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Investment arbitration in the energy sector

In what circumstances is an investor entitled to compensation under the Fair and Equitable Treatment standard of protection in the Energy Charter Treaty as a result of the exercise by the states of the right to regulate to detriment of investors? A special analysis on photovoltaic arbitration cases in Italy, Spain and the Czech Republic.

Abstract: A significant development in the renewable energy field has happened in several countries like Italy, Spain and the Chez Republic over the last years mainly due to the state´s support for renewable energy projects. However, because of the financial crisis, these countries decided to review and change the policies. As a result of the changes implemented renewable investors were affected in some manner. Consequently, many arbitrations claim against these states have been brought under the Energy Charter Treaty. The present Chapter analyses this jurisprudence. Based on the results of these arbitrations the lack of consistency results evident. Different interpretations around the Fair and Equitable Treatment standard and how to find a balance between the need for a stable and predictable investment framework and the sovereign right to regulate are the principal cause of diverse decisions. The concept of the standard in the treaty is reviewed and compared with the evolution of the concept in other investment agreements. In conclusion, possible amendments to increase consistency in the arbitrations under the Energy Charter Treaty will be proposed.

Key words: Fair and Equitable Treatment, Legitimate Expectations, Investment Arbitration, Energy Charter Treaty, Regulatory Changes.

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Arbitraje de inversión en el sector energético

¿En qué circunstancias un Inversor tiene derecho a recibir una compensación en el marco de la provisión de Tratamiento Justo y Equitativo del Tratado de la Carta de Energía como consecuencia del ejercicio del Estado de su derecho regulatorio en detrimento de los inversores? Análisis de casos de arbitraje de inversiones en el sector fotovoltaico en Italia, España y República Checa.

Resumen: Un desarrollo importante de las energías renovables ha ocurrido en países como Italia, España y República de Checa en los últimos años, principalmente debido al apoyo del estado a proyectos de energía renovable. Sin embargo, debido a la crisis financiera, estos países decidieron revisar su marco regulatorio. Como resultado de los cambios implementados, los inversores en el sector renovable se vieron afectados. En consecuencia, demandas de arbitraje de inversiones contra estos estados se han presentado al amparo del Tratado de la Carta de la Energía. El presente Capítulo analiza esta jurisprudencia. En base a los resultados de los arbitrajes se evidencia la falta consistencia en los laudos arbitrales. Las diferentes interpretaciones en torno al estándar de Tratamiento Justo y Equitativo y a cómo equilibrar la necesidad (para el inversor) de un marco de inversión estable y predecible y el derecho soberano (del Estado) a regular, son la causa principal de las diversas soluciones. El concepto del Estándar de Tratamiento Justo y Equitativo en el Tratado se revisa y se compara con la evolución del concepto en otros tratados de inversión. En conclusión, se propondrán posibles enmiendas para aumentar la certeza en los arbitrajes de inversiones presentados al amparo del Tratado de la Carta de la Energía.

Palabras clave: Tratamiento Justo y Equitativo, Expectativas Legítimas, Arbitraje de Inversiones, Tratado sobre la Carta de Energía, Cambios Regulatorios.

Arbitragem de investimento no setor energético

Em que circunstâncias um investidor tem o direito de ser compensado no âmbito do tratamento justo e equitativo previsto no Tratado da Carta de Energia, em consequência do exercício do Estado do seu direito regulamentar em detrimento dos investidores? Análise de casos de arbitragem de investidores no setor fotovoltaico em Itália, Espanha e República Checa.

Resumo: Ocorreu um desenvolvimento importante das energias renováveis em países como a Itália, Espanha e República Checa, principalmente devido ao apoio do Estado a projetos de energias renováveis. No entanto, devido à crise financeira, estes países decidiram rever o seu marco regulatório. Em resultado das alterações introduzidas, os investidores no setor das energias renováveis foram afetados. Consequentemente, foram apresentados pedidos de arbitragem de investimentos contra estes Estados com o amparo do Tratado da Carta da Energia. O presente capítulo analisa esta jurisprudência. Com base nos resultados das arbitragens, verifica-se a falta de consistência nas sentenças arbitrais. As diferentes interpretações entorno do tratamento justo e equitativo e a forma de equilibrar a necessidade (para o investidor) de um quadro de investimento estável e previsível e o direito soberano (do Estado) de regular, são a principal causa das diversas soluções. O conceito de padrão de tratamento justo e equitativo no tratado é revisto e comparado com a evolução do conceito em outros tratados de investimento. Em conclusão, serão propostas possíveis alterações para aumentar a certeza nas arbitragens de investimentos apresentadas com o amparo do Tratado da Carta da Energia.

Palavras- chave: Tratamento Justo e Equitativo, Expectativas Legítimas, Arbitragem de Investimentos, Tratado sobre a Carta de Energia, Mudanças Regulatórias.

1. Introduction and background

Investment in electricity generation from renewable energy sources is rarely considered to be financially viable without state support (Selivanova, 2018, p.433). The principal aim of which is to cover projects high investment costs and encourage sustainable generation. Furthermore, the energy sector is characterized by the existence of long-term contracts (Mistelis, 2018, p.153). The reason for this is that energy projects involve large sums of capital investment and the use of technology that generally has a long useful life (Scherer, 2018, p.14). The application by a state of significant changes to these schemes or to the legal framework which governs a renewable energy investment –after a project has been constructed– may affect the investor's expectations to receive a reasonable return on their investment and to recover costs (Selivanova, 2018, p.433).

Investors often seek guarantees that the legal framework in which an investment is made will remain stable during the entire term of the contract. However, from the state's perspective, it is a challenge to grant the freezing of the legal regime which governs the sector during such a long period of time. The existence of conflicting interests between both parties –investors and states– is, therefore, a fact. This, in some cases, gives rise to disputes. That occurred during the financial crisis due to the over-subsidisation phenomenon. Consequently, several states reversed some of the benefits initially conceded to photovoltaic investors through schemes (Gallagher, 2018, p.250). Investors in photovoltaic energy decided to invest considering a legal framework which was subsequently changed in some way. When the changes that occurred in the regulation did not have an impact on the terms of the business conducted by the investors, the consequence is irrelevant. However, when the changes affect the economic equation of the business, investment arbitration appears as the main tool for the investors (Charles A., 2019, "Investment Disputes Involving the Renewable Energy Industry under the Energy Charter Treaty", Global Arbitration Review).

The state's right to regulate and modify the existing legal framework –once the investment was made– is not under debate. It constitutes an exercise of the principle of state sovereignty, according to which it has right to regulate in its domestic jurisdiction (*Charanne v. Spain*, SCC Case No. V 062/2012, Final Award, 2016, para. 449-503; *Charanne v. Spain*, SCC Case No. V 062/2012, Partial Dissenting Opinion, 2015, para. 11; *Eiser. v. Spain*, ICSID Case No. ARB/13/36 (2017) Final Award, para.362; *Blusun v Italy* Final Award, 2016, para. 317,367 y 372; *Antaris v Czech Republic,* PCA Case No. 2014-01 Final Award, 2018, para. 360 y *Antaris v Czech Republic,* PCA Case No. 2014-01, Dissenting Opinion of Gary Born, 2018, para. 39).

However, certain limits should be imposed on the state's right to regulate domestic matters if such regulations adversely affect the foreign investor's –previously made– investments (Selivanova, 2018, p.433). It has been argued that undertakings or representations that a state has made to attract renewable investments might –in specific situations- create ´legitimate expectations´ for the investors (Graham, 2018, p.221). Although certain tendency seems to be appearing in case-law, there is still not a *jurisprudence constante* regarding this matter. The breach by states of the legitimate expectations of the investors is being considered by some arbitral tribunals (for instance: *Eiser v. Spain*, ICSID Case No. ARB/13/36, 2017; *Infrastructure v. Spain*, ICSID Case No.

ARB/13/31, 2018; *Masdar v. Kingdom of Spain*, ICSID Case No. ARB/14/1, 2018, and *CEF v. Italy*, SCC Case No. 158/2015, 2019) as a violation of the fair and equitable treatment standard of protection ("FET") under the Energy Charter Treaty ("ECT" or Treaty). Article 10(1) of the ECT provides that: "Each Contracting Party shall, in accordance with the provisions of this Treaty, encourage and *create stable, equitable, favourable and transparent conditions for Investors* of other Contracting Parties to make Investments in its Area. Such conditions shall include a commitment to accord at all times to Investments of Investors of other Contracting Parties *fair and equitable treatment*". Nevertheless, other tribunals –in analogous situations- rejected claims regarding the breach of the FET provision, invoking similar arguments (*Charanne v. Spain*, SCC Case No. V 062/2012 Final Award (2016) para. 486-492; *Blusun v Italy* Final Award, 2016, para. 395).

