

Modification of Renewable Energy Support Schemes Under the Energy Charter Treaty: *Eiser* and *Charanne* in the Context of Climate Change

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Abstract

Nearly half of the claims brought under the *Energy Charter Treaty*¹ raise issues related to the modification of the Renewable Energy Support Schemes (RESs), but only two decisions have been published: *Charanne* and *Eiser*. This paper evaluates these decisions in light of the existing general practice on expropriation and Fair and Equitable Treatment, as well as from a pragmatic perspective in the context of climate change. The article concludes that tribunals should recognize reinforced stability to RESs under the *ECT*.

A. Introduction: Vulnerability of Renewable Energy Support Schemes

The decade of the 2000s witnessed the adoption of several RESs in Europe. In accordance with the Directives *2001/77/EC* and *2009/28/EC*, the Member States designed investor-friendly regulations, implementing different benefits such as Feed-in Tariffs, Feed-in Premiums, Green Certificates, Quota Obligations, Loans, Subsidies, Net-Metering or Tax Exemptions. However, the progressive elimination of some of the incentives initially provided has shown these schemes are particularly vulnerable towards regulatory changes.

If one compares renewable energies with conventional energies, one might come to the conclusion that the particular vulnerability of RESs could find its origins mainly in the high costs of production and the unpredictability of the results of its implementation. Regarding the first factor – the high costs – production from renewable energies is more expensive than production from conventional sources of energy.² In fact, the experience on RESs shows that the prices of household supply have increased due to the need for subsidization³ – jeopardizing the affordability of the service. On an industry level, the higher costs of energy supply might increase the costs of production for different sectors

¹ *Energy Charter Treaty*, 17 December 1994, 2080 UNTS 95 [ECT].

² See J. P. Morgan, 'A Brave New World: Deep De-Carbonization of Electricity Grids', *Eye on the Market Special Edition: Annual Energy Paper (2015)*, available at <https://www.jpmorgan.com/jpmpdf/1320687247153.pdf> (last visited 21 December 2017).

³ Eurostat, Eurostat statistics explained, electricity price statistics, File: Development of electricity prices for household consumers, EU-28, 2008-2016 (EUR per kWh) YB17.png, available at [http://ec.europa.eu/eurostat/statistics-explained/index.php/File:Development_of_electricity_prices_for_household_consumers,_EU-28,_2008-2016_\(EUR_per_kWh\)_YB17.png](http://ec.europa.eu/eurostat/statistics-explained/index.php/File:Development_of_electricity_prices_for_household_consumers,_EU-28,_2008-2016_(EUR_per_kWh)_YB17.png) (last visited 21 December 2017).

of the economy⁴ and, therefore, may affect their competitiveness in a globalized market. As a consequence, governments might be tempted to modify the RESs not only as a way to foster exports and maximize the social welfare, but also in order to satisfy the claims of the civil society and the industries, which might put pressure to lower the prices by returning to conventional sources of energy.

The second factor of particular vulnerability – the unpredictability of the results – refers to the fact that the production of renewable energies is less predictable than the production of conventional energies,⁵ since the technologies involved in renewable energy are heavily dependent on innovation and the natural conditions on which they rely are very often unstable. If, given this unpredictability, the adoption of a scheme reaches its objective in less time than what was expected or, on the contrary, fails to achieve the estimated results, it is likely that the government chooses to modify the legal framework by removing the benefits.

Besides the particular vulnerabilities just described, renewable energies and conventional energies share the regulatory risks typical to long long-term contracts and licenses that require a considerable amount of time to achieve pay-out. The dynamics of the regulatory instability affecting these long-term energy investments are well depicted by Cameron's *cycles*: “[...] [the] obsolescing bargain [...]” and “[...] the price cycle [...]”.⁶ In the *obsolescing bargain* cycle, the investor concludes a contract and/or obtains a license to undertake a long-term energy project under certain favorable regulatory conditions, but as time passes by, these conditions might appear obsolete to the government, who will attempt to change them to the detriment of the investor. In this regard, the change of government, the volatility of the economy, the discovery of new energy resources or the pressure of the community, etc. – in addition to the fact that the investor has already perfected the investment – may incentivize the government to force a renegotiation of the terms and conditions of the exploitation.⁷ On the other hand, *the price cycle* relates to the situation where the investor concludes a contract and/or obtains a license to undertake a long-term energy project under certain conditions based on specific price assumptions; however, the market

⁴ See ECOFYS, ‘Electricity Costs of Energy Intensive Industries an International Comparison’ (2015), available at <http://www.ecofys.com/files/files/ecofys-fraunhoferisi-2015-electricity-costs-of-energy-intensive-industries.pdf> (last visited 21 December 2017).

⁵ D. Timmons *et al.*, ‘The Economics of Renewable Energy’ (2014), 32, available at http://www.ase.tufts.edu/gdae/education_materials/modules/RenewableEnergyEcon.pdf (last visited 21 December 2017).

⁶ P. D. Cameron, *International Energy Investment Law: the Pursuit of Stability* (2010), 4-7.

⁷ *Ibid.*, 4-5.

price unexpectedly increases in a way that the firm obtains extraordinary good profits. The host government might find this situation disproportionate and, subsequently, it will attempt to adjust the contract or capture some of the investor's earnings through taxation.⁸

The experience regarding the RES adopted in Spain as well as experiences in the Czech Republic, Italy, and Bulgaria, are indeed good examples on how Cameron's cycles operate. After the heavy investments required to develop solar energy were channelled and once the production and consumption targets were achieved – sooner than expected – in the context of the 2008 financial crisis, the conditions of the RESs appeared to the host governments as an obsolete bargain and, consequently, were modified.⁹ Moreover, as if it was predicted by the price cycle, given the sharp decrease of the solar energy production costs, the profits seemed disproportionate to the host governments, adding one more reason for restructuring the RESs.¹⁰

The modification of the RESs in Spain, Czech Republic, Italy, and Bulgaria, was followed by 48 international investor-State arbitration claims under the *ECT*. This means that, currently, 48 out of 99 disputes brought under the *ECT* are related to the modification of the RESs.¹¹ 33 of these claims are against Spain; 3 of them have been resolved; two concluded that Spain is not liable to pay damages and the other considered it is. While *Isolux* remains confidential and the only information available shows that the decision favours

⁸ *Ibid.*, 5.

⁹ Regarding the modification of RESs in Europe: D. Behn & O. K. Fauchald, 'Governments Under Cross-Fire? Renewable Energy and International Economic Tribunals', 12 *Manchester Journal of International Economic Law*, (2015) 2, 117, 120; J. Tirado, 'Renewable Energy Claims Under the Energy Charter Treaty: An Overview', 13 *Oil Gas & Energy Law*, (2015) 3, 8; G. Bellantuono, 'Regulatory Stability in the Energy Sector: the Italian Experience', University of Trento, Working Paper, 2016, 4, available at <http://ssrn.com/abstract=2790980> (last visited 21 December 2017); B. Vasani *et al.*, 'Bulgaria: International Remedies for Foreign Investors in Bulgaria's Renewable Energy Sector', available at <http://www.lexology.com/library/detail.aspx?g=b755a41f-d1b0-41a3-a485-6b4108a93505> (last visited 21 December 2017).

¹⁰ In fact, from 2009 to 2014 photovoltaic modules' prices decreased in 80 %. See IRENA, 'REthinking Energy: Renewable Energy and Climate Change' (2015), 12, available at http://www.ren21.net/wp-content/uploads/2015/11/IRENA-_REthinking_Energy_2nd_report_2015.pdf (last visited 21 December 2017).

¹¹ *International Energy Charter, List of all Investment Disputes Settlement Cases*, available at <http://www.energycharter.org/what-we-do/dispute-settlement/all-investment-dispute-settlement-cases/> (last visited 21 December 2017).

Spain, *Charanne*¹² and *Eiser*¹³ are published and arrived to opposite conclusions regarding liability.

In *Charanne*, the Tribunal found that the firm did not breach the expropriation, nor the *fair and equitable treatment* (FET) protections.¹⁴ Contrarily, in *Eiser*, the Tribunal ordered the Host Government to pay the investor 128 million euros for breaching the FET provision.¹⁵ As it is shown in both cases, the Protections provided in Article 10 (1) *ECT* – on FET – and Article 13 *ECT* – concerning expropriation – should be the most frequently invoked in the massive number of claims. However, it should be noted that issues on the jurisdiction of the Tribunal were discussed in both cases¹⁶ and the effective protection and enforcement of rights duty was discussed in *Charanne*.¹⁷ Nevertheless, these two topics will not be addressed in this paper, since the former deals with procedural law rather than with protections against the risks to the investors, and the latter might not be general to all the cases for the modification of RESs.

The objective of this paper is to evaluate *Charanne* and *Eiser* in light of the existing general practice on expropriation and FET, as well as from a pragmatic point of view in the context of climate change. For this purpose, the factual background of both Decisions (B.) is followed by the study of the parties' elaboration (C.), which serves not only to understand the particular arguments that were raised, but also to lay out the variety of interpretations in the case-law when addressing the conflict between the protection of the investor's interests and the right of the States to regulate. Next, the paper critically analyses from a pure legal perspective the particular features that influenced the outcome in both cases (D.) to finally, in the last section, propose a pragmatic approach that fosters the goal of levelling global warming (E.).

¹² *Charanne B.V. and Construction Investments S.A.R.L. v. The Kingdom of Spain*, Final Award, Arbitration No. 062/2012, 21 January 2016, available at <http://www.italaw.com/cases/2082#sthash.Ut5QaoXA.dpuf> (last visited 21 December 2017) [*Charanne*].

¹³ *Eiser Infrastructure Limited and Energía Solar Luxembourg S.A.R.L. v. The Kingdom of Spain*, Final Award, ICSID Case No. ARB/13/36, 4 May 2017, available at <https://www.italaw.com/cases/5721#sthash.BgklL7i2.dpuf> (last visited 21 December 2017) [*Eiser*].

¹⁴ *Charanne*, *supra* note 12, para. 573.

¹⁵ *Eiser*, *supra* note 13, para. 474.

¹⁶ *Ibid.*, 50-109. *Charanne*, *supra* note 12, paras. 394-450; see E. Bonafé & G. Mete, 'Escalated Interactions Between EU Energy Law and the Energy Charter Treaty', 9 *The Journal of World Energy Law & Business* (2016) 3, 174-188.

¹⁷ *Charanne*, *supra* note 12, paras. 488-474.

