stations elsewhere, including less efficient coal-fired power stations than [the plant the Claimants invested in]."[72]

Similar arguments challenging the reasonableness of mitigation measures have found support in domestic climate litigation. In the recent *Milieudefensie et al. v. Shell* case, the Hague Court of Appeal accepted Shell's "market substitution" argument, which posited that if Shell does not supply the necessary fossil fuel production to meet market demand, another company will step in to fulfill that need.[73] The market substitution argument dismisses the effectiveness of emission reduction measures targeted at specific companies.[74] Following this reasoning, future investment tribunals may decide that the phase-out measure against coal plant operators cannot achieve the emission reduction purposes since the demand for coal would persist and producers in other countries would fill the gap.

Some other investment tribunals have adopted a proportionality test when determining whether a regulatory measure can be justified under an indirect expropriation clause.[75] For instance, the tribunal in *Continental Casualty v. Argentina* stated that limitations on the use of private property, which "do not impede the basic, typical use of a given asset and do not impose an unreasonable burden on the owner as compared with other similarly situated property owners,"

71. Uniper v. Netherlands, *supra* note 8, ¶ 424.

72. *Id.* The tribunals have not proceeded to the merits phase, as the case was discontinued.

73. Milieudefensie et al. v. Royal Dutch Shell plc., Court of Appeal of The Hague, Case No. 200.302.332/01, Judgment, ¶¶ 7.97-7.110 (Nov. 12, 2024).

74. *Id.*

75. For academic debates on the application of the proportionality test in international investment law, see generally Benedict Kingsbury & Stephan Schill, *Public Law Concepts to Balance Investors' Rights With State Regulatory Actions in the Public Interest—The Concept of Proportionality*, in INT'L INV. L. & COMPAR. PUB. L. 75 (2010); Prabhash Ranjan, *Using The Public Law Concept of Proportionality to Balance Investment Protection with Regulation in International Investment Law: A Critical Appraisal*, 3 CAMBRIDGE INT'L L. J. (2014); Stephan W Schill, *Cross-Regime Harmonization Through Proportionality Analysis: The Case of International Investment Law, The Law of State Immunity and Human Rights*, 27 ICSID REV. (2012); VALENTINA VADI, PROPORTIONALITY, REASONABLENESS AND STANDARDS OF REVIEW IN INTERNATIONAL INVESTMENT LAW AND ARBITRATION (2018).

should not be considered an expropriation, provided that "they do not affect property in an intolerable, discriminatory or *disproportionate* manner."[76]

This proportionality test can impose an even heavier burden of proof on host States. For the host State to prove that a coal phase-out measure is proportionate to the emission reduction goals, it may need to establish that alternative methods like the emissions trading system (ETS) and carbon capture and storage (CCS) technology, which may have lesser impact on foreign investments, are not feasible.[77] For instance, in *RWE v. Netherlands*, the claimants argued that the Coal Ban was not proportional to achieving its purpose.[78] The claimants noted that some tribunals have taken into account the proportionality of the measure in assessing whether a regulatory measure amounts to an indirect expropriation.[79] The Coal Ban Law was specifically enacted to achieve a 49 percent reduction in CO2 emissions by 2030.[80] The claimants cited the Parliamentary Papers of the Netherlands, which stated that the Netherlands government did not adopt other alternative measures because "[a]lternative instruments, such as tightening the efficiency requirements for these power plants, taking ETS allowances out of the market or an obligation for carbon capture and storage (CCS) have been studied previously and judged to be less effective, cost-efficient and/or legally untenable."[81] The claimants argued that this reasoning did not support the proportionality of the Coal Ban since the exact reason for being more "cost-efficient" is that there is no need to pay compensation.[82] The claimants also referred to other alternatives, including the revocation of permits, the nationalization of coal-fired plants (which would lead to compensation), and company-specific agreements between the Netherlands government and coal plant operators.[83] The claimants argued that "[i]f the pursuit of self-set political goals, and the intent to escape a duty of compensation, would be sufficient to convert an indirect expropriation into a non-compensable regulatory measure, this would basically lead to a self-judging and self-justifying exception that deprives [the expropriation clause] of any practical application."[84]

76. Cont'l Casualty Co. v. Argentine Republic, ICSID Case No. ARB/03/9, Award, ¶ 276 (Sep. 5, 2008) (emphasis added).

77. Some investment tribunals have assessed less restrictive alternative measures when determining the proportionality of the regulatory measures adopted by the host States. *See, e.g.*, S.D. Myers, Inc. v. Gov't. of Can., UNCITRAL, Partial Award, ¶¶ 215, 221, 255 (Nov. 13, 2000); PL Holdings S.à.r.l. v. Republic of Poland, SCC Case No. V 2014/163, Partial Award, ¶ 374 (June 28, 2017).

78. RWE v. Netherlands, *supra* note 8, ¶ 490-93.

79. *See id.* ¶ 489.

80. *Id.* ¶ 490.

81. *Id.* ¶ 491.

82. *Id.* ¶ 492-93.

83. *Id.* ¶ 492.

84. *Id.* ¶ 493.

Similarly, in *Uniper v. Netherlands*, the claimants argued that the Coal Ban Law was "not narrowly tailored to the Respondent's proffered public purpose."[85] The claimants stated that "[i]n assessing whether an expropriatory state measure was enacted for a public purpose, investment tribunals ask whether the measure bears proportionate relation to the policy objectives sought to be achieved, when viewed against the deprivation caused to the investor."[86] The claimants argued that the Coal Ban Law disproportionally "imposes the entirety of its carbon emissions reductions" on coal power plants.[87] They claimed that the Netherlands ignored other plants that emit carbon.[88] Besides, the claimants stated that "the Netherlands could have adopted a measure less draconian than the phase out of electricity produced from modern, efficient power plants and imposed a measure that reduced CO2 emissions, but shared the burden across the energy sector."[89] They also pointed out that the E.U. ETS is an alternative to a coal ban.[90]

As these case studies show, coal phase-out laws by their very nature and despite any public policy intentions may be considered expropriatory in violation of investment treaties. The next Subpart examines how coal phase-out policies may be radical changes in domestic law and have thereby been challenged as violating the fair and equitable treatment standard.