In what circumstances is a foreign investor entitled to compensation under the FET in the ECT as a result of the exercise by the states of the right to regulate to detriment of investors? Significant development has occurred on the *case-law* from *Charanne* to-date, and no comprehensive research has been conducted on this evolution, this Chapter seeks to fill this gap and contribute to the literature. Recommendations made could be useful for arbitral tribunals' in future renewable energy disputes. Besides, some amendments will be proposed in the drafting of the ECT considering the different interpretations around the FET concept. In addition, the progress some International Investment Agreements have experienced in the manner how the standard is defined will be considered.

This Chapter will be divided into five sections. The first sets the context with a brief introduction to the ECT from a theoretical perspective. It is focused on the FET provision and the dispute resolution mechanism in the treaty **(1)**. The second consist of an analysis of the renewable case-law under the ECT concerning states' right to regulate **(2)**. The third section presents the conflict between a state's right to regulate and investor's legitimate expectations. Different approaches to solve this conflict, identified in case-law, will be presented **(3).** Some thoughts on stabilization clauses in energy contracts and the impact they had and might have in future disputes will be presented **(4)**. The final section concludes with closing remarks **(5).**

The state has the sovereign right to regulate and modify its legal framework. Nevertheless, there are limits to the exercise of such power. In case the state goes beyond these limits, a breach of the FET standard under the ECT occurs. Therefore, a new right appears for the investor who is entitled to receive compensation. A new discussion –not subject to analysis herein- opened in the literature about the impact these cases might have in the Energy Transition (Tienhaara K., 2008, p. 24).

2. Overview of the Energy Charter Treaty

2.1. History, Purpose and Modernisation

Since the ECT was ratified by several states, investments in the energy sector have experienced an increase in the substantive protections. The Treaty emerged in a fossil fuel setting because of a gas supply crisis occurred during the period of the cold war. Although it has been argued that its modernization is required, it is the most broadly ratified

investment agreement applicable to energy investments and the unique multilateral treaty exclusively related to energy (Gallagher, 2018, p.256). It provides investment substantive protections, including a dispute settlement mechanism. The Treaty addresses a varied range of aspects related to energy, namely: commerce; investments (promotion, protection and treatment); energy efficiency, and environment.

The treaty's purpose is "to establish a legal framework to promote long-term cooperation in the energy field" (Article 2 of the ECT, 1998). Thus, according to its preamble, the aim of the Treaty is to encourage economic growth through the adoption of measures to liberalise investment and trade in the energy sector (preamble of the ECT, 1998). The preamble should not go unnoticed, as it constitutes a tool of interpretation in accordance with the Vienna Convention on the Law of Treaties ("VCLT"). As the Treaty does not contain a clear definition of the FET, its preamble is used by tribunals as an interpretation tool to determine its content and scope. The disputes reviewed below raised ´alleged breaches´ of some of the substantive protections of the Treaty. Since the treaty does not contain a clear definition of the scope and content of these protections, an exercise of interpretation is required to unravel their meanings.

2.2. FET Standard of Protection and Customary International Law

While the substantive protections are examined –either by the literature or tribunals–, the concepts of ´investor´ and ´investment´ always draw attention. The reason for this is simple. These concepts define the scope of application of the treaty protections determining the jurisdiction *ratione materiae* and *personae* of the tribunal in case of disputes. The definition of investment can be found in Article 1(6) of the Treaty (Article 1 of the ECT, definition of "Investment"). Moreover, according to the Treaty, to be categorized as an investment, the activity done by the investor must be associated with an economic activity in the energy sector (An interesting discussion about this could be find in this case: *Limited Liability Company Amto v. Ukraine*, SCC Case No. 080/2005, Final Award, 2008, para. 42-43). Besides, Article 1(5) defines ´economic activity in the energy sector´ comprising the construction and operation of power generation facilities including those powered by wind and other renewable energy sources. Therefore, in principle the disputes arising out of renewable energy projects –such as the examined herein- are covered by the ECT provisions (Gallagher, 2018, p.257). Regarding the concept of investor, it is defined in Article 1(7) of the Treaty which, in comparison with other investment agreements, is considered broad.

Section III of the Treaty contains the substantive protections for investments. It covers the protections usually found in Bilateral Investment Treaties ("BITs"), such as FET standard of protection; prohibition of discriminatory measures; Most-Favoured-Nation Treatment, and payment of prompt, adequate, and effective compensation for any nationalization or expropriation. The most frequently successfully invoked substantive protection -in renewable energy disputes raised out of regulatory changes- is the FET standard of protection (Dolzer, 2012, p.1; McLachlan, 2017, p. 355-357). Most of the claims, as will be exposed, are based on the states failure to provide a stable and transparent regulatory environment in light of the investor's legitimate expectations (Cyrus, 2017, p.2).

Article 10 (1) of the ECT sets an obligation for the contracting parties to accord FET standard of protection to investors without including a definition of the standard. Consequently, investors often include claims for breaches of the duty of FET in addition to claims brought under other substantial protections. It's been argued that investment treaties –like the ECT- are not self-contained regimes (McLachlan, 2017, p. 296-329). Consistently, the meaning of their terms must be interpreted considering the relevant rules of international law applicable in the relations between the parties in accordance with Article 31(3) of the VCLT. However, it has been asserted that defined by traditional means of interpretation (wording, context, object and purpose) the FET concept is challenging (Schill, 2012). Hence, the lack of definition and the absence of an unanimously accepted meaning from state practice, determine the exercise by tribunals of a significant law-making power in international investment law (Schill, 2012, p.1). Although there is not precedent in Investment-State Dispute Settlement (ISDS) (Cheng (2017) p.1014), Arbitral Awards have become a persuasive authority –at the time of defining the content of the standard- giving raise to what has been called ´normative expectations´(Schill, 2012, p.1). It implies that all stakeholders involved in an investment dispute (state, investor, counsels) expect that the tribunal decide future cases consistently with previous decisions. This flows into the idea that investment treaties will and should be applied and interpreted in the future based on how they were applied and interpreted in the past (Schill, 2012, p.1). As will be reported, this tendency is not completely followed in the analysed cases where *prima facie* inconsistency seems to be the rule (Oliver, 2007, p. 225-243).

Notwithstanding the above debate, while the FET standard continues being part of the ECT, it will require to be interpreted. Concerning the link between FET and customary international law, there is an extensive debate among authors. It is mainly focused on whether the standard of protection is part of the Minimum Standard of Treatment provided to foreign investors in customary international law or if it includes a broader meaning.

There is a consensus in jurisprudence that stability and predictability of the legal framework are important components of the FET provision under the ECT. Some authors have argued that the ECT confers investors operating in the energy field greater protections against regulatory changes than other investment treaties (Hober, 2018, p.175). This statement is based on Article 10 (1) of the Treaty which refers to a state duty to create stable and transparent conditions for foreign investments, as well as the commitment to accord Fair and Equitable Treatment to such investments. Dolzer and Schreuer have identified from the arbitral case law, factual situations or principles to which this standard has been applied. These are: transparency; stability and the protection of legitimate expectations; compliance with contractual obligations; procedural propriety and due process; good faith, and freedom from coercion and harassment (Dolzen, 2012, p. 1).

It is accepted that a reversal of promises by a state that have led to legitimate expectations in the investors will breach the FET standard (*Azurix v Argentine*, ICSID Case No ARB/01/12, Final Award, 2006, para. 287; *Glamis v United States of America*, UNCITRAL, Final Award, 2009, para. 22). Thus, the issue to be addressed is what makes an investor's expectation capable of being considered ´legitimate´. Legitimate expectations are examined in accordance with the host state's legal framework, undertakings, and representations made directly or implicitly by the host state (Levashova, 2019,

International Arbitration Law Library, Volume 50 (Kluwer Law International, 2019). The legal framework on which the investor is entitled to rely consists of legislation and treaties, assurances contained in decrees, licences, as well as contractual undertakings (Dolzen & Schreuer, 2012, p. 1). In addition, tribunals have agreed that investor's legitimate expectations must be analysed in the light of the legal order of the host state at the time the investor made the investment (*Mondev v. United States of America*, ICSID Case No. ARB (AF)/99/2, Final Award, 2002, para. 156; and *AES Summit v. The Republic of Hungary*, ICSID Case No. ARB/07/22, Final Award, 2010, para 9.3.8 and 9.3.18). It was noted that legitimate expectations are not subjective hopes and perceptions, rather, they must be based on objective facts (*Suez, Sociedad General de Aguas de Barcelona, S.A. and Vivendi Universal, S.A. v. Argentine Republic*, ICSID Case No. ARB/03/19, Decision on Liability, 2010, para. 228).

It was pointed out that "changes to general legislation, in the absence of specific stabilization promises to the foreign investor, reflect a legitimate exercise of the host state's governmental powers that are not prevented by a fair and equitable treatment standard" (*Total S.A. v. Argentine*, ICSID Case No. ARB/04/01, Decision on Liability, 2010, para. 164). However, what must be considered is whether measures exceed normal regulatory powers and fundamentally modify the regulatory framework for the investment beyond an acceptable margin of change (*El Paso v. Argentine*, ICSID Case No. ARB/03/15, Final Award, 2011, para. 402).