B. The Factual Background

The facts in both cases, even if related, originate to a considerable degree in the application of different sets of modifications that were issued in different moments. The competence of the Tribunal in *Charanne* is limited to the measures taken by the Spanish government from 2007 to 2010, leaving aside the modifications from then onwards. *Eiser* comprehends a wider universe, which covers not only the measures taken by the Host Government from 2007 to 2010, but also those that were adopted from 2012 to 2014, which had a deeper impact on the profits of the solar energy investors in Spain.

Charanne (2007-2010)

In November 1997, the Spanish Parliament enacted the *Ley 54/1997* (Act 54/1997)¹⁸ on the regulation of the energy sector.¹⁹ The *Ley 54/1997* established two regimes: a general regime and a special regime.²⁰ As opposed to the general regime, which was applicable to conventional sources of energy, the special regime contained special benefits to investments in renewable energies.²¹ The benefits of the special regime included priority access,²² the right to connect the facilities to distribution and transmission grids, the right to use third parties' energy, and the redistribution through a premium tariff scheme.²³

Almost 8 years after the enactment of *Ley 54/1997*, the government passed the *Real Decreto 436/2004* (*Royal Decree 436/2004*)²⁴ in order to regulate the special regime. However, this instrument – practically immediately – proved itself insufficient to foster considerable investments in the energy sector. Consequently, beginning in 2005, the government adopted an aggressive campaign to promote

¹⁸ *Boletín Oficial del Estado* (B.O.E), number: 285/1997, publication date: 28 November 1997, 35097-35126, available at <https://www.boe.es/buscar/doc.php?id=BOE-A-1997-25340> (last visited 21 December 2017).

¹⁹ *Charanne*, *supra* note 12, para. 82.

²⁰ *Ibid.*, para. 84.

²¹ *Ibid.*

²² *Ibid.*

²³ *Ibid.*, paras. 87-88.

²⁴ *Boletín Oficial del Estado* (B.O.E), number: 75/2004, publication date: 27 March 2004, 13217-13238, available at <https://www.boe.es/buscar/doc.php?id=BOE-A-2004-5562> (last visited 21 December 2017).

investments, such as road shows and official documents emphasizing the need for regulatory stability, as well as forecasting brilliant returns for investors.²⁵

The promotion of investments in the Spanish solar energy sector resulted in the enactment of the *Real Decreto 661/2007 (Royal Decree 661/2007)*,²⁶ which developed the principles established in the *Ley 54/1997* regarding solar power and confirmed that the operators of photovoltaic installations were entitled to a reasonable return.²⁷ The benefits under this Decree encompassed the connection to the distribution and transportation grid, the access of the total energy produced to the grid, the right to a regulated tariff or prime, the possibility of performing direct sales, priority access, and priority connection.²⁸

The *Real Decreto 661/2007* rocketed investments in photovoltaic installations and the production of solar energy in Spain.²⁹ The success of this scheme was rooted in setting an attractive regulated tariff or a premium to investors for a 25-year period (Arts. 35-37 and 44; Annexes 7-8 and 12), which would be, subsequently, amended for a second period (Art. 36). Very soon after the enactment of the *Real Decreto 661/2007*, the goals established by the Spanish government for solar energy production were achieved. Thus, the government enacted a new Decree, *Real Decreto 1578/2008 (Royal Decree 1578/2008)*,³⁰ which established a pre-registry burden on photovoltaic installations and a quarterly tender process for the applicability of regulated tariffs (Arts. 4 and 5). It also limited the application of the regulated tariff to the first period of 25 years (Art. 11.5).

The limitation of 25 years was later extended to the photovoltaic installations registered under *Real Decreto 661/2007* by the enactment of the *Real Decreto 1565/2010 (Royal Decree 1614/2010)*³¹ (Art. 29.2). In other words,

²⁵ Charanne, *supra* note 12, para. 95 and paras. 102-130, Eiser, *supra* note 13, para. 358.

²⁶ *Boletín Oficial del Estado* (B.O.E), number: 126/2007, publication date: 1 June 2007, 22846-22886, available at <https://www.boe.es/buscar/doc.php?id=BOE-A-2007-10556> (last visited 21 December 2017).

²⁷ Charanne, *supra* note 12, para. 111.

²⁸ *Ibid.*, para. 118.

²⁹ *Boletín Oficial del Estado* (B.O.E), number: 126/2007, 22846-22886, publication date: 1 June 2007, available at <https://www.boe.es/buscar/doc.php?id=BOE-A-2007-10556> (last visited 21 December 2017).

³⁰ *Boletín Oficial del Estado* (B.O.E), number: 234/2008, publication date: 27 September 2008, 39117-39125, available at <https://www.boe.es/buscar/doc.php?id=BOE-A-2008-15595> (last visited 21 December 2017).

³¹ *Boletín Oficial del Estado* (B.O.E), number: 298/2010, publication date: 28 December 2010, 101853-101859, available at <https://www.boe.es/buscar/doc.php?id=BOE-A-2010-18915> (last visited 21 December 2017).

the regulated tariff for the second period was abolished for installations regulated under *Real Decreto 661/2007*. This measure was only the first of a set of measures that would affect *Charanne's* interests in solar energy production. Succeeding its implementation, the *Real Decreto Ley 14/2010 (Royal Decree Act 14/2010)*³² imposed on operators the payment of an access fee to the grid of 0.5 euros per megawatt and *Real Decreto 1614/2010* limited the operation hours that would be subject to the benefits of the regulated tariff (Art. 2). Additionally, *Real Decreto 1565/2010 (Royal Decree 1565/2010)*³³ imposed some technical obligations regarding the control to the tension gaps, which significantly increased the costs for the investors without obtaining any compensation.³⁴ These new burdens and costs were justified in the government's perspective by the considerable growth in energy production and the deficit of the tariff scheme.

According to the claimant, the abovementioned modifications reduced the profitability of the firm by 10 % with regards to the installations subjected to the *Real Decreto 1578/2008* and 8.5 % to those subjected to the *Real Decreto 661/2007*.³⁵ Consequently, on May 7 2012 – after the parties failed to reach an agreement on the controversy within the three-month period provided by Article 26 *ECT* – *Charanne* filed notice of arbitration request before the Arbitration Institute of the Stockholm Chamber of Commerce (SCC).³⁶

Eiser (2012-2014)

In December 2012, a new government was appointed in Spain. The government publicly expressed its intention to tackle the tariff deficit of the energy system, whose amount was calculated to be 22.000 million euros.³⁷ The enactment of *Ley 15/2012 (Act 15/2012)*,³⁸ which taxed the access to the grid

³² *Boletín Oficial del Estado* (B.O.E), number: 163/2010, publication date: 6 July 2010, 59628-59652, available at <https://www.boe.es/buscar/doc.php?id=BOE-A-2010-10707> (last visited 21 December 2017).

³³ *Boletín Oficial del Estado* (B.O.E), number: 283/2010, publication date: 23 November 2010, 97428-97446, available at <https://www.boe.es/buscar/doc.php?id=BOE-A-2010-17976> (last visited 21 December 2017).

³⁴ *Charanne*, *supra* note 12, para. 152.

³⁵ *Charanne*, *supra* note 12, para. 284.

³⁶ *Ibid.*, para. 14.

³⁷ *Eiser*, *supra* note 13, paras. 137 and 150.

³⁸ *Boletín Oficial del Estado* (B.O.E), number: 312/2012, publication date: 28 December 2012, 88081-88096, available at <https://www.boe.es/buscar/doc.php?id=BOE-A-2012-15649>

at 7 % (Art. 8), was the first measure in this regard. This tax caused a loss of 95 % to the operator company's income and put the investor in a position where the income was barely enough to service debt – being its service coverage ratio nearly 1.³⁹ Afterwards, *Real Decreto 2/2013 (Royal Decree 2/2013)*⁴⁰ abolished the possibility to adopt the regulated prime, thus the options for the investors were restricted to choose between the market price and the regulated tariff. Furthermore, this Decree discarded inflation as a factor for the calculation of tariff adjustment by replacing it with a lower index.

The group of measures that followed in Spain obliterated the difference between the special regime for solar energy and the general regime for conventional energy. Firstly, *Real Decreto Ley 9/2013 (Royal Decree Act 9/2013)*⁴¹ derogated *Real Decreto 661/2007* and established a new tariff system where the redistribution was based on model costs instead of real costs. This legislation was later complemented by *Ley 24/2013 (Act 24/2013)*,⁴² which derogated *Ley 54/1997 (Act 54/1997)*⁴³ and *Real Decreto 413/2014 (Royal Decree 413/2014)*,⁴⁴ which intended to promote a reasonable profit under the model of an efficient plant. Finally, the *Orden Ministerial IET/1045/2014 (Ministerial Order IET/1045/2014)*⁴⁵ detailed the technical parameters for the assessment of the redistribution.

The investor suffered a huge negative impact as a result of these changes in legislation. On the one hand, the expected income of the investment decreased

(last visited 21 December 2017).

³⁹ *Eiser*, *supra* note 13, para. 144.

⁴⁰ *Boletín Oficial del Estado* (B.O.E), number: 29/2013, publication date: 29 February 2013, 9072-9077, available at https://www.boe.es/diario_boe/txt.php?id=BOE-A-2013-1117 (last visited 21 December 2017).

⁴¹ *Boletín Oficial del Estado* (B.O.E), number: 167/2013, publication date: 13 July 2013, 52106-52147, available at https://www.boe.es/diario_boe/txt.php?id=BOE-A-2013-7705 (last visited 21 December 2017).

⁴² *Boletín Oficial del Estado* (B.O.E), number: 310/2013; publication date: 27 December 2013, 105198-105294, available at <https://www.boe.es/buscar/doc.php?id=BOE-A-2013-13645> (last visited 21 December 2017).

⁴³ *Boletín Oficial del Estado* (B.O.E), number: 285/1997, publication date: 28 November 1997, 35097-35126, available at <https://www.boe.es/buscar/doc.php?id=BOE-A-1997-25340> (last visited 21 December 2017).

⁴⁴ *Boletín Oficial del Estado* (B.O.E), number: 140/2014, publication date: 10 June 2014, 43876-43978, available at https://www.boe.es/diario_boe/txt.php?id=BOE-A-2014-6123 (last visited 21 December 2017).