B. The Radical Nature of Coal Phase-Out

Coal phase-out policies have been challenged not only for their substance under expropriation theories, but also for the dramatic shift in policy they represent under the FET standard. The FET standard is a key standard in international investment law that mandates the host State to accord fair and equitable treatment to foreign investors. However, most investment treaties do not specifically define the broad terms "fair" and "equitable," granting significant discretion to investment tribunals in interpreting these terms.[91] Investment tribunals have mostly interpreted the FET standard as requiring the

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85. Uniper v. Netherlands, *supra* note 8, ¶ 410.
86. *Id.*
87. *Id.* ¶ 414.
88. *See id.*
89. *Id.*
90. *Id.* ¶ 415.
91. Some recent investment treaties have clarified the clause to refrain from an overly broad interpretation of the standard. For example, the 2022 Israel - Philippines BIT provides that the FET standard is breached

> if a measure or series of measures constitute: (a) denial of justice in criminal, civil, or administrative proceedings; (b) fundamental breach of due process, including a fundamental breach of transparency, in judicial and administrative proceedings; (c) manifest arbitrariness; or (d) targeted discrimination on manifestly wrongful grounds, such as gender, race, or religious belief.

Agreement between the Government of the State of Israel and the Government of the Republic of the Philippines on Promotion and Protection of Investments, Article 2(2), Phil.-Isr., Mar. 14, 2024.

host State to ensure a stable investment environment and safeguard the legitimate expectations of foreign investors at the time of investment.[92]

In recent cases, foreign investors in the coal sector have claimed that the coal phase-out policies in host States have breached the FET standard. For instance, in *RWE v. Netherlands*, the claimants argued that the Netherlands "ha[d] failed to provide a stable and consistent legal framework" by enacting the coal phase-out legislation.[93] Citing previous jurisprudence, the claimants argued that the FET standard imposes an obligation on the host State to "provide fundamental stability in the essential characteristics of the legal regime relied upon by investors in making long-term investments."[94] Similarly, in *Westmoreland v. Canada*, Westmoreland claimed that Canada's coal phase-out program was in breach of the FET standard because it frustrated Westmoreland's reasonable expectations.[95] Westmoreland claimed that it made investments in 2014 based on expectations that the investment would provide reasonable return beyond 2030.[96] Westmoreland claimed that the coal phase-out program adopted in 2015 breached its reasonable expectation of return on its investment.[97]

Recent investment tribunals have generally recognized that the FET standard should not be interpreted as freezing the host State's legal framework at the time of investment.[98] However, a key issue is how to strike a balance between protecting foreign investors' expectations of a stable investment environment and countries' sovereign right to change their regulations. Tribunals have considered the "radical" or "drastic" nature of the regulatory change in determining whether it breaches the stability requirement under the FET standard.[99]

For instance, the *Silver Ridge v. Italy* tribunal stated that "even in the absence of specific commitments, the fair and equitable treatment standard protects foreign investors from fundamental or radical modifications to the legal framework in which they made their investment."[100] Similarly, in *Eisner v. Spain*[101] the tribunal noted that the FET standard "protect[s] investors from a

92. Dolzer, *supra* note 25, at 105-06.

93. RWE v. Netherlands, *supra* note 8, ¶ 513.

94. *See id.*

95. *See* Westmoreland v. Canada Final Award, *supra* note 6, ¶¶ 94, 97 (Jan. 31, 2022).

96. *See id.* ¶¶ 75, 97.

97. *See id.* ¶¶ 78, 97.

98. Yulia Levashova, *Revisiting the FET Standard and the Right to Regulate in Times of Crisis: The Notion of Stability in an Assessment of Legitimate Expectations*, *in* INTERNATIONAL INVESTMENT LAW AND THE PANDEMIC 149 (Antonino Alì, Sondra Faccio, & Marco Pertile eds., 2025).

99. *Id.* at 149-50; Chen Yu, *Disentangling Legal Stability from Legitimate Expectations: Towards Greater Deference to Regulatory Changes in Renewable Energy Transition Policies in Investment Arbitration*, 24(1) WORLD TRADE REV. 101, 106 (2025).

100. Silver Ridge Power BV v. Italian Republic, ICSID Case No. ARB/15/37, Award of the Tribunal, ¶ 410 (Feb. 26, 2021).

101. Eiser Infrastructure Ltd. et al.v. Kingdom of Spain, ICSID Case No. ARB/13/36, Final Award (May 4, 2017).

fundamental change to the regulatory regime in a manner that does not take account of the circumstances of existing investments made in reliance on the prior regime."[102] The tribunal acknowledged that the FET standard does not mean that the host State's legal framework cannot evolve; rather, the FET standard requires that "regulatory regimes cannot be radically altered as applied to existing investments in ways that deprive investors who invested in reliance on those regimes of their investment's value."[103] In *El Paso v. Argentina*, the tribunal found that Argentina had breached the FET standard due to the cumulative effect of regulatory measures that were "a total alteration of the entire legal setup for foreign investments."[104] The tribunal stated that "Argentina went too far by completely dismantling the very legal framework constructed to attract investors."[105]

However, evaluating the fairness of a regulatory action based on the degree of change from existing regulation is inappropriate for coal phase-out, which necessitates "fundamental" and "radical" regulatory changes that inherently conflict with the stability requirement under the FET standard. This conflict has been reflected in recent cases where coal sector investors argued that coal phase-out measures amounted to radical changes that violate the FET standard. For instance, in *RWE v. Netherlands*, the claimants stated that they expected "reasonable changes and amendments in the legal frameworks," not radical alterations that would deprive investors of their investment's value in the host State.[106]

Moreover, the claimants stressed that the energy sector especially values the stability of the legal framework since energy investments are often planned for decades.[107] The claimants argued that they had relied on the message in the Coal Covenant and Energy Reports that "coal-plants are necessary until 2050 and their CO2 emission are regulated only by the ETS."[108] Additionally, by obtaining all relevant permits for their coal investments, claimants stated that they "did not expect a coal ban and had no need to."[109] Given both the general energy policies of the Netherlands at the time of investment and the attainment of all necessary permits, the claimants stressed that the enaction of the Coal Ban Law was such a "radical change" that it violates the FET standard.[110]

102. *Id.* ¶ 363.
103. *Id.* ¶ 382.
104. El Paso Energy Int'l Co. v. Argentine Republic, ICSID Case No. ARB/03/15, Award, ¶ 517 (Oct. 31, 2011).
105. *Id.*
106. *See* RWE v. Netherlands, *supra* note 8, ¶ 513.
107. *Id.* ¶ 515-16.
108. *Id.* ¶ 411.
109. *Id.* ¶ 520.
110. *See id.* ¶ 521-23.

