GOVERNMENT ATTORNEY'S OFFICE
DIRECTORATE FOR STATE LEGAL SERVICES

SUBDIRECTORATE GENERAL OF LITIGATION SERVICES

IN THE CASE OF ARBITRATION UNDER THE 1965 CONVENTION ON THE SETTLEMENT OF INVESTMENT DISPUTES BETWEEN STATES AND NATIONALS OF OTHER STATES (ICSID CONVENTION)

AND

UNDER THE ENERGY CHARTER TREATY
(ICSID ARBITRATION CASE No.ARB/15/16)

BETWEEN:

BAYWA R.E. RENEWABLE ENERGY GMBH

BAYWA R.E. ASSET HOLDING GMBH

Claimant

- and -

THE KINGDOM OF SPAIN

Respondent

COUNTER MEMORIAL ON THE MERITS AND MEMORIAL ON JURISDICTIONAL OBJECTIONS

ARBITRATORS:

Mr. James R. Crawford
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15 June 2016

CONTENTS

I. LIST OF PRINCIPAL ABBREVIATIONS

"**Act 15/2012**": Act 15/2012, of 27 December 2012, on fiscal measures for energetic sustainability.

"**Act 54/1997**": Act 54/1997, of 27 November 1997, on the Electricity Sector. It was repealed by Act 24/2013, of 26 December 2013, on the Electricity Sector, in the terms stipulated in its sole Repealing Provision

"**Act 24/2013**": Act 24/2013, of 26 December, on the Electricity Sector.

"**AREPF**": Administrative record of electricity production facilities.

"**Baywa RE**": BayWa r.e. renewable energy GmbH (the first claimant).

"**Baywa AH**": BayWa r.e. Asset Holding GmbH (the second claimant).

"**BIT**": Bilateral Investment Treaty.

"**CJEU**": Court of Justice of the European Union.

"**Claimants**" or "**Claimant party**": BayWa r.e. renewable energy GmbH and BayWa r.e. Asset Holding GmbH.

"**CNE**": National Energy Commission. The Regulatory Body of the energy systems in Spain (since 7 October 2013, its functions have been taken over by the National Markets and Competition Commission).

"**CNMC**": National Markets and Competition Commission.

"**Contracting Party**": State or Regional Economic Integration organisation which has agreed to bind itself to the Treaty on the Energy Charter and for which the Treaty is in force, according to the definition of "Contracting Party" set out in Article 1(2) of the Energy Charter Treaty.

"**CPI**": Consumer Price Index.

"**CPI-CT":** Consumer Price Index at constant tax rates, excluding unprocessed food and energy products.

"**DCF**": *discounted cash flow*, or the current value of future cash flows.

"**IDAE**": Energy Diversification and Savings Institute.

"**Intra-EU dispute**": dispute between an investor of the EU and an EU member state.

"**Damages Expert Witness Report":** Expert report on financial damages drafted by KPMG, dated 3 March 2016, which accompanies the Memorial on the Merits submitted by the Claimant in this arbitration.

"**Directive 2001/77/EC**": Directive 2001/77/EC of the European Parliament and of the Council, of 27 September 2001, on the promotion of electricity produced from renewable energy sources in the internal electricity market.

"**Directive 2009/28/EC**": Directive 2009/28/EC of the European Parliament and of the Council of 23 April 2009 on the promotion of the use of energy from renewable sources and amending and subsequently repealing Directives 2001/77/EC and 2003/30/EC.

"**ECT**": Energy Charter Treaty, executed in Lisbon on 17 December 1994.

"**Econ One Research Report**": Expert Report by Econ One Research, Inc, dated 14 June 2016, drawn up by Econ One, which accompanies this Counter-Memorial on the Merits and Memorial on Jurisdictional Objections.

"**EU**": European Union.

"**Intra-EU investment**": investment in the EU by an EU investor.

"**KPMG Expert Witness Report**": Expert report dated 3 March, 2016, drawn up by KPMG, which accompanies the Memorial on the Merits submitted by the Claimant in this arbitration.

"**Ministerial Order HAP/703/2013**": Ministerial Order HAP/703/2013, of 29 April 2013, approving form 583 "Tax on the value of the production of electrical energy. Self-assessment and Part Payments", and establishing the form and procedure for its submission.

"**NREAP**": Spain's National Renewable Energy Action Plan

"**ORIE**" or by its English acronym "**REIO**": Regional Economic Integration Organisations

"**OR**": Ordinary Regime.

"**PPRE**": 2000-2010 Plan for the Promotion of Renewable Energies.

"**RD 2818/1998**": Royal Decree 2818/1998, of 23 December 1998, on production of electric energy by installations supplied with renewable energy, waste or cogeneration resources or sources.

"**RD 1432/2002**": Royal Decree 1432/2002, of 27 December, on the methodology of the average reference tariff.

"**RD 413/2014**": Royal Decree 413/2014, of June 6 2014, which regulates the electric energy production activity from renewable energy sources, cogeneration and waste.

"**RD 436/2004**": Royal Decree 436/2004, dated 12 March 2004, establishing the methodology for the updating and systematisation of the legal and economic regime for electric power production activity under the special regime.

"**RD 661/2007**": Royal Decree 661/2007, of 25 May 2007, regulating the activity of electricity production under the special regime.

"**RD 1578/2008**": RD 1578/2008, of 26 September, on remuneration for the activity of electricity production using solar photovoltaic technology for facilities after the deadline for the maintenance of the remuneration fixed under Royal Decree 661/2007, of 25 May, for such technology.

"**RD 1565/2010**": Royal Decree 1565/2010, of 19 November 2010, which regulates and modifies certain aspects of the electricity production activities under the Special Regime, published in the Official State Gazette on November 23, 2010.

"**RD 1614/2010**": Royal Decree 1614/2010, of 7 December, regulating and modifying certain aspects related to electric energy production using thermoelectric solar and wind power technologies.

"**RD-Law 7/2006**": Royal Decree-Law 7/2006, of 23 June, establishing urgent measures in the energy sector.

"**RD-Law 6/2009**": Royal Decree Law 6/2009, of 30 April 2009, which adopts certain measures in the energy sector and which approves the Social Tariff.

"**RD-Law 1/2012**": Royal Decree-Law 1/2012, 27 January 2012, which proceeds to the suspension of the remuneration pre-assignment procedures and the elimination of the economic incentives for new electric energy production plants based on cogeneration, renewable energy sources, and waste.

"**RD-Law 2/2013**": Royal Decree-Law 2/2013, of 1 February 2013, on urgent measures in the electricity sector and in the financial sector.

"**RD-Law 9/2013**": Royal Decree-Law 9/2013 of 12 July 2013, establishing urgent measures to ensure the financial stability of the electricity system.

"**RD-Law 14/2010**": Royal Decree Law 14/2010, of 23 December, establishing urgent measures for the correction of the tariff deficit in the electricity sector published in the Official State Gazette of 24 December 2010

"**RD-Law 20/2012**": Royal Decree-Law 20/2012, of 13 July, on measures to guarantee budgetary stability and promotion of competitiveness.

"**RE**": Renewable Energies.

"**Respondent**" o "**Respondent party**": the Kingdom of Spain.

"**TVPEE**": Tax on the value of the production of electrical energy. It was created with effect from 1 January 2013 by Act 15/2012 and is regulated in Articles 1 to 11 of such Act 15/2012.

"**SR**": Special Regime.

"**SEE**": Spanish Electricity System.

"**This arbitration**" or "**the present arbitration**": BayWa r.e. renewable energy GmbH and BayWa r.e. Asset Holding GmbH against The Kingdom of Spain (ICSID Case no. ARB/15/16).

"**This Memorial**", "**this statement",** or "**the present statement":** Counter-Memorial on the Merits and Memorial on Jurisdictional Objections, of 15 June 2016.

"**TFEU**": Consolidated version of the Treaty on the Functioning of the European Union, published in the Official Journal of the European Union on 26 October 2012.

"**Wind farms subject to this arbitration**": La Carracha Wind Farm and Plana de Jarreta Wind Farm.

II. INTRODUCTION

1. Pursuant to the provisions of Procedural Resolution No. 1, of 29 December 2015, and to the schedule set out in Annex A of the aforementioned Procedural Resolution, the Kingdom of Spain (hereinafter the "Respondent" or the "Respondent party") hereby submits its Counter-Memorial on the Merits and Memorial on Jurisdictional Objections.

2. In their Memorial on the Merits, dated 3 March 2016,, BayWa r.e. renewable energy GmbH (hereinafter, "BayWa RE") and BayWa r.e. Asset Holding GmbH (hereinafter "BayWa AH") (both hereinafter known as the "Claimants" or the "Claimant Party) maintain that the Kingdom of Spain has breached the obligations assumed under the Energy Charter Treaty (hereinafter "ECT") through the adoption of a range of legislative and regulatory measures approved by the Spanish Parliament and Government that affect the producers of electrical energy from renewable energy sources.

3. In particular, the Claimants allege that the Respondent has supposedly violated the obligations contained in article 13 of the ECT, on expropriation, as well as paragraph (1) of article 10 of the ECT referring to: i) fair and equitative treatment, ii) not impairing, in any way, through exorbitant or discriminatory measures, the management, maintenance, use, enjoyment or liquidation of the investments, iii) complete protection and security and iv) fulfilment of obligations contracted with investors or investments (umbrella clause).

4. Regardless of the defense submitted by the Respondent regarding the merits of the matter, proving that the Kingdom of Spain has not in any way violated international obligations assumed under the ECT, this Memorial contains two Jurisdictional Objections of essential relevance that arise in this case.

5. Firstly, the **Jurisdictional Objection** contained in **section III.A** of this Memorial makes reference to the lack of jurisdiction of the Arbitral Tribunal due to the non-existence of investors protected according to the ECT, as the investors in question do not come from the territory of another Contracting Party, as required by Article 26 of the ECT to be able to resort to arbitration. Both Germany, the country of the Claimants, and the Kingdom of Spain are Member States of the European Union (hereinafter "**EU**"), also an ECT Contracting Party. The arbitration mechanism for resolving disputes envisaged in Article 26 of the ECT does not apply to an intra-EU dispute such as this one, which determines that the Arbitral Tribunal lacks jurisdiction for hearing the dispute.

6. Secondly, the **Jurisdictional Objection** contained in **paragraph III.B** of this Memorial refers to the lack of jurisdiction of the Arbitral Tribunal to hear the dispute on an alleged breach of section (1) of Article 10 of the ECT through the adoption of taxation measures, particularly through the introduction of the Tax on the Value of the Production of Electrical Energy (hereinafter "**TVPEE**") by Act 15/2012, of 27 December 2012, on fiscal measures for energy sustainability (hereinafter "**Act 15/2012**"). That lack of jurisdiction is due to the fact that the Kingdom of Spain has not given its consent to submit such issue to arbitration given that, pursuant to Article 21 of the ECT, section (1) of Article 10 of the ECT does not create obligations regarding taxation measures of Contracting Parties.

7. The first of the mentioned Jurisdictional Objections is an Objection of a total nature, that is, it affects the dispute raised by the Claimants in its entirety. Thus, should this Objection be

upheld, it would entail the exclusion of the entirety of the dispute from the jurisdiction of the Arbitral Tribunal. The second of the mentioned Jurisdictional Objections is an Objection of a partial nature, that is, it only affects a certain part of the dispute raised by the Claimants.

8. To these effects, in line with rights reserved by the Claimants on the possibility of including subsequent claims, this party also reserves the power to raise additional objections in view of any new claims that the Claimant party may file in proceedings ulterior to this present arbitration[1].

9. As regards the merits of the matter, the Respondent henceforth states that the measures discussed by the Claimants do in no way represent a breach of international obligations assumed by the Kingdom of Spain under the ECT. The Kingdom of Spain has at all times fulfilled its obligations arising from the ECT.

10. Therefore, and regardless of the stated Jurisdictional Objections, the Kingdom of Spain will request the Tribunal to fully dismiss the pretensions of the Claimants in the merits, and a ruling for them to pay the costs of this Arbitration.

11. The Claimants based their claim on the fact that at the time of making their investment, the Kingdom of Spain had assumed a commitment to freeze the remuneration regimen for Renewable Energies (hereinafter "RE") contained, in the last instance, in Royal Decree 661/2007, of 25 May 2007, regulating the activity of electricity production under the special regime (hereinafter "RD 661/2007") and the registration in RAIPRE.

12. The Claimants consider that this commitment was strengthened by: a) subsequent legislation such as Royal Decree-Law 6/2009, of 30 April 2009, adopting certain measures in the energy sector and approving the social bonus (hereinafter "RD-Law 6/2009") and Royal Decree 1614/2010, of 7 December, regulating and modifying certain aspects related to electric energy production using thermoelectric solar and wind power technologies (hereinafter "RD 1614/2010") together with the official press release of 3 of December referring to its approval and the press release of 3 of December 2010; b) an alleged "agreement" between the Ministry of Industry and the wind and solar thermal sectors, dated 2 July of 2010 and the official press release of 2 of July of 2010; c) Royal Decree-Law 14/2010, of 23 December, which establishes urgent measures for the correction of the tariff deficit in the electrical sector, published in the state Official Gazette on 24 December of 2010 (hereinafter, RD-Law 14/2010") and the press release of 23 of December of 2010 following its approval, and d) Royal Decree-Law 1/2012, of 27 of January of 2012, which proceeds to suspend remuneration pre-assignment procedures and eliminate economic incentives for new electrical energy production facilities based on co-generation, renewable energy sources and waste (hereinafter, "RD-Law 1/2012") and the press release dated 27of January 2012, concerning its approval.

13. The position of the Claimants is based on a partial, biased and out-of-context conception of the Spanish Electricity System (hereinafter "**SEE**"), which can only be reached by omitting basic and essential aspects such as the following:

[1] Memorial on the Merits, para. 1100.

- That the Spanish regulatory system is based on a hierarchical principle, and all of its component regulations stem from legally stipulated regulation drafting procedures.
- The fundamental principle that Special Regime (hereinafter "**SR**") subsidies are a SEE cost subordinated to the principle of its economic sustainability.
- That the Special Regimen remuneration has always consisted on the earning of the market price for the energy produced, plus a subsidy, with the aim of providing SR Plants with a reasonable return, according to the capitals market.
- That premiums have always been determined based on the evolution of the demand and other base economic data, laid down in the Renewable Energy Plans and according to the "Installation Types" costs and revenue model.
- That this principle of reasonable return bestows a dynamic and balanced nature onto the special regime's remuneration regime, as has been insistently stated by the Supreme Court case law. In relation to the measures questioned in this arbitration process, this Supreme Court case law has been confirmed by the Constitutional Tribunal of the Kingdom of Spain, in its status of the highest level guarantor of fundamental rights. The value of this case law as a determining factual element for configuring the Legitimate Expectations of any investor has been highlighted by the first arbitration award that has reached a decision on the interpretation of the Spanish renewable energy support system
- That the motivation behind different regulatory changes in the RE remuneration regime, including those that occurred prior to the investment of the Claimants, was (i) either to correct situations of over-remuneration, (ii) or due to the severe changes of the economic data that served as a basis for the initial configuration of the premiums.

14. As they are unaware of these basic aspects of the SEE, the Claimants intend to submit to the Tribunal a biased view of the activity of generating electricity from renewable sources. In particular, they intend to make the Tribunal believe that wind generation facilities could be on an "island" outside the system of which they form a part. The Claimants ignore the fact that activity of generating electricity from renewable sources forms part of the SEE. Therefore, this activity participates in the objectives of the SEE, and it is also subject to its governing principles.

15. Upon making their alleged investment, the Claimants were aware, or should have been aware that electricity supply is a service of general economic interest. They also knew that the main objective of the SEE is to guarantee that all consumers have access to electrical energy under conditions of equality and quality. This implies that access to electricity must be given at the lowest possible cost, also taking environmental protection into account.

16. At the time of making their investments, the Claimants were also aware, or should have been aware, that the different amendments which were adopted in relation to the remuneration regime were aimed at (1) guaranteeing the technical and economic sustainability of the SEE and (2) correcting situations of over remuneration. Proof of this is the fact that the RE Sector itself was fully aware of these circumstances, as will be amply accredited throughout this Memorial.

17. Within this artificial construction, the Claimants intend to transmit the image that the principle of "*reasonable return*" is an innovation created ex novo by the measures in dispute. This thesis collides head-on with reality.

18. The reasonable return, according to the capitals market is the main backbone on which the legal remuneration regime is constructed. A minimum diligent knowledge of the Spanish regulatory framework makes it clear that all regulations passed since the approval of Act 54/1997, of 27 November, of the Electricity Sector (hereinafter, "LSE 1997" or "Act 54/1997") have been based on this principle. Furthermore, out of over 100 Supreme Court rulings that have been handed down on this subject, 100% were resolved based on this *Principle of reasonable return*.

19. Therefore, the Spanish system of support to the renewable energies has always been based on the principle of "*reasonable return on the cost of money in the capitals market*" as an aim. This Principle was initially established in article 30.4 of Act 54/1997, and has remained in article 14.7 of Act 24/2013, of 26 December, on the Electricity Sector (hereinafter, "LSE 2013" or "Act 24/2013"). This Principle guaranteed and guarantees to the investor, until a "level playing field" is achieved, the recovery (1) of the investment in the plant´s construction, (2) of operating costs and (3) obtaining a profit, which must be reasonable according to the capitals market.

20. This principle of reasonable return, as determined by the Supreme Court case law, must apply to the entire regulatory life of the facility, in the sense of ensuring that the investments made in the facilities earn a reasonable return throughout the existence of the same as a whole. This does not mean the permanence of a certain premium during the entire life of the facility, given that it could so happen that the investments may have already been amortised and may have generated the aforementioned reasonable return long before the end of its operational period.

21. The same methodology has always been maintained for this purpose. This consisted, and consists of defining, within each technology and according to lex artis existing in each period of time, different *installation-types*. Once these Installation Types had been determined, different *standards* were established in each one (cost of investment, operating cost, useful life of the plant, production hours subject to a premium, market price), that allowed such an *installation type* to reach a *reasonable return*, according to the cost of money in the capital market.

22. The Claimants, who invested since 2003, were aware that the *leitmotiv* of such regulatory adaptations and of the RE sector reform proposals has always been the same: the guarantee of a reasonable return within the framework of a sustainable SEE. This *leitmotiv* was made explicit in each and every measure adopted between 2004 and 2013.

23. The Respondent will accredit that the regulations of the Spanish Electricity System (hereinafter, "SEE") have never committed to, nor promised nor guaranteed the freezing of the regime. There have been successive amendments based on the purpose of guaranteeing the sustainability of the SEE and correcting situations of over-remuneration. These reforms could therefore improve or worsen the situation of the Claimants. The reason for the reform was never to maintain or increase investor return to attract them to the SEE. As we will accredit later, the harsh criticism of several of these reforms made by Associations do not differ much from the criticisms that they have subsequently made regarding the measures contested in this arbitration.

24. The Respondent will also demonstrate that Royal Decree 2818/1998, of 23 December 1998, on the production of electrical energy by facilities supplied by renewable energy, waste or generation resources or sources (hereinafter, "RD 2818/1998"), for the first time developed a *subsidy* (Premium) based remuneration system that completed the market price of the energy produced, plus a supplement for reactive energy. All of the above, to comply with the legal principle of reasonable return.

25. The Respondent will also accredit, that Royal Decree 436/2004, of 12 March 2004, establishing the methodology for the updating and systematisation of the legal and economic regime for electric power production under the special regime (hereinafter, "RD 436/2004") modified the remuneration model. This RD 436/2004, linked to the RE Development Plan 2000-2010, continued to follow the methodology consisting of defining different *installation types*. Once the mentioned installation types had been determined, different *standards* were established in each one (cost of investment, operating cost, useful life of the plant, production hours subject to a premium, market price), which allowed these installation types to reach a *reasonable return*, according to the cost of money on the capitals market.

26. This methodology was in turn linked to, and dependent on the base economic parameters (such as electricity demand) which were reflected in the aforementioned Plan. No diligent investor could be unaware of this situation.

27. The Respondent will demonstrate that Royal Decree 436/2004 linked the the evolution of the subsidies in the collection to the evolution of the Average Reference Electricity Tariff (hereinafter, ARET). This link generated a potential danger to the economic sustainability of the SEE in addition to producing situations of over-remuneration. Thus in 2006 Royal Decree Law 7/2006 was passed, adopting urgent measures in the energy sector (hereinafter, "RD-Law 7/2006") which, being a modification that was not foreseen in Royal Decree 436/2004, froze the subsidies of the SR until a new remuneration model be legally developed. This freezing caused what the Sector of the Renewable Energies considered damage to its investments.

28. The Respondent will also accredit that RD 661/2007": Royal Decree 661/2007, of 25 May 2007, regulating the activity of electricity production under the special regime (hereinafter, "RD 661/2007") was the consequence of RD-Law 7/2006. This royal decree did not improve remuneration conditions of the Claimant party. Proof of this is the fact that it was appealed by several producers of electricity under the special regime, who alleged that article 40.3 of RD 436/2004 contemplated the "freezing" of the previous incentives scheme and that, therefore, the approval of RD 661/2007 violated its legitimate expectations. As we will accredit, these arguments were rejected by the Supreme Court.

29. RD 661/2007, on the determination of subsidies, maintained its link to the methodology explained above for installation types, set out in the RE Plan 2005-2010. Similarly, it maintained its link to the base economic parameters set out in the aforementioned Plan.

30. In 2009, the impact of the international crisis caused an economic imbalance of the SEE. Consequently, RD-Law 6/2009 was passed, introducing amendments to RD 661/2007 that were not envisaged in its articles. Furthermore, it supposed a warning about the need for all

the income and expenditure items of the system to adapt to the new base economic circumstances, while respecting the principle of reasonable return.

31. The Respondent will also demonstrate that, in light of this situation, the Sector (1) criticized harshly this RD-Law and (2) proposed in May 2009 a Draft amendment comprehensive of the remuneration model of REs, defined by the Sector itself as the best (a) to achieve *reasonable rates of return* with reference to the cost of money in the capital market, (b) provide *"security and stability to investments"* and (c) allow *"the REs to develop their full potential in a sustainable and lasting manner".*

32. This model was based on two essential points: (a) Linking the reasonable return to the 10-year government Bonds of the Spanish State + 300 basis points and (b) that such return would be fixed in relation to the various *"kinds of installations, differentiated by technology and size, in a manner that reflects the common values reached by such investments in reality."* The similarity with the remuneration model implemented from 2013 on is more than evident.

33. The measures taken during 2010 (Action Plan for Renewable Energy, Royal Decree 1565/2010, of 19 November 2010, which regulates and modifies certain aspects of electricity production activities under the Special Regime (hereinafter, "RD 1565/2010"), RD 1614/2010 and the subsequent RD-Law 14/2010 responded, like the previous measures, to the need to guarantee the technical and economic sustainability of the SEE, as well as the need to correct any detected situations of over-remuneration.

34. Due to the fact that it has been omitted by the Claimants, Spain will accredit that electricity demand suffered an exceptional reduction during 2010. The aforementioned circumstance, The aforementioned circumstance, among other circumstances, caused the RE Sector to require a reform of the Electricity Sector.

35. No diligent investor could reasonably deduce, from this regimen and its successive modifications, interpreted by the Supreme Court in its case law, the existence of a commitment to freeze a specific remuneration model in their favour. That is, Spain never committed itself to always maintain or improve the situation of investors. And even less to grandfather subsidies indefinitely

36. The only guarantee that investors had was to achieve a reasonable return in the context of a technically and economically sustainable SEE. Spain will demonstrate that the Claimants had or had to have that understanding of the System and knew the *"relatively wide margin of the "ius variandi" of the Administration in a regulated industry where general interests are involved."*

37. In the same vein, in the years 2012 to 2014, the Kingdom of Spain adopted measures to reform the Electricity Sector which had been announced publicly and which obeyed the same guiding thread. These measures are reasonable and proportionate and affected all subjects of the SEE. In particular, the measures affected Consumers, whose electricity bill increased disproportionately between 2003 and 2012. Measures affecting Transporters, Distributors and ordinary Producers were also adopted. In addition, for the first time ever the promotion of renewable energies was charged to the State Budget.

38. This reform has maintained the following essential elements of the renewables support system:

    (a) Priority access.

    (b) Priority dispatch.

    (c) The methodology for fixing subsidies based on the establishment of installation types and standards.

    (e) The perception of the *market price* for energy sold, plus a *subsidy* in order to achieve reasonable rates of return, with reference to the cost of money in the capital market, which allows them to compete on equal terms on the market.

    (f) Premiums are a SEE cost that must guarantee its operation in a sustainable manner.

39. All the regulations included in the new regulatory economic framework have complied with the procedure laid down by Spanish law. All the necessary reports, even non mandatory ones, have been recollected to ensure the full compliance of the new regulatory text with the Spanish legal system. There have been several hearing procedures, in which all the parties in the Sector were able to participate. All of this processing lasted for almost a year, so that all stakeholders would have the opportunity to participate.

40. Thus, the Kingdom of Spain has made a predictable, reasonable and proportionate use of its regulatory power with an accredited public interest purpose. That regulatory power was not limited by any *specific* commitment. In this regard, the Kingdom of Spain has not assumed with the Claimant, or with any of the investments set out in the Claimants´ Memorial, a commitment to the immutability of RD 661/2007 in their favour.

41. Therefore, the Kingdom of Spain has not broken any specific commitment that it had previously undertaken with the Claimant. The Kingdom of Spain has limited itself to exercising its regulatory power fairly, in accordance with the legally established procedures to ensure, at all times, (1) the sustainability and balance of the SEE and (2) the reasonable return of renewable energy Plants. The Kingdom of Spain has thus not violated the standard of Fair and Equitable Treatment of Article 10(1) of the ECT

42. This Counter-Memorial brings to light the relevance and applicability of various Tests proposed by Arbitral Tribunals. These Tests credit that the measures adopted by the Kingdom of Spain were neither discriminatory, exorbitant nor disproportionate. On the contrary, the treatment provided by the Kingdom of Spain to the Claimant has been Fair and Equitable taking into account (1) what the Claimants knew when they executed their alleged investment, (2) the lack of commitments by the Spanish State towards the Claimants, (3) the correct functioning of the regulatory framework, (4) the concurrent economic circumstances and (5) the purpose of the public policy underlying all the measures.

43. The Kingdom of Spain has not entered into any obligation with the Claimants or their investment that could be covered by the umbrella clause of article 10.1, final paragraph of the ECT. In accordance with Spanish domestic law, no obligation has arisen in the regulations, in press releases or in the other acts invoked by the Claimants, that can be protected at an international level. Neither has the registration of the Claimants' wind farms

in the Administrative Register of Special Regimen Production Facilities (hereinafter "RAIPRE") implied the establishment of a *vis-á-vis* relationship between the facilities and the Kingdom of Spain. The RAIPRE is simply a section of the Register in which it is obligatory for all conventional and renewable electricity production installations to be registered, to allow the Regulator to control the fulfilment of their planning objectives and the correct operation of the SEE.

44. The Kingdom of Spain has limited itself to regulate the SEE according to the provisions of the Law, at all times maintaining the economic Framework on which the SEE is based. It is the Claimants who artificially intend to convert statutory and regulatory hearing procesdures into "agreements" that lead to obligations that do not exist in Spanish law.

45. Therefore, and as explained in this Counter-Memorial, the Kingdom of Spain has not violated the obligations set out in article 10.1 of the ECT.

46. The measures adopted by Spain have not entailed the expropriation of any of the Claimants' assets or rights. In fact, the Claimants have not been able to precisely define the subject of the alleged expropriation. The Claimants did not invest in the subsidies that could be earned by wind farms in which they invested indirectly, but in indirect stakes in the entities and in the subordinated debt of the holding companies of RE facilities. The Claimants neither possess nor control the future revenue of wind farms, or the power to administer and dispose of them. These rights have not been incorporated into their assets. Therefore, the rights that have supposedly been invoked do not constitute an expropriable asset in the sense of article 13(3) of the ECT in relation to the concept of protected investment contained in article 1(6) of the ECT.

47. Consequently, and as explained in this Counter-Memorial, the Kingdom of Spain has not violated the obligations set out in article 13 of the ECT.

48. Finally, and subsidiarily, this Counter-Memorial shows that the alleged damages are completely and absolutely speculative. The Claimants have not fulfilled the burden of proof required of them for their claim to be addressed.

49. In the present case, the discounted cash flows method (hereinafter "DCF") is inappropriate due to the concurrent circumstances, in accordance with doctrine: the scarce track record of CSP Plants and forecasting errors of wind farms, the lack of proportion between investments and the claimed damages, etc.

50. In addition, the expert report accompanying the Memorial on the Merits is opaque and the supplied information is incomplete, positioning this Respondent party in a defenceless situation for this reason.

51. An expert report dated 14 of June of 2016 is attached to this Counter Memorial. The expert report focuses on the economic-financial aspect of the Claimant, the thermosolar plants and the wind farms and its claim (hereinafter, "**Econ One Research Report":** Expert Report by Econ One Research, Inc, dated 14 June 2016, drawn up by Econ One, which accompanies this Counter-Memorial on the Merits and Memorial on Jurisdictional Objections) in which the following aspects are analysed: (i) Ownership structure and history of Projects, (ii)

Economic Features of the Projects, (iii) Economic Impact of the Measures on the Projetcs (iv) KPMG´s Economic Impact Analysis.

52. Based on the above arguments, extensively developed in this Statement, the Kingdom of Spain will request the Tribunal to fully dismiss the pretensions of the Claimant, and a ruling for them to pay the costs of this Arbitration.

53. Similarly, a witness statement is attached to this Counter-Memorial on the Merits. This, the statement of the following witness is provided:

- D. Juan Ramón Ayuso.

54. This Counter-Memorial on the Merits will be submitted, pursuant to section 11.4 of Procedural Order 1 of 29 December 2015, in Spanish and English. However, in the event of a discrepancy between the two versions, preference will be given to the Spanish version of the Counter-Memorial.

III. JURISDICTIONAL OBJECTIONS

A. Lack of jurisdiction of the Arbitral Tribunal *ratione personae* to hear the dispute raised by the Claimants due to the absence of protected investors under the ECT. The Claimants are not from the territory of another Contracting Party, given that both Germany and the Kingdom of Spain are Member States of the European Union. The ECT does not apply to disputes relating to intra-EU disputes

(1) Introduction: need for the existence of an investor "of another Contracting Party"

56. The Claimants have resorted to this arbitration attempting to benefit from the protection of Article 26 of the ECT[2], referred to the settlement of disputes between an investor and a Contracting Party.

57. Article 26(1) of the ECT requires that the dispute occurs between "*a Contracting Party*" and an "*investor of another Contracting Party*", which inevitably implies the exclusion from this Article of any case where an investor of a European Union (EU) State has a dispute with an EU State, in relation to an investment in said State (hereinafter respectively referred to as "**intra-EU dispute**" and "**intra-EU investment**").

58. BayWa r.e. renewable energy GmbH (BayWa RE) and BayWa r.e. Asset Holding GmbH (BayWa AH) are legal persons located in Germany.

59. Based on the previous premises, that the claimant party must prove, it should be taken into account that both Germany and the Respondent, the Kingdom of Spain, are members of the EU, also an ECT Contracting Party.

60. Furthermore, both the Kingdom of Spain and Germany were already members of the EU at the time of their ratification of the ECT, which is why there were unable to contract obligations between themselves within the ambit of the Internal Energy Market, harmonised by the EU.

61. The Claimants´ investment is an investment made within the ambit of the Internal Electricity Market of the EU. Within this framework, the EU system grants to the EU-national investor particular protection which is preferential to the protection granted by the ECT and any Bilateral Investment Treaty (hereinafter "**BIT**").

62. In the event of conflict between the ECT and EU Law, which is also applicable international Law, the latter must prevail. EU Law forbids the existence of any dispute settlement mechanism other than that established by its Treaties, which may interfere with the bases of the Internal Market.

63. To resolve this arbitration, the Honourable Tribunal will have to deliver an opinion on the rights before the Spanish State of alleged intra-EU investors within the Internal Electricity Market, thus interfering with the competence of the judicial system of the EU.

64. That is why the Arbitral Tribunal, with all due respect, does not have jurisdiction to rule on the claim submitted by the Claimants.

[2] ECT. RL-0006

(2) The EU system grants to the EU-national investor particular protection which is preferential to the protection granted by the ECT and any BIT

65. The EU is an economic integration area which includes as part of its regulations on the Internal Market a comprehensive system to promote and protect intra-EU investments, which prevails over the provisions of the ECT.

66. The aforementioned Internal Market comprises, as indicated in Article 26 of the current Treaty on the Functioning of the EU (hereinafter "**TFEU**")[3], an "*area without internal frontiers in which the free movement of goods, persons, services and capital is ensured*".

67. The Internal Market measures include the Directives that have established the objectives that the Member States must achieve to become part of the Internal Electricity Market[4]. On the other hand, the energy policy has been part of the EU policies since before the ECT was signed[5].

68. In fact, the promotion of the investment in renewable energies by the Kingdom of Spain is enshrined in the obligations that Spain, in its capacity as a Member State, undertook in order to achieve the aims established by the Directives approved by the EU, as recognised by the Memorial on the Merits itself. One of the main aims imposed by the aforementioned Directives is to protect the investor. Directive 2009/28/EC of the European Parliament and of the Council of 23 April 2009 on the promotion of the use of energy from renewable sources and amending and subsequently repealing Directives 2001/77/EC and 2003/30/EC (hereinafter "**Directive 2009/28/EC**"), states in its whereas clause (14):

[3]Consolidated versions of the Treaty on European Union and the Treaty on the Functioning of the European Union, published in the Official Journal of the European Union of 26 October 2012 (the former and latter hereinafter respectively "TEU", and "TFEU"). RL-0001 and RL-0005.

[4]Council Directive 90/547/EEC of 29 October 1990 on the transit of electricity through transmission grids, published in the Official Journal of the European Union on 13 November 1990 (English version) (RL-0012); Council Directive 90/377/EEC of 29 June 1990 concerning a Community procedure to improve the transparency of gas and electricity prices charged to industrial end-users, published in the Official Journal of the European Union on 17 July 1990. (English versions) (RL-0013); Directive 96/92/EC of the European Parliament and of the Council of 19 December 1996 concerning common rules for the internal market in electricity, published in the Official Journal of the European Union on 30 January 1997. (English version) (RL-0014); Directive 2001/77/EC of the European Parliament and of the Council of 27 September 2001 on the promotion of electricity produced from renewable energy sources in the internal market in electricity published in the Official Journal of the European Union on 27 October 2001. (RL-0015); Directive 2003/54/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in electricity, published in the Official Journal of the European Union on 15 July 2003. (Spanish version) (RL-0016), Directive 2009/28/EC of the European Parliament and of the Council of 23 April 2009 on the promotion of the use of energy from renewable sources and amending and subsequently repealing Directives 2001/77/EC and 2003/30/EC published in the Official Journal of the European Union of 5 June 2009 (RL-0017).

[5] Currently Title XXI of the TFEU. The origins of the current EU date back to the signing of the Treaty of Paris of 18 April 1951, creating the European Coal and Steel Community (main sources of energy in the region at that time) or "ECSC". It was followed by the creation of the European Economic Community ("CEE") and the European Atomic Energy Community ("EURATOM") in the Treaty of Rome of 25 March 1957. RL-0005.

> *"The main purpose of mandatory national targets is to provide certainty for investors (…)."*[6]

69. These same Directives are precisely those which enabled the Kingdom of Spain to incentivise investment by means of the concession of State Aid, as permitted by the EU with certain limitations.

70. This single area that the Internal Market amounts to is supplemented by a comprehensive protection of Fundamental Rights and a principle of liability of Member States for breaches of the Legal System, all of which are guaranteed by the jurisdictional system of the EU, to which the monopoly in the ultimate interpretation of EU Law is attributed.

71. Indeed, the institutional and judicial framework of the EU provides the appropriate means and legal actions when the rights of investors are violated. The investor can always claim damages against the State before the corresponding national courts on the basis that it has been unduly discriminated against in relation to the nationals of that same Member State. It can also report any breach of EU Law, which can be directly invoked, including legislation in matters of energy. In the event that, in resolving the dispute, a doubt arises as to the interpretation of EU law, national courts have the option and obligation, if they are the final instance, to submit a preliminary ruling before the European Court of Justice pursuant to Article 267 TFEU. When a national court fails to fulfil its obligations pursuant to EU Law, the injured party has grounds to claim damages from the Member State.

72. This integral system to promote and protect investments determines that no distinction is made within the EU between investors from one State or another but rather simply between EU investors and investors from third countries. The category of foreign investor in the EU therefore corresponds exclusively to the investor of third countries.

73. The EU protection standard implies an additional obligation, without comparison, not only in Investment Treaties, but also in any other International Treaty, which prohibits any kind of legislation which dissuades the EU investor from establishing itself if the Member State. As established by the European Court of Justice (hereinafter "**ECJ**") regarding the predecessor of Article 54 of the TFEU:

> *"According to settled case-law, Article 43 EC precludes any national measure which, even if applicable without discrimination on grounds of nationality, is liable to hinder or render less attractive the exercise by Union nationals of the freedom of establishment that is guaranteed by the Treaty (see, to that effect, inter alia, Case C‑19/92 Kraus [1993] ECR I‑1663, paragraph 32; Gebhard, paragraph 37; Case C‑442/02 CaixaBank France [2004] ECR I‑8961, paragraph 11; and Case C‑169/07 Hartlauer [2009] ECR I‑0000, paragraph 33 and the case-law cited) ."*[7] *(emphasis added)*

[6] Whereas clause (14) of Directive 2001/77/EC also states*: "one important means to achieve the aim of this Directive is to guarantee the proper functioning of these mechanisms in order to maintain investor confidence"* (in reference to the support mechanisms for renewable energy sources). RL-0015.

[7] Judgement of the Court of Justice of the European Union, of 11 March 2010, Case C−384/08, Attanasio Group [2010] ECR I−2055, paragraph 43. R-0078

(3) The preferential application between EU Member States of their own protection system is reflected in the wording, context and purpose of the ECT

74. The application of the intra-EU investor protection system prevails over any other international Treaty. This conclusion, derived simply from the peculiar nature of the EU, also has its literal recognition in the ECT itself.

(3.1) The literal interpretation of the ECT provides that the EU system prevails between EU Member States

75. Indeed, the definition of the Contracting Parties of Article 1(2) of the ECT, includes Regional Economic Integration Organisations (hereinafter "**REIO**") such as the EU, the only REIO that is part of the ECT.

76. Similarly, Article 1(3) of the ECT defines the REIO as:

> *"an organization constituted by states to which they have transferred competence over certain matters a number of which are governed by this Treaty, including the authority to take decisions binding on them in respect of those matters"(emphasis added)*

77. This article acknowledges the special nature of the EU as an international organisation constituted by States to which they have transferred competence over certain matters in an irrevocable and binding way. It is obvious that if the ECT had not wanted to consider that part of the matters comprised by the ECT were exclusively decided by the EU, it would have omitted the final part of the sentence, bearing in mind that the EU is the only REIO that has subscribed to the ECT.

78. Similarly, Article 1(10) of the ECT defines the "Territory" of the REIO, by referring once again to the provisions of this organisation, that is, the EU.

79. Article 16 of the ECT establishes rules for compatibility between previous and subsequent treaties and the ECT. Among these Treaties are those that regulate the EU, which prevail over the ECT in intra-EU relations.

80. As a consequence of the signing of the ECT and through the most favoured nation clause, Article 25 of the ECT prevents the integral intra-EU investment promotion and protection system from extending to ECT signatory States that are not Member States.

81. Similarly, this situation is considered in Article 36(7) of the ECT, when it is permitted that the EC and Member States vote on matters that fall under their respective competences, providing that: "*A Regional Economic Integration Organisation shall, when voting, have a number of votes equal to the number of its member states which are Contracting Parties to this Treaty*".

82. Finally, section (1) of Article 26 of the ECT requires that the dispute occurs between the Investor of a Contracting Party and another Contracting Party. While section (6) requires disputes to be resolved "*in accordance with this Treaty and applicable rules and principles of international law*", which means treating EU law and applicable International Law on equal terms when it comes to resolving the dispute.

(3.2) Article 26 of the ECT prevents arbitration between an intra-EU investor and an EU Member State

83. It is precisely Article 26(6) of the ECT that prevents an intra-EU investor from bringing arbitration proceedings against an EU Member State regarding its investment. Accepting this possibility would be contrary to EU Law, which is applicable International Law. In *Electrabel S.A v. The Republic of Hungary*, the Arbitral Tribunal determines that:

> *"[…]the Tribunal concludes that Article 307 EC precludes inconsistent preexisting treaty rights of EU Member States and their own nationals against other EU. Member States; and it follows, if the ECT and EU law remained incompatible notwithstanding all efforts at harmonisation, that EU law would prevail over the ECT's substantive protections and that the ECT could not apply inconsistently with EU law to such a national's claim against an EU Member State."*[8]

84. Article 344 of the TFEU establishes that: "*Member States undertake not to submit a dispute concerning the interpretation or application of the Treaties to any settlement procedure other than those provided for therein*." The application of this provision means that Spain cannot submit any matters relating to the Internal Electricity Market to arbitration.

85. Accepting arbitration would mean that the Arbitral Tribunal would have to rule on the rights of the European investor in the Internal Market.

86. The ECJ has already categorically issued an opinion on the impossibility of this interference. In Decision 1/91, Economic Area Agreement[9], of the CJEU, the Court pronounced on the "*Draft agreement between the Community, on the one hand, and the countries of the European Free Trade Association, on the other, relating to the creation of the European Economic Area*." The ECJ declared the incompatibility of the legal system created by the draft because it determines the future interpretation of the EU rules on free movement and competition.

87. To reach this conclusion, the first thing stipulated by the ECJ is that:

> *"when a dispute relating to the interpretation or application of one or more provisions of the agreement is brought before it, the EEA Court may be called upon to interpret the expression 'Contracting Party', within the meaning of Article 2(c) of the agreement, in order to determine whether, for the purposes of the provision at issue, the expression 'Contracting Party' means the Community, the Community and the Member States, or simply the Member States. Consequently, the EEA Court will have to rule on the respective competences of the Community and the Member States as regards the matters governed by the provisions of the agreement.*
>
> *[…] It follows that the jurisdiction conferred on the EEA Court under Article 2(c), Article 96(1) (a) and Article 117(1) of the agreement is likely adversely to affect the*

[8] *Electrabel S.A v. Hungary*, ICSID Case no. ARB/07/19, Decision on jurisdiction, applicable Law and liability, of 30 November 2012 (original version in English), paragraph 4.189. RL-0002.

Opinion 1/91 of 14 December 1991 issued by the Court of Justice of the European Union regarding the "Agreement to Create a European Economic Area" (EEA) (original Spanish version). R-0001

> *allocation of responsibilities defined in the Treaties and, hence, the autonomy of the Community legal order, respect for which must be assured by the Court of Justice pursuant to Article 164 of the EEC Treaty. This exclusive jurisdiction of the Court of Justice is confirmed by Article 219 of the EEC Treaty, under which Member States undertake not to submit a dispute concerning the interpretation or application of that treaty to any method of settlement other than those provided for in the Treaty. Article 87 of the ECSC Treaty embodies a provision to the same effect."*[10]

88. The ECJ also states that:

> *"It follows that in so far as it conditions the future interpretation of the Community rules on the free movement of goods, persons, services and capital and on competition the machinery of courts provided for in the agreement conflicts with Article 164 of the EEC Treaty and, more generally, with the very foundations of the Community. As a result, it is incompatible with Community law."*[11]

89. Finally, the same Opinion of the ECJ recalls that:

> *"It must be pointed out that the agreement is an act of one of the institutions of the Community within the meaning of indent (b) of the first paragraph of Article 177 of the ECC Treaty and that therefore the Court has jurisdiction to give preliminary rulings on its interpretation. It also has jurisdiction to rule on the agreement in the event that Member States of the Community fail to fulfill their obligations under the agreement."*[12] *(emphasis added)*

90. On the other hand, it should be pointed out that when the ECT was signed, the Member States of the then European Community were unable to contract obligations between them as regards the Internal Market as it is an area in which they had granted their sovereignty to the then European Community. It is for this very reason that the EU is a Contracting Party. Hence, Article 26 of the ECT does not generate any obligations between the Member States.

91. The only possible arbitration in the context application of the ECT, in an interpretation which is in harmony with the EU system (Articles 16 and 26(6) of the ECT) is, as is asserted in *Electrabel S.A v. Hungary*, that of *"a non-EU investor and an EU Member State or between an EU investor and a non-EU Member State."*[13]

92. In this way, the intra-EU investor, with a protection level provided by EU Law, is protected by the judicial system of the EU. The investor from a third party country which is a signatory to the ECT (for example, a Japanese investor) which does not receive through the ECT in the EU Member States the "national" treatment which EU Citizen investors do receive because they are from the EU, may resort to arbitration to defend the rights granted to it by Article 10(1) of the ECT. Any Arbitral Tribunal solving this dispute will never

[10] Ibid, paragraph 34.
[11] Ibid.
[12] Ibid, paragraph 38.
Electrabel S.A v. Hungary, ICSID Case no. ARB/07/19, Decision on jurisdiction, applicable Law and liability, of 30 November 2012 (original version in English), paragraph 4.158 RL-0002.

interfere with the competences of the ECJ because the EU system does not apply to the investor from a third party country.

(3.3) The purpose of the ECT confirms the interpretation of the Kingdom of Spain

93. Assuming that intra-EU disputes are included within the context of the protection of the ECT would also mean giving up the objective and purpose of the ECT. To be precise, it would mean assuming that the EU and its Member States promoted, as key players, the creation and conclusion of the ECT to cover an area, that of intra-EU investments, which had been totally covered -and in a far superior manner- for years by EU Law. What's more, it would mean taking competences away from the ECJ and mistrusting the very protection system given by the EU to its Citizens.

94. The objective of the ECT is to establish "a legal framework in order to promote long-term cooperation in the energy field, based on complementarities and mutual benefits, in accordance with the objectives and principles of the Charter"[14]. In turn, the purpose of the Charter was "*to promote East-West industrial cooperation through the establishment of legal safeguards in fields such as investment, transport and commerce*". The ECT "*is the basis of an energy community between regions of the world that were divided by the iron curtain.*"[15]

95. In actual fact, the origin of the ECT lies in the wish of the Council of the then European Community to speed up the economic recovery of Eastern Europe after the fall of the Berlin Wall through cooperation in the energy sector[16].

96. Hence, the literal interpretation of Article 26 of the ECT, not only section (1) thereof but also section (6), in accordance with its context and purpose, leads to the absence of grounds for submitting to arbitration disputes between an intra-EU investor and an EU Member State.

(4) The position of the Kingdom of Spain is confirmed by the doctrine

97. The position manifested by this Respondent party is also endorsed by the doctrine. In this regard, Bruno Poulain has indicated that:

> *"The [ECT] was initially concluded with the former Soviet republics to improve the safety of the energy supply from Eastern Europe. Bearing in mind the initial raison d'ètre of this instrument, we cannot do any more than have reservations about its application to purely intra-community situations. Certain elements of its text also seem to endorse the inapplicability of [ECT] Article 26 to intra-Community situations."*[17] *(free translation) (footnote omitted)*

Article 1 of the ECT. RL-0006.
Preface to the ECT. RL-0006.
Ibid.

[17] Développements récents du droit communautaire des investissements internationaux, Bruno Poulain, Revue Générale de Droit International Public, C XIII/2009, 4; page 881. The omitted footnote says: "Our opinion is based on Article 25 of the [ECT], which proposes a disconnection clause to the benefit of the

98. Moreover, as aptly stated by Professor Jan Kleinheisterkamp:

> *"Why should investors from certain member states enjoy a greater degree of protection than that afforded by the European Treaties? Why should arbitral tribunals, in a purely intra-EU context, not be bound to the same restrictions on judicial review as courts of the Union and the member states? Moreover, in the light of the fact that the European Treaties have put into place the well-tested procedural mechanisms that ensure that the EU laws, establishing supra-national standards of protection of investments within the internal market, are they applied and interpreted autonomously, untainted by national parochial conceptions, and uniformly? And going beyond the substantive standards of protection: why should European investors in the Internal Market be allowed to crosscut the existing supranational judicial system of the ECJ by using an alternative system of international arbitration?*
>
> *[…]In summary, there seem to be good reasons for the Commission to push for ensuring that EU law is the only regime governing investment flows within the European market and that the ECJ is the only ultimate instance for interpreting and applying these rules. And, indeed, it does not seem too far-fetched to expect the ECJ to follow the Commission on this point.[…]*
>
> *Given the Commission's strong determination to eliminate the parallelism of standards and recourses for investments inside the Internal Market, it can be expected that also the intra-EU dimension of the ECT will be eventually targeted by the Commission and may disappear if member states cooperate or are forced to cooperate by the ECJ."*[18] *(footnotes omitted)*

99. This author adds that:

> *"The essence of this conflict is, indeed, about whether tribunals can be allowed to review, on the basis of the latter, the legality of government measures that are, at least in theory, fully under the ECJ's control of the European market rules and fundamental rights, and the above sketched 'policy space' they reserve to the Union and the Member States."*[19] *(footnotes omitted)*

100. In actual fact, as is stated by Professor Jan Kleinheisterkamp, the problem raised is not a problem of the selection and application of the "*most favourable regulation*". The issue is that between EU Member States and their Citizens, EU Law puts aside the application of any other regulation by virtue of the principle of primacy.

101. It is thus a question of determining whether in the light of EU Law, it is valid to apply within the European Union in conflicts between an EU investor and an EU State the provisions of an International Treaty or whether, by contrast, in these intra-EU relations solely EU Law applies. Assuming that is not disputed that EU Directives on Renewable

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parties of a regional economic integration organisation and in Article 16, which appears to link material right and the controversy settlement mechanism." (free translation). RL-0060.

[18] *Investment protection and EU Law: the intra- and extra- EU dimension of the Energy Charter Treaty*, Jan Kleinheisterkamp, Journal of International Economic Law 15 (1), Oxford University Press, 2012, pages 101, 103 and 108. RL-0064.

[19] Ibid.

Energies are the framework for Spanish legislation which the Claimants supposedly relied on when making their investment, the issue must be settled in the light of the interpretation of EU Law and with regard to these matters Spain cannot submit its decision to venues other than the EU judicial system pursuant to Article 344 of the TFEU.

102. As has been stated above, any dispute settlement system introduced by a Treaty affecting the foundations of the EU is incompatible with EU Law. Article 26(6) of the ECT requires the settlement of those issues under litigation in accordance with "*the ECT and applicable rules and principles of international law*". The rules and principles of the EU are rules and principles of International Law and must be applied with the same hierarchy as the ECT itself. Accepting arbitration to solve disputes which affect the freedom of establishment and the free movement of capital of an EU investor in EU territory in the context of Renewable Energies is contrary to EU Law and incompatible with the actual content of Article 26(6) of the ECT.

(5) Conclusion

103. In view of the above, it is considered that the Arbitral Tribunal, with all due respect, lacks the jurisdiction to hear the present intra-EU dispute brought by alleged German investors against the Kingdom of Spain. Both Germany and Spain were EU member States when the ECT came into effect. Hence, the Claimants fail to comply with the requirement foreseen in Article 26(1) of the ECT which states that to access arbitration the dispute must be between a Contracting Party and an investor from a different Contracting Party.

B. Lack of jurisdiction of the Arbitral Tribunal to hear an alleged breach by the Kingdom of Spain of obligations derived from Article 10(1) of the ECT through the introduction of the TVPEE by Act 15/2012: lack of consent from the Kingdom of Spain to submit this matter to arbitration, given that, pursuant to Article 21 of the ECT, section (1) of Article 10 of the ECT does not create obligations regarding taxation measures of the Contracting Parties

(1) Introduction

104. Without prejudice to the rest of Jurisdictional Objections, the Arbitral Tribunal, with all due respect, lacks jurisdiction to hear the dispute on the alleged breach by the Kingdom of Spain of obligations derived from section (1) of Article 10 of the ECT through the creation of the Tax on the Value of Production of Electrical Energy (TVPEE) by Act 15/2012, of 27 December 2012, on fiscal measures for energy sustainability (Act 15/2012) [20].

105. This lack of jurisdiction of the Arbitral Tribunal is due to the fact that the Kingdom of Spain has not given its consent to submit such dispute to arbitration.

106. In this regard, the Contracting Parties of the ECT, among which is the Kingdom of Spain, have only consented to submit to investment arbitration alleged breaches of obligations derived from Part III of the ECT, pursuant to Article 26 of the ECT.

20. Act 15/2012, of 27 December, regarding fiscal measures for energy sustainability. R-0003

107. As we shall see, according to Article 21 of the ECT, section (1) of Article 10 of the ECT invoked by the Claimants, although located in Part III of the ECT, does not generate obligations with respect to taxation measures of the Contracting Parties.

(2) Taxation measures disputed by the Claimants: the TVPEE

108. In their Request for Arbitration[21] and Memorial on the Merits[22], the Claimants include the following taxation measure among the disputed measures: the TVPEE introduced by Act 15/2012[23].

109. Act 15/2012, which introduced among other taxes the TVPEE, entered into force on 1 January 2013[24].

110. The TVPEE is levied on the performance of the activities of production and incorporation into the electricity system of electrical energy within the Spanish electrical system. The TVPEE is a tax of general application, that is, it applies to the production of all generation facilities, both renewable and conventional.[25]

111. The tax base of the TVPEE consists of the total amount that the taxpayer is to receive for the production and incorporation into the electricity system of electrical energy, measured in power plant busbars, at each installation, in the taxable period.[26]

112. The applicable tax rate is 7%.[27]

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21. Request for Arbitration, of 16 April 2015, paragraphs 41, 42 and 64.
22. Memorial on the Merits, of 3 March 2016, paragraphs 19 and 408 to 463.
23. The TVPEE is regulated by articles 1 to 11 of Act 15/2012. R-0003
Act 15/2012, Final Provision Five:
"Final Provision Five Entry into force.
This Act shall come into force on 1 January 2013." R-0003

[25] The TVPEE is regulated by articles 1 to 11 of Act 15/2012. Article 1 of Act 15/2012 refers ot the nature of the TVPEE:
"Article 1 Nature
The tax on the value of the production of electrical energy is a tax of direct character and real nature that taxes the performance of activities of production and incorporation into the electric system of electric energy, measured at power plant busbars, through each of the installations indicated in Article 4 of this Act." R-0003.
Article 4 of Act 15/2012 regulates the taxable event of the TVPEE:
"Article 4 Taxable event
1. The taxable event is constituted by the production and incorporation into the electricity system of electrical energy, measured at power plant busbars, including the peninsula electricity system and island and extra-peninsula territories, at any of the facilities referred to by Title IV of Law 54/1997, of 27 November, on the Electricity Sector". R-0003
Article 5 of Act 15/2012 regulates TVPEE taxpayers:
"Article 5. Taxpayers
Individuals and legal persons, and entities referred to in article 35(4) of Act 58/2003, of 17 December, on General Taxation, conducting the activities stated in article 4, are taxpayers of the tax." R-0003

[26] Article 6 of Act 15/2012 regulates the tax base of the TVPEE:
"Article 6 Tax base
1. The tax base consists of the total amount that the taxpayer is to receive for the production and its incorporation into the electricity system of electrical energy, measured in power plant busbars, at each installation, in the taxable period. […]" R-0003

[27] Article 8 of Act 15/2012 regulates the tax rate of the TVPEE:

113. The taxable period will generally coincide with the natural year and the TVPEE will accrue on the last day of the taxable period.[28]

114. According to the Claimants, the introduction of the TVPEE allegedly implies a breach by the Kingdom of Spain of its obligations under section (1) of Article 10 of the ECT. In particular, according to the Claimants[29], the creation of the TVPEE would have supposedly breached the following standards of protection included in section (1) of Article 10 of the ECT:

- Fair and Equitable treatment.
- Constant Protection and Security.
- Not to impair, in any way, by unreasonable or discriminatory measures the management, maintenance, use, enjoyment or disposal of the investments.
- To observe any obligations entered into with an investor or an investment (umbrella clause).

115. As analysed below, the Claimants are mistaken in their approach since, according to Article 21 of the ECT, section (1) of Article 10 of the ECT does not generate any type of obligation for the Contracting Parties, nor correlative rights for the investors, with respect to taxation measures of the Contracting Parties. Therefore, there is no possible alleged breach of obligations derived from section (1) of Article 10 of the ECT through the introduction of the TVPEE that enables the Claimants to submit such matter to the Arbitral Tribunal.

(3) The Kingdom of Spain has only consented to submit to investment arbitration disputes related to alleged breaches of obligations derived from Part III of the ECT, pursuant to Article 26 of the ECT

116. It is usual for the signing States of international Treaties on reciprocal protection of investments, whether bilateral or multinational, to envisage the possibility of resorting to arbitration to resolve controversies that derive from these treaties. It is also usual for those signing States to delimit in those Treaties, as is the case of the ECT, the scope of their consent for resorting to arbitration.

117. The Arbitral Tribunal for the matter *ST-AD GmbH v. Republic of Bulgaria*, clearly indicated this idea:

> *"At the outset, the Tribunal wants to restate that it is of the utmost importance not to forget that no participant in the international community, be it a State, an international organisation or a physical or a legal person, has an inherent right of access to a jurisdictional recourse. For such right to come into existence, specific*

"Article 8 Tax rate
The Tax will be levied at a rate of 7 percent." R-0003

[28] Article 7 of Act 15/2012 regulates the taxable period and the accrual of the TVPEE:
"Article 7 Taxable period and accrual
1. The taxable period shall coincide with the calendar year, with the exception of the case that the taxpayer ceases activity at the facilities during the financial year, in which case it shall end on the day that the termination is understood to have occurred.
2. The tax shall accrue on the last day of the taxable period." R-0003

[29] Memorial on the Merits, of 3 March 2016, paragraphs 454 and 684.

> *consent has to be given. As far as investment arbitration is concerned, such consent can be given in a contract, a domestic law or an international bilateral or multilateral treaty. In all these different hypotheses, the State can shape its consent as it sees fit by providing the conditions under which it is given – in other words, the conditions subject to which an "offer to arbitrate" is made to the foreign investors."*[30] *(emphasis added)*

118. In the particular case of the ECT, Article 26 of the ECT grants the investor the possibility of resorting to arbitration in the case of alleged breach by a Contracting Party of an obligation derived from Part III of the ECT:

> *"Article 26. Settlement of disputes between an investor and a contracting party*
>
> *1. Disputes between a Contracting Party and an Investor of another Contracting Party relating to an Investment of the latter in the Area of the former, which concern an alleged breach of an* ***obligation of the former under Part III*** *shall, if possible, be settled amicably.[.*
>
> *2. If these disputes cannot be resolved pursuant to the provisions of section 1, with a period of three months counted from the date on which any of the conflicting parties requests an amicable solution, the affected investor may opt to submit a dispute for solution: […]*
>
> *c) Pursuant to the following sections of this article.* [referring to arbitration or international reconciliation] *[…]"*[31] *(emphasis added)*

119. That is to say, in the field of the ECT the Contracting Parties, among them the Kingdom of Spain, have only given their consent to submit to arbitration disputes with an investor relating to alleged breaches of obligations derived from Part III of the ECT.

120. In view of the cited Article 26 of the ECT, there is no doubt that if no obligation derived from Part III of the ECT exists, there cannot be an alleged breach of it and thus, there is no consent of the Contracting Party to resort to arbitration, Arbitral Tribunals therefore lacking jurisdiction to hear the matter.

121. This is precisely what occurs in this case regarding the TVPEE. There cannot be an alleged breach of obligations that legitimises resorting to arbitration simply because there is no obligation with respect to taxation measures, in this case, the TVPEE.