⁴⁵ *Boletín Oficial del Estado* (B.O.E); number: 150/2014, publication date: 20 June 2014, 46430-48190, available at https://www.boe.es/diario_boe/txt.php?id=BOE-A-2014-6495 (last visited 21 December 2017).

by 66 % in comparison to what was foreseen under *Real Decreto 661/2007*.⁴⁶ On the other hand, the company's income in 2015 was not even enough to cover the operational costs and the service of debt.⁴⁷ Therefore, the investor had to renegotiate with creditors⁴⁸ and reach the agreement that all future incomes above the operational costs would cover financial debt, leaving no room for returns.⁴⁹ As a result, *Eiser* claimed 196 million euros in compensation for loss of profit and 13 million euros for historical loss.⁵⁰

C. Elaboration of the Parties: Investor's Protection v. the Right to Regulate

Charanne and *Eiser* plainly picture the never-ending conflict in international investment arbitration between the State's right to regulate and the investor's protection under international investment agreements (IIAs): while the investors claim that the measures disrupted the regulatory stability and, consequently, negatively affected interests protected under the *ECT*, Spain contends that the measures are in the public interest and correspond to the usual exercise of sovereignty. Both assertions are true, though the question on how to balance the interests between the parties depends to a large extent on the arbitrators' discretion. Certainly, not only the IIA's protections have an open texture, but also the elements used by Tribunals to determine liability, sometimes respond to opposing positions – e.g. police-power doctrine v. sole-effects doctrine – or their scope may differ in the extent – such as the assessment of legitimate expectations or proportionality. This section represents how the lack of consistency of the Tribunals provides fairly good arguments to both parties when addressing the Expropriation and the FET Provisions, by examining the parties' elaborations in light of the existing practice. However, it should be noted that while *Charanne* describes, to a certain extent, the elaboration of the parties regarding both protections, *Eiser* only illustrates the parties' arguments on FET. In the latter, the Tribunal considered, for reasons of judicial economy, that all of the claimant's allegations could be subsumed in the FET.⁵¹ Accordingly, this

⁴⁶ *Eiser*, *supra* note 13, para. 151.

⁴⁷ *Ibid.*, para. 152.

⁴⁸ *Ibid.*

⁴⁹ *Ibid.*

⁵⁰ *Ibid.*, paras. 460 and 457.

⁵¹ *Ibid.*, paras. 352-353.

section addresses both protections in *Charanne*, but only the FET protection in *Eiser*.

Expropriation

The definition of expropriation in the *ECT*, as it has been standardized in most of the IIAs, is broader than the definition endorsed in many national legal systems. The meaning of expropriation in this regard is not restricted to the physical and/or legal taking of property rights (direct expropriation), but also comprehends government actions that produce a similar effect (indirect expropriation). In the *ECT*'s language, this includes measures “[...] having effect equivalent to nationalization or expropriation [...]” (Art. 13 (1)). In general, there is no problem for identifying direct expropriations.⁵² On the contrary, determining when an indirect expropriation has occurred requires a deeper analysis, which entails evaluating the substantiality of the loss, the character of the Host State’s measure, and the generation of legitimate expectations.

The most palpable characteristic of and the first element to be analysed in indirect expropriation cases is *substantiality*. In this regard, the impact must be significant enough to assert that the measure *destroyed* the investment.⁵³ Therefore, an indirect expropriation occurs when the lack of control on the assets “[...] is not merely ephemeral [...]”⁵⁴ and the “[...] rights are rendered so useless that they must be deemed to have [...] expropriated [...]” them.⁵⁵

Given the importance of this criterion, it is natural that, in this kind of dispute, the investor affirms that the measures adopted by the Host Government have an impact substantial enough to constitute an indirect expropriation, while the respondent, on the contrary, holds that the impact of the measures on the company’s asset’s value or control is non-existent or not significant. In this regard, *Charanne*’s dispute is not different from the general practice.

⁵² P. D. Isakoff, ‘Defining the scope of indirect expropriation for international investments’, 3 *Global Business Law Review* (2013) 2, 189, 192.

⁵³ *Técnicas Medioambientales Tecmed S.A. v. The United Mexican States*, Award, ICSID Case No. ARB (AF)/00/2, 29 May 2003, 44, para. 116, available at <http://www.italaw.com/cases/1087#sthash.9Pg82zdi.dpuf> (last visited 21 December 2017) [Tecmed S.A.].

⁵⁴ *Tippetts, Abbott, Mc Carthy, Stratton v. TAMS-AFFA*, Award, 6 Iran-US CTR, 22 June 1984, 225.

⁵⁵ Iran-United States Claims Tribunal, cited in OECD, ‘Indirect expropriation’ and the ‘Right to Regulate’ in International Investment Law’, OECD Working Papers on International Investment, 2004/04, 11, available at <http://dx.doi.org/10.1787/780155872321> (last visited 21 December 2017).

In fact, the loss of the shares' value as well as the loss of profit from the photovoltaic installations due to the Spanish legislative changes were considered by the claimant as measures having an equivalent effect to expropriation, falling under the scope of Article 13 (1) *ECT*.⁵⁶ The claimant considered that *Charanne* – through its subsidiaries – acquired vested rights on the regulated tariffs established in *Real Decreto 661/2007* and *Real Decreto 1578/2008* (*Royal Decree 1578/2008*)⁵⁷ when it registered the installations within the time provided by these regulations.⁵⁸ Consequently, the retroactive application of *Real Decreto 1565/2010* (*Royal Decree 1565/2010*)⁵⁹ and *Real Decreto Ley 14/2010* (*Royal Decree Act 14/2010*)⁶⁰ constituted an expropriatory measure that reduced profitability by approximately 10 %, as mentioned previously.⁶¹ Furthering its elaboration, the claimant stated that this percentage was significant and sufficient to constitute an expropriation, since in its concept “[...] the arbitral jurisprudence does not require the total destruction of the investment [...]”⁶²

The defendant opposed these arguments by stating that the loss experienced by *Charanne* was not substantial enough to constitute an expropriation according to the arbitral jurisprudence.⁶³ In its opinion, the measures did not involve the deprivation of the exploitation or economic use of the investment, neither the interruption of operations nor the control of its shares or assets.⁶⁴ The Host Government added that the measures did not destroy the company's value and, in any case, that there is not any precedent recognizing a concept such as partial expropriation.⁶⁵

Once substantiality has been established, the Tribunal must assess the character of the government's measure in order to determine whether an indirect

⁵⁶ *Charanne*, *supra* note 12, para. 280.

⁵⁷ *Boletín Oficial del Estado* (B.O.E), number: 234/2008, publication date: 27 September 2008, 39117-39125, available at <https://www.boe.es/buscar/doc.php?id=BOE-A-2008-15595> (last visited 21 December 2017).

⁵⁸ *Charanne*, *supra* note 12, para. 282.

⁵⁹ *Boletín Oficial del Estado* (B.O.E), number: 283/2010, publication date: 23 November 2010, 97428-97446, available at <https://www.boe.es/buscar/doc.php?id=BOE-A-2010-17976> (last visited 21 December 2017).

⁶⁰ *Boletín Oficial del Estado* (B.O.E), number: 163/2010, publication date: 6 July 2010, 59628-59652, available at <https://www.boe.es/buscar/doc.php?id=BOE-A-2010-10707> (last visited 21 December 2017).

⁶¹ *Charanne*, *supra* note 12, para. 284.

⁶² *Ibid.*, 64, para. 283.

⁶³ *Ibid.*, para. 343.

⁶⁴ *Ibid.*

⁶⁵ *Ibid.*, paras. 344-345.

expropriation happened, i.e. whether or not the measure is characterized as a public interest measure, non-discriminatory, rational, adequate, proportional, in good faith, etc. A propos, arbitral decisions have adopted two clashing theories. For one theory, the *sole-effect doctrine*, liability should arise disregarding the *public interest* character of the measure, since the expropriation provision focuses on protecting the investor from the economic result.⁶⁶ On the contrary, *the police power doctrine* proposes that a non-discriminatory measure taken in the public interest and in good faith should not entitle the investor to a compensation.⁶⁷ As a consequence, it is normal to find in investor-State arbitration disputes that the claimant adheres to the sole-effect doctrine and the Host State to the police power doctrine; *Charanne* was not the exception.

In this respect, following the sole-effect doctrine, and in order to support the idea that the mere loss was sufficient to define the measure as expropriatory, the company asserted “[...] that it is not necessary to prove the bad faith of the State, but that the essential element [of expropriation] is the effect suffered by the investment.”⁶⁸ Moreover, the claimant affirmed that the most visible evidence that an expropriation occurred was the transfer of wealth from the operators to the Government to cover the electricity tariff deficit.⁶⁹ As a counterargument, following the police power doctrine, Spain argued that the investor’s position in this regard was based on a doctrine that was rejected by subsequent decisions and emphasized on the need to evaluate the nature, purpose, and character of the measures.⁷⁰

⁶⁶ *Metalclad Corporation v. The United Mexican States*, Final Award, ICSID Case No. ARB(AF)/97/1, 30 August 2000, para. 111, available at <http://www.italaw.com/cases/671#sthash.2TPwidW3.dpuf> (last visited 21 December 2017) [*Metalclad Corporation*]; *Azurix Corp. v. The Argentine Republic*, Final Award, ICSID Case No. ARB/01/12, 14 July 2006, paras. 309-313, available at <http://www.italaw.com/cases/118#sthash.pz1dK8UU.dpuf> (last visited 21 December 2017) [*Azurix Corp.*]; *Compañía del Desarrollo de Santa Elena S.A. v. Republic of Costa Rica*, Final Award, ICSID Case No. ARB/96/1, 17 February 2000, para. 72, available at https://www.italaw.com/documents/santaelena_award.pdf (last visited 21 December 2017).

⁶⁷ *Methanex Corporation v. United States of America*, Final Award, 3 August 2005, available at <https://www.italaw.com/sites/default/files/case-documents/ita0529.pdf> (last visited 21 December 2017) [*Methanex Corporation*]; *Saluka Investments B.V. v. The Czech Republic*, Partial Award, 17 March 2006, 52, para. 255, available at <https://www.italaw.com/sites/default/files/case-documents/ita0740.pdf> (last visited 21 December 2017) [*Saluka Investments B.V.*].

⁶⁸ *Charanne*, *supra* note 12, 65, para. 286.

⁶⁹ *Ibid.*, para. 289.

⁷⁰ *Ibid.*, para. 842.

