INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES

In the arbitration proceeding between

OPERAFUND ECO-INVEST SICAV PLC and SCHWAB HOLDING AG

Claimants

and

KINGDOM OF SPAIN

Respondent

(ICSID Case No. ARB/15/36)

DISSENT ON LIABILITY AND QUANTUM

PROFESSOR PHILIPPE SANDS QC

1. I support the conclusion that the Tribunal has jurisdiction over large parts of the claims brought by OperaFund and Schwab, including the dismissal of the Respondent's intra-EU jurisdictional objection (Award, paras. 378-388). I agree too that the Tribunal does not have jurisdiction with respect to the Tax on the Value of the Production of Electrical Energy (TVPEE) (Award, paras. 402-405).

2. I regret, however, that I am not able to support the conclusion of the Majority on liability and quantum, to the effect that Spain has violated Article 10 of the Energy Charter Treaty (ECT)

(Award, paras. 480-490, 508-513). This conclusion, with the consequences that are said to follow in relation to other findings and the assessment in relation to quantum of damages (Award, paras. 682-688), is premised on certain findings of fact by the Majority, namely that the Claimants:

(i) had an expectation that the tariff regime established by RD 661/2007 was immutable during the reasonable life of their investments,

(ii) relied on that expectation in making their investments, and

(iii) carried out the necessary exercise in due diligence required by the Energy Charter Treaty.

As set out below, these findings of fact are entirely unsupported by evidence on the record, and reached without reasoning or explanation. Accordingly, I dissent from the finding of a violation of Article 10, on the basis of the record before the Tribunal in this case. I regret, further, that the Majority has failed to set out a legal standard applicable to its conclusion on legitimate expectations, and provided no explanation or reasons on a number of important points, not least the substitution of its views on Spanish law for those adopted by the Spanish Supreme Court on the meaning and effect of RD 661/2007.

3. It is telling that the Majority devotes just a page of a 273-page Award to this central issue, and offers no real response to the points raised in this dissent (see Award, para. 491). The system of investor-State arbitration is a fragile creature, and one that attracts an increasingly critical eye. This Award – long on description of the Parties' arguments, short on scrutiny of the actual evidentiary record and reasoning as to the legal principles to be applied – will not enhance confidence in the system, or a sense of its legitimacy.

FACTS

4. This case was brought by two Claimants, OperaFund Eco-Invest SICAV PLC (*OperaFund*), existing under the laws of the Republic of Malta, and Schwab Holding AG (*Schwab*),

established under the laws of the Swiss Confederation. They made their investments in Spain in July 2008 and April 2009 respectively, in the renewable energy sector.[1]

5. They did so in the context of global, regional and national efforts to address human-induced climate change, aimed at the reduction of emissions of carbon dioxide from the energy sector. Against the background of the 1992 UN Framework Convention on Climate Change (UNFCCC) and the 1997 Kyoto Protocol to the UNFCCC, the European Union adopted legislation committing Member States, including Spain, to reduce greenhouse gas emissions. The legislation included measures to encourage the use of renewable and other new technologies.

6. In November 1997 the European Commission published a White Paper on renewable energy, which set out a strategy and action plan to increase the share of renewables in the EU, to reach 12% of energy consumption.[2] An EU Directive subsequently required EU Member States, including Spain, to set indicative national targets for electricity produced from renewable resources, in line with "the global indicative target of 12% of gross national energy consumption by 2010 and in particular with the 22.1% indicative share of electricity produced from renewably energy sources in total Community electricity consumption by 2010."[3] New targets were set in January 2007, aimed at further cuts in greenhouse gas emissions, improved energy efficiency, and at least a 20% share of energy consumption from renewables, all by 2020.[4]

7. Spain adopted national rules to implement these EU requirements. In 1997 it passed legislation to achieve the goal that 12% of energy consumption should be from renewables by 2010,[5] and introduced a "special regime" to remunerate qualifying renewable energy producers. Royal

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[1] Award, paras. 2 & 173.
[2] *Energy for the Future: Renewable Sources of Energy – White Paper for a Community Strategy and Action Plan*, COM(97)599 final (26/11/1997).
[3] Directive 2001/77/EC, on the promotion of electricity produced from renewable energy sources in the internal electricity market, Article 3(4).
[4] These targets were enacted in EU Directive 2009/28/EC, which replaced the 2001 Directive. See Article 3(1).
[5] Act 54/1997 on the Electricity Sector, R-0059.

Decree (RD) 2818/1998 established a remuneration regime for the generation of electricity from renewables introducing a feed-in tariff for energy generated.[6]

8. Six years later, RD 2818/1998 was replaced by RD 436/2004, to amend the previous system of subsidies, prices, incentives and methodology.[7] Three years later, in 2007, RD 661/2007 was adopted, to replace RD 436/2004 with a different set of rules on tariffs.[8] Within two years, amendments were then made to RD 661/2007, following the adoption of EU Directive 2009/28/EC. These were introduced, in part, to address a tariff deficit that had occurred as a result of the global financial crisis that took root in 2007, as well as the availability of new technologies.[9] In 2010, Spain introduced further amendments to RD 661/2007, including reward limits on the quantity of electricity produced by photovoltaic plants and new tariff levels,[10] and on the number of hours of operation,[11] and seeking to avoid over-remuneration of existing investors.[12] In 2014 a new energy regulation was adopted, entirely replacing the tariffs set in RD 661/2007.[13]

9. Between 1994, when Spain first legislated to promote the use of renewable energy, and 2009, when both Claimants had made their first investment, the regulatory framework was changed on multiple occasions.[14] The changes were prompted by a range of factors, including the desire

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[6] RD 2818/1998, of 23 December, on the production of electrical energy by facilities supplies with renewable energy, waste or cogeneration resources or sources, R-0067.

