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The Past, Present and Possible Future of the Spanish Renewable Energy Arbitration Saga

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Introduction

It is not easy to write about, and even harder to make predictions as to future developments involving, a topic that is a moving target. This is especially true where the movement is in fits and starts, with occasional lengthy periods of stability or inactivity followed by bursts of frenetic and often unanticipated developments.

The Spanish renewable energy arbitration saga (currently involving nearly 40 investment treaty arbitrations against the country claiming some U.S. $9 billion in total) is such a moving target: a fascinating, complicated and ever-evolving situation bringing into focus a number of important and timely issues of policy and threads of public discourse.

As such, the topic is difficult to write about, especially in traditional print form where the time lag between preparing a piece and its actual publication can be significant. And this all the more in an area in which recent weeks and months have been particularly active and the coming weeks and months will surely be even more so. With the caveat, then, that this article speaks only as of May 25, 2018, the following serves as an introduction to the three-dimensional chess game that this series of claims has become.

We start with the relevant background, then summarize the final awards that have been issued to date, and finally turn to some potentially game-changing issues that have arisen which might restrict or prevent enforcement of the awards already rendered and/or limit or preclude further awards in favor of investors.

Background

Until three or four years ago, the Energy Charter Treaty (ECT)—a multilateral treaty for the protection of foreign investment and the promotion of international trade and competition in the energy sector—and arbitration based on it as well as similar multilateral or bilateral investment treaties, were virtually unknown in Spain.

Investment arbitration itself was a rarefied specialty, known only to a handful of intrepid companies and a small cadre of advisors. The few Spanish practitioners who had any exposure typically involved claims brought by Spanish entities against recalcitrant states such as Venezuela and Argentina. For so long as ECT and other

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investment arbitration against Spain was limited to one or two exceptional cases, the Spanish press paid little or no attention to the issue, and the Spanish public remained blithely ignorant. To that point, the recently raging debate over the pros and cons of the arbitration-based investor-state dispute resolution system (ISDS) drew little attention in Spain.

All of this has changed due to Spain's regulation, and then re-regulation, of the renewable energy sector.

In the past two decades, Spain adopted a clear and concerted policy favorable to the development of renewable energies of all types. The lynchpin of the then-government's Renewable Energy Plan 2005-2010 was a series of incentives for long-term investment, which included a generous guaranteed feed-in tariff. The policy worked: investment in Spanish renewable energies grew spectacularly, and Spain as a country, along with a number of Spanish companies, became leaders in the field.

The policy, it seems, may have worked too well. The amount of investment attracted was excessive. Long-term maintenance of the feed-in tariff and the generous remuneration system turned out to be a practical impossibility causing government officials to conclude, after the financial crisis of 2008 hit, that the country could not afford to maintain the remuneration system in place. For a variety of reasons, a gaping "tariff deficit" had opened, with revenues generated by electricity sales being vastly outweighed by the associated costs. As a result, starting in 2010, Spanish governments changed course and implemented a bevy of legal and regulatory measures, limiting payments to renewable investors and investments in an effort to reduce and (finally) eliminate the tariff deficit.

An essential and highly controversial aspect of the reforms was the implementation of a new remuneration scheme for electricity generation, based on assuring "reasonable profitability" (linked to the yield of Spanish government bonds) for renewable plants.

Countless challenges to these measures have been filed in the Spanish courts by domestic investors. But the Spanish Supreme Court's jurisprudence in the area seems to cast a cloak of immunity on the State in its regulatory activity, essentially concluding that sophisticated investors should be aware of the inherent regulatory risk involved in their investments. In so doing, the court has shut the door on their claims, so long as a reasonable return was provided and subsidies or benefits already granted were not required to be returned.

The recourse of foreign investors, though, is not limited to the Spanish courts; they are entitled to arbitrate under the ISDS system. So, what began as a trickle in late 2011 with a still-pending ECT claim brought under the UNCITRAL rules by a series of international investors in the Spanish photovoltaic sector has now become a barrage involving the whole range of renewable energies. At last report, nearly 40 ECT cases have been brought against Spain, the vast majority under ICSID, with a handful being administered by the Stockholm Chamber of Commerce (SCC), in addition to the initial UNCITRAL claim (the ECT contemplates these three alternatives).

Awards Issued to Date

International arbitrations take time, and investment arbitrations—frequently bifurcating jurisdictional issues and/or permitting the appearance of public or public interest entities as amici curiae—tend to take longer than commercial cases. As of this writing, only five of the nearly 40 cases have reached a final award.