Subsequently, the debate deviated from the doctrinal discussion abovementioned and focused on the character of the measures as such. The claimant insisted that 2010's regulation did not pursue a valid public purpose,⁷¹ was discriminatory, did not comply with due process, and was not complemented by a prompt, adequate, and effective compensation.⁷² Furthermore, according to the claimant, the tariff deficit was not a valid argument to justify the measures against the investor's interests, since it existed long before and was attributable to the government's mismanagement.⁷³ Conversely, Spain stated that the measures constituting the modification of the scheme, rather than being expropriatory, are within the usual expressions of the right of the States to regulate grounded on their sovereignty, were adopted in good faith, were non-discriminatory, complied with due process, and were proportional to the protection of the public interest, as well as adequate to avoid the collapse of the Spanish electricity system.⁷⁴

The third and last element to evaluate indirect expropriations is the presence of investment-backed expectations. The evaluation of this element consists of assessing whether the investor has objective grounds to believe that the legal framework will not be modified during the life of the investment.⁷⁵ Therefore, legal changes are not contrary to investment-backed expectations – or expropriatory – when these should be envisioned by the investor according to the governments' representations, the circumstances surrounding the investment, and the context or the information available. Surprisingly, in *Charanne*, there was not any elaboration from the parties in this regard when discussing the breach of the expropriation protection. However, since the analysis of investment-backed expectations somehow overlaps with the evaluation of the creation of legitimate expectations in the FET protection, the interplay between the Host Government's representations and the due diligence, which usually determine the existence of expectations, was discussed when addressing FET.

⁷¹ *Ibid.*, para. 285.

⁷² *Ibid.*

⁷³ *Ibid.*, para. 289.

⁷⁴ *Ibid.*, paras. 342-345.

⁷⁵ OECD, 'Indirect expropriation and the right to regulate in international investment Law', OECD Working Papers on International Investment, OECD Publishing, 2004, 19, available at <http://dx.doi.org/10.1787/780155872321> (last visited 21 December 2017).

FET

The FET protection compels the Host State to act before the investor in accordance with the business standard of fairness⁷⁶ in order to maintain “[...] stable, equitable, favourable and transparent conditions [...]” (Art. 10 *ECT*). The analysis of legitimate expectations is the key element to identify whether or not the Host Country has breached the FET protection.⁷⁷

The concept of *Legitimate Expectations* is related to the investor’s confidence that the Host State will not change the conditions of the investment or, at least, that the changes in the legal framework will not be unreasonable and/or disproportionate. A first dogmatic approach takes on a clearly pro-investor interpretation of legitimate expectations. This approach holds that the conditions at the moment of the investment should remain untouched during the life of the investment, being any change in the investment framework contrary to legitimate expectations.⁷⁸ A second, more flexible approach suggests that the Host State has some room of manoeuvre to modify the investor’s legal framework without dishonoring legitimate expectations, subject to some qualifying requirements (State’s representations, the general regulatory environment, and the legitimacy of the regulatory measures).⁷⁹ Therefore, while the claimant in this kind of dispute usually relies on the first approach, the defendant naturally adopts the second approach.

In the decisions under analysis, the parties addressed the dogmatic discussion just described. In *Charanne*, although in the beginning the claimant gave the idea of adopting the second approach by expressing that the Tribunal has “[...] a wide margin of appreciation to analyse the just character of the acts of the States [...]”⁸⁰, its main argument consisted of asserting that the legislation valid at the time of the investment is sufficient to create legitimate expectations.⁸¹ Accordingly, the mere fact of “[...] breaking the stability of the

⁷⁶ C. Dugan *et al.*, *Investor-State Arbitration* (2011), 504.

⁷⁷ *Fair and Equitable Treatment*, UNCTAD Series on Issues in International Investment Agreements II, 2012, xiii, 63, available at http://unctad.org/en/Docs/unctad-diaeia2011d5_en.pdf (last visited 21 December 2017) [UNCTAD Fair and Equitable Treatment].

⁷⁸ *Tecmed S.A.*, *supra* note 53 para. 122; *CMS Gas Transmission Company v. The Republic of Argentina*, Final Award, ICSID Case No. ARB/01/8, 12 May 2005, para 138, [CMS Gas Transmission Company].

⁷⁹ *UNCTAD Fair and Equitable Treatment*, *supra* note 77.

⁸⁰ *Charanne*, *supra* note 12, para. 291.

⁸¹ *Ibid.*, para. 296.

regulatory framework [...]” constitutes their violation⁸²; a position that matches with the first approach. Similarly, the claimant in *Eiser*, after emphasizing on stability as a core value of the *ECT* – expressed that the *Real Decreto 661/2007* created legitimate expectations because it was the reason why the company decided to invest. According to him, it was accepted that a legal framework itself can originate legitimate expectations and its mere modification leads to liability.⁸³

In opposition, Spain claimed in both cases that agreeing with the claimants’ position would be accepting that the legislation should be kept petrified during the life of the investment as if the Government was compelled by a stability contract to maintain the regulation unmodified, which was not the case. Subsequently, adopting the second approach, the defendant in both issues complemented its elaboration by expressing that the analysis of legitimate expectations must be developed along with the evaluation of the reasonability of the measures, as well as taking into consideration the balance between the investor’s expectations and the Host State’s interest to fulfil public needs.⁸⁴

If one agrees with the first approach, the evaluation of legitimate expectations is exhausted by simply verifying whether or not the changes in the law were detrimental to the investor’s interest. However, if one adheres to the second approach, one opens the key question on how to determine what could the investor legitimately expect, bearing in mind that the power of the State to regulate and adapt to the changing situations cannot be completely curtailed. To answer this key question, it is necessary to divide it in two different sub-questions, which correspond in reality to two different expectations. While the first sub-question depends on whether the representations from the government created the expectation that the legal framework would remain untouched during the life of the investment, the second ponders whether or not the changes in the law were reasonable, in the sense that the investor expects changes to be legitimate.⁸⁵

In regards to when representations create legitimate expectations, in general, two positions could be adopted. Under the first, legitimate expectations could only originate in specific commitments. The second position proposes that

⁸² *Ibid.*, para. 294.

⁸³ *Eiser*, *supra* note 13, paras. 357-358 and para. 363.

⁸⁴ *Ibid.*, para. 359; *Charanne*, *supra* note 12, paras. 348-349.

⁸⁵ See F. Mutis Téllez, ‘Conditions and Criteria for the Protection of Legitimate Expectations under International Investment Law’, 27 *International Centre for Settlement of Investment Disputes Review* (2012) 2, 432, 434.

legitimate expectations could arise, not only from specific commitments, but also from other different host government's representations and the legislative background. There is significant opposition to the adoption of this second position in the case law.⁸⁶ However, the acceptance of the other position – the one that relies on specific commitments – is not less problematic, since its application has been inconsistent in the investor-State arbitration jurisprudence.⁸⁷ Nevertheless, there is more or less a consensus that specific commitments are endorsed throughout a stabilization clause, stabilization contract or any similar representation; or where the regulation, though it is not directed at a specific investor, is intentionally drafted to incentivize an identifiable group of investors.⁸⁸ In this regard, claimants will always try to promote the soundness of the theory that the formation of legitimate expectations can be grounded in any representation from the government and, contrarily, defendants will insist on the narrowest interpretation of representations.

In this respect, in *Charanne*, the company asserted that legitimate expectations were grounded on commitments, representations, and actions from the host government that led the investor to believe that the conditions of the investment were going to be maintained throughout the whole project. In *Charanne's* opinion, the most palpable representation was the enactment of *Real Decreto 661/2007* and *Real Decreto 1578/2008*, which had as a clear intention the attraction of investments in photovoltaic technologies.⁸⁹ Besides there were other representations and actions that the investor claimed enhanced its confidence, such as the expected profits described to the investors in the promotional presentations entitled *El Sol Puede ser Suyo 2005 (The Sun*

⁸⁶ *Ibid.*, 435-437.

⁸⁷ It should be highlighted that decisions regarding specific commitments and representations are unsystematic and contradictory. In *Enron v. Argentina and CMS v. Argentina*, the Tribunal considered that, since the legislation on gas tariffs was addressed to a particular type of investors, it created legitimate expectations. Consequently, the measures that compelled investors to recalculate the tariff in pesos instead of dollars and the measures that restricted the tariff adjustments were against legitimate expectations. On the contrary, in *Metalpar v. Argentina*, which was grounded on the same facts, it was held that legitimate expectations cannot arise in the absence of a license, permit or contract. Nevertheless, to make it even more confusing, in *Hamester v. Ghana and Parkerings v. Lithuania*, the Tribunals expressed that a contract by itself is not proof of specific commitments.

⁸⁸ M. Hirsch, 'Between Fair and Equitable Treatment and Stabilization Clause: Stable Legal Environment and Regulatory Change in International Investment Law', 12 *The Journal of World Investment & Trade* (2011) 6, 783, 784.

⁸⁹ *Charanne*, *supra* note 12, para. 297-298.

can be Yours 2005)⁹⁰ and *El Sol puede ser Suyo 2007 (The Sun can be Yours 2007)*,⁹¹ as well as the aim of providing stability to investors expressed in the *Spanish Plan for Renewable Energies*' development for the period 2005-2010, drafted by the government.⁹² In the same way, in *Eiser* it was argued that, in addition to the legislation itself and some of the documents just described, legitimate expectations were grounded on different government actions such as road shows or several resolutions from the authorities reiterating that the investor was covered under the regime of the *Real Decreto 661/2007*.⁹³

As a response, Spain categorically rejected the investors' arguments in the two cases, by pointing out the absence of a specific commitment such as a stabilization clause that guaranteed the inalterability of the scheme and, thus, denying the existence of legitimate expectations based on the theory that restricts the origin of legitimate expectations to stability clauses or similar representations.⁹⁴

Representations, however, cannot be interpreted in a vacuum; they must be capable of creating legitimate expectations on an objective and subjective basis.⁹⁵ In this sense, the regulatory stability and the context of the Host State in which the investment is made should be measured by the investor as part of his due diligence.⁹⁶ If the investment is done in a Host Country particularly prone to regulatory instability or experiencing particular unstable circumstances, it would be very difficult from an objective analysis to conclude that legitimate

⁹⁰ Ministerio de Energía, Turismo y Agenda Digital and IDAE, 'El Sol Puede Ser Suyo: Respuestas a Todas las Preguntas Clave sobre Energía Solar Fotovoltaica' (2005), available at [http://www.erasolar.es/pdf%27s/EL-SOL-PUEDA-SER-SUYO-\(FV-IDAE\)%202005.pdf](http://www.erasolar.es/pdf%27s/EL-SOL-PUEDA-SER-SUYO-(FV-IDAE)%202005.pdf) (last visited 25 December 2017) [*The Sun can be Yours 2005*].

⁹¹ Ministerio de Energía, Turismo y Agenda Digital and IDAE, 'El Sol Puede Ser Suyo: Respuestas a Todas las Preguntas Clave sobre Energía Solar Fotovoltaica' (2007), available at <http://biblioteca.climantica.org/resources/25/fotovoltaicaelsolpuedesersuyojunio2007.pdf> [*The Sun can be Yours 2007*].