[7] RD 436/2004, dated 12 March, establishing the methodology for the updating and systematisation of the legal and economic regime for electric energy production in the special regime, R-0069.

[8] RD 661/2007, of 25 May, regulating the activity of electricity production under the special regime and the production of certain facilities with similar technologies under the ordinary regime, R-0071.

[9] RD-L 6/2009, of 30 April, adopting certain measures in the energy sector and approving the social tariff, R-0057.

[10] RD 1565/2010, of 19 November, which regulates and modifies certain aspects of the electricity production activities in the Special Regime, R-0074.

[11] RD 1614/2010, of 7 December, regulating and modifying certain aspects related to electric energy production using thermoelectric solar and wind power technologies, R-0075.

[12] RD-L 14/2010, of 23 December, establishing urgent measures to correct the tariff deficit in the electricity industry, R-0058.

[13] RD 413/2014, of 6 June, which regulates the electricity production activity from renewable energy sources, cogeneration and waste, R-0080.

[14] Most of the sixteen items of legislation or regulation here listed were taken from the legal opinions the Claimants provided to the Tribunal, with an indication in italics of those that explicitly referred to changes. This list is not intended to be exhaustive, but to provide an overview of the legislative changes in that period:

1. RD 2366/1994, on the Production of Electrical Energy;
2. Act 40/1994, on the Organization of the National Electric System;
3. Act 54/1997, on the Electric Sector;
4. RD 2019/1997, organising and regulating the electric energy production market;
5. Ministerial Order, dated December 17, 1998, *modifying* the Order dated December 29, 1997, *developing* certain aspects of RD 2019/1997, organising and regulating the electric energy production market;

to increase standards of environmental protection, make use of new and cheaper technologies, and reduce costs and budget deficits in the face of an unprecedented global financial crisis that began in the spring of 2008 and caused a contraction in Spain's economy of -3.6% in the GDP between 2008 and 2010.[15]

10. This was the background against which the Claimants invested in two photovoltaic renewable energy projects, one in Majorca (the PASO Palma Sol Project), the other in Badajoz (the ECO 3 Project). The investments were made in the form of shares in special purpose vehicles (SPVs), which owned the PV installations in Spain, and participative loans granted to the SPVs. Both projects were developed in 2004, sponsored in part by Deutsche Bank, which subsequently provided loan finance to OperaFund and Schwab. Deutsche Bank lent €57.71 million to Paso Palma Sol (in which OperaFund held a 75% stake, and Schwab a 25% stake). For ECO 3, HSH Nordbank agreed to lent up to €66.95 million (OperaFund acquired a 100% equity stake in ECO 3 with third-party financing loans).[16] For the Majorca Project, the funds provided by Deutsche Bank were granted as a loan facility with a repayment period of 22 years; for the Badajoz Project the repayment period was between 19-20 years, depending on the final amount.[17]

11. The Claimants' case is that they invested on the basis of an expectation that the tariff regime established by RD 661/2007 – which would *inter alia* give them a rate of return of 7.8% after

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6. RD 1663/2000, on connection of photovoltaic facilities to the low voltage network;
7. RD 842/2002, *approving* the technical electric regulation for low voltage;
8. RD 1432/2002, establishing the method for approving or modifying the average or reference electricity tariff;
9. RD 436/2004, *establishing the method for updating and systematising the economic and legal framework* for the production of electric energy under the special regime;
10. RD 1454/2005, *modifying* certain dispositions related to the electric sector;
11. RD 1556/2005, *establishing* the electric tariff for 2006;
12. RD-Law 7/2006, *adopting urgent measures* in the energy sector;
13. RD 809/2006, which *revises* the electric tariff as of July 1, 2006;
14. RD 661/2007, by which the electricity production activity under the special regime is regulated;
15. Act 17/2007, which *adapts* Act 54/1997, on the electric sector to European Directive EC/2003/54, of the European Parliament and the Council, on common rules for the internal market; and
16. RD 1110/2007, approving the unified regulation on the power system measurement points.

[15] These numbers are based on GDP growth data provided by the IMF. In 2009, Spain's GDP decreased by 3.6%. In 2010 no changes were registered and there were further contractions in 2011, 2012 and 2013 of 1%, 2.9% and 1.7% respectively.

[16] Brattle Quantum Report, CER-2, paras. 26-30.

