RENEWABLE ENERGY INVESTMENTS – INTERNATIONAL PROTECTIONS TO MITIGATE RISKS

Samantha J. Rowe, Merryl Lawry-White, Alma M. Mozetič
Debevoise & Plimpton LLP

I. Introduction

The 191 parties to the Paris Agreement have committed to its goal to limit global warming to below two degrees Celsius, preferably to 1.5 degrees Celsius, compared to pre-industrial levels. They are increasingly relying upon renewable energy sources as part of the transition to a net-zero future. Japan, South Korea, the U.S., the U.K. and the EU, among others, have all committed to net zero by 2050, and the U.K. has committed to a world-leading reduction of 78% by 2035.

This shift in energy sources has increased importance following the International Energy Agency's May 2021 roadmap to net zero, which "requires the immediate and massive deployment of all available clean and efficient energy technologies, combined with a major global push to accelerate innovation."[1] The IEA's roadmap also envisages that "[b]eyond projects already committed as of 2021 . . . no new oil and gas fields [should be] approved for development . . . and no new coal mines or mine extensions are required."[2]

To meet these goals, countries need to attract private investment estimated at approximately US$1.7 trillion by 2030.[3] Governments across the globe have created incentives regimes to attract private investment into alternative and renewable energy sources. Such regimes are particularly attractive to investors in this sector because of the high up-front capital investment requirements and the need to wait several years to realize a return on investment. But incentives can be vulnerable to subsequent reversal or amendment by governments that may significantly impact the viability of the investment.

Investment treaties and the protection and remedies they offer to foreign investors can mitigate against these political and legal risks. This article provides a brief overview of the main protections available in investment treaties and highlights

[1] International Energy Agency, *Pathway to critical and formidable goal of net-zero emissions by2050 is narrow but brings huge benefits, according to IEA special report* (18 May 2021), available at https://www.iea.org/news/pathway-to-critical-and-formidable-goal-of-net-zero-emissions-by-2050-is-narrow-but-brings-huge-benefits-according-to-iea-special-report.

[2] International Energy Agency, *Net Zero by 2050: A Roadmap for the Global Energy Sector* (May 2021), available at https://iea.blob.core.windows.net/assets/20959e2e-7ab8-4f2a-b1c6-4e63387f03a1/NetZeroby2050-ARoadmapfortheGlobalEnergySector_CORR.pdf, at 21.

[3] International Renewable Energy Agency ("IRENA"), *Investment Needs*, available at https://www.irena.org/financeinvestment/Investment-Needs.

some procedural and strategic considerations that investors should keep in mind when they make or restructure their investments. The article then addresses changes to the renewables regulatory regime in certain jurisdictions, and how investment treaty protections have been used—or may in the future be used—in these contexts.

II. What International Protections and Remedies Are Available to Investors?

Investment treaties are agreements between states aimed at attracting and promoting foreign investment. They set out certain protections that an investor from one party to the treaty will enjoy in relation to its investment in another party. If a state does not respect the written protections, most treaties provide investors with a direct right of action before an international arbitration tribunal against the government for breach of the treaty.

Over 2,600 investment treaties are currently in force. They can be broadly divided into two categories: bilateral (such as the U.S-Argentina 1994 Bilateral Investment Treaty) and multilateral (such as the Energy Charter Treaty (ECT) or the United States-Mexico-Canada Agreement (USMCA), which succeeded the North American Free Trade Agreement (NAFTA)). While each treaty is unique and contains its own specific definitions of investor and investment, investments treaties typically will protect foreign investors in renewable energy projects, whether the investment is in the form of equity or debt.

Each treaty is also unique in terms of substantive protections, but many protect against unfair or inequitable treatment, expropriation without compensation (including “indirect” or “creeping” expropriation), and arbitrary or discriminatory measures. The fair and equitable treatment and expropriation provisions have proved to be the most relevant to renewable investors.

III. Spain and Italy: Tariff Cuts and International Claims

Spain and Italy have faced the highest number of investment treaty claims by aggrieved investors as a result of the roll-back of investment incentives in the renewable energy sector.