The legitimate expectation and the proportionality criteria are the main tools applied by tribunals in the *case-law* to evaluate whether the host-state breached the FET provision under the ECT. In the following paragraphs, after a special consideration of the dispute resolution mechanism under the ECT, an analysis of the determination tribunals have done around this concept will be conducted.

2.3. Dispute Resolution Mechanism

International arbitration is the principal tool used by investors under the ECT in case of violation of its substantive protections. The procedures and circumstances under which an investor of a contracting party might submit an investment dispute to International Arbitration are set in Article 26 of the ECT (Gaillard, 2018, p. 1). The Treaty contemplates a *cooling off* period of three months from the request of amicable settlement. After this period, the investor is entitled to choose to submit the dispute for resolution either to the courts or administrative tribunals of the contracting party to the dispute, or in accordance with a previously agreed dispute settlement procedure or to International Arbitration. Article 26 of the ECT clearly grants this choice to the claimant as it states that if the dispute cannot be amicably settled, "the investor party to the dispute may choose to submit it for resolution" (Gallagher, 2018, p. 262). Thus, under the ECT it is only at the investor's instigation that arbitration can be commenced. The text of the Treaty differs significantly from other treaties which provide that a dispute may be submitted at the request of either party to an *ad hoc* arbitral tribunal or arbitration under the auspices of ICSID (See the Article 9(3) of the China-Ethiopia BIT, 1980). Therefore, a *fork in the road* provision is contained in the Treaty that potentially bars an investor's claim if another dispute-settlement mechanism has been selected (Gaillard, 2018, p.1). Moreover, the Treaty gives right to any party involved in the dispute to set as a place of arbitration a

state that has ratified the New York Convention, which reaffirms the enforceability of the award (Article 26 (5) (b) of the ECT). This is notwithstanding the debate in cases of intra-European Union investment arbitration awards which will not be examined herein (*Achmea B.V. v. The Slovak Republic*, UNCITRAL, PCA Case No 2008-13, 2008). Therefore, International Arbitration constitutes a guarantee for the investor. Point was made that it would be of little benefit to foreign investors if they were obliged to enforce their rights under investment treaties in the local courts of the host state responsible for their mistreatment, since often the action complained of is a change in the local law the relevant court is obliged to uphold (King, 2012, p. 1). The investor is also afforded a wide choice in terms of institutions and rules which can have a significant impact on its claim (Article 26 (4) of the ECT).

The above overview lays the foundations for the analysis of renewable energy arbitration disputes in the next chapter.

3. Renewable ECT Arbitrations and Investors' Legitimate Expectations

3.1. Regulatory changes and context of its implementation

Political risk has always been a problem for renewable energy investors. An exponential growth in renewables has occurred across the world–especially in Europe- during the last decade. The growing focus on renewable energy was reflected in the creation of the International Renewable Energy Agency (IRENA). IRENA is an intergovernmental agency. Its principal objective in accordance with the Article II of its Statute is to "promote the widespread and increased adoption and the sustainable use of all forms of renewable energy". The reasons for this can be found either at a domestic or an international level. Concerning the latter, -through treaties- several commitments were taken on by states to reduce green-house gas (GHG) emissions to combat climate change (CC) (United Nations Framework Convention on Climate Change (UNFCCC) signed in 1992 and entered into force in 1994; Paris Agreement on Climate Change in 2015). Since then, they intended to reproduce the assumed international obligations in their domestic jurisdictions. Consequently, different supports were given at a local level to incentivize renewable development. For instance, Feed-in-Tariffs (FIT); Feed-in Premiums; green certificates; quota obligations; loans, and tax exemptions. The FIT regime resulted in a tariff deficit, meaning that the subsidies the government was paying to the operators of photovoltaic parks were higher than the end-price the government charged for that energy. Conversely, because of the financial crisis and over-subsidisation, several states decided to modify the policies connected with the granted supports (Gallagher, 2018, p. 257). In general, the regulatory modifications implemented by the states comprised cutbacks on subsidies for renewable energy; creation of new taxes; implementation of a state levy on solar energy, limitation of the term for regulated tariffs; imposition of limits on equivalent production hours; obligation to fulfil new technical requirements; obligation to pay a charge for grid access, and the reversal of the prioritised dispatch (Restrepo, 2017, p. 8). Therefore, renewable investors who invested based on a regime that was then modified were affected in some manner. Subsequently, several investment-

arbitration claims against host-states -mainly Spain, the Czech Republic and Italy- have been brought under the ECT provisions.

The fact is that these countries adopted measures to comply with their international obligations to reduce GHG. It was the global financial crisis that made the measures unsustainable. There are those who argue that tribunal decisions should take the global intention to lower GHG emissions into account and consider the international instruments supporting this aim (Restrepo, 2017, p. 8). However, this approach is not considered in the Awards reviewed here. This confirms that Tribunals have little room to review international law on climate change. Some concerns have been expressed about the impact the awards may represent to the aim of combating Climate Change (CC) (Restrepo, 2017, p. 8). The main concern is that it may incentivize host-states not to take CC measures to avoid the risk of facing high value claims and eventually, adverse decisions (Restrepo, 2017, p. 8). This phenomenon is well- known in literature as *´regulatory chill´* (Baetens, 2011, p.11). Nevertheless, there is no evidence about its occurrence, which must be evaluated over the next few years when pending cases are finished and in relation to the subsequent conduct of states (Tienhaara, 2018, p.24).

3.2. Tendencies and Unsuccessful Allegation of Indirect Expropriation

It is a fact that the FET is the most successful substantive protection in the studied cases. As explained, the modification of renewable regulation in Spain, the Czech Republic and Italy resulted to date in sixty international arbitration claims under the ECT (See list of all arbitrations filed against Italy, Spain and The Czech Republic in THE ect database: https://energycharter.org/what-we-do/dispute-settlement/all-investment-dispute-settlement-cases/). Investors' who were affected as a consequence of the regulatory changes seek protection under the substantive provisions of the ECT by means of investment arbitration. This means that, currently, sixty out of one hundred and twenty-two disputes brought under the ECT are related to the modification of renewable' regulations in the mentioned countries.

Firstly, forty-five of these claims are against Spain; six (*Charanne; Isolux;Antin;Eiser;Masdar;Novenergia)* of them have been resolved and the awards are publicly available; two *(Charanne &Isolux)* concluded that Spain is not liable to pay damages and the remaining four considered it is *(Antin;Eiser;Masdar & Novenenergia)*. The regulatory changes that motivated investors' claims were different in *Charanne* and *Isolux* -cases decided in favour of the state- in comparison with the regulatory changes considered in *Antin; Eiser; Masdar; Novenergia* -decided in favour of the investor. The existence of different regulations on which the claimants based their claims and the different impact they caused in the investors' business seem to be *prima facie* the principal reasons for different Awards (Kudrat, 2018, p. 5).

Secondly, nine of these claims are against Italy; three (*Blusun; CEF & Greentech*) of them have been resolved and the awards are publicly available; one concluded that Italy is not liable to pay damages (Blusun) and the other two considered it is (*CEF & Greentech*).

Thirdly, six *(Antaris; Voltaic; Photovoltaik; WA; ICW; ICW*) of these claims are against the Czech Republic; five *(Antaris; Voltaic; Photovoltaik; WA; ICW)* of them have been resolved concluding that the state is not liable to pay damages.

Hence, out of a total of fourteen awards publicly available, eight have been decided in favour of the host-state and six in favour of the foreign investor. However, the jurisprudence changed significantly since the first Award was rendered in *Charanne*. The vast number of pending cases against Spain and extra official information accessible about the non-publicly available awards suggest that this tendency would be probably modified rapidly (Tones, 2019).

As was asserted, under the ECT different wording cannot serve as an explanation for divergent interpretations (D'Agostino, 2007, p.50). However, the above tendencies show how tribunals have achieved different conclusions considering similar facts and a unique Treaty.

From the reviewed awards emerges that substantive protections under which most of the investors presented their claims in the hypothesis of regulatory changes were the FET-standard and Indirect Expropriation. In the case of the claims against Spain, four of the investors claimed jointly a violation of the FET-standard and indirect expropriation (*Charanne*; *Eiser; Isolux* ; & *Novenergía,*), while two investors (*Antin*; *Masdar)* merely claimed a breach of the FET-standard. Concerning the claims filed against Italy, from the awards follow that merely one of the investors claimed jointly a violation of the FET-standard and Indirect Expropriation (*Blusun*), while two only claimed exclusively a breach of the FET-standard (*CEF & Greentech*). Regarding the claims filed against the Czech Republic, follows that all the investors claimed solely a violation of the FET standard (*see* the following Final Awards: *ICW,* para.125; *Photovoltaik,* para.124; *Voltaic,* para.125; *WA* para. 125). Consequently, the above figures show that the FET standard is preferred by the investors to base their claims in case of regulatory changes by host-states. In addition, there is no case in which the investors invoked exclusively indirect expropriation. In terms of the awards' outcomes, it flows that all the cases decided in favour of the investors (*ICW*; *Photovoltaik*; *Voltaic*; *WA*; *Antin*; *Eiser*; *Novenergia*; *Masdar*; *CEF*; and *Greentech)* the state liability was determined based on a breach of the FET-standard. Thus, considering the above analysis, the FET standard is not only the most preferred standard by the investors to base their claims on, it is also the most successful of them.