122. As analysed below, section (1) of Article 10 of the ECT, on which the Claimants try to base their claims, despite being located in Part III of the ECT, does not generate any obligation with respect to taxation measures of the Contracting Parties. For this reason, there can be no alleged breach of obligations derived from that section through the adoption by the Kingdom of Spain of taxation measures, in particular, through the introduction of the TVPEE. As a consequence, we are facing a dispute on which the Kingdom of Spain has not given its consent to submit to arbitration.

ST-AD GmbH v. Republic of Bulgaria, UNCITRAL, PCA Case No. 2011-06. Award on Jurisdiction of 18 July 2013, paragraph 337. RL-0044.

[31] ECT, Article 26(1). RL-0006.

(4) Section (1) of Article 10 of the ECT does not generate obligations for Contracting Parties with respect to taxation measures, according to Article 21 of the ECT

(4.1) The ECT does not generate obligations or rights with respect to taxation measures of the Contracting Parties, with certain stipulated exceptions

123. The ECT does not impose obligations or create rights with regard to taxation measures of the Contracting Parties, with certain exceptions expressly stipulated in Article 21 of the ECT. This is set out in Article 21 of the ECT itself, on taxation, which clearly provides the following in its section 1:

> *"Article 21. Taxation.*
>
> *1. Except as otherwise provided in this Article, nothing in this Treaty shall create rights or impose obligations with respect to Taxation Measures of the Contracting Parties. In the event of any inconsistency between this Article and any other provision of the Treaty, this Article shall prevail to the extent of the inconsistency."*[32] *(emphasis added)*

124. That is to say, Article 21 of the ECT is clear and express when it states that:

- The ECT does not include any provision that creates rights or imposes obligations with respect to taxation measures of the Contracting Parties, with certain exceptions stated in Article 21 of the ECT itself. That is, Article 21 of the ECT contains a general exclusion of taxation measures from the scope of application of the ECT (*taxation carve-out*) which only presents certain exceptions (*claw backs*) expressly stipulated in such Article 21.

- In the case of conflict between Article 21 of the ECT and any other Article of the ECT, the Contracting Parties give priority to the cited Article 21.

125. Regarding what those exceptions are, Article 21 itself sets out in its sections (2) to (5) the Articles or sections of Articles of the ECT that do apply to taxation measures of the Contracting Parties. Those Articles or sections of Articles mentioned in Article 21 are, therefore, the only ones that do generate obligations to the Contracting Parties with respect to taxation measures.

126. In this sense, sections (2) to (5) of Article 21 ECT provide the following:

> *"2. Section 3 of article 7 shall apply to Taxation Measures other than those on income or on capital, except that such provision shall not apply to: [...]*
>
> *3. Article 10(2) and (7) shall apply to Taxation Measures of the Contracting Parties other than those on income or on capital, except that such provisions shall not apply to:[...]*
>
> *4. Article 29(2) to (6) shall apply to Taxation Measures other than those on income or on capital.*

[32] ECT, Article 21(1). RL-0006.

5. a) Article 13 shall apply to taxes." [33]

127. The wording of the cited Article 21 of the ECT is absolutely clear: the ECT excludes taxation measures of the Contracting Parties from its scope of application, with the only exceptions expressly stipulated in sections (2) to (5) of the cited article 21.

128. This is recognised by the Secretariat of the Energy Charter itself in its document "*The Energy Charter Treaty. A Reader´s guide*":

> *"The issue of taxation has great significance both for the private economic agents in the energy sector and the involved states. While foreign companies have a keen interest that they are not fiscally discriminated, host countries may wish to retain some discretion concerning their tax treatment. In an international context, the issue is primarily and most commonly dealt with in bilateral agreements on the avoidance of double taxation.*
>
> *The ECT confirms the priority of the latter agreements and seeks to avoid a potential conflict with them. Accordingly, Article 21 excludes taxation matters, in principle, from the scope of application of the agreement. However, this carve-out of taxation issues does not affect the application of the principle of non-discrimination as included in agreements on the avoidance of double taxation existing among ECT CPs.*
>
> *Article 21 does not entirely exclude taxation matters:*
>
> *According to Article 21 (2),(3), the principle of non-discrimination in transit and investment matters shall apply to taxation measures other than those on income and capital. […]*
>
> *Pursuant to Article 21 (4), the ECT covers taxation matters in trade with the exception of income or capital taxes.*
>
> *According to Article 21 (5), the provision on expropriation (Article 13) applies to taxes. A foreign investor may therefore claim that a tax measure has expropriatory effects."*[34] *(emphasis added)*

129. This meaning of Article 21 of the ECT is totally peaceful, and we can also mention in this same sense that indicated by the Tribunal in *Plama Consortium Limited v. Republic of Bulgaria*, which stated the following:

> *"The Arbitral Tribunal cannot see how this claim gives rise to a violation of Bulgaria's obligations under the ECT. In the first place, Article 21 of the ECT specifically excludes from the scope of the ECT's protections taxation measures of a Contracting State, with certain exceptions, […]."*[35] *(emphasis added)*

[33] ECT, Article 21, sections (2) to (5). RL-0006.
[34] *The Energy Charter Treaty: A Reader´s Guide*, Energy Charter Secretariat, pages 38 and 39. RL-0053.
[35] *Plama Consortium Limited v. the Republic of Bulgaria*, ICSID case No. ARB/03/24. Award of 27 August 2008, paragraph 266. RL-0034.

130. Thus, there is no doubt that taxation measures of the Contracting Parties are excluded from the scope of protection of the ECT, with the only exceptions stipulated in Article 21 of the ECT.

(4.2) Section (1) of Article 10 of the ECT is not among those stipulated exceptions. Therefore, section (1) of Article 10 of the ECT does not generate obligations with respect to taxation measures of the Contracting Parties

131. None of the exceptions stipulated in Article 21 of the ECT by which taxation measures are included in the scope of protection of the ECT comprises section (1) of Article 10 of the ECT. That is, according to Article 21 of the ECT, it is clear that section (1) of Article 10 of the ECT on which the Claimants try to base their pretensions, does not impose any obligations for the Contracting Parties with respect to taxation measures.

132. The only sections of Article 10 that do apply, if the case, to taxation measures of the Contracting Parties are sections (2) and (7), sections on which the Claimants do not base any of the claims in their Memorial on the Merits. This is clearly established in Article 21 of the ECT:

> *"1. Except as otherwise provided in this article, nothing in this Treaty shall create rights or impose obligations with respect to taxation measures of the Contracting Parties. [..]*
>
> *3. Sections 2 and 7 of article 10 shall apply to Taxation Measures of the Contracting Parties other than those on income or on capital, except that such provisions shall not apply to: […]."*[36] *(emphasis added)*

133. Apart from such mention to the application of sections (2) and (7) of Article 10 of the ECT to certain taxation measures, Article 21 of the ECT does not contain any additional mention that any other section of Article 10 of the ECT applies to taxation measures.

134. As a consequence, section (1) of Article 10 of the ECT, invoked by the Claimants, is not applicable to taxation measures of the Contracting Parties. Therefore, with respect to taxation measures of the Contracting Parties, section (1) of Article 10 of the ECT does not impose any obligation on the Contracting Parties nor does it generate any correlative right for the investors.

135. We should recall that, in this arbitration, the Claimants allege that the introduction of the TVPEE by Act 15/2012 represents a breach of two provisions of the ECT[37]:

- section (1) of Article 10 of the ECT, and
- Article 13 of the ECT, on expropriation.

136. For the avoidance of doubt, the Kingdom of Spain would like to emphasise that the present Jurisdictional Objection only makes reference to the claim of the Claimants

[36] ECT, Article 21. RL-0006.
[37] Memorial on the Merits, paragraph 454.

regarding the TVPEE with respect to section (1) of Article 10 of the ECT, not with respect to Article 13 of the ECT.

137. Pursuant to the cited sections (1) and (5) of Article 21 of the ECT, Article 13 of the ECT does create obligations with respect to taxes.[38] Therefore, the Arbitral Tribunal does hold jurisdiction to hear an alleged breach by the Kingdom of Spain of Article 13 of the ECT, on expropriation, through the introduction of the TVPEE. In any case, from this moment and as will be analysed in this submission, the Kingdom of Spain firmly denies that the TVPEE is expropriatory and that it represents a breach of Article 13 of the ECT.

138. Furthermore, it should be noted that, according to Article 21(5)(b) of the ECT, when an investor alleges that a tax is expropriatory, or that the tax that alleged to be expropriatory is discriminatory, the investor has the obligation to refer the issue to the competent tax authorities, so that they may rule on the matter within a maximum period of 6 months, before being able to submit the issue to arbitration. There is knowledge that the Claimants have referred the issue of whether or not the TVPEE is expropriatory or discriminatory to the General Directorate of Taxes of the Spanish Ministry of Finance and Public Administrations.

(5) The provisions relating to the TVPEE of Act 15/2012 are a taxation measure for the purposes of the ECT

139. As analysed below, the provisions relating to the TVPEE of Act 15/2012 are considered as a taxation measure for the purposes of the ECT.

(5.1) According to Article 21(7) of the ECT, the term "taxation measure" includes any provision relating to taxes of the domestic law of the Contracting Party

140. Article 21 of the ECT itself, on taxation, makes reference to what is to be understood as a "taxation measure" for the purposes of the said Article 21. Thus, section (7)(a)(i) of Article 21 of the ECT states that the term "taxation measure" includes any provision relating to taxes of the domestic law of the Contracting Party:

> *"7. For the purposes of this Article:*
>
> *a) The term "Taxation measure" includes:*
>
> *i) **Any provision relating to taxes of the domestic law of the Contracting Party** or of a political subdivision thereof or a local authority therein;*
>
> *ii) any provision relating to taxes of any convention for the avoidance of double taxation or of any other international agreement or arrangement by which the Contracting Party is bound."*[39] *(emphasis added)*

[38] ECT, Article 21(1) and (5):"1. Except as otherwise provided in this article, nothing in this Treaty shall create rights or impose obligations with respect to taxation measures of the Contracting Parties. [..] 5. a) Article 13 shall apply to taxes." RL-0006.
[39] ECT, Article 21(7)(a). RL-0006.

141. In view of the aforementioned Article 21(7)(a)(i) of the ECT, the following question should be raised: what is the applicable law to determine whether we stand before provisions relating to taxes? When faced with this question, there could be two interpretations: understanding that the applicable law for determining whether we stand before provisions relating to taxes should be the domestic law of the Contracting Party, or understanding that it should be international Law.

142. With regard to the first interpretation, there are several reasons to consider that the Law governing the determination of whether certain provisions are provisions relating to taxes should be the domestic Law of the Contracting Party.

143. The first reason is the text of the cited Article 21(7)(a)(i) of the ECT itself. From the ordinary sense of its terms it can be understood that this Article includes a referral to the domestic legislation of the Contracting Party for the purposes of determining whether we stand before provisions relating to taxes:

> *"i) Any provision relating to taxes* ***of*** *the domestic law of the Contracting Party,[...][40] (emphasis added)*

144. Arbitration case law has acknowledged the possibility that international investment treaties can define a certain term by reference to the domestic law of a Contracting Party. In this sense, the Arbitral Tribunal of the *Saipem v. Bangladesh* case can be cited, which acknowledges such a possibility, although it does not occur in that case:

> *"in the absence of any indication that the contracting states intended to refer to 'property' as a notion of Bangladeshi law, the Tribunal cannot depart from the general rule that treaties are to be interpreted by reference to international law."*[41] *(emphasis added)*

145. *The Oxford Handbook of International Investment Law* also acknowledges the possibility that international treaties contain explicit references to domestic Law:

> *"While treaty claims are obviously to be decided on the basis of international law, national law still has a role to play. […] Some of the facts on the basis of which to resolve international claims have been produced by, and may only be assessed by applying, national law […]. Examples of such 'preliminary' or 'incidental' questions governed by national law are whether an investment is valid, or a contract has been concluded […]. Further examples may, depending on the exact claim, comprise such issues as […] taxation, […]. Also, a treaty may make express reference to national law."*[42] *(emphasis added) (footnotes omitted)*

146. Another reason to interpret that Article 21(7)(a)(i) of the ECT refers to domestic law to determine whether we stand before provisions relating to taxes, is the referral to domestic law contained in the Agreement to avoid double taxation between Spain and Germany, the

[40] ECT, Article 21(7)(a). RL-0006.
[41] *Saipem S.p.A. v. Popular Republic of Bangladesh*, ICSID case No. ARB/05/07, Decision on Jurisdiction and Recomendation on Provisional Measures dated 21 March 2007, paragraph 82. RL-0029.
[42] *The Oxford Handbook of International Investment Law*, Muchlinski, Ortino and Schreuer, Oxford University Press, pages 110, 111 and 112. RL-0066.

country of the Claimants. Thus, Article 3 of this Agreement to avoid double taxation provides that:

> *"2. As regards the application of the Agreement at any time by a Contracting State, any term not defined therein shall, unless the context otherwise requires, have the meaning that it has at the time under the law of that State for the purposes of the taxes to which the agreement applies, any meaning under the applicable tax laws of that State prevailing over a meaning given to the term under other laws of that State."*[43] *(emphasis added)*

147. Note that the Agreement to avoid double taxation between Spain and Germany is an international treaty in force between the Respondent and the State of the Claimants. Therefore, this Agreement must be taken into consideration pursuant to Article 31(3)(c) of the Vienna Convention, which states, regarding the interpretation of international treaties, that:

> *"3. There shall be taken into account, together with the context: [...] c) any relevant form of international law applicable in the relations between the parties."*[44]

148. Lastly, it should be taken into account that, under the scope of other international investment treaties other than the ECT, it may be necessary to refer to international law to define the concept of a taxation measure given that the Treaties themselves do not include a provision such as that contained in Article 21(7)(a)(i) of the ECT. For example, Article 2103 of NAFTA[45] also includes a general taxation carve-out (with certain exceptions) with regard to taxation measures, by such Treaty makes no reference to what is understood by "taxation measure", as the ECT does.

149. On the other hand, a second interpretation of Article 21(7)(a)(i) of the ECT implies understanding that, in order to consider that we stand before provisions relating to taxes, it is necessary to refer to international Law. This can be argued based on the provisions of Article 26(6) of the ECT, which provides the following:

> *"By virtue of section 4) a tribunal will be created that will rule on any disputed issues, in accordance with this Treaty and the applicable rules of International Law."*[46]

150. The Kingdom of Spain particularly shares the first of the stated interpretations of Article 21(7)(a)(i) of the ECT. However, in terms of the interests of this arbitration, either of the two stated interpretations of Article 21(7)(a)(i) of the ECT leads us to conclude that the TVPEE is a tax.

151. In short, as explained, Article 21(7)(a)(i) of the ECT states that the term "taxation measure" includes any provision relating to taxes of the domestic law of the Contracting

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[43] Agreement between the Kingdom of Spain and the Federal Republic of Germany to avoid double taxation and prevent tax evasion regarding taxation of income and capital, done in Madrid on 3 February 2011 and published in the Official State Gazette on 30 July 2012. Article 3(2). R-0004.
[44] Vienna Convention. RL-0010.
[45] Article 2103 of the NAFTA. https://www.nafta-sec-alena.org/Home/Legal-Texts/North-American-Free-Trade-Agreement. RL-0011.
[46] Article 26(6) of the ECT. RL-0006.

Party. As we will analyse below, Act 15/2012 is part of the domestic law of the Kingdom of Spain, and the provisions relating to the TVPEE of Act 15/2012 are in any case provisions relating to taxes, both if we use a concept of tax of the Kingdom of Spain's domestic law and if we use a concept of tax of international law.

152. Therefore, there is no doubt that provisions relating to the TVPEE of Act 15/2012 are a taxation measure for the purposes of the ECT.

(5.2) Act 15/2012 is part of the domestic law of the Kingdom of Spain

153. Firstly, Act 15/2012 is part of the domestic law of the Kingdom of Spain. In particular, Act 15/2012 is a domestic law passed by the Parliament of the Kingdom of Spain (comprised of the Congress of Deputies and the Senate) in accordance with the ordinary legislative procedure provided for in the Spanish Constitution and the rest of the Spanish legal system.[47]

154. In this respect, the Spanish Constitution provides in its Article 66 that:

> *"1. The Parliament represents the Spanish people and shall consist of the Congress of Deputies and the Senate.*
>
> *2. The Parliament exercises the legislative power of the State, [...]."*[48]

155. Moreover, Act 15/2012 that introduces the TVPEE was passed in accordance with Article 133 of the Spanish Constitution, which grants the State the original authority to establish taxes, by law. In this sense, Article 133(1) of the Spanish Constitution provides that:

> *"1. The original power to establish taxes corresponds exclusively to the State, by law."*[49]

(5.3) The provisions on the TVPEE of Act 15/2012 are provisions relating to a tax

156. Secondly, as we will analyse below, the TVPEE is a tax both under the domestic law of the Kingdom of Spain, and under international law.

157. Therefore, provisions relating to the TVPEE of Act 15/2012 are provisions relating to taxes, both under the Respondent's domestic law and under international law.

(a) The TVPEE is a tax according to the Domestic Law of the Kingdom of Spain

158. From the perspective of the domestic law of the Kingdom of Spain, there is no doubt that the TVPEE is a tax. The Spanish Constitutional Court itself has ratified the nature of the TVPEE as a tax, as well as its compliance with the Spanish Constitution.

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[47] The procedure of processing and approval of Act 15/2012 by the Spanish Congress of Deputies and the Senate is public and can be consulted in detail on the website of the Congress of Deputies and of the Senate. R-0005.

[48] Spanish Constitution of 1978 (consolidated version), Article 66. R-0006.

[49] Spanish Constitution of 1978 (consolidated version), Article 133(1). (R-0006). Act 58/2003, of 17 December, on General Taxation, provides the same when stating in its Article 4 that *"1. The original power to establish taxes corresponds exclusively to the State, by means of law. [...]".* R-0007.

159. In this regard, Act 15/2012 is clear about the taxation nature of the TVPEE. According to Act 15/2012, the TVPEE is a direct tax levied on the performance of the activities of production and incorporation into the electricity system of electrical energy within the Spanish electrical system. In this regard, Article 1 of Act 15/2012 provides the following:

> *"Article 1 Nature*
>
> *The tax on the value of the production of electrical energy is a tax of direct character and real nature that taxes the performance of activities of production and incorporation into the electric system of electric energy, measured in power plant busbars, through each of the installations indicated in Article 4 of this Act."*[50] *(emphasis added)*

160. The concept of tax and its different types (imposts, fees and special contributions) under Spanish Law is set out in Article 2 of Act 58/2003, of 17 December, on General Taxation:

> *"Article 2 Concept, purposes and classes of taxes*
>
> *1. Taxes are public incomes that consist of monetary contributions required by a public Administration as a consequence of the performance of an act to which the law connects the duty to contribute, with the primary purpose of obtaining the necessary income to finance public spending.*
>
> *As well as being a means to obtain the resources needed to support public spending, taxes may also serve as instruments of general economic policy and attend to the compliance with the principles and purposes contained in the Constitution.*
>
> *2. Taxes, whatever its denomination, are classified in fees, special contributions and imposts: [...]*
>
> *c) Imposts are taxes required without compensation, whose taxable event is made up of deals, acts or events that show the economic capacity of the taxpayer."*[51]

161. As we have indicated previously, the TVPEE applies to the production of all installations for electricity production, both renewable and conventional. The tax base of the TVPEE consists of the total amount that the taxpayer is to receive for the production and incorporation into the electricity system of electrical energy, measured in power plant busbars, at each installation, in the taxable period. The applicable tax rate is 7%. The taxable period will generally coincide with the natural year and the TVPEE is accrued on the last day of the taxable period.

162. The self-assessment and payment to the Public Treasury of the TVPEE is made through Form 583 "Tax on the value of production of electrical energy. Self-assessment and part payments".[52] Form 583 was approved by Ministerial Order HAP/703/2013, of 29 April

[50] Act 15/2012, Article 1. R-0003
[51] Act 58/2003, of 17 December, on General Taxation, Article 2. R-0007.
[52] Website of the State Tax Administration Agency where information is provided about Form 583 and where it can be submitted electronically. R-0008. https://www.agenciatributaria.gob.es/AEAT.sede/procedimientoini/DR01.shtml

2013, which also establishes the form and procedure for its presentation (hereinafter "**Ministerial Order HAP/703/2013**").[53]

163. It should also be noted that the Spanish National High Court has declared that this Ministerial Order HAP/703/2013 is in accordance with the law.[54]

164. The taxation nature of the TVPEE has also been recognised by organisations such as the Institute of Accounting and Accounts Auditing (ICAC)[55], which, upon analysing the accounting treatment of the TVPEE, established in a consultation in June 2013 that:

> *"The tax on the value of the production of electrical energy is a tax of a direct character and real nature [...], and should be recorded as an expenses on the losses and gains account; account 631 Other taxation may be used for this purpose."*[56]

165. Furthermore, it should be considered that, according to Spanish law, the TVPEE is a Corporations Tax deductible expense for taxpayers taxed by the TVPEE.

166. In this regard, as stated by the aforementioned ICAC, taxpayers must record the TVPEE as an expense on their accounts. This accounting expense corresponding to the TVPEE is tax deductible from the Corporations Tax of taxpayers. In this sense, Article 15 of Act 27/2014, of 27 November, on the Corporations Tax, sets ou the expenses that are not considered as tax deductible expenses. Expenses corresponding to the TVPEE do not fit in any of those non-deductible expenses categories and, therefore, are considered as tax deductible expenses for Corporations Tax purposes.[57]

167. This tax deductible nature of the TVPEE accounting expense according to Spanish Law has been confirmed by the General Directorate of Taxes[58] of the Kingdom of Spain. Thus, in a reply dated 23 December 2014 to a written taxation query that was received, the General Directorate of Taxes stated the following:

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[53] Order HAP/703/2013, of 29 April, which approves Form 583 "Tax on the Value of the Production of Electrical Energy. Self-assessment and Instalment Payments", and establishing the manner and procedure for its submission. R-0009.

[54] The Spanish National High Court has dismissed several contentious-administrative appeals brought against Ministerial Order HAP/703/2013, of 29 April 2013, and has declared that this Order is legal. In this sense, the following Rulings of the National High Court can be cited: i) National High Court ruling, of 2 June 2014, dismissing contentious-administrative appeal 297/2013 (R-0010.), ii) National High Court Ruling, of 2 June 2014, dismissing contentious-administrative appeal 298/2013 (R-0011), and iii) National High Court ruling, of 30 June 2014, dismissing contentious-administrative appeal 296/2013 (R-0012).

[55] The Institute of Accounting and Accounts Auditing (ICAC) is an Autonomous Organism of the Spanish State Administration, adscribed to the Ministry of Economy and Competitiveness. Its functions include answering queries made to it regarding the application of rules contained in the applicable financial reporting regulatory framework, and the regulatory framework of the accounts auditor activity. R-0013.

[56] Query 1, ICAC Official Gazette 94/June 2013. R-0014.

[57] Act 27/2014 of 27 November, on Corporations Tax, Article 15. R-0015.

[58] The General Directorate of Taxes is an organ of the Kingdom of Spain's Ministry of Finance and Public Administrations, whose functions include the interpretation of tax legal provisions by, among other ways, answering the written taxation queries that it receives. Website of the Ministry of Finance and Public Administrations that makes reference to the structure and functions of the General Directorate of Taxes. R-0016.

> *"The consulting party asks whether the self-assessed amount as "Tax on the value of the production of electrical energy", through the submission of form 583, is considered as a tax deductible expense, in the electrical energy production activity (epigraph 151.4), both for the Corporations Tax taxpayer, as well as in the directly estimated calculation of the profit of the activity, for Individual Income Tax taxpayers. [...] to the extent that Corporations Tax regulations do not contain any specific provision relating to the Tax on the value of the production of electrical energy, [we will resort to [...] its accounting treatment, [...] In conclusion, the taxpayer of the tax on the value of the production of electrical energy must register in its accounts an expense corresponding to it, on the month of November of each year;* ***this expense will be tax deductible*** *in the accounting taxable period.[...]"*[59] *(emphasis added)*

(i) The Spanish Constitutional Court has ratified the taxation nature of the TVPEE and its conformity with the Spanish Constitution

168. The Spanish Constitutional Court itself has ratified the tax nature of the TVPEE and its legality.

169. In this regard, the Spanish Constitutional Court, the supreme body for interpretation of the Spanish Constitution[60], through its Ruling of 6 November 2014, has dismissed unconstitutionality appeal number 1780-2013 submitted to it against the TVPEE, particularly against articles 4, 5 and 8 of Act 15/2012, relating respectively to the taxable event, taxpayers and the tax rate of the TVPEE.

170. In paragraph 635 of their Memorial on the Merits, the Claimants make reference to the aforementioned unconstitutionality appeal. However, they remain completely silent on the aforementioned Ruling of 6 November 2014, through which the Spanish Constitutional Court dismissed the appeal.

171. In the aforementioned Ruling of 6 November 2014, the Spanish Consitutional Court declared that the said TVPEE regulation contained in Act 15/2012 is perfectly valid and in accordance with the Spanish Constitution.[61]

172. Therefore, there is no doubt that the TVPEE is a tax under Spanish law.

(b) The TVPEE is a tax according to international law

173. Furthermore, even from the perspective of the international law, there is no doubt that the TVPEE is a tax.

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[59] Answer from the General Directorate of Taxes on 23 December 2014 to Binding Taxation Query V3371-14. R-0017.

[60] Organic Act 2/1979 of 3 October, on the Constitutional Court, Article one:
"Article one
1. The Constitutional Court, as the supreme body for interpretation of the Constitution, is independent from other consitutional bodies and its only subject to the Constitution and this Organic Act.
2. Its order is unique and its jurisdiction extends throughout Spanish territory." R-0018.

[61] Judgement 183/2014 of 6 November 2014 from the Plenary Session of the Constitutional Court in constitutional challenge number 1780-2013 promoted by the Council of Government of the Autonomous Government of Andalusia in relation to articles 4, 5 and 8 of Act 15/2012 (and other regulations), published in the Official State Gazette on 4 December 2014. R-0019.

174. In this regard, as we will see below, the TVPEE is a tax according to the concept of tax of international law used by arbitral case-law. In addition, the European Commission has ratified the taxation nature of the TVPEE and its compliance with EU Law.

(i) The TVPEE is a tax according to the concept of tax of international law used by arbitral case law

175. If we use a concept of "tax" of international law, especially the concept that Arbitral Tribunals have repeatedly applied, it can be observed that there is no doubt that the TVPEE is a tax.

176. *Black´s Law Dictionary* contains the following definition of a tax:

> *"**tax**, n. (14c) A charge, usu. monetary, imposed by the government on persons, entities, transactions, or property to yield public revenue. […]"*[62]

177. It should be noted that this ordinary concept of a tax is substantially the same as the concept included in Spanish Law in Article 2 of Act 58/2003, of 17 December, on General Taxation -in essence, a mandatory contribution to the Public Treasury-.[63]

178. Arbitral Tribunals have ruled repeatedly along the same lines as *Black's Law Dictionary*.

179. The Arbitral Tribunal of the *EnCana v. Ecuador* case made reference to the meaning of the term "taxation measures", which was not defined in the Canada-Ecuador BIT applicable in that case, stating the following:

> *"It is in the nature of a tax that it is imposed by law.[…]The question whether something is a tax measure is primarily a question of its legal operation, not its economic effect. A taxation law is one which imposes a liability on classes of persons to pay money to the State for public purposes. The economic impacts or effects of tax measures may be unclear and debatable; nonetheless a measure is a taxation measure if it is part of the regime for the imposition of a tax.[…]"*[64] *(emphasis added)*

180. The opinion of this Arbitral Tribunal was welcomed by the Arbitral Tribunal of the *Duke Energy v. Ecuador* case, which, when making reference to the concept of "matters of

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[62] *Black´s Law Dictionary*, Ninth Edition, Bryan A. Garner Editor in Chief, page 1594. RL-0025.

[63] Article 2 of Act 58/2003, of 17 December, on General Taxation:
"Article 2
Concept, purposes and classes of taxes
1. Taxes are public incomes that consist of monetary contributions required by a public Administration as a consequence of the performance of an act to which the law connects the duty to contribute, with the primary purpose of obtaining the necessary income to finance public spending.As well as being a means to obtain the resources needed to support public spending, taxes may also serve as instruments of general economic policy and attend to the compliance with the principles and purposes contained in the Constitution.
2. Taxes, whatever their denomination, are classified in fees, special contributions and imposts: […]c) Imposts are taxes required without compensation, whose taxable event is made up of deals, acts or events that show the economic capacity of the taxpayer." R-0007.

[64] *EnCana Corporation v. Republic of Ecuador*, LCIA Case No. UN 3481, Award of 3 February 2006, paragraph 142. RL-0027.

taxation" mentioned in Article X of the United States-Ecuador BIT and not defined by that BIT, stated the following:

> *"The Treaty does not define the term "matters of taxation". In seeking to elucidate its meaning, the ruling in EnCana v. Ecuador appears to be of particular relevance."*[65]

181. Along these lines, the Arbitral Tribunal for the matter of *Burlington Resources v. Ecuador*, also when making reference to the concept of "matters of taxation", provided the following:

> *"To answer the question whether Law 42 is a tax for purposes of Article X of the Treaty under international law, the Tribunal finds that the EnCana and Duke Energy decisions are indeed apposite. In EnCana, the tribunal held that a "tax" is "imposed by law" and that this "taxation law is one which imposes a liability on classes of persons to pay money to the State for public purposes." In Duke Energy, the tribunal, dealing with the Treaty applicable to this dispute, held that "the ruling in EnCana v. Ecuador appears to be of particular relevance" to elucidate the meaning of "matters of taxation" under Article X of the Treaty.*
>
> *Building on EnCana's ruling, Duke Energy stands for the proposition that there is "tax" under Article X of the Treaty if the following four requirements are met: (i) there is a law (ii) that imposes a liability on classes of persons (iii) to pay money to the State (iv) for public purposes. Under this definition, the Tribunal is of the view that Law 42 is a tax."*[66] *(emphasis added)*

182. In view of all of the above decisions, the concept of tax in international law repeatedly used by Arbitral Tribunals has a series of defining characteristics that can be summarised as follows:

- The tax is established by law,
- That law imposes an obligation on a class of people, and
- That obligation involves paying money to the State for public purposes.

183. As can be seen below, the TVPEE meets all of these defining characteristics, so there is no doubt that we stand before a tax from the perspective of international law.

The TVPEE is established by Law

184. In first place, as has already been analysed, the TVPEE was established by Law: Act 15/2012. Act 15/2012 was approved by the Parliament of the Kingdom of Spain (Congress of Deputies and the Senate) according to article 133 of the Spanish Constitution, according to which the originary authority for setting taxes corresponds exclusively to the State, by law.

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[65] *Duke Energy Electroquil Partners & Electroquil S.A. v. Republic of Ecuador*, ICSID Case No. ARB/04/19, Award of 18 August 2008, paragraph 174. RL-0033.

[66] *Burlington Resources Inc. v. Republic of Ecuador*, ICSID Case No. ARB/08/5, Decision on Jurisdiction, 2 June 2010, paragraphs 164 and 165. RL-0036.

This law imposes an obligation on a class of people

185. Secondly, Act 15/2012 regulating the TVPEE imposes the obligation to pay this tax on a class of people. Specifically, as has also already been analysed, according to Act 15/2012 the TVPEE taxes all persons who carry out the activities of production and incorporation into the electricity system of electrical energy within the Spanish electricity system, both if the electrical energy production facilities use renewable or conventional energies.

This obligation involves paying money to the State for public purposes

186. Thirdly, Act 15/2012 imposes an obligation on TVPEE taxpayers to pay money to the State for public purposes.

187. In this regard, TVPEE taxpayers are under the obligation to make payments corresponding to this tax to the State in accordance with the provisions of Article 10 of Act 15/2012, on tax assessments and payments,[67] and with Order HAP/703/2013, of 29 April, approving Form 583 "Tax on the Value of the Production of Electrical Energy. Self-assessment and Instalment Payments", and establishing the manner and procedure for its submission.[68]

188. The TVPEE is Spanish State income. Revenue corresponding to the TVPEE is public revenue included in the Spanish General State Budget. This can be clearly appreciated in the Spanish General State Budget state for the years 2013 -the first year that the TVPEE was in force-, 2014, 2015 and 2016.

189. Thus, in the most recently approved Budget, the Spanish General State Budget for 2016, it can be seen that revenue corresponding to the TVPEE is included in these General Budgets under the Section "*State Income*" (Section 98), Chapter "*Direct taxes and social contributions*" (Chapter 1) and, within this chapter, under the item entitled "*Taxes on the production and storage of electrical energy and fuel*" (item 13), sub-item "*On the value of the production of electrical energy*" (sub-item 130)[69]:

[67] Act 15/2012, Article 10. R-0003

[68] Order HAP/703/2013, of 29 April, which approves Form 583 "Tax on the Value of the Production of Electrical Energy. Self-assessment and Instalment Payments", and establishing the manner and procedure for its submission. R-0009.

[69] Excerpt from the Spanish General State Budget for 2016. R-0020.This can be consulted on the website of the Secretariat of State for Budgets and Spending under the Ministry of Finance and Public Administrations: http://www.sepg.pap.minhap.gob.es/Presup/PGE2016Ley/MaestroDocumentos/PGE-ROM/doc/1/2/1/2/1/N_16_E_R_2_101_1_2_198_1_101_1.PDF

NATIONAL BUDGET
STATE

BUDGET YEAR
2016

Section: 98 STATE INCOME
Service: 01 STATE INCOME

(Thousands of euros)

Economic	Explanation		Total
1	DIRECT TAXES AND SOCIAL CONTRIBUTIONS		
10	Income tax		66,466,000.00
100	On Natural Persons		39,610,000.00
10000	Personal Income Tax	39,854,000.00	
10099	Tax assignment to the Catholic Church	-244,000.00	
101	On Corporations		24,868,000.00
10100	Corporations Tax	24,868,000.00	
102	On non-residents		1,988,000.00
10200	Non-residents Income Tax	1,988,000.00	
11	On capital		151,000.00
119	Other capital taxation		151,000.00
11900	General Inheritance and Gift Tax	113,000.00	
11901	Wealth tax	38,000.00	
12	Social contributions		923,000.00
120	Contributions from the special regimes for civil servants		923,000.00
12000	Pension contributions	923,000.00	
13	Tax on the production and storage of electrical energy and fuel		1,868,000.00
130	Tax on the value of the production of electrical energy.		1,627,000.00
131	On the production of spent nuclear fuel and radioactive waste resulting from the generation of nuclear energy		230,000.00
132	On the storage of spent nuclear fuel and radioactive waste in centralised facilities		7,000.00
	TOTAL DIRECT TAXES AND SOCIAL CONTRIBUTIONS		69,404,000.00
2	INDIRECT TAXES		
21	On Added Value		31,334,000.00
210	Value Added Tax		31,334,000.00
21000	VAT on imports	5,956,000.00	
21001	VAT on interior operations	25,369,000.00	
22	Excise duty		7,923,000.00
220	Special taxes		7,923,000.00
22000	On alcohol and derived beverages	361,000.00	
22001	On beer	126,000.00	
22003	On tobacco products	3,236,000.00	
22004	On hydrocarbons	3,605,000.00	

190. Similarly, TVPEE revenue is also included in the Spanish General State Budgets for the years 2013, 2014 and 2015 as State income, in the same sections that we have indicated above for the 2016 Budget.[70]

191. Thus, the TVPEE is a public income that, along with all other State incomes, contributes to constitute the State resources with which public expenditure is financed.

[70] Excerpt from the Spanish General State Budgets for 2013. R-0021.This can be consulted on the website of the Secretariat of State for Budgets and Spending of the Ministry of Finance and Public Administrations: http://www.sepg.pap.minhap.gob.es/Presup/PGE2013Ley/MaestroDocumentos/PGE-ROM/doc/1/2/1/2/1/N_13_E_R_2_101_1_2_198_1_101_1.PDF
Excerpt from the Spanish General State Budget for 2014. R-0022.This can be consulted on the website of the Secretariat of State for Budgets and Spending of the Ministry of Finance and Public Administrations: http://www.sepg.pap.minhap.gob.es/Presup/PGE2014Ley/MaestroDocumentos/PGE-ROM/doc/1/2/1/2/1/N_14_E_R_2_101_1_2_198_1_101_1.PDF
Excerpt from the Spanish General State Budget for 2015. R-0023.This can be consulted on the website of the Secretariat of State for Budgets and Spending of the Ministry of Finance and Public Administrations: http://www.sepg.pap.minhap.gob.es/Presup/PGE2015Ley/MaestroDocumentos/PGE-ROM/doc/1/2/1/2/1/N_15_E_R_2_101_1_2_198_1_101_1.PDF

192. It shluod be added that the Second Additional Provision of Act 15/2012 provides that an amount equivalent to the estimated annual collection of the State arising from the taxes included in Act 15/2012, including the TVPEE, will be allocated each year in the Laws on the Spanish General State Budgets to finance the costs of the electricity sector::

> *"Additional provision two. Costs of the electricity system.*
>
> *In the Laws of General State Budgets of each year an amount equivalent to the sum of the following will be used to finance the costs of the electricity system provided for in Article 13 of the Electricity Sector Law:*
>
> *a) The estimate of the annual collection derived from taxes and fees included in this Act.*
>
> *b) The estimated revenue from the auctioning of emission rights for greenhouse gases, with a maximum of € 500 million."*[71] *(emphasis added)*

193. This Second Additional Provision was supplemented and specified by the Fifth Additional Provision of Act 17/2012, of 27 December, on the State General Budget for the year 2013. This Fifth Additional Provision of Act 17/2012 establishes that an amount equivalent to the estimated annual collection deriving from taxes included in Act 15/2012, among which is the TVPEE, will be allocated to finance, among the costs of the electricity system provided by the Electricity Sector Law, specifically those relating to the promotion of renewable energy:

> *"Five. Contributions to Financing of the Electricity Sector*
>
> *1. In the General State Budget Acts of each year, an amount equivalent to the sum of the following will be used to finance the costs of the Electricity Sector* ***relating to the promotion of renewable energy*** *provided for in the Electricity Sector Law:*
>
> *a) The estimate of the annual collection derived from taxes included in the Act of fiscal measures for energy sustainability [Act 15/2012].*
>
> *b) 90% of the estimated income from auctioning greenhouse gas emission rights, with a maximum of EUR 450 million.*
>
> *2. 10% of the estimated income from auctioning greenhouse gas emission rights, with a maximum of EUR 50 million, is earmarked to the policy of combating climate change."*[72] *(emphasis added)*

194. It must not be forgotten that among the taxes included in Act 15/2012 to which such Fifth Additional Provision refers there is not only the TVPEE. Act 15/2012 does not only create the TVPEE. It also create three more new taxes: i) the Tax on production of spent nuclear fuel and radioactive waste from the generation of nuclear electric energy, ii) the Tax on storage of spent nuclear fuel and radioactive waste at centralised facilities, and iii) the Levy on the use of continental waters for the production of electrical energy. Thus, an

[71] Act 15/2012, Second Additional Provision. R-0003.
[72] Act 17/2012, of 27 December, on General State Budgets for 2013, Fifth Additional Provision. R-0024.

amount equivalent to the estimated annual collection derived from these three new taxes is also allocated every year in the State General Budget to fund the costs of the electricity system relating to the promotion of renewable energies.

195. The possibility of allocating State resources for specific purposes is permitted by Spanish budgetary law, specifically by Act 47/2003, of 26 November, on the General Budget, which expressly provides the following:

> *"Article 27 Principles and rules of budgetary management*
>
> *1. State public sector management is subject to the annual budget regime approved by Parliament, within the framework and limits of a multi-year scenario.[...]*
>
> *3. Resources of the State, those of each of its autonomous organisms and those of entities forming part of the State public sector with limited budget, will be allocated to financing all of their respective obligations as a whole, **unless it is established by law their allocation for specific purposes**."*[73] *(emphasis added)*

196. In short, as has been expounded, the TVPEE was established by Act 15/2012, which imposes on a class of persons the obligation to pay money to the State for public purposes.

197. Therefore, the TVPEE constitutes a tax in accordance with the international law concept of tax which has been applied repeatedly by Arbitral Tribunals.

(ii) The European Commission has ratified the taxation nature of the TVPEE and its compliance with EU Law

198. In addition, further proof that the TVPEE is a tax under international law is the fact that the European Commission has ratified the tax nature of the TVPEE and the compliance of this tax with EU Law.

199. In 2013, the European Commission initiated a procedure to request information from the Kingdom of Spain for the purpose of verify the adequacy of the TVPEE to EU Law (*EU Pilot* procedure 5526/13/TAXU). Well, the European Commission has closed this procedure, as it considers that the TVPEE complies with EU Law.

200. Such EU Pilot procedure for requesting information from the Kingdom of Spain was not initiated on the initiative of the European Commission itself, but was initiated as a result of a complaint filed with the European Commission by private individuals who alleged that the TVPEE breached EU Law. After receiving the complaint, the European Commission requested information from the Kingdom of Spain in relation to this issue.

201. After receiving the information provided by the Kingdom of Spain, the European Commission concluded that there were no reasons to consider that the TVPEE breached EU Law and, therefore, that there were no reasons to initiate the EU Law infringement

[73] Act 47/2003, of 26 November, on the General Budget, Article 27. R-0025.

procedure regulated in Article 258 of the TFEU. Consequently, the European Commission proceeded to close the aforementioned Pilot Project on 8 September 2014.[74]

202. It should be noted that an EU Pilot procedure is an information exchange process between the European Commission and an EU Member State to analyse whether a certain measure taken by that Member State complies with EU Law. The EU Pilot procedure constitutes a prior phase, if the case, to the EU Law infringement procedure regulated by Article 258 of the TFEU.

203. Thus, specifically, when a complaint is filed by citizens or companies alleging that a measure by a Member State supposedly breaches EU Law (or when the European Commission ex officio detects a possible breach of EU Law), the European Commission initiates an EU Pilot procedure. Through this EU Pilot procedure, the European Commission requests information from the corresponding Member State regarding the measure in question of said State.

204. In view of the information and observations provided by the Member State in the corresponding EU Pilot procedure, if the European Commission considers that there is reason to believe that a breach of EU Law has occurred, an EU Law infringement procedure, regulated by article 258 of the TFEU, is formally initiated. Conversely, as has occurred in relation to the TVPEE, if the European Commission considers that there is no reason to believe that a breach of EU Law has occurred, the EU Pilot procedure is closed and, as a result, no EU Law infringement procedure is commenced.

205. It is so explained on the website of the European Commission itself:

> *"Further to an enquiry or a complaint (by citizens, businesses and organisations), or on their own initiative, the Commission's services might need to gather additional factual or legal information for a full understanding of an issue concerning the correct application of EU law or the conformity of the national law with EU law. In such cases, the Commission's services submit a query to the Member State concerned via EU Pilot. Member States normally have 10 weeks to respond and the Commission's services, in turn, also have 10 weeks to assess the response (if the response is not satisfactory, the Commission will normally launch infringement proceedings by sending a letter of formal notice to the Member State concerned)."*[75]

206. In short, as we have seen, not only has the European Commission itself not doubted at any time that the TVPEE is a tax, but it has also ratified the compliance of this tax with EU Law.

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[74] Case file of the procedure EU Pilot 5526/13/TAXU relating to the TVPEE, which records the closure thereof by the European Commission in the absence of evidence that there is an infringement of EU law by the TVPEE. (R-0026). We warn that the aforementioned document is confidential and that the European Commission has only given its consent for its use in this arbitration. The identity of officials has been redacted ("deleted") for reasons of data protection.
European Commission's email to the Spanish Ministry of Foreign Affairs informing on the closing of EU-Pilot Project 5526/13/TAXU. R-0027

[75] European Commission webpage referring to "EU Pilot" procedures. http://ec.europa.eu/internal_market/scoreboard/performance_by_governance_tool/eu_pilot/index_en.htm. R-0028.

207. In summary, in view of all the expounded considerations, there is no doubt that the TVPEE is a tax, both from the perspective of Spanish domestic law, as well as from the perspective of international law, and that it has been established through a domestic law of the Kingdom of Spain: Act 15/2012.

208. In other words, from the point of view of both domestic and international law, provisions relating to the TVPEE of Act 15/2012 are provisions relating to taxes of the domestic law of the Kingdom of Spain.

209. Consequently, according to the cited Article 21(7)(a)(i) of the ECT[76], we stand before a taxation measure for the purposes of Article 21 of the ECT.

(6) Conclusion

210. Taking into account all of the above, in summary, the following is concluded:

i) The Kingdom of Spain introduced the TVPEE through Act 15/2012, passed by its Parliament (Congress of Deputies and Senate). The provisions relating to the TVPEE of Act 15/2012 are considered as a "taxation measure" for the purposes of the ECT, according to Article 21(7)(a)(i) of the ECT.

ii) The Kingdom of Spain has only provided its consent to submit to investment arbitration disputes related to alleged breaches of obligations derived from Part III of the ECT (Article 26 of the ECT).

iii) The Claimants allege a supposed breach by the Kingdom of Spain of obligations derived from section (1) of Article 10 of the ECT -an Article included in Part III of the ECT- through the introduction of the TVPEE by Act 15/2012.

iv) However, section (1) of Article 10 of the ECT does not generate obligations with respect to taxation measures of the Contracting Parties. The only sections of Article 10 that do apply, if the case, to taxation measures of the Contracting Parties are sections (2) and (7), not invoked by the Claimants (Article 21 of the ECT).

v) Thus, there is no obligation arising from section (1) of Article 10 of the ECT that could have been allegedly breached by the Kingdom of Spain through the adoption of taxation measures, in particular, through the introduction of the TVPEE by Act 15/2012.

vi) Therefore, the Kingdom of Spain has not given its consent to submit the dispute stated in section iii) above to arbitration and, therefore, with all due respect, the Arbitral Tribunal lacks jurisdiction to hear such dispute.

[76] ECT, Article 21(7)(a)(i):
"7. For the purposes of this Article:
a) The term "Taxation measure" includes:
i) Any provision relating to taxes of the domestic law of the Contracting Party or of a political subdivision thereof or a local authority therein;
ii) Any provision relating to taxes of any convention for the avoidance of double taxation or of any other international agreement or arrangement by which the Contracting Party is bound." (emphasis added) RL-0006.

211. Consequently, it is requested that the Arbitral Tribunal declares its lack of jurisdiction to hear the dispute on the alleged breach by the Kingdom of Spain of obligations derived from section (1) of Article 10 of the ECT through the introduction of the TVPEE by Act 15/2012.

IV. MERITS OF THE MATTER: THE KINGDOM OF SPAIN HAS RESPECTED THE ENERGY CHARTER TREATY (ECT)

212. To understand and resolve this case, it is necessary to analyse the following subjects: (A) The Spanish Electricity System, as a legal regulatory framework and its functioning; (B) The principle of reasonable return for investors and its economic balance with the System costs; (C) The legal regimen applicable at the time the Claimant made the alleged investment, in contrast to the perspective of the Claimant; (D) The culmination of the reform in Renewable Energy in Spain (E) The measures contested by the Claimant and (F) Respect for the ECJ standard of the ECT by the Kingdom of Spain.

A. The Spanish Electricity System (SEE)

213. The Spanish Electricity System (hereinafter **"SEE"**) is a group of activities aimed at guaranteeing electrical energy supply in Spanish territory. It is an economic, technical and legal system. The different rights, duties and legal relations deriving from participation in the SEE are set out in many regulations.

214. In order to correctly understand the evolution of the SEE, it is first necessary to analyse a number of transcendental issues: (i) types of rules used to regulate the SEE and the relationships between them, in the context of the Spanish legal system, (ii) the SEE activities and subjects and (iii) The principles of the SEE.

(1) The rules governing the SEE and the relationships between them

215. The SEE in general and renewable energies (RE) in particular (as part of the SEE) are regulated by rules of different nature. These rules fit in with the general scheme of sources of Law within the Spanish legal system.

216. Therefore, in order to explain the SEE regulations, it is appropriate to briefly describe the sources of the Spanish legal system:

- The Spanish Constitution of 1978: This is the supreme law of the Spanish legal system, which establishes the organisation of Public Authorities, their institutional and territorial structure, and regulates the essential aspects of citizen rights and duties[77].
- The Law: a written norm emanating from the Legislative Power. There are two types of Acts:

[77] Within the system of constitutional guarantees, the Constitutional Court is the supreme interpreter of the Constitution and, in accordance with Article 1 of Organic Law 2/1979, of 3 October 1979. R-0018.

- Organic Laws: those reserved for the regulation of certain matters provided for in the Constitution (Fundamental Rights and public liberties, General electoral system, among others). An absolute majority of the Congress of Deputies is required for their approval.

- Ordinary Laws: these regulate matters not reserved by the Constitution to an Organic Law. A simple majority of the Congress of Deputies is sufficient for their approval.

- The Royal Decree-law: a norm with force of law whereby the Constitution authorises the government to approve in situations of extraordinary need or urgency. The approval of a Royal Decree-law is subject to strict conditions, controls and limits, and to its subsequent parliamentary validation.[78]
- The Royal Decree: the Royal Decree is a regulatory norm emanating from the Government. It complements or implements laws and is hierarchically inferior to them[79]. It can regulate within the authorisations granted by the law, and cannot infringe it[80].
- The Ministerial Order: a regulatory norm emanating from one or several ministerial departments. In the energy sector, the most frequent is a Ministerial Order emanating from the Minister for Industry, Energy and Tourism.

217. Resolutions, in turn, are acts of a lower rank than the Ministerial Order, rather than norms, emanating from competent Government bodies, with a technical content.

218. It is worth highlighting that the corresponding procedures for drafting these norms include, in all cases, hearing[81] and information procedures for holders of rights and legitimate interests, who may be affected by the norms.

219. The aforementioned norms are articulated with each other according to the principle of regulatory hierarchy. The principle means that lower ranking norms cannot contravene

[78] The Claim Memorial mentions different Royal Decree Acts, without explaining their coordination in the Legal System, and omitting all references to subsequent ratification acts passed by Parliament.
[79] The regulatory hierarchical principle is acknowledged by the Claimant itself in footnote 44 of its Claim Memorial.
[80] In the electricity sector, the establishment of subsidies in a regulatory norm (i.e. RD 661/2007) implied that the law authorised the Government to amend this regulation with another subsequent regulation. The concerned Business Associations, in awareness of this evident risk, attempted to change this situation by requesting the determination of "*reasonable return*" of article 30.4 of Act 54/1997 in a norm with the force of a law. The most authorised doctrine stated this in 2010:"The Spanish FIT scheme has the legal Rank of a Royal Decree. Even though it is "stronger" than for instance a Ministerial Order, the Spanish renewable associations have long called for a FIT law. Before the last general elections, the current Socialist government had promised to initiate the respective legislative process, but up to now nothing has changed" (Powering the Green Economy. The feed in tariff handbook. Miguel Mendonça, David Jacobs and Benjamin Socacool. Publishing house. Earthscan, 2010. RL-0062.
[81] In effect, these procedures are mainly set out in the following norms: as regards Laws, in articles 109 and 124 of the Deputies Regulations of 10 February 1982 and article 104 of the Senate Regulation of 3 May 1994 (R-0111) (R-0112); as regards Royal Decrees in article 24 of Act 50/1997, of 27 November (R-0070), and finally, as regards administrative resolutions, in article 84 of Act 30/1992, of 26 November, on the Legal System of the Public Administrations and Common Administrative Procedure. R-0067.

higher ranking norms. This, in turn, leads to important practical consequences[82]: (1) no regulatory provision may be contrary to the law that it implements; otherwise, it is fully null and void and the courts must overrule it, (2) any regulatory provision must be interpreted and applied in line with the Law it implements (3) no regulatory provision may prevent the adoption of regulatory measures aimed at fulfilling the requirements of the Law.

220. Furthermore, the importance of European Union Law in the Spanish legal system should be highlighted. Since Spain joined the European Union in 1986, Community Law forms part of the Spanish legal system.

221. As part of European Union Law, along with the Treaties (Treaty on European Union and the Treaty on the Functioning of the European Union), the different legal acts of European Institutions - article 288 of the Treaty on the Functioning of the European Union (hereinafter "**TFEU**"), should be remembered due to their effect on the electricity sector:

- *Regulations*, which have a general scope, they are binding in their entirety and directly applicable in each Member State.
- *Directives*, which are binding on the recipient Member State in terms of the result that it should achieve; however, the choice of the form and the means is left to the national authorities.
- *Decisions,* all elements of which are binding for the recipient Member State.
- *Recommendations* and *Opinions,* which are not binding.

222. Lastly, the relevance of Supreme Court case law must be taken into consideration in the Spanish legal system. According to article 1.6 of the Spanish Civil Code:

> *" Case law shall complement the legal system by means of the doctrine repeatedly upheld by the Supreme Court in its interpretation and application of statutes, customs and general legal principles."*[83]

223. Therefore, Supreme Court case law, as it *applies* and *interprets* the legal norms (including Laws) is binding on other Courts. This case law, due to its uniform nature, forcefulness and clarity, is essential to understanding and resolving this case, particularly as the Supreme Court is the constitutional body responsible for ensuring that the Spanish Public Authorities act legally[84].

(2) SEE Activities and subjects

(2.1) Classification and description of the activities

[82] Articles 9.3 and 103 of the Spanish Constitution (R-0006), article 6 of the LOPJ (R-0066) and article 62.2 of Act 30/1992, of 26 November, on the Legal System of Public Administrations and Common Administrative Procedure. R-0067.
[83] Article 1.6 of the Spanish Civil Code. R-0095. Vienna Convention on the Law of Treaties, of 23 May 1969, published in the Official State Gazette on 17 June 1980. RL-0010.
[84] Article 106 of the Spanish Constitution. R-0006

224. Up until 1997, the SEE was structured as a regulated system in which the Government set the price of electricity, which compensated the costs (mainly electricity generation, transmission and distribution) of all electricity companies.

225. As of the entry into force of Act 54/1997, the deregulation of the sector started to occur, due to EU requirements. This deregulation is based on the vertical division of activities and its subsequent specific regulation, with the aim of introducing competition and increasing the overall efficiency of the electricity sector. The resulting division gave rise to the identification of different activities of the SEE: generation, transmission, distribution, and marketing.

226. Having identified said activities, Act 54/1997 associated each one of these activities with one of the following categories:

- *Deregulated activities*: The generation (except for generation under the special regime) and marketing of energy
- *Regulated activities*: Transmission, distribution and operation of the system[85].

227. A brief summary of each of these activities is provided below:

1. The *generation* of electricity corresponds to producers of electrical energy or entities with the capacity to supply electricity to the network. Since 1994[86], Spanish legislation distinguishes between (i) generation subject to an Ordinary remuneration Regime (hereinafter, "**OR**") and (ii) generation subject to a Special remuneration Regime (SR). Act 54/1997 of 27 November, on the Electricity Sector (hereinafter, "**Act 54/1997**") maintained this distinction and submits certain generation activities to the Special Regime (technologies that use renewable sources, waste biomass and cogeneration in the cases provided for in legislation). The main distinction between both Regimes is the regulation of the remuneration for certain renewable energies.

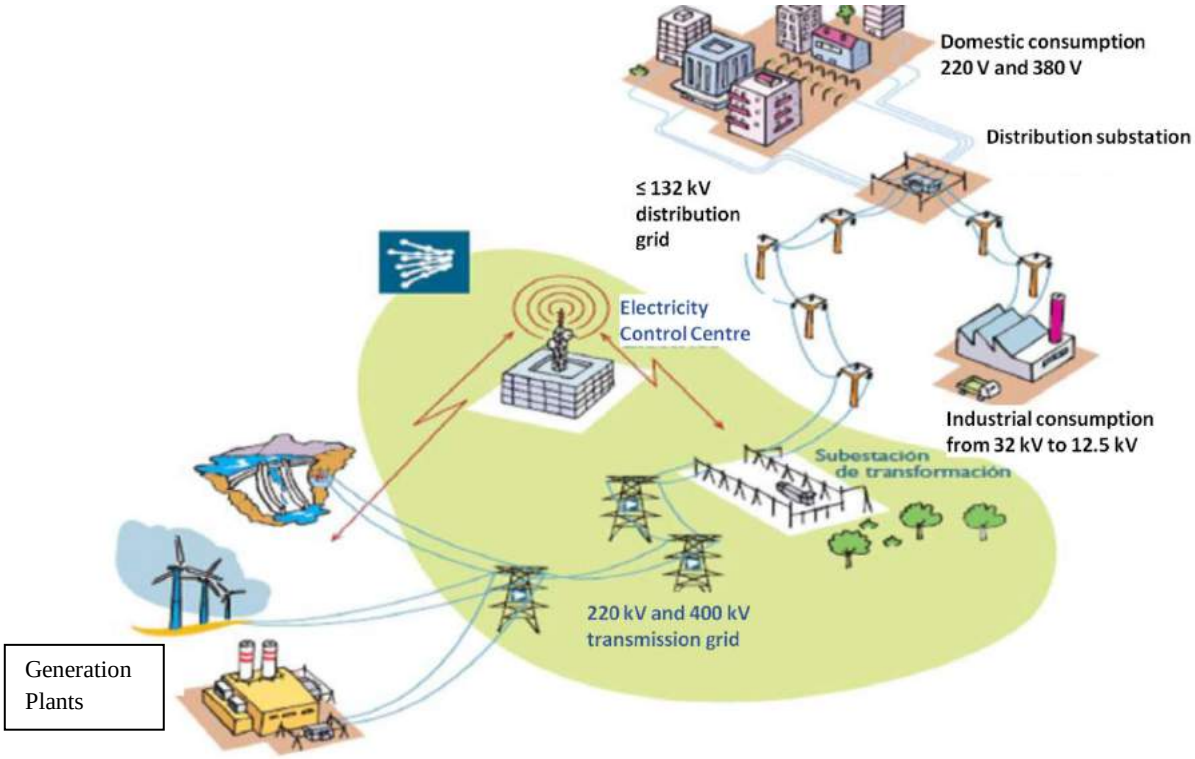
2. *Transmission* corresponds to the Spanish Electricity Network (hereinafter, "**REE**") under the monopoly regime and is regulated activity[87].

3. *Distribution* consists in the supply of electrical energy from the transmission network to the point of consumption. It is a regulated activity and is performed by distribution companies.

4. *Marketing* corresponds to companies that acquire the electricity produced and sell it to consumers.

228. The following table provides a simple overview of the various *activities* of the SEE that we have just explained: generation, transmission, distribution and marketing.

[85] Act 54/1997 of 27 November, on the Electricity Sector, Article 11. R-0079.
[86] Act 40/1994 of 30 December, on planning of the National Electricity System. R-0069.
[87] Moreover, the REE acts as the *Agent of the system*, in charge of managing and coordinating the technical aspects of the system, which includes management of the network. Together with the REE, there is another *Agent*, Compañía Operadora del Mercado Español de Electricidad (OMEL), which is in charge of coordinating the financial operations of electrical energy purchases.



229. The subjects that develop these activities do not act in the SEE separately from each other, as in isolated compartments. Quite the contrary, the SEE is characterised by strong interdependence among its agents and activities:

- The impossibility of storing electricity means that the supply has to equal demand at any given time. This means coordination between the production of electrical energy and demand, as well as coordination between the investment in generation and the infrastructure for the transmission of electrical energy.

- Technically, there is a real network structure, a system in which generation, transmission and distribution must have harmonic dynamics in their functioning and in which the agents are in fact physically interconnected.

- All operators are, both separately and jointly, subject to the intervention of a System regulator.

- The participants of the SEE share the source of their income: Spanish consumers.

(2.2) The Regulatory Bodies

230. In the SEE, there are two regulatory bodies that exercise public powers over the *activity* of the economic agents and of the subjects of the system: the Ministry of Industry, Energy

and Tourism and the National Markets and Competition Commission[88] (hereinafter, the "**CNMC**"), as a successor entity of the National Energy Commission[89] (hereinafter, the "**CNE**").

