

SPAIN

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State liability to foreign investors in the renewable energy sector: *Eiser v Spain* and its implications

An increasing number of states are tapping foreign investors as a resource for their renewable energy sectors.¹ These foreign investors, who rushed into government schemes to promote and sustain growth in the renewable energy industry, are now filing an increasing number of claims in several arbitration venues to resolve disputes arising out of contracts between investors and states under international instruments, such as the Energy Charter Treaty (ECT).² For example, as of 6 December 2016, at least six claims have been registered at the International Centre for the Settlement of Investment Disputes (ICSID) by renewable energy investors against Italy,³ and at least one has been registered against Bulgaria.⁴ This article explores investment arbitration as it pertains to foreign investors' investments in Spain's solar energy sector, specifically the *Eiser Infrastructure Limited and Energia Solar Luxembourg Sarl v Kingdom of Spain* award (the 'Eiser award'), which was recently issued on 4 May 2017. The Eiser award marked the first time a tribunal found in favour of investors on this particular issue, and it may provide a path forward for the growing number of disgruntled investors bringing claims against Spain for its recent regulatory changes affecting the solar energy sectors. Remarkably, the tribunal found that states must 'provide fundamental stability in the essential characteristics of the legal regime relied upon by investors in making long-term investments'.⁵

Spain's 2010 solar investment regulations

During 2007, Spain issued a series of regulatory measures to promote renewable energy investment.⁶ Among the measures included in this new regime were: (1) a specified feed-in tariff for a 25-year period for all new plants, following which certain generators would benefit from 80 per cent

of the feed-in tariff; (2) an entitlement to distribute all energy generated to the Spanish electricity grid; and (3) no limitation on the operating hours of generators.⁷

Then, in 2010, suffering from the effects of the global economic crisis and investments that oversaturated the solar sector after its 2007 campaign, Spain enacted two additional laws targeting this regulatory regime. These laws had a substantial impact on the regime and, among other things, removed the feed-in tariff to generators after the twenty-sixth year of the solar plant's life, reduced the number of operating hours of generators and charged €0.50 per megawatt for access to the electric grid.⁸

Claims brought by affected investors followed soon after. Most notable thus far is *Charanne and Construction Investments v Spain*.⁹ The claimants, Charanne BV, a Dutch company, and Construction Investment Sarl, a Luxembourg-based company, targeted the 2010 laws that reduced the feed-in tariffs available for renewable energy generation. The claimants were shareholders of Grupo T-Solar Global SA, a Spanish limited liability company that engages in the generation and sale of electricity produced by photovoltaic solar plants.¹⁰ They maintained that the laws retroactively altered the financial terms applicable to their earlier investment in a solar generation plant, violating Article 10(1) of the ECT by obstructing their legitimate expectations.¹¹

The tribunal ultimately dismissed all the claims and issued an award for costs in favour of Spain, finding that the 2010 regulatory measures had not resulted in a substantial deprivation of the claimants' shareholdings in its Spanish plant that rose to the level of breaching Article 10(1).¹² Part of the difficulty for the claimants was that their expectations were not grounded in specific contracts signed with the state.¹³ Thus, the tribunal highlighted that the claimants did not enjoy

any legitimate expectation that the regulatory framework governing their investments would not change over the lifetime of their venture.¹⁴ Any reasonably sophisticated investor should have foreseen the possibility of future adverse regulatory change.

Spain's 2012–2013 regulatory changes and the *Eiser* award

While claims arising out of Spain's 2010 regulatory changes may not have gained traction with arbitral tribunals, the same cannot be said for Spain's 2013 regulatory changes. Any thought that Spain was entering a hot streak of arbitral victories was extinguished when, on 4 May 2017, an ICSID tribunal ordered Spain to pay €128m plus interest to two investors on finding that Spain had violated Article 10(1) of the ECT by altering the regulatory framework governing the investments of United Kingdom-registered Eiser Infrastructure Limited and Energia Solar Luxembourg Sarl, its Luxembourg subsidiary (collectively, 'Eiser').¹⁵

In 2007, Eiser made an initial investment in the concentrated solar power (CSP) sector in Spain. CSP plants are large facilities that are expensive to build and require large initial capital investments. Due to these high costs, CSP plants have been unable to compete with traditional forms of power generation that use fossil fuels. Thus, Spain, like many other countries, decided to promote the development of CSP plants by adopting a regime of government subsidies. Under Royal Decree 661/2007, investments in renewables registered before a certain date were guaranteed the following: (1) stability under state electricity tariffs; and (2) a 'reasonable return' for their initial investment. Attracted by this favourable regime, Eiser invested more than €126m in several CSP plants.

