Article

Rockhopper v. Italy and the Tension between ISDS and Climate Policy

A Missed Moment of Truth?

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On 23 August 2022, a Tribunal constituted under the auspices of the Energy Charter Treaty (ECT) handed down a long-awaited Award in the case of *Rockhopper v. Italy*. The investor's press release in the aftermath of the Award, announcing that Italy had lost the case, sparked a number of outraged reactions (e.g. here, here, and here). Broadly speaking, these comments saw the case as confirming the expectations that investor-State dispute settlement (ISDS) is set to drive up the costs for States of the energy transition – a reality denounced by several contributions (e.g. here and here), and recently also acknowledged by the Intergovernmental Panel on Climate Change (IPCC). The ECT, in particular, has attracted much criticism. *Inter alia*, the ECT has been the target of a high-profile initiative calling for its termination; of a controversial "modernisation" process aiming at assuaging those fears; and of several withdrawals of individual Parties, reflecting a widespread perception that the modernisation process led to unsatisfactory outcomes.

With the Award now public, it can be more thoroughly assessed to what extent *Rockhopper* can inform our understanding of how climate policy will be addressed by ISDS. The present blogpost's main submission is that, in light of the Tribunal's chosen doctrinal construction and of Italy's litigation strategy, *Rockhopper* actually does not elucidate this aspect at all. While in *Rockhopper* this undeniably resulted in the regulatory space for environmental policy being curtailed, it deprived the Award of the precedential value which it was thought it would have.

The Background to the Dispute and the Award

Although the dispute's background and the Award's main tenets have been extensively reported already, a concise summary seems apposite for present purposes. Two companies obtained in 2005 a permit from the competent Italian Ministry to explore the marine site of "Ombrina Mare", close to the shores of the Italian Region, Abruzzo. In December 2008, after an oil reservoir was confirmed to lie in the site, the companies applied for an exploitation concession. This request met with fierce opposition from the local community, on mixed environmental grounds which will be addressed below. Local protests successfully turned the conflict into a national one, leading the Italian government, in 2010, to put on halt, by means of a legislative decree, all oil drilling activities within 5 nautical miles (nm) from the Italian baselines. At this point, the extent to which such ban would also apply to pending applications (including that for the Ombrina Mare site) was unclear. Therefore, a new government passed down a new legislative decree in 2012. It was so clarified that, whereas the ban on drillings was now extended up to 12 nm from Italy's baselines, pending applications were exempted therefrom. The Ombrina Mare application was thus resumed, sparking a new wave of protests in Abruzzo. Those protests successfully established ties with similar movements in other parts of Italy. The process culminated in a request by 10 Italian Regions, in July 2015, to hold a referendum aiming, *inter alia*, at making the ban applicable also to pending applications. In an attempt at de-escalating the conflict, the government had Parliament adopting a statute in December 2015, which indeed repealed the exception for pending proceedings.

Against this convoluted legal background, the UK company, Rockhopper, had acquired the applicant companies in 2014. In August 2015 the Ministry found, pursuant to an environmental impact assessment

(EIA) conducted by Rockhopper, that the relevant environmental provisions had been complied with. The companies then applied for the final exploitation authorisation to be granted, but the Ministry failed to act over the subsequent months. In January 2016, the Ministry found the exploitation of the site to be prohibited, in light of the December 2015 extension of the ban to pending applications. The Ministry hence finally rejected Rockhopper's application.

Rockhopper thus filed an ECT claim, alleging that Italy breached a number of the rights accruing to it under the ECT. In the Award, the Tribunal found that Italy had expropriated Rockhopper's investment without compensation, thus deeming it unnecessary to decide the other claims (para. 200). The Tribunal first established that Rockhopper's purchase of controlling shares in the applicant companies qualified as an "investment" under the ECT (para. 116). It then went on to find that, under Italian law, the approval of Rockhopper's EIA in August 2015 bestowed on Rockhopper a right to be granted the final exploitation permit, which had been "wiped out" by the rejection of the application in January 2016 (para. 169). Italy timidly tried to argue that no expropriation could be carried out in relation to an activity which had not actually started yet – an argument with which the Tribunal was unimpressed, confirming that the "wiping out" of the entitlement to the concession was, in itself, expropriatory (paras. 194-196). Italy thus argued that the prohibition on drilling oil close to the coast, rooted in the precautionary principle, engaged the police powers doctrine; accordingly, the measure could not be a compensable taking (para. 189). The Tribunal maintained, however, that Italy could no longer rely on the precautionary principle after the Ministry had approved Rockhopper's EIA in August 2015 (paras. 152-154). Consequently, "[t]he more likely reason" for the rejection of Rockhopper's application, far from lying in environmental concerns, "[were] the political and civic engagements" discussed above (para. 198). Thus ruling out the applicability of the police powers doctrine, the Tribunal found a breach of the ECT's protection against expropriation, no compensation having been paid to Rockhopper (para. 199).

The Tribunal's (and Italy's) Analytical Framework: Watering Down the Conflict between ISDS and Climate Policy?

The decision in *Rockhopper* was much awaited because it was seen as a potential indicator of how ISDS would be used to respond to a new wave of climate policy measures by States. In a world set to extract more than twice the amount of fossil fuels which would be compatible with the Paris Agreement's temperature objectives, reduction in the production of fossil fuels itself is seen as a crucial policy. Yet, Rockhopper's ECT claim stands for the proposition that the fossil industry is likely to avail itself of ISDS to challenge such measures.