[17] Claimants' Memorial on the Merits, para. 200; Common Terms of Agreement, 28 January 2009, C-0060; Facilities Agreement, 2 July 2008 C-0061.

tax – was immutable in relation to their investments, and that Spain subsequently altered the legal framework in such a manner as to frustrate that expectation by lowering the rate of return.

LAW

12. The Claimants' case is based on the interpretation and application of Article 10(1) ECT, on the promotion, protection and treatment of investments. This provides, in relevant part, that Spain was required to "encourage and create stable, equitable, favourable and transparent conditions for Investors of other Contracting Parties to make Investments in its Area", and that such conditions included "a commitment to accord at all times to Investments of Investors of other Contracting Parties fair and equitable treatment."

13. The Majority concludes, at paragraphs 480 to 490 and paragraphs 508 to 513 of the Award, that the Respondent's regulatory changes made after 2008 violated Article 10, by infringing the Claimants' rights under the fair and equitable treatment (FET) standard. The Majority's finding is premised exclusively on an interpretation of Article 44(3) of RD 661/2007, to the effect that its terms gave rise to a legitimate expectation on the part of the Claimants that their investment would not be subject to regulatory change of the kind that later occurred (Award, para. 483-485). The Majority states that "it is hard to imagine a more explicit stabilisation assurance than the one mentioned in Art. 44(3)" (Award, para. 485). It finds that it "does not see a lack of due diligence by the Claimants" in relation to RD 661/2007 and its Article 44(3) (Award, para. 487).

14. On the basis of the law, the facts and the submissions on the record before the Tribunal, I consider these conclusions to be without foundation.[18]

15. In determining the principles to be applied to "legitimate expectations" as part of the FET standard in Article 10 ECT, and whether it has been breached, the Parties made submissions on a great number of arbitral awards. In reaching its conclusion the Majority offers no

[18] This Dissent is based on the record in these proceedings and is limited to this Award. It expresses no view on other cases on which the evidentiary record may have been different.

substantive assessment of that case-law, and no reasoning on the legal standard it has identified and then applied in reaching its conclusions.

16. A starting point on the applicable legal standard is the proposition, which is reflected in the case-law, that a breach of the FET standard may be occasioned where legal and business stability, or the legal framework, has been altered in such a way as to frustrate legitimate and reasonable expectations or guarantees of stability.[19] Correct as it may be, the proposition does not of itself offer the principles that fall to be applied in determining the source and scope of the Claimants' expectation, or the requirement that falls on an investor to establish that its expectation is based on some degree of due diligence.

Expectation: its scope and source

17. What precisely is the expectation alleged by the Claimants, and what is its scope? The Claimants do not claim a contractual basis for their supposed expectation. Rather, their argument is that a legitimate expectation arose from "specific guarantees in legislation", namely Article 44(3) of RD 661/2007. The Majority treats the expectation as being derived exclusively from a general legislative act, a source of "general application" (para. 485). The proposition that an investor's expectation could be based on a specific guarantee in legislation is not of itself problematic.[20] The problem is what Article 44(3) says and does not say.

18. Article 44(3) of RD 661/2007 provides that "*The revisions of the regulated tariff and the upper and lower limits indicated in this section shall not affect facilities for which the commissioning certificate had been granted prior to January 1 of the second year following the year in which the revision had been performed.*" The Majority concludes that the Claimants' investments

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[19] Award, para. 510. See also *Tecnicas Medioambientales Tecmed SA v United Mexican States* (Grigera Naón, Fernandez Rozas, Bernal Verea), 29 May 2003, para. 154; *Duke Energy Electroquil Partners v Republic of Ecuador* (Kaufmann-Kohler, Gomez Pinzon, van den Berg), 18 August 2008, para. 340; *Bayindir v. Pakistan* (Kaufmann-Kohler, Berman, Böckstiegel), 27 August 2009, para. 179; *Electrabel SA v Hungary* (Veeder, Kaufmann-Kohler, Stern), 30 November 2012, para. 7.74; *El Paso v Argentina* (Caflisch, Bernardini, Stern), 31 October 2011, para. 348; *Philip Morris Brands SÀRL v Uruguay* (Bernardini, Born, Crawford), 8 July 2016, para. 320.

[20] *Enron Corporation v Argentina* (Orrego Vicuña, van den Berg, Tschanz), 22 May 2007, paras. 264-6. The point is also made in the award of *Antaris v Czech Republic* (Lord Collins, Born, Tomka), 2 May 2018, at paragraph 360 (Principle 4), but since that Award was not cited by either party, and since para. 360 purports to do no more than summarise the findings of earlier Awards, I place no reliance upon it in reaching my conclusions.

were made, between July 2008 and July 2009, in reliance on an expectation that they would, for decades, receive the economic rights provided by RD 661/2007, and that pursuant to its Article 44(3) those economics rights would "not [be] subject to regulatory change" (Award, para. 484). The Majority describes Article 44(3) as an "explicit stabilisation assurance" (para. 485). But is it?