Similarly, in *Uniper v. Netherlands*, the claimants argued that the Coal Ban Law breached the FET standard since it "fundamentally and radically" changed the existing regulatory framework.[111] The claimants also argued that the Coal Ban Law was a "radical departure" from previous policies.[112] They argued that

> successive Dutch Governments consistently, publicly and expressly encouraged and supported the Claimants' investment in MPP3. This was confirmed in meetings between the Ministry of Economic Affairs and the Claimants and also through numerous official policy documents and public statements. Moreover, the Respondent facilitated the Consortium Agreement in which it was known, from the outset, that the end-goal was the construction new [sic] coal-fired power plant. The Respondent also demonstrated support through accelerating the permit process and intervening to ensure the expansion of the necessary grid infrastructure.[113]

Moreover, foreign investors may argue that an "accelerated" phase-out schedule constitutes a radical change that undermines their expectations. For instance, in *Westmoreland v. Canada*, Westmoreland made its investments through acquisition of a number of coal mines in Alberta from 2013 to 2014.[114] Westmoreland pointed out that, before the acquisitions, in 2012, Canada enacted regulations to close down all coal-powered utilities within a fifty-year timeframe.[115] Westmoreland stated that based on such regulations it had expected, at the time of investment, a fifty-year lifespan of operation.[116] However, in 2015 the new Alberta government introduced the Climate Leadership Plan to expedite the coal phase-out process by eliminating all coal-fired power by 2030.[117] Westmoreland argued that this new plan accelerated the closure of its coal mines by twenty-five years, thereby violating its legitimate expectations.[118]

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111. Uniper v. Netherlands, *supra* note 8, ¶ 476.
112. *Id.* ¶ 480.
113. *Id.*
114. Westmoreland v. Canada Final Award, *supra* note 6, ¶ 5 (Jan. 31, 2022).
115. *Id.* ¶ 744.
116. *See id.* ¶ 75.
117. *Id.* ¶ 78. The change in government may result in policy change that adversely impacts foreign investors, leading to investment arbitration claims. *Westmoreland v. Canada* is one such example. Another example is *Thunderbird v. Mexico*, where the foreign investor claimed that a stricter enforcement of the Mexican gambling legislation after a change in leadership within the Mexican government, which resulted in the closure of the investor's gaming facilities, breached several clauses under the NAFTA, including the FET standard. The tribunal rejected the claims, finding that the enforcement of gambling law did not amount to a breach of the foreign investor's legitimate expectations. *See* Int'l Thunderbird Gaming Corp. v. United Mexican States, UNCITRAL, Arbitral Award, ¶ 166 (Jan. 26, 2006).
118. Westmoreland v. Canada Final Award, *supra* note 6, ¶ 189. The tribunal found no jurisdiction and did not analyze the merits of the case.

In sum, the current interpretation of the indirect expropriation clause and the FET clause aim to protect foreign investors from political risks such as expropriation and radical regulatory change. This framework makes coal phase-out measures vulnerable to violating investment treaties, as they necessarily form a radical change of legal framework and impact coal sector investors' fundamental interests. The next Part explores how a contextual interpretation of foreign investors' legitimate expectations can help reconcile this tension.

II. LEGITIMATE EXPECTATIONS OF FOREIGN INVESTORS IN CLIMATE TRANSITION

A. The Doctrine of Legitimate Expectations

Foreign investors usually consider two types of risks when making their investments: commercial risks and political risks. Commercial risks refer to inherent market risks such as price fluctuations, exchange rate changes, and competitive intensity, while political risks entail state intervention in the market, including legislative, administrative, and judicial actions that affect foreign investors' interests.[119] Political risks are governed and mitigated by international investment law, while commercial risks are to be borne by foreign investors.[120]

International investment law does not offer absolute protection against all political risks foreign investors face. Instead, it seeks to safeguard the "legitimate expectations" of investors at the time of their investment, preventing certain political actions that could undermine those expectations. The doctrine of legitimate expectations has been recognized as "a central concept in international investment law."[121] Although most treaties do not explicitly mention this doctrine, it has been widely applied in investment arbitration, particularly in interpreting the FET standard and, in some cases, in assessing indirect expropriation. The underlying rationale is that foreign investors should bear responsibility for their decision to invest in a particular country. Once an investment is made, the concern is that the host State might use its regulatory powers to harm those investments—especially in long-term projects, such as in the energy sector, which require substantial capital investment and typically take years to generate profits. Consequently, investment treaties provide legal

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119. DOLZER ET AL., *supra* note 35, at 28; RUDOLF DOLZER & CHRISTOPH SCHREUER, PRINCIPLES OF INTERNATIONAL INVESTMENT LAW 28 (Oxford University Press 2022); Carolina Moehlecke & Rachel L Wellhausen, *Political Risk and International Investment Law*, 25 ANN. REV. POLI. SCI. 485, 485 (2022); *see generally* Jason Webb Yackee, *Political Risk and International Investment Law*, 24 DUKE J. COMPAR. & INT'L L. 477, 477 (2013).

120. DOLZER ET AL., *supra* note 35, at 28; *see generally* Moehlecke & Wellhausen, *supra* note 119.

121. Jarrod Hepburn, *The Legal Justification for the Doctrine of Legitimate Expectations in International Investment Law*, 36.1 EUR. J. INT'L L. 43, 43 (2025).

assurances that the host State will not enact radical regulatory changes that fundamentally damage foreign investments.

Investment tribunals have widely acknowledged that the FET standard requires the protection of the foreign investor's legitimate expectations.[122] As stated by the tribunal in *Saluka v. Czech Republic*, the protection of the foreign investor's legitimate expectations is the "dominant element" of the FET standard.[123] Other tribunals have also considered the protection of legitimate expectations as "one of the major components"[124] or even "the most important function"[125] of the FET standard.

Generally, international investment law protects the legitimate expectations of foreign investors, which arise from two sources: first, the legal framework of the economic sector in which the foreign investor has invested, and second, any specific assurances provided by the host State that the foreign investor relied on when making the investment.[126] The legal framework includes not just the State's domestic legislation and executive documents, but also treaties and contractual undertakings.[127]

Moreover, some tribunals have also considered the legitimate expectations of foreign investors in the assessment of indirect expropriation. For instance, in *Tecmed v. Mexico*, the tribunal considered the foreign investors' legitimate expectations in the determination of whether the governmental measure constituted expropriation, noting that "upon making its investment, the Claimant had legitimate reasons to believe that the operation of the Landfill would extend over the long term."[128]

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122. Técnicas Medioambientales Tecmed, S.A. v. United Mexican States, ICSID Case No. ARB (AF)/00/2, Award, ¶ 154 (May 29, 2003) [hereinafter Técnicas Award]; Crystallex Int'l Corp. v. Bolivarian Republic of Venezuela, ICSID Case No. ARB(AF)/11/2, Award, ¶ 546 (Apr. 4, 2016).