This trickle will soon become a torrent. A handful of the older cases are on the verge of an award. Reportedly, two or three merits hearings are currently being held each month, so a significant and growing number of cases are nearly ready for judgment. Moreover, there have been recent developments at the European level which cast a large cloud on the future of the saga. So now is a good time to take stock of the state of play.

Final awards have been issued and are in the public domain in the following five cases: *Charanne* (SCC, January 2016); *Isolux* (SCC, July 2016); *Eiser* (ICSID, May 2017); *NovEnergía* (SCC, February 2018) and *Masdar* (ICSID, May 2018).

In all five cases, and surely in those remaining to be decided, the key issue on the merits involves the meaning and application under the ECT of the concept of "fair and equitable treatment" (FET), and its constituent element: "legitimate expectations." Both *Charanne* and *Isolux* (each by majority decision over a forceful dissent) rejected the investors' claims, the former arising from relatively limited reforms implemented in 2010 and the latter from the more significant changes implemented between 2012 and 2014. *Eiser, NovEnergía* and *Masdar,* on the other hand, found forcefully (and unanimously) for the investors challenging the 2012-2014 reforms.

A close review of the voluminous awards in these five cases suggests that they may not be as irreconcilable as certain Spanish press headlines (especially those just following the issuance of the third and fourth awards) have suggested. Rather, they can be understood to apply a similar (or, at least, substantially similar) conceptual framework to very different investors and investments, or at least to investors and investments that were viewed quite differently by the respective tribunals.

Thus, what may have appeared, on first impression, as fundamentally irreconcilable may, with the passage of time and the accumulation of further awards, be revealed as quite the opposite: comprehensible and predictable.

Charanne

The investors in Charanne acquired control of the owner of 34 photovoltaic (PV) plants in Spain in 2009. The regulatory changes enacted in 2010 eliminated regulated tariffs for such plants after 30 years of operation, limited operating hours and hours entitled to retribution in the period 2011-2013 and made other changes reducing plant profitability. The investors alleged that the changes reduced the profitability of their plants by some 10 percent.

The SCC Tribunal concluded that, although the economic and financial consequences of the reduction in profitability were significant, they did not justify a conclusion that the value of the investment had been destroyed so as to constitute indirect expropriation. The Tribunal (by majority) further concluded that the commitments of regulatory stability contained in the underlying 2007 legislation were not sufficiently targeted or specific to substantiate legitimate expectations that its provisions would not be modified.

Isolux[1]

Isolux involved a challenge to the 2012-2014 changes by claimants who made their investment decision and indirect investment in 117 entities (thus stepping into the latter's' shoes), each owning a PV plant in Spain. According to the award, in prior litigation the investor's parent company had submitted an expert report to the Spanish Supreme Court indicating an expected rate of return of some 6 percent on its investment, less than the "reasonable" rate of some 7 percent provided by the new regulation.

The SCC Tribunal concluded that the claimant could not have had a legitimate expectation at the time of its investment.[2] Moreover, that the regulatory framework would not materially, or even fundamentally, change, since (i) in the years prior to the investment, the regulatory framework had already been modified on various occasions, (ii) the Spanish Supreme Court had established clearly that, insofar as national law was concerned there were no obstacles to the modification of the regulatory regime, with a reasonable investor presumed to have knowledge of this situation; and (iii) the claimant was perfectly aware of the referenced Spanish case law.

This last element was of particular importance because the claimant's ultimate parent company had unsuccessfully challenged one of the 2010 measures before the Spanish courts. The challenge resulted in a September 2012 decision of the Supreme Court[3] which concluded that the regulatory changes were permitted so long as they respected a reasonable rate of return. The Court noted that "A party who decides to invest in a country which, according to it, lacks legal certainty, cannot later complain that it was not provided such certainty." The majority also echoed the *Charanne* finding that the legislative commitments were insufficiently targeted and specific to form the basis for legitimate expectations of essential stability.

Eiser

Eiser involved a challenge by UK and Luxembourg-based claimants who made their investment decision and investment in a series of concentrated solar power plants (CSP) in Spain in 2007. The claimants alleged that the regulatory changes from 2012-2014 constituted "a complete value destruction" of their investment because some Euro 125 million was reduced in value to a mere Euro 4 million, thereby (as indeed found by the Tribunal) "stripping claimants of virtually all of the value of their investment."

The ICSID Tribunal noted that the changes to the PV regulatory regime at issue were far more "dramatic," "sweeping" and "drastic" in terms of their impact on the economic value of the claimants' assets and interests than those at issue in *Charanne*, and created a "totally different" and "unprecedented" regulatory regime. The Tribunal concurred with the claimant that the consequence of the "total and unreasonable" change in the regulatory regime was the virtual destruction of their investment.