In 2007, Spain enacted a royal decree that provided for regulated tariffs and special premiums for solar photovoltaic (PV) energy. The 2007 decree built on Spain’s efforts since 2004 to attract investment in renewables. However, concerns that the feed-in tariffs were overly generous were exacerbated by the 2008 financial crisis. Financial losses in the electricity system totalled EUR 25.5 billion by the end of 2012,[4] a consequence of power generation and distribution costs exceeding what utilities companies could recover from consumers.

---

[4] *See also* Debevoise & Plimpton LLP, *Solar Arbitrations: A Year in Review* (22 October 2019), available at https://www.debevoise.com/insights/publications/2019/10/solar-arbitrations-a-year-in-review.

Between 2010 and 2014, Spain sought to contain these losses in part by rolling back solar energy subsidies. These measures have given rise to approximately 45 investment arbitrations against Spain, many of which were brought under the ECT. Investors most commonly complained that these policy changes breached their right to fair and equitable treatment and amounted to expropriation.

At least 16 investors have secured awards against Spain,[5] which totalled over USD 1 billion by the end of October 2020.[6] Investors routinely win tens, and even hundreds, of millions of dollars in compensation, and one investor won USD 128 million, plus interest, in a single case.[7]

Based on publicly available information, Spain has prevailed on the merits in at least six cases. Tribunals that dismissed claims against Spain usually placed emphasis on Spain's inherent right to regulate, particularly to lead the country out of financial difficulties. They also dismissed cases based on a finding of no breach of the treaty on the particular facts of the case, which often turned on the timing of a particular investment. For example, some tribunals found that investors who invested later in time should not legitimately have expected the subsidies to continue without further change. Conversely, when investments were made before the promulgation of the energy subsidies, tribunals found that such investments could not have been made in reliance on the subsidies. Other tribunals were not convinced that there was clear evidence of harm in circumstances where the claimant continued to enjoy its investment. Another tribunal found that Spain acted transparently and in good faith, particularly by consulting with lobby groups before implementing the cuts.[8]

Like Spain, Italy faced a flurry of investment claims arising from its solar subsidy cuts. Italy has been named as a defendant in twelve renewables cases, five of which are still pending. Three awards have been rendered in favor of the investors, whereas Italy prevailed in five cases. Here again, claimants have won tens of millions of dollars in damages.

IV. Lessons Learned? From Europe to Mexico and Japan

Spain and Italy may prove to be important examples for other countries that have implemented or are implementing rollbacks on renewable energy incentives, including Mexico and Japan.

---

5 The article is current as of 28 June 2021, unless stated otherwise.

6 GAR, *Renewables investors to renounce awards against Spain* (6 October 2020), available at https://globalarbitrationreview.com/renewables-investors-renounce-awards-against-spain (citing *El Pais*).

7 *Eiser Infrastructure Limited and Energía Solar Luxembourg S.à r.l. v. Kingdom of Spain*, ICSID Case No. ARB/13/36.

8 *FREIF Eurowind Holdings Ltd v. Kingdom of Spain*, SCC Case No. 2017/060, Final Award, 8 March 2021, para. 525.

A. Reforms to the Mexican Electricity Market?

Since taking office in 2018, President López Obrador has sought to introduce sweeping changes to Mexico's electricity sector and largely reverse a series of energy reforms that were enacted in 2013. The 2013 reforms opened the energy sector to private investment and provided incentives for investments in renewable energy. In March 2021, Congress enacted a bill introduced by President López Obrador that seeks to amend the Electricity Industry Law (the Reform Bill). The Reform Bill would reverse prior incentives that gave priority to renewable sources of energy by changing the order of dispatch of power to the national grid. Under the Reform Bill, renewable energy sources will be relegated behind all power generated by the Federal Electricity Commission (CFE), the former state monopoly, including power generated from fossil fuels.

Mexican courts have issued injunctions that temporarily suspend the effects of the Reform Bill. In addition, the Mexican Supreme Court has decided to hear *en banc* a challenge to the constitutionality of the legislation, with the decision expected within the next six months to a year.