123. Saluka Investments B.V. v. The Czech Republic, UNCITRAL, Partial Award, ¶ 302 (Mar. 17, 2006).

124. EDF (Services) Ltd. v. Romania, ICSID Case No. ARB/05/13, Award, ¶ 216 (Oct. 8, 2009).

125. Electrabel S.A. v. Republic of Hungary, ICSID Case No. ARB/07/19, Decision on Jurisdiction, Applicable Law and Liability, ¶ 7.75 (Nov. 30, 2012).

126. Caroline Henckels, *Justifying the Protection of Legitimate Expectations in International Investment Law: Legal Certainty and Arbitrary Conduct*, 38 ICSID REV. FOREIGN INV. L. J. (2023); Emmanuel T. Laryea, *Legitimate Expectations in Investment Treaty Law: Concept and Scope of Application*, HANDBOOK INT'L INV. L. & POL'Y (2020). *See also* DOLZER ET AL., *supra* note 35, at 208 (stating that the foreign investor's legitimate expectations "are based on the host State's legal framework and on any undertakings and representations made explicitly or implicitly by the host state").

127. DOLZER ET AL., *supra* note 35, at 209; *see also* Suez, Sociedad General de Aguas de Barcelona, S.A., et al. v. Argentine Republic, ICSID Case No. ARB/03/19, Decision on Liability, ¶ 222 (July 30, 2010) (stating that the foreign investor's legitimate expectations can be created by the host State's "laws, regulations, declared policies, and statements").

128. Técnicas Award, *supra* note 122, ¶ 149.

B. Legitimate Expectations of Foreign Investors in the Coal Sector

What should be the legitimate expectations of foreign investors in the climate transition era? Climate transition risks stemming from the shift to a low-carbon economy are a hybrid of both commercial and political risks.[129] These risks generally encompass three main components: regulatory changes (such as the introduction of carbon taxes or phase-out regulation), technological advancements, and shifts in consumer preferences.[130] Foreign investors are faced with both political and commercial risks arising from climate transition: On one hand, climate transition necessitates governmental intervention, with the dynamic and evolving world of climate governance leading to inevitable political risks from regulatory change. On the other hand, climate transition involves a structural transformation of the entire economy, which foreign investors should anticipate as a foreseeable commercial risk. The question is: During the climate transition era, how should international arbitral tribunals distinguish between the commercial risks that should be borne by foreign investors and the political risks that should be assumed by the host State?

1. The Challenges of Determining Coal Investors' Legitimate Expectations

International investment law assumes that foreign investors will exercise due diligence when investing and protect their legitimate expectations while recognizing the legal framework of the host State.[131] However, defining the scope of such legitimate expectations regarding climate transition is intricate. The host State may argue that foreign investors in the coal sector should have expectations of climate mitigation measures if, at the time of investment, the host State has already been a party to climate treaties such as the United Nations Framework Convention on Climate Change or the Paris Agreement. Nevertheless, it is difficult to prove that broad and flexible commitments under climate treaties can form a basis for legitimate expectations of foreign investors. By contrast, the foreign investor may rely more on the domestic framework and representations by government officials to generate expectations. This has been the case in *RWE v. Netherlands*, in which the claimants argued that the Coal Ban Law was unforeseeable at the time of their investment.[132] The claimants recognized that in previous jurisprudence, the legitimate expectations of foreign investors—at the time of investment—had been considered in the determination

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129. *See* Stefano Giglio, et al., *Climate Finance*, 13 ANN. REV. FIN. ECON. 15, 17 (2021).

130. *Id.* at 24; Moshe Syrquin, *Kuznets and Pasinetti on the Study of Structural Transformation: Never the Twain Shall Meet?*, 21(4) STRUCTURAL CHANGE & ECON. DYNAMICS, 248-257; Gregor Semieniuk et al., *Low-Carbon Transition Risks for Finance*, 12 WILEY INTERDISC. REVS.: CLIMATE CHANGE 678, 3 (2020).

131. Yulia Levashova, *Fair and Equitable Treatment and Investor's Due Diligence Under International Investment Law*, 67 NETH. INT'L L. REV. 233, 233-34 (2020).

132. RWE v. Netherlands, *supra* note 8, ¶ 485.

of indirect expropriation.[133] However, the claimants argued that they did not legitimately expect any form of coal ban at the time of investment, as they took into account a list of government documents that showed "a continuous line of explicit political promises" of the importance of coal plants to the Netherlands.[134]

Moreover, foreign investors have argued that the phase-out policy frustrates their expectations based on previous legal frameworks on coal regulation. For instance, in *RWE v. Netherlands*, the claimants argued that their expectations were based on the Netherlands Environmental Permitting Act, which granted them an environmental permit to operate a coal-fired plant.[135] The claimants argued that they had legitimate expectations that their coal-powered plants would remain operational and governed by the Netherlands Environmental Permitting Act.[136] They noted that they did not have reasons to expect that the permits would be withdrawn or invalidated for reasons other than those provided in the Netherlands Environmental Permitting Act, under which the permits were accorded.[137] Accordingly, the claimants argued that Netherlands had breached their legitimate expectations protected under the FET standard.[138]

Similarly, in *Uniper v. Netherlands*, the claimants argued that the Coal Ban Law frustrated their legitimate expectations at the time of investment.[139] The claimants acknowledged that the FET standard does not require a freeze of the host State's regulatory regime, but it requires the State to honor the investors' expectations and fulfill its commitments.[140]

In sum, the existing jurisprudence has mainly protected foreign investors' expectations derived from the host State's legal framework or government representations at the time of investment to protect foreign investors from future regulatory changes that are against their expectations.[141] However, some foreign

133. *Id.* ¶ 484.
134. *Id.* ¶ 485.
135. *Id.* ¶¶ 529-30.
136. *Id.* ¶ 529.
137. *Id.* ¶ 530.
138. *See id.* ¶ 534.
139. Uniper v. Netherlands, *supra* note 8, at¶ 464.
140. *Id.* ¶ 467. The claimants argued that the Coal Ban Law frustrated their legitimate expectations based on the following conduct by the Netherlands:

> (a) The Respondent actively and repeatedly encouraged investment in coal-fired power stations in order to address its concerns regarding security of supply and high energy prices in the Netherlands; (b) The Respondent recognised the decades-long lifetime of coal-fired power plants such as MPP3 and it confirmed that coal-fired power stations would be part of the energy mix until at least 2050; and (c) The Respondent granted MPP3 was granted all necessary permits, including the Environmental Permit which recognised the CO2-emissions-limiting features that MPP3 utilised in line with the DCMR Framework. (d) The Respondent repeatedly confirmed that CO2 emissions were to be governed by the EU ETS and not at the national level.