231. The Ministry of Industry, Energy and Tourism is the Department of the General Government Administration responsible for proposing and implementing the government's policy on energy. It approves the Ministerial Orders that develop energy legislation, and it proposes Royal Decrees to the Council of Ministers (the Government) for its approval thereof. It is the main regulatory body regarding energy.

232. The CNMC has the following functions, among others:

a) Acting as an advisory body of the administration regarding energy, by issuing non-binding reports.
b) Participating, through non-binding proposals or reports, in the process of drafting general provisions on energy matters.
c) Issuing circulars for implementing and executing the Royal Decrees and Orders of the Ministry of Industry and Energy that are issued on energy matters, as long as these provisions authorise it to do so. These implementing circulars are mandatory for the subjects affected by the scope of application, once published in the Official State Gazette.
d) Management of settlements of the electricity system. It performs 14 settlements for each financial year for those entitled to receive amounts from the SEE.
e) Monitoring and control in the electricity sector including, among others:
    - Monitor the suitability of the legal system of prices and conditions of supply to end consumers and publishing recommendations to adapt the supply prices to the obligations of public service and consumer protection.
    - Manage the system of guaranteeing the origin of electricity coming from renewable sources of energy and high-efficiency cogeneration.
    - Publish the final prices of the electricity market based on information from the market operator and the system operator.

233. Therefore, the CNE was (and the CNMC is) an advisory body that cooperates with the government by issuing proposals and reports. The government is the holder of regulatory power and of legislative initiative in the process of preparing general provisions on energy[90]. The CNE issued proposals or reports within the strict area of its jurisdiction.

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[88] Act 3/2013 of 4 June, on the creation of the National Commission of Markets and Competition, integrated the CNE in the CNMC. This Act is accessible by public at the following web page: http://www.boe.es/boe/dias/2013/06/05/pdfs/BOE-A-2013-5940.pdf . R-0075.

[89] The CNE, currently integrated in the CNMC, was created by Act 34/1998 of 7 October, on the Hydrocarbons Sector, in Additional Provision Eleven thereof. R-0072.
It was founded as a public body for regulating the operation of the Energy Sector. Its purpose was to "promote the competitive operation of the energy sector in order to guarantee effective availability and the provision of services and quality, with respect to the supply of electricity and natural gas, in benefit to the market as a whole and to consumers and users".

[90] Article 97 of the Spanish constitution assigns the exercise of regulatory powers to the government and Article 81 assigns the legislative initiative. R-0006

234. This nuance is highly relevant for the purposes of this case, given that upon issuing its non-binding reports, the CNE never considers nor assesses subjects beyond its jurisdiction, such as the following: macroeconomic circumstances, budget obligations or international commitments assumed by Spain.

(3) SEE Principles

235. The SEE, since Act 54/1997 of 27 November, on the Electricity Sector (hereinafter, "**Act 54/1997**")[91], and until the current Electricity Sector Law, Act 24/2013 of 26 December, on the Electricity Sector (hereinafter, "**Act 24/2013**")[92], has been based on the following principles:

1. The supply of energy is a service of strategic importance.
2. Guaranteeing the supply requires the financial sustainability of the system.

(3.1) The supply of energy as a service of strategic importance

236. The strategic importance of the electricity supply is an unquestionable fact. Its guarantee is a need for the operation of the economic and social activity of any developed country. The price of electric energy and energy intensity are factors that have a direct impact on the growth of the economy and on fundamental macroeconomic variables, such as inflation and competition.

237. This factual circumstance is reflected at a regulatory level. Act 54/1997, by requirement of Community Law[93], qualified the electricity supply activity as an "*essential service*"[94]. Subsequently, in Act 24/2013, it was qualified as a "*service of general economic interest*"[95].

238. The configuration of the electricity supply activity as a service of strategic importance gives rise to the fact that the laws of this sector regulate it in detail, thereby also establishing certain charges and obligations for the subjects that take part in the different activities thereof.

(3.2) Guarantee of supply: technical and financial sustainability of the system

239. The main objective of the SEE established by Act 54/1997[96] is to guarantee that all consumers have access to electric energy under conditions of equality and quality, thereby assuring that it involves the least possible cost and that it also takes environmental protection into account.

240. Guaranteeing the supply, essential in the SEE, means that actions of the public powers will be mainly directed at assuring that the electrical supply will be maintained under affordable conditions for consumers and that this supply is sustainable in the long term. "Sustainability" therefore means the technical, environmental, and economic-financial

[91] Act 54/1997 of 27 November, on the Electricity Sector. R-0079.
[92] Act 24/2013 of 26 November, on the Electricity Sector. R-0076.
[93] Treaty establishing the European Community (92/C 224/01), published in the Official Journal of the European Communities on 31 August 1992, Article 86. RL-0005.
[94] Act 54/1997 of 27 November, on the Electricity Sector. R-0079.
[95] Act 24/2013 of 26 December, on the Electricity Sector. R-0076.
[96] Act 54/1997 of 27 November, on the Electricity Sector. Preamble and Article 10. R-0079.

viability of the SEE. This guarantee has been maintained in Act 24/2013 of 26 December, on the Electricity Sector[97].

241. In this regard, it should be highlighted that the economic viability of the SEE rests on its financial self-sufficiency. This means that the costs of the SEE must be paid with the income of the SEE. Thus, if an imbalance occurs in the system and the costs are greater than the income, the measures that can be taken are the following: either increasing the income or decreasing the costs.

242. Financial self-sufficiency[98], already embodied in Act 40/1994 of 30 December, on planning of the National Electricity System[99] (hereinafter, "**Act 40/1994**") was expressly reaffirmed in 2011 by a law that has been omitted from the arbitral tribunal by the Claimant. Act 1/2011, on Sustainable Economy, expressly set forth the need for all planning to be done based on a ***sustainable system***.

243. The SEE's need for self-financing was likewise maintained in Act 24/2013 of 26 December, on the Electricity Sector. Exceptionally, since 2013, relevant contributions have been made by the General State Budgets, but with the sole purpose of paying the remuneration of certain electricity generation facilities that use renewable energy sources.

244. And for these purposes, it should be emphasised that, contrary to what the Claimants maintain, it is not true that LSE 2013 has imposed a new, previously non-existent obligation to finance the imbalances of the system[100]. Such a financing obligation for the imbalances was already included by Royal Decree-law 6/2010 of 9 April in additional provision twenty-one of LSE 54/1997.

245. Therefore, the financing provision for temporary imbalances contained in Article 19 of Act 24/2013 does not constitute a novelty of this law, rather a continuation of the rules that, in guarantee of sustainability, have always existed within the regulatory framework of the SEE.

246. The only difference incorporated by this Article 19 is precisely that of establishing a fairer distribution of that "system charge", by setting forth that it will be paid proportionally by all system operators, instead of making it fall on 5 specific companies. Once again, an inefficiency of the SEE has been corrected.

247. On the other hand, it should be highlighted that the Claimants once again state this "rule of sustainability" in light of their own interests, given that they fail to mention that (i) currently the SEE is generating a surplus, and therefore this provision has not been applied, and cannot be quantified, and (ii) point 3 itself of Article 19 of LSE 2013 establishes the right of those subjects to recover the contributions made due to imbalance, with the corresponding market interest rate. Therefore, this rule is neither new nor has it caused any financial impact on the Claimants, and if it were eventually applied, the Claimants would be adequately compensated.

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[97] Act 24/2013 of 26 December, on the Electricity Sector. Preamble and Article 7. R-0076.
[98] Act 54/1997 of 27 November 1997, on the Electricity Sector. Articles 15 and 16. R-0079.
[99] Law 40/1994, of 30 December. Articles 15 to 20. R-0069.
[100] Memorial on the Merits, paragraphs 579 to 582.

248. Therefore, since the SEE constitutes a closed economic structure, its sustainability depends on the balance between its income and costs:

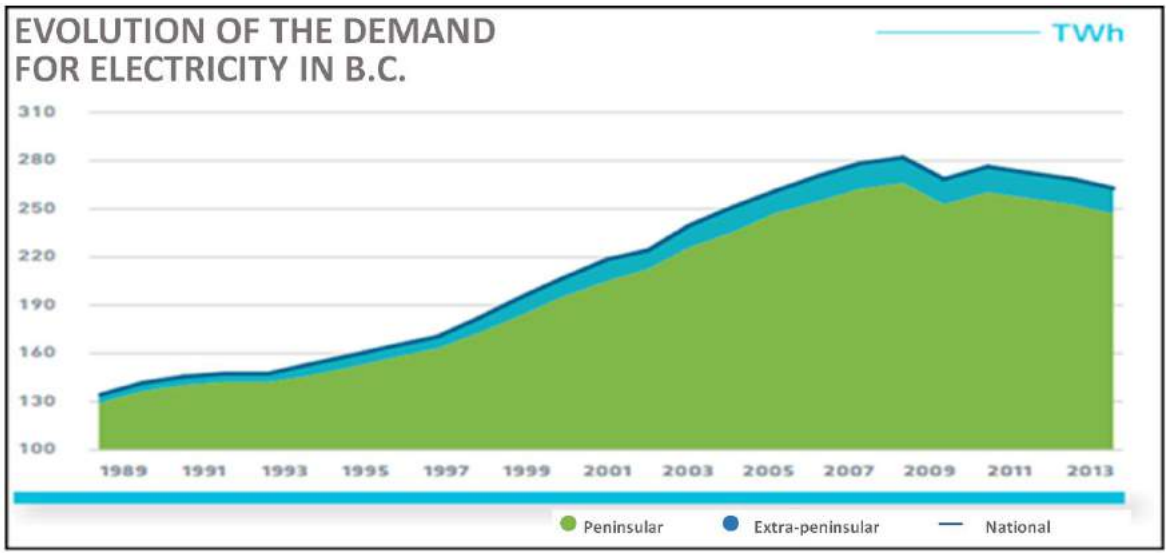
(a) Income of the SEE and the evolution thereof

249. The SEE's income comes exclusively from the Spanish consumer. Essentially, a Spanish consumer, upon paying the bill for consuming electricity, pays the price of the energy consumed and, furthermore, the amount corresponding to *tolls* and *charges*.

250. Access *tolls* are allocated to maintaining the transmission and distribution networks. In turn, *charges* pay for those costs of the system that do not respond directly to the supply of electricity received by the consumer. These *charges* include the amounts that are paid to electricity generation facilities based on renewable energy sources, which have the right to additional remuneration.

251. Therefore, the evolution of income is linked to the electricity demand. Thus, the financial sustainability of the SEE requires that the cost estimate adapt to the forecast evolution of demand.

252. The electricity demand in Spain, contrary to what was forecast by the regulatory body in its cost planning ("trend scenario"), has sustained a notable decrease as a consequence of the international economic crisis that has occurred in recent years and the impact thereof in Spain. This trend can be appreciated in the following graph[101]:



253. Despite the major reduction in demand, the attempt has been made to guarantee the financial sustainability of the SEE through a major increase in the electricity bill.

[101] Source: Electricity Network of Spain

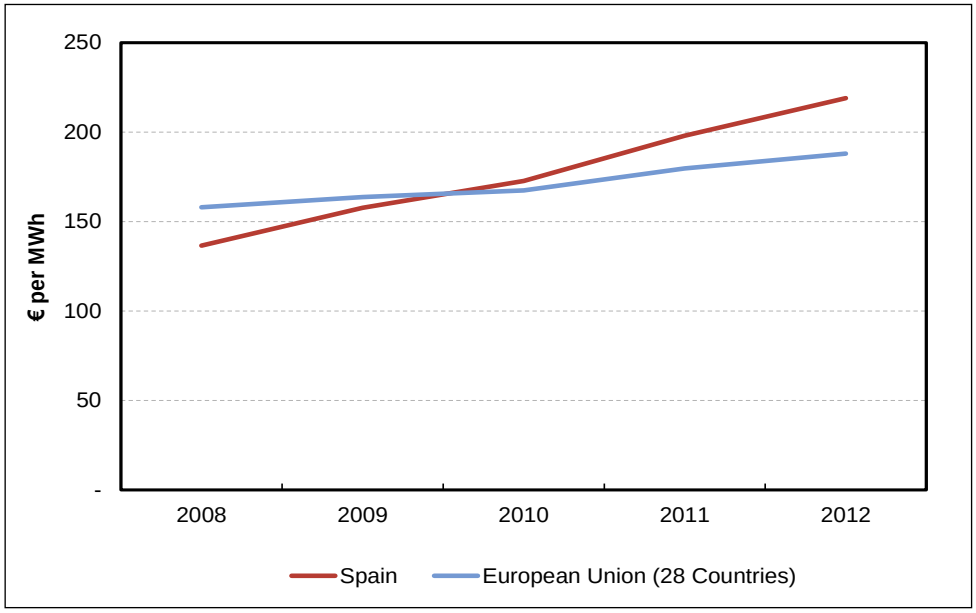
254. For this purpose, it is sufficient to observe the evolution of the annual bill of a domestic consumer in Spain responding to average consumption[102]. The data according to the amount of the annual bill and per increases are the following[103]:

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Bill, including taxes	370,0	375,3	381,7	400,0	412,6	453,7	503,2	532,6	627,0	669,7	648,7	616,2
Annual increase of bill, including taxes		1,4%	1,7%	4,8%	3,1%	10,0%	10,9%	5,9%	17,7%	6,8%	-3,1%	-5,0%
		2004-2003	2005-2003	2006-2003	2007-2003	2008-2003	2009-2003	2010-2003	2011-2003	2012-2003	2013-2003	2014-2003
Accumulated annual increase. Bill, including taxes		1,4%	3,2%	8,1%	11,5%	22,6%	36,0%	44,0%	69,5%	81,0%	75,4%	66,6%

255. Therefore, a consumer went from paying 370 euros per year for their electricity bill in 2003 to paying a total of 669 euros in 2012. In effect, the accumulated increase over those years is disproportionate, given that the same service was received, with the biggest increases occurring in 2008 (10%), 2009 (10.1%) and 2011 (17.7%).

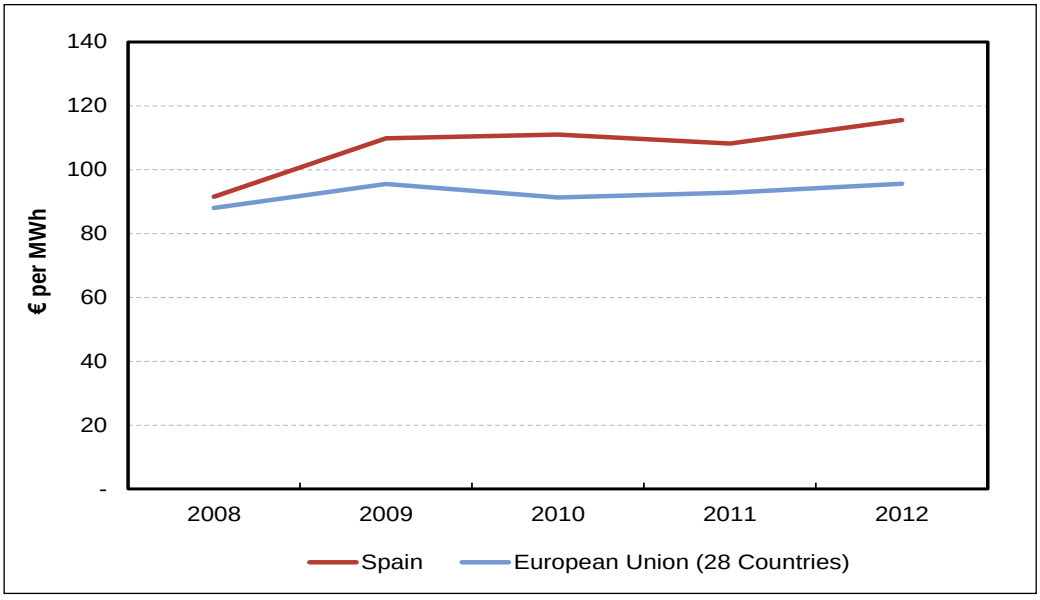
256. The following graph shows the evolution of the price of electricity between 2007 and 2015 for households in Spain and the EU average[104]:

[102] Contracted power of 3.3 kW and consumption of 3000 kW/year. Applicable to a 4-member family living in a flat.
[103] Source: own preparation based on data of the settlement reports of the CNE/CNMC for 2005-2013 (http://www.cnmc.es/es-es/energía/energíaeléctrica/régimenespecialyliquidaciones.aspx?p=p3&ti=Liquidaciones sector eléctrico) and of the Compañía Operadora del Mercado Español de Electricidad (OMEL) (http://www.omie.es/files/flash/ResultadosMercado.swf)
[104] Report of Econ One Research, 15 June 2016, appendix D, graph 24.



257. An increase is observed in the price of electricity for households in Spain over the analysed period, specifically an increase of 61.81%. This increase is far greater than what occurred during the same period in the European Union, where the total price of electricity increased 21.91% for households[105].

258. The electricity bill for Spanish industry has had the same increasing evolution. Said evolution can be seen in the following table[106]:



[105] Data per semester obtained from Eurostat and pertaining to the price of electricity in kwh, taxes not included, in Spain and the European Union for domestic consumers between the second semester of 2007 and 2014, included in Document R-0218. Said figures are obtained through the following calculations: variation of the price of electricity for households in Spain: (0.1861-0.1152)/0.1152=0.6155, variation of the price of electricity for households in the EU: (0,142-0,1164)/0,1164=0,2199.
[106] Report of Econ One Research, 15 June 2016, appendix D, graph 25.

259. An increase is observed in the price of electricity for industries in Spain over the analysed period, specifically an increase of 18.20%. This increase is far greater than what occurred during the same period in the European Union, where the total price of electricity increased 3.29% for industries.

260. The evolution of the bill has been rising, except for the last two years, in which the price of energy has determined a decrease in the final price. Therefore, consumers have borne an extraordinary increase in their bill, without a relevant increase or variation in the service provided. All of this within the context of a harsh global economic crisis.

261. The Spanish consumer, therefore, has made a major effort to cover the costs of the electricity system, thereby considering that any increase has a major impact on the economy and growth of the country. In this regard, it cannot be forgotten that companies are also included among consumers, which lose competitiveness if their costs increase (including the cost of the electricity they consume in order to produce).

(b) Costs of the SEE and the evolution thereof

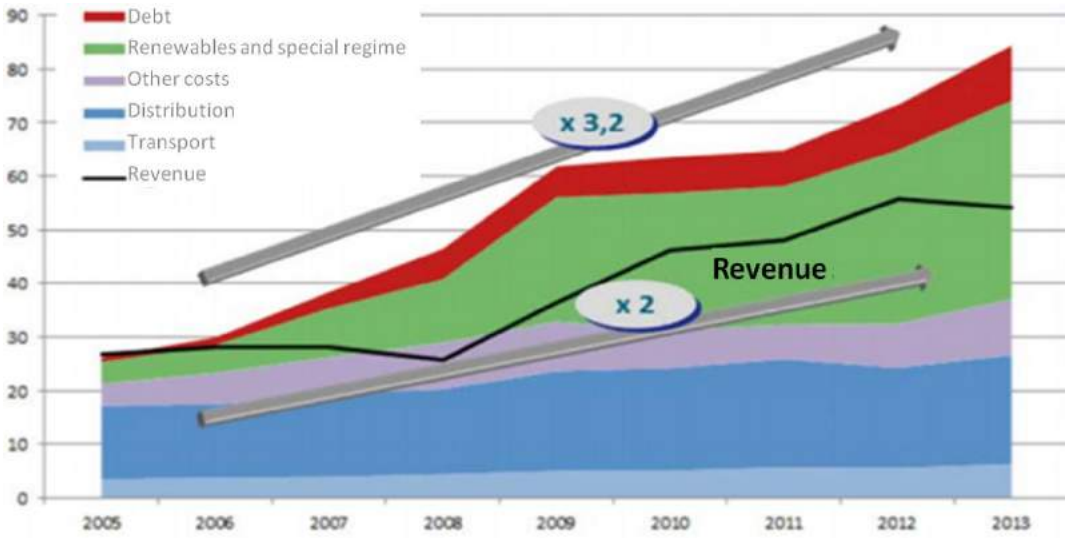
262. The costs of the electricity system have evolved exponentially according to the evolution of the investments in the various activities, particularly in *Transmission*, *Distribution* and *Generation*. In the *Generation* activity, costs have been evolving as remuneration schemes have been granted to certain facilities included in the Special Regime.

263. In addition, given that facilities which use renewable energy as a source are not "*manageable*" in general, in the sense that they do not generate electricity according to the will of human beings, rather of nature, it is necessary to establish security mechanisms that allow guaranteeing the supply. Thus, it is necessary to have facilities that remain almost inactive but serve as "backup" or support due to a decrease in production because of a sudden weather change. Therefore, ordinary production facilities such as combined cycle facilities charge the SEE for *capacity payments* in order to be able to satisfy those eventual energy production needs.

264. Consequently, the priority of selling energy generated by renewable energy and high-efficiency cogeneration facilities gives rise to the fact that it is necessary to make *capacity payments* to ordinary producers, which have to be available to produce energy. This has also led to an overcapacity in the system, which causes greater costs.

265. The evolution of the system's costs can be analysed in the following graph[107]:

[107] Source: Own preparation of data from the settlement reports of the CNE/CNMC for 2005-2013.http://www.cnmc.es/es-es/energía/energíaeléctrica/régimenespecialyliquidaciones.aspx?p=p3&ti=Liquidaciones sector eléctrico



266. The evolution demonstrates that all costs of the SEE increased by 3.2 between 2006 and 2013; and that income, despite the drop in demand, doubled through an increase in the electricity bill borne by consumers. This difference between income and costs gave rise to the so-called *tariff deficit*.

(c) The imbalance of the SEE: the tariff deficit and its evolution.

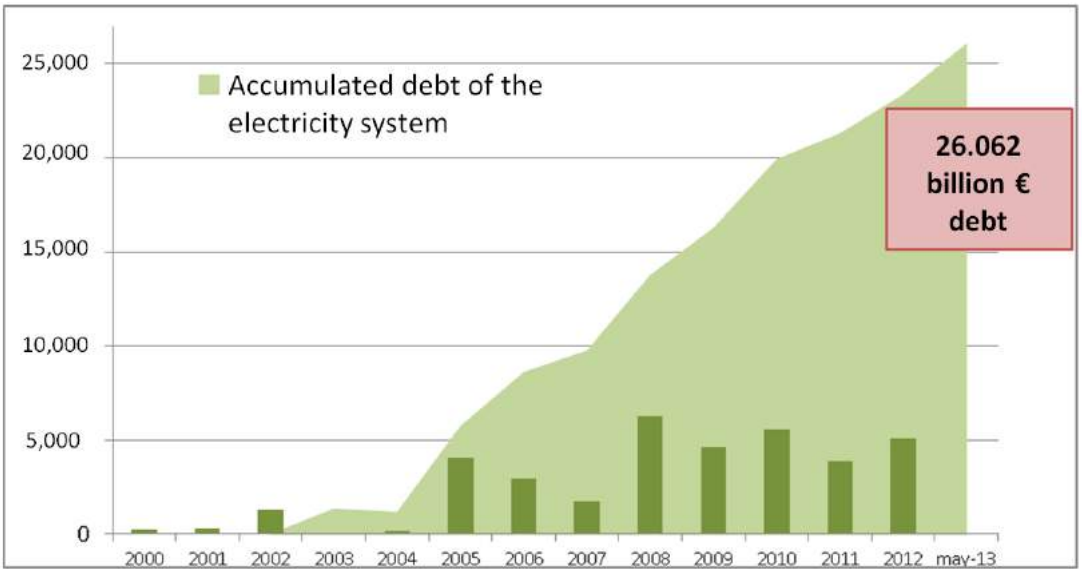
267. When the SEE's income and expenses are not equivalent, an imbalance occurs. If that imbalance is due to the fact that the income is insufficient for covering the costs, the so-called "tariff deficit" arises.

268. This imbalance in the SEE has been very considerable in recent years, given that the electricity system, despite the permanent rise in tolls and charges over the years, has not been able to cover costs, due to the fact that they have increased faster than that of the bill paid by consumers.

269. This deficit has caused an accumulated debit in recent years, which reached 40.326 billion euros. Despite the fact that this debt has been progressively amortised, in 2015 the balance thereof was still over 26 billion euros. We recall that this debt is being paid by Spanish consumers in the electricity bill at the rate of approximately 2.8 billion euros per year.

270. Moreover, a number of companies were required to finance the system by contributing the necessary amounts so that the costs were paid, thereby generating in exchange, a credit claim with respect to the electricity system. This credit claim could be securitised directly by the companies through the Electricity Deficit Amortisation Fund (hereinafter, the "FADE").

271. The evolution of the electricity deficit and of the accumulated, non-amortised debt can be appreciated in the following graph[108].



272. The average annual costs of the electricity system must be added to these amounts, which costs are around 20 billion euros, representing an annual charge for amortisation and interest of approximately 2.9 billion euros.

273. After the entry into force of challenged measures, for the first time in 2014, it can be verified that income was sufficient to cover all the regulated costs, and a positive imbalance of 550.3 million euros was recorded[109]. In other words, the final result of the settlement of the regulated activities for the 2014 financial year gave rise to a surplus of 550.3 million euros.

274. Despite this, the SEE has never ceased to fulfil its obligation to provide reasonable profitability for facilities of the special regime.

B. <u>The SEE regulation regarding renewable energies</u>

(1) EU policy

275. The Spanish energy policy is framed within the policies of the European Union, regarding both energy and environmental fields. The Claimant acknowledges this importance in the Memorial on the Merits by making numerous references to the European legislation[110].

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[108] Source: Own preparation of data from the settlement reports of the CNE/CNMC for 2005-2013. http://www.cnmc.es/es-es/energía/energíaeléctrica/régimenespecialyliquidaciones.aspx?p=p3&ti=Liquidaciones sector eléctrico

[109] This comes from the "Report on the final settlement for 2014 of the Electricity Sector. Analysis of results regarding the annual forecast of income and expenses for the electricity system", prepared by the CNMC on 24 November 2015, which can be consulted at the web page http://www.cnmc.es/Portals/0/Ficheros/Energia/Informes/Liquidaciones_Electricidad/151124_LIQ_DE_346_15_Liq_definitiva%202014_energiaelectrica.pdf. R-0134

[110] Memorial on the Merits, amongst others, paragraphs 90 to 92.

276. The European Union's policy has been characterised by establishing targets. Compliance therewith is imposed as an obligation upon Member States, and those targets are aligned with the overall targets agreed upon in the Kyoto Protocol.

277. To achieve those targets, Directive 2001/77/EC of the European Parliament and of the Council, of 27 September 2001, on the promotion of electricity produced from renewable energy sources in the internal electricity market, was approved (hereinafter, "**Directive 2001/77/EC**")[111]. This directive recognised the need to grant public aid in favour of renewable energy sources, consistent with community guidelines on state aid in favour of the environment.

278. The Claimant mentions this directive while failing to mention a relevant circumstance to the Arbitral Tribunal. This directive established that public aid for renewable energy sources would be set by the states within the obligations imposed in Articles 87 and 88 of the Treaty on State Aid[112]. In this regard, the Court of Justice of the European Union (hereinafter, the "**TJUE**") has declared that those amounts that end users pay to a private electric power producer are considered State Aid.[113]

279. In January 2007, the European Union set new targets in the so-called "20-20-20 Package". To achieve these community targets, Directive 2009/28/EC was approved, of April 23 (hereinafter, "**Directive 2009/28/EC**")[114], on the promotion of the use of energy from renewable sources. This law establishes a common framework for promoting such sources, therefore establishing mandatory national targets.

280. Directive 2009/28/EC also considers the necessary public aid for promoting electricity produced with renewable energies, "as long as electricity prices in the internal market do not reflect the full environmental and social costs and benefits of energy sources used"[115]. However, this directive acknowledges the difficulty of Member States to reach the targets and recognises the need for the EU to adopt measures to achieve them[116].

281. Therefore, Member States are required to keep in mind the Guidelines on State Aid for protection of the environment and energy approved through EC Communication

[111] Directive 2001/77/EC of the European Parliament and of the Council, of 27 September 2001, on the promotion of electricity produced from renewable energy sources in the internal electricity market, published in the Official Journal of the European Union on 27 October 2001. RL-0015.
[112] Recital (12) of Directive 2001/77/EC. RL-0015.
[113] Decision of 22 October 2014, handed down in Preliminary Ruling C-275/13 (Elcogás Case).Paragraph 21: "In order for some advantages to be qualified as aid in the sense of Article 107 TFUE, section 1, they must, on the one hand, be granted directly or indirectly through state funds, and on the other, they must be attributable to the state".Paragraph 33: "The amounts attributed to a private electric power producer which are financed by the end users of electricity as a whole established in national territory and which are distributed to companies of the electricity sector by a public organisation in accordance with predetermined legal criteria constitute State intervention or intervention by means of State funds". R-0074.
[114] Directive 2009/28/EC of the European Parliament and of the Council of 23 April 2009 on the promotion of the use of energy from renewable sources and amending and subsequently repealing Directives 2001/77/EC and 2003/30/EC. RL-0017.
[115] Recital (27) of Directive 2009/28/EC. RL-0017
[116] Directive 2009/28/EC. RL-0017.

2008/C82/01[117] and substituted for the 2014-2020 period through EC Communication 2014/C 200/01[118]. These guidelines establish that, as from 2020, the subsidies and exemptions of liability regarding balance should be gradually eliminated.[119]

(2) The regulation of subsidies for production based on renewable sources in the SEE

(2.1) Introduction: basic conditions

282. The regulation of the electricity generation activity based on renewable energy sources under the special regime in Spain since Act 54/1997 has been based on the following conditions:

- The production activity based on renewable sources is an activity built in, not isolated from, the SEE, and therefore the remuneration thereof constitutes a cost of the SEE, subordinated to the principle of financial sustainability.
- Given that the sustainability of the SEE depends on the balance between their revenues and costs, the cost of implementing renewables is determined according to the foreseeable evolution of the demand and of other basic economic data.
- To the extent that producers of renewable energies cannot recover the costs they incur through the market price, it is necessary for the SEE to complement that market price through a subsidy that guarantees *an level play field.*
- This subsidy has always been set based on the investment and operating costs of a standard facility, and its objective is for investors to be able to recover the CAPEX and OPEX and earn reasonable profitability according to the capital market.
- The principle of reasonable profitability, the corner stone of the remuneration system for energy production based on renewable sources, is characterised by its equilibrium and dynamism.

(2.2) Act 54/1997 of 27 November 1997, on the Electricity Sector.

(a) Introduction

283. Act 54/1997, on the Electricity Sector, in line with the guidelines established by legislation of the European Union, covers the regulation of renewable energies in the SEE within the activity of electric energy generation.

284. In this regard, Directive 2001/77/EC established the need to have national indicative targets[120]. In turn, Directive 2009/28/EC authorised Member States to support the

[117] Community directives on state aid in favour of the environment, 2008/C 82/01, European Commission, published in the Official Journal of the European Union on 1 April 2008. R-0064.
[118] Directives on state aid regarding environmental protection and energy 2014-2020, 2014/C 200/01, European Commission Communication published in the Official Journal of the European Union on 28 June 2014. R-0065.
[119] Directives on state aid regarding environmental protection and energy 2014-2020, 2014/C 200/01, European Commission Communication published in the Official Journal of the European Union on 28 June 2014. Paragraph 108. R-0065.
[120] Directive 2001/77/ EC, Article 3: "Member States shall take appropriate steps to encourage greater consumption of electricity produced from renewable energy sources in conformity with the national indicative targets referred to in paragraph 2. These steps must be in proportion to the objective to be attained." RL-0015.

deployment of energy coming from renewable sources. However, this power was conditioned upon achieving the implementation targets set forth in said law, which were legally binding[121]

285. For these purposes, Act 54/1997, following the design of Act 40/1994[122], distinguished between an Ordinary Scheme (RO) and a Special Regime (RE). This dual scheme was established due to the need to promote production using energy sources in which the price that they could obtain in the competitive market is insufficient for covering their costs of construction and operation, with a *reasonable return* on the investment. Therefore, they require subsidies to be profitable.

(b) Identification of the subsidised facilities

286. Article 27.1 of Act 54/1997 established the requisites that must be met by facilities to be able to voluntarily avail themselves of the special regime. Among others, they should be "*facilities whose installed power does not exceed 50 MW*" and "*which use any of the non-consumable renewable energies as the primary energy*"[123]. In any event, the possibility that a producer could avail itself of the special regime was, and continues to be, voluntary.

(c) Legal and economic integration of the RE in the SEE

287. Despite being qualified as "special", this regime was integrated into the SEE by Act 54/1997, from both a legal perspective and from a technical and economic perspective.

288. From a legal perspective, the special regime was subject to all other principles of the SEE:

> *" The power defined in article 30.2.a) shall be subject to the principles of regulation in Title II and those in Titles III and IV of this Act that may apply. "*[124]

289. Therefore, activities under the special scheme were subject, like all activity of the SEE, to the previously analysed principles of *security of supply* and *financial and technical sustainability*.

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[121] Directive 2009/28/EC of the European Parliament and of the Council of 23 April 2009 on the promotion of the use of energy from renewable sources and amending and subsequently repealing Directives 2001/77/EC and 2003/30/EC. Article 3 (3). RL-0017.

[122] Act 40/1994 of 30 December, on planning of the National Electricity System (hereinafter, "Act 40/1994"), distinguished between activities "*that constitute a natural monopoly and those that could be exercised under competitive conditions*". It established the objective of "*establishing the most appropriate remuneration for each one of them*". Article 16 of Act 40/1994, when regulating the determination of the tariffs that should be satisfied by users of the integrated system, alludes to the mandatory "*recognition of the costs attributable to each one, according to objective and non-discriminatory criteria that incentivise improvement in the efficiency of management, the efficiency of said activities and the quality of the electricity supply*". This same article establishes a system for recovering investment costs that takes into account the investment and the operating costs to be paid during the useful life of the facility, in accordance with a remuneration rate that would be established by the Ministry of Industry and Energy according to the evolution of the financial markets. This system, which was established in 1994, coincides with the current system, which will be the object of explanation further below. R-0069.

[123] Act 54/1997 on the Electricity Sector, Article 27(1). R-0079.

[124] LSE 54/1997, Article 29. R-0079

290. From an economic perspective, the main part of the remuneration of the activities of the special regime, formed by the subsidies, was integrated as another cost of the SEE. In this regard, Article 16 of Act 54/1997 qualified the subsidies for the RE as a "*supply diversification and security costs."*

291. Act 54/1997 therefore maintains the remuneration regime for electricity generation based on renewable sources under the special regime within a regulated scope, as it was already done prior to this Act. This means that the remuneration regime of generation under the special regime is assimilated in the activities of transmission and distribution[125].

292. To the extent that the subsidies were a cost of the SEE, the implementation of the special regime required planning by the regulatory body, which must adjust the costs derived from deployment of renewable energies to the SEE's income forecast, meaning the forecast evolution of demand. Therefore, Act 54/1997 was especially careful in pointing out:

> *"In order for renewable energy sources to cover at least 12% of Spain's total energy demand by the year 2010, a plan shall be drawn up to promote renewable energies and whose objectives shall be taken into account in the setting of premiums."*[126]

293. This planning has been embodied in the successive Renewable Energies Plans. In them, the cost derived from achieving the objectives of implementing renewable energies has been linked to the forecast electricity demand and other basic economic variables included in the "*trend scenario*".

294. These Renewable Energies Plans respond to the concept of indicative planning. Said plans establish the "*planning that offers guideline parameters for the way the electricity industry is expected to develop in the near future, thus facilitating the investment decisions to be made by the different economic agents*."[127]

(d) Duties and rights of producers under the special regime

295. To the extent that the special regime represents the receipt of subsidies for the beneficiaries thereof, they are subject to complying with certain, specific obligations[128]. These obligations clearly show that the so-called special scheme is subject to the technical and financial sustainability of the SEE. Highlights of these obligations include the following:

- Provide the administration with information about production, consumption, energy sales and other points that may be established.

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[125] Ibid, Article 16 (2) (3). R-0079.
[126] Act 54/1997 of 27 November, on the Electricity Sector, Transitional Provision Sixteen. Act 17/2007 of 4 July amended the content of this precept and transferred it to Additional Provision Twenty-five, thereby indicating that: *"The government will modify the Plan for the Promotion of Renewable Energies to adapt it to the objectives of 20% by 2020 that it has established with respect to the European Union, therefore maintaining the commitment that this plan established, which was 12% for 2010. These objectives will be taken into account when establishing the premiums for this type of facility".* R-0079
[127] Act 54/1997 of 27 November 1997, on the Electricity Sector, Preamble. R-0079.
[128] Act 54/1997 of 27 November 1997, on the Electricity Sector. Article 30 (1). R-0079.

- Adopt the safety rules, technical regulations and official approval or certification regulations of the facilities and instruments that may be established by the competent administration.
- Comply with the technical generation rules, as well as with the rules on transmission and technical management of the system.
- Contract and pay the toll corresponding to the distributor and transmission company with which there may be a connection for feeding energy into their networks[129].

296. Given that the subsidies represent a cost for the SEE, borne by consumers, the regulatory body is bound to respect the principle of "*reasonable profitability*", as it will be analysed below, therefore adjusting the quantity of the subsidies to the real costs of investment and operation. Therefore, Act 54/1997 requires that producers of energy under the special regime send information to the regulatory body about the investments, costs, income and other parameters of the different real facilities[130]. This obligation is not applicable to producers under the ordinary regime.x

297. Likewise, given the major technical implications that the deployment of renewable energies means for the SEE, Act 54/1997 is especially careful about warning producers under the special regime that they will be subject to the technical standards that might be established to guarantee the technical sustainability of the SEE.

298. Together with these duties, producers of renewable energies enjoy a series of rights[131], which the following are noteworthy: (i) priority for bringing into service, (ii) access priority and (iii) the right to a specific remuneration regime other than the ordinary regime. It should be pointed out that in no event does Act 54/1997 guarantee that all the net energy produced and sold must be subsidised.

(e) Specific remuneration scheme of renewable energies

299. The energy generation plants based on renewable energies that are included in the special regime of Act 54/1997 enjoy a specific remuneration regime. Its purpose is "*to achieve reasonable profitability rates with reference to the cost of money on capital markets*"[132]. In other words, plants under the special regime are assured by law that they will receive "*reasonable profitability*", unlike renewable facilities subject to the ordinary regime, such as hydraulic facilities, which receive their remuneration in market terms.

300. This principle of "*reasonable profitability*" translates into remuneration that is the sum of two components: the *market price* for the sale of electricity[133] and a *subsidy* for guaranteeing the financial viability of said activity. This subsidy is formed by the payment

[129] Royal Decree-Act 14/2010 of 23 December, establishing urgent measures for correction of the tariff deficit in the electricity sector. Article 1 (five). R-0089.
[130] Ibid, Article 30 (1) (d). This reporting obligation is specified in Circular 3/2005 of 13 October, of the National Energy Commission, on the request for information about investments, costs, income and other parameters of electricity production facilities under the special scheme. R-0117
[131] Act 54/1997 of 27 November 1997, on the Electricity Sector. Article 30 (2). R-0079.
[132] Act 54/1997 of 27 November 1997, on the Electricity Sector. Article 30 (4). R-0079.
[133] Ibid, Articles 16 and 30 (3). R-0079.

of a premium that complements the market price[134]. Said *subsidy* is established by the government via regulations[135], and the amount thereof is considered a cost of the SEE[136].

301. The government, when establishing the premium, must take into account the established criteria in Article 30.4[137] of Act 54/1997. In this regard, the last paragraph of said article, in its original draft, sets for the following:

> *"For determining the premiums, the voltage level of the energy delivered to the network will be taken into account; plus the effective contribution to improving the environment, to primary energy savings and to energy efficiency; the economically justifiable production of useful heat and the investment costs that have been incurred, in order to achieve rates of reasonable profitability in reference to the cost of money in the capital market."*[138] *(emphasis added)*

302. Thus, the market price plus premium combination of Act 54/1997 has a clear and precise objective: providing investments with reasonable profitability according to the cost of money in the capital market.

303. The principle of **reasonable profitability** is thus conferred in the Spanish legal system, and it is a concept that, conversely, does not rule for facilities not included in the so-called special regime. This principle of reasonable profitability has remained unaltered from 1997 up to now, despite the regulatory changes.

304. Indeed, both Royal Decree-Act 9/2013 of 12 July 2013, establishing urgent measures to ensure the financial stability of the electricity system (hereinafter, "**Royal Decree-Act 9/2013**")[139] and Act 24/2013[140], which are challenged in this proceeding, maintain the principle of *reasonable profitability* for facilities as the keystone of the remuneration system for renewable energies.

C. The principle of reasonable profitability: Balance between the cost of the subsidies and the profitability that they generate for investors

305. As stated above, the remuneration regime of energy production using renewable sources under the RE is based on the principle of reasonable profitability, which has remained and still remains stable since 1997.

306. Regarding this point, we must highlight that the creation of the RE occurred through Royal Decree 2366/1994 of 9 December. Since its creation, the economic regime of

[134] Ibid, Article 30 (4) (b). R-0079.
[135] Ibid, Article 30 (4). R-0079.
[136] Ibid, Article 16 (6): called "cost of diversification and security of supply". R-0079.
[137] Article 30 of Act 54/1997. R-0079.
[138] Act 54/1997, Article 30.4. R-0079
[139] Royal Decree-Act 9/2013 of 12 July 2013, establishing urgent measures to ensure the financial stability of the electricity system. R-0094.
[140] Royal Decree-Act 24/2013 of 26 December, on the Electricity Sector. R-0096.

renewable energies was oriented at guaranteeing a necessary balance between "*the adequate profitability of the project and the cost for the electricity system*" [141].

307. Reasonable profitability means receiving income that allows recovering the investment costs (CAPEX) and the operating costs (OPEX) and earning profit according to market criteria. This adaptation to market criteria fulfils a triple objective at the same time: (i) remunerating the investor proportionally so that they can compete under equal conditions ("*level playing field*") with conventional energies, (ii) ensuring the electricity supply at an efficient cost for consumers and (iii) making the SEE sustainable, as it has been previously stated.

308. Thus, the methodology followed by the regulatory body for establishing the remuneration of the generation activity under the RE, based on renewable sources, is the one which has been maintained historically for establishing the remuneration of any non-deregulated parcel of the SEE. This procedure is composed of two phases:

1. Recognising and reconstructing a financial operating structure (standard facility), therefore identifying the investment costs (CAPEX) and the operating and maintenance costs (OPEX), according to market criteria and in accordance with the actions of a "diligent investor";
2. Establishing a financial return target that is dynamic, balanced and proportionate according to the capital market. This target should be achieved by adding together two components: a) market price and b) subsidies.

309. This methodology has been followed on an ongoing basis by the Kingdom of Spain. This is demonstrated by the following documents, among others:

- 2000-2010 Plan for the Promotion of Renewable Energies in Spain[142].
- 2005-2010 Renewable Energies Plan for Spain[143].
- 2011-2020 Renewable Energies Plan[144].

310. Based on the concept of reasonable profitability and on the methodology followed to establish it, its characteristics are analysed below:

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[141] Royal Decree 2366/1994 of 9 December, on the production of electrical energy by hydraulic and cogeneration facilities and other facilities supplied by resources or sources of renewable energy. Preamble. R-0222.

[142] 2000-2010 Plan for the Promotion of Renewable Energies in Spain. Chapter 6, pages 204 to 231. R-0118.

[143] 2005-2010 Renewable Energies Plan for Spain. Chapter 3.4, pages 142 to 145 and Chapter 4, pages 270 to 313. R-0119.

[144] The 2011-2020 Renewable Energies Plan refers, in several sections, to the target of a balanced financial return in terms of reasonable profitability:- Page 14: "The premiums (...) endeavour to guarantee the reasonable profitability of investments".- Page 536: "Revisions of remuneration levels: The remuneration levels can be modified according to the technological evolution of the sectors, according to the market's behaviour, [...] thereby always guaranteeing the rates of reasonable profitability. In any event, said revisions consider the evolution of the specific costs associated with each technology, with a triple final objective so that (...) the remuneration scheme evolves towards the minimum socioeconomic and environmental cost." (emphasis added). R-0120.

i) It requires a balance between the cost of the premiums for the consumer and profitability for the investor.

ii) It is dynamic in nature.

iii) It represents a guarantee for the investor.

iv) It imposes the obligation of a result upon the regulatory body.

311. Likewise, as we will demonstrate below, this principle was known and was invoked by associations of renewable energy producers, both the most important one in Spain, APPA[145], and by minor ones (ASIF[146] and the Spanish Wind Energy Association), and as a whole by the most important renewable energy producers and consultants in Spain. Therefore, the Claimant cannot reasonably have been unaware of either this principle or of the established case-law of the Supreme Court that interprets and confirms it.

312. Profitability must be "reasonable" for the investor and "reasonable" for the system. Reasonable profitability means a point of equilibrium between the income of the producer under the special regime and the costs that that income represents for the consumer. Disequilibrium between both elements involves either non-sustainability of the system or excessive charges for consumers. The need for this equilibrium was established when the special regime was created in 1994[147], and it has been maintained in the different regulatory instruments that have implemented Act 54/1997.

313. Thus, Royal Decree 436/2004 of 12 March, which establishes the methodology for updating and systematising the legal and financial scheme of electric power production under the special regime (hereinafter, "**Royal Decree 436/2004**"), affirms the following in its Preamble:

> *"the Royal Decree guarantees that owners of facilities under the special scheme will receive reasonable remuneration for their investments and also that electricity consumers will be given fair assignment of the costs attributable to the electricity system". (emphasis added).*[148]

314. The 2005-2010 Renewable Energies Plan likewise indicated:

> *"The analysis that is made attempts to balance the application of resources in order to reach levels of profitability for the investment to make it attractive in relation to other*

[145] Proposed Bill for the Promotion of Renewable Energies of 20 May 2009 by APPA-Greenpeace submitted on 21 May 2009 to the Ministry of Industry, Tourism and Commerce and letter sent to the Institute for the Diversification and Savings of Energy (hereinafter, "**IDAE**") of the Association of Producers of Renewable Energies (APPA) and Greenpeace on the Bill for the Promotion of Renewable Energies, dated 21 May 2009. R-0187 and R-0186.

[146] Arguments submitted by ASIF to Draft Royal Decree 1565/2010. R-0190

[147] Royal Decree 2366/1994 of 9 December, on the production of electrical energy by hydraulic and cogeneration facilities and other facilities supplied by resources or sources of renewable energy. Preamble, RD 0222.

[148] Royal Decree 436/2004 of 12 March, which establishes the methodology for updating and systematising the legal and financial scheme of electric power production under the special scheme. R-0099.

alternatives in a sector with equivalent profitability, risk and liquidity, and always attempting to optimise the available public resources."[149]

315. In turn, Royal Decree 661/2007 of 25 May, regulating the activity of electricity production under the special regime (hereinafter, "**Royal Decree 661/2007**") reiterates the following in its Preamble:

> *"The economic framework established in this royal decree implements the principles set out in Act 54/1997 of 27 November, on the Electricity Sector, thereby guaranteeing that owners of facilities under the special regime will receive* ***reasonable*** *profitability for their investments and also guaranteeing that electricity consumers will receive* ***reasonable*** *assignment of the costs attributable to the electricity system."*[150] *(emphasis added)*

(1) It is dynamic in nature.

316. Article 30 (4) of the Act of 1997 defines the profitability to be conferred to producers of the special regime as "reasonable". According to the dictionary of the Royal Spanish Academy of Language, "*reasonable*" means "*adequate, according to reason, proportionate or not exaggerated*"[151]. The precept therefore does not require that the profitability granted to producers under the special regime be "inalterable", "fixed" or similarly defined. Act 54/1997 uses the term "reasonable".

317. Moreover, the law defines reasonable profitability in reference ot the cost of money in the capital market. The dictionary of the Royal Spanish Academy of Language defines reference as "*action or effect of referring*"[152] and "to refer" is defined as "*directing, guiding or ordering something towards a certain and determined purpose or object or relating something to another thing or to a person*"[153].

318. Consequently, the cost of money in the capital market is not a mere programmatic criterion. Far from it: it is the criterion of comparison imposed by the law that allows the regulatory body to determine if a profitability at a given time is reasonable or not.

319. Therefore, the criterion used by the legislature to judge said reasonableness is not a static element, rather an element that is essentially *dynamic*. As dynamic as the *cost of money in the capital market*. As it has been pointed out by the Supreme Court of the Kingdom of Spain:

> *"The thesis according to which the "reasonable profitability" that was estimated a certain point in time must remain unchanged, without further ado in the future, cannot*

[149] Renewable Energies Plan in Spain. 2005 -2010. Institute for the Diversification and Savings of Energy of the Ministry of Industry, Tourism and Commerce. Page 27. R-0119.
[150] Royal Decree 661/2007 of 25 May, regulating the activity of electricity production under the special scheme. R-0101
[151] Definition of the word "reasonable" according to the DRAE. R-0213.
[152] Meaning of the word "reference". RAE- Meaning of the word reference. (RAE) Dictionary of the Spanish language, electronic version (twenty-third edition, October 2014). R- 0214.
[153] Meaning of the word "refer". (RAE). Dictionary of the Spanish language, electronic version (twenty-third edition, October 2014). R-0215.

> *be shared. Depending on the change of financial circumstances and circumstances of other types, a percentage of profitability could be "reasonable" at that first moment and could require subsequent adjustment to precisely maintain that "reasonableness" due to the modification of other financial or technical factors."*[154] *(emphasis added).*

(2) It represents a "guarantee" for the investor.

320. Reasonable profitability means a guarantee for the investor. By legally imposing that subsidies have to provide reasonable profitability, the law seeks to provide investors with security, given that the SEE assumes the commitment to ensure that they recover their investment and operating costs and earn, in any event, profitability that could be justified within the system as a whole.

321. Investor risk is reduced with said legal guarantee. It should be recalled that investor risk is a basic financial hypothesis to be considered before undertaking an investment. Therefore, the reduction of risk implicitly involves a cushioning of the expectations of profitability to be earned by investors. It's a proof in economic theory that in the "profitability" – "risk" combination, the lower the risk, the lower the profitability.

(3) It imposes the obligation of a result upon the regulatory body.

322. Article 30.4 of Act 54/1997 does not establish the specific mechanism that must be followed for determining reasonable profitability. Said article only authorises the Government to establish it in the corresponding regulation. In this regard, the Supreme Court of the Kingdom of Spain, since its judgement of 25 October 2006, has indicated that:

> *"Conversely, the remuneration scheme that we analyse does not guarantee the intangibility of a particular level of profit or income for owners of facilities under the special scheme in relation to that which was obtained in previous years, or the indefinite permanence of the formulas used to set the premiums."*[155]

323. In view of a possible change in the mechanism of subsidies for renewables, the only limit that the law provides for is that, in any event, the new model that is implemented must continue guaranteeing "*reasonable profitability*" for investments. Reasonable for investors and reasonable for the consumers who have to pay for the cost.

D. Case-law of the Supreme Court: determination of the basic conditions of the special regime

324. In application of Act 54/1997, the Kingdom of Spain has approved various rules that have meant changes in the special regime subsidy mechanism. These changes have given rise to considerable litigation, which in turn has originated in the well established case-law of the Supreme Court of the Kingdom of Spain.

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[154] Judgement of Chamber Three of the Supreme Court of 25 September 2012, rca 71/2011, Legal Ground Three (R-0148), reiterating the decision of the judgement of Chamber Three of the Supreme Court of 19 June 2012, rca 62/2011. R-0146.

[155] Judgement of Chamber Three of the Supreme Court of 25 October 2006, RCA 12/2005, reference case-law database EDJ 2006/282164. Legal Ground Three. R-0138.

325. The Supreme Court is the ultimate interpreter of the Spanish Legal System.[156] Moreover, it is the body that holds jurisdiction to hear appeals against the regulations (royal decrees) issued by the government of Spain.[157] Its case-law complements the Spanish Legal System[158]. Therefore, no diligent investor could ignore the interpretation of the special regime made by case-law of the Supreme Court.

326. The Claimant, who knows the importance of the case-law of the Supreme Court, restricts itself to invoking that case-law at its convenience[159] to defend the existence of a supposed agreement entered into between the Ministry of Industry and the wind and solar thermal sectors in 2010. It is therefore not credible that the case-law of the Supreme Court on the rights of producers of renewable energies would not integrate the expectations of the Claimant upon investing in Spain. As we will see below, not only was the Claimant perfectly aware of the *ius variandi* limits of the regulatory body established by the Supreme Court of the Kingdom of Spain, but also the most representative associations of the wind and solar thermal sectors.

327. The Arbitral Tribunal cannot therefore be unaware of this case-law when reaching a decision about the expectations that the Claimant must have reasonably formed about the Spanish legal system when making their investment.

328. This case-law configures the nature, the scope and the limits of the remuneration regime of the RE.

329. The Supreme Court, upon hearing the direct challenge against Royal Decree 436/2004, already expressly refused the freezing of the remuneration system in its Judgement of 15 December 2005[160].

330. Following that decision, the Supreme Court had the opportunity to declare itself regarding the regulatory amendments made to Royal Decree 436/2004. In any event, it confirmed the legality thereof. In the important Judgement of 25 October 2006, the Supreme Court expressly denies that investors have the right to receive an immovable tariff. It only recognises that they have the right to obtain rates of reasonable profitability in accordance with Article 30.4 of Act 54/1997. According to this Judgement:

> *"electricity producers under the special regime do not have an "unalterable right" to remain in an unchanged economic regime governing the collection of premiums. The scheme is, in fact, to encourage the use of renewable energy through an incentive mechanism, like all of this genre, and cannot be guaranteed to remain unchanged in the future."*[161] (emphasis added)

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[156] Article 122 of the Spanish Constitution. R-0006.
[157] Act 29/1998 of 13 July, regulating Administrative Justice, Article 12. R-0071.
[158] Article 1.6 of the Civil Code. R-0095.
[159] Memorial on the Merits, paragraphs 363 to 365.
[160] Judgement from the Supreme Court of 15 December 2005: "There is no legal obstacle so that the government, exercising the regulatory power and the broad authorisations that it has in a highly regulated area such as the electricity sector, might modify a specific remuneration system, [...]." R-0137.
[161] The Judgement of the Supreme Court of 25 October 2006, rca 12/2005, subsequently adds: "The remuneration scheme that we analyse does not guarantee [...] the intangibility of a particular level of

331. Moreover, case-law expressly establishes that the financial support regime for renewable energies in the SEE is linked to and contributes to the sustainability of the system. In this regard, said Judgement of 25 October 2006 establishes that the regime of incentives and premiums is framed within the system as a whole, which is impacted by the current economic circumstances at any given time[162].

332. In this same Judgement of 25 October 2006, the Supreme Court affirms that the remuneration modifications do not contradict the principles of legal security and legitimate expectation. Regulatory changes are admissible as long as the principle set forth in Act 54/1997 is respected: reasonable profitability[163].

333. This case-law was subsequently confirmed. Thus, the Judgements of the Supreme Court of 20 March 2007[164] and of 9 October 2007 should be highlighted, in which the High Court repeats that there is no acquired right to receive the premium[165].

334. Royal Decree 436/2004 was replaced by Royal Decree 661/2007[166]. Replacement of the scheme established in Royal Decree 436/2004 gave rise to the filing of several appeals before the Supreme Court. Similarly to what the Claimant maintains in this arbitration with respect to Royal Decree 661/2007, several producers of electric power under the special regime understood that Article 40.3 of Royal Decree 436/2004[167] contemplated a "*freeze*" of the previous incentive design.

335. In 2009, the Spanish Supreme Court reiterated its case-law on the scope of regulation of the electric sector and on the rights and guarantees of economic agents. It repeated that in no event did these rights include the right to the immutability of the financial regime.

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profit or income for owners of facilities under the special scheme in relation to that which was obtained in previous years, or the indefinite permanence of the formulas used to set the premiums." (emphasis added). R-0138.

[162] Judgement of the Supreme Court of 25 October 2006, rca 12/2005: "Just like how, according to factors of economic policy [...], the premiums and incentives for the production of electric energy under the special scheme can increase from one year to the next, they can also decrease when those same considerations make it advisable. As long as, we repeat, the variations are kept within the legal limits that govern this mode of promotion, the mere fact that the updating or financial significance of the premium may increase or decrease does not constitute, by itself, reason for nullity, nor does it affect the legitimate expectation of the recipients." (emphasis added). R-0138.

[163] Judgement of the Supreme Court of 25 October 2006, rca 12/2005: legal security is not incompatible with regulatory changes from the perspective of the validity of the latter, [...] The same consideration is applicable to the principle of legitimate expectation [...] The appellants put forth that their investments in the activity of electric power production under the special scheme were made at a certain point in time, thereby "trusting that the administration would not change the legal conditions that were determinant so that (...) they would decide to build the facilities", which is the premise from which they deduce that the reduction of the premiums after Royal Decree 2351/2004 with respect to those established in Royal Decree 435/2004 would be contrary to said principle. Such reasoning, referring to an incentivising mechanism such as that of the premiums in question, cannot be shared." R-0138.

[164] Judgement of the Supreme Court of 20 March 2007. R-0139.

[165] Judgement of the Supreme Court of 9 October 2007. R-0140.

[166] Royal Decree 661/2007 of 25 May R-0101.

[167] Royal Decree 436/2004. Article 40: "Article 40. Revision of tariffs, premiums, incentives and allowances for new facilities [...] 3. The tariffs, premiums, incentives and allowances that may result from any of the revisions considered in this section will be applicable only to the facilities that come into operation after the entry-into-force date referenced in the preceding section, with no retroactivity regarding previous tariffs and premiums". (emphasis added). R-0099.

336. Indeed, according to the Supreme Court, there are only two limitations to the State's regulatory power: 1) that the change does not affect earnings already received and 2) that the principle of reasonable profitability is not infringed. It is thus set forth in three major judgements, one dated 3 December 2009 and two dated 9 December 2009. In the first of those judgements, the Supreme Court indicates the following:

> *"since the setting in stone or freezing of the remuneration system cannot be gathered from the prescriptive content of Law 54/1997, of 27 November, on the Electric Sector for titleholders of electric power facilities under the special scheme; or a recognition of the right of producers under the special scheme to the scheme unchangeability of the said scheme. The reason for it is that the Government, in compliance with the legislator's plan, has a degree of discretion to determine the energy yields offered, (...) and taking into account - on exercising its regulatory power - the obvious, essential general interests involved in the proper functioning of the electricity production and distribution system, and specifically, users' rights."*[168] (Emphasis added)

337. The clarity of the case-law that is applicable to this sector is evident: the regulatory development of the remuneration of the special regime is made dependent upon the legal regulations (Article 30.4 of Act 54/1997), to which case-law is subordinate in accordance with the principle of regulatory hierarchy. It is therefore clear that the Kingdom of Spain did not offer that its system of premiums would be frozen for investors, in prejudice to consumers or the SEE.

338. In 2009, the Claimants alleged a violation of the principle of legal security. However, the Supreme Court established that:

> *"The argument (...) must be rejected, since it is not deduced that said law (Royal Decree 661/2007 does not respond to the requirements of the principle of legal security, which includes no right to a freezing of the existing legal system."*[169] (emphasis added)

339. The Claimants also alleged in 2009 the violation of the principle of legitimate expectation. However, the Highest Spanish Court reiterated in all these Judgements that:

> *"the principle of legitimate expectation does not guarantee the perpetuation of the existing situation, which can be modified within the framework of the discretionary power of public institutions and powers to impose new regulations in appreciation of needs of general interest."* (emphasis added)

340. The aforementioned case-law is sufficiently clear. However, two other judgements of 9 December 2009 should be highlighted, issued in similar appeals against Royal Decree 661/2007. In said judgements, the Supreme Court definitively established the rights of investors in the special scheme, and it even reprimanded the Claimant for not taking applicable case-law into account:

[168] Judgement of the Supreme Court of 3 December 2009, Legal Ground Four. R-0141.
[169] Judgement of the Supreme Court of 3 December 2009, Legal Ground Four. R-0141.

