ESG in BITs (Part I): Why ESG Provisions in Recent International Investment Treaties Matter

In Dispute
Client Advisories

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Oct. 2, 2025 – This is the first of three entries in Hughes Hubbard's "In Dispute" series in which we will examine how some recent bilateral investment treaties (BITs) are incorporating and addressing environmental, social and governance (ESG) objectives. This might seem an odd topic, particularly to readers from the United States, where ESG has seemingly fallen out of favor in recent years. At the international level, however, ESG remains a priority for many governments. ESG provisions in BITs and other investment treaties are not only becoming increasingly prevalent, but they also have the power to permanently reshape investor-state arbitration.

Investor-state arbitration has attracted scrutiny in recent years from critics accusing the process of having been used to thwart global efforts to advance ESG goals. A July 2023 report from the UN special rapporteur on human rights and the environment accused the process of being "a major obstacle to the urgent actions needed to address the planetary environmental and human rights crises." This came less than a year after a September 2022 report from the UN Conference on Trade & Development analyzed a series of investor-state arbitration cases involving state measures relating to climate action and concluded that "[t]he risk of investor-[s]tate dispute settlement … being used to challenge climate policies is a major concern."

This concern appears to be more than theoretical. State officials have asserted that investor-state arbitration has had a chilling effect on their environmental regulations. For example, the climate ministers from both Denmark and New Zealand have publicly told reporters "that the threat of investor-state lawsuits has prevented their governments from being more ambitious in their climate policies." Judge Sarah Cleveland of the International Court of Justice (ICJ) also noted this concern about the potential "regulatory chill" that international investment agreements may have in her declaration appended to the ICJ's July 2025 Advisory Opinion on states' obligations concerning climate change.

Investors have two primary responses to these arguments about the chilling effect of investor-state arbitration. First, renewable energy investors say that investor-state arbitration is a tool that they can turn to if states renege on economic environmental measures, pursuant to which foreign investors make renewable energy investments in the state. Perhaps the most prominent examples are cases, such as NextEra Energy Global Holdings B.V. v. Kingdom of Spain, that were brought by renewable energy investors against the Kingdom of Spain seeking compensation for alleged losses incurred as a result of Spain's modification of its regulations and economic incentives for attracting solar energy projects to be built in Spain.

Second, more traditional investors argue that states could invoke ESG principles as a pretext for interfering with or expropriating foreign investments, pointing to past arbitration cases. For instance, in 2003, an International Centre for Settlement of Investment Disputes (ICSID) tribunal issued an award in Tecmed v. Mexico which stated that "even if [a state's regulations] are beneficial to society as a whole — such as environmental protection," such societal benefit cannot justify nonpayment of compensation to foreign investors whose investments are negatively impacted by such regulation, "particularly if the negative economic impact of such actions on the financial position of the investor is sufficient to neutralize in full the value or economic or commercial use of its investment without receiving any compensation whatsoever." (¶ 121). Similarly, in 2000, an ICSID tribunal put the issue even more bluntly in the case of Compañía del Desarrollo de Santa Elena, S.A. v. Costa Rica by stating, "Expropriatory environmental measures — no matter how laudable and beneficial to society as a whole — are … similar to any other expropriatory measures that a state may take in order to implement its policies: [W]here property is expropriated, even for environmental purposes, whether domestic or international, the state's obligation to pay compensation remains." (¶ 72).

Other tribunals have come to opposite conclusions. Urbaser S.A. v. Argentine Republic and are just two examples of cases in which arbitral tribunals rejected claims from foreign investors relating to the impact of the states' environmental measures on their investments. There is, therefore, an emerging need to examine the tension between the right of the states to regulate within their territories to achieve ESG goals and affording foreign investors the assurances and protections needed to attract investment.

States entering into new BITs in the past decade have begun to incorporate ESG principles into the text of those agreements. The first such treaty to do so was the 2016 Morocco-Nigeria BIT, Article 13 of which explicitly recognized that nothing in the agreement would prevent either signatory state from "adopting, maintaining or enforcing, in a non-discriminatory manner, any measure … that [the state] considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental and social concerns." Since 2016, new BITs have continued to emphasize the right of states to regulate within their territories to achieve ESG goals. Such ESG clauses are not only being put into new BITs, they are also being inserted into revised versions of older BITs. In July, the Inter-American Court on Human Rights issued an Advisory Opinion that urged states to "review their existing trade and investment agreements and also settlement mechanisms for litigation between investors and [s]tates to ensure they do not limit or restrict efforts relating to climate change and human rights." (¶ 351).

In the next two parts of the "In Dispute" series, we will examine how states are working to strike that balance through their adoption of ESG provisions in recent BITs. We will be specifically examining three BITs signed in the past year, all of which contain multiple provisions that specifically aim to further ESG goals: the Georgia-Hungary BIT, the Japan-Zambia BIT and the New Zealand-United Arab Emirates (UAE) BIT. Examining these new BITs, we will see that the common goal of all these provisions is to lessen the risk that investor-state arbitration will be used to undermine legitimate ESG goals while simultaneously ensuring that foreign investment is adequately protected.

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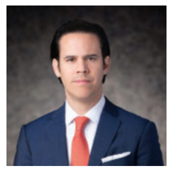

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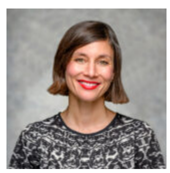

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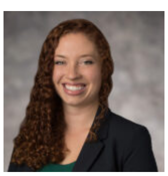

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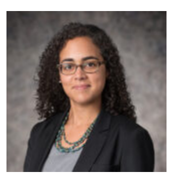

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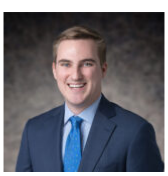

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