Id. ¶ 474.
141. *See supra* Part II.B.

investors have used this understanding of legitimate expectations to argue that they had no anticipation of coal phase-out regulations when they made their investments, thereby claiming that host States should compensate them for economic losses resulting from the transition away from coal. The following Subpart will demonstrate how a contextual analysis of the coal investors' legitimate expectations—considering the nature of climate change and the character of the regulatory environment—can address this issue.

2. A Contextual Interpretation of Legitimate Expectations Concerning Climate Transition

The climate transition introduces uncertainty and dynamism in regulation.[142] On one hand, foreign investors could generally expect that there will be an increase in climate mitigation and adaptation measures in the future. On the other hand, these investor expectations are often broad assumptions, as the specific timelines for coal phase-outs and the extent of policy flexibility in the transition phase remain uncertain. Moreover, climate policy making is highly politicized and shifts in government can result in changes to climate policies, further complicating the prediction of relevant risks at the time of investment. Thus, despite the global context of climate transition with countries making commitments under climate treaties, States' implementation of these pledges is variable, dynamic, and politically influenced, leading to uncertainty and unpredictability in how climate goals will be enforced.[143] Even the calculation of climate transition costs remains uncertain, posing challenges to the traditional assumption of investors' "rational expectations" when they make investments.[144]

Another undeniable context is that coal companies contribute significantly to climate change, which has prompted the development of phase-out regulations. Even if investments are made prior to a host State enacting climate mitigation policies, investors may have already formed expectations of future

142. Michał Krzykowski et al., *Principle of Reasonable and Legitimate Expectations in International Law as a Premise for Investments in the Energy Sector*, 21 INT'L ENVT'L AGREEMENTS: POL. L. & ECON. 75, 75 (2021).

143. *See* Lauri Peterson & Harro van Asselt, *Assessing Risks to the Implementation of NDCs Under the Paris Agreement* (2025), CLIMATE POL'Y, 1, 4-6 (investigating potential threats to the implementation of Nationally Determined Contributions (NDCs) across twenty-one countries and the E.U. and identifying multiple drivers of implementation failures including overly ambitious NDC pledges, weak institutional capacities, opposition by interest groups, policy inconsistency, and inadequate monitoring and enforcement abilities).

144. Giglio, *supra* note 129, at 21-22. The fossil fuel industries are particularly vulnerable to asset stranding, which results in the devaluation of their assets due to climate transition. *See* GASPARINI AND TUFANO, THE EVOLVING ACADEMIC FIELD OF CLIMATE FINANCE, HARV. BUS. SCH. (2023); Semieniuk et al., *supra* note 130, at 8; Caldecott et al., *Stranded Assets: Environmental Drivers, Societal Challenges, and Supervisory Responses*, 46 ANN. REV. ENV'T & RES. 417-447 (2021).

regulations aimed at reducing their environmental impact.[145] Thus, compensating foreign investors in the coal sector for losses stemming from phase-out measures might be against the polluter-pays principle.[146] It could also lead to a high regulatory burden for the host State and may create inequality between foreign and domestic investors, as only the former enjoys treaty-level protection. Moreover, this approach may give rise to moral hazard issues: Without the investment treaty protections discussed above, investors in fossil fuel industries might adjust their investments due to rising climate transition risks. However, offering complete compensation to fossil fuel investors could encourage them to maintain and possibly expand their investments.[147]

All these factors—the polluting role of coal investors and the transitional nature of climate regulation—should be considered as part of the broader context in which foreign investors form their expectations at the time of investment, even if such investments precede the host State's adoption of formal coal phase-out policies.

This contextual understanding of legitimate expectations is supported by existing investment arbitration jurisprudence. For example, tribunals have taken into account social and economic contexts when assessing the legitimacy of investors' expectations in transitional economies.[148] In *Genin v. Estonia*, the U.S. foreign investor argued that Estonia's revocation of its banking license

145. Recently released documents suggest that the coal industry has been aware of the climate change effects for over fifty years. *See* Peter Dockrill, *The Coal Industry Was Well Aware of Climate Change Predictions Over 50 Years Ago*, SCIENCEALERT (Nov. 26, 2019), https://www.sciencealert.com/coal-industry-knew-about-climate-change-in-the-60s-damning-revelations-show.

146. The polluter-pays principle states that those who cause environmental damage should bear the costs of managing and remedying that damage. For an analysis of the application of the polluter-pays principle at courts, see generally Suzanne Kingston, *The Polluter Pays Principle in EU Climate Law: An Effective Tool Before The Courts?*, 10 CLIMATE L. 1 (2020). In *RWE v. Netherlands*, the Netherlands took into account the polluter-pays principle when arguing that a transition period provided to coal investors (without other compensation) was sufficient to strike a balance between public and private interests. As stated by the Netherlands:

> In view of the foreseeability of CO2 reduction measures for the power plants as early as 2005, the 'polluter pays' principle, the possibility for the owners of the power plants to continue generating electricity using fuels other than coal and the generous transition periods offered by this bill, the cabinet believes that there is a 'fair balance' between the public interest served by this ban and the interest of the owners of the power plants affected by the regulation of their property. This bill therefore does not a priori provide for additional detriment compensation beyond the transitional periods already offered.

RWE v. Netherlands, *supra* note 8, ¶ 463.

147. For similar criticisms against Germany's compensation scheme for lignite companies, see EUROPEAN ENVIRONMENTAL BUREAU, CAN EUROPE AND GREENPEACE, LETTER TO THE EUROPEAN COMMISSION ON GERMAN STATE AID FOR COAL PHASE OUT (2020), https://eeb.org/wp-content/uploads/2020/09/EEB_GP_CAN-letter-to-Vestager-on-DE-state-aid-coalFIN2.pdf.

