



# VON WOBESER

E S G   A R T I C L E S

## The role of arbitration in ESG disputes

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### Introduction

The Paris Agreement on Climate Change adopted in 2015 gave new impetus to the growing interest of the public agenda to ensure environmental and human rights protection, and intensified the discussion on corporate social responsibility in achieving this goal.

There has been a notable increase in disputes with ESG (Environmental, Social and Governance) components in this global context. For example, just in relation to the environmental dimension of ESG, from 2015 to date, more than 1,000 lawsuits that relate to climate change in different jurisdictions have been recorded.<sup>1</sup>

For decades, arbitration has been the principal means of resolving international commercial and investment disputes, and therefore, the incorporation

of ESG elements in international business agreements has been reflected in arbitration disputes deriving therefrom. There are important precedents in investment arbitration where the compliance with environmental laws or human rights has been a material part of the dispute.<sup>2</sup>

Although with different nuances, the ESG dimensions are equally relevant in commercial arbitrations. The public scrutiny of business activity, and the desired *social license to operate* as a variable to consider for business success, have led companies to incorporate ESG commitments in their commercial contracts. These range from giving specific representations and warranties that ensure the contracting party complies with, for example, the applicable environmental

<sup>1</sup> Polly Botsford, *The rising tide of climate litigation*, *International Bar Association*, July 12, 2021, available at: [https://www.ibanet.org/The-rising-tide-of-climate-litigation?sap-outbound-id=25C69206F11AFDFABC3C85C45B1968B44D3F4C0C&utm\\_source=SAPHybris&utm\\_medium=email&utm\\_campaign=234&utm\\_term=Global%20Insight%20Aug%2FSept%202021\\_The%20rising%20tide%20of%20climate%20litigation&utm\\_content=EN](https://www.ibanet.org/The-rising-tide-of-climate-litigation?sap-outbound-id=25C69206F11AFDFABC3C85C45B1968B44D3F4C0C&utm_source=SAPHybris&utm_medium=email&utm_campaign=234&utm_term=Global%20Insight%20Aug%2FSept%202021_The%20rising%20tide%20of%20climate%20litigation&utm_content=EN)

<sup>2</sup> See for example: SCC Arbitration V2013/153 *Isolux Infrastructure Netherlands, B.V. v/ Kingdom of Spain*, Award, July 17, 2016; SCC Arbitration Case No. V 062/2012, *Charanne B.V., and Construction Investments v/ Kingdom of Spain*, January 21, 2016. In these two cases, the investors sued Spain for revoking regulatory measures that incentivized investment in renewable energies, under which the claimants had made their investment; ICSID Case No. ARB/07/26, *Urbaser S.A. and Consorcio de Aguas Bilbao Bizkaia, Bilbao Biskaia Ur Partzuergoa v/ Argentina*, December 8, 2016, where Argentina filed a counterclaim against the investor alleging that the contractual breach by the investor also amounted to a violation of the human right to water and health.

and labor regulations, to agreeing to due diligence obligations concerning human rights that allow the identification and remediation of the impact of their activities.

## The role of arbitration in ESG disputes

Practice shows that many disputes relevant to ESG are dealt with through arbitration. The 2020 Annual Report of Statistics on Dispute Resolution of the International Chamber of Commerce (ICC) (*ICC Dispute Resolution 2020 Statistics*), published in 2021, identified that construction, engineering and energy disputes represent, historically, the highest number of ICC cases, reaching 38% of all the new cases registered in 2021.<sup>3</sup> These areas are, by their nature, crucial to national policies to combat climate change and to guarantee environmental protection and human rights, thus confirming the natural existence of arbitrations with ESG components.

The question is whether international arbitration, its rules and principles are indeed appropriate to resolve ESG disputes – whose dimensions are as varied and wide-ranging as climate change itself – and, if so, why.

## Arbitration: the right process for ESG disputes?

The procedural flexibility, the high levels of specialization of the arbitrators and the possibility of executing the awards in practically any country in the world under the New York Convention are some of the attributes of arbitration that make it an attractive and effective method for resolving conflicts, including ESG disputes.

These qualities allow the parties in the arbitration to set the rules that best meet their case needs, ranging from establishing the times for presenting the parties'

memorials to creating rules for presenting evidence, requesting documents and participating in hearings. In addition, the parties also play a vital role in the designation of arbitrators, who are experts in the matters at dispute and whose education and experience allow them to fully understand highly specialized and technically complex arguments and evidence.

Other characteristics of the rules of arbitration particularly relevant for conflicts with ESG components are: the possibility of obtaining interim measures before the constitution of the arbitral tribunal or during the arbitration, which are especially relevant in the case of imminent or irreversible environmental damage, or of serious violations of human rights,<sup>4</sup> and the possibility for the arbitrators to hear third parties during the proceeding (*amicus curiae*),<sup>5</sup> which, if agreed by the parties, enables the participation, for example, of civil associations that have played a crucial role in tackling climate change, in promoting environmental and human rights protection, and in denouncing corporate practices that threaten them. Thus, the multidisciplinary nature of the ESG disputes and their particular needs can be accommodated in the flexible and sophisticated arbitral proceeding.