Between 2007 and 2012, several changes were made to Spain's regulatory framework for renewable energy, aiming to reduce the so-called 'tariff deficit', which is the difference between the subsidies paid to producers and the government's sale price to consumers.¹⁶

Specifically, in December 2012, Spain passed regulations imposing a seven per cent tax on the total value of all energy fed into the national grid by electricity producers and eliminating premiums for electricity generated with gas.¹⁷ Then, in July 2013, Royal Decree 9/2013 was passed, repealing the tariff regulations laid out in Decree 661/2007, discussed below.¹⁸ Finally, in 2014,

a new regime governing renewable energy was established, which calculated a reasonable rate of return for investors based on the hypothetical standard operating costs of 'efficient' solar energy plants.¹⁹

Despite regulatory changes that Spain implemented between 2007 and 2012, Eiser was assured on several occasions that the initial tariff rate laid out in Decree 661/2007 would be applied to their plants. However, after new regulations were imposed in 2012, 2013 and 2014, it became clear that Spain's new changes would not benefit Eiser. Specifically, the 2014 laws established standards to which Eiser's plants did not conform. As a direct consequence of these new regulations, revenue from Eiser's solar plants fell below what was required to cover financing and operating costs or to provide a return on investment, and Eiser's Spanish operating companies were forced into debt rescheduling negotiations with their lenders. Eiser argued that, taken together, these regulatory changes amounted to 'complete value destruction' of their investment.²⁰

The tribunal agreed and concluded that Article 10(1)'s obligation to afford fair and equitable treatment requires a state 'to provide fundamental stability in the essential characteristics of the legal regime relied upon by investors in making long-term investments'.²¹ The tribunal also noted that, although regulatory changes are to be expected, a state's regulatory regime cannot be '*radically* altered as applied to *existing* investments' (emphasis author's own) in ways that would deprive investors, such as Eiser, of their investment's value.²² The effect of Spain's 2013 and 2014 arbitrary regulatory changes was to retroactively apply a 'one-size-fits-all' standard to existing facilities that were previously designed, financed and constructed based on the very different regulatory scheme of the 2007 law.^{23 24}

The *Eiser* award suggests that Spain's 2012–2013 regulation overhaul may have gone too far. There are currently about 30 cases pending before ICSID tribunals alone concerning Spain's regulatory changes.²⁵ These foreign investors may be able to make the same successful claim under Article 10(1) of the ECT.

The award provides ample warning to states looking to encourage foreign investment in their renewable energy sectors. The renewable energy sector may be nascent, but it is growing quickly. For instance, global renewable power generation capacity rose

by nine per cent in 2016; solar power, specifically, rose by 30 per cent last year. For two years in a row, renewable energy has accounted for more than half of new power generation capacity added worldwide.²⁶ Thus, regulatory changes are likely to occur often as states find new and improved methods to keep up and encourage this booming industry.²⁷ However, as *Eiser* implies, states should be careful not to alter their regulatory landscapes in this industry so drastically that they neglect to provide investors with the time necessary to meet these new compliance standards.