> *"[...] [the Claimant] does not pay sufficient attention to the case-law of this Chamber that has been specifically handed down regarding the principles of legitimate expectation and non-retroactivity applied to the successive regimes for incentivising the generation of electricity. They refer to the considerations included in our judgement of 25 October 2006 and reiterated in the judgement of 20 March 2007, among others, regarding the legal situation of the owners of electrical energy production facilities under the special regime, for whom it is not possible to recognise a "non-unalterable right "to keep the remuneration framework approved by the holder of the regulatory authority unaltered in the future, as long as the prescriptions of the LSE regarding the reasonable profitability of the investments are respected."* [170]
> (emphasis added)

341. In these judgements, the Supreme Court reiterated what it already established in 2006 and 2007 regarding the regulatory modifications of Royal Decree 436/2004, now applying it in relation to Royal Decree 661/2007[171]. In other words, its case-law remains constant: there is no unalterable right to the fact that a specific framework of remuneration must be kept. It can only be expected that said framework of remuneration must respect the principle of reasonable profitability.

342. Royal Decree 661/2007 was subsequently amended by Royal Decree 1565/2010 of 19 November, thereby regulating and modifying certain aspects pertaining to the activity of electrical energy generation under the special regime (hereinafter, "**RD 1565/2010**"),[172] and Royal Decree-Law 14/2010 of 23 December, thereby establishing urgent measures for correction of the rate deficit of the electrical sector (hereinafter, "**Royal Decree-Act 14/2010**")[173]. Once again, many producers challenged this reform before the national courts, arguing that these amendments were retroactive and impossible to foresee by a diligent investor when making their investment in accordance with Royal Decree 661/2007. Regarding these challenges, the Supreme Court issued a long series of judgements between 12 April 2012 (when the first one was handed down) and November 2012, thereby once

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[170] "As it was stated by this chamber in its judgement of 25 October 2006 (R-0138), reiterated in the judgement of 20 March 2007 (R-0139): "the owners of electrical energy production facilities under the special scheme do not have an "unmodifiable right" to keep the financial scheme that regulates the receipt of premiums unaltered. Essentially, said scheme attempts to promote the use of renewable energies through an incentivising mechanism that, like all mechanisms of this kind, does not have the assurance that it will remain unmodified for the future. [...] Companies that freely decide to set up in a market such as electricity generation under that special scheme, knowing beforehand that it largely depends on the establishment of financial incentives by public authorities, are or should be aware that such incentives can be modified by said authorities within legal guidelines. One of the "regulatory risks" to which they are subject, which they will have to count on, is precisely that of the variation of the parameters of the premiums or incentives, which the Law on the Electrical Sector tempers (in the aforementioned sense) but does not exclude."[170] (emphasis added). Judgement of the Supreme Court of 9 December 2009, app. 152/2007, reference: Law 2009/307357, Legal Ground Six. R-0106.

[171] Judgement of Chamber Three of the Supreme Court of 9 December 2009, app. 152/2007, reference: Law 2009/307357, Legal Ground Five. R-0106.

[172] Royal Decree 1565/2010 of 19 November, which regulates and modifies certain aspects pertaining to the activity of electrical energy generation under the special scheme. R-0104.

[173] Royal Decree-Act 14/2010 of 23 December, which establishes urgent measures for correction of the rate deficit of the electrical sector. R-0089.

again reiterating and confirming its case-law for investors regarding the limits and scope of the concept of reasonable profitability[174].

343. In this case-law, the Supreme Court once again reiterates that the owners of facilities under the special regime do not have the unalterable right to the fact that the financial regime that regulates the receipt of their remuneration must remain unchanged. In this regard, it is notable that the Supreme Court, in its decision, introduces an assessment of the circumstances of the economic crisis to which the Kingdom of Spain was subject at that time, as well as the existence and amount of the rate deficit:

> *"If these circumstances entail adjustments in many other production sectors [...],it is not unreasonable for them also to extend to the renewable energies' sector which wished to keep receiving the regulated tariffs instead of opting for the market mechanisms [...].And this is all the more so in the event of situations involving a widespread economic crisis and, in the case of electrical energy, in view of the growth in the tariff deficit which, to a certain degree, derives from the impact that the remuneration of the former has on the calculation of access fees by way of the regulated tariff insofar as it is a cost imputable to the electricity system."*[175] (emphasis added)

344. Even more so, in that same judgement and in other, subsequent judgements, the Supreme Court made three very specific observations in which it once again reiterated the possibility of modifying the remuneration regime of renewable technologies.

345. First of all, the judgement of 12 April 2012 sets forth that Article 30.4 of Act 54/1997 does not guarantee that a regulated rate will be received for a certain period of time:

> *"The reasonable remuneration [...] does not need to imply, we repeat, that remuneration has necessarily to be by means of a regulated tariff (it may be so, in the*

[174]Judgements of the Supreme Court of 20 December 2011, app. 16/2011 (R-0143); of 12 April 2012, app. 50 and 112/11; of 19 April 2012, app. 39 (R-0029) and 97/11 (R-0030); of 23 April 2012, app. 47/2011 (R-0031); of 3 May 2012, app. 51 and 55/2011 (R-0032 and R-0033); of 10 May 2012, app. 61 and 114/2011 (R-0034, R-0035); of 14 May 2012, app. 58/2011 (R-0036); of 16 May 2012, app. 46/11 (R-0037); of 18 May, app. 70 and 74/110 (R-0038 and R-0039); of 22 May 2012, app. 45 and 49/11 (R-0040 and R-0041); of 30 May 2012, app. 59/2011 (R-0042); of 18 June 2012, app. 54/211 (R-0043), 56 (R-0044), 57 and 63/11; of 25 June 2012, app. 109 (R-0053) and 121/11 (R-0054); of 26 June 2012, app. 566/10 (R-0055); of 9 July 2012, app. 67/1, 94 (R-0057) and 101/11 (R-0058); 12 July 2012, app. 52/11 (R-0059); of 16 July 2012, app. 53/11 (R-0044), 75 and 119/11; of 17 July 2012, app. 19 and 37/11; of 18 July 2012, app. 19/11; of 19 July 2012, app. 44/2011; of 25 July 2012, app. 38/2011; of 26 July 2012, app. 36/11; of 13 September 2012, app. 48/11; of 17 September 2012, app. 43, 87, 88, 106 and 120/11; 18 September 2012, app. 41/11 (R-0045); of 25 September 2012, app. 71/11 (R-0046); of 27 September 2012, app. 72/2011 (R-0047); of 28 September 2012, app. 68/2011; of 8 October 2012, app. 78, 79, 100 and 104/11 (R-0048, R-0049, R-0050) ; of 10 October 2012, app. 76/2011 (R-0051); of 11 October 2012, app. 95 and 117/11 (R-0052 and R-0053) ; 15 October 2012, app. 64, 73, 91, 105 and 124/11 (R-0054, R-0055, R-0056, R-0057 and R-0058) ; of 17 October 2012, app. 102/2011 (R-0059) ; of 23 October 2012, app. 92/2011 (R-0060); of 30 October 2012, app. 96/2011; of 31 October 2012, app. 77 and 126/11; of 5 November 2012, app. 103/2011; of 9 November 2012, app. 89/2011; of 12 November 2012, app. 98 and 110/11; of 16 November 2012, app. 116/11; of 21 November 2012, app. 34/2011 and 26 November 2012, app. 125/2011. (those not specifically listed are document R-0142.)

[175] Judgement of the Supreme Court of 12 April 2012, app. 40/2011, Legal Ground Four. R-0144.

future, at market prices) and, in particular, that the former is ensured for more than thirty years."[176]

346. Secondly, since 2012 the Supreme Court of the Kingdom of Spain has been clear about the extent of the concept of reasonable profitability with respect to the duration of subsidies:

> " *the principle of reasonable rate of return must in fact be applied to the entire lifetime of the facilities, but not (...) as meaning that during the whole lifetime this principle guarantees the production of profits, but rather as meaning there is a guarantee that the investments made in the facilities obtain, during its existence taken as awhole, a reasonable rate of return. Which clearly (...) do not imply the continuance of a particular premium throughout the entire life of the facilities, since it is quite possible for the investments to be amortised, and for the reasonable rate of return to have been achieved long before the operating period comes to an end. Consequently, the provision cited cannot be understood as meaning the feed-in tariff scheme must remain in existence throughout the entire lifetime of the facilities."*[177].

347. In this case, the wind farms of the Claimants have ceased to receive the RI. The reason is based on the fact that the standard facilities in which said plants are included had reached a profitability of 7.398 at the time when the new regulation entered into force. In other words, said standard facilities had reached the reasonable profitability expected for the entire regulatory life of the plant before the end of its operational period.

348. Finally, the Supreme Court denies that even a specific rate of return can be kept unchanged:

> *"According to the claim, [...] the 'significant loss in returns' [...]must be viewed by comparing the rates of return resulting from this Decree with those resulting from the regulations prior to this Decree [...] <u>The idea that the "reasonable rate of return" estimated at a particular moment in time must remain unaltered, at other moments in time, cannot be shared. Depending on changing economic and other circumstances, a rate of return percentage viewed as "reasonable" in a first instance, may require subsequentadjustments precisely in order to maintain the "reasonableness" when faced with the modification of other economic and technical factors</u>."*[178] (emphasis added)

349. These decisions are reproduced in similar terms in the judgement of 25 June 2013,[179] and they have been ratified most recently by Judgement 63/2016 of 21 January 2016, of the Supreme Court, thereby dismissing new appeals against Royal Decree 1565/2010 of 19 November and Royal Decree-Act 14/2010 of 23 December. In this judgement, the Supreme Court once again insists on the fact that Royal Decree 661/2007 never froze the financial scheme in force:

[176] Judgement of the Supreme Court of 12 April 2012, app. 40/2011, Legal Ground Seven. R-0144.
[177] Judgement of the Supreme Court of 12 April 2012, app. 40/2011 (R-0144). Also cited, among others, in the judgement of the Supreme Court of 19 June 2012 (appeal 62/2011). R-0146
[178] Judgement of the Supreme Court of 19 June 2012 (appeal 62/2011). R-0146.
[179] Judgement of the Supreme Court of 25 June 2013 (RJ/2013/6733) app. 252/2012. R-0150.

" We do not consider, in effect, that the above Royal Decree [661/2007] considers a tariff regime for ever, nor that the Government, when exercising their legal power of authority, or the legislator, using their legislative authority, may not adapt or modify this regime to new circumstances (economic, productive, technological or of any other nature) that may arise in such an extended period of time."[180]

350. The definitiveness, clarity and continuity of the applicable case-law leaves no doubt about the scope, content and legal limits of the remuneration regime based on the reasonable profitability to which investors were entitled. And therefore, it leaves no doubt for assessing the real legitimate expectations that the Kingdom of Spain was offering to all national or foreign investors.

351. In other words, all investors knew or should have known the following essential conditions of the special scheme remuneration system:

a) The production activity based on renewable sources is an activity that is integrated in, not isolated from, the SEE, and therefore the remuneration thereof constitutes a cost of the SEE, subordinate to the principle of financial sustainability.
b) Given that the sustainability of the SEE depends on the balance between its income and costs, the cost of implementing renewables is determined according to the foreseeable evolution of the demand and of other basic economic data.
c) To the extent that producers of renewable energies cannot recover the costs they incur through the market price, it is necessary for the SEE to complement that market price through a subsidy that guarantees a level playing field.
d) This subsidy has always been set based on the investment and operating costs of a standard facility, and its objective is for investors to be able to recover the CAPEX and OPEX and earn reasonable profitability according to the capital market.
e) The principle of reasonable profitability, the corner stone of the renewable energies production system based on renewable sources, is characterised by its equilibrium and dynamism.

352. The importance of the case-law of the Supreme Court of the Kingdom of Spain has been expressly recognised by the first arbitration award that was handed down regarding Royal Decree 661/2007 and the general regulatory framework thereof. It was the award given in the case, *Charanne B.V. v Spain* on 21 January 2016.[181] The award gives an opinion about the value of the case-law of the Supreme Court of the Kingdom of Spain and states:

"507. (...)To the Tribunal's understanding, at the time of making the investment in 2009 the Claimants could have carried out an analysis of their investment's legal framework in Spanish law and understood that the regulations enacted in 2007 and 2008 could be modified. At least that is the degree of diligence that could be expected from a foreign investor in a heavily regulated sector like the energy industry. In such a sector, thorough prior analysis of the legal framework applicable thereto is essential to make an investment.

[180] Judgment 63/2016 of 21 January 2016 of the Supreme Court handed down on appeal to the Supreme Court 627/2012. Legal ground six. R-0155
[181] *Charanne B.V. v Spain*, SCC Arbitration No. 062/2012. RL-0049.

> *508. Although these decisions by the Spanish courts are not binding on this Arbitration Tribunal, they are factually relevant to verify that the investor was unable, at the time of the disputed investment, to have the reasonable expectation that in the absence of a specific commitment the regulation was not going to be modified during the lifespan of the plants".*[182] (Emphasis added)

353. In the *Charanne* case, the court not only gives its opinion about the value of the case-law of the Kingdom of Spain, but also about the principle of "reasonable profitability" as a guide for the remuneration given to renewable energies:

> *"518. The Arbitration Tribunal understands that Royal Decree 661/2007*[183] *and Royal Decree 1578/2008*[184] *establish specific rules whose essential characteristics are offering a guaranteed tariff (or a premium, where appropriate) as well as privileged access to the electricity transmission and distribution grid, to each energy producer that fulfils the established requirements. Within the framework of the LSE, said principles make it possible to guarantee to renewable energy producers the reasonable returns to which Article 30.4 LSE refers".*[185] (Emphasis added)

E. The applicable legal regime at the time when the Claimant made their investment.

(1) Introduction: Renerco has been involved in the development of the projects since their beginning.

354. This section will analyse the regulatory framework in force when the Claimants made their investments in the renewables sector in Spain.

355. Therefore, and as a prior step to analysing their fit in the SEE, a brief description of said investments of the Claimants will be provided.

(1.1) The Claimants' investment

356. La Muela[186] was promoted by the German company Thyssen Rheinstahl Technik GmbH ("Thyssen") in cooperation with the Danish company, NEG Micon A/S ("NEG Micon")[187], a producer of wind turbines, and its Spanish subsidiaries: TAIM Nordtank Eólica Aragonesa, S.A. ("TAIM Nordtank"), Desarrollo de Energías Renovables Aragonesa, S.A. ("DERASA") and TAIM NEG Micon Eólica, S.A. ("TAIM NEG Micon").[188]

357. In November 1997, TAIM Nordtank and Thyssen signed an agreement according to which the former transferred to the latter the rights for developing the project. In exchange

[182] Ibid, paragraphs 507 and 508.
[183] Royal Decree 661/2007. R-0101
[184] Royal Decree 1578/2008 of 26 September, on remuneration for the production of electric energy using solar photovoltaic technology for facilities after the deadline for maintaining the remuneration of Royal Decree 661/2007, of 25 May, for such technology. R-0102
[185] Ibid, paragraph 519
[186] The La Muela project includes the wind farms of La Carracha and Plana de Jarreta.
[187] This Danish company subsequently merged with Vestas Wind Systems A/S.
[188] Memorial on the Merits, paragraph 152. DERASA was the company that initially obtained the rights to develop the projects from the Government of Aragón on 22 April 1997 (Memorial on the Merits, paragraph 80).

for said acquisition, a subsidiary of TAIM Nordtank, NEG Micon, would supply the turbines that would be used at the wind farms and would collaborate with Thyssen to obtain the necessary permits for developing the project.[189]

358. In December 1998, TAIM NEG Micon obtained the construction permit for the La Carracha and the Plana de Jarreta wind farms.[190]

359. On 27 January 1997, Thyssen, Bayerische Hypo- und Vereinsbank Aktiengesellschaft ("HypoVereinsbank"), BVT Holding GmbH & Co. KG ("BVT Holding") and ETAPLAN Project GmbH & Co. KG ("ETAPLAN") founded the entity, PDF Project Development Fund GmbH & Co. KG. ("PDF Project Development Fund") for performing all the procedures of the necessary projects for construction.[191]

360. Mr Matthias Taft, current Chief Executive of BayWa RE and member of the Board of Directors of BayWa AG, had been the "*Project Manager*" of ETAPLAN since 1994.[192]

361. On 11 March 1999, PDF Project Development Fund founded La Carracha S.L. and La Plana de Jarreta S.L.[193] as holding companies of the wind farms. To manage the facilities that were common to both wind farms, the New La Muela Wind Farms Economic Interest Grouping [Agrupación de Interés Económico Nuevos Parques Eólicos La Muela, A.I.E.] ("A.I.E") was founded on 30 March 1999, held in its entirety by the two aforementioned companies.[194]

362. On 13 September 1999, the equity holdings in the projects were transferred to a subsidiary of PDF Project Development Fund, called PDF Share Capital GmbH ("PDF Share Capital").[195]

363. On 24 July 2001, the Directorate-General of Aragón (the "Government of Aragón" or "DGA") acquired a small equity holding in the projects (4.1% in La Carracha and 8.2% in La Plana de Jarreta) from PDF Share Capital.[196]

364. On 28 December 2001, a partnership agreement was signed between PDF Share Capital, PDF Project Development Fund, BVT Energie- und Umwelttechnik AG ("BVT"),[197] NEG Micon, S.A.U. and two additional investors: TXU Europe Energy Trading B.V. ("TXU") and Blue Energy AG ("BEAG") (the so-called "Framework Agreement")[198] for financing the projects.

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[189] Memorial on the Merits, paragraph 154 and document C−0042: agreement between Taim Nordtank Eólica Aragonesa, S.A. and Thyssen Rheinsthal Technik GmbH for transfer and development of the rights over the wind farms, dated 28 November 1997.
[190] Document C−0043, construction permit of 30 December 1998.
[191] Document C-0291.
[192] Sworn statement of Mr Taft dated 24 February 2016. CWS−MT, paragraphs 1 and 10.
[193] Documents C-0044 and C-0045.
[194] Memorial on the Merits, paragraph 159 and document C-0046.
[195] Documents C-0063 and C-0064.
[196] Document C−0065.
[197] BVT was in the same business group as BVT Holdings. In this regard, see **EO-##**, [https://web.archive.org/web/20010202164200/http://www.bvt.de/gruppe/fmgruppe.html].
[198] Document C−0067.

365. Mr Taft was one of the signers of the agreement in representation of BVT and was selected as a member of the new board of directors of the projects for a period of five years[199].

366. The projects were financed approximately with a structure of 25% capital and 75% debt. Regarding the capital, it was provided by the investors of the projects using a combination of equity holdings and subordinated loans. Regarding the debt, a syndicate of banks, which included Caja de Ahorros y Monte de Piedad de Madrid ("Caja Madrid") and HypoVereinsbank, contributed the bank financing for the projects.[200]

367. The projects were commissioned in November 2002, and their commercial operations began in 2003.[201] Two of the companies that had equity holdings in the projects sold them soon after the projects were commissioned. This was how Falck Renewables ("Falck") acquired the equity holdings from BEAG in June 2003[202] and Shell from TXU Energy in July 2003.[203]

368. On 28 July 2003, Renerco, the second Claimant, was created as a result of the merger of several equity holders in the projects (ETAPLAN, BVT and PDF Project Fund Management GmbH), thereby obtaining an equity holding of 30% in the capital and subordinated loans.[204] According to the Claimants, *"from the date of its inception, RENERCO owned approximately a 34% interest in the Project Companies and inherited the project portfolio and general expectations of its founding parents*."[205]

369. In December 2005, Renerco acquired a 2.6% interest in the projects from PDF Share Capital.[206]

370. On 3 November 2009, BayWa RE[207] purchased 87.8% of Renerco's equity holdings[208]. That same year, Mr Taft was appointed as Chief Executive of BayWa RE.[209]

371. On 8 September 2011, Renerco acquired Shell's equity holding in the projects and entered into an agreement with Shell for the assignment of equity loans, according to which Renerco was subrogated in Shell's position in those loans.[210] According to Mr Taft, the

[199] Document C−0067, paragraph 2; sworn statement of Mr Matthias Taft, CWS−MT, of 24 February 2016, paragraph 39.
[200] Document C−0227, paragraph 4; Memorial on the Merits, paragraph 167; Sworn statement of Mr Matthías Taft of 24 February 2016. CWS−MT, paragraphs 22.
[201] Memorial on the Merits, paragraph 167; **CWS−MT** Sworn statement of Mr Matthías Taft of 24 February 2016. CWS−MT, paragraphs 22.
[202] Document C-0071.
[203] Document C−0073.
[204] Sworn statement of Mr Matthías Taft of 24 February 2016. CWS−MT, paragraph 44 In addition to La Muela, Renerco inherited a series of renewable energy projects that were dispersed throughout Europe, according to Mr Taft's own sworn statement, paragraph 45.
[205] Memorial on the Merits, paragraph 186.
[206] Document C−0078 p. of 14 and Document C−0228, p. 14 of PDF.
[207] At the time of acquisition, BayWa RE was known as BayWa Green Energy GmbH. Sworn statement of Mr Matthías Taft of 24 February 2016. CWS−MT, paragraph 65
[208] Memorial on the Merits, paragraph 286; Document C−0098, press release issued by BayWa AG on 3 November 2009.
[209] Sworn statement of Mr Matthías Taft of 24 February 2016. CWS−MT, paragraph 12
[210] Document C−0196.

consequence of that transaction was that Renerco's equity holding in the capital of the projects was increased to 73.1% in La Carracha and 72.2% in La Plana de Jarreta.[211]

372. On 12 March 2012, Renerco acquired the equity holding that Corporación Empresarial Pública de Aragón had in both projects (0.9% in La Carracha and 1.8% in La Plana de Jarreta).[212]

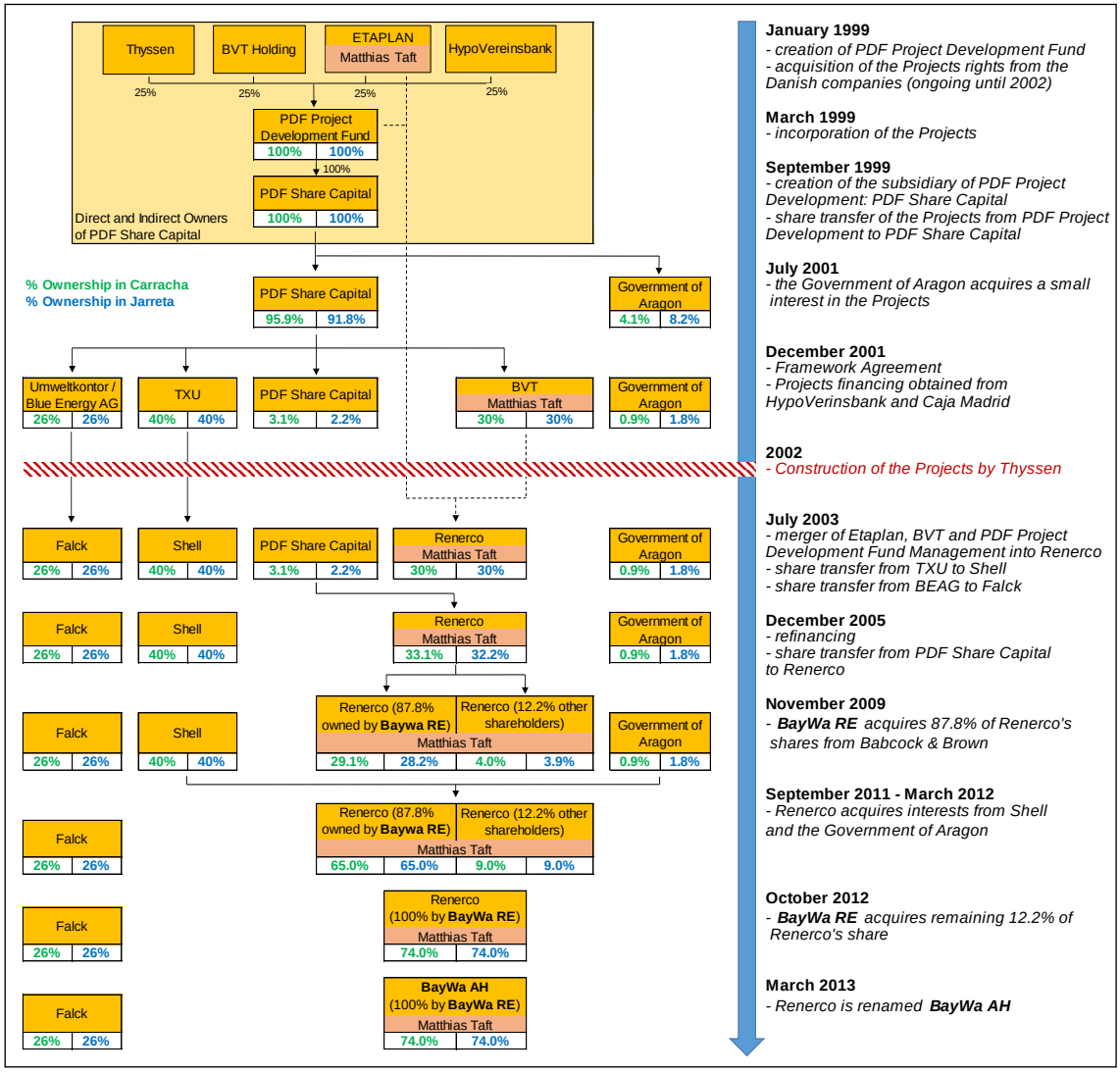
373. In October 2012, BayWa RE acquired the 12.2% of the remaining capital from Renerco and became the sole shareholder.[213]

374. At the end of 2012, Renerco (and BayWa RE, indirectly) had acquired 74% of the equity holdings in the projects. The remaining 26% belongs to Falck.

375. In 2013, Renerco changed its name to that of BayWa AH. According to the Claimants:"(as a) *result of these transactions, RENERCO acquired a 74% shareholding interest in each of the Project Companies, which corresponds to the share capital investment currently owned by BAYWA AH in La Muela*."[214]

376. This chronology of corporate operations is shown graphically in the following timeline[215]:

[211] Sworn statement of Mr Matthías Taft of 24 February 2016. CWS−MT, paragraph 87
[212] Corporación Empresarial Pública de Aragón replaced the DGA as a partner in the projects.
[213] Memorial on the Merits, paragraph 286.
[214] Memorial on the Merits, paragraph 98. BayWa AH is wholly owned by BayWa RE. BayWa AH is the successor of Renerco.
[215] Econ One Research Report of 15 June 2016, section II.B, graphic 2.



377. Now then, these facts ultimately show that BayWa AH (formally known as Renerco) and its predecessors have participated in the projects since the beginning of their development at the end of the 90s. In turn, Mr Taft, the current Chief Executive of BayWa RE, has been involved in the development of the projects since the "very early development stage."[216]

(1.2) Constant elements of the regulatory framework of the SEE

378. The Claimants have been able to see how the facilities in which they made their investment have been subject to successive regulations that have developed Act 54/1997 on renewable energies. Thus, in this arbitration proceeding we have plants that have been subject to (1) Royal Decree 2366/1994; (2) Royal Decree 2818/1998 of 23 December, on the production of electrical energy by facilities that are supplied by resources or sources of renewable energy, waste or generation (hereinafter, "**Royal Decree 2818/1998**"); (3) Royal Decree 436/2004; (4) Royal Decree-law 7/2006 of 23 June, thereby adopting urgent measures in the energy sector (hereinafter, "**Royal Decree-law 7/2006**"); (5) Royal Decree

[216] Sworn statement of Mr Matthías Taft of 24 February 2016. CWS−MT, paragraph 2.

661/2007; (6) Royal Decree-law 6/2009; (7) Royal Decree 1565/2010; (8) Royal Decree 1614/2010; (9) Royal Decree-law 14/2010 and the current regulatory framework, among other regulations.

379. The Claimants have been able to appreciate for more than 11 years how, regardless of the regulatory changes that have occurred, there are essential principles that have remained unchanged since Act 54/1997:

a. The principle that subsidies for renewables are a cost of the SEE has never been changed, and therefore setting them and maintaining them are linked to the financial sustainability of the SEE.

b. Article 30 (4) of Act 54/1997 sets forth the essence of the renewable energies remuneration system in Spain, and it has not changed since being introduced.

c. Within the framework of a sustainable SEE, subsidies have always been established with the objective of providing a standard facility with "*reasonable profitability in accordance with the cost of money in the capital market*". This profitability was linked exclusively to the cost of construction and operation of the plants.

d. The methodology used to determine reasonable profitability has always consisted in the following operations:

- To recognise and reconstruct a financial operating structure (standard facility), therefore identifying the investment costs (CAPEX) and the operating and maintenance costs (OPEX), according to market criteria and in accordance with the actions of a "diligent investor";

- To establish, based on said standard facility and within a certain period, a dynamic, balanced and proportionate target of financial return in accordance with the capital market. This target should be achieved by adding together two components: a) market price and b) subsidies

e. Regardless of the specific model of remuneration established in the successive regulations, said models have been subject to the principle of financial sustainability of the SEE and the principle of reasonable profitability.

380. Likewise, if we keep in mind that the Claimant began investing in Spain between 2003 and 2009, it would have had the opportunity for one of its qualified investors to explain to them the consistent case-law of the Supreme Court of the Kingdom of Spain, which, since 2005, determines the rights of investors with respect to changes in the remuneration models of renewable energies. This case-law, just like Article 30 (4) of Act 54/1997, has remained intact to date. This case-law is based on the following points:

- there is no right to the fact that the financial regime cannot be modified;

- as long as Article 30(4) of Act 54/1997 is not amended, the only limit that must be respected by the Government in regulatory changes is that of granting reasonable profitability to special scheme facilities in reference to the cost of money in the capital market.

- the integration of special scheme facilities into the SEE gives rise to the fact that companies have to assume a certain regulatory risk.

(2) Real Decreto 2818/1998

381. The Memorial on the Merits itself admits that:

> *"The development of La Muela goes back to 1997 when a group of foreign investors arrived in Spain with the intention to invest in wind energy production, encouraged by the Feed-in legislation recently implemented by the Respondent, through EPA 1997 and RD 2818/1998. As we will explain, some of these investors merged in 2003 following the construction of the Wind Farms and created RENERCO, today BAYWA AH*[217]*."* (Emphasis added) (footnotes omitted).

382. Article 30.4 of Act 54/1997 was first developed by Royal Decree 2818/1998. Its objective was to establish "a system of temporary incentives for those facilities that need them to have a competitive position in the free market[218]". (Emphasis added).

383. This regulation promoted the development of special scheme facilities, therefore configuring a remuneration framework based on a subsidy (premium) that complemented the market price of the energy produced, plus a complement for reactive energy[219].

384. Royal Decree 2818/1998 established that all production facilities under the special regime should be recorded in an administrative registry. This registry would allow the government to control the tariffs and premiums, thereby considering the type of energy, the installed power and, if applicable, the commissioning date. It would also allow the government to know the evolution of the electrical energy produced, the energy transferred to the network and the primary energy used.[220] The creation of this registry - subsequently called the Administrative Registry of Electrical Energy Production Facilities (hereinafter, the "**RAIPRE**")[221] - proves the desire of the legislature to verify, in any event, compliance with the targets provided for in the 2000-2010 Renewable Energies Promotion Plan in Spain.

385. The Arbitration Court's attention is drawn to the fact that all facilities, both ordinary and under the special regime, were recorded in the administrative registry[222]. The RAIPRE

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[217] Memorial on the Merits, paragraph 151.
[218] Royal Decree 2818/1998. R-0097.
[219] Articles 26 and 28 of Royal Decree 2818/1998. R-0097. Regarding the allowance for reactive energy, we must recall that it did not always represent income in favour of the producer. The payment thereof was conditioned upon the power factor according to which the energy was transferred to the distributor company. Thus, if the power factor was higher than 0.9, the producer would have a right to receive the allowance. However, if the power factor was less than 0.9, the producer would be subject to the corresponding discount.
[220] Royal Decree 2818/1998, Article 9.1. R-0097.
[221] Royal Decree 661/2007 introduces this name. R-0101.
[222] Act 54/1997 of 27 November 1997, on the Electricity Sector Article 21: "[...] 4. An Administrative Registry of Electrical Energy Production Facilities is created at the Ministry of Industry and Energy [...] 5. Recording in the Administrative Registry of Electrical Energy Production Facilities will be a necessary condition to be able to participate in the electrical energy production market in any of the contracting modes with physical delivery.6. [...] Compliance with the conditions and requisites established in

is merely a section of said administrative registry, section two[223]. Recording in this registry was therefore not a commitment by the Governemnt to indefinitely maintain the future profitability of the facilities recorded therein, rather a way to control and know who was participating in the SEE.

386. Said registry is not a novelty introduced by Royal Decree 2818/1998. Said registry already existed when Royal Decree 2366/1994 was in force[224]. It was established then, as in 1998, to also control adequate monitoring of energy planning.

387. At no time did Royal Decree 2818/1998 recognise any freeze of the subsidies. To the contrary, Article 32, under the heading of "*modifications of premiums and prices*", provided for revisions of the premiums every four years, thereby considering the following criteria: (a) the evolution of the price of electrical energy in the market, (b) the participation by these facilities in covering demand and (c) their impact on technical management of the system.

388. In other words, it provided for a mandatory revision according to said criteria, without prejudice to the fact that other circumstances or criteria, such as those related to the financial sustainability of the electrical system or the reasonability of the profitability earned by the facilities, might allow making, at any time, reforms other than those provided for in this article.

389. In any event, it is evident that no investor could undertake an investment believing that the remuneration system set forth in Royal Decree 2818/1998 would be frozen. In fact, this remuneration regime was characterised by its volatility, given that, due to being referenced to a pool, the expectation of income by an investor in renewable energies floated on the pool.

390. However, the sustained development of wind energy began under this framework. Therefore, this framework was stable enough to allow the financing of projects that required a high investment in fixed assets over a long-term time horizon.

391. The two wind farms, object of this arbitration, La Carracha and Plana de Jarreta, obtained both their definitive recording in the RAIPRE[225] and their commissioning certificate[226] while this Royal Decree 2818/1998 was in force. Nevertheless, this didn't

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authorisations or a substantial variation of the budgets that determined the granting thereof could give rise to the revocation thereof, under the terms provided for in the applicable penalty scheme. [...]". R-0079.

[223] Royal Decree 661/2007, Article 9.1. R-0101.

[224] Royal Decree 2366/1994 of 9 December. Article 6: "1. For the adequate monitoring of energy planning, both regarding installed power and the evolution of energy produced and the primary energy used, a General Registry of Special Scheme Production Facilities is created at the Directorate General of Energy of the Ministry of Industry and Energy, without prejudice to any registries of the Autonomous Communities themselves. 2. The registration of a facility in the corresponding Registry, according to the competent Administration for authorisation, will be a prerequisite for applying the special scheme regulated by this Royal Decree to said facility." As it can be observed, the content of Article 6 of Royal Decree 1994 is very similar to Article 9 of Royal Decree 2818/1998. R-0222

[225] Certificate of definitive recording of the La Carracha Wind Farm in the RAIPRE on 22 November 2002 (C-0061) and Certificate of definitive recording of the Plana de Jarreta Wind Farm in the RAIPRE on 22 November 2002 (C-0062).

[226] Commissioning certificate granted to the La Carracha Wind Farm on 25 November 2002 (C-0059) and Commissioning certificate granted to the Plana de Jarreta Wind Farm on 25 November 2002 (C-0060).

prevent, as it will be analysed below, either Royal Decree 436/2004 or Royal Decree 661/2007 from being applied to them, which, despite implementing a change in the remuneration regime, are not the object of discussion by the Claimants.

(3) 2000-2010 Plan for the Promotion of Renewable Energies

392. In execution of Act 54/1997 of 30 December 1999, the 2000-2010 Plan for the Promotion of Renewable Energies was issued[227] (hereinafter, the "**PFER**"). This close relationship between the premiums (cost of the SEE) and the financial sustainability of the SEE makes it mandatory to plan, in due detail, for the deployment of renewable technologies and for their impact on the sustainability of the SEE.

393. Said planning is developed in the so-called "*Renewable energy plans*". In these plans, there is an assessment of the costs that the deployment of renewable energies represents for the SEE, depending on the profitability that is forecast as reasonable to grant[228]. Therefore, there is an analysis as to whether or not those costs are *sustainable* by the SEE in a certain, foreseeable energy scenario.

394. Thus, the 2000-2010 PFER established the implementation objectives of renewable energies for a scenario with the trend of an annual increase in electricity demand at 2%[229]. Within the framework of this scenario, the 2000-2010 REP conducted an in-depth analysis of wind technology, among others. In this plan: (i) it analysed the situation of these technologies in the EU; (ii) it detailed their level of implementation in Spain, encompassing: their current situation and potential, the technological aspects, the regulatory aspects, the environmental aspects, the financial aspects and the existing barriers; (iii) it specified the necessary measures for eliminating the barriers; and finally, (iv) it set the implementation targets for 2010.

395. In any event, for wind technology and when discussing the necessary measures for reaching the targets, the PFER indicated that it was not necessary for remuneration to be increased:

> *"It is a sufficiently developed and implemented technology whose financial profitability is assured by simply maintaining the current policy of premiums for electricity production*[230]*".*

396. Therefore, the PFER established the basic financial and technical conditions and the methodology to be followed for establishing the renewable energies remuneration scheme that should be developed through regulations.

397. Specifically, this methodology consisted (and has always consisted) in defining, within each technology and according to the art of the science that exists at any given time, different standard facilities. Once said standard facilities have been determined, different benchmarks were established in each one (cost of investment, operating cost, useful life of

[227] 2000-2010 Plan for the Promotion of Renewable Energies. R-0118
[228] Ibid, pages 276 to 279.
[229] 2000-2010 PFER, page 31. R-0118
[230] Ibid, pages 201 and 203. R-0118

the plant, production hours subject to a premium, market price), which would allow each plant, within a certain period of time (regulatory useful life), to reach reasonable profitability according to the cost of money in the capital market. The profitability of a standard project was estimated to be "*7% with own resources, before financing and after taxes*".

398. In this regard, the 2000-2010 PPRE pointed out that:

> *"Using the proposed energy targets as the baseline, the financing needs for each technology have been determined according to their profitability, therefore defining some standard projects for the calculation model. These standard projects have been characterised by technical parameters pertaining to their size, equivalent hours of operation, unit costs, execution periods, service life, operating and maintenance costs and selling prices of the final energy unit. Likewise, some financing assumptions and a series of financial measures or aid have been applied*[231]*."*

399. Royal Decree 436/2004 was issued for the purpose of reaching, in 2011, the installed power targets provided for in the PFER.

(4) Royal Decree 436/2004

(4.1) It introduces a new remuneration scheme

400. Royal Decree 2818/1998 was repealed by Royal Decree 436/2004 of 12 March, which establishes the methodology for updating and systematising the legal and financial scheme of electric power production under the special scheme (hereinafter, "**Royal Decree 436/2004**")[232], for the purpose of reaching the PFER's targets and eradicating the volatility of the previous system of calculating the remuneration for renewable energies.

401. Everything subject to the principles of financial stability of the SEE and the concession of reasonable profitability, in accordance with the cost of money in the capital markets set forth in Act 54/1997. The characteristics of the remuneration system of Royal Decree 436/2004 were:

a. The remuneration for investors in renewable energies is integrated within the SEE. Therefore, it is not isolated from the same.
b. It establishes subsidies using the calculation methodology included in the 2000-2010 PER.[233]

402. On this point, it is applicable to point out the consideration set forth in the Financial Report of Royal Decree 436/2004. Said report points out the following:

[231] Ibid, page 182. R-0118.
[232] Royal Decree 436/2004 of 12 March, which establishes the methodology for updating and systematising the legal and financial scheme of electric power production under the special scheme. R-0099.
[233] This is the methodology described in paragraph 382. This same methodology was followed by Royal Decree 661/2007 and by legislation currently in force.

> *"Parameter A (the investment, operating and maintenance costs of each technology) is heavily weighted in setting the amount of the regulated tariff for sale to the distributor. Thus, any plant of the special scheme installed in Spain, as long as it is equal to or better than the standard plant of its group, will succeed in earning reasonable profitability".*

403. It is deduced from the aforementioned that the subsidies established in Royal Decree 436/2004 do not have the purpose of granting indeterminate profitability. Said subsidies respond to a specific methodology directed at granting reasonable profitability for a standard facility during a certain period of time. Furthermore, with Royal Decree 436/2004 having been approved based on the forecasts of the 2000-2010 PFER, the useful life used as the reference for calculating the subsidies was the useful life provided for in the plan itself, which is 20 years for wind facilities.

404. Based on this, the Royal Decree defined a system based on the free will of the owner of the facility, who could opt between (i) selling their production or electrical energy surpluses to the distributor, therefore receiving remuneration in the form of a regulated tariff or (ii) selling said production directly in the daily market, in this case receiving the price negotiated in the market, plus an incentive for participating in it and a premium, if the specific facility had the right to receive it.

405. In any event, as its Preamble points out:

> *"Regardless of the remuneration mechanisms that is selected, the royal decree guarantees that owners of facilities under the special scheme will receive reasonable remuneration for their investments and also that electricity consumers will be given fair assignment of the costs attributable to the electricity system (...)*[234] *".*

406. As it has been pointed out, Royal Decree 436/2004 essentially changed the remuneration scheme. It was thus understood by the Wind Business Association (hereinafter, the "AEE"), which pointed out that:

> *"the production of electricity within the special scheme has experienced a change in 2004 that, for wind generation, clearly transcends what has also been a redefinition of the financial model on which this electrical activity is based."*[235]

407. According to the new model, the tariff or, if applicable, the premium and the incentive consisted in a multiple of the Average Reference Electricity Tariff (hereinafter, the "ARET"). In the case of wind energy, in the tariff option, the incentive was decreasing to the extent that the regulatory life of the facility advanced. Specifically, facilities would receive a tariff that was equivalent to 90 percent of the ARET during the first five years as from the commissioning thereof, 85 percent during the next 10 years and 80 percent as from then[236].

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[234] Preamble of Royal Decree 436/2004. R-0099

[235] Spanish Wind Energy, 2004 panorama, page 13. R-0223.

[236] The possibility that the remuneration to be received by pre-existing facilities would decrease over time was endorsed by the CNE in its report of 22 January 2004 on the proposed Royal Decree according to

408. The ARET was established by the regulatory body considering the procedure established by Royal Decree 1432/2002 of 27 December, on the methodology of the average reference electricity tariff (hereinafter, "**Royal Decree 1432/2002**"),[237] and it determined the selling price of electricity to the consumer. It was subject to variables such as the electricity demand, generation costs, inflation and the cost of capital, which are all volatile variables.

409. The difference between the tariff and the premium did not break the remuneration binomial imposed by Article 30 of Act 54/1997 so that renewable energy facilities would reach reasonable profitability according to the cost of money in the capital market: market price + subsidy. It concerned two different ways to set up the subsidy. One contemplating an activity with no risk (regulated tariff) and another with a certain risk (market price plus premium). In both cases, the objective or remuneration was to provide the facility with reasonable profitability[238].

410. It should be clarified that the option of the market price plus the premium doesn't merely respond to the objective of granting reasonable profitability for plants. Said incentive was established for the purpose of promoting the participation of renewable energies in the market. For this purpose, if facilities chose the market option, they would be paid an incentive to cover the additional costs represented by participating in the market.

411. As with the previous Royal Decrees 2366/1994 and 2818/1998, Royal Decree 436/2004 maintained the obligation that all production facilities under the special scheme must be

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which the methodology for updating and systematising the legal and financial scheme of the activity of the special scheme was established:"The application, to existing facilities, of the new regulated tariff scheme, which contemplates a decrease over time, does not mean retroactivity, given that it merely constitutes a formula for remuneration according to the costs. Moreover, it must be pointed out that during the five years during which Royal Decree 2818/1998 has been in force, existing facilities have received remuneration that is equal to or exceeds the remuneration that is now proposed for the initial years of useful life. For example, during these five years, wind energy has received remuneration exceeding 90% of the mean price of electricity, which is what is established by the proposal for the first phase of its economic life (...) Therefore, it could be affirmed that, at this time, the application of decreasing remuneration according to the economic life does not jeopardise existing facilities, since these facilities have already received or are receiving remuneration that is equal to or greater than what is established in the proposal for the first part of its economic life". When talking about the transitory scheme, it adds: "The production facilities included in the special scheme have the right to receive a certain remuneration for energy sold, but logically they only have the acquired right to receive said remuneration with respect to the energy already sold, but not regarding the energy they forecast selling in the future, which only constitutes an expectation.Transitional Provision Two of the Royal Decree Draft does not therefore violate the principle of non-retroactivity of the restrictive rules of rights, and it cannot be considered that, due to being a transitional provision, the provision cannot, "in the future", modify the scheme provided for in Royal Decree 2818/98, without affecting any acquired right.It also cannot be considered that the principle of non-retroactivity of the restrictive rules is being violated due to the fact that, for the purpose of calculating the remuneration corresponding to each facility, the age of the same is taken into account (Articles 34.1,34.2, 35.1, 36.2, 37.1 and 37.2, all of the Royal Decree Draft), given that it is simply a rule of calculation, which, in addition to being reasonable, is only taken into account to establish future remuneration, meaning the energy that is sold in the future, not with respect to what was already sold in accordance with other legislation." R-0126.

[237] Royal Decree 1432/2002. R-0098.

[238] CNE Report 4/2004 of 22 January 2004 on the proposed Royal Decree, which establishes the methodology for updating and systematising the legal and financial scheme of activity under the special scheme. Pages 16 to 22. R-0126.

registered in an administrative registry to allow the government to control tariffs and premiums, thereby considering the type of energy, the installed power and, if applicable, the commissioning date. It would also allow the government to know the evolution of the electrical energy produced, the energy transferred to the network and the primary energy used.[239] The creation of this registry (called RAIPRE as from 2007)[240] proves the desire of the legislator to verify, in any event, compliance with the targets provided for in the 2000-2010 Renewable Energies Promotion Plan in Spain.

412. Recording in this registry was therefore not a commitment by the state to indefinitely maintain the future and unchanging profitability of the registered facilities, rather a way to control and know who was participating in the SEE.

(4.2) Royal Decree 436/2004 does not guarantee that the premiums and tariffs therein established would be frozen.

413. Royal Decree 436/2004 does not include any freeze on the remuneration scheme therein contained. Indeed, it sufficient to consider the literal meaning of Article 40.3 of Royal Decree 436/2004 to note that it does not constitute a stabilisation clause.

414. Thus, Article 40.3 of Royal Decree 436/2004 sets forth that:

> *"Article 40. Revision of tariffs, premiums, incentives and allowances for new facilities.*
>
> *1. During 2006, in light of the result of the follow-up reports on the level of compliance with the Renewable Energies Development Plan, the tariffs, premiums, incentives and allowances defined in this royal decree will be revised, thereby considering the costs associated with each of these technologies, the level of participation of the special regime in covering demand and it its impact on the technical and economic management of the system. A new revision will be conducted every four years as from 2006 (...).*
>
> *3. The tariffs, premiums, incentives and allowances that result from any of the revisions considered in this section will be applicable only to the facilities that come into operation after the entry-into-force date referenced in the preceding section, with no retroactivity regarding previous tariffs and premiums*[241] *".*

415. The article does not make reference to "any" revision of the premium, regulated rate and allowances. Said article limits its scope of application exclusively to the revisions provided for in "this section". In other words, it only refers to the revisions whose purpose is to control the degree of compliance with the renewable energies implementation objectives established in the PFER, which revisions must be done "in 2006" and subsequently every four years.

416. It is deduced from reading the transcribed article, in a simple "*sensu contrario*" interpretation, that as from the revisions provided for in Article 40 (3), there could be other,

[239] Royal Decree 436/2004, Article 9.1. R-0099.
[240] Royal Decree 661/2007 introduces this name. R-0101.
[241] Royal Decree 436/2004, Article 40. R-0099.

different revisions derived from the principle of regulatory hierarchy. In other words, Royal Decree 436/2004 neither provided for nor did it have to provide for all the regulatory changes that were necessary to guarantee, at all times, the sustainability of the SEE and the reasonable profitability included in Act 54/1997. Said revisions were already guaranteed and permitted by Act 54/1997 itself according to the principle of regulatory hierarchy.

417. Moreover, if we adhere to the literal wording of Article 40(3), it only makes reference to revisions *"of tariffs, premiums, incentives and allowances"*. It makes no reference to anything else. Therefore, no investor could consider any aspects other than the scheme of Royal Decree 436/2004 to be frozen in their favour. These are: (1) the years of regulatory useful life of the plants during which they would receive subsidies, (2) the hours of subsidised production, and (3) the updates of the subsidies in accordance with the ARET.

418. In fact, as we'll see below, Article 40 (3) of Royal Decree 436/2004 did not, in view of circumstances unrelated to those therein provided for, prevent the regulatory body from opting among the following:

- Freezing, in 2006, the variable subsidies of Royal Decree 436/2004.
- Repealing and replacing the remuneration scheme with a new one in 2007.

419. And this was for a simple reason: changing the remuneration scheme was not due to the cause of the revision provided for in Article 40 (3), but rather, it was due to the need to guarantee the sustainability of the SEE and guarantee respect for the principle of reasonable profitability according to the cost of money in the capital market.

420. Furthermore, if a diligent investor still had any doubt, the evolution of the model included in Royal Decree 2818/1998 to the one in Royal Decree 436/2004 gave rise to the first decisions handed down by the Supreme Court of the Kingdom of Spain. In 2005, it already confirmed its aforementioned case-law on remuneration of the special scheme[242], which has remained consistent up to now. As from 2005, any diligent investor knew or should have known that facilities under the special scheme had no right to a *specific* remuneration scheme or to the fact that the remuneration established at a certain point in time *would be received during the entire operating life* of the facilities.

(4.3) Royal Decree 436/2004 caused wicked effects for the sustainability of the SEE

421. The link between the subsidies for renewable energies and the ARET caused major problems for the financial sustainability of the SEE. This was due to the fact that the ARET was being calculated using the recognised costs of the SEE as the basis, which included the subsidies for renewable energies. Therefore, there was constant feedback in the mechanism for establishing the premiums: the premium was a percentage of the ARET, which in turn was calculated considering the amount of the premiums. This constant feedback represented a disproportionate increase in the costs of the SEE.

422. For year 2006, the weight of renewable energies in the SEE (mainly wind energy) already represented 17% of total production[243]. The problem of cost overruns became even

[242] Section IV.D of this document.
[243] 2011-2020 NREAP, P. 18. R-0120

bigger in view of the planning targets established in the 2005-2010 PER, which will be analysed below and were going to mean greater participation by renewable energies in electricity generation.

423. In addition, as from the approval of Royal Decree 436/2004, there was an extraordinary increase in the market price of energy due to the rise in the price of oil and due to the inclusion of the emission allowances of greenhouse gases in the price of energy. Thus, the price of energy eventually reached 50-60 euros/MW.

424. This meant that, from a situation in which all the facilities were under the regulated tariff option, they went to another situation in which the majority of the facilities opted for remuneration according to the market price plus the premium, thereby earning much higher remuneration than what was forecast by the regulatory body. In particular, 96% of the wind farms were under the market option, and the profitability of wind facilities had gone from 8% to 15% (even reaching 26% with financing).

425. Consequently, the regulatory body urgently approved Royal Decree-Act 7/2006 of 23 June. This law, in its Preamble, highlighted the inefficiency of the current remuneration system. Therefore, Transitional Provision Two thereof froze the subsidies for renewable energies until a new remuneration scheme could be developed based on the modifications that Royal Decree-Act 7/2006 introduced to Act 54/1997[244]. These modifications included untying of the premiums from the ARET. Therefore, the update of the ARET implemented by Royal Decree 809/2006 of 30 June, thereby revising the electricity tariff as from 1 July 2006, was not applicable to the renewable energy premiums and tariffs.

426. Royal Decree-Act 7/2006 represented a cutback of the current remunerations of Royal Decree 436/2004, and it was therefore the object of considerable criticism from renewable energy producers and associations of the sector. The latter considered the measure to be retroactive, and they demanded greater regulatory stability through the approval of a Renewable Energies Act.[245]

427. In particular, the APPA Association, in its report from May to July 2006, used the following adjectives to describe Royal Decree-Act 7/2006:

> *"On the other hand, Royal Decree-Act 7/2006 has been published like in old times: at night and with aforethought: without prior consultations of the agents involved and, contrary to what has been repeatedly stated, the rules of the game have been changed in the middle of the match. Acquired rights have been modified retroactively"*[246]

[244] Royal Decree-Act 7/2006, of 23 June, establishing urgent measures in the energy sector. Transitional provision two: "Until the provisions set forth in sections one to twelve of Article 1 are implemented through regulations, in accordance with the provisions set forth in final provision two of this Royal Decree-Act: 2. The revision of the mean tariff made by the government will not be applicable to the prices, premiums, incentives and tariffs that form a part of the remuneration for electric power production under the special scheme". R- 0087

[245] "Revision of the Financial Scheme of Renewable Energies; APPA proposals report", November 2006. R-0224.

[246] "Dead-of-Night Energy Decree", APPA info journal No. 22, May-July 2006. Editorial. R-0191.

428. Further still, the main associations of the renewables sector (AEE, APPA and ASIF) addressed a joint letter to the Minister of Industry on 26 July 2006, in which, and regarding Royal Decree-Act 7/2006 and the reform of the remuneration model of renewables announced by said Royal Decree-Act, they requested the "*immediate stoppage of the regulatory process in progress*". Said associations affirmed at that time[247]:

- *"the appearing associations can only state their rejection, there most profound discontent and their most serious concern about how and why the process is being carried out".*
- *"Royal Decree-Act 7/2006 substantially ruptures the regulation of renewable energies established in the Energy Sector Act (Act 54/1997)"*
- *"Royal Decree-Act 7/2006 eliminates the objective parameters that established minimum remuneration for the different renewable energies included in said Act. These minimums were the guarantee of stability, predictability and durability that attracted investment to the sector (...)".*
- *"This situation, already compromised and disconcerting by itself, is even more aggravated when one learns that the planned revision of Royal Decree 436/2004 is turning into the guiding light of a new regulatory framework -in which none of the undersigned associations have been able to take part before being made public through the CNE- whose remuneration criteria are manifestly and objectively discouraging for taking on the development of projects planned in accordance with the 2005-2010 Renewable Energies Plan (PER), approved by the Council of Ministers on 26 August 2005."*
- *"This way of proceeding would cause a generalised, adverse reaction by investors and financial entities, which would be very difficult to rectify and could lead to deactivation of the renewable energies sector"*

429. In the month of December 2006, the APPA association continued to very harshly criticise said Royal Decree-Act 7/2006:

- *"Royal Decree 436/2004 [...] is therefore conditioned by the elements of* ***retroactivity and legal insecurity*** *introduced in the sector by said Royal Decree-act 7/2006."*
- *"Royal Decree-Act 7/2006 was approved last June, which contains a* ***frontal assault*** *on the national policy for the promotion of renewables: it eliminates the 80-90% bracket and the mechanisms of remuneration stability [of Royal Decree 436/2004], without also considering the established guarantees and time periods. The standard, which changes the game rules mid-game, introduces* ***retroactivity*** *and* ***very seriously damages*** *the legitimate expectations of investors.*"[248] (Emphasis added)

[247] "Dead-of-Night Energy Decree", APPA info journal No. 22, May-July 2006. Editorial. R-0191.
[248] "RD-L 7/06 and review of RD 436/04. Storm in the renewables sector", APPA info journal no. 23, August-December 2006. Editorial and page 9. R-0216

430. The reform introduced through RD-Law 7/2006 has been deliberately omitted by the Claimants because it shows that it is untrue that RD 661/2007 culminates and improves the remuneration that wind-farm producers had had up until that time. In fact, RD 661/2007 was introduced as a requirement of RD Law 6/2007[249] to ensure sustainability of the SEE and in light of the planning targets introduced through the 2005-2010 REP.

(5) 2005-2010 Renewable Energies Plan

431. Alongside approval of RD-Law 7/2009, the Renewable Energies Plan in Spain (hereinafter "**REP**") 2005-2010 reviewed the Renewable Energy Development Plan (REDP) 2000-2010 with a twin purpose: (a) to maintain the undertaking to cover at least 12% of overall energy consumption in 2010 using renewable sources as part of the policy to develop renewable energies in the European Union, and (b) to include another two objectives not contained in the 2000-2010 REDP (29.4% of electricity generation with renewables and 5.75% of biofuels in transport).

432. For these purposes, the 2005-2010 REP pursued the traditional methodology and established its objectives based on calculation of the costs of the standard installations for the different technologies, and revenue forecasts based on the macroeconomic circumstances of the moment.

433. Consequently, the 2005-2010 REP is vital in understanding key aspects of the remuneration regime set out in RD 661/2007.

(5.1) The 2005-2010 REP specified the objectives of introducing wind technology.

434. Within the reference energy framework, the 2005-2010 REP determined, for all technologies, the implementation targets to be aspired to for 2010.

435. For this purpose, the 2005-2010 REP performed an in-depth analysis, as did the 2000-2010 REDP, *inter alia*, of wind technology[250]. More specifically: (i) it analysed the situation of these technologies in the EU; (ii) it detailed its level of implementation in Spain, encompassing: its current situation and potential, the technological aspects, the regulatory aspects, the environmental aspects, the economic aspects and the existing barriers; (iii) it specified the means required to remove the barriers and, (iv) finally, it set the implementation targets for 2010.

436. With regard to wind technology, the REP revealed the extraordinary development of this[251], considering the wind targets set in the 2000-2010 REDP as easily achievable prior to 2010, without the need to change the remunerative regime.

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[249] Final Provision two of RD-Law 7/2006 set out that: "The Government is empowered to statutorily implement the provisions set out in this Royal Decree-law. In any case, the remunerative regime of special regime installations for application of the provisions set out in sections 1 to 12 of article 1 must be implemented within a deadline of six months from publication of this Royal Decree-law" (Emphasis added). R-0087.

[250] Ditto, pages 35 to 67.

[251] In this regard, the 2005-2010 REP pointed out that: "During 2004, a total of 1920 MW was exploited in Spain, a figure that appreciably exceeds the average annual value forecast in the Development Plan for 2000/2006, given as 597 MW". R-0119

(5.2) Energy scenario in which the rollout of RE as per the 2005-2010 REP was scheduled

437. As with the 2000-2010 REDP, the 2005 – 2010 Renewable Energies Plan was based on electricity demand forecasts, considering:

> *"(...) two general energy scenarios (called Trend Scenario and Efficiency Scenario) and a further three scenarios of developing renewable energies (Current, Probable and Optimistic) having chosen the Trend scenario as the reference for setting the Plan objectives, and choosing the so-called "Probable" scenario for the renewable energies scenario".*[252]

438. Consequently, the specifications of profitability by technology as set out in the 2005-2010 REP was also conditioned to a specific scenario of primary energy consumption, in other words to a specific evolution of electricity demand.

(5.3) Methodology used in the REP to quantify the cost of its objectives

439. One of the main principles of the REP was to determine the cost of achieving the implementation targets set out in the plan. For these purposes, the 2005-2010 REP, just as the 2000-2010 REDP had done, described a methodology that had to be consistent with the necessary economic sustainability of the SEE:

> *"To achieve the targets set out herein, we have undertaken an in-depth assessment of the investment to be made throughout the period, of the nature of that investment and of the public aid required to achieve the objectives. The same methodology and criteria of economic and financial analysis that were applied in the 1999 Development Plan have been used. The analysis, based on the specificities of each technology -level of maturity, costs, contribution to the global objective-, is based on the equilibrium of all factors, in order to achieve the private and public profitability, mobilising the resources required to carry out the scheduled investments.* [253]*".*

440. The methodology used to determine this cost, as employed in the 2000-2010 REDP and the Economic Report of RD 436/2004, was set out as follows:

> *"Taking as the baseline the energy objectives proposed, we have determined the financing needs for each technology in accordance with its profitability, defining some standard projects for the calculation model.*
>
> *These standard projects have been characterised by technical parameters relative to their size, equivalent hours of operation, unit costs, performance periods, service life, operation and maintenance costs and sales price of the final energy unit. Furthermore, we have applied some financing assumptions and a series of financial aid or measures designed in accordance with the requirements of each technology." (Emphasis added)*[254]

[252] Ditto. Page 323.
[253] Ditto. Page 272.
[254] Ditto. Pages 281 to 283 and 280.