The Reform Bill is the latest in a series of adverse measures directed at the renewables sector over the past two years. The Mexican Government's earlier attempts to upend the regulatory framework—through executive action—were successfully challenged. As a legislative act, however, the Reform Bill presents a significant threat to the sector.

Many foreign and local investors already have invoked *amparo* proceedings under domestic law. International investment agreements between the foreign investor's home country and Mexico may also provide a strong source of protection. Mexico is party to a wide range of treaties, including the United States–Mexico–Canada Agreement, the Comprehensive and Progressive Agreement for Trans-Pacific Partnership, and bilateral treaties with Spain, the Netherlands and the U.K., among others. It is important that foreign investors in the sector devise a coordinated strategy drawing on domestic and international law to preserve their rights, as well as avenues to secure legal remedies.

B. The First Case Against Japan

Japan is another country where there is the potential for legal claims in respect of changes to incentives for renewable investments. In 2012, in the wake of the 2011 Fukushima nuclear disaster, Japan introduced the renewable energy subsidy regime in the form of generous feed-in-tariffs to encourage investment in solar and other renewable energy projects. The feed-in tariffs were effectively agreed prices at which electric utilities and merchants could purchase renewable-generated electricity. This regime reduced investment risk at a time when solar equipment costs were falling rapidly. These two conditions created a powerful incentive that led to many investments into PV plants in Japan. About a year later, however, the government began steadily cutting the feed-in tariff rates and put in place deadlines for certain plants—licensed prior to the regulatory changes—to begin operations. According to some estimates, the subsidy cuts and revised regulatory framework have forced more than 250 solar companies into bankruptcy since 2018.[9]

In March of this year, it was reported that a Hong-Kong-based energy fund had brought a claim against Japan over the rollback of renewable subsidies. This is understood to be the first-ever international arbitration claim brought under a bilateral investment treaty with Japan. There is speculation that this claim may be the first of many such claims against Japan, particularly considering that Hong Kong and Chinese investors are among the main foreign investors in Japan's renewable energy market.[10]

V. Conclusion

As climate imperatives and commitments require a dramatic and rapid shift towards renewable sources of energy, investments in renewable energy sources will continue to increase in demand. Investors would be well advised to consider investment treaties when structuring their investments. The Spanish example, in particular, illustrates how protections may be invoked when governments drastically change regulatory regimes that investors relied on when making investments.

Before formally commencing a claim and seeking damages before international arbitration tribunals, simply putting a government on notice of a claim can provide a powerful incentive for the government to negotiate. Investment-treaty claims can drive policy change. At the end of 2019, Spain introduced a new regime, Royal Decree-law 17/2019, to end pending treaty claims valued at over USD 7 billion. The new law guarantees higher returns to renewable energy investors in exchange for renouncing their pending claims or awards against Spain. A number of claimant investors reportedly have signed up or are considering doing so.[11]

---

9 Financial Times, *Hong Kong energy fund sues Japan in groundbreaking case* (3 March 2021), available at https://www.ft.com/content/155da1d7-075e-4122-adec-1e4fec51f582 (citing *Teikoku Databank*).

10 GAR, *Japan faces first treaty claim* (3 March 2021), available at https://globalarbitrationreview.com/japan-faces-first-treaty-claim (citing the *Financial Times*).

11 GAR, *Renewables investors to renounce awards against Spain* (6 October 2020), available at https://globalarbitrationreview.com/renewables-investors-renounce-awards-against-spain; *see also* GAR, *Spain offers incentives to end renewables claims* (22 November 2019), available at https://globalarbitrationreview.com/spain-offers-incentives-end-renewables-claims. Most recently, in May 2021, RREEF Infrastructure filed a joint status report before a U.S. federal district court stating that it had executed, pursuant to Royal Decree-Law 17/2019, a release to forgo the portion of the arbitral award pertaining to its investment in the wind power plants (without affecting the portion of the award corresponding to the losses in the investment in the solar power plants). *RREEF Infrastructure (G.P.)*

Limited and RREEF Pan-European Infrastructure Two Lux S.A.R.L. v. Kingdom of Spain, No. 19-cv-03783 (D.D.C. 6 May 2021) [Dkt. No. 34], at [2].