The Tribunal in *Rockhopper* seems to have been aware of the high expectations placed upon it. The first twelve paragraphs of the Award do indeed build a careful narrative on the issue. For instance, the Award underlines that:

> "[t]he Tribunal appreciates and is acutely sensitive to the fact that there are strongly-held environmental, civic and political views about offshore production in *Ombrina Mare*. However, the outcome of this case passes no judgment whatsoever on the legitimacy or validity of those views" (para. 10).

This long disclaimer appears in line with recent trends in investment arbitration, which seems to increasingly acknowledge, at least in the construction of reasoning discourses, the principled legitimacy of environmental policy. However, the final Award seems to be radically oblivious of the environmental dimension of Italy's conduct. As recalled above, the Tribunal dismissed the police powers defence by arguing that the rejection of Rockhopper's application was due not to environmental concerns, but to the political contentiousness surrounding the issue. In so doing, the Tribunal artificially neglects the basic point that the project was politically contentious *precisely because* of its environmental implications. When reconstructing the rationale for the cancellation of the exemption of pending applications from the ban, the Tribunal examined the measure's legislative history, and conceded that environmental concerns underlay the reform (paras. 109-110). This was indeed reflected in the relevant statute's language, reasoning that the ban on hydrocarbons was brought about "[f]or the purposes of protecting the

environment and the ecosystem" (para. 100). However, the Tribunal subsequently suggested that the government's willingness to prevent the referendum from taking place actually evidenced that the case was to be understood exclusively as a conflict between the central government and Italian Regions (paras. 111-114). Such reframing of the reform's rationale seems problematic. As the Tribunal put it, "the political grounds for [the referendum] were resolved through parliamentary action at a central level" (para. 114). Considering that those political grounds were environmentally-focussed in the first place, however, why would the fact that the environmental conflict was channeled through institutional processes deprive those processes of their inherent environmental rationale? The Tribunal seems here to engage in a *petitio principii* which may have perilous implications for comparable cases arising out of environmental conflicts. If a government responds to the environmental concerns of a local community by banning an activity, that ban seems, in principle, to be environmentally-motivated. Therefore, such measure should, if challenged, be treated accordingly by ISDS.

Had the Tribunal not so questionably severed the connection between environmental concerns and Italy's conduct, the police powers defence could have had a better fate. In examining the merits of that argument, however, a further difficulty would likely have arisen. Activists in Abruzzo were explicit in pointing out the dual grounds on which they opposed the Ombrina Mare project: on the one hand, because oil spillovers would (locally) threaten the marine environment (admittedly, the main catalysing factor for the community's mobilisation); on the other hand, however, also because increased extraction of fossil fuels would result in an increase in their burning, further contributing (globally) to climate change (see e.g. here and here). The legislative debate examined by the Tribunal also made clear that the 2015 ban was decided "also taking into account the need to revisit national energy policies in light of [the Paris Agreement]" (para. 109). However, as recalled above, the statute's language as such did not mention such climate (co-)rationale. Moreover, during the arbitration, Italy itself only insisted on the "local" environmental concerns (see the excerpt from Italy's Counter-Memorial reproduced at para. 189).

In fact, the climate rationale for bans on the upstream extraction of fossil fuels seems not to be commonly underlined by States when they are challenged in ISDS; rather, the localised environmental protection dimension seems to be argumentatively prevalent (see, e.g., paras. 172-228 of Canada's counter-memorial in the recently-dismissed case of *Lone Pine v. Canada*). Conceptually, this confusion of rationales speaks to the scholarly debate on what precisely counts as "climate litigation" (see, e.g., here and here). As has been underlined in the literature, however, this also has very practical implications. It is not the same to argue that a ban on the extraction of hydrocarbons at sea actually does not breach the ECT because it was adopted pursuing climate change mitigation, or because it aimed at complying with Art. 194 UNCLOS, or because it formed part of an exclusively domestic environmental policy. Different justificatory norms may be available for conduct dictated by those different motives. Had the Italian ban been framed as (also) based on climate policy considerations, as it was, the Tribunal may, for instance, have been more inclined to acknowledge the applicability of the police powers doctrine.

The consequence of the above is that, despite its obvious potential in this respect, *Rockhopper* does not really tell us much about how climate policy is treated ISDS – unless it is taken to tell us that investment Tribunals are keen to neglect the climate aspect of investment disputes, whenever the facts of the case offer a way to do so. The Tribunal's artificial framing of the analysis appears, however, to also be partly attributable to Italy's deficient argumentative strategy. Leaving the climate dimension of the case out of sight, the *Rockhopper* Award missed the opportunity to set an important precedent in the jurisprudence on ISDS and climate change mitigation.

Conclusion

All in all, *Rockhopper* appears to have refrained from tackling the case's systemic stakes. Whereas the Italian ban ostensibly had a climate policy dimension, this aspect of the case was left unaddressed by the Tribunal and (most surprisingly) by the Respondent itself. It should be noted, however, that, as in *Rockhopper*, not addressing this dimension can be *de facto* more easily conducive to finding a breach of investors' protection standards. International investment law is undeniably in tension with climate policy: however, such tension remained artificially latent in the *Rockhopper* Award. With the *Westmoreland v.*

Canada claim having been dismissed because of a lack of standing, such latency is here to stay. In the meanwhile, it would be desirable for respondent States to make the climate policy case more explicitly than Italy in *Rockhopper*.

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