19. Article 44(3) provides in terms that so long as RD 661/2007 remains in force, without amendment, the Claimants' returns would be based on that provision. In that limited sense, at least, Article 44(3) provides some degree of stability: so long as Article 44(3) and RD 661/2007 applied, the Claimants were entitled to receive the economic rights provided by the regulated tariff in accordance with that legislation. That, however, is not the end of the matter, since RD 661/2007, as a general legislative act, could in principle be amended or replaced. RD 661/2007 does not state in terms, or otherwise, that Article 44(3) could not be changed, or that it would not be changed, or that pre-existing rights would be grandfathered if the provision was repealed and replaced. Could Article 44(3) be amended or replaced? Could RD 661/2007 be repealed and replaced by a new Royal Decree, providing for a different tariff regime? Those questions are not addressed by RD 661/2007 itself. Moreover, the Majority has cited to no source or authority to support the proposition that Spain could not change the law, or that it ever said that Article 44(3) or RD 661/2007 could not be changed, or would not be changed. The Majority has read an immutability into the text of Article 44(3) that is simply not there. It has done so without reasoning.

20. In this regard, context is important. A reasonable and diligent investor would have been aware that the legal regime <u>had</u> recently changed, that earlier Royal Decrees had been changed: RD 661/2007 replaced RD 436/2004, which itself replaced RD 2818/1998. One might have thought that the regularity with which Royal Decrees were adopted and then replaced might cause a reasonable and diligent investor to take some steps to inform itself as to the risk of future changes. Indeed, the majority recognises, belatedly and in contradiction with its own conclusion, that "[t]here is no dispute that the laws changed in the past and would change in the future" (para. 486), although it provides no view as to which change would be permissible, and which would not. Yet the evidence makes clear that no due diligence was carried out on that vital point, and the Majority has pointed to none.

21. Significantly, the Spanish courts had addressed the question of immutability of tariffs and related regimes, and done so before the Claimants invested. In March 2007, for example, the Spanish Supreme Court ruled that there is no vested right to receive a specific subsidy in the future, instead only recognising that the law provides for a reasonable rate of return on investments.[21] It gave further judgments to that effect on 3 December 2009 (ruling that RD 436/2004 did not provide for a freezing of the remuneration system, and modification of the system lay within the State's discretionary power);[22] on 19 June 2012 (ruling that an obligation to offer a reasonable rate of return did not imply the continuance of a premium for the entire life of the facility, and amendments and adjustments were plausible and may be required);[23] and on 25 June 2013 (ruling that the Government was not prevented from approving measures that altered the regime).[24] On 21 January 2016 the Supreme Court went even further: it rejected the claim that the regime provided by RD 661/2007 extended indefinitely so as to apply a tariff regime forever, or that changes to the rates would undermine principles of legal security or legitimate expectations of an investor.[25] The Majority passes in total silence on the substance of these judgments on Spanish law, taking refuge in the claim that they are of no relevance. In so doing, the Majority substitutes its interpretation of a Spanish Royal Decree – whether it provides an expectation – for that adopted by the Supreme Court, and it does so without explanation or reasoning.[26] If an international arbitral tribunal is going to rule that a highest national court has got its own national law wrong – and done so on multiple occasions – it must at the very least provide an explanation, setting out why its view of Article 44(3) is to be preferred. The failure of the Majority to do so is grave.

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[21] Respondent's Counter-Memorial on the Merits and Memorial on Jurisdiction, paras. 348 & 582; Respondent's Rejoinder on the Merits and Reply on Jurisdiction, para. 525; Claimants' Reply on the Merits, para. 198(iii); all discussing Judgment of the Supreme Court, 20 March 2007 (EDJ 2007/18059), R-0119; Judgment of the Supreme Court, 9 October 2007, R-0120. See also Article in CINCO DIAS: *"The Supreme Court allows retroactive change in premiums"* (22 April 2010), R-0210.

[22] Judgment of the Supreme Court, 3 December 2009 (EDJ 2009/307349), R-0121.

[23] Judgment of the Supreme Court, 19 June 2012 (EDJ 2012/124000), R-0127.

[24] Judgment of the Supreme Court, 25 June 2013 (EDJ 2013/127521), R-0131.

[25] Judgment of the Supreme Court, 21 January 2016 (appeal 627/2012), R-0135.

[26] The Majority's approach to the Supreme Court appears somewhat quixotic, citing one decision (with apparent approval) in relation to the issue of 'transparency' (para. 526), whilst retaining a regrettable silence on this aspect of the case, taking refuge in the supposed irrelevance of the judgment of the highest court in Spain (para. 492).

22. The Majority is silent too on the relevant ICSID case-law, not least the jurisprudence which makes clear that "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".[27] The Majority simply decides – *ex cathedra*, without reasoning – that the tariff regime of RD 661/2007 was immutable, that a provision of general application could not be replaced or changed so as to subject the Claimants' investments to a less favourable (yet still profitable) regime.

23. Unreasoned, the conclusion of the Majority on the interpretation of RD 661/2007 is apt to undermine the legitimacy of, and trust in, a system of investor-state arbitration which accords to international arbitrators a vital responsibility to exercise caution if they are going to substitute their views for those of a country's highest court. No doubt there are circumstances in which an international arbitral tribunal can tell a national court that it has got its own law wrong, but if it is going to follow that path it must provide full and complete reasons.

