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Spanish Energy Arbitration Saga: Green Light for Investors Claiming Breach of FET?

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On May 4, 2017 the third final award on the Spanish energy arbitration saga was unveiled. After two wins against *Charanne* and *Isolux Infrastructure* (both SCC), this time the foreign investors scored a point, leaving the overall score table at 2-1. In *Eiser*, the first ICSID case to reach a final award related to the measures Spain applied to roll-back certain incentives and benefits offered to promote investment in the Concentrated Solar Power (CSP) sector, the tribunal awarded €128 million to the investors.

Eiser argued that the measures Spain applied in 2013 and 2014, specifically the Royal Decree-Law ("RDL") 9/2013, Royal Decree ("RD") 413/2014, and Ministerial Order IET/1045/2014, expropriated its investments, breached the FET, imposed exorbitant measures against the investment, and did not honor Spain's commitments. The Tribunal composed of John Crook (Chairman), Stanimir Alexandrov, and Campbell McLachlan, narrowed the analysis of Eiser's claim to the breach of the FET standard and found that Spain breached Article 10(1) of the Energy Charter Treaty ("ECT").

Bearing in mind that there are many cases pending against Spain based on the regulatory changes that affected the CSP sector, this piece will focus on the Tribunal's approach to the threshold of the FET standard under the ECT. Does this award represent a turning point in favor of photovoltaic foreign investors in Spain? Did this Tribunal take a different approach from the one in *Charanne* to analyze the investor's legitimate expectations under the FET standard?

In their arguments, the parties discussed two main issues relating to a foreign investor's legitimate expectations: whether FET protects the investor's right to an immutable and stable framework; and which type of profits investors can claim for violation to their legitimate expectations. Eiser argued that RD 661/2017, the regulatory framework under which they made their investment, granted Eiser immutable economic rights that were protected by the ECT's FET standard, guaranteeing stable and transparent conditions for the investment, and that Spain's measures drastically changed the regulatory framework by eliminating and substituting RD 661/2017 with a completely different and arbitrary regime. On the other hand, the Respondent sustained that Eiser could not expect that RD 661/2007 would remain frozen, and that the investor only had a right to receive reasonable

profits.

The Tribunal recognized that the FET standard does not grant foreign investors a "right to regulatory stability *per se*," meaning that States always preserve their right to modify their regulatory regimes to adapt to circumstances and changing public needs (¶362). In the absence of specific commitments of the State directly extended to investors, the key issue for the Tribunal was to determine to which extent a foreign investor can trigger the FET protection provided in an investment treaty (in this case, the ECT) and be awarded with compensation as a response to the host State's action.

The Tribunal concluded that Article 10(1) of the ECT protects investors from a fundamental regulatory change -total and unreasonable- in a manner that does not take into account the circumstances of existing investments made in reliance on the prior regime (¶363). Fundamentally the Tribunal recognized that an investor's right to a legal stability is an important element of the FET that must be protected; however, this right is not unlimited.

Three factors enabled the Tribunal to reach to this conclusion. As a preliminary matter, citing to *ADC v. Hungary,* the Tribunal recognized that the regulatory power of the state has a limit that is established by the commitments assumed under investment treaties that cannot be ignored. The Tribunal reasoned that although Spain did experience a legitimate public policy problem with the tariff deficit, and that the decision to take measures in order to remedy said situation was necessary, the Spanish authorities had to take those measures considering the obligations Spain undertook under the ECT, including the obligation to treat foreign investors in a fair and equitable fashion (¶371).

Second, the interpretation of the FET under the ECT shall take into account the ECT objectives of legal stability and transparency (¶379). This Tribunal understood that the State's obligation to provide FET to investors necessarily implies that the State shall provide fundamental stability in the essential features of the legal framework that investor relied on when making the investment. To arrive to this conclusion, the Tribunal interpreted Article 10(1) under Article 31 of the Vienna Convention on the Law of Treaties, that is, "in good faith and in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose." With this approach, the Tribunal recognized that the objective of the ECT is to provide a legal framework that will foster long term cooperation, and the treaty is just an instrument to increase the stability that is required to fulfill this purpose. Another element that reinforces this approach is that Article 10(1) expressly states that "the Parties shall create stable, equitable and transparent conditions."

Thirdly, the obligation of the State to provide stability to the essential features of the regimen under which the investments was made has become a rule to most tribunals. Indeed, in this case the Tribunal referred to leading cases that supported this view (¶383), such as *Total v. Argentina* (ARB/04/01), where it was decided that "an investor has the right to expect that the legal framework will respect basic elements of the investments." In *El Paso v. Argentina* (ARB/03/15), the tribunal concluded that the measures adopted by the State considered as a whole, altered the prior legal framework that the investor took in consideration when making the investment and

dismantled the existing regulatory framework that was established to attract investors. Moreover, in *CMS v. Argentina* (ARB/01/08) it was decided that the measures transformed and completely modified the legal and business framework in relation to the framework under which the investment was decided to be performed.

Eiser's Tribunal established a high threshold to find a breach of the ECT's FET standard in the absence of State's specific undertakings. As stated, the regulatory modification must be fundamental, total, and unreasonable, and must not consider the circumstances under which the existing investment was done. In this sense, the Tribunal concluded that Article 10(1) granted investors the right to expect that Spain would not modify the regimen under which the investment was done, in a drastic and unexpected way that would destroy the investment (¶387).

It is interesting to note that the Tribunal's approach to the applicable standard of the FET does not contradict the Tribunal's approach adopted in *Charanne*. Although the final outcomes differ greatly, *Charanne's* tribunal applied the same approach to legal stability and dramatic changes to the rules of the game. Said Tribunal considered that an investor has the legitimate expectation that any modification to the legal framework in which the investor based its investment shall not be unreasonably, contrary to the public interest, or disproportional. In effect, the Tribunal considered that a modification is disproportional when it occurs suddenly and unexpectedly removing the essential features of the regulatory framework in place (¶370). Having said this, the differences between both cases were the regulatory measures under consideration, not the standard applied by the Tribunal.

In conclusion, this award might show a trend for future cases challenging RDL 9/2013, RD 413/2014, and Ministerial Order IET/1045/2014 under the ECT's FET. For this Tribunal, Spain breached the FET standard under the ECT because the measures adopted by the State, fundamentally changed and did not consider the basic features under which Eiser's investment was made, thus frustrating Eiser's legitimate expectations. Interestingly, the difference with *Charanne* was the regulatory measures under analysis, not the approach the Tribunal used to analyze them.

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