CLIFFORD

CHANCE

Briefing note February 2016

Claim against Spain dismissed, in the first arbitration award regarding changes in the renewable energies remuneration scheme

The award rendered on 21 January 2016 dismisses the Investors' claims, finding no indirect expropriation or breach of the commitment to accord fair and equitable treatment. The Arbitration Tribunal has ordered the claimants to pay most of the arbitration costs

I. A dispute between investors and the Kingdom of Spain

SCC arbitration under the Energy Charter Treaty: claim in relation to legislative changes made in 2010 in the photovoltaic sector

The proceedings

Two subsidiaries of the Spanish company Isolux Corsán —Dutch company Charanne B.V. and Luxembourg company Construction Investments S.A.R.L. (the "**Investors**")— brought a claim on 7 May 2012 against the Kingdom of Spain ("**Spain**") before the Arbitration Institute of the Stockholm Chamber of Commerce (the "**SCC**") under the mechanism established in Article 26 of the Energy Charter Treaty ("**ECT**").

The Arbitration Tribunal

The arbitrators appointed to resolve this dispute were: Alexis Mourre of France (Presiding arbitrator), Guido S. Tawil of Argentina (arbitrator appointed by the Investors) and Claus von Wobeser of Mexico (arbitrator appointed by Spain).

Claim referred to the photovoltaic sector

The Investors claimed reimbursement for their losses incurred as shareholders of a Spanish company devoted to the generation and marketing of electricity at solar photovoltaic power plants, as a result of the legislative changes made in 2010 which affected the remuneration system regulated by means of premiums and tariffs (the "**Special Regime**") applicable to the plants owned by the Spanish company:

- Legislative changes made in 2013 and 2014 were not analysed here, as they were the subject of another claim brought by companies of the same group in other arbitration proceedings.
- The breach in question was in relation to the limitation on the life of the projects and the reduction of the number of hours of electricity generation subject to regulated remuneration.

Key aspects

- The award is not favourable to the Investors' position.
- The Arbitration Tribunal only decided on the legislative changes of 2010 and did not analyse the possible effects or consequences of the amendments made in 2013 and 2014.
- The decision refers to the photovoltaic sector and does not analyse the impact of changes on other technologies.
- This is a non-binding precedent which may well be taken into account by other arbitration tribunals in other pending and potential future claims against Spain on similar issues
- The award provides hints of the elements that should be evidenced in order to consider that Spain's actions constitute breaches of Articles 10 and 13 ECT.
- There is a dissenting opinion by arbitrator Guido S. Tawil regarding the effective breach by Spain of Article 10 ECT, because of having created legitimate expectations for the Investors as a result of the Special Regime regulated in Spanish Royal Decrees 661/07 and 1578/08.

II. The positions of the parties

Breach of the ECT vs. the Investors' lack of standing and reasonable and foreseeable changes

The Investors' position

The Investors' claim was regarding two amendments of the Special Regime made by Spanish Royal Decree1565/2010 and Royal Decree-Law 14/2010:

- Elimination of regulated tariffs as from the 26th year for solar photovoltaic power plants and the establishment of additional technical requirements so as to not lose entitlement to regulated remuneration.
- Restriction on the number of hours remunerated under the Special Regime and the establishment of a toll for the use of transmission and distribution networks.
- These amendments would have the following effects:
  - They would retroactively affect the legal and financial regime established in the regulations, based on which the Investors made their investment.
  - They would entail several breaches of the ECT: (i) indirect expropriation, in violation of Article 13 ECT; (ii) breach of the commitment to accord fair and equitable treatment, in violation of Article 10(1) ECT; and (iii) breach of the duty to provide effective channels for defending their rights, in violation of Article 10(12) ECT.

The award does not pronounce on legislative changes made in 2013/2014

The arbitration award leaves room for different decisions related to legislative changes made in 2013 and 2014, —which had a greater impact on investments in the renewable energies sector— and gives some relevant insight on the proper approach when bringing such claims against Spain.

Spain's position

Spain proposed several jurisdictional objections which would prevent the Arbitration Tribunal from hearing the case:

- Isolux and its subsidiaries brought other proceedings before the Spanish courts and the European Court of Human Rights (the "ECHR") —i.e. fork in the road clause—.
- Lack of standing, due to the Spanish nationality of the ultimate beneficial owners of the Investors.
- Lack of jurisdiction of the Court to pronounce on intra-EU disputes, due to the investors being citizens of a Member State of the European Unión, and EU law not permitting the application of the dispute resolution mechanism established in the ECT to these types of internal claims.
- Spain also argued the inexistence of any breach whatsoever of the ECT, for several reasons:
  - The modification of the remuneration system of the Special Regime did not cause the investment to be expropriated.
  - The commitment to accord fair and equitable treatment was not breached, because the measures adopted were reasonable and foreseeable.
  - The legislative changes of 2010 did not have retroactive effect, because the Investors did not hold an acquired right to regulated remuneration and the amendments did not affect the electricity already sold by the power plants.

III. The Court's decision

Dismissal of the jurisdictional objections raised by Spain and no breach of the ECT

Dismissal of jurisdictional objections

The Arbitration Tribunal found itself to have jurisdiction to hear the case, for the following reasons:

- The Investors may resort to arbitration because, although they are part of the same corporate group, they are not the same party as those companies claiming before other jurisdictional bodies. Therefore, they do not meet the 'triple identity' test required to apply the fork in the road clause.
- The Court held that the investor's status as a foreign investor is fulfilled if the vehicle is foreign-registered, regardless of who the final investor is.
- The dispute resolution mechanism established in the ECT is fully compatible with EU law and must be applied to decisions involving investors of EU Member States and other Member States.