Due diligence

24. My conclusion on the interpretation of RD 661/2007 and its Article 44(3), which accords with the rulings of the Spanish Supreme Court, disposes of the matter. If RD 661/2007 did not provide for an immutable regime, there cannot be an expectation in this case that it did so. However, let us assume that the Spanish courts (and I) are wrong as to the proper interpretation of RD 661/2007 and Article 44(3), and that it did create an expectation that the tariff regime would not be changed in relation to the Claimants' investments. The ICSID authorities argued by the parties alone are not enough to get the Claimants home: the jurisprudence makes clear that the Claimants were required to demonstrate that they had engaged in a minimum exercise of due diligence to confirm their expectation had legs.

25. As noted above, the Majority asserts that it "does not see a lack of due diligence by the Claimants" (para. 487), but offers no reasoned explanation for that summary conclusion, and no reference to the abundance of evidence in the record to the contrary. It offers no indication

[27] *Philip Morris Brands SÀRL v Uruguay* (Bernardini, Born, Crawford), 8 July 2016, para. 426.

as to the principles it applied in determining the extent of a due diligence exercise, and is silent on the jurisprudence as to the extent of due diligence that is required by an investor who claims a legitimate expectation on the basis of a law of general application, such as RD 661/2007.

26. The arbitral tribunal in *Philip Morris Brands SÀRL v Uruguay* addressed the matter as follows: "[g]iven the State's regulatory powers, in order to rely on legitimate expectations the investor should inquire in advance regarding the prospects of a change in the regulatory framework in light of the then prevailing or reasonably to be expected changes in the economic and social conditions of the host State."[28]

27. The obligation to "inquire in advance" is not a high standard, yet the record before the Tribunal shows that it is not one that the Claimants have met. Indeed, the evidence before the Tribunal shows that the Claimants made no inquiry at all in advance of their investments as to the prospects of RD 661/2007, or its Article 44(3), being changed. This is despite the fact, as noted, that by the time OperaFund and Schwab made their investments (July 2008 and April 2009 respectively):

    (i) RD 661/2007 had been preceded by a multitude of changes in the previous decade (and at least one of those acts, RD 436/2004, had an analogous "stabilisation" clause to Article 44(3) of RD 661/2007),[29]
    (ii) the Spanish Supreme Court had ruled in March 2007 that a Royal Decree could be changed, and there could be no expectation that it would not be,
    (iii) EU rules were known to be evolving, and
    (iv) a global financial crisis was underway.

28. Against this background, one might have thought that a reasonable and diligent investor would turn its mind to the possibility of yet another change in the regulatory framework, given the "prevailing or reasonably to be expected changes in the economic and social conditions" in

[28] *Philip Morris*, para. 427.
[29] Article 40.3 of RD 436/2004 reads: "The tariffs, premiums, incentives and supplements resulting from any of the revisions referred to in this section shall apply only to the facilities that became operational after the date of entry into force referred to in the preceding paragraph, without retroactivity to previous tariffs and premiums." For further analysis, see Respondent's Counter-Memorial on the Merits and Memorial on Jurisdiction, paras. 511-515.

Spain in 2008 and 2009. Such an investor would seek to inform itself as to the extent of the risk, including the possibility that the tariff regime provided for by Article 44(3) might be changed. Given that the risk was regulatory – did RD 661/2007 and/or Article 44(3) set in stone the tariff regime – a reasonable and diligent investor might have been expected to make an inquiry with an expert in Spanish law, a Spanish lawyer or law firm, perhaps.

29. What did the Claimants do? Remarkably little, if anything, according to the evidentiary record. As confirmed in a post-hearing brief, the Claimants placed reliance on just two legal opinions. Both were offered by the Cuatrecasas law firm, and neither is helpful to the Claimants' case.[30]

30. The two Cuatrecasas' legal opinions on which OperaFund and Schwab are said to have placed exclusive and complete reliance are:

- a July 2006 report ("*Opinion in the interest of Deutsche Bank – Applicable structure for PV projects in Spain*"), which was issued before RD 661/2007 had even been contemplated;[31] and

- an October 2007 report ("*Opinion in the interest of Deutsche Bank – Applicable structure for PV projects in Spain*"), analysing the legal regime applicable to PASO and ECO 3, including certain aspects of RD 661/2007.[32]

31. The two legal opinions are notable for reasons that are not helpful to the Claimants. First, they were addressed not to OperaFund and Schwab but to Deutsche Bank, who financed the investments. Second, both opinions contain a disclaimer, to the effect that they were produced "for the exclusive use" of Deutsche Bank, and could not be used "by other persons" without the prior written permission of Cuatrecasas[33] (no such written permission was in evidence before the Tribunal). Third, and most significantly, the opinions say nothing about the risk of change to the regulatory framework of RD 661/2007. Section 11 of the first opinion is on "Risks concerning legal modifications", but it is concerned only with RD 436/2004 (and