148. A transitional country is a nation undergoing a process of economic and political transformation from a centrally planned system to a market-oriented economy.

amounted to a violation of investment treaty standards.[149] In the award, the tribunal considered the transitionary state of Estonia:

> [T]he Tribunal considers it imperative to recall the particular context in which the dispute arose, namely, that of a renascent independent state, coming rapidly to grips with the reality of modern financial, commercial and banking practices and the emergence of state institutions responsible for overseeing and regulating areas of activity perhaps previously unknown. This is the context in which Claimants knowingly chose to invest in an Estonian financial institution. . . .[150]

In *Parkerings v. Lithuania*, the tribunal considered Lithuania's transitional status and noted that the foreign investor should have expected regulatory changes as a result of this transitional situation.[151] The tribunal stated that "it would have been foolish for a foreign investor in Lithuania to believe, at that time, that it would be proceeding on stable legal ground, as considerable changes in the Lithuanian political regime and economy were undergoing."[152] When examining whether Lithuania's amendment of the law constituted a frustration of the investor's legitimate expectations, the tribunal took into account the context of the Lithuania as a transitional country at the time of investment:

> In 1998, at the time of the Agreement, the political environment in Lithuania was characteristic of a country in transition from its past being part of the Soviet Union to candidate for the European Union membership. Thus, legislative changes, far from being unpredictable, were in fact to be regarded as likely. As any businessman would, the Claimant was aware of the risk that changes of laws would probably occur after the conclusion of the Agreement. The circumstances surrounding the decision to invest in Lithuania were certainly not an indication of stability of the legal environment. Therefore, in such a situation, no expectation that the laws would remain unchanged was legitimate . . . *By deciding to invest notwithstanding this possible instability, the Claimant took the business risk to be faced with changes of laws possibly or even likely to be detrimental to its investment. The Claimant could (and with hindsight should) have sought to protect its legitimate expectations by introducing into the investment agreement a stabilization clause or some other provision protecting it against unexpected and unwelcome changes.*[153]

The tribunal's statement implies that, without a stabilization clause, the foreign investor has acknowledged and agreed to the risk of regulatory changes

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149. Alex Genin, E. Credit Ltd., Inc. v. Republic of Estonia, ICSID Case No. ARB/99/2, Award ¶ 91 (June 25, 2001).

150. *Id.* ¶ 348.

151. Parkerings-Compagniet AS v. Republic of Lithuania, ICSID Case No. ARB/05/8, Award ¶ 306 (Sept. 11, 2007).

152. *Id.*

153. *Id.* ¶¶ 335-36 (emphasis added).

in a transitional setting. In assessing whether Lithuania had violated the investor's legitimate expectations by not disclosing the potential law amendments at the time of signing the investment agreement, the tribunal once more considered the transitional nature of the investment environment: "[T]he political landscape was undergoing changes during the Agreement negotiations, and the Claimant should have been aware that the legal framework was subject to unpredictability and potential evolution."[154]

Similarly, in *Lemire v. Ukraine*, U.S. businessman Joseph Charles Lemire, who invested in the Ukrainian radio broadcasting sector, initiated an investment arbitration case against Ukraine.[155] Lemire claimed that Ukraine improperly denied him radio broadcasting licenses and thus violated the bilateral investment treaty signed between the United States and Ukraine.[156] The tribunal acknowledged that:

> It must be recalled that when in 1995 Mr. Lemire made his first investment and acquired a controlling stake in Gala Radio, this was a small company in a nascent industry. Historically, before independence and political change, the radio industry in Ukraine had been in the hands of the State. In the mid 1990s the sector began to be privatized, a first Law on TV and Radio having been approved on December 21, 1993. *All these factors had a bearing on Claimant's legitimate expectations*.[157]

In sum, in *Genin v. Estonia*, *Parkerings v. Lithuania*, and *Lemire v. Ukraine*, the investment tribunals concluded that when foreign investors make an investment in a transitional economy, it is unreasonable for them to anticipate a stable and predictable environment, unless the investment is safeguarded by a stabilization clause. This principle can be extended to investors in the coal sector with one key adjustment: Unlike transitional economies that offer an uncertain domestic investment climate, climate change and the climate transition constitute a global context that influences investment expectations. Consequently, foreign investors in the coal sector should base their legitimate expectations on (1) the recognized polluting effects of coal on climate change and the polluter-pays principle,[158] and (2) the overarching global legal framework on climate

154. *Id.* ¶ 342.

155. Joseph Charles Lemire v. Ukraine, ICSID Case No. ARB/06/18, Decision on Jurisdiction and Liability, ¶ 33-37 (Jan. 14, 2010).

156. *Id.* ¶ 38-39.

157. *Id.* ¶ 266 (emphasis added).

158. The argument that investors should include coal's effects on climate change in their investment expectations is bolstered by the evidence that the industry was aware of coal's polluting effects (and took efforts to mislead regulators and the public about those effects) as early as 1966. *See* Dockrill, *supra* note 145; Élan Young, *Exxon Knew—and so did Coal*, GRIST (Nov. 29, 2019), https://grist.org/energy/exxon-knew-and-so-did-coal. Understanding the context that the coal industry was aware of coal's effects on climate change may suggest that investors' expectations that coal would continue to be promoted were, to some degree, illegitimate due to the industry's manipulation of the regulatory context.

transition, including both treaty-level commitments and domestic climate policies.

III. Reconciling Coal Phase-Out and Investment Protection through a Contextual Interpretation of Legitimate Expectations

The previous Parts illustrate how foreign investors can, and have, claimed coal phase-out measures as violations of investment treaties and propose a contextual understanding of coal investors' legitimate expectations. This Part proposes applying such contextual assessment of legitimate expectations in investment treaty standards. It submits that, absent an otherwise specific assurance to foreign investors, the adoption of a coal phase-out regulation will not constitute a violation of investment treaties as long as it is adopted in a non-discriminatory manner. This requires a two-step assessment: First, if the host State has provided explicit assurances in an agreement with foreign investors regarding the coal phase-out timeline and compensation, the host State should comply with those assurances. Second, in the absence of such assurances, the tribunal will assess whether the phase-out regulation is implemented in a non-discriminatory manner. If the host State has not provided explicit assurances and the phase out is non-discriminatory, the tribunal should determine that such regulation does not breach investment treaty standards.

This approach contributes to the existing jurisprudence by clarifying a balanced approach for examining coal phase-out regulation under investment treaties. It considers the legitimate expectations of foreign investors protected under investment treaties but adopts a narrow approach in safeguarding these expectations. The rationale for this narrow approach is that the legitimate expectations of foreign investors in the coal sector should be examined within the context of the climate transition. Additionally, this approach grants discretion to the host State in determining how to allocate transition costs between foreign investors and the host State as a whole, while also requiring that such allocation be conducted without discrimination against foreign investors.

A. Step 1: Protecting Foreign Investors' Legitimate Expectations Based on Specific Assurances

Investment tribunals should take into account the specific commitments made by the host State to the foreign investor that the investor relied on when making investment choices. For instance, a stabilization clause in the agreement between the foreign investor and the host State may ensure that any future regulatory changes do not harm the foreign investor's operations. Such specific assurances should form a basis of foreign investors' legitimate expectations to be protected under investment treaties.