Notes

- * Meriam Al-Rashid is a partner and Diora Ziyeva is a senior associate at Dentons' New York Litigation and International Arbitration practice groups. The views expressed in this article are exclusively those of the authors and shall not be attributed to Dentons US or its clients. The authors gratefully acknowledge comments by and editorial assistance from Christina Dumitrescu.
- 1 Eg, Russia is starting its largest renewable energy auction to award contracts to purchase 1.9 gigawatts of clean electricity by luring in foreign investment to increase local jobs. From 29 May 2017 to 9 June 2017, foreign investors will be invited to submit their bids to build a project of a certain capacity in a given year. As of 29 May 2017, Fortum Oyj, Finland's largest energy company, and Enel SpA, an Italian company, have already expressed interest in participating. Anna Hirtenstein and Stephen Bierman, 'Russia Starts Largest Renewable Energy Auction in Bid for Jobs' *Bloomberg* (New York, 29 May 2017) www.bloomberg.com/news/articles/2017-05-29/russia-starts-largest-renewable-energy-auction-in-bid-for-jobs accessed 29 June 2017.
 - 2 Of all current ICSID cases involving a state party from the European Union, 44 per cent of them involve the electric power and other energy sectors. 'The ICSID Caseload – Statistics', *International Centre for Settlement of Investment Disputes* (Issue 2017-1), 2017.
 - 3 See eg, Zoe Williams, 'As Sun Sets on One Italy Renewables Arbitration, Another Rises' *Investment Arbitration Reporter* (Santa Monica, 9 December 2016) www.iareporter.com/articles/as-sun-sets-on-one-italy-renewables-arbitration-another-rises accessed 29 June 2017. In one decision, *Blusun SA v Italy*, the tribunal applied a proportionality test to the claimants' Article 10(1) claims under the ECT and determined that Italy's regulations were proportionate and did not amount to 'crippling or disabling' changes. See Jarrod Hepburn, 'ANALYSIS: In New Award, Italian Renewables Changes Appear Less Dramatic Than Those In Recent Spain Case, Thus Leading to Failure of Blusun's FET Claim; Arbitrators Disagree on Expropriation Assessment' *Investment Arbitration Reporter* (Santa Monica, 7 June 2017), www.iareporter.com/articles/analysis-in-new-award-italian-renewables-changes-appear-less-dramatic-than-those-in-recent-spain-case-thus-leading-to-failure-of-blusuns-fet-claim-arbitrators-disagree-on-expropriation-assessment accessed 29 June 2017.
 - 4 See eg, Zoe Williams, 'Bulgaria Faces Energy Charter Treaty Claim After Investor Warned of Harms Due to Feed-In Tariff Changes and Renewables Regulation' *Investment Arbitration Reporter* (Santa Monica, 13 July 2016), www.iareporter.com/articles/bulgaria-faces-energy-charter-treaty-claim-after-investor-warned-of-harms-due-to-feed-in-tariff-changes-and-renewables-regulation accessed 29 June 2017.
 - 5 *Eiser Infrastructure Limited and Energia Solar Luxembourg Sarl v Kingdom of Spain*, ICSID Case No ARB/13/36, final award dated 4 May 2017 ('Eiser'), para 382.
 - 6 Spain initiated a campaign during 2007 and 2008, under the slogan 'The Sun Can Be Yours' to encourage investment in its solar energy sector; *Charanne and Construction Investments v Spain*, SCC Case No V 062/2012, Award dated 21 January 2016, paras 102–104.
 - 7 Richard Power and Paul Baker, 'Energy Arbitration' *Global Arbitration Review*, 14 October 2016.
 - 8 *Ibid.*
 - 9 *Charanne and Construction Investments v Spain*, SCC Case No V 062/2012, award dated 21 January 2016.
 - 10 *Ibid* at paras 1–4. The claimants very specifically *did not* ask the tribunal to analyse the 2013 regulatory framework, which was the subject of the *Eiser* award. *Ibid* at paras 481–482.
 - 11 *Ibid* at paras 296, 475–542. In total, the claimants alleged that Spain breached Article 13(1) of the ECT (expropriation), Article 10(12) of the ECT (obligation to provide effective means for the assertion of claims) and Article 10(1) of the ECT (fair and equitable treatment). *Ibid* at para 451. This article only focuses on the claimants' arguments vis-à-vis Article 10(1).
 - 12 *Ibid* at paras 539–542.
 - 13 *Ibid* at paras 490, 492–493, 496–497.
 - 14 *Ibid.*s
 - 15 *Eiser Infrastructure Limited and Energia Solar Luxembourg v Spain*, ICSID Case No ARB/13/36, award dated 4 May 2017. The tribunal comprised of Professor John R Crook, who served as a Chairman; Dr Stanimir Alexandrov, appointed by the claimants; and Professor Campbell McLachlan QC, appointed by the respondent.
 - 16 *Ibid* at paras 111–113, 137–38, 144.
 - 17 *Ibid* at para 144.
 - 18 *Ibid* at para 146.
 - 19 *Ibid* at paras 147–49.
 - 20 *Ibid* at para 154.
 - 21 *Ibid* at para 382.
 - 22 *Ibid.*
 - 23 *Ibid* at para 400. After the award was issued, Eiser applied to the United States District for the Southern District of New York for ex parte enforcement of the award.
 - 24 Benjamin Button Stephens and Sebastian Perry, 'New Fronts Open in Spanish Solar Battle' *Global Arbitration Review* (London, 23 May 2017) <http://globalarbitrationreview.com/article/1141975/new-fronts-open-in-spanish-solar-battle> accessed 29 June 2017.
 - 25 This number does not include treaty claims that have also been brought with respect to these regulatory changes under the United Nations Commission on International Trade Law (UNCITRAL) rules and the Stockholm Chamber of Commerce. See n 24, above.
 - 26 Pilita Clark, 'The Big Green Bang: how renewable energy became unstoppable' *Financial Times* (London, 18 May 2017).
 - 27 In fact, the next wave of regulatory changes may try to compensate for an overall dip in costs resulting from a wave of demand for renewable energy, particularly solar energy, that has helped to drive down energy costs worldwide. New regulations may even shift away from providing subsidies to companies in the renewable energy industry to focusing on creating and implementing auctions for solar energy; *Ibid.*