NovEnergía

In *NovEnergía*, a SCC panel found in favor of a Luxembourg investor in several Spanish PV plants. As in *Eiser*, the Tribunal distinguished *Charanne* as having only addressed the more limited regulatory changes of 2010 and *Isolux* as involving an investment made at a much later stage (2012) when a reasonable investor would not have legitimately maintained an expectation of regulatory stability.

Departing, to some extent, from *Charanne* and its rather strict requirement that legitimate expectations be based on specific, focused assurances or undertakings, the *NovEnergía* Tribunal indicated that legitimate expectations "arise naturally from undertakings and assurances given by the state, whether or not specifically targeted to the investor or included in contractual stabilization clauses."

Departing, to some extent, from *Eiser*, the *NovEnergía* Tribunal further indicated that the FET standard protected against more than changes that actually destroyed the investment or deprived the investor of the investment's value. Instead, a "balancing exercise" was required, in which destruction of value is only one factor, i.e., the fact that a "healthy profit" was still being made after the "radical, drastic and unexpected" changes was not a bar to the claim where the investor's legitimate expectation and reliance had been that no such change would be implemented, and where the change caused "quantifiable prejudice" to the investor.

Masdar

Finally, in *Masdar*, an ICSID panel found in favor of a UAE-owned Dutch investor with a 40 percent stake in a number of Spanish CSP plants, holding that the recent regulatory changes (those at issue in the *Eiser* and *NovEnergía* cases) violated the ECT's fair and equitable treatment standard. The panel awarded damages of Euro 64.5 million.

Beyond confirming the apparent trend commenced in *Eiser* and *NovEnergía* towards unanimous findings in favor of investors challenging the 2013-2014 regulations as FET violations, the award is of interest for three reasons. First, in its emphatic finding that the maintenance of the 2007 remuneration regime for the plants in question had been the subject of specific assurances amply sufficient to create legally protected legitimate expectations under the ECT. It noted, "It would be difficult to conceive a more specific commitment than a Resolution issued by Spain addressed specifically to each of the Operating Companies, confirming that each of the Plants qualified under the RD661/2007 economic regime for their cooperation lifetime" and observed that there was "not any indication at the time when Claimant was making its investment that there was the slightest possibility that the RD661/2007 regime…would be swept away by the Disputed Measures, or that any reasonable investor might foresee that they might be." Second, for the split between the majority and dissent as to whether discounted cash flow (DCF) or an asset-based valuation (ABV) is the more appropriate method to assess the fair market value of the investments in question for purposes of assessing damages. And third, and perhaps most importantly, for its summary dismissal (and perhaps, rather restrictive or literal application) of the *Achmea* decision discussed below, stating that *Achmea* "had no bearing upon the present case" since it "cannot be applied to multilateral treaties, such as the ECT, to which the EU itself is a party."

Jurisdictional Objections

In each of the cases discussed, Spain, generally, with the European Commission's participation as amicus curiae, raised a series of jurisdictional objections which (as in certain parallel Italian cases) were uniformly, and rather summarily, dismissed. Were it not for the recent developments discussed below, they would require only a passing reference (if that) in this article.

Specifically, in *NovEnergía*, Spain argued first that the Tribunal lacked jurisdiction under the ECT since NovEnergía was not "an investor of another Contracting Party." That is, because both Spain and claimant's home state, Luxembourg, were EU member states, and because the EU was itself a party to the ECT, the dispute was essentially one within a single ECT contracting party, the EU, and not between one contracting party and an investor of another contracting party.

This objection was rejected. The Tribunal refused to read into the ECT the jurisdictional limitations suggested by Spain. As long as the investor hailed from another contracting state, ECT's jurisdictional requirements were satisfied.

Spain also contended (in an argument first developed by the European Commission) that the ECT contained an "implicit disconnection clause," according to which the ECT would not apply between EU member states, but only with respect to third states. However, the Tribunal saw no basis for such an implicit clause in the "clear" terms of the ECT.

The Tribunal also rejected a set of further arguments based on EU law. According to Spain, for instance, EU law prevailed over and displaced any other law (including the ECT) due to a "principle of primacy" in intra-EU legal relations, which thus barred the Tribunal from upholding jurisdiction over investor's claims. Spain also asserted that the Tribunal was barred from addressing questions of EU law, as EU courts have exclusive jurisdiction over such questions. These objections were also readily dismissed. The Tribunal concluded that the claim was based on the ECT and not on EU law, that the ECT gives the Tribunal exclusive jurisdiction, and that there is no conflict between ECT investor protections and EU law, which would require a ruling by the CJEU.