Although indirect expropriation is not subject to analysis herein, some brief assertions will be done regarding the cause of its unsuccessful allegation. In *Charanne* the Tribunal pointed out that the concept of expropriation is generally accepted as ´a taking involving a deprivation of property´ (*Charanne v. Spain*, SCC Case No. V 062/2012, Final Award, 2016, para 460). The tribunal followed the standard of indirect expropriation under international law, which requires the presence of a substantial effect on the property rights of the investors (*Charanne v. Spain*, SCC Case No. V 062/2012, Final Award, 2016, para 461). It was pointed out that a loss of value considered as expropriation must be of such magnitude as to amount to a deprivation of property (*Charanne v. Spain*, SCC Case No. V 062/2012, Final Award, 2016, para 464). Consequently, it was concluded that the claimants failed to prove that the disputed measures had an effect tantamount to an expropriation (*Charanne v. Spain*, SCC Case No. V 062/2012, Final Award, 2016, para 462). This conclusion reflects the high threshold in jurisprudence to consider that government measures amounted to an expropriation (*Blusun v Italy,* Final Award, 2016, para 408 & *Greentech Energy Systems A/S, et al v. Italian Republic*, SCC Case No. V 2015/095 Final Award (2018), para. 727).

Normally, in renewable energy cases involving adverse regulatory measures -as the studied herein- investors remain in ownership of the affected investment, nonetheless the investment has suffered a loss of value due to the regulatory changes implemented. In the facts the investor continues operating the photovoltaic park which continues to generate energy, and thus profit.

In this sense, the *Isolux* Tribunal determined the non-occurrence of expropriation after comparing the profitability of the investor at the time of investing with the current profitability of the solar plants. Being the latter higher, the tribunal concluded that ´in no way can a "severe" or "radical loss" occurred concluding the not expropriator nature of the measures adopted by Spain (*Isolux Netherlands, BV v. Kingdom of Spain*, SCC Case V2013/153, Final Award, 2016 para. 852-853).

3.3. FET as a protection against Host-State Regulatory Changes

The allegation of a breach of the FET by investors in the cases is followed by a response of the states denying such breach. The main arguments presented by both parties will be presented here-after. As was pointed out, state support has been a necessary precondition for investments in renewable projects (Selivanova, 2018, p.433). Although currently renewables are becoming quite competitive, when they were trying to compete at the beginning with a very entrenched fossil fuel industry, they faced many challenges. Some of them were inertia to change, high capital costs, and lack of appreciation of the urgency of climate change mitigation (Outka, 2012, p. 65).

There is consensus that the reversal of supports by host-states that had led to legitimate expectations in the investors would violate the FET standard under the ECT (Dolzer, 2012, p.1). However, as will be exposed, there is no general agreement, neither in literature nor in jurisprudence, about when the investor has a legitimate expectation that the legal framework would not be modified. Thus, the key legal issue to be addressed is what makes an investor's expectation liable to be considered 'legitimate' (Tellez, 2012, p.27). A review of the investors' and host-states' assertions about this concept will be conducted in the following paragraphs.

The *rationale* behind investors' claims is the idea that the regulatory modifications introduced by states have affected the legal and economic regime established by previous regulation, on which they relied at the moment of making their investments (Selivanova, 2018, p.433). They asserted that the changes caused damages and thus it must be repaired (Tellez, 2012, p. 27). By means of a Treaty interpretation and referring to several *case-law*, investors alleged that the FET standard imposes an obligation for the states to maintain a stable and predictable legal framework (*Charanne v Spain,* Final Award,, 2016, para. 293). They likewise affirm to have a legitimate expectation that the legal framework considered when investing would not be modified (*Charanne v Spain Final Award,* 2016, para. 294*)*. They pointed out that, via regulatory reforms, states breached their obligations to provide FET under Article 10 (1) of the ECT. The investors mostly recognized that states -as part of their sovereign power- are permitted to change their regime under the ECT, but those changes must be predictable and in line with investors' expectations (*Antin v Spain* Final Award, 2018, para. 414 & 377). To justify the existence of a legitimate expectation, the criteria usually used –which is commonly accepted in jurisprudence- consist of identifying certain elements in the conduct either of the state or the investor.

These elements are an explicit or implicit representation made by the authorities of the state (about the freezing of the legal framework); such representations must be relied by the investor at the moment of investing, and the legitimacy and reasonableness of the expectations at the light of the circumstances of the cases. Regarding the representations made by states, investors alleged that mostly are contained in the legislation –whatever form it adopts (*Charanne v Spain*, 2016, Final Award para 295). In addition, could be identified -apart from the legislation- in other type of evidence, such as press release; declarations made by public officials; meetings with government representatives, and publicity through which the state promotes the investment such as the Spain campaign, *´The sun can be yours´* (*Antin v Spain*, 2018, Final Award, para. 366). In some cases investors alleged that the promise of stabilization was indirectly contained in the legislation, while others -going beyond this argument- affirmed that a stabilization clause with a specific commitment of freezing the legal framework was expressly contained in the legislation (Ivaylo, 2018).

Conversely, the *rationale* behind host-states' responses is that although the FET standard provides that a stable regulatory framework must be granted to investments, this does not imply that the legal system must be unmodified. The idea that the FET standard is not a stabilisation clause is repeatedly alleged by states. It was affirmed that they can continue to legislate responding to changing circumstances if they do so in an equitable and reasonable manner (*Charanne v Spain* Final Award, 2016, para. 355). States alleged that the violation of legitimate expectations requires a specific commitment that the legal framework that governed the investments would not be modified (*Charanne v Spain Final Award,* 2016, para. 356). Thus, in absence of a specific commitment, the only expectation that the investor would have is that the legal framework would be modified. Host-states stated that investors' expectations must be objective, reasonable and legitimate. To determine their scope, they observe what knowledge the investor had or should have had about the regulatory framework in the country in which the investment was done (*Charanne v Spain* Final Award, 2016, para. 364). Therefore, they asserted that what makes a state measure reasonable is the public interest pursued by it (*Antaris v Czech Republic* Final Award, 2018, para. 354). Thus, the adjustments to the legal framework are considered by states to be coherent and reasonable as they aim to adapt to changing economic circumstances and solve the problem of tariff deficit responding to a public interest (*Antaris v the Czech Republic* Final Award, 2018, para. 365).

While setting a general overview of the arguments presented either by investors or host-states, tribunal determinations on the subject will be examined in the following section. The strength of the arguments presented by both parties is unquestioned. Beyond their arguments, some principles could be identified. Behind states' arguments, the *principle of sovereignty* (Byers, 2002, p.47) and the *public interest exception* appear as a main ground. The principle of sovereignty has been defined as "the full power of the state in its territory and its independence from other states" (Feshenko, 1988, p.40). This power includes the ability of the state to create their own legislation and to modified it when circumstances so required. This idea governs the states´ arguments the in the cases under study. Alternatively, in some dissenting opinions of the cases under study, some argue that while there is a right to regulate, it does not forgive a state of its obligation to compensate (*Charanne v Spain* Dissenting Opinion Guido Tawil, 2015, para 5 & *Antaris v Czech Republic* Dissenting Opinion Gary Born, 2018, para. 7). Conversely, it has been

pointed out that a compensation requirement would discourage regulation and without forgiveness of liability, the right to regulate could not exist (Giest, 2017, p.18).

In addition, the public interest exception is used by states to justify the regulatory changes implemented. It has been argued that generally acknowledged that states need to be given some freedom for public interest regulation (Giest, 2017, p.18). And thus, public interest exceptions are incorporated into investment treaties to reduce liability when the regulation is intended to benefit the public and prevent the chilling of such regulation (Giest, 2017, p.18). In the reviewed cases states alleged that the regulatory changes implemented responded to a public interest as a result of the financial crisis being that an exception to the ECT promise of stability.

However, under investor's argument, the doctrine of *no venire contra factum propium* or e*stoppel* (Sombra, 2016, p.9) –by which the legitimate expectations rule is influenced- is easily recognised. The doctrine of *no venire contra factum propium* consists of the prohibition of disloyal or inconsistent behaviour. It lies in avoiding contradictory behaviours regarding previous manifestations of will that are based on good faith and that can cause damages (Sombra, 2016, p.9). Similarly, the concept of estoppel in common law is related to the protection of the practice of an initial behaviour that results from a legitimate expectation that such practice conforms with good faith (Sombra, 2016, p.9).

At the end, it appears that after a confrontation between state rights to regulate and investor legitimate expectations, that who wins the battle will obtain an award in its favour. Thus, the decision-maker role that arbitrators play in these cases is not simple. This not only because of the strength of the arguments alleged by both parties, but also because of a rising concern about the possible interference of international investment rules with domestic law (Lise, 2014).