441. More specifically, in accordance with the state of the art at any given time, 3 standard installations were established for the wind sector. In all cases the different parameters were set to enable each standard installation to achieve a return on the project and with own resources close to 7%[255] throughout its useful life.

442. In this regard, the 2005-2010 REP, in line with the 2000-2010 REDP, established the following conception of profitability of standard projects:

> "Return on standard projects: calculated on the basis of maintaining an Internal Rate of Return (IRR), measured in common currency and for each standard project, close to 7%, with own resources (before financing) and after taxes." *(Emphasis added)*[256]

(6) Real Decreto 661/2007

(6.1) Introduction

443. The need to implement the provisions of the 2005-2010 REP and of RD-Law 7/2006 led the Regulator to enact RD 661/2007. In other words, this Regulation was of mandatory enactment.

444. The Claimants maintain that Royal Decree 661/2007 was the result of negotiation between the Government and the *Asociación Empresarial Eólica* (hereinafter, "AEE")[257]. However, this "negotiation" is simply the result of applying the legal provision of consultations and formalities with citizens and the associations that represent them, during the preparation of the royal decrees[258], in accordance with article 24 of Law 50/1997, of 27 November, from the Government.

445. So, this is exactly what happened, nothing more and nothing less. Throughout the procedure of preparing the Draft RD 661/2007, the Ministry of Industry, as the competent body, attempted to get the opinion of interested parties through their associations, under the aegis of the possibility set out under article 24.1 c) of the LGob.

446. In fact, the AEE was not the only organisation representative of economic and social interests that was listened to during the formalities[259].

447. In addition, the Claimants transmit an erroneous interpretation with regard to the purpose and effects of approval of RD 661/2007. They maintain that RD 661/2007 was enacted to enshrine the rights that had been granted to the developers through RD 436/2004, indicating, superficially, that the Government was concerned by the high cyclical prices of

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[255] Ditto, page 274.
[256] Ibid. Pág. 274.
[257] Memorial on the Merits, pages 249 to 254.
[258] Article 24 of Law 50/1997, of 27 November (R-0070) and section IV. A of this statement
[259] News: "CCOO welcomes the approval of RD 661/2007...". In this news items the union describes its participation in the process for approving RD 661/2007 and adds that: "*although the new decree gives back certain stability to the sector, CCOO claims the need to institute a stable and long-lasting framework for renewable energies that avoids the lengthy process of negotiation we have experienced on this occasion being repeated every few years, a stability that would be obtained with the approval of a Renewable Energies Act*". R-0217

electricity[260]. However, and as we shall see, RD 661/2007 was not enacted because of "mere concerns of the Government", but because of the need to guarantee the economic sustainability of the SEE, which could be affected by a system of subsidies tied to the Average Regulated Tariff (ART). Furthermore, this risk was heightened through the new targets of implementation of renewables as established in the 2005- 2010 REP.

448. The Claimants seem to forget that RD-Law 7/2006 required a new implementation of article 30(4) LSE 54/1997, consistent with the principle of economic sustainability of the SEE[261]. In effect, the Preamble of RD 661/2007 made it very clear that it was subject to the principles of economic and technical sustainability of the SEE and a fair return:

> *"The economic framework established in this royal decree implements the principles set out in Law 54/1997, of 27 November, on the Electricity Sector, guaranteeing owners of installations under the special regime a fair return on their investments and also providing electricity consumers with a fair assignment of the costs attributable to the electricity system."*[262]

449. This means that the different articles of RD 661/2007 cannot be analysed in an isolated way. The aforementioned articles must be analysed in a harmonious way and without contradicting the principles set out in Law 54/1997. Moreover, proper understanding of RD 661/2007 requires acknowledgement that the tariffs set out in the same are the result of major preliminary studies carried out by the Regulator on the basis of the 2005-2010 REP and the previously mentioned methodology.

450. Having set out the basic aspects of RD 661/2007 we must now address the following issues: (i) the measures introduced through RD 661/2007 to guarantee the economic and technical sustainability of the SEE (ii) the tariffs of RD 661/2007 as a measure to achieve the fair return pursuant to the methodology known by all investors; (iii) the fact that the premiums and tariffs are subject to the economic sustainability of the SEE (ii) the impossibility of article 44.3 of RD 661/2007 preventing the take-up of measures targeted at guaranteeing the economic sustainability of the SEE or maintaining the principle of a fair return.

(6.2) Measures introduced through RD 661/2007 for the economic and technical sustainability of the SEE

(a) Measures introduced through RD 661/2007 to guarantee the economic sustainability of the SEE

451. As we have already mentioned, RD 661/2007, of 25 May was enacted to remove the perverse effect that the previous system, based on the ART, produced for the economic sustainability of the SEE. The Preamble of RD 661/2007 sets out:

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[260] Memorial on the Merits, paragraph 250.
[261] As set out in Final Provision Two of Royal Decree-Law 7/2006, of 23 June, establishing urgent measures in the energy sector. R-0087.
[262] RD 661/2007. R-0101.

> *"The economic regime established in Royal Decree 436/2004, of 12 March, due to the behaviour of market prices, which in recent times have seen certain variables take on greater relevance and which were not considered in the aforementioned special regime, requires modification to the system of remuneration, disassociating this from the Average or Reference Electricity Tariff used until now."*[263]

452. Consequently, RD 661/2007, respecting the limits of article 30.4 of Law 54/1997, represented a change in the way remuneration was paid. Thus, it became disassociated from the subsidies of the ART and these subsidies were updated in accordance with the adjusted Consumer Price Index(Hereinafter the "**CPI**"). In this regard, the tariffs were pegged to the CPI, although not directly, and instead the update was limited by deducting 25 base points from the CPI until 31 December 2012 and 50 base points from then on.[264].

453. In addition, the option between regulated and pool plus premium tariff remained in force, although not for all technologies[265]. However, with regard to the latter option, some cap and floor limits were set to avoid what happened under the previous remunerative system: whereby an unforeseen increase of the pool prices gave rise to overpayment (or underpayment) situations that jeopardised the economic sustainability of the SEE. As set out in the Preamble of RD 661/2007:

> *"This new system protects the developer whenever revenue resulting from the market price is excessively low, and removes the premium when the market price is high enough to guarantee coverage of his costs, removing irrationalities in the remuneration of technologies whose costs are not directly tied to the oil prices in international markets."*[266] *(Emphasis added).*

454. This new remunerative regime shall be applicable to all installations, including those that are already in operation, from 31 December 2012. In effect, Transitory Provision One of Royal Decree 661/2007[267] meant that those installations which, in accordance with RD 436/2004, opted to sell electricity at market price plus premium, would continue to benefit

[263]RD 661/2007. R-0101

[264] RD 661/2007, article 4 and Additional Provision 1. R-0101.

[265] For example, the photovoltaic technology which, during the enforceability of Royal Decree 436/2004, was able to use both options, could only use the regulated tariff option following the coming into force of Royal Decree 661/2007.

[266] RD 661/2007, Preamble. R-0101.

[267] RD 661/2007. Transitory Provision One: "1. Installations covered under categories a), b) and c) of article 2 (therefore including wind energy) of Royal Decree 436/2004, of 12 March, that have a certificate of definitive commissioning, prior to 1 January 2008, may remain within the transitory period set out in the next paragraph. Consequently they must choose, prior to 1 January 2009, one of the options for selling electricity set out under article 22.1 of Royal Decree 436/2004, of 12 March, without the possibility of changing option. If the option chosen is option a) of foregoing article 22.1, this transitory regime shall apply to the remaining life of the installation. If no change of option is notified, this option shall become permanent from the aforementioned date. Those installations referred to in the previous paragraph that have opted for option a) of article 22.1 shall not be subject to application of the tariffs regulated in this royal decree. Those that have chosen option b) of article 22.1 shall be entitled to maintain the values of the premiums and incentives established in Royal Decree 436/2004, of 12 March, instead of those set out in this royal decree, until 31 December 2012. These installations shall be registered with a marginal note, indicating the particular nature of being covered by a transitory provision, arising from Royal Decree 436/2004, of 12 March. Payment of the incentives shall be carried out in accordance with the provisions set out for the premiums under article 30 of this royal decree." (Emphasis added)". R-0101

from subsidies, but only until 31 December 2012. From that moment onwards, their economic regime would be governed by the provisions set out in Royal Decree 661/2007.

455. Furthermore, the installations that temporarily accept the market price regime plus premium of RD 436/2004 would not be able to benefit from the premium updates set out in RD436/2004, given that the update pursuant to the ART had been removed through RD-Law 7/2006.

456. Consequently, it is evident that Transitory Provision One of RD 661/2007 had an economic impact on the subsidies that would be received by wind farms that opted to maintain the premiums of RD 436/2004 until 31/12/2012, given that these premiums had not been updated since 2006 and would continue without being updated.

457. Neither the draft of Royal Decree 661/2007 nor its final approval were well received by the wind sector, as this represented a cut in its remuneration regime[268]. Proof of this is that virtually all installations, including the wind farms of the Claimants took up the transitory option of the pool plus premium of RD 436/2004 as they considered it to be more beneficial.

458. Further proof that this change of regime represented a reduction in the remuneration received by SR producers were the appeals filed by ER producers against RD 661/2007 and, more specifically, against its Transitory Provision One. The Judgement from the Supreme Court of 3 December 2009, on ruling on these challenges, sets out:

> *"There are no grounds for challenging Transitory provision one, section 4 of the royal decree contested, of infringing the principle of legitimate expectations, given that the mercantile companies appealing, as companies that operate in the electricity production business (...) do not have a right for the remunerative regime of the electricity sector to remain unaltered, given that, as we upheld in the judgement of this Chamber of Contentious-Administrative Matters of the Supreme Court of 15 December 2005, "there is no legal obstacle to prevent the Government, in the exercise of regulatory powers and broad entitlements that it has in such a strongly regulated matter as electricity, from modifying a specific system of remuneration providing that this remains within the framework established through the Electricity Sector Act"*[269].

(b) Measures introduced through RD 661/2007 to guarantee the technical sustainability of the SEE

459. As regards the technical sustainability of the SEE, the Preamble of RD 661/2007 reasoned that:

[268] The press echoed both the situation of over-remuneration experienced by the wind sector under the previous regime, as well as the discontent of the sector in light of the announcement to reform this regime. In this regard, the accompanying news items are provided. R-0159, R-0160, R-0161 and R-0162. The documents provided by the Claimants also demonstrate this poor reception of RD 661/2207 (in this regard, please see documents C-0319 and C-0320).Subsequent to the reform, the AEE itself declared the reduction in the remuneration arising from introduction of RD 661/2007. R-0163, R-0164 and R-0184.

[269] Judgement from the Supreme Court of 3 December 2009, rec. 151/2007. R-0141.

> *"(...) The growth experienced through the special regime in recent years, coupled with the cumulative experience during application of Royal Decrees 2818/1998, of 23 December and 436/2004, of 12 March, have shown the need to regulate certain technical aspects thus safeguarding the security of the electricity system and ensuring its quality of supply."*[270]

460. RD 661/2007 imposed: (i) the obligation of secondment to control centres that would act as liaison points of the system operator for installations with power equal to or greater than 10 MW[271] and (ii) the obligation to comply with certain response requirements with regard to voltage dips for wind farms[272]. Breach of these requirements was considered fundamental to allow proper operation of the system under conditions of security and, as a consequence of this, making it possible for maximum integration of RE technologies in the SEE.

461. For wind farms prior to 1 January 2008, RD 661/2007 established the final date for compliance with the response requirements to voltage dips as 1 January 2010. Breach of this obligation determined the forfeiture of the right to receive the premium or, where appropriate, the equivalent premium for the energy produced. In this way, it is clear that RD 661/2007 imposed new obligations on wind farms, targeted at guaranteeing the technical sustainability of the SEE, with an economic repercussion.

462. The aforementioned obligation had nothing to do with any agreement between the sector businesses and the Government to maintain the remuneration regime, as the Claimants appear to uphold. This was an obligation that was imposed for the purpose of guaranteeing the technical sustainability of the SEE, which could have been jeopardised through the penetration of RE into the SEE.

463. In addition, RD 661/2007 regulated the reactive energy supplement through maintaining certain energy factor values. This supplement should be reviewed every year.[273]

(6.3) The premiums and tariffs of RD 661/2007 as a means to achieve a fair return

464. The subsidies set in RD 661/2007 represented the average to achieve the fair return pursuant to the methodology known by all investors.

465. The Claimants maintain that RD 661/2007 undertook to pay the subsidies, in either option, for the entire production and for the entire useful life of the installations. This statement ignores the fact that the tariffs are for the purpose of achieving the objective of a fair return required under Law 54/1997. Furthermore, it involves accepting the preposterous assumption that the tariffs cropped up spontaneously outside any prior analysis. Far from that, any investor that had been being given the slightest advice would have known that the

[270] RD 661/2007, Preamble. R-0101.
[271] RD 661/2007, article 18.d). R-0101.
[272] RD 661/2007, additional provision seven. R-0101.
[273] RD 661/2007, article 29. However, it means that installations that choose to sell their energy on the market, and which comply with certain technical requirements, would be able to relinquish this supplement and voluntarily take part in the voltage control operation procedure, applying its remuneration mechanisms. R-0101.

tariffs established in RD 661/2007 were tied to macro-economic, technical and methodological bases as set out in the 2005-2010 REP.

466. More specifically, the subsidies set out in RD 661/2007, both with regard to the regulated tariff option as well as the pool plus premium option, were set for the purpose of providing standard installations with a return of **close to 7%**, with own resources (prior to financing) and after tax. This was shown in the 2005 – 2010 REP, as we have referred to previously.

467. On this point, it should be noted that the Regulatory Impact Report of Royal Decree 661/2007, responding to the methodology used in the 2000-2010 REDP, Economic Report of Royal Decree 436/2004 and 2005-2010 REP specified the following:

> "The regulated tariff has been calculated for the purpose of guaranteeing a return of between 7% and 8% depending on the technology. The premiums have been calculated using the same criteria as Royal Decree 436/2004, in other words the premium has been calculated as the difference between the regulated tariff and the average forecast market price for these technologies"[274]

468. For wind technology, the Regulatory Impact Report specified:

> *"There are still two sales options. In the case of the market option, the value of the premium to be received by the energy generated shall be variable, depending on the limits established. (…)*
>
> *Consequently, the current scaling of tariffs has been kept, although the amounts have been calculated in such a way that the wind projects have a fair return, for the standard cases considered.*
>
> *With the remuneration considered, the return obtained would be 7% in the regulated tariff option and limited to between 5 and 9% if choosing the option to sell in the market"*[275]

469. Furthermore, this is how the CNE understood the regulated tariffs. The CNE contemplated these tariffs as the means to achieve the target of a Fair Return pursuant to Law 54/1997 on the different standard installations[276].

470. In this regard, the Manual "*Powering the Green Economy. The feed in tariff handbook*" having analysed the Spanish regulatory framework stated that the tariffs set out in Royal Decree 661/2007 were for the purpose of providing a specific target of a fair return on investments.

> "*Different names have been used to describe the tariff calculation approach based on actual cost and profitability for producers. The German FIT scheme is based on the notion of "cost-covering remuneration", the Spanish support mechanism speaks of a*

[274] Regulatory impact report of Royal Decree 661/2007. R-0081.
[275] Regulatory impact report of Royal Decree 661/2007. R-0081.
[276] CNE Report 4/2004, of 22 January pages 8 to 10 (R-0126) and CNE Report 3/2007, pages 13 and 14. R-0128.

> *"reasonable rate of return" and the French "profitability index method" guarantees "fair and sufficient" profitability. Despite the variety in names and notions, in all cases the legislator sets the tariff level in order to allow for a certain internal rate of return, usually between a 5 and 10 per cent return on investment per year*".[277] (Emphasis added)

471. In the Spanish case, the aforementioned manual is aware of the legislator's will to provide a return of around 7% on the investment:

> *"To give an example, the Spanish legislator calculated the tariffs based on 7 per cent returns on investment under the fixed tariff option, and 5-9 per cent under premium FIT option."*[278]

472. The foregoing Manual goes on to say that:

> *"After a good frame of reference is established for tariffs, cost factors related to renewable electricity generation have to be evaluated. We recommend basing the calculation on the following criteria:*
>
> *. Investment cost for each plant (including material and capital cost);*
>
> *. Grid-related and administrative cost (including grid connection cost, costs for the licensing procedure, etc.);*
>
> *. Operation and maintenance costs;*
>
> *. Fuel Costs (in case of biomass and biogas); and*
>
> *. Decommissioning costs (where applicable)"*[279]

473. We must also remember that, in the Spanish model, the CAPEX and the OPEX have never been designed in reference to a specific installation of particular investor. These costs have always referred to a *standard* installation, always considering an efficient investor in issues of costs. Furthermore, the foregoing Manual states:

> *"For the estimate of the average generation cost, regulators can use standard investment calculation methods (such as the annuity method). The Spanish legislator even obliges renewable electricity producers to disclose all costs related to electricity generation in order to have optimal information when setting the tariff."*[280]

474. The link between the subsidies established in Royal Decree 661/2007 and the methodology set out in the 2005-2010 REP has been so evident that the main consultants in Spain have emphasised this relationship:

- The Expert Report of 23 May 2011 from Deloitte estimates that the forecast return is close to 7%. This Expert Report calculates the return of the PV plants following RD 661/2007 at 6.41%, and following RD 1565/2010 it quantifies this at 5.43% or 5.77%.

[277] Powering the Green Economy. The feed in tariff handbook., pag 19. RL-0062.
[278] Powering the Green Economy. The feed in tariff handbook., pag 42. RL -0062.
[279] Powering the Green Economy. The feed in tariff handbook., pag 20. RL -0062.
[280] Powering the Green Economy. The feed in tariff handbook., page 20. RL-0062.

The Expert Report from Deloitte, of 23 May 2011 sets out the return it considers "fair" within the Regulatory framework of RE in Spain in 2011:

"The Renewable Energies Plan in Spain 2005-2010 (August 2005) from the Ministry of Industry, Tourism and Trade-Institute for Energy Diversification and Saving (IDAE), is based on the assumption that the return of a standard project for renewable energies is 7%.

Renewable Energies Plan in Spain 2005-2010 (August 2005)

"Return on standard projects: calculated on the basis of maintaining an Internal Rate of Return (IRR), measured in common currency and for each standard project, close to 7%, with own resources (before financing) and after taxes."[281] *(emphasis added)*

Furthermore, Deloitte's Experts draw a comparison with the parameter deemed comparable, the Spanish Bond at 10 years, in order to examine the return resulting from RD 1565/2010 for photovoltaic plants[282].

- In line with the foregoing, in its report of May 2012 KPMG pointed out that:

"The concept of a fair return:

• The regulation that regulates the development of the Special Regime is based on the concept of a fair return, which is mentioned in Law 54/1997 on the Electric Sector but does not define a value for this.

• In this report we understand the fair return as a return of 7% (prior to financing) and after taxes, which is the benchmark value used in the 2005-2010 REP and the one used by the CNE In its reports."[283]

(6.4) The tariffs of RD 661/2007 are subject to the economic sustainability of the SEE

475. The Claimants maintain that RD 661/2007 included in its article 44 (3) an undertaking not to review the tariff set out therein for those plants that had been registered at the due time with the Administrative Register of Special Regime Installations (RAIPRE). According to this precept:

"The reviews referred to in this section of the regulated tariff and the cap and floor limits shall not affect those installations whose certificate of coming into service had been granted before 1 January of the second year following the year in which the review was carried out."[284] *(Emphasis added)*

476. The statement of the Claimants requires us to ignore the fact that the subsidies to the special regime represent costs of the SEE and are therefore tied to its sustainability. As we have already pointed out with regard to article 40.3 of RD 436/2004, the wording of which is practically identical and even clearer, if possible, than article 44.3 of RD 661/2007, the

[281] DELOITTE Expert Report of 23 May 2011, pages 57/177. R-0130
[282] DELOITTE Expert Report of 23 May 2011, page /177. R-0130.
[283] KPMG Report, May 2012. R-0234.
[284] Royal Decree 661/2007. R-0101

reviews on the grounds set out therein did not prevent the possibility of addressing other reviews that could be required through the need to guarantee the sustainability of the SEE or the principle of a fair return.

Article 40.3 of RD 436/2004	**Article 44.3 of RD 661/2007**
1. During 2006, in light of the result of the follow-up reports on the level of compliance with the Renewable Energies Development Plan, there shall be a review of the tariffs, premiums, incentives and allowances defined in this royal decree, in accordance with the costs associated to each of these technologies, the level of participation of the special regime in covering demand and it its impact on the technical and economic management of the system. A new review shall be carried out every four years, from 2006 onwards. 2. The tariffs, premiums, incentives and allowances that may result from any of the reviews contemplated in this section shall enter into force on 1 January of the second year after the year when the review is carried out. 3. The tariffs, premiums, incentives and allowances that result from any of the reviews considered in this section shall apply only to the installations that come into operation after the date of coming into force referred to in the previous section, with no backdating with regard to previous tariffs and premiums.	3. During 2010, In light of the result of the follow-up reports on the level of compliance of the Renewable Energies Plan (REP) 2005-2010 and the Energy Efficiency and Saving Strategy in Spain (E4), as well as the new targets included in the next Renewables Energy Plan for 2011-2020, there shall be a review of the tariffs, premiums, allowances and floor and cap limits defined in this royal decree. This review shall be based on the costs associated to each of these technologies, the level of participation of the special regime in covering demand and its impact on the technical and economic management of the system, always guaranteeing fair rates of return with reference to the cost of money in the money markets. From then on, a new review shall be carried out every four years, maintaining the foregoing criteria. The reviews referred to in this section of the regulated tariff and the cap and floor limits shall not affect those installations whose certificate of coming into service had been granted before 1 January of the second year following the year in which the review was carried out.

477. In fact, the existence of said article 40.3 did not prevent the Regulator, in application of Law 54/1997, from introducing modifications, through RD 661/2007, that altered the premiums and tariffs being received by RE producers to guarantee the economic sustainability of the SEE and avoid situations of over-remuneration.

478. The modification instrumented through RD 661/2007 was reviewed by the Supreme Court of the Kingdom of Spain, which gave a ruling on the effect that article 40.3 of RD 436/2004 had with regard to the modification of the subsidies, as we have already seen[285].

479. It is relevant to point out that article 44.3 of RD 661/2007 makes no reference to "any" review of the regulated tariff and of the cap and floor limits. This article circumscribes its scope of application exclusively to the reviews set out in "this section". In other words, it only makes reference to the reviews that had to be made "in 2010" and to the reviews that had to be made every "four years". On the other hand, apart from the reviews set out in

[285] See section III.D of this pleading.

article 44(3), there could be other different reviews. Reviews that in the event of taking place would be outside the margin of article 44(3).

480. In addition, if we abide by the literal wording of article 44(3), this only refers to the reviews *"of the regulated tariff and of the cap and floor limits".* It makes no reference to anything else. As a consequence, no investor could consider any aspects other than the regime of RD 661/2007 in their favour, such as: (1) the years of useful life of the plants during which they would receive subsidies, (2) the hours of subsidised production, and (3) the updates of the reviews in accordance with the CPI.

(6.5) Conclusion: RD 661/2007 is subject to the regulatory principles of the SEE

481. The foregoing shows that no investor that received the smallest amount of information could overlook the fact that the subsidies set in RD 661/2007 were tied to certain economic data, on which the rollout of renewable energy targets was planned. The cost of achieving these targets for the SEE had to adapt to the forecast revenue of the SEE. This is required under the principle of the economic sustainability of the SEE.

482. By the same token, as we have already mentioned, no investor could be unaware of the fact that the tariffs of RD 661/2007 were established for the purpose of granting a fair return within the framework of a sustainable SEE. Consequently, if the tariff generated situations of an excess return, any investors should be aware that the Regulator would act to redress this situation.

483. Therefore, no investor could expect the subsidies set in RD 661/2007 to remain unaltered in the event of a substantial change to the economic data on which these were based, or whenever the subsidies generated excessive remuneration. And far less so if these situations jeopardise the economic sustainability of the SEE.

484. The theory of the Claimants, who defend the non-changeability of the remunerative conditions set out in RD 661/2007, is contrary to the doctrine of the Supreme Court of the Kingdom of Spain that existed during that time with regard to the effects of regulatory changes in the context of article 30(4) of Law 54/1997[286].

485. This case law, as is to be expected, is referred to in the report from the CNE 3/2007 of 25 January 2007[287] to support its point of view on the regulatory changes introduced by RD 661/2007. A diligent investor could not be unaware of this fact.

(7) Royal Decree-Law 6/2009

486. As referred to previously, one of the pillars on which the SEE is based is that of financial sustainability. RD-Law 6/2009, of 30 April[288] was approved to guarantee this sustainability. This regulation has been deliberately left out by the Claimants in their claim, despite being the regulation closest in time to the investment of BayWa RE in Spain.

[286] Section III.D of this pleading.
[287] CNE Report of 14 February 2007 pages 16 and 17. R-0128.
[288] Memorial on the Merits, paragraph 283

487. It must be remembered that royal decree laws have force of law that the Executive can enact in extraordinary and urgent cases. At that time it was extraordinarily urgent and necessary to try to rebalance the sustainability of the SEE. Furthermore, RD-Law 6/2009 created the so-called "discount rate" to protect the most vulnerable consumers that could not pay the growing cost of the electricity bill.

488. In this regard, the Preamble of RD-Law 6/2009 states:

> *"The growing tariff deficit, [...] is causing serious problems which, in the context of the current international financial crisis, is having an in-depth effect on the system and jeopardising not only the financial situation of electricity sector companies but the very sustainability of the system itself. This imbalance is unsustainable and has serious consequences on impoverishing the security and capacity of financing the investments required for the supply of electricity at levels of quality and security required by Spanish society. [...]*
>
> *Because of its growing impact on the tariff deficit, mechanisms are hereby established with regard to the remunerative system of installations under the special regime. In the short term, the trend of these technologies could jeopardise the sustainability of the system, both from the economic point of view because of its impact on the electricity tariff, as well as from a technical standpoint, also compromising the economic feasibility of the installations already completed, whose performance depends on a suitable balance between manageable generation and non-manageable generation."*[289] *(Emphasis added)*

489. The main measure of this RD-Law was, then, to establish a target to remove the tariff deficit. In particular, it sets out that from 1 January 2013 onwards, the access tolls had to be sufficient to satisfy all of the costs of the regulated activities without any ex-ante deficit[290].

490. The Regulator made it clear that he would adopt, within the Spanish legal framework, the regulatory measures required to achieve the aforementioned sustainability of the SEE. In other words, until this objective was achieved, all of the costs and revenue of the SEE should contribute to achieving this.

491. Furthermore, RD-Law specified that the RE would not be left outside of the regulatory measures that needed to be adopted. RD-Law 6/2009 expressly warned that due to *"the trend of these technologies, the short-term sustainability of the system could be jeopardised both from the economic point of view, because of its impact on the electricity tariff, as well as from the technical standpoint (...)".* Consequently, RD-Law stated that, without prejudice to the different immediate measures that could be adopted, it was necessary to put in place *"the fundamentals for the establishment of new economic regimes that propitiate compliance with the objectives sought."*[291]

492. In this way, for the purpose of achieving the objective sought, RD-Law 6/2009 introduced major modifications to RD 661/2007: a) it created the Pre-assignment register and b) gave the Government the power to scale the entry into operation of preregistered

[289] Royal Decree-Law 6/2009, of 30 April, which adopts certain measures in the energy sector and approves the discount rate. Preamble. R-0088.
[290] Ditto Article 1.
[291] Ditto Preamble. R-0088.

Installations whenever the economic or technical sustainability of the SEE so required. A power that was made effective with the Council of Ministers' Agreement of 13 November 2009[292], scaling the entry into operation of preregistered installations.

493. In May 2009 the most important association in the RE Sector -APPA- addressed a tough editorial against the former Minister for Industry, making him responsible for publication of RD-Law 6/2009. When it comes to analysing the RD-Law, this editorial states[293]:

- "[The Minister] *has never received* [the RE Sector] *nor taken it into consideration for the regulatory changes affecting the sector"*
- "*It adopts different measures targeted at reducing the tariff deficit and which increase the administrative shackles of clean energies".*
- *"The measures of the RDL, [...], make it even more difficult for development of the sector which, like all the rest, is suffering the problems of financing as a consequence of the crisis"*
- "*The Government has a unique opportunity with the Renewable Energies Act, for which it has a proposal from Greenpeace and APPA to demonstrate its commitment to the green economy and to allow Spain to spearhead, for the first time in its history, the technology and development at a worldwide level"* (Emphasis added)

494. The foregoing editorial was accompanied by a joint Pleading signed by different associations from the renewable sector against R-DL 6/2009. The title of the Memorandum read "*RDL 6/2009, a new decree that does not have the support of the majority against renewable energies*"[294].

495. This pleading was shown by APPA In its newsletter for Associates:

> *"APPA, ADAP, APREAN, EolicCat, GiWatt and the Energy Cluster in Extremadura fiercely oppose the decree and ask the government for its contents to be developed in the future Renewable Energies Act." (Emphasis added)*

496. Through this joint Pleading, the different signatory Associations fiercely opposed this regulation, referring to its similarity to the previous RD 1578/2008, of 26 September, on the remuneration of the electricity production activity through photovoltaic technology for installations after the final date for maintenance of the remuneration of Royal Decree 661/2007, of 25 May, for this technology (hereinafter "**RD 1578/2008**")[295], enacted in the photovoltaic sector months beforehand:

[292] Agreement of the Council of Ministers of 13 November 2009. C-0113.
[293] "Europe, a new directive. Spain, a new decree that does not have the support of the majority". APPA info of May 2009. Editorial. R-0219
[294] "Europe, a new directive. Spain, a new decree that does not have the support of the majority". APPA info 29, May 2009. Pages 12 to 13. R-0219.
[295] RD 1578/2008, of 26 September, on remuneration of electricity produced through solar technology. R-0102.

> *"There is a clear and ill-fated experience in RD 1578, which regulates the photovoltaic solar technology activity and which has caused the shutdown of this sector, with the closure of plants and the relocation of investments. The new RDL could have the same effect as the remaining renewable technologies and even affect the one that is the most developed, wind technology."*[296]*. (Emphasis added)*

497. The regulatory evolution revealed thus for shows that the Regulator adopted at each time (2006, 2007, 2008 and 2009) the measures required for the corresponding RE sectors to ensure the economic sustainability of the system. A simple reading of the Preamble of RD-Law 6/2009 shows that Spain had not undertaken or guaranteed to ensure that the legal regime remained unchanged. Quite the opposite, the Government was persuaded of the need to introduce measures to rebalance the tariff deficit.

498. The imbalance situation of the SEE was largely the result of a huge reduction of electricity demand, as a consequence of the crisis. This made it necessary to reform the SEE, at least with regard to the remuneration regime of the RE. As we have already stated, that was the understanding of the Regulator and of the Sector. For this purpose a proposal was compiled for the RE Sector to reform the Framework of remuneration for renewable energies, as shown below.

(8) Proposal for the Remunerative framework of the RE Sector of 20 May 2009.

499. The Associations of Producers were aware of the dynamic nature of the fair return and of the long-term economic non-sustainability of the system. This perception was aggravated by the international crisis.

500. Since January 2009, the Association of Producers of Renewable Energies (APPA), the largest Spanish association of renewable producers, has been working on a Draft Bill that would satisfy the sector's objectives. To this end, it commissioned a Legal practice (by chance Cuatrecasas, the lawyer of the Claimants) to draft a Bill for the Renewable Energies Development Act.

501. This Draft was presented jointly by the APPA Association and by Greenpeace on 20 May 2009 through a Press Release[297]. This APPA Press Release refers to the need to change the energy model, by formulating a Draft Bill based on the *"best practices of legislation for RE"* and on *"a sustainable energy model"*:

> *"APPA and Greenpeace, with the legal support of Cuatrecasas, Gonçalves Pereira, have worked on <u>their own bill for the promotion of RE</u>, whose first objective is transposition of the new directive into Spanish legislation. This bill is <u>based on the best practices of legislation for RE</u> in various countries and <u>on a sustainable energy model</u>, and it conceives of the new RE directive [...] as a starting point for changing <u>the current energy model</u>. Moreover, its objective is to help the government in coming up with an <u>ambitious and visionary RE law</u>. But above all, this bill endeavours to be a*

[296] Europe, a new directive. Spain, a new decree that does not have the support of the majority". APPA info of May 2009. Pages 12 to 13. R-0219.
[297] Press Release from APPA-Greenpeace on the Draft Bill of the Renewable Energies Development Act, 20 May 2009. R-0167.

legislative instrument that provides security and stability for the necessary investments so that RE develop all their potential in a sustainable and long-lasting manner." (Emphasis added)

502. The two most popular newspapers in Spain covered this news, both in El Mundo[298] as well as El País[299]. It is evident that the main association of the RE Sector would be interested in publicising its Draft Bill. Furthermore, this presentation was referenced by other RE Associations in May 2009[300]. This proposal was subsequently reiterated by the APPA Association[301].

503. APPA and Greenpeace made a proposal to the Government whereby the fair return guaranteed to the RE, as the focal point of their remunerative regime, would be determine through reference to the return on the 10-year Treasury bonds, plus a spread of 300 base points:

"The government will establish the amount of the regulated tariffs, premiums and complements, therefore assessing, in all cases, the operating and maintenance costs and the investments costs incurred by the owners of a facility in order to obtain reasonable rates of return in reference to the cost of money in capital markets. As a fee for the remuneration of capital, an annual percentage equal to the mean of the preceding year for the remuneration of 10-year Treasury bonds will be used, increased by 300 base points."[302] *(Emphasis added).*

504. The index proposed by the interested associations to set the fair return is equivalent to the one established by the Kingdom of Spain in the measures contested in this Arbitration. As stated by the most important Association of the RE Sector on proposing it, this is a method that provides *"security and stability to the investments required to enable the RE to fulfil all their potential in a sustainable and long-lasting way."*[303]. We couldn't agree more.

505. Furthermore, in 2009 the APPA Association proposed that the estimate of investment costs be carried out using *standard installations*, in accordance with *usual market prices* to avoid speculative costs:

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[298] Press release, "Spain could be 100% renewable by 2050" El Mundo, 25 May 2009. R-0168.
[299] Press release, "Too many renewables or too expensive?" El País, 26 May. El País of 26 May 2009, on this presentation: "The Association of Renewable Energy Producers (APPA) And Greenpeace. This very week, both organisations presented a bill for the promotion of renewable energies that proposes reaching 30% from renewable energies in 2020 based on the gross final consumption." R-0182.
[300] Apecyl Press Release "Greenpeace and producers of renewables propose a law to make Spain a leader in clean energies" 20 May 2009. R-00181
[301] APPA Journal, "Info" No. 30, from 2010, page 14: "The APPA-Greenpeace consensus model of agreement to consolidate Spain as world leader in renewables". [...] the Renewables Bill presented last May by APPA and Greenpeace is to date the only document supported in the sector [...] As such It is a proposal open to debate with the various public administrations and with the social agents involved." R-0189 and PowerPoint Presentation of 27 April 2010 on the APPA and Greenpeace proposal, given at the XII Sustainable Energy Forum. R-0189.
[302] Article 23.4 of the Bill presented by APPA-Greenpeace in May 2009. R-0187.
[303] Presentation to the Ministry of Industry, Energy and Tourism with an inbound stamp of 21 May 2009 R-0187 and a Letter sent to the IDAE on 21 [...] 2009. R-0186.

> *"For the preceding purposes, the Government will estimate the investment costs associated with the various classes of Installations, differentiated by technology and size, such that they reflect the usual values that said investments actually reach"*[304] *(Emphasis added).*

506. The similarity between the proposal from the RE Sector in May 2009 and the measures adopted by the Kingdom of Spain in 2013 is clear. In 2009 the RE Sector was already fully aware of the difficulties surrounding the economic and technical sustainability of the SEE at that time. It therefore proposed a Law that modified the remuneration system of the Renewable Energies, within the limit of respecting the principle of a "fair return in accordance with the money market" enshrined in Law 54/1997.

507. Furthermore, as the RE sector was fully aware that the principles surrounding the remunerative regime of the SEE were contained in the Law (not in the implementing regulations), it attempted to ensure that the fair return had the full force of law. The most authorised doctrine backed this demand:

> *"The Spanish FIT scheme has the legal Rank of a Royal Decree. Even though it is "stronger" than for instance a Ministerial Order, the Spanish renewable associations have long called for a FIT law. Before the last general elections, the current Socialist government had promised to initiate the respective legislative process, but up to now nothing has changed."*[305]

508. The Preamble of the 2009 Bill proposed by APPA to the Government alludes to this need to make the legal certainty more robust:

> *The rank of the [proposed] law itself should serve to reflect the will for the stability and continuity of the measures it contains, For the purpose of generating the necessary confidence and credibility in the chosen legal and economic model and thereby guaranteeing the security and certainty needed for investments under the same." (Emphasis added)*

509. The Draft Bill shows that any investor in Spain was aware of or should have been aware of the *dynamic* nature of the fair return guaranteed under article 30.4 of Law 54/1997 and the need for *sustainability* of the SEE. Consequently, all investors were aware of or should have been aware of the fact that no regulation enacted in enforcement of Law 54/1997 could promise investors unchanged remuneration *sine die*. And far less so in a scenario of an international crisis, falling electricity demand and a tariff deficit that had been increasing since 2008.

510. In fact, it has been substantiated that since January 2009 the main Spanish RE Association was aware of and gave public importance to the influence of the tariff deficit and the international crisis on the sustainability of the SEE, as grounds that justified the need to modify the regulation and the remuneration applicable.

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[304] Article 23.5 of the Bill presented by APPA-Greenpeace in May 2009. R-0187.

[305] Powering the Green Economy. The feed in tariff handbook. Miguel Mendonça, David Jacobs and Benjamin Socacool. Publishing house. Earthscan, 2010. RL-0062.

(9) Spain's National Renewable Energy Action Plan 2011 - 2020

511. Directive 2009/28/EC from the European Parliament and the Council, of 23 April 2009, on increasing the use of energy from renewable sources, set out the need for each Member State to compile a National Renewable Energy Action Plan (hereinafter "**NREAP**") for 2011-2020 and to notify this to the European Commission (EC) by 30 June 2010 at the latest, in compliance with the binding objectives set out in the Directive.

512. In compliance with this mandate, the Kingdom of Spain approved its NREAP on 30 June 2010[306]. Prior to final approval, the aforementioned NREAP was open to a process of participation by companies, associations and the public at large, until 22 June 2010. During this stage there were a great many contributions and suggestions that were very useful in drawing up the final 2011-2020 NREAP document.

513. The NREAP, having conducted an analysis on the forecast final consumption of energy during the 2010-2020 period and having defined the targets and trajectories of renewable energy, determined the measures of support required to achieve these targets. More specifically, on establishing the measures in the field of electricity production with renewable energies, the NREAP included the following:

> *"To establish a stable, predictable, flexible, controllable and secure remunerative framework for promoters and the electricity system*".[307]

514. Furthermore, with regard to the support measures that require economic resources, the NREAP stated:

> *"The application of measures that involve the dedication of economic resources shall be undertaken in a manner that is compatible with the needs of adjustment and budget equilibrium that the Spanish economy must deal with.*"[308]

515. Subsequently, on describing the legal framework on which the financial aid to electricity production with renewable energies is based, it pointed out that the tariff and premium regime of the special regime installations "*considers levels of remuneration for electricity production that seek to obtain fair rates of return on the investment. The determination of this takes into consideration the specific technical and economic aspects of each technology, the power of the installations and the date they came into service, all of this employing criteria of sustainability and economic efficiency within the system"*[309].

516. Next, the NREAP described the required mechanisms of control and adaptability with which the Spanish system provides subsidies to renewable energies. In particular, and with regard to the flexibility mechanisms, the NREAP gave the possibility of modifying the levels of remuneration to renewable technologies:

> *"The levels of remuneration may be modified in accordance with the technological evolution of the sectors, the behaviour of the market, the level of*

[306] Spain's National Renewable Energy Action Plan (NREAP) 2011 - 2020 R-0120
[307] Ditto. Page 50. R-0120
[308] Ditto, Page 61. R-0120
[309] Ditto. Page 116. R-0120

compliance with the renewable energy targets, the level of participation of the special regime in covering demand and its impact on the technical and economic management of the system, always guaranteeing fair rates of return -current RD 661/2007 sets out reviews every four years-. In any case, these reviews deal with the evolution of the specific costs associated to each technology, with the triple overall aim of ensuring that renewable technologies reach the highest level of competitiveness possible with the technologies of the Ordinary Regime; favouring a balanced technological development, and allowing the remunerative system to evolve towards the minimum socio-economic and environmental cost"[310] *(Emphasis added)*

517. Furthermore, when it comes to addressing the future evolution of the remunerative regime of renewable energies, in accordance with the methodology followed to date, the NREAP sets out a premise:

> *"To determine the remuneration we shall take into account the technical parameters and the investment costs incurred in order to achieve fair rates of return with reference to the cost of money in the money market, pursuant to the provisions set out in the Electricity Sector Act"*[311] *(Emphasis added)*

518. The NREAP then goes on to highlight the duty of the Administration to control the remunerative system of subsidies and, where appropriate, to take up the measures required to avoid undesired remunerative imbalances:

> *"By the same token, the effective guardianship by the Administration must guarantee that any gains made in the appropriate evolution of these technologies is passed onto society with regard to the competitiveness in relative costs, minimising speculative risks, caused in the past through excessive returns that not only damage consumers but also the industry itself with regard to the way it is perceived. Consequently, it will be necessary to introduce systems that are sufficiently flexible and transparent in order to give and to obtain the economic and market signals that minimise risks, both those tied to the investment and return on the investment, as well as those caused by fluctuations of the energy markets*[312] *". (Emphasis added)*

519. Consequently, the Kingdom of Spain, through the NREAP, stated that maintenance of the remuneration mechanism of renewable energies, based on the principle of a fair return on investments, needed to revolve around its necessary "flexibility" in order to avoid undesired situations.

(10) RD 1565/2010

520. The need to guarantee the technical sustainability of the SEE, as a consequence of the growing penetration of renewable energies, obliged the Regulator to enact Royal Decree 1565/2010. In this regard, the Preamble set out that the RE Sector:

[310] Ditto. Page 119. R-0120
[311] Ditto. Page 123. R-0120
[312] Ditto. Page 123. R-0120

> *"Is a very dynamic sector with an extremely rapid pace of technological evolution. Currently, approximately 25% of electricity produced comes from renewable energies. These facts, coupled with the structural characteristics of our electricity system, make it necessary to introduce additional technical requirements to guarantee the performance of the system and enable these technologies to grow".*[313]

521. Firstly, due to reasons of technological development, this Royal Decree agreed to extend the final date for wind farms to comply with the requirements of response in the light of voltage dips[314].

522. Secondly, it included additional requirements in the issue of reactive energy allowance[315]. In this regard, all installations covered by the special regime, except for the exceptions that were established under the regulations, would receive an allowance or a penalty, as appropriate, for maintaining certain power factor values.

523. In addition, it proceeded to specify the definition of the concept of a substantial modification[316] of an installation for the purposes of renewal of the economic regime, to the extent that it set out that this figure would be used in masse in forthcoming years, given that the production facilities were of an age that made it necessary to renew equipment.

524. It is striking that the Claimants[317] only refer to this RD 1565/2010 for the purposes of highlighting its impact on the photovoltaic sector, without making any allusion to its technical and economic measures on the Wind Sector and, therefore, on their own wind farms. This omission is particularly noteworthy, given the arguments submitted by the AEE to the CNE during the processing of this RD 1565/2010[318].

525. In those arguments, the AEE, having recalled the case law of the Supreme Court, states that:

> *"any review of the remuneration regimen laid down in Royal Decree 661/2007 must necessarily guarantee the fair return on investments, and must also meet criteria laid down in this Royal Decree (which have not been modified) and the higher principles of legal certainty and proportionality."*[319]

526. Consequently, it accepts the possibility of amending the remunerative regime of RD 661/2007, for the sole purpose of guaranteeing a fair return.

527. Moreover, the measures introduced by this RD 1565/2010 appear to be left outside the alleged process of negotiation between the RE and the Government which, according to the

[313] RD 1565/2010, Preamble. R-0104.
[314] RD 1565/2010, article 15 which amends transitory provision five of RD 661/2007. R-0104
[315] RD 1565/2010, article 8, which amends article 29 of RD 661/2007. R-0104.
[316] RD 1565/2010, article 1 which modifies article 4.3 of RD 661/2007. R-0104.
[317] Memorial on the Merits, paragraph 354, among others.
[318] Arguments from the AEE to the CNE during proceedings with the Electricity Advisory Board concerning the Draft Royal Decree that regulates and modifies certain aspects relating to the special regimen. R-0166.
[319] Ditto, Page 7. R-0166

Claimants " led to" approval of RD 1614/2010, despite their evident technical and economic impact.

(11) RD 1614/2010

(11.1) Announcement and processing of RD 1614/2010

528. Continuing with the same *leitmotif* of the preceding measures, in other words the need to guarantee the economic sustainability of the SEE, RD 1614/2010 was adopted by the Government of Spain in light of the imminent need to reform the remuneration of regime of Renewable Energies. The Initiative came solely and exclusively from the Government of Spain, which was aware of: (i) the objectives of the reform to be carried out[320], (ii) the limits of its regulatory power, defined by settled case law of the Supreme Court, and (iii) the measures with which to achieve those objectives.

529. As we have seen earlier, the main Association of our RE producers, APPA, also recognised the need to introduce a reform of the regime governing Renewable Energies and to this end submitted its draft Renewable Energies Act, analysed previously. Along the same line, the AEE was aware of the need to introduce measures given "*the exceptional drop in electricity demand*".[321]

530. Consequently, the entire RE sector was aware that approval of RD 1614/2010 served a basic purpose and this was set out in its Preamble:

> *"So the backup system, as set out in formulation of the same, needs to adapt itself, safeguarding the legal certainty of investments and the principle of a fair return, to the dynamic reality of the learning curves of the different technologies and to the technical conditioning factors that flourish with the increase of the penetration of renewable energies in the generation "mix". This will enable us to maintain the necessary and sufficient support that is consistent with market conditions and with the strategic targets in energy issues and help to transfer to society the gains of an appropriate evolution of these technologies (...)[322]".*

531. In summary, this dealt with rebalancing the contribution of the different technologies to sustainability of the SEE, based on their different levels of penetration. It was clear, and the investors were well aware of this, that the government had a clear wish to achieve that objective and that consequently whatsoever measures would be taken to achieve this[323], Irrespective of whether the affected sectors accepted this. In fact, it should be remembered

[320] In this regard, see C-0180 which sets out the objectives of the reform. These objectives are included in the Report on the analysis of the regulatory impact of the draft Royal Decree which regulates and amends certain aspects concerning electricity production using solar energy and wind technologies. R-0082

[321] Arguments from the AEE to the CNE during proceedings with the Electricity Advisory Board concerning the Draft Royal Decree that regulates and modifies certain aspects relating to the special regimen, page 2. R-0166.

[322] Royal Decree 1614/2010, preamble. R-0105.

[323] In this regard, to analyse the PowerPoint Presentation given by Protermosolar to the *Partido Popular* (People's Party) in July 2010. R-0080. And also the news item "The Government decides to put a limit on the energy bubble", La Vanguardia, 21 March 2010. R-0180.

that there were also other more rigorous measures that were adopted with regard to the photovoltaic sector, despite its opposition.

532. The circumstance whereby the preparation of RD 1614/2010 managed to achieve support or acceptance of the reform by the wind and solar energy sectors does not alter (i) either its legal nature of an *erga omnes* regulation, (ii) or its content (iii) or the possibility of adopting new measures targeted at achieving the same purpose, if the macroeconomic circumstances so require.

533. As we have already specified with regard to the processing of RD 661/2007, these consultations with the sector are simply the consequence of application of the legal provision of consultations and hearing procedures during the preparation of the royal decrees[324], pursuant to article 24 of the **LGob**, previously transcribed[325]. This consultation procedure was backed by several hearing procedures, the existence of which is expressly acknowledged by the Claimants[326] (section c.) of article 24 of the LGob).

534. So,[327] the associations representing the technologies that could be affected by the reforms were sent two draft versions of the royal decrees (which would give rise to RD 1614/2010 and RD 1565/2010), to allow these associations to make suggestions. The appropriate hearing procedures then took place and the mandatory reports required under law were requested in order to draw up a regulation, as expressly acknowledged by the Claimants.

535. In fact, the AEE Association submitted arguments to the CNE through a claim of 29 August 2010, without affirming the existence of any undertaking not to change the regime. It thus limited itself to stating:

> *"In any case, safeguarding legal certainty and the guarantee of a fair return on investments are set out as inviolable limits to any modification to legislation that would affect existing facilities."*[328]

536. In other words, the AEE not only acknowledges the nonexistence of any undertakings but accepts that there could be new modifications to the profitability and to the regime governing existing installations. It only asks for two principles to be respected: legal certainty and the guarantee of a fair return.

537. Furthermore, the AEE Association expressly recognises the existence and binding nature of the consolidated case law with the CNE:

> *It is true that, in relation to these types of retroactive modifications, that the Supreme Court has declared that there is no "unmodifiable right" to the economic regimen remaining unchanged and that "the prescriptive content of Law 54/1997, of 27*

[324] Section III. A of this statement.
[325] Law 50/1997, of 27 November, from the Government. R-0070.
[326] Memorial on the Merits, paragraphs 368 and 369
[327] Email sent by the State Secretary for Energy (C-0177).
[328] Arguments from the AEE to the CNE during proceedings with the Electricity Advisory Board concerning the Draft Royal Decree that regulates and modifies certain aspects relating to the special regimen, page 2. R-0166.

November, on the Electrical Sector, neither leads to the setting in stone, or freezing of the remuneration regimen for owners of special regimen electrical energy facilities, nor the non-modificability of this regimen", thus recommending a relatively broad margin to the "ius variandi" of the Administration in a regulated sector in which general interests participate. Now, notwithstanding the foregoing, case law has established limits to this "ius variandi" of the Administration regarding the retroactive modification of this remuneration framework, particularly "the prescriptions of the Electrical Sector Act should be respected regarding reasonable profitability of investments.". Furthermore, infringement of the principle of legal certainty through a retroactive regulation "can only be resolved on a case-by-case basis "(...)".[329] *(Footnotes omitted).*

538. In summary, in its arguments the AEE reveals perfect knowledge of the Spanish Legal System, citing the Supreme Court Judgements of 25 October 2006, 3 December 2009 and 9 December 2009. To this end, it clearly reflects the Expectations that RE producers had with regard to "any" regulatory change. AEE does not claim either the setting in stone of the remunerative regime contained in RD 661/2007, or the alleged undertakings set out in RD-Law 6/2009 or in the alleged agreement reached with the Ministry of Industry one month prior to submitting these arguments. The only thing it claims is respect of the legal principle of a fair return and legal certainty.

539. Given the foregoing, we have made it clear that the processing referred to by the Claimants, even though they are trying to modify the *nomen iuris*, is the one legally provided for any royal decree, pursuant to the regulations of the Kingdom of Spain. This regulatory processing cannot, in any case, be compared or confused with that of an "agreement", "contract" or any other private law instrument, simply because the sector affected has had the opportunity to make consultations.

(11.2) Royal Decree 1614/2010 heeds the same *leitmotif*: sustainability of the SEE

540. The Claimants are trying to give the message that RD 1614/2010 represents an alleged agreement with the Wind Sector. However, it is sufficient to read the Regulatory Impact Analysis Report of the Draft RD 1614/2010 (hereinafter, "RIAR"), to see that its purpose is simply to guarantee sustainability of the SEE, by containing the expenditure tied to the RE subsidy:

"The installed power targets set out in the2005-2010 Renewable Energies Plan have been reached or exceeded for the solar energy and wind technologies. Although this development may be considered a very important achievement by all players involved (...) it has also occasioned problems that need to be addressed before they represent an irreversible risk for the economic and technical sustainability of the system[330]*."* *(Emphasis added).*

541. This Report adds the following:

[329] Ditto. Page 6. R-0166.
[330] Regulatory Impact Analysis Report of the draft Royal Decree which regulates and amends certain aspects concerning electricity production using solar energy and wind technologies. R-0082.

> *"This royal decree considers a series of austerity measures in order to, duly safeguarding legal certainty of the investments and the principle of a fair return, contribute to transferring to society the gains of the appropriate evolution of these technologies with regard to competitiveness in relative costs, reducing the deficit of the electricity system[331]" (emphasis added).*

542. Consequently, it is evident that the purpose of RD 1614/2010 was consistent with the other measures adopted up until that time: to guarantee a fair return to investors within the framework of a sustainable SEE. In fact, this purpose is the one that motivates each and every one of the measures set out in RD 1614/2010, as analysed hereunder.

(11.3) RD 1614/2010 did not incorporate any setting-in-stone guarantees

543. To achieve the aforementioned objectives, RD 1614/2010 adopted the following measures with regard to the wind sector:

(a) Limiting the hours of performance with the right to a premium (article 2).

544. This measure was also adapted with regard to Photovoltaic Technology through RD 1565/2010[332] and RD-Law 14/2010[333].

545. This measure helped to guarantee the economic and technical sustainability of the SEE. In effect, by limiting the hours of performance during which each renewable technology could feed-in the electricity generated with a subsidised Tariff, the cost associated to the subsidies could be controlled.

546. However, the limitations on the equivalent hours of performance introduced through RD 1614/2010 cannot be considered arbitrary, as they were based on the 2005-2010 REP. In this regard, the descriptions of the standard installations of each kind of RE technology set out in the 2005-2010 REP[334] included a delimitation of performance hours. These hours were used to determine the tariff which, for the purpose of achieving a fair return, was subsequently set out in RD 661/2007.

547. The reality showed that the installations were producing during more hours than initially set out in the 2005-2010 REP. Consequently, payment of the tariffs for a few hours of performance in excess of those taken into consideration in setting the tariff revealed that a return higher than the one considered to be fair was being obtained.

548. Note that this did not prevent ER reproducers from producing electricity above the corresponding limit of performance hours. In this case, the additional hours could not benefit from the subsidy, and had to be sold exclusively at market price. The electricity produced during these additional hours also had access and feed-in priority guaranteed under Law 54/1997.

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[331] Ditto. R-0082
[332] RD 1565/2010. R-0104.
[333] RD-Law 14/2010. R-0089.
[334] 2005-2010 REP, Chapter 4 Financing. R-0119

549. The foregoing measure reveals the unquestionable link between the methodology used by the Regulator and the subsidies set out in RD 661/2007. These subsidies were not established spontaneously, and were in fact the result of a major analysis targeted at setting a fair return for standard installations based on the standards established for each of them. An analysis that is set out in the different Renewable Energy Plans. Subsidies are the means used to achieve the fair return established for the different standard installations.

550. In this regard, the RIAR of RD 1614/2010 sets out that:

> *"The remunerative values of Royal Decree 661/2007 were calculated for the purpose of obtaining fair rates of return and on the assumption of the average performance hours of the installations that use these three technologies.*
>
> *These performance hours are set out in the 2005-2010 Renewable Energies Plan, for all technologies.*
>
> *Subsequently, in the actual operation of the system, it is been demonstrated that the performance hours of the installations, in some cases, exceed those that were initially planned (...). Under all circumstances, this means that, for these installations, the remuneration being obtained is higher than the fair remuneration*[335] *".*

(b) The future remunerative regime is not set in stone (article 5 (3))

551. A simple reading of RD 1614/2010 reveals that this regulation does not contain any undertaking or agreement whatsoever between the Government of Spain and the Wind Sector. Far from this, the Regulation represents a unilateral action by the regulator in the exercise of his powers[336] which does not incorporate a future setting in stone of a specific remunerative regime[337] as the Claimants appear to interpret this in article 5 (3) of said Royal decree.

552. However, said statement means ignoring the reason that justified the introduction of this article and the actual wording of the same.

553. As regards the reason for the introduction of article 5 of RD 1614/2010, we should remember that the Agreement of the Council of Ministers of 13 November 2009[338], left out of the arguments of the Claimants, led to, under the aegis of the provisions set out in

[335] Regulatory Impact Analysis Report of the draft Royal Decree which regulates and amends certain aspects concerning electricity production using solar energy and wind technologies. R-0082.
[336] VAT Section (1) of this Memorial on the Merits.
[337] RD 1614/2010. Article 5.3: "Without prejudice to the provisions set out in the royal decree, for the wind technology installations covered under Royal Decree 661/2007, of 25 May, the reviews of the tariffs, premiums and floor and cap limits, as referred to in article 44.3 of the foregoing royal decree, shall not affect the installations definitively registered with the Administrative Registry of Installations that Produce under the Special Regime which answers to the Directorate General for Energy Policy and Mines at 7 May 2009, nor those that had been registered with the Pre-allocation of Remuneration Register under the aegis of transitory provision four of Royal Degree-Law 6/2009, of 30 April and which comply with the obligations set out in its article 4.8." R-0105.
[338] Agreement of the Council of Ministers of 13 November 2009. R-0116

transitory provision five of RDL 6/2009[339], a scaling of the entry into operation of the wind farms registered with the Pre-Allocation of Remuneration Register.

554. This scaling meant that certain wind farms that came into operation after 2010 could be affected by the periodic review that had to take place in 2010, and thereafter, every four years. The literal wording of 44 (3) of Royal Decree 661/2007 led to this result.

555. In light of this circumstance, article 5 (3) of Royal Decree 1614/2010 was introduced. This was not about giving greater protection to these wind farms, but rather enabling the Regulator to redress an undesired result. To this end, the Preamble of Royal Decree 1614/2010, sets out that:

> *"Consequently, this Royal decree aims to resolve certain inefficiencies in the application of said Royal Decree-Law 6/2009, of 30 April, for wind and solar energy technologies. This aimed to make sure that the prevailing economic regime in Royal Decree 661/2007, of 25 May, which regulates the production of electricity under the special regime, covered the projects that were in a state of advanced maturity".*[340]

556. A simple reading of article 5 (3) of RD 1614/2010 shows that, as we have explained, all this article does is extend the provisions set out in paragraph two of article 44(3) paragraph 2 of RD 661/2007 to installations whose certificate of coming into operation is after 1 January 2012.

557. However, at no time does its state that article 5 of RD 1614/2010 has to apply to reviews or modifications other than those established in article 44 (3) of RD 661/2007. Furthermore, at no time does it say that wind farms are outside the margin of Law 54/1997 and that, consequently, they are not subject to application of the regulatory measures required to guarantee the economic sustainability of the SEE or prevent situations of excess remuneration, if such situations exist.

(c) Review of the premiums of RD 661/2007

558. Royal Decree 1614/2010 also modified the premiums of installations that use wind power technology of Royal Decree 661/2007, of 25 May. Article 5 regulated the reviews of the reference premiums of RD 661/2007, considering several possibilities[341]:

a) Premiums applicable from 7/12/2010 to 31/12/2012:
   The reference premiums are established as those corresponding to the date of coming into force of RD 661/2007 reduced by 0.35% and without updates.
   These premiums would apply to the installations covered by the remuneration regime of RD 661/2007, excluding those covered by Transitory Provision One.
b) Premiums applicable from 1/1/2013:
   The premium values set for 2010 apply (through Order ITC 3519/2009), updated in accordance with the coefficients of article 44.1 of RD 661/2007.