Non-existence of breach of the ECT

Having confirmed its jurisdiction, the Arbitration Tribunal dismissed the Investors' claim, finding no breach whatsoever of the ECT:

- In order to determine the existence of indirect expropriation and a breach of Article 13(1) ECT, the legislative change must imply a loss in value of the investment, to such an extent that it represents a "destruction of its value". But no such "destruction of its value" was demonstrated in the proceedings because, although the power plants did see their profitability decrease, they continued to earn a profit.
- No breach of the duty to accord fair and equitable treatment to the investment exists, because: (i) at no time did Spain define a regulatory framework which might legitimately lead the Investors to believe that such legislation could not be amended; (ii) there was no specific undertaking by Spain in the original regulation of the Special Regime; (iii) registering in Spain's Administrative Registry of Power Plants adhering to the Special Regime ("RAIPRE") was merely an administrative requirement in order to be able to sell energy and it did not imply that the power plants registered had an acquired right to receive certain remuneration, and (iv) although the Court acknowledged the legitimate expectation that the regulation used as the basis for making the investment would not be amended irrationally, disproportionately or contrary to public interest, the Court found that the legislative changes made in 2010 did not entail an action of such characteristics.
- In particular, with regard to the Investors' expectations, according to the evidence examined and the expert opinions analysed, the Court: (i) rejected the argument that the Investors could expect to exploit the solar photovoltaic power plants during a period of between 35 and 50 years without essential modifications to the power plants being made which would have entailed the loss of the regulated tariff, and (ii) declared that it was not reasonable to expect that no changes could be made to the number of hours eligible for the tariff.
- Basically, the Court rejected the claim that the amendments are disproportionate, because it considered these to be adjustments and adaptations which "did not suppress the fundamental characteristics of the existing regulatory framework", since the operators of solar photovoltaic power plants retained their rights to receive a tariff and sell, as a matter of priority, all the energy they generated to the system.
- In addition, the Arbitration Tribunal considered the protection mechanisms offered under Spanish law against the amendments, to be sufficient.
- The Court also stated that the legislative changes are not retroactive because the 2010 regulations were applied from the time of their entry into force to those power plants already operating, but not retroactively to previous periods.

Decision on costs

The decision of the Arbitration Tribunal considers all of the Investors' petitions to have been rejected and Spain's jurisdictional objections to have been dismissed. As a result, the Award:

- Ordered the Investors to pay 50 % of the fees of Spain's legal representative —while considering the attorney's fees claimed by Spain to be out of proportion and limiting the total in this regard to 1 million euros (i.e. ordering the Investors to pay 500,000 euros for this)—.
- Ordered the Investors to pay 50 % of the costs of the arbitration proceedings.
- Ordered the Investors to pay all fees charged by the experts in preparing their opinions for Spain and all expenses for holding the hearings.

All in all, the Investors were ordered to pay arbitration expenses totalling 1.31 million euros.

Dissenting opinion

The arbitrator Guido S. Tawil expressed an opinion which dissented from that of the majority of the Tribunal:

- He did not disagree with the finding of no breach in terms of indirect expropriation (Art. 13 ECT).
- He disagreed regarding the creation of legitimate expectations for the Investors, with the ensuing breach of Article 10 ECT, considering that the remuneration system of the Special Regime contained in RD 661/07 and 1578/08 led to the investment being made and that the Investors were thus led to objectively believe that the tariff system contained in said Royal Decrees would not change.

IV. Conclusions

This decision by the Arbitration Tribunal is important, because: (i) it is the first award in relation to claims brought against Spain due to breaches of the ECT, (ii) it was rendered by a Court consisting of highly-reputed arbitrators, and (iii) the substantiation of the case is clear and exhaustive.

However, its significance with regard to pending awards in proceedings underway or others to be potentially brought in the future will be limited, because:

- Due to the very nature of the award, it is not binding upon other arbitration tribunals or jurisdictional bodies.
- The decision only pronounces on the legislative changes of 2010 in the photovoltaic sector, which are less significant in scope than those made in 2013 and 2014.
- That said, for claims against Spain due to regulatory changes in respect of the same or similar technologies to succeed, the award is very useful in indicating that it will be important to establish:
  - The investment must have lost nearly all of its value as a result of the legislative changes.
  - The frustration of legitimate expectations must be due to the suppression of the fundamental characteristics of the existing regulatory framework (i.e. the right to receive the tariff and the priority sale of the electricity generated) and must not be subject to objective criteria.
  - The retroactivity must affect power plants existing prior to the date when the legislative changes are approved.

CONTACTS

Clifford Chance
Paseo de la Castellana, 110
28046 Madrid
T. +34 91 590 75 00

José Antonio Caínzos
Head of Litigation & Dispute Resolution
E. Joseantonio.Cainzos@CliffordChance.com

Juan José Lavilla
Head of Public Law
E. JuanJose.Lavilla@CliffordChance.com

Ignacio Díaz
Senior Associate, LItigation & Resolution
E. ignacio.diaz@cliffordchance.com