3.4. Tribunal Approaches to FET Standard in the Context of Regulatory Changes

Due to the lack of definition of the FET in the ECT, tribunals have interpreted the provision differently. There is consensus in the jurisprudence that the duty to provide FET implies an obligation to create a stable, equitable, favourable, and transparent conditions for investments (*Charanne v Spain* Final Award, 2016, para. 447). The following have been construed by arbitral tribunals as elements of the FET-standard: the legitimacy (reasonableness) of investor expectations; the stability, predictability and transparency of treatment by the state, and the absence of arbitrariness or discrimination in such treatment (Restrepo, 2017, p. 8).

This interpretation is done by means of a literary analysis of the text of the treaty in terms of the meaning of the words *´fair´* and *´equitable´*, in cooperation with some provisions of its preamble in accordance with the criteria defined to interpret treaties in the VCLT.

There is also a compromise about the fact that the state cannot induce an investor to make an investment generating legitimate expectations, to later ignore the commitments that had generated such expectations (*Charanne v Spain* Final Award, 2016, para. 486). It is also accepted that investors' legitimate expectations come from specific commitments of the state, for example those assumed by means of a stabilization clause. Some tribunals

understood that in the absence of a specific commitment, an investor cannot have a legitimate expectation that existing legal framework will not be modified. However, regarding the rules that are not specifically addressed to a particular investor –normally designed to encourage foreign investment-, there is no consensus in tribunals about its ability to be considered as a source of a commitment of the state. In this sense, some have expressed that the existence of a specific commitment – whether of a contractual nature, or based on statements or specific terms granted by the host-state– can be based on the legal order in force when the investment was made (*see Gary Born* and *Guido Tawil* dissenting opinions). This installed the discussion about whether a representation is valid to create a legitimate expectation in the investor, a debate that makes the lack of consistency evident.

The idea that the state has a reasonable degree of regulatory flexibility to face to the changing circumstances in the public interest is generally accepted (*Eiser v Spain* Final Award, 2017, para 387. However, those subsequent changes –in case they happen- should be made fairly, consistently, and predictably, taking into consideration the circumstances of the investment (*Charanne v Spain* Final Award, 2016, para 500). Nevertheless, in some dissenting opinion it's been argued that if in the valid exercise of that regulatory power of the host-state it affects acquired rights or legitimate expectations of the investor, the state must compensate the damage caused (*Charanne v Spain* Dissenting opinion Guido Tawil, 2016, para. 11).

There is also consensus regarding the fact that the regulatory measures, to be in violation of investors' legitimate expectations must not have been reasonably foreseeable by the investor (*Charanne v Spain* Final Award, 2016, para 506). To prove this aspect, investors use either reports or other type of evidence to support the fact of having done a due diligence process before the investment decision to mitigate or avoid any type of risk that could appear. This suggests how important the evidence may be in the resolution of this cases. Although *prima facie* the expectation seems to be located in the subjective scope of the investors, it is generally accepted by tribunals that the legitimate expectation must be proved objectively and assessed on a case-by-case basis (*Antin v Spain*, 2018, Final Award, para. 536). This idea reveals the importance of the realization of a due diligence by the investor prior to make the decision to do an investment. This is not only to assess possible risks, and eventually mitigate or avoid them, but also to pre-establish evidence to be prepared in case of dispute. The expectation is in the subjective sphere of the investor who eventually will face the challenge to make visible in an objective manner. The investor is who has the burden of proving such expectations, thus, as was alleged, the strongest the evidence is, the more likely to obtain an award in which the legitimate expectation be recognized (*Antaris v Czech Republic,* 2018, Final Award, para. 368).

There are other aspects that in a case by case basis are analysed by the tribunals when assessing a legitimate expectation. For instance, the lifespan of the technology used in a project -such as the solar panels-, or the term of the lease agreement for the land above which the photovoltaic project is to be built (*Charanne v Spain* Final Award, 2016, para 521 & 522). This elements contribute to exteriorize in some way the expectations the investor has and the reasonableness of its expectations at the light of the circumstances of the projects.

Some tribunals refer to a *test of proportionality* when assessing the regulatory changes. This test analyses that the modifications are not capricious, unreasonable, arbitrary, contrary to public interest, disproportionate or unnecessary, and do not suddenly and unpredictably eliminate the essential characteristics of the existing regulatory framework (*Charanne v Spain*, 2016, Final Award para. 517 & 539).

Others refer to *´an acceptable margin of change´* in the regulation by the states in parallel to the *´margin of appreciation doctrine´* (*see* dissenting opinion of Gary Born, 2018, para. 39). The basic idea behind is that the state is entitled to a certain '*room to maneuver*', within which its conduct is exempt from full-fledged review. Tribunals appear to conclude that the state retains a margin of discretion to balance the investor's expectations against public policy objectives and that only the exercise of regulatory power exceeding that margin can constitute a breach of a state's obligations under the treaties' FET standard.

The Spanish, Czech and Italian renewable energy arbitrations are likely to focus on whether the host-state acted with consistency, transparency, and reasonableness in modifying the existing regime, and whether investors had legitimate expectations that the legal framework would not be modified. As emerges from the tribunals determinations, there is not an exclusively standard as to when investors' expectations deserve treaty protection under the FET standard, any evaluation will depend on several aspects, such as the facts of the cases, the evidence provided by the parties, the scope of the regulatory modifications adopted, and the impact they caused on the investors. The legitimate expectations' rule developed by tribunals as an instrument to assess the breach of the FET standard will be explained in detail in the following paragraph. Such analysis will bring us a step closer to the answer this Chapter questions.

3.5. What Attributes must an Expectation have to be considered as Legitimate?

As was largely argued hereinbefore, it is accepted that a violation of a legitimate expectation of the investor would derive in a breach of the FET-standard. Since there is no provision in the ECT referring specifically to investors' legitimate expectations, the determination of the extent and content of protection of such expectations is being assessed by Tribunals through a review of the relevant case law on the matter (Tellez, 2010, para. 110).

The lack of rigorous analysis by tribunals supporting the use of legitimate expectations is noted in most of the reviewed awards. Some exceptions to this rule are the cases against the Argentine Republic (*Continental Casualty Company v. The Argentine Republic*, ICSID Case No. ARB/03/9, Final Award, 2009, para, 260-262*; Total S.A. v. The Argentine Republic*, ICSID Case No. ARB/04/01, Decision on Liability, 2001, para. 113 and *El Paso El Paso Energy International Company v. The Argentine Republic,* ICSID Case No. ARB/03/15, Final Award, 31/10/2011, para. 356-364 which contain important analysis of the subject matter and are constantly referred by tribunals in the cases under study).

The doctrine of legitimate expectation has been established on precedents —awards citing prior awards that have mentioned the concept. However, as will be explained, this approach without additional elaboration is unsatisfactory. The *rationale* behind the legitimate expectations doctrine is that the investor should not be protected from the

ordinary business risk of an investment, and that the expectations of the investor must have been reasonable and legitimate in the context in which the investment was made. The logic behind the rule is to encourage foreign investors to make adequate business decisions based on the legal regime in force in the state, and the representations made by the host-states. Therefore, this doctrine requires to be assessed in a case by case basis.

It has been argued that little justification has been provided by tribunals to account for the use of legitimate expectations in the context of the FET-standard (Potestá, 2013, p.88). This is surprising considering the lack of explicit definition of the concept in the ECT. However, there is a tendency to define the content of the standard in the last Investment Agreements. For instance, the United States-Mexico-Canada agreement (USMCA) contains a provision expressly excluding the legitimate expectations to the scope of the FET standard (Article 14.6(4) of the USMCA). Conversely, the Investment Agreement recently signed between the European Union and Vietnam (*see* the Investment agreement between the European Union and Vietnam) provided a clear definition of the FET standard including a protection of the investor´s legitimate expectations in its scope. The latter seems to be the rule in the last Investment Agreements, reason why some authors speaks about its evolution (Behn, 2015, p.363). This reaffirms the need to modify the ECT to make it participant of such evolution.

Tribunals have accepted that the mere subjective belief held by the investors is insufficient to create a legitimate expectation (*Charanne* Final Award, 2016, para 493). Therefore, some objective criteria have been identified in jurisprudence to evaluate whether a legitimate expectation exists. The following paragraphs identify different elements and forms in relation to which a breach of legitimate expectations has been found by tribunals. The absence of a clear definition of the standard in the text of the ECT obliges tribunals to find mechanisms to define it. What is curious about the tribunal's decisions is the use of some extracts of other awards to underpin their positions, while they were rendered under the scope of application of a different legal framework (Chen, 2019, p.47). This installs the discussion -that will not be subject to analysis herein- about whether there is a universal concept of the FET-standard, or if, on the contrary, it has a different meaning and content depending on the legal framework it is contained on.

