

CEPS COMMENTARY



Thinking ahead for Europe

Why the future of European renewables policy may be decided in Washington and not in Brussels

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In the last few years, several EU member states have reduced support to renewable energy, leading to numerous claims that these policy changes retroactively affected existing investments and that the practice of ‘grandfathering’ should have been observed. Among these, the case of Spain stands out, both due to the material size of the cuts and the large volume of investments affected, although the Czech Republic, Bulgaria, Poland, Romania and Italy have also introduced reforms with deleterious consequences to their renewable energy sectors.

As a result, investors have taken action in national courts and international arbitration tribunals. Claiming that national schemes under the renewables Directive (2009/28/EC) created an expectation that support schemes for existing investments would not be changed, investors are challenging the retroactive nature of these reforms. In Spain, for example, hundreds of cases brought before the Supreme Court by investors are presently being heard. With regard to the 2014 legislative changes, in June 2016, the Court ruled against the investors in its first three decisions.¹ In April 2016, there was a ruling in favour of claimants with solar PV investments, but it was only in relation to the 2012 introduction of a moratorium for feed-

¹ In Spain, the Supreme Court judged the cut of almost €1,700 million to the renewables sector by the government consistent with the Constitution. See R. Rincón, “El Supremo avala el recorte de 1.700 millones de Rajoy a las renovables, El País, 1 June 2016 (economia.elpais.com/economia/2016/06/01/actualidad/1464802624_717002.html). The Court reached this judgement by a narrow margin of four out of seven magistrates, showing how legally divisive this issue is in Spain. Two of the magistrates issued a statement declaring that in their view the reforms have impacts equivalent to retroactive changes de facto, even if not strictly in legal terms. One magistrate stated that while the sentence is not in favour of the investors, the reforms may be incompatible with the principles of ‘legal certainty’ and ‘legitimate trust’. See APPA (2016), “APPA recurrirá las sentencias del Tribunal Supremo sobre el recorte a las energías renovables”, Press Release, 3 June 2016 (www.appa.es/descargas/APPA_SENTENCIAS_SUPREMO_20160603_VF.pdf).



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in-tariffs for new installations, and thus was not related to the core issue of ‘retroactivity’.² International investors have claimed that Spanish courts do not “provide effective channels for defending their rights, in violation of Article 10(12)ECT”.³ Beyond Spain, investors elsewhere have complained that the judicial systems of other member states are also not meeting the expected standards – by the admission of the European Commission – for example, in Bulgaria and Romania.⁴

As a consequence, investors have turned to international arbitration courts. Complaints have been brought before the International Court of Arbitration in Washington, D.C., the Stockholm Chamber of Commerce (SCC) and ad-hoc tribunals convened by UNCITRAL (United Nations Commission on International Trade Law), under the mechanism established in Art. 26 of the Energy Charter Treaty (ECT). All EU member states (except Poland, and since last year, Italy⁵) are signatories to the ECT, which was set up to protect international investors in the energy sector, although the necessity to provide for intra-EU dispute settlement was not originally anticipated. Since 2011, 32 cases against Spain have been filed, seven against the Czech Republic and the rest against Italy, Romania and Bulgaria.⁶ In the case of Poland, the situation is particularly complex, first because of the indirect nature of some of the legal changes (not directly related to support schemes, but to building permit rules and the taxation system). In addition, Poland is not a member of the ECT, which prevents it from following the same steps as the other countries mentioned above.

The European Commission has challenged the legitimacy of these arbitration courts for intra-EU disputes. In the only decision available so far, however, the SCC rejected this claim and ruled that intra-EU claims are allowed under the ECT.⁷ Investors claim that there is an EU dimension to the dispute, as member states introduced support schemes in compliance with the renewables Directive.⁸ Investors argue that retroactive changes by member states are leading to the opposite outcome of what it intended to do: instead of boosting investors’ confidence to promote investment in the sector, changes are causing losses to existing investments and jeopardising future investments.

Notwithstanding this case, the first arbitration decision dismissed the investors’ claims. However, this case only addressed the reforms of 2010, which were limited to a portion of the

² The Court stated that the legislative changes have violated “the principle of legitimate expectations”. See K. Tom, “Spain Supreme Court ruling ‘oxygen’ for future solar cases”, pv-tech, 10 May 2016 (www.pv-tech.org/news/spain-supreme-court-ruling-oxygen-for-future-solar-cases).

³ Clifford Chance (2016), “Claim against Spain dismissed, in the first arbitration award regarding changes in the renewable energies remuneration scheme”, February 2016 (www.cliffordchance.com/briefings/2016/02/claim_against_spaindismissedinthefirs.html).