⁹² Ministerio de Energía, Turismo y Agenda Digital and IDAE, 'Plan de Energías Renovables en España' (2005), paras. 289-299, available at [http://www.idae.es/uploads/documentos/documentos_PER_2005-2010_8_de_gosto-2005_Completo.\(modificacionpag_63\)_Copia_2_301254a0.pdf](http://www.idae.es/uploads/documentos/documentos_PER_2005-2010_8_de_gosto-2005_Completo.(modificacionpag_63)_Copia_2_301254a0.pdf) (last visited 25 December 2017) [*Spanish Plan for Renewable Energy*].

⁹³ *Eiser*, *supra* note 13, para. 358.

⁹⁴ *Charanne*, *supra* note 12, para. 356.

⁹⁵ Mutis Téllez, *supra* note 85, para. 433-434.

⁹⁶ *MTD Equity Sdn. Bhd. and MTD Chile S. A. v. Republic of Chile Case*, Final Award, ICSID Case No. ARB/01/7, 25 May 2004, paras. 164, 167 and 242-243.

expectations arose.⁹⁷ Similarly, if the investor had access to special information showing that the investment conditions might change, it would be contradictory to conclude the formation of legitimate expectations. In this respect, Spain argued in *Charanne* that a “[...] reasonably informed investor [...]”⁹⁸ would expect the RES to change and suggested that the investor did not perform a proper due diligence,⁹⁹ because several judicial and administrative decisions, issued before the investment was made, confirmed that the only expectation for a RESs producer was obtaining a reasonable return.¹⁰⁰ In response, the claimant contended that, despite acting diligently and seeking advice from experts to assess all the risks associated to the investment, including legal aspects, “[...] it was impossible to foresee the subsequent actions of Spain[...]” (para. 305). In *Eiser*, Spain was even more incisive and suggested that the investor knew, based on the due diligence that regulatory changes were within the probabilities, but that even with this information it decided to invest.¹⁰¹ The investor’s response was that the due diligence, which was performed by a top law firm, as well as the financial creditors’ assessment concluded that it was a secure investment in terms of regulatory stability and, therefore, the company was diligent in measuring this risk.¹⁰²

The second key sub-question on legitimate expectations – whether or not the changes in the law were legitimate – involves the analysis of the *bona fide* and public interest character of the measure, as well as its necessity and proportionality.¹⁰³ Even if it is true that the conclusion of an IIA and the existence of the FET protection does not entail that the regulation should be indefinitely frozen, the investor has the legitimate expectation that any change in the law must be reasonable. As a result, in international arbitration disputes there is always tension between the parties about the reasonability of the measure. Surprisingly, in *Charanne*, the claimant did not really confront the legitimacy of

⁹⁷ *Alex Genin, Eastern Credit Limited, Inc. and A. S. Baltoil v. The Republic of Estonia*, Final Award, ICSID Case No. ARB/99/2, 25 June 2001, paras. 348 and 370, available at <http://www.italaw.com/cases/484#sthash.b3eW6wYx.dpuf> (last visited 21 December 2017); *Parkerings-Compagniet AS v. Republic of Lithuania*, Final Award, ICSID Case No. ARB/05/8, 11 September 2007, paras. 332-335, available at <http://www.italaw.com/cases/812#sthash.z7iv7m6q.dpuf> (last visited 21 December 2017) [*Parkerings-Compagniet AS*]; *Methanex Corporation*, *supra* note 67.

⁹⁸ *Charanne*, *supra* note 12, 82, para. 365.

⁹⁹ *Ibid.*, para. 366.

¹⁰⁰ *Ibid.*, para. 365.

¹⁰¹ *Eiser*, *supra* note 13, para. 360.

¹⁰² *Ibid.*, para. 118.

¹⁰³ *Saluka Investments B.V.*, *supra* note 67.

the measures but rather just pointed out, as a general rule, that Host States breach legitimate expectations when they perform 'acts incompatible with criteria for economic rationality, the public interest or the principle of rationality'.¹⁰⁴ On the contrary, the respondent presented an extensive elaboration to explain that the new regulations were a reasonable and predictable response to the tariff deficit.¹⁰⁵ Within those reasons, it is worth highlighting that the limitation of the period benefited by the regulated tariff established in the new regulations matched the expected operative life of a photovoltaic installation: that the imposition of technical requirements concerning the power tension gaps complied with the needs of enhancing the security of the electricity system and avoiding its collapse, and that the limitations on the operating hours were predicted in the *Spanish Plan for Renewable Energies* for the period 2005-2010.¹⁰⁶

In *Eiser*, the debate on proportionality was the central issue. Indeed, it was argued that 2014's regulations, which cancelled the special regime for renewables, were endorsed after the tariff deficit was resolved, thus they were not needed.¹⁰⁷ Furthermore, the claimant argued these measures were disproportionate because they changed the basis of the legal framework that incentivized the company to invest, which was the calculation of the fees based on real costs instead of hypothetical costs (the change in nature of the calculation factors destroyed the value of the investment: after investing 124 million euros, the value of the investment was only 4 million euros when the claimant filed the notice of arbitration).¹⁰⁸ Additionally, the company had to renegotiate the terms of payment with its financial creditors and agreed to direct any future income that surpassed operational costs to the payment of debt. The defendant, on the other hand, asserted that the measures were needed to create a sound tariff scheme in the long run, and that the new tariff scheme was adjusted to the innovation in the solar sector. In addition, it was said that the loss suffered by the defendant was in reality the result of the mismanagement of the company.¹⁰⁹ Finally, Spain reiterated that a 'reasonable return' was the only legitimate expectation that the investor had and that the new scheme guaranteed this 'reasonable return'; thus, there was no real frustration of legitimate expectations.¹¹⁰

¹⁰⁴ *Charanne*, *supra* note 12, para. 294.

¹⁰⁵ *Ibid.*, paras. 350-354.

¹⁰⁶ *Spanish Plan for Renewable Energy*, *supra* note 92, para. 353.

¹⁰⁷ *Eiser*, *supra* note 13, para. 150.

¹⁰⁸ *Ibid.*, para. 418.

¹⁰⁹ *Ibid.*, para. 361.

¹¹⁰ *Ibid.*, paras. 149 and 361.

D. Pure Legal Analysis

As it has been stressed in this paper, as well as depicted in the previous section, the different legal approaches developed by the investment arbitration decisions regarding the criteria to determine liability for the breach of the expropriation and FET protections provide a high degree of flexibility to arbitrators who, even if not bound by prior decisions, can support their argumentation based on this variety. The aim of this section is to critically analyse some special features of the decision that were crucial for the outcome in both cases, from a purely legal perspective. For the same reasons explained in the analysis of the parties' elaboration, this section deals with both protections in *Charanne*, but only with the FET protection in *Eiser*.

I. Particular Features Regarding Expropriation (Article 13 (1) *ECT*)

In regards to expropriation, it is worth highlighting the conclusions of *Charanne* on the expropriation of the “[...] expected value cash flow [...]”¹¹¹ and the *substantiality*:

Expropriation of the Expected Value of Cash-Flow

The Tribunal in *Charanne* firmly discarded the assumption that the *expected value of cash-flow* was covered under the scope of Article 13 (1) *ECT*. According to the Decision, the *expected value of cash-flow* is not an investment which fits within the definition of Article 1 (6) *ECT*. While this provision requires the asset to be “[...] owned or controlled directly or indirectly [...]” in order to be qualified as *investment*, the expected revenues are, by their nature, incapable of being possessed or controlled by the investor. If the *expected value of cash-flow* is not an investment, then it would be a mistake to claim expropriation under Article 13 (1) *ECT*.¹¹²

On a first approach, there is little room to disagree with the logic of the Tribunal. However, the text of Article 1 (6) could generate misperception as it includes *returns* in the catalogue of investments protected under the *ECT*. Nevertheless, a proper understanding of the expression *returns* in line with the general statement of Article 1 (6) would be to grasp this expression as

¹¹¹ *Ibid.*, 71, para. 316.

¹¹² *Charanne*, *supra* note 12, 105-106, para. 459.

earned returns as opposed to *expected returns*. While the *expected returns* are uncertain and do not constitute part of the investor's patrimony, the *earned returns* certainly constitute part of the investor's patrimony and can be within the scope of Article 1 (6).

It must be noted that the compensation of *lucrum cessans* in expropriation claims has been admitted in several international investment arbitration decisions.¹¹³ Nonetheless, in these cases, the debate was not centred on whether the expected returns were investments subject to be expropriated, but rather on the content of concepts such as adequate compensation, appropriate compensation, fair market value, just value, etc., in order to determine the extent of reparation in expropriation cases. Therefore, the interpreter must be careful not to generalize the conclusion of the Tribunal when rejecting the compensation of *expected returns*, without examining first if it matches the text of the particular IIA that governs the relationship between the parties involved.

Substantiality

After defining expropriation as the total or partial deprivation of the investor's property rights, the decision established two forms in which indirect expropriation can be perfected under Article 13 (1): the deprivation of its assets or the loss of the value equivalent to deprivation of the investor's property rights.¹¹⁴ In the specific case, the Tribunal correctly considered that, regarding the first type of expropriation, *Charanne's* investments were not expropriated since the shares of its Spanish subsidiaries were still in its portfolio.¹¹⁵

With respect to the second form of expropriation – the loss of value equivalent to deprivation of the property rights – the Tribunal evaluated whether the decrease of the expected returns was substantial enough to fall under Art. 13.¹¹⁶ It must be noted that the evaluation of the Tribunal was not

¹¹³ *Texaco Overseas Petroleum Company v. The Government of the Libyan Arab Republic*, Ad Hoc Award, 19 January 1977, ILM, 1978, 36-37, paras. 110-112; *Libyan American Oil Company (LIAMCO) v. The Libyan Arab Republic*, Award, 18 January 1980, ILC Model Rules on Arbitral Procedure (1958), Vol. II, 1179; *Greek Telephone Company v. Government of Greece*, 1 March 1935, cited by R. Doak Bishop *et al.*, Foreign Investment Disputes, (2005), 1303; *CME Czech Republic B.V. v. The Czech Republic*, Final Award, 14 March 2003, 115-116, para. 497 available at <https://www.italaw.com/cases/281> (last visited 21 December 2017).

¹¹⁴ *Charanne*, *supra* note 12, paras. 460-461.

¹¹⁵ *Ibid.*, para. 462.