Based on the determinations of the tribunals in the case law analysed in this dissertation, four elements can be identified as decisive in evaluating whether the expectations of an investor are legitimate (Levashova, 2019, p.51). Firstly, the specific representations made by the host-state to an investor. Concerning the representations, the analysis will include situations where the investor invokes contractual commitments or unilateral representations of the state through general legislation. Secondly, the stability of the general regulatory framework will be assessed. Regarding states right to regulate, it has been argued that unqualified protection of legitimate expectations may have the effect of limiting the state's right to regulate (Potestá, 2013, p.88). That is why this issue will be addressed in the following chapter, as it deserves specific analysis. Thirdly, tribunals consider the economic and socio-political circumstances in the host-state at the moment of the investment. And finally, the investor's conduct before making the investment -due diligence and risk assessment- will be examined as an element also being considered by tribunals.

Regarding the first element -specific representations by host-state- the arbitral practice confirms that representations by the state are, in principle, capable of creating legitimate expectations, and thus may be protected under the FET-standard, if they are later unknown by the state. Regarding the form in which the state can make those promises, commitments, or representations, lack of consistency appears in case-law.

There are two approaches in case-law to assess the existence of a state representation. The first entails the host state to have made clear, direct and specific assurances to the investor regarding the specific relationship -which is normally a contract- that the legal framework will not be modified. As an example, *Charanne* tribunal has affirmed that "in the absence of a specific commitment, an investor cannot have a legitimate expectation that existing rules will not be modified" (Charanne, Final Award, 2016, para. 499). The second approach understands that the expectations could be based on assurances of the state provided in general applicable laws of a country, or the legal framework at the time of the investment. A tribunal is more likely to find a breach of the FET where the host-state, implicitly or explicitly, made specific representations, commitments, assurances or promises on which the foreign investor relied in making the investment.

Some claimants intended to rely on statements by the host-state in investment promotion documents, in which it was asserted that high return in photovoltaic sector could be reached. Another strategy used by claimants is invoking the legal framework in force at the time of investing as the basis of their legitimate expectations (Charanne, Final Award (2016) para. 491). Some tribunals asserted that the investment promotion documents and the legislation per se could not create a legitimate expectation that specific laws would not modified (Charanne, Final Award, 2016, para. 496 & 497). However, in some dissenting opinions –in all circumstances issued by arbitrators appointed by investors-, a different position was expressed regarding this matter (Gary Born and Guido Tawil Dissenting Opinions).It was asserted that legitimate expectations could arise from the legal system in force at the time of the investment. An UNCTAD publication on FET is used to justify the idea that an investor may derive legitimate expectations from "rules that are not specifically addressed to a particular investor, but which are put in place with a specific aim to induce foreign investments and on which the foreign investor relied in making his investment" (UNCTAD´FET: UNCTAD Series on issues in International Investment Agreements II´, 2012).

Thus, it is clear from case-law that not every representation or assurance creates legitimate expectations. A certain degree of precision, specificity or lack of ambiguity for representations to be enforced under the theory of legitimate expectations is required. In this sense tribunals seem to follow the principles set on the ILC Guiding Principles. This principles reflect the idea that state's statement would involve obligations for the expressing state "*only if it is stated in clear and specific terms*" (Guiding Principles applicable to unilateral declarations of States capable of creating legal obligations´, in:<http://legal.un.org/ilc/texts/instruments/english/draft_articles/9_9_2006.pdf>). The requirement of the specificity of the promise is analysed by tribunals from different angles. Firstly, regarding the object or content of the promise. Secondly, considering who the promise or representation is addressed to. In terms of the content, what is assessed is whether there is a promise to maintain the legal framework unmodified. Regarding the addressee of the representation, what is discussed is if a promise addressed to a specific investor

is required, or if statements of a more general nature, such as legislation or statements by politicians or government representatives directed to investors, are able to create legitimate expectations.

In *Charanne*, the tribunal asserted that the commitment of the state could have been made based on a stabilization clause, or a statement directed to the investors assenting that the existing regulatory framework will not change. The Tribunal concluded that these declarations have not been addressed to the investor. However, in the dissenting opinion of the same case, Tawil expressed that the legitimate expectation can originate or be based on the legal order in force when the investment is made. The *Charanne* decision was determinant in the change of strategy adopted by the investor in later arbitrations. This notwithstanding the fact that in Charanne the tribunal only considered the first regulatory changes implemented by Spain. Thus, this case can be distinguished on the facts to the subsequent awards against Spain which considered additional regulatory changes. According to the tribunals, while in *Charanne* the regulatory changes did conserve the principal characteristics of the investment, in *Eiser* they did not. Consequently, one can easily arrive at the conclusion that the main factor to determine proportionality was the substantiality of the loss (Restrepo, 2017, p.101). For instance, in *Eiser* the investors alleged that the decree, which was designed to attract investment, contains a stabilization clause (*Eiser* Final Award, 2018, para. 357). Although the tribunal did not analyse the nature of the decree provision –whether it constitutes a stabilization clause-, it concluded that ´investors must expect that the legislation will change, absent a stabilization clause or other specific assurance giving rise to a legitimate expectation of stability´ (*Eiser* Final Award, 2018, para. 362).

However the *Isolux* tribunal based on an *UNCTAD report* concluded that an investor may derive legitimate expectations not only from specific commitments addressed personally, but also from rules that are not specifically addressed to a particular investor but which are put in place with a specific aim to induce foreign investments, and on which the foreign investor relied in making his investment ("UNCTAD´FET: UNCTAD Series on issues in International Investment Agreements II", 2012). The *Novenergia* Tribunal concluded that Spain actively promoted the perception of its legal framework as stable, transparent, and welcoming to investors through its reports, *´The Sun Can Be All Yours´* and other prospectuses creating legitimate expectation that the legal framework was not going to be modified (*Novenergi*a *v Spain*, 2018, Final Award, para. 556). The *Antin* tribunal concluded that state undertakings were sufficiently specific to generate legitimate expectations for the investor. The tribunal based the decision on the stabilization commitment contained in a decree and specific representations addressed to the investor in meetings (*Antin v Spain*, 2018, Final Award, para. 365).

In the cases against Italy, *Blusun* tribunal states that, in the absence of a specific commitment, the state has no obligation to grant subsidies such as FIT, or to maintain them unchanged once granted (*Blusun v Italy*, 2016, Final Award, para.319). The *CEF* tribunal, however, based the existence of investor's legitimate expectations on the recognition letters issued by the state, in which certain fixed price and term were mentioned (*CEF v Italy*, 2019, Final Award, para. 211). The Tribunal also took into consideration the agreements signed by the state and the investor; these, even though did not contain a stabilization clause, did contain a clause of modification asserting that

the only mechanism to modify the contract was by mutual agreement in writing (*CEF v Italy*, 2019, Final Award, para. 214).

In the cases against the Czech Republic in *Antaris* the tribunal concluded that "*the provisions of general legislation applicable to a plurality of persons or a category of persons, do not create legitimate expectations that there will be no change in the law*" (Antaris, 2018, Final Award, para. 360.6). However, in the dissenting opinion it was asserted that the state enacted legislation that provided specific and unambiguous guarantees to investors in renewable energy guaranteeing that specified minimum tariffs would be payable for electricity produced by renewable energy sources for a period of 15 years, being this guarantees the instrument by which the legitimate expectations were created (*Antaris*, Dissenting Opinion, para.7). In *Photovoltaik*, the tribunal asserted that in the absence of a stabilization commitment -either contractual, legislative, or individual- it is not possible to allege that changes in the law applicable to the foreign investment in question were unlawful (Photovoltaik, Final Award, para. 482).

There is a general agreement in jurisprudence about the fact that if there is a specific commitment of the state in an agreement about the freezing of the legal framework –by a stabilization clause-, the lack of compliance with this will determine a violation of the FET-standard. Nevertheless, when there is no stabilization clause, the jurisprudence is divided. The general and less specific the representation is -in terms of content and addressee- the less likely to be considered valid to create legitimate expectations. However, this element never is assessed alone, being evaluated considering the specific circumstances of the case.

Regarding the second element considered by tribunals when evaluating the existence of legitimate expectations -stability of the regulatory framework- tribunals agree that the FET-standard involve an element of stability of the regulatory framework. Thus, some tribunals have been willing to extend protection under this standard to the state's duty to maintain a stable framework. Often, this has been supported by reference to the ECT preamble, which refer to stability of investments in the energy sector. However, certain tribunals have asserted that, as a matter of principle, the state's right to regulate cannot be considered frozen or restricted as a result of the existence of investment treaties. In *Saluka Investments v Czech Republic*, one can find repeated statements to the effect that no investor may reasonably expect that the circumstances prevailing at the time of the investment remain totally unchanged Tribunal required due diligence from the investor, who 'must anticipate that the, circumstances could change, and thus structure its investment in order to adapt it to the potential changes of legal environment' (*Saluka Investments B.V. v. The Czech Republic*, UNCITRAL, Partial Award, 17/03/2006).