[339] Royal Decree-Law 6/2009, of 30 April, which adopts certain measures in the energy sector and approves the discount rate. Transitory Provision Five R-0088.
[340] Royal Decree 1614/2010, of 7 December, regulating and modifying certain aspects related to of electric energy production using thermoelectric solar and wind power technologies Preamble. R-0105
[341] RD 1614/2010. Article 5. R-0105.

> Consequently, instead of applying the corresponding premium, pursuant to RD 661/2007, for 2013 those corresponding to 2010 would be applied, in other words the premium would be frozen, in accordance with the one in place for 2010.
>
> This regulation applied to all installation, including those covered by transitory provision one of RD 661/2007. With regard to these latter installations, we should remember that since 2006, through approval of RD Law 7/2006, the updating of the premiums and tariffs of RD 436/2004 pursuant to the ART had been removed. These premiums and tariffs had not been updated from 2004 until 1/1/2013. Added to this is the fact that, following approval of this RD 1614/2010, from 2013 onwards they were not subject to application of the premiums of RD 661/2007 updated to that date, but rather to the premiums of 2010. So, first the premium update is frozen for six years and then they are subject to application of premiums that were frozen two years previously.
>
> It is unquestionable that this involved a reduction of the premium to be received by the wind farms, given the lag between the freezing of the premiums and the increase of the CPI that took place during those years.

(11.4) Conclusion: proportionate nature of the measures introduced

559. All modifications of the remunerative regime were appropriate and proportionate to the level of implementation of wind technology in the SEE and its repercussion on the tariff deficit.

560. In this way, we see that contrary to what the Claimants are stating, RD 1614/2010, as had been the case with RDL 6/2009 and previously RD 661/2007, once again confirmed that wind technology could not be configured as an island within the SEE and that under no circumstances had there been any guarantee of a setting in stone with regard to the subsidies.

(12) Royal Decree-Law 14/2010, of 23 December.

561. The maximum limits of the deficit established by Royal Decree-Law 6/2009 for 2010, 2011 and 2012 were raised by Royal Decree-Law 14/2010[342] (hereinafter **"RD-Law 14/2010"**) given the impossibility of complying with previous limits. In fact, this was set out in its Preamble, when it stated that:

> *"Since approval of the aforementioned Royal Decree-Law (in reference to RD-L 6/2009) there has been a series of ensuing circumstances that have had a direct impact on the forecast tariff deficit of the electricity system and which have meant that the maximum limits of the deficit ex ante established in the aforementioned additional provision 21 have been widely surpassed. The impact of the global crisis affecting the Spanish economy has meant a significant drop in the demand for electricity while, on the supply side, aspects such as the evolution of fuel prices in the international markets in 2010 or the favourable weather conditions that have led to greater electricity production using renewable sources have all had an impact. The current underlying situation has not had symmetrical effects on all electricity sectors: while*

[342] Royal Decree Law 14/2010, of 23 December, establishing urgent measures for the correction of the tariff deficit in the electricity sector. R-0089.

the ordinary regime (traditional power stations) have seen their performance hours reduced and their revenue reduced through the fall of prices in the wholesale market, the special regime producers are faced with a different situation because of their specific regime which guarantees them the sale Of feed-in energy .[343]*" (Emphasis added).*[344]

562. RD-Law 14/2010 set out in article 1.2 with regard to all of the RE technologies that:

"The remuneration of regulated activity shall be financed through the income collected through access tolls to the transport and distribution grids paid by consumers and producers." [345]

563. This RD-Law therefore meant that all electricity producers, both OR and RE, were obliged to pay a toll for using the transport and distribution grids[346]. This affected the profits of the RE producers. It shows the inconsistency of the Claimants' argument on the *setting in stone* or non-changeability of the regime of RD 661/2007 following RD 1614/2010. In fact, RD-Law 14/2010 was interpreted by some photovoltaic producers as a modification of the economic regime to which they were entitled and they took their case to the Supreme Court, which dismissed their challenge, reiterating (once again) its settled case law[347].

564. Once again, this case law showed that the investors were aware that their remuneration could be affected by subsequent measures, whether positive or negative, without the right to immutability of the remuneration over time or of a mechanism to obtain this. They were

[343] Royal Decree Law 14/2010, of 23 December, establishing urgent measures for the correction of the tariff deficit in the electricity sector. R-0089.
[344] Note that the Preamble focuses on the new circumstances that made it necessary to adopt additional measures proportionate to the level of implementation of the different technologies. So then, the implementation of solar energy technology had increased, and the syllogism is clear, the greater the implementation, the greater the obligation to contribute to reducing the deficit.
[345] Ditto. R-0089
[346] Ditto. Transitory Provision One. R-0089.
[347] In this regard, the Supreme Court has also ruled on different appeals filed against the ministerial orders setting the tolls for 2011 (starting with Order 1TC/3353/2010), in which the RD-Law was the object of an indirect challenge. We should highlight the judgement from the Supreme Court of 25 June 2013 which, among other considerations, sets out:"The basis of the appellants' censorship is limited, in summary, to the fact that payment of the toll had a negative impact on their profit and loss statements and therefore on the return on their investments. And given that they base themselves on the premise -although they do not express it in these terms- that the legal situation configured through Royal Decree 661/2007 is virtually immutable or unchangeable for the next 30 years (and even subsequent years), any unfavourable measure that alters this would rupture the principles repeatedly invoked (the principles of legal certainty and legitimate expectations). Immutability which, according to their theory, would also extend to the subsequent provisions of a tax nature -a nature that they attribute to the tolls- that also could not have a negative impact on profits stemming from the remunerative regime that they enjoyed in accordance with RD 661/2007.The Chamber has rejected this premise in the preceding judgements and shall do the same in this case. If in those cases, referring to the challenge of RD 1565/2010, we upheld that the principles invoked by the appellants did not prevent the holder of regulatory powers -respecting the limits of the "fair return" set through the LSE- from introducing certain changes in the remunerative regime set out in RD 661/2007, we must also uphold the fact that these principles do not prevent the holder of the legislative powers (...) from adopting general measures, whether or not taxation measures, that have an impact on this. So then, to legitimately decide that all electricity producers, without exception, contribute through the payment of tolls to the costs attributable to the investments required to transport and distribute the energy." (emphasis added). R-0150.

also aware, in accordance with such settled case law, that the measures would always have to respect the principle of a *fair return.*

565. More precisely, the access tolls and the limitation of equivalent hours of performance introduced through this RD-Law 14/2010, coupled with other adjustment measures adopted for the photovoltaic sector through RD 1578/2008, were the object of an initial international arbitration procedure against the Kingdom of Spain. This arbitration has been resolved through the Award of 21 January 2016, which dismissed all claims lodged by the Claimants.[348]

566. The Claimants invoke the Preamble of RD-Law 14/2010 to set out their legitimate expectations on the setting in stone of the remunerative regime established in RD 661/2007[349]. However, they failed to explain that the implementation of the tolls had an economic impact that reduced the remuneration established in RD 661/2007. In this regard, the Preamble of RD-Law 14/2010 stated:

> *"Given that the production installations, especially those under the special regime, have experienced significant growth, there has been an increase of investments in the transport and distribution of electricity grids in order to feed in the energy. In the current context of the crisis and the tariff deficit, it is justified that producers contribute to payment of the costs attributable to the required investments through the payment of tolls (...)".*[350]

567. The speech given by the Minister for Industry (Mr Sebastián) in the Lower House of Parliament, given during the session held for validation of this RD-Law in 26 January 2011, clearly revealed its purpose (removal of the deficit) as well as the absence of any setting in stone of the remunerative regime in force following approval of RD 1614/2010. Thus, the Minister says:

> *"...since 2009, the Government has been working to adopt a set of measures whose common denominator is the streamlining of regulated costs and the reduction of the tariff deficit (...) All these measures have come about from dialogue, both with the sectors affected as well as with the main political forces. But these measures of 2009 and 2010 have not been enough. The imbalances have been accentuated as a consequence of the appearance of a series of adverse circumstances, in some cases exceptional, of which I should like to highlight two. Firstly, the above forecast growth of some of the regulatory costs during 2010, in particular the premiums of the special regime, and secondly, the evolution of electricity demand, which in 2009 fell 4.7%. This is the first fall in electricity demand after 25 years of sustained increases of around 4% per year. These decreases in electricity demand reduce the income of the system and entail fixed costs that have to be paid by fewer users of electricity, which raises the cost per user. These two circumstances have increased the tariff deficit and have meant that the measures adopted thus far to guarantee the progressive reduction*

[348] Award given in the *Charanne B.V. vs Spain Case*. RL-0049.
[349] Memorial on the Merits, paragraph 835.
[350] RD-Law 14/2010. Preamble. R-0089

of the tariff deficit in a balanced way among all sector agents proved to be inefficient. Consequently, the need to urgently approve new measures (...). "[351]

568. Consequently, approval of RD-Law 14/2010, of 23 December 2010 (in other words, 16 days following RD 1614/2010), shows that the latter royal decree in no case entailed the setting in stone of the economic regime contained in RD 661/2007.

F. The measures challenged by the Claimant in this procedure.

(1) Justification of the regulatory measures challenged

569. Justification of the measures adopted by the Kingdom of Spain can only be understood from a rational understanding of the SEE as a whole. In this regard, we should not forget that the subsidised production using renewable sources is an integral part of the SEE and, consequently, is subject to its principles and its objectives.

570. More precisely, achieving and maintaining those principles and objectives led to the take-up of the different regulatory measures that are the object of this arbitration. We should point out that, contrary to what appears to be shown in the Memorial on the Merits, these measures affected all activities of the SEE and not only the Renewable Energies used for production.

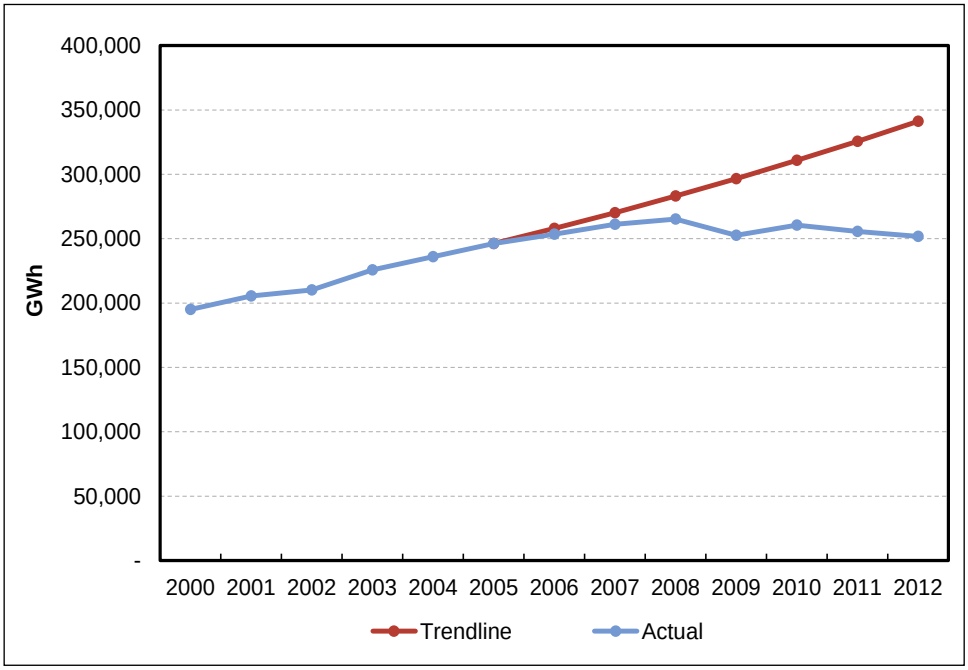
571. In effect, as justified in the Econ One Research Report, Spain suffered a major economic crisis from 2007 onwards. This meant that GDP growth fell from 3.8% in 2007 to 1.1% in 2008, and was once again negative in 2009, leading to an economy that shrank by 3.6%. There was no economic growth in 2010, and the economy continued to shrink in 2011 and 2012. By the same token, as a consequence of the crisis the rate of unemployment rose from 8% in 2007 to 25% in 2012.

572. Along the same line, Spain's financial position worsened significantly as a result of the crisis. So, having experienced a surplus during 2006 and 2007, Spain then had a deficit that exceeded 10% of GDP in 2012. The accumulation of the budget deficit grew from 39% of GDP in 2008 to 85% of GDP in 2012.

573. This crisis situation led to a major drop in electricity demand in the SEE. This fall in Demand led to a substantial reduction of revenue for the SEE with which to pay its costs, which include subsidies to renewable energies.

574. Here it is relevant to compare forecast consumption of electricity, based on the growth trend between 2000 and 2005, the period during which the 2005 -2010 REP was compiled, with the actual electricity consumption[352]:

[351] Record of Proceedings. Recognition of RD-Law 14/2010. R-0227.
[352] Econ One Research Report, 15 June 2016, appendix D.



575. Meanwhile, the costs of the SEE, designed in the context of a radically different economic situation, not only stayed the same but also increased. This compromised the economic sustainability of the SEE.

576. In this context, the different preliminary analyses, the regulatory evolution, the technical knowledge and the technological evolution revealed the existence of remunerations which, either by default or by excess, failed to maintain the criterion of a fair return established for remunerations under the so-called special regime.

577. The regulatory adjustment measures adopted by the Respondent have not only affected the installations such as those of the Claimants, but have also been extended to all installations that received payments charged to the electricity system. The aim was to give a global and proportionate response to the problem of the no sustainable imbalance at the SEE. Furthermore, the measures have been taken, *inter alia*, in accordance with an in-depth analysis of remuneration, which affects virtually all of the activities of the electricity system.

578. In this way, prior to addressing the measures challenged in this arbitration procedure, we shall take a brief look at the measures concerning other sectors of activity of the SEE, which have been affected by the regulatory adjustments.

(1.1) Transport and Distribution Activities

579. The reform reviews the methodologies of remunerating the Transport and Distribution activities in accordance with the costs required to enable an efficient and properly run company to perform the activity and through the application of uniform criteria throughout Spanish territory[353].

[353] Royal Decree-Law 9/2013. Article 1(1). R-0094.

580. However, they were not guaranteed a fair return, rather an *appropriate remuneration*. This concept has involved setting the return as the average return of State Bonds over 10 years in the secondary market, plus a spread of 200 base points[354]. Consequently, at 6.398 %; in other words, lower remuneration for these activities than the remuneration received by installations that produce electricity using renewable sources.

581. It also sets regulatory periods of six years and reviews based on the remunerative parameters that influence payment of the remuneration of each of these activities with regard to their investments. This new regulation affects all installations, irrespective of the date they came into operation, and it is implemented through the regulatory standards that were approved on 27 December 2013[355].

(1.2) Remunerative regime for Production in the non-mainland systems.

582. Very relevant changes have affected the remuneration of the economic regime for production of electricity in the non-mainland electricity systems (Balearic Islands, Canary Islands, Ceuta and Melilla).

583. The measures adopted have given rise to a reduction of the remuneration received by companies that produce electricity in these territories of more than 600 million euros. These measures have affected the net value of assets, the non-remuneration of installations, the accrual period of the amounts, the updating of the price of fuels used, the criteria surrounding the technical management of the system and the procedural processes of installations.

584. The regulation has been introduced in royal decree laws 13/2012[356], 20/2012[357], 9/2013[358], in Law 24/2013[359] and in Law 17/2013[360], of 29 October, to guarantee the supply and to increase competition in the mainland and non-mainland electricity systems.

(1.3) Payments for capacity

585. The payments for capacity are those subsidies paid to the owners of certain electricity production installations, mainly combined cycles, for these to provide security to the electricity supply even when their energy is not fed into the system. These payments are given on the basis of increased renewable generation and given the fact that renewable energies are not man-manageable.

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[354] Ditto. Article 6(1). R-0094.
[355] Royal Decree 1047/2013, of 27 December, which sets out the methodology for calculating remuneration of the transport of electricity (R-0108) and Royal Decree 1048/2013, of 27 December, which establishes the methodology for calculating remuneration of electricity distribution and other regulatory provisions. R-0109.
[356] Royal Decree-Law 13/2012, of 30 March. R-0091.
[357] Royal Decree-Law 20/2012, of 13 July. R-0092.
[358] Royal Decree-Law 9/2013, of 12 July. R-0094.
[359] Law 24/2013, of 26 December 2013. R-0076.
[360] Law 17/2013, of 29 October, to guarantee the supply and to increase competition in the mainland and non-mainland electricity systems. R-0077.

586. In other words, there is no way of managing wind so that there is wind production every day, or with greater intensity in certain areas. As explained by the SEE[361], "backup energy" is required to guarantee the supply in the event of production decreases.

587. The amount corresponding to the incentive for long-term capacity investment for production installations was reduced from €26,000 to €10,000/MW/year and period left to cover the 10-year period was doubled.[362]

(1.4) System of Non-interruptibility

588. The system of non-interruptibility has also suffered a very pertinent regulatory change that has led to a decrease, in 2014, of 300 million euros over remuneration of less than 700 million[363] euros.

589. A system of auctions has been established for this purpose. Based on this system, all companies that wish to provide the service offer the price at which they would be willing to interrupt their consumption of electricity. In this way, the energy they would consume is used to cover situations where there is insufficient generation.

(1.5) Procedure of restrictions through supply guarantee.

590. The procedure of restrictions through supply guarantee which subsidised the operation of coal-fired power stations with partial autochthonous use has been removed. Its annual amount was higher than 480 million euros[364].

(1.6) Contributions of the General State Budgets to the electricity system for the development of renewable energies

591. Lastly, we should underline the fact that the General State Budgets have included, in 2013[365], 2014[366] and 2015[367], budget entries that represent direct contributions to the electricity system in order to mitigate the deficit situation that existed.

592. In 2015[368] there was a contribution of 887 million euros to finance the generation of electricity in the non-mainland systems. There is a second entry of 330 million euros to finance the remunerative regime of renewable energies, and a third entry of 2.989 billion euros for the same purpose.

593. This means that Spanish taxpayers pay a total of 4.206 billion euros to the electricity system for the purpose of developing installations with a special remunerative regime and which generate electricity using renewable energies. These amounts are taken from other

[361] Section IV.A.3 of this Memorial on the Merits.
[362] Royal Decree-Law 9/2013. Article 7. R-0094.
[363] Order IET/2013/2013, of 31 October, regulating the competitive mechanism of assigning the demand management of non-interruptibility service R-0114.
[364] Sole Article of Royal Decree 134/2010, of 12 February, which establishes the procedure for ruling on restrictions through supply guarantee and modifies Royal Decree 2019/1997, of 26 December, which organises and regulates the electricity production market. R-0103.
[365] Statement from the Spanish General State Budgets for 2013. R-0021
[366] Statement from the Spanish General State Budgets for 2014. R-0022.
[367] Statement from the Spanish General State Budgets for 2015. R-0023.
[368] Statement from the Spanish General State Budgets for 2015. R-0023.

public policies due to the fact that the State has decided to keep the subsidies in accordance with the principle of a fair return.

(1.7) Discount rate

594. The discount rate involves a significant reduction of the electricity bill for certain groups of societies, such as unemployed persons, pensioners, large families and others.[369]

595. This aid has moved from being a cost charged to the electricity system to being a cost assumed by parent companies or companies that simultaneously perform the activities of production, distribution and sales of electricity. More specifically, this affects traditional electricity companies and not companies such as those of the Claimants.

596. In other words, there is a series of companies that have to accept a cost, even when this affects their profitability and even when they are owners of renewable energy installations, as they form part of the SEE.[370]

(2) The announcement of the challenged measures.

597. In this context and more specifically with regard to the renewable energies sector, at the end of 2011 it was decided to undertake a reform of the electricity sector targeted at improving the regulatory framework, taking into consideration the changes that have taken place in the SEE since approval of Law 54/1997.

598. As we have already set out, this improving has represented an evolution of the regulation of all SEE activities. The foregoing evolution respects, under all circumstances, the essential principles of the SEE defined in section V.A.(3)

599. The need for these regulatory measures had been announced since 2011, as we explain below.

(2.1) Law 2/2011, of 4 March, on a Sustainable Economy

600. Here we should remember that in April 2011 the Sustainable Economy Act was published. This legal text sets out the following criteria to which the regulation in energy matters had to adapt in general and with regard to the incentives to the premium regime in particular[371]:

- The link between the planning and the legislation with regard to organisation of public incentives required to comply with the targets of this planning.
- The need for the planning to include several scenarios on the future evolution of energy demand, on the resources required to satisfy this demand, on the power needs and, in general, useful provisions for the taking of investment decisions through private initiative and for energy policy decisions, fostering an appropriate balance between system efficiency, security of supply and environmental protection.

[369] Article 45.2 and transitory provision 10 of Act 24/2013. R-0076.
[370] Royal Decree-Law 9/2013, Article 8. R-0094.
[371] Act 2/2011, of 4 March, on a Sustainable Economy, articles 77, 78 and 79. R-0073.

- Legislation will sort the public incentives guaranteeing an appropriate return on investments in special regime technologies, which motivates an installation volume compatible with the objectives set out in the Energy Plans.
- In all circumstances legislation will sort the public incentives, adapting to the need whereby compliance with the planning targets is reached taking into consideration the principles of economic efficiency among the different alternatives and of the economic sustainability of the measures adopted.

(2.2) Announcement of measures by the Prime Minister

601. On 19 December 2011, the Prime Minister announced in the Lower House of Parliament the possible measures to be adopted in the energy sector:

> *"We need to be well aware that Spain has a major energy problem, in particular in the electricity sector, with an annual deficit that exceeds three billion euros and a cumulative tariff debt of more than 22 billion.*
>
> *The electricity tariffs for household consumers are the third most expensive in Europe, and the fifth highest for industrial consumers.*
>
> *[...] If we do not address reforms, the imbalance will be unsustainable and the increases of prices and tariffs would place Spain at a biggest disadvantage in energy costs in the whole of the developed world. We must therefore apply a policy based on slowing down and reducing the average costs of the system, in which decisions are taken without demagoguery, using all available technologies, without exceptions, and which is regulated for the primordial purpose of ensuring our economy is competitive."*[372] *(emphasis added)*

(2.3) CNE Press Release of 28 December 2011

602. The regulating authority of the Spanish electricity system, the CNE, issued a press release on 28 December 2011 in which, on the occasion of its report on the draft order that would establish the access tolls from 1 January 2012 and the tariffs and premiums of special regime installations, it set out that:

> *"The lack of convergence between revenue and costs of the regulated activities over the last 10 years has generated a growing debt of the electricity system, which has entailed a progressive increase of payments to finance this through current and future access tolls paid by electricity consumers, as well as a temporary impact on the debt of those companies that are obliged to finance the system's deficit. Consequently, the CNE reiterates the need to introduce immediately, inter alia, proposals on the regulation of activities, targeted at removing the structural deficit of the system and mitigating the costs of financing the debt."*[373] *(emphasis added)*

[372] Transcription of Mariano Rajoy's inaugural debate as Prime Minister, Spanish Parliament, Monday, 19 December 2011, www.lamoncloa.gob.es. R-0192.
[373] "The CNE is analysing the review of access tolls and certain tariffs and premiums of special regime installations", press release from the National Energy Commission (CNE), 28 December 2011. R-0170.

603. In this context of announcing a structural reform, on 27 January 2012 the first measures with legal rank were adopted with regard to reforming the electricity sector: the approval of a standard that avoids an increase of the deficit and the application for a report from the Spanish electricity regulating authority on proposals for measures to be adopted.

(2.4) Royal Decree-Law 1/2012, of 27 January.

604. First of all, Royal Decree-Law 1/2012, of 27 January, is approved, which proceeds to the suspension of the pre-allocation remunerative procedures and the elimination of the economic incentives for new electric energy production plants based on cogeneration, renewable energy sources, and waste (hereinafter, "**RD-Law 1/2012**")[374].

605. In the press release from the Ministry of Industry, Energy and Tourism, following the Council of Ministers that approves this RD-Law 1/2012, confirmation is given that work is taking place on reforming the electricity sector:

> *"The complex economic and financial situation, coupled with the situation of the electricity system, make it advisable to remove the incentives for the construction of these installations, on a temporary basis, while we introduce a reform of the electricity system that avoids the generation of the tariff deficit, namely the difference between the revenue from tolls to access the electricity transport and distribution grids and the costs of the regulated activities of the system."*[375] *(emphasis added)*

(2.5) The report from the National Energy Commission on the Spanish Energy Sector of 7 March 2012.

606. The second measure adopted by the Government on 27 January 2012 was to request the CNE[376], in its capacity as the advisory body in energy matters, to compile a report on regulatory adjustment measures that could be adopted in the energy sector. In particular, it was asked to study measures targeted at stopping the evolution of the tariff deficit in the electricity sector[377].

607. The CNE issued Report 2/2012 *"On the Spanish Energy Sector"*[378] on 7 March 2012, the first part of which is dedicated to the *"Measures to Guarantee Economic-Financial Sustainability of the Electricity System".* In drawing up this report, the CNE had opened a

[374] Royal Decree-Law 1/2012, of 27 January, which proceeds to the suspension of the pre-allocation remunerative procedures and the elimination of the economic incentives for new electric energy production plants based on cogeneration, renewable energy sources, and waste. R-0090.
[375] "*The Government will temporarily suspend the premiums of new special regime installations"*. Press release from the Ministry of Industry, Energy and Tourism, 27 January 2012. R-0172.
[376] Copy of the letter from the State Secretariat of Energy to the Chairman of the National Energy Commission of 27 January 2012. R-0193.
[377] Information on the public consultation process regarding regulatory adjustment measures in the energy sector of 2 February and 9 March 2012, published on the website of the National Energy Commission, www.cne.es. R-0194.
[378] Report on the Spanish Energy Sector Part I. Measures to guarantee the economic-financial sustainability of the electricity system, National Energy Commission, 7 March 2012. R-0131.

period of public consultation at the beginning of 2012 in which a total of 477 arguments were obtained from companies and sectors affected[379].

608. The report on the SEE is accompanied by an Introduction and Executive Summary[380] in which the CNE sets out the situation of the sector[381], pointing out its non-sustainability and emphasising that the economic crisis, the increase in the price of fossil fuels and the introduction of measures to fight climate change had led to rising prices for end consumers.[382]

609. In this context, the CNE proposes a series of short-term and medium-term measures on all activities of the electricity sector, including renewable energies, which reflect the urgent need to make changes to the regimes.

610. So, with regard to the latter, the CNE, for the purpose of guaranteeing the economic sustainability of the SEE, proposes a series of short-term measures: (i) "*laminate the temporary path of the premiums that will be received by solar energy power stations registered with the pre-allocation register, but without a definitive certificate of coming into operation, as this is the technology with the highest level of penetration in the medium-term and the greatest commitment* "[383]; (ii) limit the use of fossil fuels for which a premium is paid to 5% of primary energy[384]; (iii) avoid the automatic increase of the efficiency X factor in the updating of tariffs and premiums (IPC-X); (iv) bring the premium into line with the tariff applicable to the solar energy plants to avoid situations of excess remuneration[385] (v) partially finance the RE premiums with revenue charged to CO2 auctions, under the aegis of Directive 2009/29/EC[386]; (vi) partially finance the RE premiums by charging this to sectors responsible for the consumption of fossil fuels or alternatively through the General State

[379] Information on the public consultation process regarding regulatory adjustment measures in the energy sector of 2 February and 9 March 2012, published on the website of the National Energy Commission, www.cne.es. R-0194.
[380] Report on the Spanish energy sector. Introduction and Executive Summary. National Energy Commission, 7 March 2012 R-0131.
[381] The same issues would be declared by the European Commission in its document European Commission guidance for the design of renewable support schemes, Commission Staff Working Document, SWD (2013) 439 final, 5 November 2013. R-0200.
[382] Report on the Spanish energy sector. Introduction and Executive Summary, National Energy Commission, 7 March 2012, page 2: *"In recent years we have seen the flourish of new challenges and problems in the regulatory models that were established on commencement of the liberalisation of the European energy markets. There are many triggering factors, and these are largely specific for each country. Among the common factors, we can point to a fall in the demand for energy products, the difficulties in funding new infrastructures associated to the economic crisis, the increase in the price of fossil fuels as well as the introduction of measures to fight climate change. All of these put upward pressure on the prices that end consumers pay for use of the energy installations and/or to purchase energy, depending on the regulation and the financing mechanisms chosen in each country."* (emphasis added). R-0131.
[383] *"Report*on the Spanish energy sector Part I. Measures to guarantee the economic-financial sustainability of the electricity system, National Energy Commission, 7 March 2012, page 52. R-0131.
[384] Ditto, pages 23 and 24.
[385] Ditto, page 23.
[386] Ditto, page 40.

Budgets; (vii) modulate the pace of penetration initially envisaged in the NREAP in line with the provisions set out in RD-Law 1/2012[387].

611. Similarly, the CNE proposed measures to be adopted in the medium-term: (i) review existing regulations and propose two mechanisms: the introduction of competitive mechanisms (auctions) and premiums based on cost regulatory information[388] and (ii) remove subsidies from finalisation of the economic life (estimated service life) of the plant[389]; (iii) consider the cap and floor of the premium so that whenever the market price exceeds the cap, the premium is returned as income from the System[390]; (iv) allocate the actual costs of operation (reserving additional power, management of deviations in real time or mechanisms for cross-border balancing services[391].

(2.6) National Reform Programme and Memorandum of Understanding with the EU of 2012

612. On 27 April, the Government approved[392] the "National Reform Programme 2012"[393]. In the section: "*Actions targeted at resolving the imbalance that exists between revenue and cost of the electricity system*" (pages 208 and 209), reaffirming the Kingdom of Spain's commitment to eliminating the tariff deficit.[394]

613. This need was appreciated and expressly declared by the International Monetary Fund in June 2012[395]. Moreover, it was also appreciated and declared in the Recommendation from the Council of the European Union on 10 July 2012, with regard to the National Reform Programme of 2012 and the appraisal from the Council on the Stability Programme of Spain for 2012-2015:

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[387] Ditto, pages 40 and 41.
[388] Ditto, pages 73-80.
[389] Ditto, pages 81-82.
[390] Ditto, pages 82 and 83.
[391] Ditto, pages 84 and 85.
[392] Reference from the Council of Ministers of 27 April 2012, ww.lamoncloa.gob.es. R-0195.
[393] National Reform Programme 2012, Government of Spain. R-0121.
[394] National Reform Programme 2012, Government of Spain: *"The Government is firmly committed to eliminating the tariff deficit and repaying the accumulated debt within reasonable period. The effort to achieve this objective will be distributed fairly among consumers, the public sector and the private sector, within a framework of sweeping reforms of the electricity sector, which will entail measures to cut costs of the regulated activities, increase revenue through tolls, review the energy planning and introduce a stable regulatory framework. Cutting costs of the regulated activities: The costs of regulated activities have risen sharply since 2006. Since that year, average revenue from access tolls has increased 70% in cumulative terms, while access costs have increased by 140%. Currently, the three most significant types of access costs are the special regime premiums (40.3% of overall costs); the entries with the highest contribution to the growth of costs of regulated activities have been the special regime premiums [...] which have multiplied fivefold since 2006. [...] In the immediate future more details will be given about these measures, so that all sectors contribute fairly to the adjustment of regulated costs."* (emphasis added). R-0121.
[395] The International Monetary Fund, in "Consultations of Article IV with Spain Final Declaration of the IMF Mission, Madrid, 14 June 2012" sets out in section 19: *"The introduction of the other structural reforms scheduled will be important in complementing the labour reform. [...] and the schedule of Government reforms is appropriately focused on [...] elimination of the tariff deficit. It will be important for these reforms to be introduced quickly and effectively - a detailed and ambitious calendar would help to structure and communicate the efforts"*. (emphasis added). R-0196.

"To complete the electricity and gas interconnections with neighbouring countries and to tackle the tariff deficit of the electricity sector in a global manner, in particular improving the profitability of the electricity supply chain"[396] *(emphasis added).*

614. In other words, the reform that was announced was part of a set of structural measures of macroeconomic control adopted by Spain pursuant to the recommendations from the European Union and the International monetary Fund. These measures have affected all citizens and Spanish businesses, who have had to bear certain sacrifices or encumbrances in a highly negative economic context. As such, we can refer to the macroeconomic control measures adopted in: (i) the job market, (ii) social protection through a reduction of expenditure, (iii) Public Administrations through the take-up of measures to reduce their size, (iv) a reduction of salaries in the public sector, and a lengthy etcetera.

615. The Kingdom of Spain addressed macroeconomic control measures within the framework of the electricity regulation in order to deal with international commitments. The Council Recommendations of March 2012 have already been given[397]. However, because of its binding nature, we should also highlight the Memorandum of Understanding signed with the European Union on 20 July 2012, as a consequence of the need to perform a financial bailout of certain Spanish banks. This Memorandum links the financial situation with other macroeconomic imbalances and forces the Kingdom of Spain to adopt structural reform measures to redress these imbalances[398]. Among these structural reforms, the Memorandum expressly mentions the need to "*address the electricity tariff deficit in a comprehensive way*".

616. In this economic and legal context, it was reasonable and justified to adopt macroeconomic control measures also in the framework of electricity regulation. And this, in light (1) of the unsustainable imbalance of the SEE, as demand had fallen as a consequence of the economic crisis, and (2) of the accumulated tariff deficit. This need for reform was expressly verified and demanded, as we have substantiated, by the IMF and the EU.

(2.7) Other warnings from the Government on the reform of the Electricity Sector

617. Following the worsening of the economic and financial crisis stemming from the financial bailout of banks and some Spanish Autonomous Communities, the Government

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[396] Council Recommendation of 6 July 2012 on the National Reform Programme 2012 of Spain and delivering a Council opinion on the Stability Programme for Spain for 2012-2015. R-0061.

[397] Council Recommendation of 10 July 2012 on the National Reform Programme 2012 of Spain and delivering a Council opinion on the Stability Programme for Spain for 2012-2015. R-0062.

[398] Memorandum of Understanding signed with the European Union on 20 July, 2012. "*VI. Public Finances, Macroeconomic Imbalances And Financial Sector Reform:* 29. *"There is a close relationship between macroeconomic imbalances, public finances and financial sector soundness. Hence, [...], with a view to correcting any macroeconomic imbalances as identified within the framework of the European semester, will be regularly and closely monitored in parallel with the formal review process as envisioned in this MoU. [...]*

31. Regarding ***structural reforms****, the Spanish authorities* ***are committed*** *to implement the country-specific recommendations in the context of the European Semester. These reforms aim at* ***correcting macroeconomic imbalances,*** *as identified in the in-depth review under the Macroeconomic Imbalance Procedure (MIP). In particular, these recommendations invite Spain to: [...] 6) [...] address* ***the electricity tariff deficit in a comprehensive way****."* (emphasis added). RL-0067.

undertook different actions to show the markets the proximity of the structural reforms announced in the Prime Minister's inaugural debate and which have been backed by both the International Monetary Fund and the European Union.

618. In September 2012, the Government publishes another Paper *"The reforms of the Government of Spain: Determination in overcoming the crisis"*[399]. In the Chapter called "*Projected reforms*", there is reference to the "Reform of the energy sector":

> *"Very shortly, the reform of this sector shall be approved through a Bill of Energy Reform, to ensure that the cost of energy does not condition the competitiveness of our economy to such an extent. The aim is to provide a definitive solution to the problem of the huge tariff deficit of our energy system."*

619. On 27 September, at the Council of Ministers, the Government approves the "Bill of General State Budgets for 2013"[400]. This Council of ministers also approves the "Spanish Strategy for Economic Policy: Balance and structural reforms for the next six months"[401]. This strategy makes reference to the "Energy reform" and announces the take-up of structural measures to correct the tariff deficit once and for all, as well as presentation of a new Electricity Sector Act to resolve the inefficiencies that had been detected.

620. In 2012, in addition to RD-Law 1/2012, the Government approved a further two royal decrees-laws (Royal Decree-Law 13/2012[402] and Royal Decree-Law 20/2012[403]) which contained important measures to cut the cost of the system. Neither of these measures affected the installations that use renewable sources, although they did affect the installations of ordinary generation and the owners of the distribution and transport installations, who saw their remuneration reduced significantly.

621. Furthermore, there was an important increase of the access tolls payable by consumers[404].

622. However, these measures failed to prevent the continuing growth of the tariff deficit and the consequent aggravation of the risk of financial unsustainability of the SEE.

(2.8) The request to reform by the Sector

[399] *The reforms of the Government of Spain: Determination in overcoming the crisis*, State Secretariat of Communication of the Ministry of the Presidency, September 2012. Chapter III, Page 18. R-0174.
[400] Reference from the Council of Ministers of 27 September 2012, www.lamoncloa.gob.es.R-0197.
[401] Spanish Strategy of Economic Policy: Balance and structural reforms for the next six months, Government of Spain, 27 September 2012. Section C.8, page 70. R-0122.
[402] Royal Decree-Law 13/2012, of 30 March, which transposes directives in matters of the domestic electricity and gas markets and in issues of electronic communications, and through which measures are introduced to correct the deviations through imbalances between the costs and revenue of the electricity and gas sectors. R-0091.
[403] Royal Decree-Law 20/2012, of 13 July, on measures to guarantee budgetary stability and promotion of competitiveness. R-0092.
[404] Order IET/843/2012, of 25 April, which establishes the access tolls from 1 April 2012 and certain tariffs and premiums of the special regime installations. R-0113.

623. The reform in the premium remunerated system was not only duly announced as we have stated, but was also considered as an urgent necessity by the sector. In this regard, in March 2010 the APPA Association stated:

> *"The long promised and long-awaited Renewable Energies Act will be delayed for many further months."*[405] *(Emphasis added)*

624. In line with the foregoing APPA it emphasises, in March 2010, the need for a comprehensive reform of the remuneration regime of renewable energies, by stating that:

> "*The renewable energies sector continues to wait for the promised Renewable Energies Act and fears that the publication thereof will be postponed beyond this legislature due to being subordinate to development of the Sustainable Economy Act"*[406] *(Emphasis added).*

625. With the focus on that necessary Renewable Energies Act, the APP alludes to the draft Bill to which we have made reference and which was submitted together with Greenpeace. In this regard, APPA summarises the fundamental parts of that proposed regulation in the following sentence:

> *"It is based on the best legislative practices of various countries and on an economically and environmentally sustainable energy model"*[407].

626. In line with the foregoing, in July 2012 it once again pushes the need for a comprehensive and sweeping review of the energy system due to the profound economic crisis suffered by Spain. More specifically:

> *"The Association of Renewable Energy Producers considers that we need a comprehensive and sweeping review of the energy system, particularly in the current context of an economic crisis and in the scenario of rising prices of hydrocarbons"*[408].

(3) Measures challenged by the Claimants in this Arbitration

627. The Claimants challenge certain specific measures, a more thorough analysis of which shall be carried out on answering their statements concerning the alleged infringement of the ECT. However, they are summarily described hereunder:

i. Tax on the value of the production of electrical energy (TVPEE).
ii. The use of remuneration, tariffs and premiums from activities of the electricity sector pegged to the Consumer Price Index at constant taxes excluding unprocessed foods or energy products.

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[405] "The investment in renewables is very profitable for Spain", APPA Info No. 30 of March 2010. Editorial. R-0189.
[406] The investment in renewables is very profitable for Spain", APPA Info No. 30 of March 2010. Pages 14 and 15. R-0189
[407] The investment in renewables is very profitable for Spain", APPA Info No. 30 of March 2010. Pages 14 and 15. R-0189.
[408] "Renewables: Moving forward in the world, on the back foot in Spain". APPA info 33, July 2012, pages 14 to 18. R-0221.

iii. Reduction to 0 euros of the premium in the pool plus premium remuneration option.
iv. RDL 9/2013, Act 24/2013 and its implementing norms.

628. In accordance with the aforementioned announcement and using the terminology of the CNE, the first three correspond to measures adopted in the short term and the fourth to medium-term measures. To make things clear, we shall start by analysing the first three in order to conclude with the fourth which, because of its importance, requires a separate chapter, as it represents the current remunerative regime of renewable energies. Under all circumstances, we need to make the following reservations:

- The possible economic repercussions that the measures referred to in points (i), (ii) and (iii) could have on the installations have been absorbed by the measures referred to in point (iv). In other words, in the final reform adopted we have taken into consideration the cost of the tax on producing electricity and the remaining measures whereby the economic impact of the measures has been neutral.
- The measures referred to guarantee the fair return of the installations within a sustainable SEE.

(3.1) Tax on the value of the production of electrical energy (TVPEE)

629. This measure was introduced through Act 15/2012[409], an Act to which we need to make a brief reference before specifically referring to the TVPEE.

630. Act 15/2012 is a tax regulation that came into force on 1 January 2013.[410]

631. Act 15/2012 creates three new taxes: i) the TVPEE, ii) The tax on production of spent nuclear fuel and radioactive waste from the generation of nuclear electric energy, and iii) The tax on storage of spent nuclear fuel and radioactive waste at centralised facilities. Furthermore, Act 15/2012 creates a levy on the use of continental waters for the production of electrical energy. Moreover, Act 15/2012 amends Act 38/1992, of 28 December, on Excise Duties[411] in order to, among other issues, introduce changes into the Hydrocarbons Tax and the Coal Excise Duty. More specifically, the tax rates established for natural gas and coal are modified and the exemptions set out for energy products used in the production of electricity and in the cogeneration of electricity and useful heat are removed.

632. By the same token, Act 15/2012 sets out that the cost of the electricity system shall be financed both with the revenue from the access tolls and other regulated prices, as well as the corresponding entries from the General State Budgets.

633. In addition to collecting the aforementioned taxes for an approximate annual amount of 2.7 billion euros, an equivalent amount has been included in the General State Budgets for the purpose of financing in the electricity system the costs arising from development of renewable energies.

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[409] Act 15/2012, of 27 December, regarding fiscal measures for energy sustainability R-0003.
[410] Act 15/2012, of 27 December, regarding fiscal measures for energy sustainability Final Provision Five. *"This Act shall come into force on 1 January 2013."* R-0003.
[411] Act 38/1992, of 28 December, on Exercise Duty, the consolidated version at 28 November 2014. R-0068.

634. In this regard, pursuant to Act 15/2012[412], complemented by Act 17/2012, of 27 December, on General State Budgets for 2013[413], the State, in the General Budget Acts of 2013, 2014, 2015 and 2016, has targeted one part of the amount equivalent to the collection of taxes included in Act 15/2012 at funding the cost of the electricity system with regard to the development of renewable energies.

635. In addition, Act 15/2012 sets out that the amounts obtained through the auctions of CO2 emission rights also be targeted, with a maximum limit, at development of renewable energies, and paying this amount of the electricity system. In 2013 and 2014 these amounts exceeded 300 million euros.

636. With regard to the TVPEE created through Act 15/2012, as already set out in the section on Preliminary Objections[414], this tax encumbers the activities of production and feed-in of energy into the Spanish electricity system.

637. The TVPEE is applied to the production of all installations that generate electricity. In other words, the new tax is a measure of general application that affects both conventional production facilities as well as installations that produce using renewable energies with and without recognised economic regime.

638. The tax base of the TVPEE consists of the total amount that the taxpayer is to receive for the production and incorporation into the electricity system of electrical energy, measured in power plant busbars, at each installation, in the taxable period. The applicable tax rate is 7%.

639. The impact of the TVPEE on the producers of renewable energies such as the ones that concern us has been neutralised given that the TVPEE is one of the costs paid to these producers through the specific remuneration that these receive, as set out in this statement on analysing the current remunerative regime paid to renewable energy producers. In other words, the specific remuneration received by renewable energy producers enables them, in addition to obtaining a fair return, to recover certain costs which, unlike conventional technologies, cannot be recovered in the market. These costs include the TVPEE.[415]

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[412] Act 15/2012. Additional provision two: *"Additional provision two. Costs of the electricity system.In the General State Budget Acts of each year, an amount equivalent to the sum of the following shall be targeted at funding the cost of the electricity system as per article 16 of Act 54/1997, of 27 November, on the Electricity Sector:a) The estimate of the annual amount collected by the State as a consequence of taxes and levies included in this Act. b) The estimated revenue through the auction of greenhouse gas emission rights, up to a maximum of 500 million euros"*. R-0003.

[413] Act 17/2012, of 27 December, on General State Budgets for 2013. Fifth additional provision: *"Five. Contributions to Financing of the Electricity Sector 1. In the General State Budget Acts of each year, an amount equivalent to the sum of the following shall be targeted at funding the cost of the electricity system as per the Electricity Sector Act, with regard to the development of renewable energies:a) The estimated annual amount collected as a consequence of taxes included in the fiscal measures act for energy sustainability [Act 15/2012].b) 90% of the estimated revenue through the auction of greenhouse gas emission rights, up to a maximum of 450 million euros.2. 10% of the estimated revenue through the auction of greenhouse gas emission rights, up to a maximum of 50 million euros, is targeted at the policy on combating climate change"*. R-0024.

[414] Section III.B of this statement.

[415] Order IET/1045/2014, of 16 June, approving the remuneration parameters of standard facilities for certain electricity production facilities using renewable energy sources, cogeneration and waste, Preamble

640. Furthermore, as set out, pursuant to Additional provision two of Act 15/2012, complemented through Additional provision five of Act 17/2012, of 27 December, an amount equivalent to the estimate of the annual amount collected as a consequence of the TVPEE -and of the other tax included in Act 15/2012- is targeted in the General State Budgets at financing the cost of the electricity system with regard to the development of renewable energies.

(3.2) The updating of remuneration, tariffs and premiums from activities of the electricity sector pegged to the Consumer Price Index at constant taxes excluding unprocessed foods or energy products.

641. This measure was introduced through Royal Decree-Act 2/2013, of 1 February, on urgent measures in the electricity sector and in the financial sector (hereinafter "**RD-Law 2/2013**")[416] The Judgement from the Constitutional Court of the Kingdom of Spain 28/2015, of 19 February 2015, declares the constitutionality of this Royal Decree Act.[417] The Supreme Court has backed the legality of this measure, because these indexes, as specified by the Spanish Supreme Court *"have no reason to be the same for the different activities or to remain unalterable over time."*[418]

642. Royal Decree-Act 2/2013 agrees to replace the Consumer Price Index that governed the updating of remuneration, tariffs and premiums of activities in the electricity sector, including the production of renewable energy, with the Consumer Price Index at constant taxes without unprocessed foods or energy products (Hereinafter "**CPI-CT**"). Said change shall come into effect from 1 January 2013

643. This measure, justified both from a scientific standpoint as well as a legal one, has led to some effects that are not detrimental to the Claimants, as it has been beneficial for the

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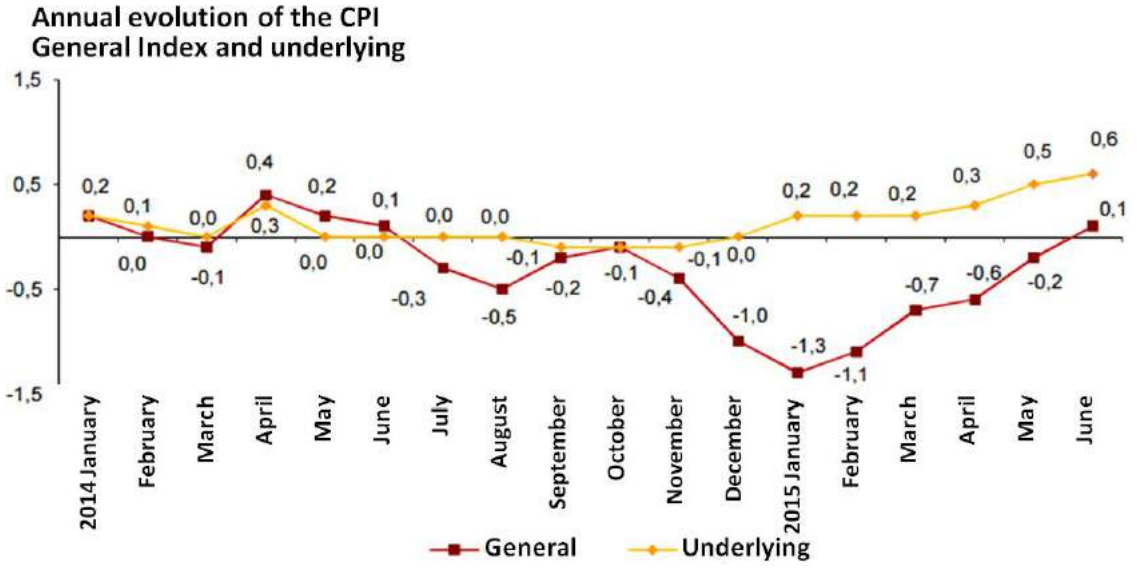
III: *"Furthermore the variable operating costs based on production of the standard installation include, for merely illustrative purposes, the following: insurance costs, administrative expenses and other overheads, cost of representation in the market, cost of the toll to access the transport and distribution grids that need to be paid by producers of electricity, operation and maintenance (both preventive and corrective), tax on the value of the production of electrical energy as per Act 15/2012, of 27 December, on fiscal measures for energy sustainability, as well as the remaining taxes regulated in said Act.[…]"*. R-0115.

[416] Royal Decree-Act 2/2013, of 1 February, on urgent measures in the electricity sector and in the financial sector. R-0093.

[417] Judgement of the Constitutional Court 28/2015, of 19 February 2015, delivered in constitutional challenge 6412-2013. Finding of Law 3: *"The situation to be addressed by the measures contested here was the deviation of the costs of the electricity system as a consequence of different factors (excess cost of the special regime premiums, inclusion of the non-mainland costs of electricity systems and the increase of the deficit through a fall in the demand for electricity) which are explained in the preamble or in the parliamentary debate. Factors which jointly led to a higher tariff deficit than initially forecast by the Government. Thus, we can consider that, [...], the Government has complied with the requirements to explain and justify the existence of an extraordinary and urgent situation, […] it is clear that the measures proposed, insofar as they seek an adjustment of costs in the electricity sector, feature the necessary connection between the extraordinary and urgent situation and the measures adopted to address this.*" R-0151.

[418] Judgement of the Supreme Court of 26 March 2015. Finding of Law Five. R-0153.

installations. The CPI at constant taxes has evolved above the CPI in certain periods of 2013, 2014 and 2015. This evolution can be seen in the following table[419]:



644. The methodological change this measure represents solely involves modifying the general CPI for a type of underlying CPI at constant taxes. In this regard, the use of underlying consumer price indexes at constant taxes is broadly provided for in world economics doctrine[420] and it avoid distortions of the general index caused by the volatility of some of its elements or to modifications of indirect taxes.[421]

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[419] Information from the Spanish National Institute of Statistics, available on the website: http://www.ine.es/daco/daco42/daco421/ipc0615.pdf.
This information does not include the tax effects, which can be depreciated quantitatively during the period considered.

[420] By way of an example, these types of indexes are considered in the method of analysing price indexes in the *Consumer price index manual. Theory and practice*, prepared jointly by the International Labour Organisation, the International Monetary Fund, the Organisation of Economic Cooperation and Development, the Statistical Office of the European Union, the United Nations and the World Bank. 2006. R-0183.
In the same way, the main report on the economic situation worldwide, the *World Economic Outlook* of the International Monetary Fund, uses the underlying price index analysis in its Methodology. *World Economic Outlook*, International Monetary Fund, April 2014. R-0201.
The same method of analysing underlying inflation is used by the US Federal Reserve *What is inflation and how does the Federal Reserve evaluate changes in the rate of inflation?* Board of Governors of the Federal Reserve System, available on the website www.federalreserve.gov, 10 April 2015 (date of last access).

[421] In terms of the report on the issue from the Organisation of Economic Cooperation and Development (hereinafter "OECD") *Measuring and assessing underlying inflation*, OECD Economic Outlook, Preliminary Edition, 2005, page 187): "*Headline inflation rates can be volatile, often because of substantial movements in commodity or food prices. Such volatility in a key price index can make it difficult for policymakers to accurately judge the underlying state of, and prospects for, inflation. Therefore, core inflation rates -- excluding or downplaying the more volatile price changes so as to reveal the underlying, more persistent component -- can be helpful."* (emphasis added). R-0127.
More precisely, one of the most common methods to calculate the underlying price index is the one used by Royal Decree-Act 2/2013, viz., the exclusion in the general CPI of unprocessed foods and energy

645. In other words, the methodological change of the updating instrumented through Royal Decree-Act 2/2013 responds, in general, to usual standards of calculating consumer price indexes in the international economy and the aim is to prevent distortions in the consumer price index that are unconnected to the basics of the economy. This is explained in detail in the analysis of the ECT protection standards. This is also a change backed by the European Union rules and criteria[422].

646. It is, furthermore, a change that was announced through the proposals set out in the different reports from the National Energy Commission (CNE)[423] and from the National Markets and Competition Commission[424].

647. The expectation of this modification by a prudent and diligent economic operator, given that it is a measure adopted within an economic context that required the take-up of urgent decisions, has also been recognised by the Supreme Court on repeated occasions, on stating that:

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products, as well as indirect taxes or changes to these. As set out in the aforementioned report: "*A standard core measure excludes food and energy from the overall CPI. This is often the one that receives the most public attention. There are, however, other variants that are readily available or in use: for example, there are versions for the euro area and the United Kingdom that exclude energy and unprocessed food; in Japan, fresh food is removed; and in Canada, the eight most volatile components, as well as indirect taxes, are taken out of the index. […] The economic argument for excluding these components from the calculation of headline inflation rates is that they are the ones most likely to be subject to disruptions in supply, as opposed to reflecting aggregate demand. In this case, and provided that the stance of monetary policy has not changed, the influence of such large, one-off price changes (either positive or negative) will fade over time. Hence, excluding them provides a better picture of existing underlying inflation pressures.*"(emphasis added). *Measuring and assessing underlying inflation*, OECD Economic Outlook, Preliminary Edition, 2005, pages 188 and 189. R-0127.

[422] With regard to this reform, the proposal from the Commission already dated back to 2009 and this is the reason why the National Institute of Statistics, the Spanish authority responsible for publishing statistics, already began to publish the CPI-CT in September of that year.

Once the reform had been formally approved on 26 September 2012, the INE (Spanish National Institute of Statistics) proceeded to incorporate this into the sphere of the CPI and published it on 11 October 2012 in a press release on its website, clarifying, among other points, the following: "*This indicator is for the purpose of discounting from the variation of prices the part that could be due to modifications in the taxes on consumption. To this end, we measure the evolution of the CPI under the assumption that these taxes have not changed from the time of reference. […] The CPI-CT will normally only vary from the CPI when there are changes in the taxes considered in its calculation: the value-added tax (VAT), the taxes on fuels, taxes on tobacco, tax on vehicle registration, and taxes on insurance premiums.*" Regulation (EC) 2494/95 from the Council, of 23 October 1995, with regard to HICPs (RL-0018, page 1), developed with regard to the subindexes through Regulation (EC) 2214/96 from the Commission, of 20 November 1996, on HICPs: transmission and dissemination of the HICP subindexes (RL-0022, page 8). The last of these is the one that was modified through the proposal approved on 26 September 2012, giving rise to Regulation (EU) 119/2013 from the Commission, of 11 February 2013, modifying Regulation (EE) No. 2214/96, with regard to the establishment of HICP-CT. (RL-0023, page 1).

[423] Report on the Spanish energy sector, Part I. Measures to guarantee the economic-financial sustainability of the electricity system, National Energy Commission, 7 March 2012, page 16. "In line with what has been observed by the Council of European Energy Regulators (CEER)", and it pointed out that *"we need to review the prevailing updating mechanisms with fixed X and Y efficiency factors and associate these to improvements to objective efficiency. Temporarily, and until these parameters have been studied in accordance with the efficiency analysis, we propose a downward review of the updates, taking into consideration the current economic setting."* R-0131.

[424] Report from the National Commission On Competition 103/13 on the Draft Electric Sector Act, page 11. R-0132.

> *"A "prudent and diligent economic operator" could not, therefore, feel surprised by the adoption, in 2013, of a measure of this kind, all the less as it was neither unpredictable - on the contrary it had been suggested by the energy regulator, nor, in the words of the Court of Justice previously cited, "could economic operators legitimately expect that an existing situation would continue when it can be modified at the discretion of national authorities".*
>
> *Against a backdrop of widespread crisis, as in the Spain of late 2012 and early 2013, similar changes to adjustment indices were made in this and other sectors of economic life."*[425]

648. More precisely, the Spanish Supreme Court has given a ruling in this regard by specifying that the change instrumented through Royal Decree-Act 2/2013 has a limited scope, as the differences between the two updating methodologies are not especially significant.

(3.3) Reduction to 0 euros of the premium in the pool plus premium remuneration option.

649. The second measure introduced through Royal Decree-Act 2/2013, of 1 February, involved reducing the amount of the premium to a value of €0 in the pool plus premium option set out in Royal Decree 661/2007[426], in order to guarantee the principle of a fair return[427].

650. This measure was motivated by the need to redress the inconsistency that existed in the determination of the premiums which led to over remuneration. This was expressly warned about with regard to the thermo-electrical sector by the CNE in its Report on the Spanish Energy Sector of 7 March 2012[428]. The CNE declared that redressing this measure did not

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[425] Judgement from Chamber Three of the Supreme Court of 26 March 2015, RCA 133/2013, reference CENDOJ: 28079130032015100087. Finding of Law Nine (R-0153) and Judgement from Chamber Three of the Supreme Court, of 16 March 2015, RCA 118/2013, reference CENDOJ: 28079130032015100072 (R-0152).

[426] Royal Decree-Act 2/2013, of 1 February, on urgent measures in the electricity sector and in the financial sector. Art. 2 section one. R-0093.

[427] *"Elsewhere, taking into consideration the volatility of the production market price, the option of remunerating energy produced under the special regime with a premium that supplements this price makes it difficult to comply with the twin aim of guaranteeing a fair return for these installations and simultaneously avoiding excess remuneration of the same, which would be payable by the other users of electricity. Consequently, the economic regime with a premium needs to be backed solely with the regulated tariff option, without prejudice to the owners of installations being able to feed in their energy freely in the production market without receiving any premium."* RD-Law 2/2013. R-0093.

[428] "*The prevailing regulation is inconsistent with regard to the relative values of the premium and the tariff of solar energy technology (the current tariff has a value of €298.96/MWh while the premium has a value of €281.89/MWh, which represents a theoretical market price of €17.1/MWh). As the economic-financial study of the installations is carried out with the regulated tariff, with an average market price of €50/MWh, the premium should have a value of €249/MWh, which is 12% lower than the current one. In an initial approximation it would be necessary to reduce the premium corresponding to the solar energy plants already preregistered by 12%. This would enable us to achieve a saving in the access tariff of some 47 million euros in 2012, 90 million in 2013 and 200 million from 2014 onwards. Under all circumstances, it must be remembered that this measure would be justified by redressing an inconsistency in the determination of premiums. The correction of the premium maintains the principle of obtaining a fair return as per the Act, given that the economic feasibility studies of new installations are carried out*

prevent the plants from obtaining a fair return, to the extent that the economic feasibility studies of these plants are conducted with the regulated tariff.

651. On this point we should remember that RD 661/2007 removed the pool plus premium option for photovoltaic installations. Consequently, we cannot consider that we are faced with an arbitrary, unreasonable or unforeseeable measure. In the same way as this was not the case for the photovoltaic technology in 2007.

652. However, we should point out that the effect of this measure has been restricted from a time point of view. The effects of this measure disappeared with the entry into force of the new subsidies model introduced through the global reform of the SEE.

G. The current model of remuneration for certain installations that produce energy with renewable sources.

(1.1) Objectives of the current system.

653. The analysis of the electricity system reveals that the remuneration paid, through the electronic invoice, ought to be reviewed for the purpose of complying both with EC regulations as well as the domestic legal system, to ensure the guarantee of a fair return.

654. The resulting model of this review is set out in Act 24/2013, which has been developed through Royal Decree 413/2014, of 6 June 2014, regulating the production of electricity energy using renewable sources, cogeneration and waste (hereinafter, "**Royal Decree 413/2014**")[429] and Order IET/1045/2014[430], the main characteristics of which are shown hereunder.