¹¹⁶ *Ibid.*, para. 462.

focused on the expected returns themselves, but on the impact that the decrease in the expected returns could have on the value of the shares.¹¹⁷ On this issue, it was established that a substantial loss entails the fully annihilation of the investment – a standard that is consistent with previous awards.¹¹⁸

The Arbitrators considered that the impact on the value of *Charanne's* shares was not substantial. Albeit, the investor was negatively affected, the loss was not significant enough to state that the value was totally destroyed. The Tribunal acknowledged that the opposite conclusion would be equal to finding indirect expropriations whenever the share's value decreases as a result of the government's measures, which "[...] of course, cannot be the case."¹¹⁹ However, it remains unclear from which point the loss is sufficiently large to be considered substantial.

II. Particular Features Regarding FET (Article 10 (1) *ECT*)

Two aspects draw our attention regarding the FET. First, the conclusions of the Tribunal on the representations capable of creating legitimate expectations and, second, the methodology to assess the proportionality of the measure.

Representations

Both Tribunals discarded the existence of specific commitments and, thereby, the appearance of legitimate expectations arising from these commitments.¹²⁰ The basis of this decision was the absence of any stability contract or any declarations from the Government directed specifically to the investor.¹²¹ Additionally, the Tribunal in *Charanne* categorically rejected that the regulation itself could lead to the legitimate expectation that the law will be unmodified, because – in its view – that would be equal to restrict the State's capability to adapt the legal framework to the circumstances.¹²² *Eiser*, in turn, emphasized that in the absence of a stability clause or any similar commitment the investor should envision that the regulation might change.¹²³ In this regard, *Eiser* and *Charanne* adhere to the case law that tends to narrow the interpretation

¹¹⁷ *Ibid.*, para. 459.

¹¹⁸ *Tecmed S. A.*, *supra* note 53, para. 116.

¹¹⁹ *Charanne*, *supra* note 12, para. 465.

¹²⁰ *Ibid.*, 490; *Eiser*, *supra* note 13, para. 362.

¹²¹ *Charanne*, *supra* note 12, para. 490.

¹²² *Ibid.*, paras. 498-503.

¹²³ *Eiser*, *supra* note 13, para. 362.

of representations by confining the emergence of legitimate expectations to the existence of stability clauses and or any other similar specific assurance given to the investor.¹²⁴

On the contrary, Guido Santiago Tawil – in the Dissenting Opinion of *Charanne* – opposed the Tribunal’s narrow interpretation of representations. He claims that the applicable law at the moment of investing is capable of generating legitimate expectations.¹²⁵ Regarding the argument posed by the Tribunal that a wider recognition of representations would lead to the crystallization of the regulation, the dissenting opinion states as a very strong counterargument that the acknowledgment of legitimate expectations arising from the valid law at the moment of the investment does not involve depriving the State of the right to regulate, but merely generate the obligation of the State to redress the damage suffered by the investor when his expectations were frustrated.¹²⁶

In addition to Professor Tawil’s argument, the Tribunal’s assertion may be contradictory, because if it is acknowledged – as it was by the Tribunal – that the idea of specific commitment arising from legislation would be a disproportionate restriction to the ability of the State to change the law, forcefully, it must be also acknowledged that a specific commitment arising from stability clauses hinders this ability too. The validity of stability clauses as a means to generate legitimate expectations would be put into question if one accepts the Tribunal’s reasoning in this regard.

A more flexible concept for the determination of representations, capable of creating specific commitments and legitimate expectations, would also be consistent with the principle of good faith. The Tribunal in *Charanne* recognizes “[...] that a State cannot induce an investor to make an investment, hereby generating legitimate expectations, to later ignore the commitments that had generated such expectations [...]”¹²⁷, but does not apply this principle to the extent that fits to the several expressions that can generate the convincement that the legal framework will remain unaltered during the whole project. In fact, legislation could be enacted in a way that convinces a certain group of foreign investors that it is feasible to invest in a certain market or industry under certain conditions that will be maintained for a certain period. Furthermore,

¹²⁴ *Total S.A. v. The Argentine Republic*, Decision on Liability, ICSID Case No. ARB/04/01, 27 December 2010, para. 107, available at <http://www.italaw.com/cases/1105#sthash.wTdX5hQc.dpuf> (last visited 21 December 2017).

¹²⁵ *Charanne*, *supra* note 13, para. 5.

¹²⁶ *Ibid.*, paras. 11 and 12.

¹²⁷ *Charanne*, *supra* note 12, 111, para. 486.

the evaluation of the regulation along with other actions of the Host State and the circumstances surrounding the relationship between the parties, might objectively generate the conviction that the legal framework will stay unaltered. An analysis like this one is not unusual in the arbitral jurisprudence.¹²⁸

Proportionality

The analysis of proportionality was the key factor that influenced the decision in both cases. Here, far from being contradictory, the two decisions complement each other. In fact, *Eiser* based the analysis of proportionality on the methodology adopted in *Charanne*, where the Tribunal established that the proportionality is fulfilled where the modifications to the legal framework are not “[...] capricious or unnecessary [...]” and do not “[...] suddenly and unpredictably eliminate the essential characteristics of the existing regulatory framework.”¹²⁹

While the Tribunal in *Eiser* does not pay much attention to the analysis of predictability and simply states that 2014’s measures were abrupt, as a side effect of the radical changes,¹³⁰ *Charanne* went deeper on the predictability of 2010’s measures by asserting that the cancellation of the regulated tariff for the second period was predictable, given the fact that the expected operative period of solar installations matches the period redefined in the modifications.¹³¹ Likewise, regarding the limitation of the amount of operation hours, the *Charanne* Tribunal asserted that it was expected according to the government’s representations.¹³²

Additionally, in general terms, the Tribunal in *Charanne* made clear that, as the investor was an expert in the energy market, a *level of care* was expected from him which included envisioning legislation changes.¹³³ This last assertion should be taken with certain reserves, since its adoption as a general rule would entail that an expert-investor should always forecast any changes in the legislation, which would render any IIA useless. Then, the analysis of predictability should be assessed by reference, for example, to the representations made by the host

¹²⁸ *El Paso Energy International Company v. The Argentine Republic*, Award, ICSID Case No. ARB/03/15, 31 October 2011, para 375-376, available at <https://www.italaw.com/cases/documents/383> (last visit 21 December 2017).

¹²⁹ *Charanne*, *supra* note 12, 118, para. 517.

¹³⁰ *Eiser*, *supra* note 13, para. 387.

¹³¹ *Charanne*, *supra* note 12, paras. 518-529.

¹³² *Ibid.*, paras. 530-534.

¹³³ *Ibid.*, para. 507.

government, the context, the dynamic of industry, and the information available to the investor. Indeed, to arrive at the conclusion that the modifications of the period and the operation hours were predictable, the Tribunal not only took into account the expertise of *Charanne* but also the representations and the technical characteristics of the solar panels' operation. Consequently, regarding predictability, rather than stating that the *level of care* requires that the investor forecast in general the changes in the law, it is preferable to use the language of *reasonably foreseeable* changes – as the Tribunal did in paragraph 505 – when describing the range of the regulatory changes that the investor should have expected.

As for the second requirement of proportionality – that the “[...] changes are not capricious or unnecessary [...]”¹³⁴ – neither *Charanne* nor *Eiser* expressed which test was used to assess *necessity* or *capriciousness*. Nevertheless, in the former decision, the arbitrators stated that the measures taken by the government were rational and non-arbitrary given the fact that they were supported by objective criteria.¹³⁵ Similarly, in the latter, the Tribunal was emphatic in clarifying that it was not questioning that the changes were addressing a real problem – the tariff deficit – that needed to be tackled.¹³⁶ The elaboration in both cases seems to follow the test used in other decisions, which consists on the question of whether or not there was a “[...] manifest lack of reason for the legislator [...]”¹³⁷, where only the measures that are “[...] manifestly arbitrary[.]”¹³⁸ are considered as disproportional. This low standard is generally justified by the fact that a higher standard might entail that arbitrators are entitled to judge the accuracy of Host State's public and “[...] [the role of the Tribunal is not] [...] to supplant its own judgement [...] for that of a qualified domestic agency.”¹³⁹

On the third requirement of proportionality – the preservation of the essential characteristics of the existing regulatory framework – *Charanne's* Tribunal considered that 2010's changes were not disproportionate because they did not change the basic benefits for the investor, i.e. the perception of a tariff and the priority access were still operating.¹⁴⁰ On the contrary, according

¹³⁴ *Ibid.*, 118, para. 517.

¹³⁵ *Ibid.*, para. 534.

¹³⁶ *Eiser*, *supra* note 13, para. 371.

¹³⁷ *Glamis Gold, Ltd. v. The United States of America*, Award, 8 June 2009, para. 803, available at <https://www.italaw.com/sites/default/files/case-documents/ita0378.pdf> (last visited 21 December 2017).

¹³⁸ *Ibid.*

¹³⁹ *Ibid.*, para. 779.

¹⁴⁰ *Charanne*, *supra* note 12, para. 533.

to *Eiser*, 2014's modifications eliminated a favorable scheme that benefited the investor and replaced it with a completely different scheme, grounded on completely different premises, such as assessing the fee based on hypothetical costs instead of real costs, not including costs of debt in the calculation, or based on the capacity of production instead of the energy actually produced.¹⁴¹ These modifications caused a substantial reduction of the subsidies and, in the end, the claimant's precarious situation.¹⁴²

In *Eiser*, the scheme was regarded by the Tribunal as “[...] profoundly unfair and inequitable [...]”¹⁴³ because it dispossessed the investment from its whole value.¹⁴⁴ In fact, the decision reduces the analysis of proportionality *strictu sensu* to the *devastator*¹⁴⁵ *dramatic effects*¹⁴⁶ that were by “[...] far less sweeping [...]” in *Charanne*.¹⁴⁷ This type of analysis of proportionality does not really reflect a balance of interests or, in any case, does not indicate what weight was given to the interests at issue. The absence of the evaluation of these factors poses the idea that in the end the decision is made on the grounds of justice. The appropriateness of a proportionality analysis has been argued as “[...] a clearer and more transparent structure that requires tribunals to be explicit about their reasoning and thus produce better quality awards.”¹⁴⁸ In this regard, neither *Eiser* nor *Charanne* is explicit about the significance given to the interests of other stakeholders such as taxpayers or consumers, or the weight given to other more general interests such as the soundness of economy or, equally important, the national and global interest of cutting greenhouse gas emissions. These considerations do not mean that we do not agree with both decisions in their ruling, it means that a well-structured proportionality test would be a desirable scrutinizing element for having clarity on the political and the pragmatic motivations behind it.¹⁴⁹

¹⁴¹ *Eiser*, *supra* note 13, paras. 397-398.

¹⁴² *Ibid.*, para. 390.