[30] Schwab claimed that the Cuatrecasas' reports were confirmed to Claimants by another law firm as well as their project managers, but no documentary evidence was tendered in support of the contention. See: Transcript, Day 2, pg, 59, ln. 24 – pg. 60, ln. 17; pg. 66, ln. 2-11.
[31] *Opinion in the interest of DEUTSCHE BANK – Applicable structure for PV projects in Spain*, July 2006, C-0211.
[32] *Opinion in the interest of DEUTSCHE BANK – Applicable structure for PV projects in Spain,* C-0095.
[33] C-0211, p. 25 & C-0095, p. 26.

recognises a risk of change, which proved to be correct). The second opinion has no equivalent section, and is completely silent on risks of regulatory change to RD 661/2007; it expresses no opinion as to whether the framework set forth in RD 661/2007 could be relied upon for the life of the investments, or less, and makes no reference to Article 44(3), not even once. What the two Cuatrecasas' opinions do refer to is the fact of multiple prior changes, identifying no less than fourteen acts of legislation that have come and gone in the past decade.[34] A reasonable reader would conclude that what has happened before – regulatory change – could happen again, as it did.

32. This is the only evidence as to due diligence before the Tribunal, and the only evidence to which the Majority refers. Remarkably, the Majority asserts that "Claimants' reliance on a legal opinion by Cuatrecasas was also sufficient at least in confirming their expectations, because the Tribunal cannot see what other better means of information they could have obtained than that provided by what seems to have been the most competent law firm for these matters in Spain" (para. 487). It is astonishing that the Majority relies on the October 2007 Cuatrecasas' legal opinion as confirming the Claimants' "expectations" that they could rely on the tariff arrangements in RD 661/2007 without any risk of change. In that opinion Cuatrecasas offers no opinion on regulatory risks, does not mention Article 44(3), and says nothing to support the conclusion that the tariffs in force in 2008/9 were immutable for the Claimants. No other evidence on the record told the Claimants they could rely on the Article 44(3) regime for the life of their projects.

33. In the course of the hearing, witness testimony was given which confirmed that Deutsche Bank, the project sponsors and providers of loan finance to the Claimants, proceeded only on the basis of the regulatory framework set forth in RD 436/2004, which offered a less advantageous regime and rates of return, not RD 661/2007. Mr Bauermeister formerly a project manager with Deutsche Bank and now an executive board member of DeanSolar, involved in the technical and commercial management of PASO and ECO 3, who appeared as a fact witness for the Claimants, repeatedly stated that the investments in the PASO and ECO 3 projects were made on the basis of RD 436/2004, not RD 661/2007. "436 was the major regulation for us,

[34] See C-0095, pg. 3 & C-0211, pg. 3-4 and footnote 14 above.

and 661 happened later"[35], he said in response to one question. In response to another, he confirmed that Deutsche Bank's involvement was not premised at all on RD 661/2007, or on any expectations in relation to the regulatory framework it provided: "The expectation of Deutsche Bank, we were working with 436 as the basic decree."[36] And then:

> Arbitrator Sands: "As your company proceeded to take the decisions to invest, did it proceed on the basis of the regulatory framework in RD 436? Was that the basis upon which the investments were made?"
>
> Mr Bauermeister: "436, yes."[37]

34. This evidence was not challenged, and it explains why the two Cuatrecasas legal opinions have nothing to say about any expectation as to stability that was said to be offered by RD 661/2007. It confirms that the two opinions were prepared for another purpose, and do not allow any reliance to be placed on them to establish any expectation of Deutsche Bank or the Claimants in relation to RD 661/2007. The testimony was not contradicted by Mr Kofmel, member of the executive board of Schwab, who stated that "as far as future regulatory changes were concerned, I wasn't interested in those, because it was very clear to me that there would be no retroactivity as regards our investment."[38] He did not identify any evidence to support that view. It seems there is none on the record, from which it can be inferred that none was given.

35. In sum, there is no evidence – none – in the record to show that OperaFund or Schwab were induced to make their investment by reliance upon Article 44(3) of RD 661/2007, or that they carried out any exercise in due diligence that addressed future regulatory change, or that they ever received advice that there was no risk of regulatory change. In particular, there exists on the record:

    (i) no document prepared by Deutsche Bank or anyone else to the effect that the Claimants could rely on a representation in Article 44(3), or elsewhere, that there would or could be no change in the regulatory framework;

[35] Transcript, Day 2, pg. 25, ln. 3-5.
[36] Transcript, Day 2, pg. 26, ln. 1-3.
[37] Transcript, Day 2, pg. 24, ln. 15-19.
[38] Transcript, Day 2, pg. 73, ln. 1-4.

(ii) no legal advice stating that Article 44(3) would or could not change, or lawfully be changed in accordance with Spanish law (or the Energy Charter Treaty); and

(iii) no internal document of either OperaFund or Schwab to support the claim that either Claimant had the expectation that RD 661/2007 and/or Article 44(3) would or could not change in accordance with Spanish law (or the Energy Charter Treaty).

36. There is no evidence that the Claimants had an expectation, or that it was premised on any exercise of due diligence. I am unable to understand the basis for the contrary conclusion of the Majority. My co-arbitrators have pointed to no evidence to show that Claimants conducted any sort of due diligence with regard to the risk of changes in the regulatory framework offered by RD 661/2007. The absence of such a due diligence, and the failure of it to produce confirmation of the existence of an expectation on which the Majority finds the Claimants to have relied, makes clear the conclusion that there was no basis for such an expectation.