(1.2) Remuneration regime.

(a) Determination of the fair return.

655. We have proceeded to set the fair return in a specific way and to establish the criteria for reviewing this every six years, pursuant to the regulatory mechanisms set out hereunder[431].

656. In line with the provisions set out in Act 54/1997 and case law on the matter, which is known and accepted, the remuneration system is based on project profitability, which will revolve around, before taxes, the average return in the secondary market of Government-10-year Bonds, applying the appropriate spread. This spread, according to RD-Law 9/2013, is

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with the regulated tariff." Report on the Spanish energy sector, Part I. Measures to guarantee the economic-financial sustainability of the electricity system, Report from the National Energy Commission on the electricity sector of 7 March 2012. Page 23. R-0131.

[429] Royal Decree 413/2014. R-0110.

[430] Order IET/1045/2014. R-0115.

[431] As set out in the Preamble of Act 24/2013, of 26 December, the investments in certain installations that use these technologies: *"shall continue to be protected and developed in Spain through this new regulatory framework, which enshrines the principle of a fair return and establishes the criterion of review of the remunerative parameters every six years in order to comply with this principle. This attempts to consolidate the ongoing adaptation that the regulation has experienced to maintain this fair return through a predictable system and subject to a specific timeline."* R-0076.

300 base points[432], a figure that fully matches the proposal given by the APPA Association in 2009.

657. The specific figure for facilities already operating is around 7.398 percent profitability for the whole of project for a standard facility.[433]

658. This figure is not a cap on profitability, as it is simply a forecast return for that installation, whose investment and operating costs match the parameters of the standard installation applicable.

659. In this regard, if the investor is efficient and manages to reduce their investment cost below the parameters established for the standard installation applicable, they will obtain a higher return on the investment. Similarly, if the installation manages to reduce its operation and maintenance costs below the parameter established for the standard installation, there will be greater remuneration through operation. Consequently, if the installation manages to improve the investment and operation parameters, it will obtain a return in excess of 7.398%.

660. In line with the foregoing, if we analyse the profitability of plants subject to this arbitration in the actual scenario we can see how all wind farms improve the objective return of 7.398% forecast for standard installations. More specifically, the wind farms of the Claimants in the current scenario achieve an average return of 8.11% [434].

661. On the other hand, this return has not been set taking into consideration the financing of projects, in other words it is not a system that caters to the method or amount of financing of a sector company or companies. As a result, if a company obtains external financing, irrespective of the amount requested, they shall assume the costs and benefits of the borrowing, apart from the remunerative model. However, it should be remembered that this has always been the methodology used. Proof of this can be seen in the 2000-2010 PPRE[435], 2005-2010 REP[436] and the Environmental Impact Report of Royal Decree 436/2004[437].

662. Furthermore, these new measures do not impose any restriction on the production by the installations, as these installations can continue to produce and to sell all of the electricity they produce in the market (with feed-in priority and once their operating costs have been covered).

(b) Recovery of the investment costs.

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[432] Royal Decree-Act 9/2013 of 12 July 2013, establishing urgent measures to ensure the financial stability of the electricity system. Additional provision one. R-0094.

[433] As regards the fair return of installations, in calculating the remunerative parameters we have taken into consideration firstly, for installations with the right to receive a premium on the entry into force of Royal Decree-Act 9/2013, of 12 July, the average return in the secondary market over the 10 years prior to the entry into force of the foregoing royal decree-act, in other words, the period from 1 July 2003 to 30 June 2013, of Government 10-Year Bonds, as set out in final provision three of Act 24/2013, of 26 December, and additional provision two of Royal Decree 413/2014, of 6 June, for installations with the right to receive a premium. Royal Decree-Act 9/2013. Article 1 (two) Additional provision one. R-0094.

[434] Econ One Research Report, 15 June 2016, section IV, paragraph 132.

[435] 2000-2010 Plan for the Promotion of Renewable Energies. R-0118.

[436] 2005-2010 Renewable Energies Plan. R-0119

[437] Environmental Impact Analysis Report of 436/2004. R-0100

663. As referred to previously, the recovery of the investment costs in general represents one of the essential components of the new model. However, let us not forget that the mandate whereby the remunerative regime needed to allow the recovery of the investment costs is provided for under Spanish law, for this specific remuneration regime, from the original wording of article 30 of Act 54/1997[438].

664. The new regulation maintains the principle whereby the remunerative regime must guarantee the return of the investment costs and simply provides it with greater development and specification[439] [440].

665. In this way, Act 24/2013 emphatically affirms that the investment value assigned to the installation cannot be subject to review, in order to maintain the security and non-changeability of that value[441].

666. Based on these principles, the system or outline of remuneration is structured around, as is standard practice in the Spanish regulatory framework, the definition of standard installations; the calculation of the investment and operation costs of each one of these types and the setting of the remuneration to be received by each of them to guarantee the fair return.

667. To determine the standard value of the initial investment of each installation, we have taken into consideration main new equipment, as well as the remaining electromechanical systems and equipment, regulation and control equipment, measuring equipment and connection lines, including transport, installation and commissioning, together with the associated engineering and works management, among other items.

668. This determination of the investment value has been conducted in accordance with an in-depth and specific study of actual data obtained from regulatory reports, scientific documentation and the knowledge of the regulatory authorities with their extensive experience in this issue.[442]. The specific determination of the standard values is explained in detail in the Witness Statement of Juan Ramón Ayuso[443].

669. This determination of the value is fully in accordance with the proposal given by the APPA Association in 2009, which requested that the investment costs be estimated in

[438] Article 30.4 last paragraph of Act 54/1997 original wording: "In order to determine the premiums, the voltage level of energy fed in to the grid shall be taken into consideration, along with the effective contribution to environmental improvement, the saving of primary energy and energy efficiency, as well as the investment costs incurred, for the purpose of achieving fair rates of return with reference to the cost of money in the money market. R-0079.
[439] Articles 14, 21, 26, 27, 33, 53 and 61 et seq of Act 24/2013. R-0076.
[440] The new regulation is also consistent with the declarations of the regulating authority, the National Energy Commission (CNE), in its report of 7 March 2012. R-0131.
[441] Article 14.4 2 of Act 24/2013: "In no case, once the regulatory useful life or the standard value of the initial investment of an installation has been recognised may said values be reviewed". R-0076.
[442] This means that the remunerative regime is based on standard parameters in accordance with the different standard installations that were established following a thorough analysis in Order IET/1045/2014. R-0115.
[443] Witness statement of Juan Ramón Ayuso of 14 June 2016. Section 6. RW-0001.

accordance with the different *types* of installations, differentiated by *technology and size*, in order to reflect the standard values that these investments actually achieve[444].

670. Under no circumstances has there been a retroactive determination of the investment costs as claimed by the Claimants. The investment costs taken into consideration by the regulation are those actually made for the construction of the standard installations at the time when the construction work took place.

671. If the statement given by the Claimants were true it would make no sense that the investment costs established in MO IET/1045/2014 for standard installations that use wind technology were, as was the case, higher than the investment costs forecast for standard installations in the different Renewable Energies Plans. It would also not make sense for these to be higher than the figures published by the International Energy Agency[445].

672. This datum is sufficiently revealing to demonstrate that the investment costs of the different standard installations are neither arbitrary nor attempt to artificially reduce the profitability of the installations.

673. However, during the stage of producing the documents we shall request the Claimants to provide the information that will clearly show that their argument is groundless.

674. The investment value set by the Government is for the Project. It therefore does not include speculative values or profits that the first owners of the plants obtained on transferring these to third parties. In other words, the investment has been set over the value of the initial investment, not over the value of second and subsequent transfers, which already include the capital gains and profits obtained by the transferring parties.

675. This is because the remunerative systems cannot cover and include the profits which, through sale or other act in the law that affects the installation, have been obtained by the owners of the installations and the subsequent acquiring parties. As declared in the 2010 NREAP:

> *"By the same token, the effective guardianship by the Administration must guarantee that any gains made in the appropriate evolution of these technologies is passed onto society with regard to the competitiveness in relative costs, minimising speculative risks, caused in the past through excessive returns that not only damage consumers but also the industry itself with regard to the way it is perceived."*[446]

676. Other subsidies that finance or remunerate these transfers would alter the free market rules within the EU, implying the possibility of incurring State Aid that is contrary to community regulations.

(1.3) Items that make up the remuneration to recover the investment.

(a) Price obtained through the sale of energy in the market.

[444] Article 23.5 of the Bill proposed by APPA-Greenpeace in May 2009. R-0187.
[445] Witness Statement of Juan Ramón Ayuso of 14 June 2016. Section 6. RW-0001.
[446] 2010-2020 NREAP. R-0120

677. As with the previous regime, the remunerative regime of renewable energies, cogeneration and waste is based on the necessary participation of these installations in the electricity market. Consequently, the determination of the fair return is based on revenue resulting from participation in the market, coupled with additional remuneration, where necessary, to cover those investment costs that an efficient and well-run company is unable to recover in the market.

678. The system takes into consideration the remuneration that the installations obtain by taking part in the market. However, to reduce the uncertainty on estimating the energy price in the market, which is applied in the calculation of the remunerative parameters and which directly affects the remuneration obtained by the installation for the sale of energy it generates, floor and cap limits for this estimate are defined.

679. To determine the revenue obtained by the installations until the entry into force of Royal Decree-Act 9/2013, of 12 July, the actual average income published by the CNMC was taken for each standard installation.

680. Thus, given that they are technologies that do not recover the investment costs solely with the remuneration obtained from the market, a specific regulated remuneration is set that enables these technologies to compete under equal conditions with the other technologies in the market and to obtain the aforementioned fair return on their investment.

(b) Return on investment (Ri) and Return on operation (Ro).

681. This specific supplementary remuneration is sufficient to achieve the minimum level required to cover the costs which, unlike conventional technologies or other renewables such as hydraulic energy, cannot be recovered in the market. This enables them to obtain an appropriate return with reference to the standard installation applicable in each case.

682. This additional remuneration comprises the Return on investment (Ri) and Return on operation (Ro) items. Ri is the specific remuneration comprising a term per unit of installed power and which covers, where appropriate, the investment costs for each standard installation that cannot be recovered through the sale of energy in the market. Ro is the specific remuneration that covers, where appropriate, the difference between the operating costs and the revenue through participation by said standard installation in the production market.

683. To calculate the return on investment and the return on operation we have considered, for a standard installation, the standard revenue through the sale of energy measured at the market price, the standard operating costs required to carry out the activity and the standard value of the initial investment, all of this with regard to an efficient and well-run company.

684. To calculate the operating cost, we have considered those costs associated to electricity production for each technology, required to carry out the activity in an efficient and well run way.

685. The variable operating costs based on production of the standard installation include, for merely illustrative purposes, the following: insurance costs, administrative expenses and other general operating costs, cost of representation in the market, cost of the toll to access

the transport and distribution grids that need to be paid by producers of electricity, operation and maintenance (both preventive and corrective).

686. Also the costs stemming from payment of the tax on the value of the production of electrical energy as per Act 15/2012, of 27 December, as well as the remaining taxes regulated in this Act such as the tax on hydrocarbons, mainly gas.

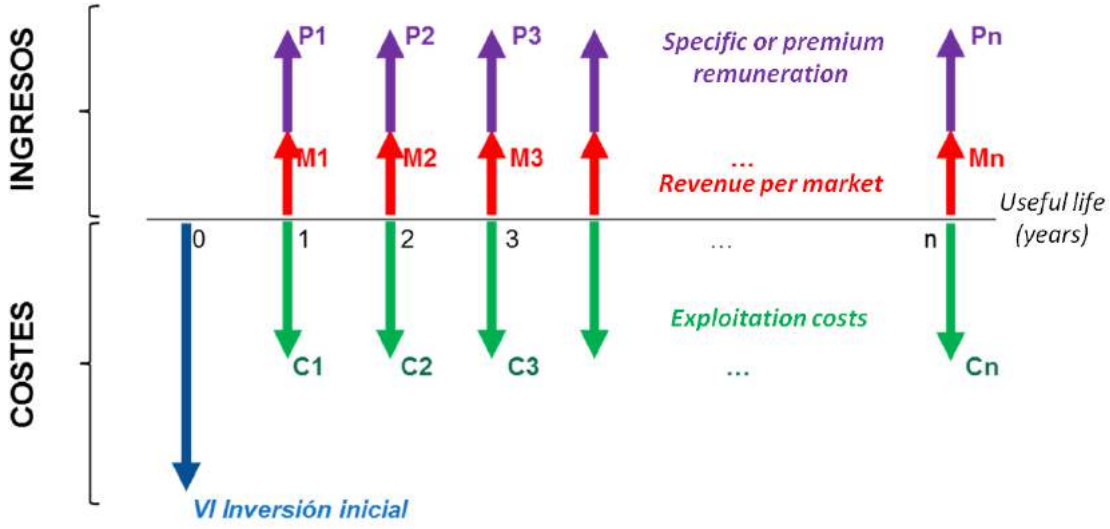
687. Where appropriate, we have also considered ancillary consumption (water, gas, etc.) and the fuel costs associated to operation of the standard installation.

688. In addition, among the fixed operating costs we have considered, *inter alia*, the cost of renting the lands, the expenses associated to security of the facilities and the tax on properties with special features (BICES).

689. Furthermore, the specific costs or investments determined through administrative acts or regulations that do not apply throughout Spanish territory are expressly included, as are those that do not exclusively involve the production of electricity[447].

690. The specific determination of the standard values is explained in detail in the Witness Statement of José Ramón Ayuso[448].

691. The following table explains the flows for the different items[449]:



692. In this way, as we have seen thus far, the owner of an installation has certain investment costs and other operation costs and receives revenue from the electricity system, comprising: (i) the amount that he receives for the sale of energy in the electricity market, and (ii) the additional remuneration granted by the electricity system to cover the difference

[447] Royal Decree-Act 9/2013. Article 1 (Two). (R-0094). Article 13.3 of Royal Decree 413/2014, of 6 June. R-0110.
[448] Witness Statement of Juan Ramón Ayuso of 14 June 2016. Section 6. RW-0001
[449] Source: Page 12 of the Environmental Impact Analysis Report included in the Administrative file relating to the draft order that approves the remunerative parameters for standard plants that are applicable to specific electricity production plants that use renewable energy, cogeneration and waste sources. R-0083.

between the costs and the revenue obtained through the market and which includes the Ri and the Ro.

693. We should point out that in the case of wind farms, the market price (pool), covers the estimated operating costs for standard installations. For this reason, wind farms do not receive the Ro. Consequently, these installations only receive the Ri, which allows them to recover the investment costs and to obtain the fair return guaranteed by Law. The Ri will not be received by those installations which had already recovered their investment costs at the time the reform came into force and which have also obtained the fair return.

(1.4) The period for receiving additional remuneration. Regulatory useful life.

694. The remunerative regime is supplemented with another parameter, the regulatory useful life. The number of years set for each technology is the representative number for each standard installation, based on the design life of the main equipment and assuming that the appropriate preventive and corrective maintenance actions are undertaken.

695. This useful life shall remain unchanged for each standard installation pursuant to the provisions set out under article 14 of Act 24/2013, of 26 December. Consequently, it is expected that once the installations exceed the regulatory useful life they shall no longer receive the return on investment and the return on operation.

696. The end of the regulatory useful life determines the moment when the investor has recovered all of his investment costs and operation costs, having received a sufficient amount from the sale of energy in the market and the Ri and Ro concepts.

697. The setting of the useful life also allows us to perform the annual calculation of the remunerative regime, and this is required to determine the fair return[450].

698. However, this setting of the useful life does not imply that those installations which, on the entry into force of the reform, have already recovered their investment costs and obtained the fair return, are entitled to continue receiving the subsidies. This would be contrary to EU recommendations[451] that clearly establish that, once the level playing field has been achieved there will not be payment of any additional subsidies. It would also go against the essence and purpose of any system of feed-in tariff.

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[450] We should also highlight the opinion of the Council of State with regard to the regulation and more specifically with regard to its remunerative regime, the Report from the Council of State of 6 February 2014: "*In summary, to calculate this specific remuneration, we base ourselves on the figures from the entire regulatory useful life of the installations, therefore including those prior to the entry into force of the current reform. The environmental impact analysis report makes a commendable effort to point out in economic terms that the concept of a "fair return", to be guaranteed to owners of installations, "irrespective, from the financial point of view, of whether the flows of revenue (or costs) take place at the beginning or at the end… it is the legislation of coverage which designs a remunerative model for existing installations based on the consideration of the entire useful life of the project.* (emphasis added) Administrative enquiry relating to draft Royal Decree 413/2014 (document 20.02) R-0124.

[451] Guidelines on State Aid in the issue of protection of the environment and energy approved through EC Communication 2008/C82/01 (R-0064), and substituted for the 2014-2020 period through EC Communication 2014/C 200/01 (R-0065).

699. Furthermore, since 2012 the Supreme Court of the Kingdom of Spain has been clear about the extent of the concept of a fair return with respect to the duration of subsidies:

> *"the principle of a fair return should be applied [...] to the entire life of the facility, but not [...] in the sense that during that entire life said principle might guarantee the generation of profits, but rather in the sense that it is ensured that the investments used in the facility earn a fair return throughout the existence of the same as a whole. This [...] does not mean the permanence of a certain premium during the entire life of the facility, given that it could so happen that said investments have already been amortised and have generated said fair return long before the end of the operational period."*[452].

700. The time limitation for receiving the subsidies does not prevent these installations from remaining owned by the investor and being kept in operation. If they continue to operate, they can sell all of the production and obtain the corresponding market price.

701. Once again, on setting a prudent regulatory useful life with regard to the life of the equipment that makes up the facility and, furthermore, on making a provision for investments in the renewal of this equipment in the remunerative items, a diligent and well-run company can continue to obtain a return on its investment.

702. In other words, the shorter the regulatory life the greater the additional remuneration to be received by the investor, given that the investment value of the installation is paid in fewer years.

703. Consequently, setting the regulatory life is fully consistent with the purpose of the support mechanisms to guarantee the operability of the installation during its useful life and allow a fair return to be obtained. This is without, said mechanisms needing to continue to pay a premium to the installation, once it has received the amounts that enable it to amortise the same. For wind farms, the regulatory useful life is set at 20[453], figures that are higher than those given in the financial statements of the companies that own the installations that are the object of this arbitration[454].

704. In this regard, it is striking that the Financial Statements of Parque Eólico la Carracha S.L. at 31 December 2003 set out the following:

> *"During the year we have completed the installation of the wind farm and so the investments considered as fixed assets in progress have been transferred to Property, Plant and Equipment to be depreciated over 17 years*[455]*".*

[452] Judgement of the Supreme Court of 12 April 2012, app. 40/2011 (R-0144) Also cited, among others, in the Judgement of the Supreme Court of 19 June 2012 (appeal 62/2011). R-0146
[453] Article 5 Order IET/1045/2014. R-0115.
[454] In the Financial Statements of Parque Eólico la Carracha S.L. and Parque Eólico Plana de Jarreta S.L. at 31 December 2003, a useful life of 17 years is established (respectively, pages 15 and 805 of 1599 of exhibit 2 of the Expert Report from KPMG of 3 March 2016).
[455] In the Financial Statements of Parque Eólico la Carracha S.L. at 31 December 2003, a useful life of 17 years is established (page 15 of 1599 of exhibit 2 of the Expert Report from KPMG of 3 March 2016).

705. The financial Statements of Parque Eólico Plana de Jarreta S.L.[456] are similar in this regard. In other words, at the time of construction, the owners of the wind farms set the useful life of these at 17 years, below the 20 years established by the measures that are the object of this arbitration.

(1.5) Criteria for calculating cost. An efficient and well-run company.

706. To calculate the parameters, revenue and costs, these have been based on those corresponding to an "*efficient and well-run company*"[457]. This refers to a company equipped with the means required to carry out its activity, the costs of which are those of an efficient company in this activity and considering both the corresponding revenue as well as a reasonable return for the performance of its functions.

707. The aim of this regulatory parameter is to guarantee that the high costs of an inefficient company are not taken as reference given that, firstly, it is the electricity consumer that must pay these costs and, secondly, the Spanish regulation has always been supported on principles of efficient management, minimum cost possible and a reasonable return.

708. This principle has been set out successively in all acts of the electricity sector that have been referred to in this document, given that the obligation to guarantee that all consumers have access to electricity under conditions of equality and quality, but at the lowest possible cost, has always been taken as the guideline.

709. As a consequence, it is difficult to agree with the idea that the previous system protected business owners that were inefficient in the construction or operation of their plants, generating an excessive and unnecessary cost in the SEE.

710. As regard the arguments of the Claimants, it is clear that given that roughly 31.8%[458] of overall revenue from their RE plants came from direct contributions from Spanish consumers, it is reasonable to require such installations to be efficient and well run. This term means excluding from the parameters those costs that do not correspond with this principle.

(1.6) Standard installations pursuant to standard costs and remuneration. Determination of the remunerative parameters. Order IET/1045/2014.

711. Based on the aforementioned legal framework and pursuant to the investment and operation cost estimates, we have proceeded to set the standard installations. The procedure and content of the standards has been backed by the regulatory authorities[459].

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[456] In the Financial Statements of Parque Eólico Plana de Jarreta S.L. at 31 December 2003, a useful life of 17 years is established (page 805 of 1599 of exhibit 2 of the Expert Report from KPMG of 3 March 2016).

[457] Royal Decree-Act 9/2013. Article 1 (Two). (R-0094), 14.7 and final provision three of Act 24/2013, of 26 December, *on the* Electricity Sector. R-0074.

[458] Witness Statement of Juan Ramón Ayuso of 14 June 2016. paragraph 139. RW-0001.

[459] Administrative enquiry relating to the Draft Royal Decree 413/2014; Report of the State Council, 6 February 2014: *"For these installations, the standard value of the initial investment cannot be determined through a competitive procedure, and will therefore need to be set in the ministerial order of remunerative parameters of standard installations, which shall be classified based on the technology,*

712. The classification criterion used responds to the renewable resource employed in the generation of electricity, for example wind, solar or biomass. In accordance with that classification, we have compiled standards pursuant to the technology used, the range of power, fuel type and year in which definitive exploitation was authorised, among others. Consequently, the standards have been compiled taking into consideration the actual average costs incurred by the plant owners.

713. Order IET/1045/2014[460] contains the list of all standards, detailing the costs of investment, operation and exploitation, revenue from the sale of energy, consumption of ancillary services, as well as the equivalent hours of performance.

714. This sets the remunerative parameters of the standard installations pursuant to what has already been explained and in accordance with the categories, groups and subgroups, establishing for each of the latter the different standard installations and their corresponding codes, for the purpose of determining the applicable remuneration regime.

715. The Order, of 1761 pages, considers 1967 different standard installations. As explained in the Witness Statement of Juan Ramón Ayuso[461], each standard installation has a set of remunerative parameters associated to it that form the specific remunerative regime and allow this to be applied to the installations associated to said standard installation. Chief among these remunerative parameters are the return on investment (Ri) and the return on operation (Ro), the calculation of which in turn considers a series of elements, including:

a) Standard value of the initial investment of the standard installation.
b) Electricity production.
c) Exploitation costs. For example: renting of lands, overheads and management expenses, insurance, Tax on Properties with Special Features (BICEs), wind energy royalty, O&M expenses, costs of representation and deviations, production toll, generation levy.
d) Revenue received by the standard installation.
e) Regulatory useful life.
f) Minimum number of equivalent hours of performance and operational threshold.

716. The definition of such a high volume of standard installations and the calculation of a series of parameters for each of them represented a technical task of much greater magnitude than initially envisaged. A task that was undertaken with documentation comprising around 150,000 sheets and which involved transposing to the new regulation a remunerative framework with a level of detail extraordinarily greater than that of previous regulations. During the processing of the royal decree and the ministerial order, citizens and other interested parties submitted a great number of allegations[462].

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power, years of service, electricity system, as well as any other segmentation deemed appropriate. In this regard, based on the regulatory impact analysis report, we are carrying out "an in-depth analysis with a level of detail far greater than that hitherto carried out, to properly recalculate all remuneration of approximately 63,000 installations of this group, classified into approximately 900 standard installations." R-0124.

[460] Order IET/1045/2014. R-0115.

[461] Witness Statement by Juan Ramón Ayuso, 14 June 2016. Section 5.RW-0001.

[462] We attach the table of contents of the RD 413-2014 6 file of June (R-0085) and of ORDER IET-1045-2014, which show the number of allegations submitted. R-0086.

717. In this case, we should highlight the fact that from 2012 onwards both the AEE and Protermosolar and APPA submitted allegations on the draft RD[463] and MO[464].

718. Under all circumstances, regarding the transparency of the procedure, we should point out that the new remunerative model is similar to the one proposed by the RE Sector in 2009. There is evident willingness on the part of the Regulator to address and to provide a solution to the tariff deficit in a way that closely matches the petitions of the RE sector in 2009. What is surprising is that the Claimants talk about "obscurity" in the RE Sector, when the associations and their associates were aware of the draft regulations shortly after Act 24/2013 came into force.

(1.7) Regulatory periods. Non-changeability of the investment value.

719. Another of the essential elements of the legal and economic regime that applies to the Claimants' installations are the different regulatory periods provided for. These represent flexible regulatory tools, in order to adapt the remunerations to cover costs and to provide a reasonable return[465]. The setting of these regulatory periods, as analysed hereunder, provides the system with greater stability and predictability.

720. The need for both stability and predictability is provided for in the economic standards and criteria, setting out the requirement for remunerative regimes[466] to adapt in order to comply with their objectives as well as the legal system. This responds to a regulated technique that is accepted in a great many countries and provides for predictability of modifications and adaptations in order to comply with the purpose of the economic regimes. Consequently, it permits the full recovery of costs and a reasonable return on investments.

721. In effect, the regulatory periods represent an appropriate mechanism to prevent insufficient remuneration through changes to prices and other circumstances that have an influence on costs. However, in accordance with this purpose, neither the value of the investment nor the regulatory useful life can be amended in any of the regulatory periods.

722. In other words, under no circumstances -once the regulatory useful life or the standard value of the initial investment of an installation has been recognised- can these values be

[463] The Spanish Wind Energy Association presented allegations in response to the proposed draft of RD 413/2014 (R-0232) on 1 August 2013 (R-0232) and 11 December 2013 (R-0233). Protermosolar, for its part, submitted allegations on the same draft of RD on 30 July 2013 (R-0236) and 11 December 2013 (R-0235). APPA, also presented comments (R-0241). Likewise, the three producer associations presented allegations during the processing of MO ITE/1045/2014, provided as R-0204, R-0205, R-0237, R-0238, R-0242 and R-0243.

[464] The association UNEF also presented allegations on two occasions on the draft of Ministerial Order of 25 February 2014 (R-0203) and 26 May, 2014 (R-0206).

[465] The 2010 NREAP revealed the need for the remuneration model for renewable energy production to be based on flexible formulae that enable this to be adapted to different concurrent circumstances. By the same token, when it comes to configuring the support regime for renewable energies for Member States, the European Commission has demanded flexibility of the remunerative regime. The new regulation is limited to verifying this dynamism. See. The section on Spain's National Renewable Energy Action Plan (NREAP) R-0120.

[466] Act 24/2013. Article 14(4). R-0076.

reviewed. This means that the investor will have the amounts of the investment fixed in their standard, and will be unable to change this in the future[467].

723. This mechanism represents a relevant guarantee for the protection of investments already made or which may be made in the future, by protecting new economic regimes and which is not considered for the remaining activities of the electricity sector.

724. Stability is related to the permanence of the regulatory periods. Based on the new regime, each regulatory period is enforceable for six years[468]. Any changes shall take into consideration the cyclical situation of the economy, the demand for electricity and the fair return for the activity[469].

725. In the review that takes place with each regulatory period, all of the remunerative parameters may be amended, including the value on which the reasonable return shall be based for the rest of the regulatory life of standard installations.[470]

726. Each regulatory period has an enforceability of three years[471]. The income estimates through the sale of energy produced shall be reviewed in the regulatory period, measured at market price of production, based on the evolution of market prices and the forecasts of hours of performance with regard to the estimates made for the previous three-year period.

727. Every year, the return on operation values will also be reviewed for those technologies whose operating costs depend essentially on the price of fuel[472], in order to adapt to the price of this. The purpose of this is to adapt it in accordance with market variations so that undue amounts are not received, whether too much or too little. Likewise, the remunerative parameters may be reviewed at the end of each regulatory period in accordance with the terms set out therein.

(1.8) Reasonableness of the prevailing Legal regime.

(a) It maintains the priority of feeding-in energy and in access and connection to the grid.

728. The regulation maintains the principles of priority of access and feed-in of electricity generated by installations that use sources of renewable energy and highly efficient cogeneration.

[467] Act 24/ 2013, of 26 December, on the Electricity Sector. Article 14(4). R-0076.
[468] As regards the six-year regulatory periods, it sets out that the first regulatory period is from the date of coming into force of Royal Decree-Law 9/2013, 12 July, and 31 December 2019, Royal Decree 413/2014. Additional provision one. R-0094 and R-0110.
[469] Article 14.4 of Act 24/2013, of 26 December. R-0076.
[470] Royal Decree 413/2014. Article 20(1). R-0110.
[471] Each regulatory period is divided into two regulatory half-periods of three years each, with the first regulatory half-period corresponding to the one that exists between the date of entry into force of Royal Decree-Law 9/2013, of 12 July, and 31 December 2016. Royal Decree 413/2014. R-0110.
[472] Act 24/ 2013, of 26 December, on the Electricity Sector. Article 14(4). R-0076.

729. This regulation even goes beyond the provisions set out in community regulations[473] and represents a novelty as an explicit recognition of this privilege, as this was not contained in the previous regulation.

730. With regard to priority dispatch, article 26 of Act 24/2013 states that[474]:

> *"Electricity from plants that use renewable energy sources and, after these, high-efficiency cogeneration plants, will have priority dispatch on an equal economic playing field in the market, without prejudice to the requirements relating to the maintenance of the reliability and the safety of the system, under such terms and conditions as may be defined in regulations issued by the Government.*
>
> *Without prejudice to the security of supply and the cost-effective development of the system, producers of electricity from renewable sources of energy and high efficiency cogeneration plants shall have priority of access and connection to the grid, under such terms and conditions as may be defined by regulations, on the basis of objective, transparent and non-discriminatory criteria."*[475]

731. From a simple reading of this regulation, it is clear that priority dispatch and access and connection to the grid are rights that are held by producers of energy from renewable sources. This right may only be limited because of reasons relating to the maintenance of the reliability and the safety of the Spanish Electricity System (hereinafter SEE). Furthermore, in contrast to that which was set forth in the previous regime, this priority dispatch even prevails over high-efficiency cogeneration plants.

(b) It maintains the legal guarantees of the investments.

732. The remunerative regime of specific electricity production plants that use renewable energy sources has been regulated in legally binding regulations and as a result said regime may only be modified by an Act of Parliament. The Renewable Energy sector has been calling for this for years[476].

733. The importance of plants that produce electricity from renewable energy sources which receive financial contributions from the SEE has led to their accounting for half of the costs

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[473] Directive 2009/28/EC of the European Parliament and of the Council of 23 April 2009 on the promotion of the use of energy from renewable sources and amending and subsequently repealing Directives 2001/77/EC and 2003/30/EC. Article 16(2) (c): "*Member States shall ensure that when despatching electricity generating installations, transmission system operators shall give priority to generating installations using renewable energy sources in so far as the secure operation of the national electricity system permits and based on transparent and non-discriminatory criteria*." RL-0017.

[474] Act 24/2013, of 26 December, on the Electricity Sector, Article 26 (2). R-0076.

[475] The above wording of the Act has been reiterated in article 6(2) of Royal Decree 413/2014, when it states that: "electricity from plants that use renewable energy sources and, after these, high-efficiency cogeneration plants, will have priority dispatch on an equal economic playing field in the market, without prejudice to the requirements relating to the maintenance of the reliability and the safety of the system, under such terms and conditions as may be defined in regulations issued by the Government" Royal Decree 413/2014. Article 6 (2) R-0110.

[476] Draft Bill presented in 2009 by APPA-Greenpeace R-0187, referred to in the book "Powering the Green Economy". The feed-in tariff handbook. Miguel Mendonça, David Jacobs and Benjamin Socacool. Publishing house. Earthscan, 2010. Page 87. RL-0062.

of the entire system. As a result, a remunerative system has been set up that allows these plants to participate in the SEE's balancing markets.

734. Electricity prices are higher in these markets, allowing such plants to compete with other plants, once they have met the corresponding technical requirements. However, this unification has taken place regardless of the unique considerations that should be established and maintained as far as existing plants are concerned.

735. We find one example in priority dispatch and access and connection to the grid, as analysed above. What has also been regulated is the obligation whereby the assignation of a financial regime such as that enjoyed by the plants of the Claimants should be carried out through a competitive procedure.

736. Such procedures may only take place when there is an obligation to meet energy objectives that derive from European Directives or other regulations inherent in European Union Law or when the introduction thereof implies a reduction of the cost of electricity and of the dependency on overseas energy.

737. This measure is also congruent with the guidelines and policies of the European Union in support of renewable energies and the protection of the environment. However, in order to protect investments that have already been made, it does not affect existing plants such as those of the Claimants.

738. Furthermore, a specific Administrative Register of the Remunerative Regime has been created, as it was necessary for the monitoring and the correct application of the financial regime to plants that produce electricity from renewable energy, cogeneration and waste sources, with a specific remunerative regime[477].

(c) Participation of parties interested in regulatory procedures.

739. All the regulations that are included in the new legal framework have been adapted to the procedure envisaged in Spanish law. All the necessary reports have been gathered together, in order to ensure that the new regulatory text fully complies with Spanish Legal Order. Reports have been requested, even reports that were not compulsory[478], and several public opinion hearing procedures have been arranged in which all interested parties have been able to take part. Furthermore, an important part of the allegations of the citizens and interested parties, who presented allegations, have been accepted.

740. Examining the allegations of the public and sector, the State Council, the Government's supreme consultive body[479], has issued three Rulings or legal opinions. The State Council has endorsed the new remunerative regime, expressly admitting the legitimacy of the regulatory change, given that the previous regulation did not contemplate the right to

[477] Royal Decree-Act 9/2013. Article 1 (Four). R-0094.
[478] For example, by the issuance of Ruling 539/2014 by the State Council to Order IET/1045/2014, which was not obligatory, as this consultative body expressly stated. Administrative enquiry relating to Draft Order IET/1045/2014. R-0125.
[479] The State Council is a body that is consecrated in the Constitution as the supreme consultative body of the Government. Article 107, Spanish Constitution of 1978. R-0006.

regulatory petrification. The State Council also insists on the notoriety of the need for the reform[480].

741. The State Council also confirmed that the approved regulation should not be retroactive. In this way and far removed from that which is repeatedly sustained in the Memorial on the Merits, it declares that it lacks any "*retroactive vocation*" given that it does not affect the amounts that were effectively received prior to Royal Decree Act 9/2013 coming into effect[481]. The State Council itself, also unlike the Claimants, praises and explains in its reports the complex processing and the effective participation of the public in it.[482]

742. This process was prolonged for almost a year, to ensure that the public and interested parties might have the opportunity to participate as and when the regulatory process progressed and at different times during that progress, before different bodies and without imposing whatsoever limitation insofar as their allegations were concerned[483].

743. The National Markets and Competition Commission also issued no less than four reports on the procedure of the reports referred to above.

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[480] Ruling 937/2013 of the Permanent Committee of the State Council, of 12 September 2013. General Observation VI: *"On the other hand, with respect to the principle of legitimate expectation, the reform of the electricity sector should not be thought of as something unexpected; given the gradual deterioration of the sustainability of the electricity system, those who are involved in the different activities in the supply of electricity, aware of such deterioration, could not legitimately expect that the parameters that had degenerated into the situation that has been described could be preserved.."*(emphasis added). R-0123.

[481] Ruling 937/2013 of the Permanent Committee of the State Council, of 12 September 2013. General Observation VI: *"the draft bill lacks retroactive vocation, given that it is not called upon to determine the past remuneration of the existing plants, rather that which the plants may receive, no matter whether they already exist or they are new ones, subsequent to the effective date of the reform that began with Royal Decree-Act 9/2013, of 12 July."* (Emphasis added). R-0123.

[482] Administrative enquiry relating to the Draft Royal Decree 413/2014; Report of the State Council, 6 February 2014: *Report 18/2013 of the National State Council contained myriad observations on the contents of the draft bill, many of which were accepted into the draft). As stated in the report on the analysis of the regulatory impact, following the analysis of said report and of the allegations presented as to the text through the Electricity Advisory Board, important modifications were made to the text, which justified beginning its processing again, based on the draft of 26 November 2013. This led to the report by the National Markets and Competition Commission (CNMC) of 17 December 2013, in which the Electricity Advisory Board participated for the second time. This report took into consideration the allegations that were made during the hearing that took place in the headquarters of the Electricity Advisory Board and which were attached as an annex to the actual report. During the enquiry, this Board received several requests for a hearing, which were duly granted. Thirteen written allegations were presented during this procedure. In the written allegations that were presented during this procedure, the participant parties invoked or reiterated the arguments that had been put forward in the headquarters of the Electricity Advisory Board, adding the comments that they considered to be in their best interests*." (Emphasis added). R-0124.

[483] *Administrative* file relating to the Draft Royal Decree that regulates the production of electricity from renewable energy, cogeneration and waste sources (Royal Decree 413/2014); State Council Report of 6 February 2014: *"The renewal of the procedure allowed the Electricity Advisory Board and the National Markets and Competition Commission (CNMC) to participate once again; the hearing procedure for those interested should be considered to have been completed, insofar as all the sectors that are affected by the draft have had the opportunity to participate in the drafting of the regulation - in this particular case, in fact, on two occasions, through the Electricity Advisory Board."* (emphasis added). R-0124.

744. All the Reports that the CNMC has issued have been favourable and have acknowledged that the fixed remuneration is reasonable, and that is in fact higher than that which is set forth in any one of its reports[484]. The CNMC has insisted that the procedure and the values that have been used are correct, majoring on the previsibility of the values and on the operator's awareness thereof[485].

745. Furthermore, the National Markets and Competition Commission expressed surprise as to the increase in remuneration that is produced for certain plants, which also saw how their remuneration was adjusted to the fixed reasonable profitability[486]. At the same time, this regulatory body submitted the remitted texts to the Electricity Advisory Board.

746. During certain of these procedures, more than 600 allegations were sent by all the interested parties belonging to all the sectors that participate in the electricity system and the other State Public Administrative bodies. These comments were explained and answered in the procedural file of the regulatory legislation.[487].

(1.9) Conclusions.

747. The Spanish State, by dint of its legislative and executive powers, has conferred a legal regime on plants that generate renewable energy and which received of may receive in the future remunerations payable by the electricity system.

748. This legal regime is framed within a complete reform of the different activities within the electricity system that have taken place, primarily, from January 2012 to the present day.

749. The aim of the reform has been to revise each and every one of the costs that are assumed by the electricity system in order to comply with the current legal order, both

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[484] The report by the CNMC stated that: "Generally speaking, it is noted that the investment ratio data, in euros per MW installed, employed at that time by the CNE when estimating the tariffs and premiums, even though in certain cases they were of no statistical importance, were positioned, with some exceptions, close to or beneath those that are now being proposed. Therefore, the reduction of the remuneration cannot be attributed generically to the application of low investment ratios. The remunerative adjustment is fundamentally due therefore, to the establishment of a rate of profitability applicable to the entire useful reglementary life of each plant that is less than the rate implied in the premiums and tariffs in force in the remunerative regime prior to Royal Decree-Act 9/2013, premiums that it is worth mentioning were in many cases significantly higher than those envisaged at that time by the Commission in their mandatory reports on the proposed regulatory changes that have taken place throughout the past decade." (emphasis added). Administrative file relating to Draft Order IET/1045/2014. CNMC report. R-0133. (Procedure, document 01.05).

[485] Administrative file relating to the Draft Order IET/1045/2014); CNMC Report: *"the classification employed is, notwithstanding its complexity, possibly the most objective, and probably also the most robust"* ((Procedure, document 01.05). R-0133.

[486] The regulatory body states that: *"One of the aspects of the Proposal that appears to be that paradoxical, in a context of important realignment and the possible closure of plants, is the fact that it contemplates an increase in the remuneration of specific plants, especially in their first years of exploitation."* Administrative file relating to Draft Order IET/1045/2014. CNMC report. (Procedure, document 01.05). R-0133.

[487] Administrative file relating to Draft Order IET/1045/2014); Report on the analysis of the *regulatory* impact of the draft order that approves the remunerative parameters for typical plants that are applicable to specific electricity production plants that use renewable energy, cogeneration and waste sources. Point 3 (2). (Procedure, document 15.03). R-0083.

domestic and that of the European Union, so that the consumer of electricity should not have to assume cost overruns in the different activities.

750. The result of the reform has been that certain activities and their plants have seen how their remunerations have been increased and other plants have seen theirs decrease. The intention being to respect the basic principles of the return of the investment, maintaining the operation and obtaining a reasonable return.

751. This legal regime has respected the principles that have been legally established, developed and validated by jurisprudence and are known by each and every diligent operator.

752. The new regulations are characterised by their comprehensiveness given that they carry out a detailed examination of the costs of some 2,000 typical plants, the publicity given to the procedure that led to the IT being established and the parameters and given the thoroughness that went into their establishment.

753. The different remunerative parameters have been calculated in accordance with prudent appraisal criteria, in accordance with data that is verifiable and can be perfectly replicated in the activity of the renewable energy sector.

754. The parameters are revisable as the case may be, for regulatory periods that are fully foreseeable and determined in time[488], even though the investment value and the useful regulatory life remain invariable and are not subject to review during the regulatory periods. In this way, at the end of the useful regulatory life of the plants, these continue to be the property of the investors and may remain operational, selling the energy with priority dispatch in the electricity market, without such income being in any way taken into account in the remunerative regime.

755. Consequently, above and beyond the regulatory life, it is not possible to continue to receive further public aid, as this would incur in a situation of excess remuneration or of unjustified remuneration, contrary to the legal order. It is even possible that certain plants no longer receive subsidies to the account of the new remunerative model as they have already received, prior to its coming into force, the reasonable profitability guaranteed by Law.

756. The appraisal of the impact on a specific plant that the different measures that have been adopted during the past year have had, must be made in the light of the new remunerative regime and its future projection on income, costs and profitability.

[488] It should also be pointed out that the modifications to the remunerative regime are not exclusively envisaged for the generation of electricity from renewable sources. Act 24/2013, of 26 December, on the Electricity Sector. Article 14(4) states, specifically: "*The remunerative parameters of the activities of transport, distribution, production based on renewal energy, high-efficiency cogeneration and waste sources with a specific remunerative regime and production in non-peninsular electricity systems with an additional remunerative regime shall be established taking into account the cyclical situation of the economy, of the demand for electricity and the appropriate profitability for these activities for regulatory periods that shall last be in effect for six years.*" R-0076.

757. The new remunerative regime has taken into account both the positive and the negative measures, so that the profitability of the plant may be maintained in terms of reasonability.

758. For that reason, the following elements have been accepted as costs included in the R.O.: the tax on the value of the production of electrical energy, the BICES, and all those costs that are not contemplated nor taken into account under previous regulations.

759. Furthermore, the new remunerative regime responds to the new model established by the European Commission for State aid in the renewable sector that is eligible for such subsidies.[489]

760. In conclusion, this regulatory framework has provided a global answer to the protection and promotion of investments in Spain.

761. To this end, it is worth pointing out that the Economic Report of Order IET/1045/2014 includes the following cost estimation[490]:

TECNOLOGIA	Estimación de primas recibidas 1998-2013 (millones de €)	Estimación primas pendientes de recibir desde 2014 hasta el final de la vida util (millones de €)	Estimación del total de primas recibidas en toda la vida útil (millones de €)
COGENERACION	12.917	19.504	32.421
FOTOVOLTAICA	14.617	64.234	78.851
TERMOSOLAR	2.640	32.464	35.104
HIDRAULICA	4.263	1.250	5.513
EOLICA	15.400	20.500	35.900
BIOMASA Y BIOGAS	2.003	6.685	8.688
TRATAMIENTO DE RESIDUOS	2.626	4.220	6.846
COMBUSTIÓN DE RESIDUOS Y LICORES NEGROS	1.827	1.708	3.535
TOTAL RENOVABLES, COGENERACIÓN Y RESIDUOS	**56.294**	**150.565**	**206.859**

(2) Existence of a European Commission State subsidy procedure in relation to Order IET/1045/2014 and the regulations that this replaces.

762. As has already been stated, in the European Union, the remuneration policy in favour of renewable energies is subject to a number of directives that have been approved by the European Commission.

763. Until recently, there were different interpretations as to whether amounts received by producers through invoices paid by consumers ought to be considered State aid. Such doubts of interpretation have been clarified by the Order of 22 October 2014 of the Court of

[489] Directives on state aid in the area of environmental protection and energy 2014 -2020, 2014/C-2020, point 129. "Aid may only be granted until the plant has been completely amortised in accordance with normal accounting regulations and whatsoever investment subsidy were to have been received beforehand, must be deducted from the operational aid". R-0065.

[490] Administrative enquiry relating to Draft Order IET/1045/2014); Report on the Analysis of the Regulatory Impact, page 100. R-0083. (Procedure, document 15.03).

Justice of the European Union laid down regarding preliminary ruling C- 275/13, (ELCOGAS case) referring to Spain, paragraph 33, which concludes as follows[491]:

> *"Article 107 of the TFEU, section 1, must be interpreted in the sense that the amounts attributed to a private electricity producing company which are financed by all the electricity end users established in national territory and which are distributed to Electric Sector companies by a public organisation in accordance with predetermined legal criteria, constitute a State intervention or by means of State funds."*

764. As a result of said legal resolution, Spain communicated to the European Commission the support measures for renewable energies and cogeneration that it had adopted by dint of Ministerial Order IET/1045/2014. The Commission has opened to that effect, procedure SA.40348 2014/N.

765. Article 4.3 of the Treaty of the European Union (TUE) establishes the obligations that the State assumes by virtue of the principle of sincere cooperation. In this way, in accordance with paragraphs two and three of this precept:

> *"The Member States shall take any appropriate measure, general or particular, to ensure fulfilment of the obligations arising out of the Treaties or resulting from the acts of the institutions of the Union.*
>
> *The Member States shall facilitate the achievement of the Union's tasks and refrain from any measure which could jeopardise the attainment of the Union's objectives".*

766. This prevision does not establish a mere principle of an illustrative nature, rather it imposes obligations that may be demanded of the States whose non-compliance may give rise, by the application of articles 258 and 260 of the Treaty on the Functioning of the European Union (TFUE), to a Sentence by the Court of Justice of the European Union that may impose an economic penalty and/or a coercive fine on that State.

767. Within the obligations that TFUE imposes on Member States is the prohibition to grant State aid, save in cases permitted by the Treaties. In accordance with article 107.1 TFUE, *"Save as otherwise provided in the Treaties, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market".*

768. In the light of the definition in the Elcogas Sentence as to the concept of State aid, the Respondent was obliged, under the provisions of articles 107 and 108 TFUE, to notify the European Commission as to the existence of measures to support renewable energy and cogeneration in Spain, related to the arbitration that this Arbitral Tribunal is hearing.

769. The notification of the aid allows the State to not only comply with the obligations that derive from the Treaties, but to also ask the Commission to declare them compatible on the basis of the Directives that govern state aid in the area of environmental protection and

[491] Order of the Court of Justice of the European Union laid down regarding preliminary ruling C-275/13, ELCOGAS, of 22 October 2014. R-0074.

energy 2014-2020. The declaration of compatibility by dint of a Commission Decision is the applicable procedure, in the light of articles 107.3.c) and 108 TFUE.

770. In accordance with article 108 TFUE, the Commission has exclusive competence for declaring whether an aid is compatible with Union Law; the only body with competence to review the legality of this Decision is the Court of Justice of the European Union, as per a very consolidated jurisprudence.

771. Both the exclusive competence of the Commission to declare the compatibility of the aid and that of the Court of Justice of the Union to review the legality of said declaration are imperative regulations that cannot be derogated under any circumstances and that form part of the public order of the European Union.

772. Therefore, and for reasons of transparency and goodwill in the development of the arbitration procedure, the Kingdom of Spain makes the Arbitral Tribunal aware of the existence of said procedure.

773. This communication is of particular relevance in the light of the decision of the Commission dated 26 May, 2014[492], in which it ordered the suspension of the payment by Rumania of an arbitration award laid down in an ICSID arbitration, *Micula c. Rumania*.

774. Thereafter, by a decision dated 30 March, 2015[493], the Commission has resolved that *"the payment of compensation by Rumania to two Swedish investors by virtue of the abolished aid regime violates the rules governing EU State Aid"* and that *"by means of the compensation granted to the Claimants, Rumania is in actual fact awarding an equivalent advantage to the abolished aid regime"*. The Commission thus concluded that said compensation is equivalent to an incompatible State Aid and must be returned by the beneficiary companies.

H. The Measures that are in conflict have been acknowledged as necessary macro-economic control measures that stabilise the economy and are reasonable.

775. The Claimants question the reasonable and proportional nature of the measures from a regulatory point of view, basing themselves on the subjective opinion of their experts. However, said opinion contrasts with the opinions of different institutions and agents who have appraised the new regulatory framework.

(1.1) Appraisal of the measures by the Internal Courts of the Kingdom of Spain

776. The new remunerative model has been subjected to examination by the highest judicial institutions in the Kingdom of Spain. They have all ratified the rationality and the proportionality of the new system.

(a) The Position of the Constitutional Court of the Kingdom of Spain.

[492] Document of the Commission C (2014) 6848 final, of 1 October 2014, which orders the suspension of the payment by Rumania of an arbitration award laid down in an ICSID arbitration, *Micula c.* Rumania. R-0208.

[493] Decision (EU) 2015/1470 of the European Commission of 30 March 2015 which declares as State aid that is incompatible with the TFUE, the compensation that was granted in the arbitration award in the case *Micula c. Rumania* (Commission press release, English version). R-0002.

777. The Constitutional Court of the Kingdom of Spain has already issued several pronouncements as to whether the new system violates the Spanish Constitution. Specifically, it has already resolved the constitutional challenges presented by the Autonomous Comunidad of Murcia[494], the Autonomous "Foral" Community of Navarra[495] and the Socialist Parliamentary Group to Royal Decree Act 9/2013.[496]

778. The Constitutional Court[497], the maximum interpreter of the Spanish Legal Order in the sphere of the protection of fundamental rights, in its Sentence of 17 December 2015[498], has come to ratify and consolidate the jurisprudential line set by the Supreme Court, with regard to the conformity of the reforms introduced in the SEE to the principles of legal security and its corollary of legitimate expectation, that of regulatory hierarchy and the non-retroactivity of the rules regarding regulations that are punitive or restrictive of individual rights.

779. In fact, when resolving the constitutional challenge filed by the Government Council of the Autonomous Community of the Region of Murcia, against article 1, paragraphs two and three and the first additional provision, transitional provision three and the second final provision of Royal Decree-Act 9/2013, of 12 July, which adopted urgent measures to ensure the financial stability of the electricity system, it analyses, successively, the alleged breaches of the principles of regulatory hierarchy, legal security, legitimate expectation and the non-retroactivity of punitive provisions that are unfavourable or that restrict individual rights, which the petitioners alleged in respect of the said provisions.

780. However, as has been advanced above, the Constitutional Court reproduces the same criteria that was sustained by the Supreme Court in its consolidated jurisprudence.

781. As for the alleged infringement of the principles of legal security and legitimate expectation, the Constitutional Court establishes that:

> *"Respect for this principle and its corollary, the principle of legitimate expectation, is compatible with changes in the remuneration system for renewable energy by Royal*

[494] Sentence of the Constitutional Court of 17 December 2015, delivered in constitutional challenge 5347/2013. R-0154.
[495] Sentence of the Constitutional Court of 18 February 2016, delivered in constitutional challenge 5582/2013. R-0156.
[496] Sentence of the Constitutional Court of 18 February 2016, delivered in constitutional challenge 6031/2013. R-0157.
[497] The functions of the Constitutional Court are expressly set out in article 161 of the Spanish Constitución, which states that: "*1. The Constitutional Court has jurisdiction throughout the Spanish territory and is competent to hear:*a) *Constitutional challenges against laws and legally binding regulatory provisions. The declaration of unconstitutionality of a legally binding legal regulation, interpreted by the jurisprudence, will affect this latter, although the recurred sentence or sentences do not lose their value as a res judicata.b) Writs for protection due to the violation of the rights and liberties referred to in article 53, 2, of this Constitution, in the cases and forms laid down in law.c) Conflicts of competence between the State and the Autonomous Communities or between the Autonomous Communities.d) Such other matters as are attributed to it by the Constitución or by organic law.2. The Government may challenge before the Constitucional Court the provisions and resolutions that are adopted by the organs of the Autonomous Communities. Such a challenge shall give rise to the suspension of the challenged provision or resolution, but the Court, in such cases, must ratify it or raise an objection within no more than five months* ». R-0006.
[498] Sentence of the Constitutional Court of 17 December 2015, delivered in constitutional challenge 5347/2013. R-0154.

Decree-Law 9/2013, even - as in the present case - in an area subject to high administrative intervention by virtue of its effect on general interests, and a complex regulatory system that makes it unfeasible to claim that more favourable elements are invested with permanence or inalterability faced with the exercise of legislative power that forces government to adapt this regulation to a changing economic reality."[499] *(Emphasis added).*

782. Furthermore, it adds with respect to both principles that:

"The change that has taken place cannot be described as unexpected, since the changing circumstances affecting that sector of the economy, made it necessary to make adjustments to this regulatory framework, as a result of the difficult circumstances of the sector as a whole and the need to guarantee the required economic balance and proper management of the system. There are, therefore, no grounds for arguing that changing the compensation system under review was unforeseeable for a "prudent and diligent economic operator", based on the economic circumstances and the insufficient measures taken to reduce persistent and continuously rising deficits in the electricity system not sufficiently tackled with previous provisions.

The preamble of the Royal Decree-Law determines that its purpose is to avoid "over-remuneration" of certain facilities under the special system[500] *" (Emphasis added).*

783. Finally, with regard to the claimed violation of the principle of non-retroactivity, it concludes by stating that:

"The operators of electricity production facilities under the subsidised system are subject to this new remuneration system from the date of entry into force of Royal Decree-Law 9/2013, (...) without that subjection entailing an unfavourable effect on acquired rights, from a constitutional point of view, i.e. it does not affect property rights previously consolidated and definitively incorporated into the assets of the recipient, or legal situations already expired or consummated[501] *".*

784. This clarity and assertiveness have been reinforced by the concurring opinion put forward by Judge Juan Antonio Xiol Rios in respect of the Sentence itself, joined by Judge Adela Asua Batarrita and Judge Fernando Valdés Dal-Ré[502]. Far from rectifying or disagreeing with the operative part of the judgment, this concurring opinion actually reaffirms it, endowing it with greater legal precision and argumentative foundation.

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[499] Sentence of the Constitutional Court of 17 December 2015, delivered in constitutional challenge 5347/2013. Legal basis seven (a). R-0154.
[500] Sentence of the Constitutional Court of 17 December 2015, delivered in constitutional challenge 5347/2013. Legal basis seven (a). R-0154.
[501] Sentence of the Constitutional Court of 17 December 2015, delivered in constitutional challenge 5347/2013. Legal basis seven (c). R-0154.
[502] Sentence of the Constitutional Court of 17 December 2015, delivered in constitutional challenge 5347/2013. Dissenting / concurring opinion made by Judge Juan Antonio Xiol Ríos in respect of the Judgment set down in constitutional challenge No. 5347-2013, joined by Judge Adela Asua Batarrita and Judge Fernando Valdés Dal-Ré. R-0154.

785. Although the clarity of exposition and the accuracy of this concurring opinion may well justify its reproduction in full, we are going to extract those pronouncements that most faithfully reflect the reality of the SEE and its regulations, which, moreover, all prudent investor should be well aware of. In this regard, the aforementioned concurring opinion contextualises the reason for its issuance, stating that *least three important elements converging in this area that should have led the majority opinion not to analyse in such a cursory manner the question of legitimate expectation, such as:*

> **(i)** *the regulatory evolution in which the regulation of renewable energies has been immersed and the controversy that has arisen between the different legal operators concerning the principle of legitimate expectation;*
>
> **(ii)** *the fact that until now the Constitutional Court, despite the different times when it has been raised, had not had the opportunity to rule on the matter, with the legal and economic operators having reasonable expectations that it would provide a solid constitutional answer to this question; and*
>
> **(iii)** *the existence of numerous multimillion-dollar lawsuits against the Kingdom of Spain raised by foreign investors against these regulatory changes in international arbitration courts precisely for infringement of the principle of legitimate expectation, in relation to which a resolution more widely established by the Constitutional Court seems particularly necessary*[503] *".*

786. Starting from this contextualisation, this concurring opinion focuses on clarifying the concept of legitimate expectation. It defines it as the principle that protects the legitimate expectations of citizens who adapt their economic behaviour to the legislation that is in force against regulatory changes that are not reasonably foreseeable; to back up their deliberations they allude to criteria used by the Court of Justice of the European Union. In this context, it states that:

> *"(b) the modification brought about by Royal Decree-Act /2013 meant a new incentive regime characterised by (i) the existence of an additional remuneration to that of market participation that covers the investment costs that an efficient and well managed enterprise might not recover in the market; (ii) that this remunerative regime shall not exceed the minimum level needed to cover the costs that allow plants to compete on a level playing field with other technologies that are available in the market and which make it possible to obtain a reasonable profitability, referring to a typical plant in each applicable case; and (iii) that the reasonable profitability, before taxes, will hinge on the average yield in the secondary market for ten-year Government Bonds, applying the appropriate differential.*
>
> *On the other hand, and as was justified extensively in the explanatory statement of Royal Decree-Act 9/2013 itself, this regulatory modification derives from the need to satisfy urgent and higher public interests that were crystallised in the need to reduce a*

[503] Sentence of the Constitutional Court of 17 December 2015, delivered in constitutional challenge 5347/2013. Concurring opinion made by Judge Juan Antonio Xiol Ríos in respect of the Judgment set down in constitutional challenge No. 5347-2013, joined by Judge Adela Asua Batarrita and Judge Fernando Valdés Dal-Ré. Legal basis II (6). R-0154.

tariff deficit which, over time, had become structural, due to the real costs associated, inter alia, with regulated activities being higher than the revenue from the tolls established by the Administration and paid by consumers[504] *".(Emphasis added)*

787. On this basis, the dissenting opinion concludes categorically:

"Despite this, the legitimate expectations created by the amended legislation have been essentially maintained, both in the sense of giving continuity to a system of incentives and in subjecting it to the obtaining of a reasonable return with reference to the cost of money in the capital market. However, maintaining a situation involving very high levels of profitability outside the market cannot be qualified as a legitimate expectation nor, therefore, can it be claimed as protected by economic operators on the basis of the principle of legitimate expectation, once that reasonable profitability has been guaranteed, and it may be contrary to overriding public interests.