It is essential for tribunals to distinguish between general assurances, such as statements made to the public at large, and specific commitments that are

expressly provided to foreign investors. Given the politicized nature of climate issues and their frequent appearance in public discourse, broad and unspecific statements lacking a contractual basis should not be considered as valid grounds for establishing foreign investors' legitimate expectations protected under investment treaties. Recent investment arbitration cases have shown examples where foreign investors have cited public statements as evidence that they were not expecting a ban on coal when they made their investments. For example, in both *RWE v. Netherlands* and *Uniper v. Netherlands*, the investors cited the Dutch government's public statements promoting coal power as the foundation of their expectations at the time of investment.[159]

In *RWE v. Netherlands*, the claimants argued that their expectations of no coal ban regulation were not only based on the legal framework at the time of investment but also were "reinforced in the light of numerous explicit representations."[160] The claimants listed a series of public statements, including the Energy Reports issued by the Netherlands government, as well as the Energy Agreement signed between the government and energy companies, to illustrate that the Dutch government was supporting the operation of coal-fired powerplants at the time of investment.[161]

Future investment tribunals should reject the legitimacy of expectations from coal sector investors that are solely based on general, public statements without a contractual nature. While some tribunals have acknowledged that representations made by the host State can give rise to legitimate expectations—such as in *Metalclad v. Mexico*, where government officials' assurances formed the basis for investor expectations—a different approach is warranted in the context of climate change.[162] Public statements on climate transition can be inconsistent or evolve over time. Allowing foreign investors to base their legitimate expectations solely on such statements could lead to an unreasonably broad and unpredictable scope of claims, undermining the balance between investor protections and States' regulatory authority.

B. Step 2: Deference to a Non-Discriminatory Phase-Out Regulation

Without an otherwise specific assurance accorded to the foreign investor, tribunals should find that coal phase-out measures do not violate investment treaty obligations, unless they are conducted in a discriminatory manner. This means: First, phase-out measures cannot be discriminatory against foreign investors because of their foreign nationality. Second, if a phase-out regulation

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159. RWE v. Netherlands, *supra* note 8, ¶ 531; Uniper v. Netherlands, *supra* note 8, ¶¶ 474, 101-123.

160. RWE v. Netherlands, *supra* note 8, ¶ 531.

161. *Id.*

162. Metalclad Corp. v. United Mexican States, ICSID Case No. ARB(AF)/97/1, Award, ¶ 107 (Aug. 30, 2000).

is not discriminatory, tribunals should accord deference to the host State in deciding the reasonability of the phase-out regulation.

1. Non-Discrimination of the Coal Phase-Out Regulation

Although host States have discretion in the implementation of climate obligations, their coal phase-out measures should not be designed in a way that is discriminatory to foreign investors. In other words, there should be no nationality-based discrimination under the phase-out measure in terms of the schedule or compensation scheme. Non-discrimination is a fundamental principle in international investment law, which is reflected in most investment treaties through three key provisions: (a) national treatment, which prohibits discrimination between foreign and domestic investments; (b) most-favored nation treatment, which prohibits discrimination between foreign investments and those from a third State; and (c) prohibition of discriminatory treatment, which generally bars any form of discriminatory treatment of foreign investments.[163]

Investment tribunals have recognized a three-step approach to assess these non-discrimination provisions: First, tribunals examine whether there is a comparable third country or domestic investment that is "in 'like circumstances'" to the foreign investment.[164] The national treatment provision would apply to comparable investments made by domestic actors, while the most-favored nation treatment provision would apply to investments from a third country.[165] The second step involves determining if the foreign investor has received "less favorable treatment" than the identified counterpart.[166] Finally, the third step entails assessing whether such less favorable treatment can be justified by a legitimate public interest rationale.[167]

I submit that, in the assessment of whether a phase-out measure was discriminatory, tribunals should consider whether the foreign investor has been discriminated against under the phase-out measure because of their nationality. For instance, if foreign investors are accorded less favorable treatment under the phase-out regime as compared to domestic investors or investors from another third country in like circumstances, the phase-out regime should be deemed discriminatory and cannot be justified under investment treaties.[168] On the other

163. ANDREW PAUL NEWCOMBE & LLUÍS PARADELL, LAW AND PRACTICE OF INVESTMENT TREATIES: STANDARDS OF TREATMENT 147-50 (2009).

164. DOLZER & SCHREUER, *supra* note 35, at 254-56.

165. *See id.* at 249, 253.

166. *Id.* at 254, 256-9.

167. *Id.* at 259-61 (noting that tribunals have considered various grounds as legitimate to justify differential treatments, such as subsidies for promoting national policies and local production requirements for governmental projects).

168. For instance, in previous investment arbitration cases investment tribunals have assessed whether environmental regulation violated the non-discrimination standards such as national treatment

hand, a differentiation between investors based on rational grounds other than nationality should be justified and not deemed as discrimination.

For instance, *Westmoreland v. Canada* concerned a differentiation under the Coal Phase-Out Plan based on economic sector rather than nationality. In this case, Alberta signed Off-Coal Agreements with the three companies to make transition payments.[169] These payments were to be made over the course of a fourteen-year period, totaling CAD$ 1.36 billion.[170] The payments were subject to conditions including minimum annual investment requirement and "a commitment to (*i*) continue generating electricity or otherwise participate in the Albertan electricity market and (*ii*) cease emissions from the six generating units by 2030."[171] Moreover, the three Alberta companies agreed to waive any claims regarding this coal phase-out.[172] However, the transition payments were not made to a U.S. company whose assets were later transferred to Westmoreland.[173] Canada explained that "this is because the Transition Payments were made in respect of capital at risk of stranding relating to affected coal-fired generation units and not in respect of any interest in any coal mine, coal mining not being the object of Alberta's emissions reduction policy."[174] However, Westmoreland claimed that the different treatment to it as compared to the three Alberta companies had violated the national treatment clause and the FET clause of the NAFTA.[175] The tribunal dismissed the claim in the jurisdiction phase, finding that Westmoreland did not have standing to bring the claim.[176] However, a future tribunal in a similar case should find the phase-out measure to be non-discriminatory since the differentiation is not based on nationality but rather based on the investors' sectors, i.e., between the coal mining companies and the coal-fired generation units.

2. Deference to the Host State in Assessing the Reasonability of the Phase-Out Regulation

Unlike the discrimination assessment, investment tribunals should accord deference to host States in deciding the reasonability of coal phase-out regulation. Climate transition measures usually involve highly controversial and complicated distributive justice problems, including how to achieve social justice by protecting the rights of vulnerable people from climate impacts, and

or most-favored nation treatment clauses. *See generally* Ying Zhu, *Environmental Discrimination in International Investment Law*, 51 N.Y.U. J. INT'L L. & POL'Y 385 (2018).

169. Westmoreland v. Canada Final Award, *supra* note 6, ¶¶ 80-81.

170. *Id.* ¶ 81.