Europe Comes to Spain's Defense

On the (sole) basis of the first four final awards discussed above, Spain's position appeared rather bleak. As mentioned, it had prevailed (by majority) only in cases challenging early, less drastic regulatory changes (*Charanne*) or involving investments made when the handwriting of impending change was clearly on the wall (*Isolux*) and the negative consequences to the investment were limited. On the other hand, it had lost (unanimously) in the two cases challenging the more radical changes, which were the subject of the vast majority of the pending cases, one where the changes had produced devastating consequences on the investment (*Eiser*), the other where the impact of the changes was much less drastic, allowing the investor a healthy profit (*NovEnergía*).

Speculation in the market was that Spain would be likely to lose the large majority of the pending cases, the facts and circumstances of which were understood to echo more closely *NovEnergía* and *Eiser* than *Charanne* and *Isolux*. Rumors of the possibility of settling the claims (pending the results of annulment proceedings, ongoing in the case of *Eiser* and anticipated in the case of *NovEnergía*) began to circulate. And this notwithstanding the delicate political problem that might arise from settling an ECT claim with an international (non-Spanish) investor when a Spanish investor, without recourse to ISDS, has (under established Spanish case law) no effective recourse against the same measures. (The more recent *Masdar* case highlights this last point: there, the foreign investor with access to the ECT procured an award protecting its 40 percent investment, whereas its Spanish joint venture partner has no effective recourse for its 60 percent investment.)

But, with the help of the EU (the Commission and Court of Justice of the European Union (CJEU), respectively), Spain has recently received two lifelines that could be game-changers. The effect is to put into possible doubt the ability of the investors in *Eiser* and *NovEnergía* to enforce their awards (assuming the annulment actions are rejected) and potentially even tilt the scales towards Spain in the still-pending cases and any yet to be filed.

State Aid

The first European lifeline thrown to Spain is one based on concepts of unlawful state aid. This line of thought is predicated on the Commission's efforts currently on appeal to the CJEU to defeat enforcement of an ICSID award under an intra-EU BIT in the *Micula* case on the ground that paying the award would violate EU law as constituting new, un-notified and thus illegal state aid in violation of EU law.

Based on its *Micula* strategy, the Commission in a controversial decision (Decision 2017/C442) issued in November 2017 found that the 2012-2014 reforms were compatible with EU law, and specifically referring to the *Eiser* decision issued some months prior, essentially prohibited Spain from paying compensation under the award on the grounds that this (unless approved by the Commission) would constitute new un-notified and thus illegal state aid.

The decision repeated the Commission's position that intra-EU investor-state arbitration is contrary to EU law. Thus the ECT is inapplicable to investors from EU member states with disputes against other member states and observed that the decision itself is part of EU law and therefore binding on arbitral tribunals applying EU law. In this scenario its validity can only be challenged before European courts.

The decision went even further, concluding as a matter of substance that there was and could be no FET violation in *Eiser* or any other case alleging legitimate expectations based on the 2007 Spanish remuneration regime since that regime involved un-notified, and thus illegal, state aid and "no investor could have, as a matter of fact, a legitimate expectation stemming from illegal state aid."

Pending an ultimate decision by the CJEU, this lifeline to Spain risks undermining the ICSID system of automatic recognition and enforcement of ICSID awards within the EU and, as a result, may render non-EU jurisdictions (such as the United States and in particular, New York) the key battleground for enforcement purposes.

Incompatibility of BIT (and ECT?) Arbitration With EU Law

A second and potentially even stronger lifeline was handed to Spain in early March 2018 by the CJEU in the case of *Achmea v. the Slovak Republic*, in which it finally and definitively confirmed the Commission's view that clauses in BITs providing for arbitration were contrary to EU law since the arbitral tribunals established cannot be considered courts or tribunals of a member state within the meaning of the Lisbon Treaty and, as such, have no power to refer questions to the CJEU. In making this decision the CJEU declined to follow the (non-binding) contrary view of the EU's Advocate General advisory opinion issued some months prior and aligned itself with the views expressed by a majority of EU member states (particularly those being on the receiving end of arbitration claims).

The CJEU thus concluded that ISDS, as contemplated in intra-EU BITs, was incompatible with EU law as it deprived courts within the judicial system of the EU from deciding questions of EU law, with the possibility of referring questions of EU law to the CJEU (as the German court before which the claimant was seeking to enforce the award had done), if necessary.