¹⁴³ *Ibid.*, para. 365.

¹⁴⁴ *Ibid.*, para. 365.

¹⁴⁵ *Ibid.*, para. 409.

¹⁴⁶ *Ibid.*, para. 368.

¹⁴⁷ *Ibid.*, para. 368.

¹⁴⁸ L. Isatolo, ‘Climate Compatible Investment Treaty Law: The Role of Legitimate Expectations’, Scottish Centre for International Law Working Paper Series 2016/6, 23, available at http://www.scil.ed.ac.uk/__data/assets/pdf_file/0004/172039/Laura_Isatolo_SCIL_Working_Paper_6_FINAL_for_publication.pdf (last visited 21 December 2017).

¹⁴⁹ *Ibid.*

E. Pragmatic Approach in the Context of Climate Change: Reinforced Stability of RESs

There are conflicts and synergies between IIAs and the climate change international instruments.¹⁵⁰ On the one hand, the existence of investor-State arbitration represents a threat to the common objective of levelling global warming, as it may incentivize the Host States not to take climate change measures in order to avoid the risk of facing high value claims and/or adverse decisions. This phenomenon is known in the law and economics literature as regulatory chill.¹⁵¹ On the other hand, IIAs also promote the fight against global warming by attracting foreign investment for the implementation of green technologies, as well as by providing some degree of regulatory stability to the investors and, therefore, to the operation of low carbon energy projects.¹⁵² Investment Arbitration Tribunals should not ignore the interaction between investor-State arbitration and climate change, since its dogmatic constructions, argumentation, and adjudication may have an impact on climate change i.e. to a certain degree they make climate change law decisions. A pragmatic approach when dealing with RESs should be in line with the objective of levelling global warming by reinforcing the regulatory stability.

Charanne and *Eiser* did not make any explicit mention to the weight given to the objective of cutting emissions, neither expressed the importance to align the interests of the parties with the interests of levelling global warming or resolving the possible conflicts in this regard. However, *Eiser* concludes that the *ECT* entails a higher degree of stability given the particular functioning of the energy investments.¹⁵³ Its reasoning is based on Article 2 of the *ECT*, which establishes that the treaty's general purpose is "[...] to promote long-term cooperation in the energy field based on complementarities and mutual benefits, in accordance with the objectives and principles of the Charter." According to *Eiser*, the aim of promoting long-term cooperation in energy projects supposes that the treaty

¹⁵⁰ See J. E. Viñuales, *Foreign Investment and the Environment in International Law* (2015), 24-55 [Viñuales, *Foreign Investment and the Environment*].

¹⁵¹ F. Baetens, 'Foreign Investment Law and Climate Change: Legal Conflicts Arising from Implementing the Kyoto Protocol through Private Investment', CISDL Working Papers Series 2010, 11, available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2117950 (last visited 21 December 2017).

¹⁵² See A. Boute, 'Combating Climate Change through Investment Arbitration', 25 *Fordham International Law Journal* (2012), 3, 613, 617.

¹⁵³ *Eiser*, *supra* note 13, para. 377.

is an instrument to achieve the stability required to meet this aim.¹⁵⁴ Moreover, the Tribunal invoked the content of the European Energy Charter to stress the to stress the importance of approving treaties that promote a “[...] high degree of regulatory stability [...]”¹⁵⁵ and asserts that Article 10 (1) *ECT* expressly reinforces the idea of stability.¹⁵⁶

The “[...] high degree of regulatory stability [...]” should be reinforced in the case of RESs because, as expressed in the introduction, renewable energy projects face higher risks than conventional energy projects, and they are vital instruments to achieve the objective of levelling global warming. The integration of the concept of reinforced stability for RESs based on climate change considerations should not represent a problem for arbitrators under the *ECT*. Despite the controversy regarding the legitimacy of relying on international environmental and climate instruments in investor-State arbitration¹⁵⁷ or the trend to protect these interests by means of interpretation of legal concepts,¹⁵⁸ the *ECT*'s preamble recalls “[...] the United Nations Framework Convention on Climate Change, the Convention on Long-Range Transboundary Air Pollution and its protocols, and other international environmental agreements with energy-related aspects[...]”, as well as recognizes “[...] the increasingly urgent need for measures to protect the environment [...]”. Additionally, Article 19 (d) *ECT* expressly highlights the duty of host governments to foster RESs: “[...] Contracting Parties shall [...] have particular regard to Improving Energy Efficiency, to developing and using renewable energy sources, to promoting the use of cleaner fuels and to employing technologies and technological means that reduce pollution [...]”.

In this section, this paper openly takes sides for the dogmatic constructions that maximize the stability for RESs. For this purpose, it is suggested that Tribunals should adopt the sole effect doctrine, a broad interpretation of representations, the *less harmful measure* standard and the analysis of proportionality in the context of climate change, when dealing with this kind of disputes. However, it is important to highlight that the increasing stability for RESs could be counter-productive if it fosters the inefficiency of the investors.

¹⁵⁴ *Ibid.*

¹⁵⁵ *Eiser*, *supra* note 12, para. 378.

¹⁵⁶ *Ibid.*, para. 380.

¹⁵⁷ J. E. Viñuales, Green Investment after Rio 2012, 16 *International Community Law Review* (2014), 2, 153, 173 [Viñuales, Green Investment].

¹⁵⁸ *Ibid.*

Consequently, our pragmatic interpretation also requires demanding from investors an *expert's level of care*.

The *Sole-Effect Doctrine*

As previously explained, the sole-effect doctrine, as opposed to the police-power doctrine, entails that the Host State is found liable to pay damages under the expropriation protection whenever the investor has been deprived of the control or the value of the investment, “[...] even if not necessarily to the obvious benefit of the host State.”¹⁵⁹ In this sense, “[...] the issue is not so much whether the measure concerned is legitimate and serves to a public purpose, but whether it is a measure that, being legitimate and serving a public purpose, should give rise to a compensation claim.”¹⁶⁰

From our pragmatic approach of *reinforced stability of RESs*, it is appropriate to adopt the sole-effect doctrine rather than the police-power doctrine. The fact that the host government is aware that the good faith or the legitimate public interest of the measure would not serve as defense for excluding liability, would incentivize the authorities to implement the modification of the RESs in a subtle way that does not deprive the investment from its whole value and, therefore, would protect as much as possible the production of low carbon emissions from dramatic changes in the regulation.

Indeed, a position like this one might also provide some coherence to the problem of expropriation and FET overlapping each other. In this sense, under the approach proposed, while the expropriation protection would take the form of strict liability when the full value or control of the investment is destroyed, and the compensation would correspond to the *fair market value*, the FET would require the frustration of the investor's legitimate expectations, where the reasonability and proportionality of the measure might exclude the host government's liability. Actually, despite the fact that the decision in *Eiser* was the result of the evaluation of the FET, the defining feature for finding the host government liable was the substantiality of the loss and the amount of the compensation was very close to the value that the company actually invested. Somehow, this might reflect that the Tribunal took a longer route through the FET to find out that an expropriation happened.

However, opting for strict liability when the modification of RESs involves expropriation would foster the investor's inefficiency if a proper degree of

¹⁵⁹ *Metalclad Corporation*, *supra* note 49, para 103.

¹⁶⁰ *Azurix Corp.*, *supra* note 66, para. 310.

diligence is not required from him. Consequently, it is important for arbitrators, in order to avoid this inefficiency, to examine in depth to which proportion the loss was foreseeable to the investor according to the analysis of the investment-back expectations, and to evaluate to which degree the mismanagement of the investor contributed to the destruction of the investment.

Broad Interpretation of Representations

The Tribunals' position of restricting the creation of legitimate expectations to stability contracts or any similar direct representations has the advantage of providing certainty, since it can be synthesized in a simple-fix rule that does not admit much interpretation: either the State creates legitimate expectations by providing clear, specific, and direct assurances, like stability clauses, or it does not. Nonetheless, a solution as such may bend the balance in favor of the Host State. Indeed, none of the Spanish companies involved in RES disputes concluded stability contracts with the authorities.¹⁶¹

Our approach of 'reinforced stability of RESs' suggests that the assessment of specific commitments and legitimate expectations should be perfected in a less strict manner in order to bring balance to the investors' and States' interests, as well as to promote the global interest of levelling global warming. As a consequence of broadening the interpretation of representations, host governments are forced to be more cautious in not sending the wrong message to the investors and, furthermore, they may be incentivized to design sustainable RESs. In the case of Spain, it seems that the authorities designed a system that was not sustainable in the long-term and ended up in what they described as the tariff deficit.

This does not mean that any change in the regulation that affects the investment shall be deemed against legitimate expectations and may give rise to liability, as some arbitral decisions proclaimed based on the dogma of stability under IIAs.¹⁶² It means that arbitrators should apply a wider interpretation to define whether the action or inaction of the government, from an objective perspective, was sufficient to generate the conviction that the legal framework would remain unaltered during the life of the project. Informal and formal representations, regulations, negotiations, meetings, public and private declarations, etc., should be considered – isolated and/or jointly – to infer whether or not specific commitments were endorsed by the host government.

¹⁶¹ *Eiser*, *supra* note 13, para. 359.

¹⁶² *Tecmed S.A.*, *supra* note. 53; *CMS Gas Transmission Company*, *supra* note 78.

In section 4.2, it was already mentioned that a broader approach to specific commitments is consistent with the principle of good faith and has support not only in the dissenting opinion of *Charanne* but also in investor-State arbitration case law.

Less Harmful Measure Standard

The standard of *capriciousness* or *arbitrariness* adopted by the Tribunals to assess whether the conduct was proportional does not match the pragmatic approach of *reinforced stability of RESs*. The standard that the Host State's measures should reach to be exempted from liability appears to be very low, since a measure that is mistaken or reckless, but not capricious or unnecessary, will not be regarded as contrary to proportionality. Concerning RESs, hardly one could find a conduct of the government that is capricious or arbitrary. The current technology and costs of low carbon industries require some sort of state aid to be developed and, consequently, represents a burden for taxpayers and consumers. In this regard, cutting benefits to investors in renewable energy might always be justified for economic reasons.