Eiser tribunal recognized that the states have the right to regulate -including the right to change existing regulations. However, the tribunal noted that the ECT protected investors against what it characterized as 'fundamental' and 'unprecedented' regulatory changes that led to a 'totally different' regulatory regime than the one in place when the investment was made, particularly when those changes had a significant negative impact on prior investments that had been made in reliance on the previous regulations. This right may involve some modifications in previous regulations when necessary. In this sense was pointed out that the FET-standard cannot suppose the freezing of the legal regulation of economic activities in contrast to the state regulatory power and the

evolutionary character of economic life (*EDF v. Romania*, ICSID CASE No ARB 05/13 (Final Award) 08/10/2009, para. 217). Accordingly, arbitral tribunals have emphasised, in rejecting claims based on an alleged breach of the FET, that: 'No investor may reasonably expect that the circumstances prevailing at the time the investment is made remain totally unchanged'. Rather, a determination 'whether frustration of the foreign investor's expectations was justified and reasonable' requires consideration of 'the host-state's legitimate right subsequently to regulate domestic matters in the public interest'.

In its assessment of the legitimacy of investor expectations, the tribunal considered it pertinent, referring to *Electrabel v Hungary*, to look at the information available to investors at the moment of the investment: "Fairness and consistency must be assessed against the amount of information that the investor knew and should reasonably have known at the time of the investment and of the conduct of the host-state" (*Electrabel S.A. v. Republic of Hungary,* ICSID Case No. ARB/07/19 (Final Award) 25/11/2015, para7.78). For the legitimate expectations of investors to be violated, such new regulatory changes should not be foreseeable for a prudent investor (*Isolux Netherlands, BV v Kingdom of Spain*, SCC Case V2013/153 (Final Award) 12/07/ 2016, para.781).

The expectations as to the regulatory framework must be assessed *in concreto* regarding all circumstances, including the specificities of the host-state, its level of development, as well as the sector in which the investment was made. However, if an alteration of the law has benefitted the investor, then the latter's legitimate expectations, far from being violated, are protected, and enhanced (Tellez, 2012, p.432).

Another element that tribunals consider is the reasonableness of the investors' expectations in the specific economic and socio-political context of the host-state. It is obvious that what an investor can legitimately expect -particularly in terms of stability- cannot be alike in a developing country than in a developed country. Tribunals have considered that the ´reasonableness requirement´ intrinsic in the expectations requires a scrutiny of all the circumstances that the investor should have considered when making the investment, including the level of development in the host state. In the analysis of this element -which *prima facie* seems to be objective- is maybe where most of the subjective evaluations are made by tribunals.

For instance, the *WA tribunal* finds that the changes introduced by the state were part of the exercise of the sovereign right of the state to regulate tariffs –in particular in the context of ´the solar boom´ (*WA v Czech Republic*, Final Award, 2019, para.576). The tribunal also stated that, with regard to the treaty obligation to maintain a stable and predictable legal framework, in the absence of an express stabilization commitment, changes to address the solar boom were within the state regulatory power (*WA*, Final Award (2019) para. 586. The *Voltaic* tribunal in the same sense asserted that "before the Claimant started its investment project, political and energy sector circles in the Czech Republic were aware that the then current Incentive Regime was problematic and, because of the solar boom, would become even more problematic with time" (*Voltaic v Czech Republic*, Final Award, 2019, para. 471). The context of the investment and the political situation are also considered by tribunals to assess the existence of a legitimate expectation. *Blusun* Tribunal asserted that the expectations were even less powerful since it was clear that the incentives offered were subject to modification, considering changing costs and improved technology (*Blusun v Italy,* Final Award, 2016, para. 371). *Charanne*

tribunal, in the same line of thinking, asserted that the investor could have easily foreseen possible adjustments to the regulatory framework as the law of the host-state clearly left open the possibility that the system of compensation applicable to photovoltaics could be changed (Charanne, Final Award, 2016, para. 505).

As emerges from the above exposition, the consideration of socio-economic circumstances of the host-state contribute to shape the content of legitimate expectations.

Finally, another element that has been evaluated repeatedly by tribunals in the cases under study is the 'reasonableness' of the investor expectations at the light of its conduct.

It has been recognized that expectations required to be analysed *in concreto* in order to determine whether the investor has acted with due diligence and thus can be said to hold the expectations in the specific circumstances. For instance, *Masdar* tribunal asserted that if general legislation is alleged as the source of an investor's legitimate expectations, such investor must demonstrate it has exercised appropriate due diligence, and it is familiarised with the existing laws (*Masdar*, Final Award, 2018, para. 494).

The rationale behind the tribunals' assessment is in the idea that not all risks an investment may face deserve protection under international investment law. For instance, the investor is not protected from the ordinary business risk that any investment implies. Thus, the investor must make the investment decision based on a risk assessment, examining all potential complications in the investment project, and the political and economic situations in particular. In this sense, it is argued that, since the FET standard represents a certain assurance to the investor, it does not play the role of insurance policy, and thus it cannot protect the investor from all the risks that its investment may face (Dolzer, 2012, p.1).

4. Renewable Energy Disputes and State's Right to Regulate

4.1. Conflict between the investor's legitimate expectation vs states' right to regulate

According to the ECT, it is unquestionable that host-states have a duty to encourage and create stable, equitable, favourable and transparent conditions for investors. However, it was repeatedly asserted in the awards that the article of the treaty in which the stability duty is contained does not constitute *per se* a stabilization clause (*AES v. The Republic of Hungary*, ICSID Case No. ARB/07/22, Final Award, 23/09/2010, para. 9.3.29). Thus, states are entitled to amend their regulatory framework -which is normally subject to change- to adapt it to new circumstances that may appear (*AES v. The Republic of Hungary*, ICSID Case No. ARB/07/22, Final Award, 23/09/2010, para. 9.3.29). The right to make modifications in the domestic legislation is been widely recognized as a key element of the sovereign rights of the states (Yaw, 2002, p.21). That is why some tribunals have asserted that the FET-standard imposes the obligation to implement regulatory changes in a way (*Blusun v Italy*, 2016, Final Award, para. 319.4). Consequently, a balance is required between state's rights to regulate and the obligation of the state to provide FET to the foreign investor (Kudrat, 2018, p.87). After reviewing the awards in the cases under study, either the arguments alleged by states or investors seem to be valid. It was

pointed out that the question on how to balance the interests between both rights depends on the arbitrators' discretion (Jaunius Gumbis & Rapolas Kasparavicius, 2017, p.5). The diverse methods adopted to ´find a balance´ between both conflicting rights have been the principal reason for different decisions (Rivkin, 2015, p.130).

Different approaches to resolve this conflict have been adopted in case-law. One of these consists of the analysis of the circumstances that surround the decision of the investor to make the investment. Another consist of the analysis of whether there was a public interest behind the measure adopted by the state (*see AES* Final Award , 2010). Through these approaches the tribunals attempted to put itself in the position of both parties in the conflict before making a decision. These approaches find their origins in the *proportionality* and the *sole effects doctrine* (Gumbis, 2017, p.153).

The *sole effect doctrine* assumes that the host-state has a compensation obligation to the foreign investor if its actions significantly damage the economic value of the investor's assets (Gumbis, 2017, p.153). It is being argued that this doctrine does not restrict the sovereign rights of the state (Gumbis, 2017, p.153). This is because in case of breach by the state of its international undertakings, the remedy is not an order to cease from exercising sovereign powers, but to pay the investor a compensation for the damage caused (Gumbis, 2017, p.153)).

The *proportionality doctrine* obstructs the state's liability if it is proved that the adopted measures -in these cases the regulatory changes- were adopted in a proportional manner, considering the investors´ expectations (Gumbis, 2017, p.153). This doctrine is based on a risk that the *sole effects doctrine* creates by discouraging states from taking an action when there is a need to protect the public interest. According to this doctrine, if regulatory changes adopted by states are reasonable and proportional in light of the circumstances, the investor has to accept the negative impact on its investment without receiving a compensation. Accordingly, the ECT provides that the treaty does not prevent any contracting party from taking any measure considered necessary for the maintenance of public order (*see* Article 24.3(c) of the ECT). This provision gave the perfect argument to states to allege the existence of a public interest behind the adopted measures and thus break the causal link between them and the alleged damage. However, according to some authors, the increase in the electricity price does not destabilise the public order and thus falls outside the scope of an exception provision, such as the one contained in ECT art 24(3)(c) (Reuter, 2015, p.12). Correspondingly, it was pointed out that the responsibility for the risk of an excessive cost on energy consumers lies in the scope of the host-state legislator rather than in the foreign investor (Reuter, 2015, p.12).

The arbitral tribunal may at its discretion apply one doctrine or the other to balance states and investors interests in the specific circumstances. If the proportionality doctrine is chosen, the threshold for the investor would be high as it has to prove that the states' measures were not proportional in light of the circumstances given. It has been pointed out that the standard of FET contains an element of proportionality (Scheu, 2017, p.449). The *proportionality test* consists of three elements: suitability, necessity, and proportionality *stricto sense* (Scheu, 2017, p.449). This three step analysis assumes that the state is acting for the promotion of a public interest. Consequently, before analysing whether a host state measure can be characterized as proportional, it must be first established that the host state has taken the action to pursue a legitimate purpose (Scheu, (2017) p.449).