⁴ See reports under the Cooperation and Verification Mechanism (ec.europa.eu/cvm/progress_reports_en.htm).

⁵ Italy left the ECT in 2015, but ECT will still apply to legal changes carried out before Italy’s exit.

⁶ UNCTAD annual reports of investor state dispute settlement cases, (<http://investmentpolicyhub.unctad.org/Upload/ISDS%20Issues%20Note%202016.pdf>; http://unctad.org/en/PublicationsLibrary/webdiaepcb2015d2_en.pdf) and Energy Charter Treaty website (www.energycharter.org).

⁷ Namely, the renewable energy arbitration case against Spain, described in Clifford Chance (2016), op. cit.

⁸ The Directive states in its introductory clause, para. 25: “One important means to achieve the aim of this Directive is to guarantee the proper functioning of national support schemes (...) in order to maintain investor confidence and allow Member States to design effective national measures for target compliance.” In addition, a footnote in Annex I states: “In order to be able to achieve the national objectives set out in this Annex, it is underlined that the State aid guidelines for environmental protection recognise the continued need for national mechanisms”.

solar PV market and had limited impact. Other pending cases refer to the 2013 and 2014 changes, which had far deeper impacts and entailed a radical overhaul of the regulatory framework under which around €50 billion of investments had been made. In addition, the tribunal declared that amendments to support policies that harm investors could be in breach of the ECT if they are “irrational, disproportionate or contrary to public interest”.

Future cases will be all-determining. If the investors’ claims can be easily dismissed, it would send a signal that renewable energy investments are suddenly not ‘bankable’, because governments can change incentives, such as feed-in-tariffs at their whim.

Depending on the developments to come, the number of arbitration cases may increase. Given the present lack of an EU arbitration system, this would mean de facto determining the future of EU renewable energy policy from Washington or Stockholm.

Policy implications

Regardless of the outcome of these cases, the future of EU renewables policy is likely to be affected. If the courts rule in favour of the investors, member states will be even more cautious when designing support mechanisms, ensuring a tight control of costs and avoiding commitments. As a result, they may lower their ambitions in setting their own targets for 2030 – an upcoming task planned for 2018, as part of the ‘governance’ for the 2030 energy and climate framework.

If the courts rule against these cases, however, investors are likely to shy away from countries that lack a means of litigation and will only do business in those member states where a robust system with effective courts is in place. In either case, investment in renewables will be drawn away from countries whose politicians are unable to convey genuine support for renewable energy. Investments will persist in member states with stable, functioning policies and unambiguous long-term commitments. Having refrained from making damaging or retroactive changes to policy, Austria, Denmark, Germany, Ireland, the UK and Portugal are positive examples of countries on track to achieve and even exceed their targets for 2020, while openly committing to lasting renewable energy support.

It is therefore time for the European Commission to explore ways to re-establish investor confidence. The most obvious solution would be to launch an EU-wide arbitration procedure. Whether this will be feasible is uncertain. Other possibilities exist. An option, but one that cannot address the existing disputes, would be to integrate provisions in the Directive that are de facto similar to the ECT requirements to protect investments. While the Directive gives member states the right to provide state aids to the renewable sector as a way to reach stated targets for 2020 and 2030, it fails to set some rules on the stability of the schemes. It would be advisable to introduce a principle of legal certainty and rationality.

In addition, projects supported by guarantees of the European Investment Bank (EIB) could include partial protection from policy risks in the event that a project becomes non-viable. But such protection would leave all investors that are not supported by EIB funds out in the cold, which is rather unsatisfactory. For EU grants, such as the structural funds, it is difficult to link them to any policy guarantee. However, the EU has a duty to protect its financial interests and may consider the merits of introducing a penalty clause. This clause would require the member states to compensate the European Commission if projects financed by the EU budget fail, due to national policy reforms that unduly damage the viability of such projects. There may be a case for the EU to take action under the present rules, as it is highly probable that many projects co-financed by the EU have been affected by the reforms. The changes have likely led projects funded by the EU into insolvency (which means that EU funding has been wasted) and/or have led regional programmes to fail in meeting their targets. The nature of

the problem is unprecedented and further analysis is needed in order to ascertain how far this can lead to a recovery of EU funding or to reductions in regional aid, following the review this year of the implementation of EU structural funds.

None of the solutions presented can substitute for an arbitration court, but they could address investors' confidence to a certain extent. There is an additional reason for putting forward an EU arbitration process. It would complement the Investor-State Dispute Settlement (ISDS), which is currently a point of contention in discussions over the Transatlantic Trade and Investment Partnership (TTIP) and the Comprehensive Economic and Trade Agreement (CETA) with Canada.