Establishing a higher standard would incentivize the authorities to modify the RESs only if necessary. This higher standard should require the host government to implement the *less harmful measure*,¹⁶³ in the sense that, if it appears to be a better alternative than the one the authorities have chosen, they should be liable to compensate damages. This seems to be a common approach in WTO disputes.¹⁶⁴ However, in investor-State arbitrations, there are not many examples. *S. D. Myers* could be the referent of this higher standard. According to this decision, the purpose of Canada when promoting the ability to process PCBs was legitimate, however, for achieving this purpose “[...] there were a number of legitimate ways by which CANADA could have achieved it, but preventing SDMI from exporting PCBs [...] was not one of them.”¹⁶⁵ Similarly, in *Oxy v. Ecuador*, the Tribunal concluded that the host government had other options than declaring the termination of the contract such as the “[...] insistence on payment of a transfer fee [...] improvements to the economic terms

¹⁶³ This expression is taken from Viñuales, *Foreign Investment and the Environment*, *supra* note 150, 270.

¹⁶⁴ Isatolo, *supra* note 148, 30.

¹⁶⁵ *S.D. Myers Inc. v. Government of Canada*, Partial Award, 13 November 2000, para. 255, available at <https://www.italaw.com/sites/default/files/case-documents/ita0747.pdf> (last visited 21 December 2017).

of the original contract; and/or a negotiated settlement [...]”¹⁶⁶ Consequently, the Tribunal “[...] finds that the Respondent’s argument that there was really no option but to terminate is unsound and it is not accepted.”¹⁶⁷

Nevertheless, this standard needs to be applied by tribunals in a very careful manner. As previously mentioned, the authorities are better equipped and prepared than the Tribunals to take measures regarding RESs. The technical questions regarding RESs usually require a high level of expertise. Accordingly, the operation of this standard demands a high degree of deference to the decision of local authorities and local courts.¹⁶⁸ In the cases of *Charanne* and *Eiser*, it is surprising that the Tribunals did not provide any deference to the Spanish Courts, which found that the modifications were adjusted to the Constitution and proportional.¹⁶⁹ Deference to the national authorities and courts might give more legitimacy to the Tribunals’ decisions.

Proportionality *Stricto Sensu* in a Climate Change Context

Eiser and *Charanne* did not weight all the interests at issue e.g. consumers, taxpayers, the economy, and climate change. In both cases, proportionality was assessed by evaluating three elements: necessity, predictability, and the preservation of the fundamental characteristics of the investment legal framework. According to the Tribunals, while in *Charanne* the modifications did preserve the fundamental characteristics, in *Eiser* they did not. However, upon examining the cases, one can easily arrive at the conclusion that the main factor to determine proportionality was the substantiality of the loss. This might give a sense that the decision was based on a pure instinct of fairness or that it covers an indirect expropriation.¹⁷⁰ Indeed, the Tribunal in *Eiser* expressed that dispossessing the investment from its entire value was “[...] profoundly unfair and unequal [...]”¹⁷¹

¹⁶⁶ *Occidental Petroleum Corporation and Occidental Exploration and Production Company v. The Republic of Ecuador*, Final Award, ICSID Case No. ARB/06/11, 5 October 2012, para. 434, available at <https://www.italaw.com/sites/default/files/case-documents/italaw1094.pdf> (last visited 21 December 2017) [Occidental Petroleum Corporation].

¹⁶⁷ *Ibid.*, para. 436.

¹⁶⁸ Isatolo, *supra* note 148, 30.

¹⁶⁹ See C. Otero García Castrillón, ‘Spain and Investment Arbitration: The Renewable Energy Explosion’, CIGI, paper No. 17, Investor-State Arbitration Series, 2016, 8-10.

¹⁷⁰ *Ibid.*

¹⁷¹ *Eiser*, *supra* note 13, para. 365.

An approach that takes into account the importance of tackling global warming, naturally, requires not only that the evaluation of proportionality include climate change as one of the interests at issue, but also requires giving a considerable weight to it. Yet, we are not suggesting that the climate change interest should always prevail so the RESs are preserved no matter the particularities of the case. The Tribunal should weigh all the factors and make a decision on a case-by-case basis. Nevertheless, it is important to highlight that under, our approach decisions should first take the climate change interest into account, second, give a proper weight to the interest of climate change, grounded on the global intention to lower greenhouse emissions and the international instruments supporting this objective, and finally, conceive transparently how the interaction between the climate change interest and other interests give shape to the final decision.

An analysis on proportionality like the one proposed provides more transparency and legitimacy to the ruling, as well as forces arbitrators to take the context of climate change into account. However, arbitrators might find the task of weighing financial interests – such as the loss for investors, the tariff deficit, the burden for consumers, etc.- against the interest of leveling global warming, very difficult to measure. This level of complexity also requires a high degree of deference to the local authorities and courts.

Expert's Level of Care Standard

In *Charanne*, the Tribunal expressed that the investor was expected to have a level of care that would drive him to envision that the RES would change in the future.¹⁷² This statement suggests that the level of care required from the investors in RESs is the level of an expert. Even though, in *Charanne*, this concept was used to define whether the investor had legitimate expectations, this level of care should be required throughout the whole project. Indeed, as mentioned previously, our approach of 'reinforced stability of RESs' might lead to the inefficiency of the investor if he is not required to act with the level of care of an expert.

The expert's level of care required of the investors might play an important role in RESs' cases. In fact, around 120 large solar energy firms, mostly in Europe and the United States of America, were bankrupted from 2010 to 2015. It would be excessive to blame governments for all these failures. Many investors leveraged

¹⁷² *Charanne*, *supra* note 12, para. 507.

their investments in unhealthy proportions and bore inefficient operational costs, motivated by what has been described as an “[...] equivalent to the real-state bubble [...]”.¹⁷³ In *Eiser*, while the Tribunal seemed very strict in analyzing the reasonability of the modifications, it did not give much attention to the level of care employed by the investor. In this regard, the Tribunal merely stated that the leverage of the company was normal¹⁷⁴ and even put the burden of proof on the defendant by claiming that he did not prove that the costs of the investor were unreasonable.¹⁷⁵ Moreover, the Tribunal did not present any deep analysis or weigh importance to the fact that the investor commenced construction nearly four years after the enactment of *Real Decreto 611/2007*; neither wondered why the 7 % tax from 2012 had such a huge impact on the investor’s finance or that its service coverage ratio was nearly 1.¹⁷⁶ This reflection is not to controvert the Tribunal’s analysis of the evidence or its decision, but simply calls attention to the necessity to evaluate the facts according to the *expert’s level of care* standard, in order ensure that decisions do not foster inefficient investments in a market that has proven to be risky and requires the participation of the most competent firms.

The contribution of the investor’s mismanagement to the loss should influence the decision by excluding liability when the loss is completely attributed to the investor or lowering the compensation when the loss is partially attributed to him. In *MTD*, the arbitrators ruled that Chile was liable to pay damages but only in a proportion of 50 % since the other 50 % was a consequence of the investor’s bad decision to buy land that was earmarked for agricultural use.¹⁷⁷ Similarly, in *Oxy v. Ecuador* the compensation was reduced 25 % because the investor provoked the termination of the contract by not asking the authorities for the approval for a farm-out agreement.¹⁷⁸

¹⁷³ D. Lacalle, ‘La mayor quiebra solar, el fin de la burbuja de deuda’, *El Español*, 25 April 2016, available at http://www.elspanol.com/economia/20160424/119868015_13.html (last visited 21 December 2017) (Translation by the author).

¹⁷⁴ *Eiser*, *supra* note 13, para. 415.

¹⁷⁵ *Ibid.*, para. 414.

¹⁷⁶ *Eiser*, *supra* note 13, para. 144.

¹⁷⁷ *MTD Equity Sdn. Bhd. and MTD Chile S. A. v. Republic of Chile*, Final Award, ICSID Case No. ARB/01/7, 25 May 2004, para. 243, available at <https://www.italaw.com/sites/default/files/case-documents/ita0544.pdf> (last visited 21 December 2017).

¹⁷⁸ *Occidental Petroleum Corporation*, *supra* note 166, paras. 669-670.

F. Conclusion

The modifications to the RES in Spain ended by erasing any differences with respect to the general scheme for conventional energies. In *Charanne*, the loss was considered not to be substantial enough to constitute an expropriation, neither were the changes in the 2010 regulation regarded as sufficiently drastic to frustrate the investor's legitimate expectations. Contrarily, the reforms to the RES adopted from 2012 to 2014 were considered by the Tribunal in *Eiser* to be against the investor's legitimate expectations, since they abruptly dispossessed the investment of its value by changing the core characteristics of the RES. Even though the Decisions arrive at opposing conclusions concerning the liability of Spain, the two decisions complement each other. The dogmatic approach they have is, in general terms, the same and *Eiser* even claims to be aligned with *Charanne*. The difference in the ruling originates in the different set of measures that were evaluated in each of the cases.

It is too soon to predict what will be the outcome of the 30 pending cases on RESs against Spain. However, the paper identifies some of the features that influenced both Decisions. The analysis of expropriation in *Charanne* shows that the *expected value of cash-flow* is relevant as far as it impacts the value of the shares, but it is not by itself subject to expropriation under the *ECT*. Concerning the FET, we have found that both decisions agree on the conclusion that the representations only create legitimate expectations when they take the form of stability clauses or any similar direct expressions from the host government. Additionally, both decisions concur in the assumption that a measure is disproportionate when it is “[...] capricious or unnecessary [...]” or “[...] suddenly and unpredictably eliminates the essential characteristics of the existing regulatory framework.”¹⁷⁹

Although the legal concepts that support *Charanne* and *Eiser's* rulings follow prior decisions from investor-State arbitration Tribunals, this paper demonstrates, by presenting the parties' elaboration, how the arguments to defend either the claimant's or the defendant's position can find convincing support in the case law. Moreover, the performance of a purely legal analysis in section 4 argues that restricting specific commitments to stability contracts or similar representations could be contradictory and against the principle of good faith. Furthermore, we claim that the approach of the Tribunal regarding necessity, as an element of proportionality, appears to apply the very low standard of non-arbitrariness and that the test of proportionality lacks a proper weighing

¹⁷⁹ *Charanne*, supra note 12, para 517.

of all the interests, leaving the impression that the decision is made on a pure sense of justice.

The universe of legal elaborations that was described in section 3, as well as the critics of the Tribunal's interpretations from a purely legal perspective presented, in section 4, provide enough elements to find within this universe what is the *best possible law* to foster the aim of levelling global warming.

The *ECT* integrates the global climate change law instruments and promotes RESs. Accordingly, our pragmatic approach assumes that the *ECT* entails reinforced stability for the RESs. This reinforced stability suggests that the disputes related to RESs under *ECT* should be resolved by applying the sole effect doctrine, a broad interpretation of representations, the *less harmful measure* standard, and the analysis of proportionality in the context of climate change. However, as this reinforced stability might be counterproductive if it fosters the inefficiency of the investor, we suggest that the investor should be required to perform his operations according to the *expert's level of care* standard.