Another approach used in the cases under study is the *doctrine of margin of appreciation,* which origins lie in the European Court of Human Rights (ECHR) (Spielmann, 2012, p.381). The margin of appreciation is a tool used by the ECHR in it assessments of those provisions of the European Convention on Human Rights (ECOHR) and its Protocols that require balancing with other rights, or need to be weighed against other aspects of the public interest (Frantziou, 2019). Regarding this doctrine, it considers that national authorities were better placed to determine whether measures implemented were in the public interest because of their "direct knowledge of their society and its needs" (Frantziou, 2019, p.1). It has been noted that this doctrine is one of the forms in which the principle of proportionality appears (Henckels, 2015, p.1). Notwithstanding the above, in some dissenting opinion it's been argued that the application of a margin of appreciation to a state´s FET under investment treaties is not a generally accepted principle of international law. Asserting that outside the ECHR there is no place for its application (*Antaris,* Dissenting Opinion of Gary Born, para. 47-48).

The principle of proportionality was adopted by most of tribunals to ground their decisions on the cases under analysis. For instance, in *Charanne*, the tribunal asserted that the proportionality of the measures is fulfilled as the modifications to the legal framework are not capricious or unnecessary and do not abruptly and unforeseeable eliminate the vital characteristics of the existing legal framework (Charanne, Final Award, 2016, para. 517). Moreover, the investor's condition of expert in the energy market is used as an argument to justify that it should have foreseen the legislation changes. *Charanne* tribunal considered that regulatory changes were not disproportionate since they did not modify the basic benefits of the investor (*Charanne*, Final Award, 2016, para. 517).

In *Eiser* the Tribunal emphasized the idea that Spain introduced a completely new regulatory regime, which deprived claimants from all the value of their investment, in a disproportionate manner. Furthermore, it was highlighted that the measures adopted by the state in order to be justified require a rational public policy aim and a rational act of the state in relation to that policy (*Eiser v Spain*, Final Award, 2018, para. 418). The impact of the measure on the investor should be proportional to the policy objective sought. It is noted that the test of proportionality ´requires the measure to be suitable to achieve a legitimate policy objective, necessary for that objective, and not excessive considering the relative weight of each interest involved´ (Electrabel S.A. v. Republic of Hungary, ICSID Case No. ARB/07/19, Final Award, 25/11/2015, para.179).

Moreover, a new approach involving CC has appeared in literature to complement the way in which tribunals are addressing the balance of rights phenomenon. Although it was not considered by tribunals in the reviewed awards, its rapid growth in literature indicates that it probably would be alleged by the parties in future disputes. The idea behind this approach is that investor-state arbitration may became a threat to the aim of combating climate change, as it may encourage the states not to take CC measures to avoid the risk of high value claims as a consequence of eventual adverse decisions. Supporters state that tribunals should take into consideration the interaction between investment arbitration and CC, since its decisions and arguments may have an impact on CC (Restrepo, 2017, p.101). Thus, it is noted that, to a certain degree, tribunals make CC law decisions (Restrepo, 2017, p.101). Supporters argue that the *sole effect doctrine* must be considered by tribunals by means of adopting a wide interpretation of representations;

less harmful measures standard, and an analysis of proportionality in the context of climate change. Consequently, the balancing test must give a proper weight to the CC interest grounded on the global intention to lower GHG emissions and the international instruments supporting this aim (Restrepo, 2017, p.101).

Another approach followed consist of limiting the existence of legitimate expectations to stability contracts or other explicit representations. It has the advantage of creating a certainty framework. Either the state creates legitimate expectation by providing clear, specific, direct assurances –as it happens in the case of stabilisation clauses- or it does not. However, this approach is clearly favourable for the state interests in detriment of investors, as frequently states refuse to include this type of clauses in their agreements (Cameron, 2010, p.1). Nevertheless, in cases in which stabilization clauses are present, the will of the states should not be unknown, being the specific commitment a limit to its regulatory powers. In this line, *Blusun* tribunal asserted that that FET standard conserves the state right to change its laws to adapt to the changing circumstances, but subject to respect the specific commitments made (*Blusun v Italy*, 2016, Final Award, para. 319.4).

Perhaps the most novel approach regarding the balance between investors' expectations and state´s rights to regulate appeared in some recent BITs. The Morocco-Nigeria treaty which entered into force in 2016 is an example of this (Nigeria-Morocco BIT). It contains a provision in its Article 23, called ´Right of State to Regulate´, which recognizes the right of the states to take regulatory or other measures to ensure that development in its territory is consistent with the goals and principles of sustainable development. It also recognizes some limits to the regulatory powers of the state referring to the balancing test in this terms: "the rights to regulate shall be understood as embodied within a balance of the rights and obligations of Investors and Investments and Host States, as set out in the Agreement". This BIT is in line with recommendations by the UNCTAD, which called for the inclusion in investment treaties for the protection of the environment (*See* the Road Map for International Investment Agreement Reform: available in; https://unctad.org/en/PublicationsLibrary/diaepcbinf2019d6_en.pdf, accessed 17/08/2019).

4.2. Role of Stabilization Clauses in Renewable Energy Disputes

One of the main features of energy agreements is that they are long-term contracts. This is what makes these contracts vulnerable to political risk. As was noted, the occurrence of significant changes in the law during the life of a project is almost unavoidable. To mitigate that risk, the common practice is the use of contract drafting as a mean of achieving the aim of stability through the stabilization clauses (Mistelis, 2018, p.1). As was quite rightly asserted, lawyers pretend to ´Play God´ with contract drafting under the illusion that the draftsman can draft away all the vagaries of the future (*Waelde*, 1996, p.215). The principal aim of these clauses is to preclude the application to an agreement of any subsequent legislative or administrative act issued by the state which modify the investor situation (Kuyper, 1995, p.1)

Although generally states do not accept the inclusion of this type of clause in their agreements, sometimes they are used as a mechanism to attract investment. In addition, as several renewable energy developments are built under project finance structures the inclusion of this clause in agreements is sometimes a requirement established by

the financial institutions to granting credit (Lee, 2013, p.1). It has been pointed out that "the more stability there is at the treaty level, the less stability is arguably needed at the contractual level" (Lee, 2013, p.1). However, this assertion is not always true. In the scope of the ECT the stability is generally accepted. Nevertheless, in absence of a stabilization clause, some tribunals have been reluctant to accept the existence of a specific commitment of the state possible to create a legitimate expectation in the investor that the legal framework would not be modified.

In this sense, *Charanne* Tribunal recognized that a specific commitment of the state in the form of a stabilization clause is possible to create legitimate expectations (*Charanne* Final Award, 2016, para. 489-490). Likewise, *Antaris* Tribunal recognized the state power to modify the legislation asserting that ´at least in the absence of a stabilization clause´ is not prevented to implement regulatory changes (Antaris, Final Award, 2018, para. 360.7).

The tribunal in *Masdar* concluded that "on the basis of the due diligence exercised by the investor, it had a legitimate expectation that the laws would not be modified, as they included stabilisation clauses" (Masdar Final Award, 2018, para. 499).

In conclusion, from the reviewed Awards follows that tribunals recognized the existence of legitimate expectations because of a stabilization clause.

5. Conclusion

Based on the reviewed awards it is possible to conclude that investors are entitled to receive compensation under the FET provision of the ETC -in the scenario of implementation of regulatory changes in its detriment- if a legitimate expectation is violated. However, the diverse ways in which the concept of legitimate expectation is being interpreted by tribunals and the different approaches regarding how to balance investor´s expectations and state´s sovereign right to regulate are the principal cause for divergent awards in similar situations.

Thus, the lack of consistency in case-law regarding this matter is, therefore, a fact. Similar scenarios have resolved either in favour or against the state. Although in theory there is no precedent in Investor State Dispute Settlement, the common practice by the tribunals is using prior awards to ground their decisions. Decide a dispute considering as the main tool the determination of a previous tribunal seems to close the door to the evolution of the FET standard. Regarding this, international investment agreements have evolved, including a more detailed concept of the FET standard, comprising in some cases expressly references to the legitimate expectations.

The ECT requires to evolve urgently in the same direction. The Treaty does not contain a clear definition of the FET-standard and it does not mention the legitimate expectations rule. As a tool to mitigate the lack of consistency, a clear definition of the standard must be included in the text of the treaty. The way how the standard was recently defined in some BITs and the criteria set to balance public and private interest may be a benchmark for the drafters of the new Treaty.

Besides, considering the role the evidence has in the resolution of these cases, it is important for the investors to carry a due diligence prior to the decision of investing. Similarly, the inclusion of stabilization clauses in energy agreements is suggested at the light of the determinations made by tribunals in the cases.

Finally, the cases reviewed open a new discussion, which must be assessed the next years, about the impact these awards may have in the Energy Transition. Although some concerns have been expressed about an eventual *regulatory chill*, nowadays there is no evidence of its occurrence. Nonetheless, and due to the increasing number of awards decided against the states, if it happens it would not be surprising.

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El autor es responsable intelectual de la totalidad (100 %) de la investigación que fundamenta este estudio.

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