37. A proper and reasonable assessment of evidence is a part of the judicial and arbitral function, a part of the reasoning process. A conclusion that is not based on actual evidence is not a reasoned conclusion, unless the evidence is irrelevant, which is not what the Majority concludes. The assessment of evidence is a time consuming exercise, and it may lead to different conclusion for cases that are based on a similar fact matrix. An arbitral award must be based on the evidence that is actually before the Tribunal. In this case the evidence cannot be said to be open to interpretation, it is incontrovertible. There is no evidence to show that the Claimants were induced to make their investments on the basis of a representation made by or attributable to the Respondent that they could rely on the tariff regime applicable at the time the investments were made for the life of those investments. There is no evidence to show that the Claimants engaged in an exercise of due diligence to address the risk of regulatory change. There is no evidence to show that the Claimants sought or obtained advice on the risk of regulatory change. The conclusions of the Majority to the contrary are entirely unsupported by any evidence before the Tribunal and, in this way, bereft of reasons.

Rates of return

38. No doubt the measures adopted by the Respondent between 2010 and 2014 affected the extent of the economic returns generated by the investments. In the face of the global financial crisis, the reality and consequences of which were not challenged, the Respondent was bound to act to limit an economic crisis and reduce a burgeoning budget deficit. It did so by reducing the rate of return on the Claimants' investments, from 7.8% to 6.1% (or 5.7% on the Claimants' case) after tax. The plants were still profitable, but they were less profitable. The rate of return granted by Spain was, nonetheless, still aligned with those granted by other European Union Member States.[39]

39. Given the circumstances faced by Spain, the change that occurred did not "exceed the exercise of the host State's normal regulatory power in the pursuance of a public interest", and it did not "modify the regulatory framework relied upon by the investor at the time of its investment outside the acceptable margin of change."[40] The Respondent was faced with a delicate balancing act: it had to reduce public expenditures without imposing excessive burdens on consumers of electricity and citizens, while at the same time continuing to encourage environmental protection and the renewable energy sector, and protecting the legitimate rights of existing investors in the sector.

40. The case-law turns its back on the kind of absolute immutability embraced by the Majority, making clear, that "the requirements of legitimate expectations and legal stability as manifestations of the FET standard do not affect the State's rights to exercise its sovereign authority to legislate and to adapt its legal system to changing circumstances".[41] The case-law confirms that Spain was not required to elevate the interests of the investors above all other considerations; the application of the FET standard allows for a balancing exercise by the State.[42]

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[39] Such as France, Italy, Estonia and Latvia. See: *Decision of the European Commission C(2017) 7384 final – State aid SA.40348 (2015/NN) – Spain, Support for electricity generation from renewable energy sources, cogeneration and* waste, 10 November 2017, RL-0080, para. 120.
[40] *Philip Morris*, 8 July 2016, para. 388 (recognising a "margin of appreciation enjoyed by national regulatory agencies when dealing with public policy determinations.") and para. 423.
[41] *Philip Morris*, para. 422.
[42] *Saluka Investments B.V. v Czech Republic* (Watts, Fortier, Behrens), 17 March 2006, paras. 305-306; *Electrabel SA v Hungary* (Veeder, Kaufmann-Kohler, Stern), 25 November 2015, para. 165.

41. The path taken by Spain was the subject of consideration and consultation. No doubt a range of alternative options were available to it. The Respondent might have decided to sacrifice the Claimants' investments, or it might have decided to protect the Claimants' economic returns and profitability and imposed greater costs on electricity consumers, or on the public purse, knowing that such an approach risked exacerbating the economic crisis. It chose neither path, opting instead for something of a middle course, a revised and reduced rate of economic return that nevertheless fell within parameters, accepted and approved by the European Commission.[43]

42. In short, the Claimants were not deprived of their investments, although the income generated by them was reduced. That reduction fell within "the acceptable margin of change"; against the background of the economic and environmental challenges faced by Spain, and the generous rates of return offered by RD 661/2007, which created a bubble of great profitability for investors, Spain opted instead for a balanced approach. I accept the conclusions of the Respondent's experts: "imagining that what was originally considered to be reasonable was 7% we would contend that this 1% difference falls within a very reasonable level of discretion or consideration of the regulator of whatever new economic factors occur in the market that the regulator has to regulate."[44]

43. Accordingly, I do not concur with the Majority's conclusion that Spain breached its obligation under Article 10(1) of the ECT to provide fundamental stability of the economic and legal regime in place, or that it is liable for any damages, or that it should pay any of the costs of this arbitration or the Claimants' costs. Nor am I able to accept, as the Majority puts it, that the FET requirement of Article 10 ECT protects against changes in the "essential characteristics of the regulatory regime relied upon by investors", and that those "essential characteristics" were altered (paras. 508, 513). It is notable that the Majority's conclusion is premised on the supposed reliance and "expectations" of the Claimants in relation to RD 661/2007 (paras. 512-13), a conclusion that is entirely unsupported by the evidence in the record.