This decision, infallible because it is final, not final because it is infallible, probably raises more questions than it answers, especially insofar as the Spanish renewable cases (based on the ECT, not on BITs) are concerned. These include whether

- The decision should be understood to be applicable only to BITs (at issue in *Achmea*), or also to multilateral treaties such as the ECT, to which the EU is party and thus arguably can be deemed to have accepted the ECT's arbitration mechanism;
- In the absence of any temporal discussion in the decision, it should be understood to require that ongoing intra-EU BIT cases be discontinued (or alternatively, whether it should be understood to apply only to newly-filed cases);
- And to what extent the decision should be applicable in the case of intra-EU ICSID disputes, where ICSID's self-contained/automatic recognition and enforcement regime precludes by definition the review or involvement of domestic (EU) courts upon which Achmea was fundamentally predicated; and
- In the case of BIT proceedings seated outside the EU, Tribunals should or will pay any attention to *Achmea* and EU law generally.

The coming months will be indicative of how tribunals in ongoing cases view the relevance of Achmea. It would not be surprising to find different views taken in different cases, with the nature of the arbitration (ICSID/SCC/UNCITRAL) and the seat potentially pushing tribunals in different directions. As for recognition and enforcement, the EU would seem now to be off-limits; award creditors will focus on non-EU jurisdictions to seize assets with which to satisfy their claims. Indeed, press reports indicate that the Swedish court hearing Spain's action to set-aside the *NovEnergía* award has granted Spain's request for a temporary stay of any potential enforcement of the award in Sweden (presumably in light of the state aid and/or *Achmea* issues).

In all events, what is clear is that, when Spain most needed it, both the EU Commission and the CJEU threw it a lifeline. In so doing, however, these institutions have rendered problematic the satisfaction of existing awards. They have also made the process more expensive as the proper structuring of claims has become more complex, and, more unlikely and possibly even pyrrhic the obtaining of further awards in the dozens of ECT cases that remain to be decided.

Conclusion

After a slow start, the saga involving upwards of three dozen investment treaty claims against Spain has accelerated in recent months. After two initial losses by investors, the two subsequent final awards had evened the score and appeared to augur well for the remaining claimants (and badly for Spain). But the recent action by the EU Commission and the decision by the CJEU cast a large cloud of uncertainty as to the enforceability of awards eventually issued in favor of the investors in these two cases, and may–notwithstanding the *Masdar* Tribunal's forceful assertion to the contrary, at least insofar as ECT claims are concerned–also impact the outcome of the still-pending cases and the prospects for any to-be-filed cases.

Surely by the time this piece is printed and in the hands of the reader, the situation will have evolved further, perhaps much further. Some investors, frustrated by the apparent obstacles to enforcement posed by the recent EU actions, may consider selling their claims to entities with more patience and more stomach for what could still, post-award, be a long and grueling battle. On the other hand, certain investors who have stayed on the sidelines during recent years, might be sufficiently heartened by the seeming favorable trend in the awards to file claims now, betting that the recent EU law obstacles will be able to be circumvented and will only delay, but not defeat, the ability to both bring a successful claim against Spain, but also to enforce it. The state aid and *Achmea*-related issues will be trotted out before each and every body hearing annulment or enforcement actions. There is no reason to expect that all decisions in this regard will be of a piece: for example, annulment and enforcement decisions involving CIADI awards may well come to different conclusions than those involving SCC awards in arbitrations seated in Europe where enforcement is sought in the EU.

Hopefully, this article will have permitted the reader a useful background (as of May 25, 2018) against which to measure future developments. So, stay tuned and keep your seatbelt buckled—there could be substantial turbulence ahead!

Author's note: This article draws, to a certain extent, on some of the principal author's previously published materials on the topic, including "Squaring the Circle: Reconciling the Conflicting Awards in the *Eiser* and *Isolux* Spanish Renewable Cases (Part I)," Kluwer Arbitration Blog, July 2017; "Squaring the Circle: Reconciling the Conflicting Awards in the *Eiser* and *Isolux* Spanish Renewable Cases (Part II)," Kluwer Arbitration Blog, July 2017; "Before the Other Shoe Drops," EFILA Blog, September 2015; "Before the Other Shoe Drops (II): The First ICSID Final Award in the Spanish Renewable Energy Arbitration Saga Finds for the Investors—Crossing the Line?," EFILA Blog, May 2017; and the chapter *The Energy Charter Treaty*, The Investment Treaty Arbitration Review, 1st Edition, March 2016.

Endnotes

1. In many respects, a companion case to *Charanne*, brought by related investors—parts of the group of companies controlled by the Spanish construction group of the same name, now the subject of insolvency proceedings—with the same counsel, and the same co-arbitrators named by each party.
2. Determined by the majority to be October 2012, as Spain had argued, instead of June 2012, as claimant had argued.
3. Per above, the court determined the date of the investment to be October 2012.

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