The international community has continued to drive the evolution of the arbitral proceeding toward standards specifically contemplated for addressing the particular needs of these types of disputes. For example, in 2014, the UNCITRAL Rules on Transparency in Treaty-Based Investor-State Arbitrations entered into force to encourage higher standards of transparency

<sup>3</sup> *ICC Dispute Resolution 2020 Statistics*, 2021, p.17, available at: <https://iccwbo.org/publication/icc-dispute-resolution-statistics-2020/>

<sup>4</sup> See, for example, ICC Rules of Arbitration, 2017, article 28 and article 29; London Court of International Arbitration (LCIA) Arbitration Rules, 2020, articles 9B and 25; Singapore International Arbitration Centre (SIAC) Arbitration Rules, 2016, article 30; Hong Kong International Arbitration Centre Arbitration Rules (HKIAC), 2018, article 23; American Arbitration Association (AAA), rules 37 and 38.

<sup>5</sup> *ICC Commission Report. Resolving Climate Change Related Disputes through Arbitration and ADR*, November 2019, \$5.80. See also: International Centre for Settlement of Investment Disputes (ICSID) Arbitration Rules, 2006, rule 37; Singapore International Arbitration Centre Investment Arbitration Rules, 2017, rule 29.

in investment arbitrations.<sup>6</sup> Other efforts equally valuable for establishing models and best practices in arbitrations with ESG components are the Report of the ICC Task Force on Arbitration in Climate Change Related Disputes; the PCA Optional Rules for Arbitration of Disputes Relating to the Environment and/or Natural Resources; and The Hague Rules on Business and Human Rights Arbitration.

Despite the advantages of arbitration as a means of resolving ESG disputes, there are also criticisms of its suitability. For example, some authors point to a potential imbalance of resources between the parties that may be implied in ESG disputes in investment arbitrations (e.g., multinationals vs. governments),<sup>7</sup> and to a lack of adequate standards of transparency in arbitration proceedings – primarily commercial – that involve the public interest as shortcomings of the arbitral proceeding,<sup>8</sup> which in their view render it inadequate for resolving ESG disputes.<sup>9</sup>

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6 See, for example, article 3 of the rules, which contains a presumption in favor of the publication of the parties' briefs and the decision of the tribunal.

7 For example, according to figures of Global Justice Now, in 2017, 157 out of the 200 principal economic entities by revenue were companies and not states. According to these figures, corporations such as Walmart, Apple and Shell accumulate more wealth than countries such as Russia, Belgium or Sweden. See Global Justice Now, October 17, 2018, available at: <https://www.globaljustice.org.uk/news/69-richest-100-entities-planet-are-corporations-not-governments-figures-show/>; see also: Joe Myers, *How do the world's biggest companies compare to the biggest economies?*, *World Economic Forum*, October 19, 2016, available at: <https://www.weforum.org/agenda/2016/10/corporations-not-countries-dominate-the-list-of-the-world-s-biggest-economic-entities>

8 For example, in commercial arbitrations where state companies participate –with public funds– any of the parties can request the arbitral tribunal to issue orders on the confidentiality of the proceeding and on any matter related to the arbitration (e.g. article 22 of the ICC Rules of Arbitration, see also article 1(4) of Appendix II – Internal Rules of the International Court of Arbitration). In practice, a request is generally presented by the private parties in these proceedings, causing that the information on the existence and the reasoning behind such proceedings are confidential and, therefore, unknown to the general public. This means that only the parties to the dispute may access documents and evidence filed during the arbitration, thus limiting access to other users to these precedents.

9 Herbert Smith Freehills, *The Rising Importance of ESG and*

Regarding transparency standards in commercial arbitrations, recent efforts of arbitral institutions (such as the ICC) to establish presumptions in favor of the publication of information on the composition of the arbitral tribunal and arbitral awards lead one to question whether such criticism is still valid.<sup>10</sup>

## Conclusion

The growing importance of doing business in accordance with ESG principles and the traditional and widespread use of arbitration as a means of international dispute resolution augur a considerable increase in the number of arbitrations on ESG matters in the coming years.

Hence the importance of arbitration as a means for resolving these disputes, and of strengthening this mechanism to balance the needs of the parties and interests involved, so as to increase the legitimacy of the processes and decisions. This is the goal that, for several years, the international community has been pursuing, achieving important results, such as those mentioned above.

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*its Impact on International Arbitration*, July 27, 2021, available at: <https://www.herbertsmithfreehills.com/latest-thinking/the-rising-importance-of-esg-and-its-impact-on-international-arbitration>.

10 For example, although the most recent *Note to Parties and Arbitral Tribunal on the Conduct of Arbitration Under the ICC Rules of Arbitration*, published in January 2021, recognizes the right of the parties to object to the publication of decisions, documents or awards at any time prior to their publication, and to access information on the composition of the tribunal, it now contains a default rule of publication and dissemination of information, unless the parties object (see paragraphs 50 to 64).

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