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[43] *Decision of the European Commission 10.11.2017 C(2017) 7384 final*, RL-0080, para. 120. See also: *Response from the European Commission on Petition No 2520/2014 on the situation of the photovoltaic sector and the legality of the changes made to the law by the Spanish government*, R-0160; Respondent's Rejoinder on the Merits and Reply on Jurisdiction, paras. 326-329.

[44] Transcript, Day 4, pg. 188, ln. 10-15.

44. In the absence of evidence, the decision of the Majority will be seen as prioritising the interests of foreign investors over and above the interests of all other social actors. That it does so in the face of the evidentiary record before the Tribunal is a matter of considerable concern. The Majority has treated the ECT rules on FET as being akin to an insurance mechanism, one that allows the Claimants to benefit from a regulatory framework that was widely seen to be generous in creating windfall profits in the face of an unprecedented economic crisis and historically low rates of interest.[45] Mr Caldwell, the expert witness tendered by Claimants, in effect confirmed that an immutable, high rate of return coupled with unexpected and historically low interest rates resulted in a windfall for an investor with which the State was stuck.[46] His answer seems wholly unrealistic, in a real world in which governments seek to balance the demands of competing interests. It is also unsupported by the case-law, which confirms that in the absence of a specific promise or representation made by the State to the investor, "the latter may not rely on a bilateral investment treaty as a kind of insurance policy against the risk of any changes in the host State's legal and economic framework".[47] The expectation of an immutable rate of return identified by the Majority is not supported by the evidence or the case-law. It is an approach that is neither legitimate nor reasonable.[48]

A concluding matter

45. By way of conclusion, I wish to raise a final point of concern. It arises in relation to the Claimants' supposed exercise in due diligence, as noted above, and reliance said to have been placed on the two legal opinions prepared by the Cuatrecasas law firm. The opinions were prepared in 2006 and 2007 for Deutsche Bank, the project sponsors, who were at the time advised by the law firm. Cuatrecasas subsequently represented the Claimants in these

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[45] For effects of excessive tariffs, see for example: Mahalingam, A. & Reiner, D.M.: *Energy subsidies at times of economic crisis: A comparative study and scenario analysis of Italy and Spain,* Energy Policy Research Group – Working Paper, 23 January 2016, retrieved at: https://www.eprg.group.cam.ac.uk/wp-content/uploads/2016/02/1603-PDF.pdf; *New York Times – Spain's Solar Market Crash Offers a Cautionary Tale About Feed-In Tariffs,* 18 August 2009, retrieved at: https://archive.nytimes.com/www.nytimes.com/gwire/2009/08/18/18greenwire-spains-solar-market-crash-offers-a-cautionary-88308.html?pagewanted=1; *Financial Times – Shadow Falls Across Spanish Solar Energy Industry,* 31 May 2010, retrieved at: https://www.ft.com/content/275db4d0-6cdf-11df-91c8-00144feab49a.

[46] Transcript, Day 4, pg. 107, ln. 22 – pg.108, ln. 7.

[47] *Philip Morris*, para. 423-424, citing to: *EDF (Services) Ltd v Romania* (Bernardini, Derains, Rovine), 8 October 2009, para. 219.

[48] *Philip Morris*, para. 424 (*Antaris*, Principle 10).

proceedings, notwithstanding the apparently different legal interests and arguments of Deutsche Bank (as noted above, Deutsche Bank relied on RD 436/2004, whereas Claimants argued they relied on RD 661/2007). Claimants' repayment period of 22 years of the debt owed to Deutsche Bank has not yet expired.

46. In the course of the hearing Cuatrecasas sought to defend the legal opinions it wrote in 2006 and 2007. As noted, those legal opinions went to the heart of the due diligence issue, and offered no assurance – or even a view – as to risk of future regulatory changes in relation to RD 661/2007. Yet in legal submission Cuatrecasas sought to persuade the Tribunal that the legal opinions it wrote for Deutsche Bank – which testified before the Tribunal that it placed reliance on RD 436/2004 – could be relied upon by two other clients for an entirely different purpose, namely to establish reliance on a different regulatory framework (RD 661/2007) and the conduct of a proper exercise in due diligence.

47. This was doubly unfortunate. First, it is generally accepted that a witness (or potential witness) in legal proceedings should not also act as counsel in the same proceedings, yet Cuatrecasas made submissions on two legal opinions it had prepared, when it could have been giving witness testimony on the preparation of those opinions. Second, the avoidance of an actual or potential conflict of interest (Cuatrecasas' duty as adviser to Deutsche Bank is to be treated as distinct from its duty as counsel to the Claimants in these proceedings) is a necessary pre-requisite to confidence in the legitimacy of a legal order. The revolving door that seemed to operate in this case, between the bank that lent and the investors who borrowed, on the one hand, and the law firm that advised both, on the other, will hardly enhance public perceptions as to the legitimacy of the system of investor-state arbitration. If the system of investor-State arbitration is to retain – or, in the views of some, regain – its legitimacy, it is imperative that the very strictest standards are applied in the quest to avoid perceptions of conflict.

[Signed]

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Prof. Philippe Sands, Q.C.
Arbitrator
Date: August 13, 2019