171. *Id.*

172. *Id.*

173. *Id.* ¶¶ 82-90.

174. *Id.* ¶ 82.

175. *See id.* ¶¶ 82, 85, 92.

176. *Id.* ¶ 252.

how to achieve an equitable distribution of the benefits and burdens of climate transition in society.[177] Governments are commonly faced with the task of compensating actors who bear the costs of coal phase-out, in order to enhance the socio-political feasibility of energy transition.[178] A recent survey shows that more than half of countries that have made coal phase-out commitments have "just transition" policies that compensate coal-dependent regions, companies, and workers.[179] Those just transition policies can play an important role in determining the reasonability of new regulations, even though the policies vary among countries regarding the source and amount of compensation, as well as the affected actors to be compensated.[180]

In recent investment arbitration cases, the host States commonly argued that they had made a fair balance among the interests of actors affected by the phasing out of coal. For instance, in *Westmoreland v. Canada*, Canada stated that its coal phase-out plan was made based on three guiding principles: "(*i*) electric system reliability; (*ii*) reasonable stability and electricity prices for consumers and businesses; and (*iii*) investors' confidence in Alberta by not unnecessarily stranding capital and ensuring that workers, communities, and affected companies were treated fairly."[181] In *RWE v. Netherlands*, the Netherlands insisted that it had made a "fair balance" between public interests and coal-fired plant owners' interests by taking into account "the foreseeability of CO2 reduction measures for the power plants as early as 2005, the 'polluter pays' principle, the possibility for the owners of the power plants to continue generating electricity using fuels other than coal and the generous transition periods offered by this bill."[182]

In assessing the reasonability of coal phase-out measures, investment tribunals should preserve host States' regulatory space in designing a just transition mechanism without second-guessing the reasonability of the coal phase-out scheme. As stated in Part II, host States may face difficulties in justifying the effectiveness of the phase-out measures in achieving global climate goals due to the potential carbon leakage problem.[183] For instance, in *RWE v. Netherlands*, the claimants argued that the coal ban was "not suitable" to achieve its policy objective of the "required CO2 reduction."[184] This was because there

177. For a review of climate justice, see generally David Schlosberg & Lisette B Collins, *From Environmental to Climate Justice: Climate Change and the Discourse of Environmental Justice*, 5 WILEY INTERDISC. REVS.: CLIMATE CHANGE 359 (2014); Stephen M Gardiner, *Climate Justice*, THE OXFORD HANDBOOK OF CLIMATE CHANGE AND SOCIETY (2011).

178. Lola Nacke et al., *Compensating Affected Parties Necessary for Rapid Coal Phase-Out but Expensive if Extended to Major Emitters*, 15 NATURE COMMC'NS 3742, 1 (2023).

179. *Id.*

180. *Id.* at 3.

181. Westmoreland v. Canada Final Award, *supra* note 6, ¶ 79.

182. RWE v. Netherlands, *supra* note 8, ¶ 463.

183. *See supra* Part II.A.2.

184. RWE v. Netherlands, *supra* note 8, ¶ 444.

would be a "carbon leakage effect," which prevents the ban from achieving its reductions goals.[185] The claimants argued that this effect had been acknowledged by the Netherlands government since "[t]he studies commissioned by the Government in 2016 showed that the CO2-reductions in the Netherlands would lead only to 50% net reductions on an Europe-wide level, i.e. that approx. 50% of the saved emissions would be leaked to other EU member states."[186] Considering the competence and expertise of investment tribunals,[187] it is doubtful that they have the ability to play an appropriate role in deciding the effectiveness of the phase-out measure of the host States, and even if so, they should not play this role of second-guessing the reasonability of the phase-out measure.

Investment tribunals should also accord deference to host States' judgement on the proportionality of coal phase-out measures. The existence of multiple alternative methods for achieving climate objectives such as the ETS regime or CCS should not automatically negate the necessity or proportionality of a coal phase-out strategy. For instance, in *RWE v. Netherlands*, the claimants argued that they were disproportionally affected by the Coal Ban Law.[188] The claimants argued that the Coal Ban Law was "not necessary" to achieve the emission reductions goals, since there are "less drastic but more cost-efficient" alternatives (such as the strengthening of the ETS system) to achieve the same goal.[189] The claimants further argued that the Coal Ban Law was "grossly excessive and unduly burdensome" for them since the ban of coal firing was absolute, without considering how much CO2 would be emitted by the claimants and without taking into account whether the claimants would install CCS by 2030 to capture CO2.[190] In response to arguments like these, an investment tribunal should respect the host State's regulatory authority and conclude that the State itself should assess the necessity of the coal phase-out measure, rather than being subject to second-guessing by the tribunal.

In conclusion, a non-discriminatory phase-out measure that does not frustrate specific assurances a host State makes to a foreign investor should not violate the indirect expropriation and FET standards. This assessment does not include a reasonability or proportionality test, so as to provide deference to the host State's distributive judgments in climate regulation. In this way, investment

185. *Id.*

186. *Id.*

187. *See* Caroline Henckels, *Balancing Investment Protection and the Public Interest: The Role of the Standard of Review and the Importance of Deference in Investor-State Arbitration*, 4 J. INT'L DISP. SETTLEMENT 197, 210 (2013).

188. RWE v. Netherlands, *supra* note 8, ¶ 442.

189. *Id.* ¶¶ 445-46.

190. *Id.* ¶¶ 449-50.

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tribunals can strike a balance between foreign investors' economic interests and a host State's climate objectives, with due regard to the character of coal phase-out regulation.

CONCLUSION

Designing regulations to phase out coal raises distributive justice issues that require States to strike a fair balance among various stakeholders' interests. When foreign investors are affected by coal phase-out plans the situation becomes more complex, as host States must balance climate objectives and foreign investors' rights protected by investment treaties. International investment law aims to minimize political risks for foreign investors arising from regulatory changes in host States. However, this objective inherently conflicts with the demands of climate transition, which necessitates a fundamental restructuring of the economy. This leads to a tension between the host States' phase-out measures and two investment treaty obligations: indirect expropriation and the FET standard.

The Article proposes that tribunals can resolve this tension through a contextual examination of foreign investors' legitimate expectations in the transitional environment and suggests a two-step methodology to be adopted in future investment arbitration cases to harmonize climate and investment interests. First, host States should comply with specific commitments made to foreign investors regarding their plans to continue coal investments. Second, in the absence of such commitments, host States' phase-out measures should not be deemed a violation of investment treaty obligations unless they discriminate against foreign investors. This approach assists tribunals in balancing climate objectives with investors' rights, while also ensuring adequate regulatory space for effective climate transition.