(c) ***Nor can this regulatory change be considered to be unforeseeable for a prudent economic operator*** *in response to the different circumstances that arise, including developments in the general economic situation and the electricity industry in particular (...).*

To this end, among other concurrent factors to be taken into account for concluding that the amendment at issue was not unforeseeable, we can cite some of those that were already discussed at length in the above-mentioned STS of 12 April 2012, in connection with other previous amendments, such as (i) the uniqueness of an economic sector that is strategic in nature, implying a great density of regulations, the presence of underlying public interests and, consistent with this, the need for regulatory changes that adapt the regulatory framework to the contingencies of the industry and the variations that may arise in the economic data; (ii) the nature of the incentives in the form of regulated tariffs, which is a rare and unusual situation in a free market system because it eliminates the investment risk arising from free market system; and (iii) the implicit conditioning of all incentive measures to the fact that their ongoing permanence cannot be assured and the explicit conditioning that it is linked to achieving a number of goals. To these should be added, in the specific case referred to in this appeal on the grounds of unconstitutionality, the fact that the successive reforms implemented in the administrative implementing regulations already anticipated a change in the system of incentives that could affect at least the quantification of profitability levels. "[505] *(Emphasis added).*

788. The forcefulness, clarity and continuity of the applicable Jurisprudence leaves no doubt about the scope, content and legal limits of the reasonable profitability to which investors

[504] Sentence of the Constitutional Court of 17 December 2015, delivered in constitutional challenge 5347/2013. Concurring opinion made by Judge Juan Antonio Xiol Ríos in respect of the Judgment set down in constitutional challenge No. 5347-2013, joined by Judge Adela Asua Batarrita and Judge Fernando Valdés Dal-Ré. Legal basis II. (7.ii). R-0154.

[505] Sentence of the Constitutional Court of 17 December 2015, delivered in constitutional challenge 5347/2013. Dissenting / concurring opinion made by Judge Juan Antonio Xiol Ríos in respect of the Judgment set down in constitutional challenge No. 5347-2013, joined by Judge Adela Asua Batarrita and Judge Fernando Valdés Dal-Ré. Legal basis II. (7.ii). R-0154. Please note that SCJ means Supreme Court Judgment.

were entitled. And therefore, to assess the real legitimate expectations that the Kingdom of Spain offered to all national or foreign investor. It is therefore essential to specify the objective legitimate expectations that the Claimant may have had in mind when they made their investment.

(b) The Position of the Supreme Court of the Kingdom of Spain.

789. In its Judgment 63/2013 of 21 January 2016[506], the Supreme Court has dismissed the claim for liability on the part of the State legislator for damage caused:

- By Royal Decree 1565/2010, of 19 November, which regulates and modifies certain aspects pertaining to the activity of electrical energy generation under the special scheme.

- By Royal Decree-Act 14/2010, of 23 December, which establishes urgent measures for the correction of the deficit of the electrical sector.

790. In fact, in line with its jurisprudential doctrine that began in the year 2005, the Supreme Court reiterates that same doctrine, pointing out that RD 661/2007 did not result in a petrifaction of the economic regime in force at that time. Thus, it has expressly established that:

> *"And it shall also require to start with a presupposition which, in the opinion of the Court, does not concur (nor will it concur when the same installations start operation): that the legal regime established in Royal Decree 661/2007 shall be extended indefinitely and that it shall be done, moreover, under the same conditions that were expressly forecast at that time. We do not consider, in effect, that the above Royal Decree considers a tariff regime for ever, nor that the Government, when exercising their legal power of authority, or the legislator, using their legislative authority, may not adapt or modify this regime to new circumstances (economic, productive, technological or of any other nature) that may arise in such an extended period of time.*
>
> *In short, not only do we not esteem (as already indicated in the Third Section of this Chamber in the afore-mentioned Judgement) that the temporal modification we are analysing violates the principles of legal security and legitimate confidence, but that, from the point of view of the institute of the patrimonial liability, it cannot be stated by any means that the alleged damage has the characteristics of effectiveness and timeliness that would allow it to be classified as payable[507]"*

791. Furthermore, the Supreme Court has recently pronounced itself in multiple judgments[508] on the legality of RD 413/2014 and Order EIT/1045/2014, rejecting the existence of prohibited retroactivity, the violation of the principle of legitimate expectation enshrined by

[506] Judgment 63/2013 of 21 January 2016 of the Supreme Court handed down on appeal 627/2012. R-0155.
[507] Judgment 63/2013 of 21 January 2016 of the Supreme Court handed down on appeal 627/2012. Legal basis six. R-0155.
[508] Among many others, Judgment 1260/2016 (Rec. 649/2014) and Judgment 1266/2016 (Rec.564/2014). R-0149 and R-0158.

the EU and recognising the foreseeable nature of the measures. It also sustains that the measures maintain the essential lines of the Spanish system of remuneration for renewable energies, and therefore it understands that it maintains regulatory stability. The Supreme Court reaches these conclusions after reproducing the doctrine of the Constitutional Court established in earlier judgments, as well as its consolidated jurisprudence in the area of Special regime remuneration.

792. A more detailed analysis of these recent judgments will be made in the section relating to the FET.

(1.2) Appraisal of the measures by the institutions of the European Union

793. The new system has been analysed by the European Union. The European Commission has issued various reports on the evolution of the macroeconomic measures taken by Spain. In these reports, it has acknowledged that Spain is in compliance with the agreements concluded with the EU to adopt measures of macroeconomic control since March 2012509.

794. The European Union, after having examined the evolution of the economy of the Kingdom of Spain since 2012, has issued a favourable judgment of the macroeconomic control measures that it has taken. This examination refers to the Macroeconomic measures taken in different sectors: finance, public administration, the labour market, education, insolvency, energy and infrastructure. The European Union has stated in its 2014 Report, with regard to the Energy Sector, that:

> *"The reform of the electricity sector is being completed [...] The reforms in the gas and electricity sectors are helping to contain the tariff deficits [...] On the basis of the analysis in this report, repayment risks for the ESM loan are very low at present. This assumes that the authorities continue to improve the state of public finances and keep reforming the economy to address the challenges. The Spanish state can now borrow cheaper* ***thanks to policy actions at national and European level,*** *restored confidence in the Spanish economy and its public finances."*[510] *(Emphasis added)*

795. The more thorough examination of the "Progress on Policy Measures Relevant for the Correction of Macroeconomic Imbalances" elaborates upon these measures. The European Commission stated in 2014:

> *"The 2013 reform of the electricity sector helped to contain the tariff deficit, and the 2014 deficit should be considerably smaller or the system should be in balance. The 'electricity tariff deficit' reached [...] EUR 28.5 bn at the end of 2013, almost 3% of GDP. The increase in access tariffs and the reduction in various costs of the*

[509] Each year the European Commission draws up a *"Country Report"*, carrying out a thorough examination of the economic situation of each State. These Reports form part of the so-called "*Macroeconomic Imbalance Procedure*" which is a monitoring mechanism to correct existing *Macroeconomic imbalances*. The result of the in-depth examinations serves as a basis so that the Council may issue *Recommendations to the Member States of the EU* as to the steps to be taken to correct these macroeconomic imbalances.

[510] Spain – Post Programme Surveillance Autumn 2014 Summary Report, page 3. (R-0202) Accesible on the web address:
http://ec.europa.eu/economy_finance/publications/occasional_paper/2014/pdf/ocp206_summary_en.pdf

electricity system applied with the 2013 reform help to balance the system in 2014. The authorities consider that the measures taken up to date should be sufficient to close the deficit structurally."[511] *(Emphasis added)*

796. In the subsequent 2015 review, the European Commission stated that the costs of the tariff Deficit from the previous regulatory regime were being excessively passed on to consumers:

"The 2013 reform of the electricity sector helped to contain the tariff deficit, and the 2014 deficit should be smaller than in previous years. Energy policy choices in Spain over the last decade have resulted in an increase in regulated costs of the electricity system (Graph 3.4.1) and have been, to a large extent, passed on to electricity consumers."[...] The energy regulator, CNMC, expects that, in 2014, the system was closer to equilibrium in structural terms than in previous years."[512] *(Emphasis added)*

797. As a result of the Measures taken in the Electricity Sector by the Kingdom of Spain, the Recommendations of the Council in the year 2015 consider that the macroeconomic problem derived from the tariff deficit has been resolved513. Therefore, it does not include any Recommendation whatsoever that the Kingdom of Spain should take measures in 2015 and in 2016 in this area.

798. In 2014, the National Association of Producers and Investors in Renewable Energies addressed a petition to the Commission requesting that it investigate the situation in which the photovoltaic industry found itself due to the different regulatory changes that are, at the same time, the subject of this arbitration. In the light of this situation, in its reply of 29 February 2016 the Commission stated:

"In previous 'EU semester' recommendations to Spain, the Council emphasised the need for Spain to make the structural and comprehensive reforms to the electricity sector necessary to address this tariff deficit.(...)

The Commission has considered the petition carefully and does not believe that under Directive 2009/28/EC there are grounds for the Commission to take legal action against Spain with regard to the changes in their legislation affecting the level of support given to investors in renewable energy projects. In particular, pursuant to Article 3(3) of Directive 2009/28/EC, support schemes are but one instrument that can be chosen by Member States to achieve the binding national targets established by the Directive for the share of renewable energy in gross final energy consumption as well as in transport in 2020. Member States retain full discretion over whether they use support schemes or not and, should they use them, over their design, including both the structure and the level of support. This comprises the right for Member States to

[511] Spain — Post Programme Surveillance Autumn 2014 Report. page 27, accessible in: http://ec.europa.eu/economy_finance/publications/occasional_paper/2014/pdf/ocp206_en.pdf

[512] Macroeconomic imbalances Country Report – Spain 2015, page 62. (R-0209) accessible in: http://ec.europa.eu/economy_finance/publications/occasional_paper/2015/pdf/ocp216_en.pdf

[513] Council Recommendation on the 2015 National Reform Programme of Spain and delivering a Council opinion on the 2015 Stability Programme of Spain: "(9) [...] *The deficit in the electricity system has been effectively eliminated as of 2014*".(R-0063) accessible in: http://ec.europa.eu/europe2020/pdf/csr2015/csr2015_spain_en.pdf

enact changes to their support schemes, for example to avoid overcompensation or to address unforeseen developments such as a particularly rapid expansion of a precise renewables technology in a given sector.

Therefore, in cases of changes to a support scheme as such, there is no breach of Directive 2009/28/EC" (Emphasis added)[514]

(1.3) Appraisal of the Measures by other International Organisations

799. The measures implemented in the Spanish electricity sector in the year 2013 were recognised by the International Monetary Fund (IMF) in its July 2014 report on Spain in which it stated:

"While there is encouraging progress, especially the important market unity law (Box 2) there should be no slippage on the planned reforms. For example, it will be important to move ahead with an ambitious liberalization of professional services, improve training for the unemployed, and fully implement an energy reform that eliminates the electricity tariff deficit and contains costs, while promoting a stable business environment and appropriate levels of investment. Given the many regulations at all levels of governments, regions have a critical role to play in improving the business environment—the planned introduction of regional World Bank's "Doing Business" indicators is a positive initiative"[515].

800. For its part, the International Energy Agency (IEA) has emphasised the relevance of the measures taken and has stressed the importance of keeping them to preserve the sustainability of the financing for the electrical system in the future:

"The IEA welcomes the government's actions, which have eliminated the annual deficit from 2014 on. The accumulated tariff deficit has thus stopped from growing and will gradually be eliminated. The government must maintain a strong long-term commitment to balancing the costs and revenues in the natural gas system."[516]

801. In its report for the year 2015, the International Energy Agency makes the following considerations as far as the reform that is the subject of this arbitration is concerned:

"The tariff deficit, which had been accumulating since 2001, began to spiral out of control after 2005. From 2005 to 2013, the costs in the electricity system grew by 221% while revenues increased by only 100%. Subsidies for renewable electricity are the single largest cost element. By 2012, the accumulated debt in the system had reached more than EUR 20 billion and was set to expand by billions every year unless action was taken. In 2012, the government temporarily eliminated subsidies for new installations. It also reduced remuneration for transmission and distribution network activities, increased access tariffs, and introduced a 7% tax on electricity generation

[514] Response of the European Commission of 29 February 2016. R-0185.
[515] IMF Country Report 14/192 Spain, July 2014, pages 6 and 23. R-0207.
[516] Energy Policies of IEA Countries - Spain 2015 Review, Executive summary and key recommendations, published by the International Energy Agency, page 10. R-0211.

(22% for hydropower). Nevertheless, the deficit grew to EUR 26 billion by the end of 2012.

In July 2013, the government introduced a broader electricity market reform package. The reform reduced the remuneration and compensation for the activities in the electricity system by several billion euros per year. It also introduced the principle of "no new cost without a revenue increase". Importantly, the reform introduced a new way of calculating compensation for renewable energy, waste, and co-generation (combined production of heat and power). With some exceptions, by mid-2015 the comprehensive reform had been implemented. The reform has reached its aim: the sector's costs and revenues are back in balance, and the accumulated deficit, which peaked at the end of 2013 at EUR 29 billion or 3% of GDP, should gradually disappear over the next 15 years.

Electricity market reform has been complex but necessary. The electricity system's future financial sustainability depends both on macroeconomic developments and on a sustained commitment to the reform by the country´s politicians. To overcome any perceived risks for investing in electricity infrastructure in Spain, the government should closely follow the principles of transparency, predictability, and certainty when revising the parameters for defining reasonable return. More generally, to avoid any political interference in the future, the principle of "no new cost without a revenue increase" should be strictly enforced."[517]

802. This report continues stating:

"Spain underwent an electricity market reform from early 2012 to 2015, with the aim of ensuring the sustainability of the system, balancing costs and revenues and protecting electricity consumers. The reform was developed to give predictability and transparency to the Spanish electricity system, to put an end to a burgeoning tariff deficit that had become a financial liability for the government and to bring the electricity system back to financial stability.

Since the last in-depth review in 2009, also the Electricity Directive (Directive 2009/72/EC) was approved. The new Electricity Law approved in December 2013 revised the Spanish legal framework in accordance with the new European regulations and directives (the Third Package), but taking account of the Spanish situation regarding the integration of renewable energy sources and the low level of interconnections with other EU member states."[518]

(1.4) Appraisal of the Measures by the Markets

803. The favourable reception the macroeconomic control measures taken by Spain since 2012 should also be stressed. The rating issued by the various rating agencies such as Fitch or Moody's Investors Service has improved since 2014[519]. This change is explained in part

[517] IEA_IDR_Spain2015 Report, Pag 10. R-0226.
[518] Ibid, page 21. R-0226.
[519] Econ One Research Report of 15 June 2016, section V.

by the macroeconomic measures taken by the Spanish State in recent years, which have made it possible to rebalance the tariff deficit of the electric sector.

804. Additionally, in 2015, with the reform of the electrical system now complete, the regulatory uncertainty has disappeared and investment in renewable energy is recovering. It is worth drawing the attention of the Tribunal to the many press reports that have remarked upon (1) the stability of the system created by the reform and (2) the so-called "renewable energy boom" which is taking place in Spain due to the confidence of investors, both national and foreigns, have in the profitability and stability of this system:

> *"Soria envisages an electricity system surplus for 2015"*[520]*: "The Minister of Industry has pointed out that "it is good news that there is a surplus", but has insisted that, "whatever that amount may be, it will be used to reduce the total amount of accumulated deficit in the system".*
>
> *"Wind Operators in Spain and Portugal attract investor interest*[521]*": "What is attracting these investors is the stable profitability that renewable energy companies usually generate. The context of low interest rates at the global level requires managers to search for profitability above and beyond equities and fixed income PROFITABILITY:*
> *And although the profitability offered by renewable energies is lower now than before the reduction of the remuneration, Spain still guarantees an annual yield of 7.5% for the electricity that most of the wind farms in the country".*
>
> *"Operations boom in the renewable energy sector after the reform"*[522]*: "The purchase of solar and wind power plants so far this year is already in excess of 1,000 million. Experts agree that there will be new operations in the sector in the coming months."*
>
> *"What the disappearance of the premiums has given rise to is a race to rationalise the [Wind] industry through mergers, taking advantage also of the abundance of liquidity and the legislative stability with which the above-mentioned energy reform has endowed the sector."* [523]
>
> *"The boom in renewables attracts 5 billion in investments"*[524]*: "So far this year, the renewable energies sector has accumulated almost 5,000 million euros in buying and selling operations [...]"*
>
> *"Renewable energies are regaining their momentum in Spain"*[525] *"Millions of euros in a maelstrom of renewable energy buying and selling operations. [...] For months now, not a week goes by without a corporate move in the renewable energies sector. [...]The renewable energy business map is changing at the stroke of a pen."*

[520] Press item; "Soria envisages an electrical system surplus for 2015", El País, 16 June 2015, R-0169.
[521] News item from EFE Agency, dated 9 June 2015, R-0175.
[522] News item in the "El Mundo" newspaper, "Operations boom in the renewable energy sector after the reform", dated 22 July 2015. R-0179.
[523] Editorial in the financial newspaper The Economist, dated 24 July 2015. R-0176.
[524] News item in the financial newspaper "The Economist", dated 17 July 2015. R-0178.
[525] News item in the financial newspaper "Expansión", dated 17 July 2015.

805. It is clear that the reform is not as irrational and disproportionate as the Claimants sustain. If it were so, domestic and foreigns investors would not be interested in making investments or purchases in the Spanish energy sector. This investor boom debunks the Claimant's arguments. It is clear that as far as the media and investors are concerned, a profitability of 7.398% is reasonable. Especially in the current international economic context, after the global financial crisis suffered between 2010 and 2013.

806. It is also worth noting that there was an auction in 2015 for producers of RE, of 500 megawatts (MW) of Wind and 200 MW of Biomass energy. In this auction, offers were received from national and foreigns companies for 5 times more power than was finally awarded in January 2016526. This confirms the interest of the markets, both national and foreigns, in the regime that has derived from the contested measures.

807. Diario Expansión, a daily financial newspaper with one of the largest circulations in Spain, recently published the views of business executives and industry analysts and according to them, the measures have provided the regulatory framework with the stability it needed:

> *"The electricity reform, which began in July 2013, is already bearing fruit in the market in the form of stability. Marta Méndez Villaamil, Legal Director of Mergers and Acquisitions at EDP Renovaveis, explains that the market has become more professional, it is much more sophisticated and investors are more qualified"*[527]

808. These news items, the positive ratings of the Rating Agencies and the favourable Reports from the European Commission, are yet more proof of the reasonable and proportional nature of the macroeconomic control measures taken in the energy Sector by the Kingdom of Spain between 2013 and 2014.

I. <u>The Energy Charter Treaty Objective and scope of protection</u>

(1) Objective and purpose of the ECT: To grant a national or non-discriminatory treatment to the foreign investor, without preventing States from exercising their legitimate right to regulate in such a strategic sector as the energy sector.

809. The Claimants consider that the measures taken by the Kingdom of Spain have violated several provisions of the ECT (Articles 10.1 and 13). However, it must be emphasised that, even when the Claimants allege that the standards of protection of the ECT must be analysed within its context[528] and in accordance with its objective and purpose[529], they have

[526] Resolution of 17 March 2016, of the Directorate General for Energy Policy and Mines, by which awarded bidders in the auction for the assignment of the specific remunerative regime to new facilities that produce electricity from biomass and are located in the peninsular electricity system and for wind technology plants, are entered as "pre-allocated" in the register of the specific remunerative regime. R-0220.

[527] News item in Diario Expansión dated 3 May 2016: "Spain creates a secure legal framework to avoid another energy bubble". R-0084.

[528] It is thus considered in respect of the interpretation of the umbrella clause in paragraph 786 and in respect of the standards of the ECT in paragraph 864, among others.

[529] Memorial on the Merits, paragraph 866.

barely dedicated a paragraph of their Statement[530] to the analysis of the objectives of the ECT.

810. In fact, the Claimants acknowledge that the objective of the ECT, according to its article 2, is to establish "a legal framework in order to promote long-term cooperation in the energy field, based on complementarities and mutual benefits, in accordance with the objectives and principles expressed in the Charter" (Emphasis added). However, they neglect to add for the benefit of the Arbitral Tribunal any reference to the objectives and principles of the European Energy Charter, which the ECT expressly accepts with its remission of Article 2. These objectives are:

> *"foster the development of an efficient energy market throughout Europe and a better functioning of the global market, based in both cases in the principle of non-discrimination and on a determination of prices based on the market, taking into account the concerns expressed in relation to the environment"*[531].

811. To achieve this goal, the countries that signed the letter state that they are "determined to create a favourable climate for companies to work in and for the flow of investments and technologies, by applying market economy principles in the field of energy".[532] Therefore, the protection that the ECT offers to investments is geared toward the achievement of that free energy market throughout Europe, based on the principle of non-discrimination and on the formation of prices that are in line with the market.

812. This line of protection of investments is understandable if one takes into account that it was the European Community (today the EU) that promoted the signing of the ECT, as Professor Wälde recalls[533]. In this way, the ECT endeavours to lay the basis for the progressive liberalisation of the energy market between Western Europe and the former Soviet Socialist Republics after the fall of the Berlin Wall. The ECT is therefore *"the basis of an energy community among the regions of the world that were divided by the iron curtain."*[534] In order to achieve this objective, the signatory States had "*the support of the European Community, in particular through the implementation of its internal energy market"*[535].

813. It was ultimately an attempt to export the energy Market model that existed in the EU to other countries beyond its frontiers. And this was because it was considered, as stated in the Treaties establishing the European Communities, that "*more extensive cooperation in the field of energy between the signatories is essential for economic progress and, in general*

[530] Memorial on the Merits, paragraph 866.
[531] European Energy Charter. RL-0006.
[532] Ibid, Title I. RL-0006.
[533] "*...The ECT is largely a product of EU external, political, economic and energy policy. It is meant to integrate the formerly Communist countries, provides an ante-chamber and preparation area for EU accession for many of them*". T W Wälde, "Investment Arbitration Under the Energy Charter Treaty: From Dispute Settlement to Treaty Implementation" (1996) 12 Transnational Dispute Management 4. RL-0065.
[534] "The Energy Charter Treaty and related documents", consolidated text, page 8. Accessible in the Energy Charter page", Preface (Spanish Version). RL-0006.
[535] European Energy Charter, preamble. RL-0006.

terms, for social development and the improvement of the quality of life."[536] (Emphasis added).

814. Therefore, the main objective of the ECT as far as the protection of the investor is concerned, is to achieve the introduction of a free market in order to carry out energy-related activities without discrimination on the grounds of the investor's nationality.

815. However, the objective of non-discrimination has not been fully achieved in the ECT. The reluctance of States to limit their regulatory powers in such a strategic sector as the energy sector, led the signatories of the ECT to differentiate two moments: 1) the so-called "making-investment process" (paragraphs (2) and (3) of article 10 of the ECT), in which the conditions to ensure the objective of national treatment or non-discrimination were postponed until the signing of a "supplementary treaty", which has not yet been signed and 2) the moment after the investment is made, in which the guarantee of national treatment and the most favoured nation clause are applied to the foreigns investor, albeit with certain limitations, as we shall shortly see.

816. It should be noted, in this regard, that with respect to the moment when the investment is made, Article 10 TEC already warns in its first subparagraph, as soft law, that:

> *"In accordance with the provisions of this Treaty, the Contracting Parties shall promote and create stable, equitable, favourable and transparent conditions so that investors of the other Contracting Parties may make investments in their territory."*

817. As C. Bamberger, a participant in the ECT drafting process notes:

> *"As announced in a preambular provision of the ECT, national treatment and MFN treatment is expected to be applied to the making of investments pursuant to a "supplementary treaty". Paragraphs (2) and (3) of Article 10 therefore provide only for a "best efforts" ECT commitment to accord the better of national treatment or MFN treatment to investors of other Contracting Parties with regard to the making of investments".*[537]

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[536] Ibid. RL-0006.

[537] C Bamberger, *"An Overview of the Energy Charter Treaty"*, in T W Wälde (ed), The Energy Charter Treaty: An East-West Gateway for Investment and Trade, (Kluwer Law International, 1996),(RL-0038). En el mismo sentido, Wälde dice: *"The Treaty distinguishes two phases of investment and treats them differently: the pre-investment phase (access of obligations imposing a duty of "best efforts" at non-discrimination, national and most-favoured treatment. This solution represents a compromise between states' discretion to admit investors and determine the terms of admission on one hand and some attempt to introduce non-discriminatory access –along the model of EU integration law. Once an investment is made ("post-investment phase"), i.e. once an investor has committed its capital and assumed the considerable political risk of such exposure, the protection intensity afforded by the Treaty increases significantly: in addition to what is probably a reformulation of the traditional international minimun standards, the investments are protected against discrimination, breach of contractual and other commitments, expropriation, destruction and impediments against transfer of capital and earnings (Arts.10-17)* "Investment Arbitration Under the Energy Charter Treaty – From Dispute Settlement to Treaty Implementation" by Thomas W.Wälde. RL-0052.

818. Once the investment has been made, the highest standard of protection that the ECT offers the foreigns investor and investment is that of "national treatment". The greatest ambition of the ECT is non-discrimination. In this regard, Professor Wälde says:

> *"The main standard imposed by the Treaty on investors is according to all authoritative accounts of the Treaty, "national treatment". (...). The strategy of the Treaty has been to incorporate the "favourable" element of national treatment, i.e. non-discrimination vis-à-vis national business, while countervailing the negative element, i.e. the application of possibly low-quality standards to foreigners, by the inclusion of international minimum standards. In other words, international law sets the minimum standard, even if national treatment would be much worse, but when it comes to governments favouring their own companies, then national treatment takes precedence".*[538] *(Emphasis added).*

819. That is to say, when Article 10.1 of the ECT makes it obligatory to offer to investments a "*treatment no less favourable than that required by international law*", it is resorting to the minimum standard of protection guaranteed by international law. The maximum aspiration of the ECT is, however, national treatment, since this treatment will be applied to foreign investments whenever it is more favourable. As Bamberger states:

> *"The Key Article 10 on "Promotion, Protection and Treatment of Investments" begins, in paragraph (1), with general statements concerning the favourable conditions which Contracting Parties must maintain for investments by investors of other Contracting Parties. These provisions are intended to assure an absolute minimum standard of treatment such as has been established in bilateral investment treaty practice, based to a considerable extent on developments in international law. (...)"* [539].

820. In this regard, paragraph 7 of Article 10 of the ECT states that:

> *" Each Contracting Party shall accord to Investments in its Area of Investors of other Contracting Parties, and their related activities including management, maintenance, use, enjoyment or disposal, treatment no less favourable than that which it accords to Investments of its own Investors or of the Investors of any other Contracting Party or any third state and their related activities including management, maintenance, use, enjoyment or disposal, whichever is the most favourable."(Emphasis added)*

821. However, in paragraph 8 of Article 10, this guarantee of national treatment to investments that have already been made contains a significant exception in the area of public subsidies or aid:

> *" The modalities of application of paragraph (7) in relation to programmes under which a Contracting Party provides grants or other financial assistance, or enters into*

[538] T W Wälde, *"International Investment under the 1994 Energy Charter Treaty"* in T W Wälde (ed) The Energy Charter Treaty: An East-West Gateway for Investment and Trade (Kluwer Law International, 1996). RL-0051.
[539] C. Bamberger, "An Overview of the Energy Charter Treaty", in T W Wälde (ed), The Energy Charter Treaty: An East-West Gateway for Investment and Trade, (Kluwer Law International, 1996). RL-0052.

contracts, for energy technology research and development, shall be reserved for the supplementary treaty described in paragraph (4).". (Emphasis added)

822. This exception is applicable to the present case, in which the Claimants claim "public aid" granted by the Spanish State within the framework of the EU Directives.

823. The "supplementary treaty" has not yet been signed, so the States that signed the ECT are still not obliged to grant national treatment to the foreign investor in the area of programmes by which a Contracting Party provides grants or "another type of financial aid" to the investor.

824. In the same line, we must remember that Article 9 of the ECT, when regulating the public aid regime to promote foreigns trade or investment, expressly provides in its fourth paragraph that nothing in this Article 9 "shall in any way prevent the Contracting Parties from adopting measures":

(i) for prudential reasons, including the protection of Investors, consumers, depositors, policy-holders or persons to whom a fiduciary duty is owed by a financial service supplier; or

(ii) to ensure the integrity and stability of its financial system and capital markets."

825. In case the literal words of the ECT, the European Energy Charter and the opinion of the aforementioned Doctrine were not sufficiently clear, the Secretariat of the ECT, in its "*Decision of the Energy Charter Conference, Subject: Road Map for the Modernization of the Energy Process*", of 24 November 2010, establishes as an objective in Area D, concerning "Investment Promotion and Protection":

"A comprehensive Review of the exceptions to non-discriminatory treatment in the Blue Book of the Charter"[540].

826. That is to say, the Secretariat of the ECT confirmed in 2010 that the maximum aspiration of the ECT in its future evolution is to eliminate barriers to non-discrimination. This ECT objective does not remain unfulfilled, as we shall see, as regulatory measures that are (1) proportionate, (2) justified on grounds of public interest and (3) applied without distinction to national and foreign investors alike, have been adopted erga omnes.

827. Finally, it should be borne in mind that under no circumstances does the ECT prevent signatory States from exercising their right to regulate. It is unrealistic, as the Claimants purport, that the signatory Parties to the ECT would agree, in such a strategic sector as this, to give an "insurance Policy" to foreign investors that would shield them from regulatory reforms due to general interest reasons.

828. The Guide to the Energy Charter Treaty makes it quite clear that the ECT does not preclude States from exercising their power of macroeconomic control:

[540] Energy Charter Secretariat, "Decision of the Energy Charter Conference, Subject: Road Map for the Modernisation of the Energy Process", Energy Charter Secretariat, 24 November 2010. RL-0063.

> *"8. Many* ***Governments actions****, for example the* ***macroeconomic control*** *or the introduction of environmental and security legislation,* ***may affect investment profit*** *but cannot be subject to absolute rules. In this case, the best defence for an foreign investor is the guarantee that he or she will be treated at least as well as national investors, because no government will wish to destroy its own industry."*[541] *(Emphasis added)*

829. Section 8 of the Energy Charter Treaty Guide has been incorporated into the official Texts, amongst other languages, in Spanish, French542, Italian543 and German544.

830. These official versions of the ECT Guide explain graphically the aim of the ECT: the guarantee that investors will be treated at least as well as national investors ("*since no Government will wish to destroy its own industry*"), without limiting the possibility of the States adopting macroeconomic control measures for reasons of general interest.

831. This matter is certainly important in order to decide pursuant to the FET standard that establishes the ECT. Indeed, it has been subject to discussion in the Precedents that applied the FET standard to the ECT, as we will now discuss.

832. The Claimants consider, nonetheless, that the Kingdom of Spain has violated a series of provisions of the ECT, namely:

(i) The obligation of not expropriating without compensation (article 13);

(ii) The obligation of meeting any obligation that it has entered into with the Claimant, as well as with the Claimant's Investment ("umbrella clause") (Article 10.1. in fine);

(iii) The commitment of offering the Claimants fair and equitable treatment at all times ("FET") (article 10.1);

(iv) The right of the Claimant's investments to enjoy full protection and security ("P&SC") (article 10.1);

(v) The obligation not to impair, in any way, by unreasonable or discriminatory measures the management, maintenance, use, enjoyment or disposal of the Claimant's investments (article 10.1).[545]

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[541] "The Energy Charter Treaty and related documents", consolidated text, page 8. Accessible in the Energy Charter page": RL-0006.
http://www.energycharter.org/fileadmin/DocumentsMedia/Legal/ECT-es.pdf

[542] "The Energy Charter Treaty and related documents", consolidated text, page 8. Accessible on the Energy Charter page": RL-0006. http://www.energycharter.org/fileadmin/DocumentsMedia/Legal/ECT-es.pdf
Le Traite sur la Charte de l'Energie et documents connexes", Consolidated text. Accessible at:http://www.energycharter.org/fileadmin/DocumentsMedia/Legal/ECT-fr.pdf RL-0007.

[543] "Trattato Sulla Carta Dell'energia e documenti correlati", page 7, RL-0008. Accessible in: http://www.energycharter.org/fileadmin/DocumentsMedia/Legal/ECT-it.pdf. RL-0008.

[544] "Der Vertrag Über Die Energiecharta und dazugehörige Dokumente", page 9, RL-0009. Accessible at http://www.energycharter.org/fileadmin/DocumentsMedia/Legal/ECT-de.pdf . RL-0009.

[545] Memorial de Demanda, par.684.

833. Below, it will be argued and demonstrated that the Respondent has not incurred IN any of the failures to comply cited by the Claimants, although in a different order than the one chosen in the Memorial on the Merits. We will analyse, first of all, the supposed violations of article 10.1 of the ECT (including the so-called "umbrella clause") and subsequently, those concerning article 13 on the subject of expropriation, so as to follow the order established by the ECT.

(2) Regulations that apply for resolving the dispute

834. Before beginning the analysis of these questions, we express our agreement with the Claimant's statement that, in accordance with articles 42.1 of the ICSID Agreement and 26.6 of the ECT, the present dispute should be resolved pursuant to the ECT and other regulations of International Law that apply.[546]

835. For its part, Spanish national law will have to be taken into account, not only to evaluate the supposed commitments assumed by the Respondent, but also[547] to determine what expectations could objectively be formed by the Claimant based on Spanish law, which obligations have arisen under Spanish law that might be protected by the umbrella clause and which assets could be considered as expropriable.

J. The Kingdom of Spain has respected the standard of Fair and Equitable Treatment of Article 10.1 of the ECT.

(1) Introduction.

836. The Claimants state that the measures adopted by the Kingdom of Spain involve a violation of the standard of Fair and Equitable Treatment of article 10(1) of the ECT. Thus, the Memorial on the Merits states that the following elements of this FET standard have been violated: (1) protection of the Legitimate Expectations of investors, (2) prohibition of arbitrariness and duties of transparency and due process by approving the measures being challenged.[548]

837. To determine the meaning of the FET, the Claimants understand that the objective and purpose of the ECT should be considered[549.] We agree with this statement and, therefore, unlike the Claimants, who have omitted any explanation in this respect, we have analysed the objective and purpose of the ECT in the preceding part of this document, to which we refer.

838. However, we do not share with the Claimants the idea that the FET of the ECT is an "autonomous standard separate from the minimum requirements in international common law and that goes beyond them"[550.] As we have also explained in the preceding section, the maximum objective aimed at by the ECT is to achieve national treatment of foreign investors, unless this is less favourable than the minimum standards of international law, in which case the latter will apply.

[546] Memorial on the Merits, paragraphs 687 and 688.
[547] Memorial on the Merits, paragraph 689.
[548] Memorial on the Merits, paragraphs 859 and 868.
[549] Memorial on the Merits, paragraph 866.
[550] Memorial on the Merits, paragraph 862.

839. In any case, the Claimants have the burden of proof of accrediting that the measures adopted violate the FET standard of the ECT. Thus, the Tribunal recently declared in the Electrabel Case:

> *"The Tribunal starts with the premise that it is Electrabel which bears the burden of proving its case under the ECT's FET standard."*[551]

840. This same Tribunal pointed out, paraphrasing the reasoning of the Court in the Saluka v Czech Republic Case and that of Arif v Moldova, that:

> *"(...) the Tribunal considers that the application of the ECT's FET standard allows for a balancing exercise by the host State in appropriate circumstances. The host State is not required to elevate unconditionally the interests of the foreign investor above all other considerations in every circumstance. As was decided by the tribunals in Saluka v Czech Republic and Arif v Moldova, an FET standard may legitimately involve a balancing or weighing exercise by the host State."*[552]

841. Below it will be demonstrated that the Kingdom of Spain has not violated the FET standard contained in the ECT, as this standard has been interpreted by the Courts of Arbitration that have applied it. For this purpose, we will follow the order laid down by article 10.1 of the ECT.

(2) The Kingdom of Spain has not violated the Legitimate Expectations of the Claimants.

(2.1) Claimant's Approach

842. To determine that the Kingdom of Spain has violated their legitimate expectations, the Claimants have set out the following arguments in their Memorial on the Merits.

1. They first of all explain the concept of legitimate expectations in general and state that the commitments, promises or guarantees on which they are based may be included in national legislation regarding the regulatory framework that applies to a specific economic sector.[553] Furthermore, they understand that the legitimate expectations "*may be linked to what is generally termed as 'regulatory stability*"[554], an idea that, according to the Claimants, is especially relevant in the context of the ECT, given that it obliges the contracting parties to create "*stable conditions*" for investors.[555] According to the Claimants: "*An investor is entitled to expect that the regulatory framework will remain stable and consistent and, hence, legitimate expectations may also be breached by infringing the implicit requirement for stability and consistency".*[556]

[551] *Electrabel S.A. v. Hungary* (ICSID Case No. ARB/07/19), Award 25 November 2015, paragraph 154. RL-0048.
[552] Ibid, paragraph 165
[553] Memorial on the Merits, paragraph 872.
[554] Memorial on the Merits, paragraph 874.
[555] Memorial on the Merits, paragraph 876.
[556] Memorial on the Merits, paragraph 887.

2. The Claimants base their alleged legitimate expectations on the supposed promises, commitments and guarantees contained, according to them, in the following instruments: a) Royal Decree 661/2007 and definitive registration with the RAIPRE; b) the press release dated 25 May 2007 on the approval of RD 661/2007; f) the supposed agreements with the CSP and wind power subsectors and the official press release of 2 July 2010; g) RD 1614/2010 together with the official press release of 3 December referring to its approval and the press release of 3 December 2010; h) RD-Law 14/2010 and the press release of 23 December 2010 following its approval; i) RD-Law 1/2012 and the press release of 27 January 2012 concerning its approval.[557]

3. The Claimants then sustain that the stability generated both by the conditions set out in the so-called Regulatory Framework No. 1 and by the numerous promises and commitments mentioned above were "*determining factors in the Claimants' decision to invest in Spain*"[558]. They add that this uncertainty is particularly important in the case of investments which, like those of the Claimants, are financed though "Project finance"[559]. In short, according to the Claimants, all of the circumstances occurring at that time (Spain's membership of the OECD and the EU, development of the various Renewable Energy Plans and resolute willingness of the various governments to promote renewable energies), made it reasonably possible for any investor to think that the so-called Regulatory Framework No. 1 would remain stable.[560]

4. Finally, the Claimants consider that the Respondent violated their supposed legitimate expectations as a result of the subsequent approval of what it calls "*Regulatory Framework No. 2*" and "*Regulatory Framework No. 3*". The Claimants understand that: "*The numerous and persistent changes made to Regulatory Framework No. 1 since December 2012 breached the Claimants' legitimate and reasonable expectations that the regulatory framework existing at the time of the investment would remain stable and consistent over time, in accordance with the representations, commitments and promises made by the Respondent*"[561] and that they do not offer any future regulatory stability.

843. Below, the Kingdom of Spain will prove, first of all, that it has not violated the legitimate expectations of the Claimants at the time of making their investment, in accordance with the criteria contained in the arbitration awards that have applied the ECT.

844. Secondly, there will be a separate analysis of why the Kingdom of Spain has not violated the obligation of providing "stable conditions" as stated in the ECT.

(2.2) General considerations about the legitimate expectations protected by the ECT.

845. To determine whether a violation of the FET standard has taken place, the legitimate expectations that the Claimants had concerning the treatment that would be given to their investment at the time of making it should be assessed. Such expectations should be reasonable and objective in respect of the existing regulatory framework. As part of this assessment, the investors' knowledge of the regulatory framework on making their

[557] Memorial on the Merits, paragraphs 889 to 908.
[558] Memorial on the Merits, paragraph 909.
[559] Memorial on the Merits, paragraph 910.
[560] Memorial on the Merits, paragraph 913 to 924.
[561] Memorial on the Merits, paragraph 925.

investment should be analysed or, in other words, what their knowledge should have encompassed.

846. International arbitration case law is clear in this respect. When it comes to making their investment, an investor should know and understand (i) the regulatory framework, (ii) how it is applied and (iii) how it affects their investment. An investor makes an investment based on this knowledge and should be aware of the risks assumed on making the investment.

847. In this respect, the clarifying Award in Invesmart v. Czech Republic can be cited:

> *"for the Tribunal, the test of whether such an expectation can give rise to a successful claim at international law is an objective one. It is not enough that a claimant have sincerely held an expectation; the expectation must be reasonable and the Tribunal must make the determination of reasonableness in all of the circumstances. If the expectation was unreasonable (for example, ill-informed or overly optimistic), it matters not that the investor held it and it will not form the basis for a successful claim."*[562]

848. There is already a relevant number of arbitral precedents that have applied the standard of Legitimate Expectations contained in the ECT. Among the existing precedents, it is worth mentioning the following characteristic notes, from which a basic principle is derived: the ECT is not some kind of insurance policy in favour of the investor against the risk of changes to the regulatory framework and, therefore:

a) There must be *specific commitments* made to *an investor* that the regulations in force will remain unchanged. Thus, it was declared in the *Plama Case*[563] and this has been ratified by other precedents of the ECT, such as the *AES Summit*, *EDF* and *Charanne* Cases[564].
b) The investor's expectations have to be reasonable and justified in relation to any changes to the laws of the host country[565].

849. The Precedent Electrabel v Hungry, states concerning the diligence of investors that:

> "*Fairness and consistency must be assessed against the background 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"*[566].

[562] *Invesmart B.V. v. Czech Republic* (UN-0036-01) Award of 26 June 2009, paragraph 250. RL-0047.
[563] *Plama Consortium Limited v. Republic of Bulgaria, ICSID Case No. ARB/03/24, Award of 27 August 2008, paragraph. 219 "the Tribunal believes that the ECT does not protect investors against any and all changes in the host country's laws. Under the fair and equitable treatment standard the investor is only protected if (at least) reasonable and justifiable expectations were created in that regard. It does not appear that Bulgaria made any promises or other representations to freeze its legislation on environmental law to the Claimant or at all." (emphasis added)* .RL-0034.
[564] *Cases Charanne B.V. v. Spain, paragraph 499 (RL-98), EDF v. Romania, paragraph 217 (RL-0055) and AES Summit v. Hungary,* paragraph 9.3.29. RL-0049.
[565] *Plama Consortium Limited v. Bulgaria,* paragraph 219. RL-0034.
[566] Award in *Electrabel S.A. v. Hungary* (ICSID No. ARB/07/19) 25 November 2015, paragraph 7.78. RL-0048.

850. In the specific case of the measures adopted by Spain in the renewable energy sector, the Award in Charanne v. the Kingdom of Spain on 21 January 2016 clearly states that:

> *"The determination of whether the investor's legitimate expectations have been defeated must be based on an objective standard or analysis. The mere subjective belief that the investor could have had at the time of making the investment does not suffice. [...]*
>
> *the Arbitration Tribunal agrees with the Respondent, which claims that "in order to rely on legitimate expectations, the Claimants should have conducted a diligent analysis of the legal framework applicable to their investment"*[567].

851. And it adds that:

> *"To the Tribunal's understanding, at the time of making the investment in 2009 the Claimants could have carried out an analysis of their investment's legal framework in Spanish law and understood that the regulations enacted in 2007 and 2008 could be modified. At least that is the degree of diligence that could be expected from a foreign investor in a heavily regulated sector like the energy industry. In such a sector, thorough prior analysis of the legal framework applicable thereto is essential to make an investment."*[568]

852. An investor that had made a preliminary and exhaustive analysis of the legal framework applicable to the renewable energy sector, explained in the statement of facts in this document, was aware, or should have been aware that this Regulatory Framework had the following basic principles:

(1) It is included in a regulatory system governed by the *principle of regulatory hierarchy* and it is the result of the legally stipulated procedures for drafting regulations, as explained in section IV.A. (1) of this statement.
(2) The applicable regulatory framework is not limited to RD 661/2007 and to RD 1614/2010, as stated by the Claimants, but it is based on Act 54/1997, the Renewable Energy Plans and the norms implementing the Act 54/1997, supplemented by the Case Law of the Supreme Court, as explained in section IV.D of this statement.
(3) The SR subsidies are a SEE cost subordinate to the principle of its *economic sustainability*, pursuant to what is stated in section IV.A (3) of this statement.
(4) Remuneration of the SR consists of receipt of a subsidy which, added to the market price, provides renewable energy plants with *reasonable profitability*, in accordance with the capital market and on the investment costs of standard facilities. This subsidy should not necessarily be received throughout the entire operational life of facilities which, like those of the Claimants, have already achieved *reasonable profitability*. This has been described in Sections IV.E and G of this document.
(5) This principle of reasonable profitability imposes a *dynamic and balanced* nature on the renewable energy remuneration regime, as the case law of the Supreme Court

[567] Award in the case of Charanne B.V. and Construction Investments S.A.R.L v. the Kingdom of Spain, 21 January 2006, paragraphs 495 and 505. RL-0049.
[568] Ibid.

was establishing for a long time before the Claimants made their investment, under the terms set out in Section IV. D of this statement.

(6) Premiums are determined based on the evolution in demand and other basic economic data, laid down in the Renewable Energy Plans. Once again, this principle is set out in section IV.E of this statement.

(7) The *motivation* behind different regulatory changes in the renewable energy remuneration regime, including those that occurred prior to the investment of the BayWa RE, was (i) either to correct situations of over-remuneration, (ii) or due to major changes to economic data that served as a basis for the initial configuration of the premiums. Furthermore, we refer on this matter to sections IV.E, F and G of this statement.

(8) Neither RD 661/2007 nor RD 1614/2010, nor RD-Law 14/2010 nor RD-Law 1/2012, which apparently created the legitimate expectations of the Claimants, contain a guarantee or promise to set the regime in stone in favour of the Claimants, as described in section IV.E of this statement.

853. These basic principles constitute the objective legitimate expectations of a diligent investor. Therefore, no diligent investor could expect that, if there is a situation of deficit or economic imbalance that affects the sustainability of the SEE, the Spanish government would not adopt measures in order to address this. As has been accredited, the leitmotif inherent in all measures has been to guarantee the economic sustainability of the SEE and correct situations of excess remuneration.

854. The attention of the Arbitral Tribunal is drawn to an obvious fact. The relevance of the case law of the Supreme Court in the configuration of the Legitimate Expectations of an investor is declared in the Charanne Case Award[569]. However, the Claimants invoke the Supreme Court in their Statement in a completely biased manner to defend the existence of the supposed agreement between the Government and the wind power and solar power subsectors in 2010[570]. They thus omit the interpretation that the Supreme Court made in respect of the rights of investors in renewable energies in Spain since 2005 in over a hundred judgements.[571]

855. This constant case law was resumed in 2016 by the Supreme Court in the judgements delivered regarding the legal compliance of RD 413/2014 and Order IET/1045/2014:

> *"this Court has repeatedly insisted, in the face of successive regulatory amendments, that is was not possible in the future for owners of electrical energy production facilities under the special scheme to retain a "non-modifiable right" to keep the remuneration framework approved by the holder of the regulatory authority unaltered, as long as the prescriptions of the LSE regarding the reasonable profitability of the investments are respected."*[572]

[569] Award in the case of Charanne B.V. and Construction Investments S.A.R.L v. the Kingdom of Spain, 21 January 2006, paragraphs 506 to 508. RL-0049.
[570] Memorial on the Merits, paragraphs 363 to 365.
[571] This Case Law is explained in section IV.D of this statement.
[572] Amongst many others; the Judgement of the Supreme Court of 1 June 2016, 1260/2016 (Appeal 649/2014). R-0149.

856. Thus, the Supreme Court of the Kingdom of Spain has considered, as with the award handed down in the Charanne case, that no investor may have the legitimate expectation of the freezing of what the Claimants call Regulatory Framework No.1.

857. It is inexcusable for the Claimants not to have known and to have ignored this case law in order to configure their Expectations.

858. Consequently, the alleged violation of their legitimate expectations by the Kingdom of Spain should be dismissed, given that the understanding of the regulatory framework by the Claimants has been incorrect, as has been demonstrated.

(2.3) The Claimants may not have the legitimate expectation of the freezing of a specific renewable energy remuneration regime

859. None of the regulations, press releases or documents cited by the Claimants contain any specific commitments to freeze a specific remuneration regime.

860. As it has recently been stated by the Supreme Court, using the doctrine of the Constitutional Court, on delivering a judgement on the legal compliance of RD 413/2014 and Order IET/1045/2014:

> *"In this case, there is of course no type of commitment or external sign, or at least none is invoked in the claim, made by the Administration to the appellants in relation to the immutability of the regulatory framework in force at the time of the start of their activity of generating energy from renewable sources.*
>
> *Nor do we consider that the system in place at that time could be considered -in itself- as an external sign conclusive enough to generate legitimate trust in the appealing party, i.e. the rational and reasoned belief that the electrical energy remuneration regime that it produced could not be altered in the future, since no provision of RD 661/2007, which applied to their facilities, guaranteed that the regulated tariff would remain unchanged.*
>
> *In this respect, the case law of this Court has been constant throughout the years by stating, in the interpretation and application of the regulations governing the legal and economic system of production of electrical energy from renewable sources, that they guarantee the owners of these facilities the right to reasonable profitability of their investments, but they do not recognise their immutable right for the regulatory framework approved by the holder of the regulatory power to remain unchanged (...)".*[573]

861. In view of what has been stated, it is obvious that the regulatory framework existing at the time when the Claimants made their investment allowed regulatory changes to be made to existing facilities, always maintaining the principle of reasonable profitability.

862. Despite the fact that the firmness with which the definitive interpreter of the Spanish legal system has expressed itself would be sufficient to dismiss the Claimants' arguments,

[573] Amongst many others; the Judgement of the Supreme Court of 1 June 2016, 1260/2016 (Appeal 649/2014). R-0149.

we will demonstrate, below, the absence of specific commitments in each of the regulations and other documents invoked by the Claimants as elements giving rise to their legitimate expectations.

(a) Lack of commitments as a result of the definitive registration with the RAIPRE.

863. The Claimants sustain that through definitive registration with the RAIPRE:

> *"a particular relationship was already "perfected" with the Administration: the installation acquired a specific right to benefit from the economic regime offered by RD 2818/1998 (subsequently, RD 436/2004 and RD 661/2007) only after having applied and being authorized in the Special Regime by the Administration, as a result of accrediting that it had installed the required energy production equipment and met the conditions established by the governmental regulations."*[574]

864. However, and as has been explained in the part of this Memorial concerning the facts, the entry in this administrative register was an obligation imposed on all facilities, both Ordinary and Special Regime[575]. The RAIPRE is merely a section of said administrative registry, the section two[576]. This obligation to register already existed under RD 2366/1994.

865. Recording in this registry was therefore not a commitment by the state to indefinitely maintain the future profitability of the facilities recorded therein, rather a way to control and know who was participating in the SEE. The purpose of this administrative registry was therefore to facilitate appropriate monitoring of compliance with the energy planning objectives.

866. In this respect, the Supreme Court of the Kingdom of Spain has made it clear that there is no link between the right to receive the subsidies and recording in the RAIPRE, which is mandatory for all facilities:

> *"the fact that a specific photovoltaic facility does not meet the conditions required for collecting the premium does not mean, per se, that it is no longer a special regime facility. Under this condition, it can still remain on the corresponding registers and legitimately operate in the market (as we already stated as recognised by the Royal Decree itself), obviously without the benefits derived from availing itself of the most favourable premium regime".*[577]

867. In this respect, the Award in the Charanne case rejected that recording in this administrative registry generated any type of commitment of the Kingdom of Spain to the investor.

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[574] Memorial on the Merits, paragraph 894.

[575] Act 54/1997 of 27 November 1997, on the Electricity Sector. Article 21: "[...] 4. An Administrative Registry of Electrical Energy Production Facilities is created at the Ministry of Industry and Energy [...] 5. Recording in the Administrative Registry of Electrical Energy Production Facilities will be a necessary condition to be able to participate in the electrical energy production market in any of the contracting modes with physical delivery.6. [...] Compliance with the conditions and requisites laid down by authorisations or a substantial variation in the budgets that determined the granting thereof could give rise to the revocation thereof, under the terms provided for in the applicable penalty scheme. [...]". R-0079.

[576] RD 661/2007, article 9.1 R-0101

[577] Judgement of the Supreme Court of 30 March 2012 (app. 1/432/2010). R-0228

> *"509. In this regard, the Claimants have submitted that according to the existing regulatory framework, registration on the RAIPRE granted energy producers a vested right to receive the tariff, which provided a legitimate expectation that it would not be subsequently modified. The Tribunal does not agree with this argument.*
>
> *510. Firstly, the Respondent has convincingly proved that, under Spanish law, registration with the RAIPRE was a mere administrative requirement in order to be able to sell energy, and by no means implied that registered facilities had a vested right to a certain remuneration. Secondly, the existence of legitimate expectations has to be analysed on the basis of international law, not under domestic law. However, as has been stated in prior sections of this award, in the absence of a specific stability commitment, an investor cannot have the legitimate expectation that a regulatory framework like the one disputed in this arbitration would never be modified in order to adapt it to market needs and the public interest.*
>
> *511. Therefore, the Tribunal concludes that the Claimants could not have the reasonable expectation that RD 661/2007 and RD 1578/2008 were not going to be modified during the lifespan of their facilities."*[578]

868. Furthermore, even if, for dialectical purposes, we were to follow the argument of the Claimants, we have to bear in mind that their wind farms obtained, according to the Memorial on the Merits, definitive registration with the RAIPRE on 5 December 2002.[579] This did not prevent the Claimants' wind farms from being affected by the changes introduced by RD 436/2004, RD-Law 7/2006, RD 661/2007, RD-Law 6/2009 and RD 1614/2010. It makes no sense to allege that registration of the wind farms with the RAIPRE could shield them from the amendments introduced by the measures that are the subject of this arbitration.

(b) Lack of existence of commitments in the regulations invoked by the Claimants:

(i) Lack of existence of specific commitments in RD 661/2007 and in its press release of 25 May 2007 that its remuneration regime would remain unchanged.

869. The lack of existence of commitments in RD 661/2007 regarding the immutability of its regime in favour of the Claimants has already been accredited in the part of this Memorial concerning the Facts[580]. This lack of existence of a commitment has been expressly corroborated by the Court in the Charanne Case, which examines the Legal Framework existing in the Electricity Sector in Spain in 2007 and 2008.

> *"503. In this case, the Claimants could not have the legitimate expectation that the regulatory framework laid down by RD 661/2007 and RD 1578/2008 would remain unchanged during the entire lifespan of their plants. Accepting such an expectation would, in fact, amount to freezing the regulatory framework applicable to eligible*

[578] Award in the case of Charanne B.V. and Construction Investments S.A.R.L v. the Kingdom of Spain, 21 January 2006, paragraphs 509 to 511. RL-0049.
[579] Memorial on the Merits, paragraph 169.
[580] See section IV.E.(6) of this document.

plants, even though the circumstances may change [...] The Arbitration Tribunal cannot accept such a conclusion. [...].

504. The conclusion drawn by the Tribunal, i.e. that in the absence of a specific commitment the Claimants could not reasonably expect that the applicable regulatory framework provided in RD 661/2007 and RD 1578/2008 would remain unchanged, is backed by case law from the highest courts in Spain. Prior to the investment, these courts had clearly established the principle that domestic law could modify the regulations in force.

505. [...] However, in the present case the Arbitration Tribunal considers that the Claimants could have easily foreseen the possibility that the regulatory framework was going to be modified, (…). Indeed, Spanish law left wide open the possibility of modifying the remuneration scheme applicable to photovoltaic energy [...]

511. Therefore, the Tribunal concludes that the Claimants could not have the reasonable expectation that RD 661/2007 and RD 1578/2008 were not going to be modified during the lifespan of their facilities."[581]*. (Emphasis added)*

870. This award has corroborated, as a result, that RD 661/2007 did not contain any promise or guarantee of freezing of its regime, neither (i) the remuneration regime nor (ii) the operating regime regarding the hours of years of subsidised operation nor (iii) with respect to the tariff update regime. No diligently informed investor could expect this freezing in their favour due to meeting the regulatory requirements for obtaining the subsidies.

871. Furthermore, it should be remembered that RD 661/2007 was introduced to guarantee the economic sustainability of the SEE, consolidating the untying of the update of the premiums and tariffs according to the TMR, in order to avoid situations of excess remuneration.

872. The proof that RD 661/2007 involved a cut in the remuneration that wind power producers had been receiving comes from the fact that the great majority of them opted to remain in the option of market plus premium under RD 436/2004, which was temporarily allowed by RD 661/2007, although with the premium frozen. According to the AEE:

"In the seven months in which the new RD 661/2007 has been in effect, the premium has been €5,07/MWh lower than that of RD 436/2004. All facilities have remained under RD 436/2007 with an average remuneration of €77.62/MWh throughout 2007, given that if they had changed to RD 661/2007, it would have been €74.11/MWh."[582]

873. Therefore, nothing prevented RD 661/2007 from repealing RD 436/2004, which contained an article 40.3 with wording which, according to the producers, was much more protective of the remuneration conditions set out in said RD 436/2004. In fact, the AEE considered that RD 661/2007 implied that an "*increase in the discretion supposed by future*

[581] Award in the *case of Charanne B.V. and Construction Investments S.A.R.L v. the Kingdom of Spain*, 21 January 2006, paragraphs 504 to 508. RL-0049.
[582] AEE Press Release of 10 January 2008, *Remuneration of wind power in 2007 fell to2003 and 2004* levels. R-0163.

developments in wind power will depend on the Government's willingness expressed each time in the reviews of the remuneration".[583]

874. While RD 661/2007 did lack commitments for freezing a specific remuneration regime, the press release issued by the Ministry of Industry on 25 May 2007[584], which merely gave a summary of the contents of this regulation, could not contain more commitments than those incorporated in RD 661/2007: i.e. none. Merely reading the press release makes it possible to ascertain that it does not contain any promises to freeze the remuneration framework. In fact, what it says is that:

> *"It will be in 2010 that the tariffs and premiums set out in the proposal will be reviewed in accordance with the achievement of the objectives set in the 2005-2010 Renewable Energies Plan and in the Energy Saving and Efficiency Strategy and in accordance with the new objectives included in the next Renewable Energies Plan for the 2011-2020 period."*[585] *(Emphasis added)*

875. In any case, the Claimants have not substantiated that their investments in 2003, 2009, 2011 and 2012 in the La Carracha and Plana de Jarreta wind farms were based on these alleged commitments. They could not have done so because the annual accounts of the Claimants' wind farms for 2007 state that: *"(...) we are awaiting a change to the regulations that govern the sector and therefore we are unaware at the moment of the impact that this regulation may have*".[586] This statement is maintained in the annual accounts corresponding to 2008. It does not therefore seem that the Claimants' wind farms were relying at this time on the freezing of the remuneration regime contained in RD 661/2007.

876. Nor does it appear that the Claimants had this trust in the fact that the remuneration regime under RD 661/2007 would not be modified, in view of the exchange of emails between BayWa ER, Renerco and Shell in June 2008:

> *"Considering it came from the AEE, I was expecting there would be updates in there on the Eolica tariffs (group b.2.1), however skimming through it I now see that is not the case. I am not sure however if the govt sneaked in some other tariff revision or cost like they did when announced RD661 the last time"*[587] *(Emphasis added)*

877. Additionally, events after both RD 661/2007 and its official press release and immediately prior to the Claimants' investments of 2009, 2011 and 2012 highlighted the lack of freezing of a specific remuneration regime.

(ii) Lack of existence of specific commitments of freezing of the remuneration regime of RD 661/2007 in RD 1614/2010, in the supposed agreement reached on its draft version and in the press release related to the latter.

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[583] AEE press release dated 29 May 2007 on the rather negative appraisal of 661/2007. This did not contain its proposals. C-0322.
[584] Official Press Release dated 25 May 2007. C-0094.
[585] Official Press Release dated 25 May 2007, p. 1. C-0082
[586] Document number 2 accompanied by expert's report CER-0002.
[587] Emails exchanged between BAYWA, RENERCO and Shell between 18 and 20 June 2008. C-0305.

878. The Claimants rely on RD 1614/2010 to defend the strengthening of the commitments supposedly assumed by RD 661/2007 regarding the freezing of the remuneration regime contained therein. In fact, according to the Claimants, the existence of this Royal Decree, which was the result of a supposed agreement between the Government and the wind and solar power sectors, is what makes it possible to distinguish their case from the case judged by the Charanne case award.[588]

879. However, as has already been studied in the facts and revealed in its economic report, RD 1614/2010 was enacted by the Government to guarantee the economic sustainability of the SEE. In addition, its articles 4 and 5 merely extended article 44.3 of RD 661/2007, which is analysed in section IV.E of this Statement, to certain wind and solar power facilities as a result of the entry into force of RD-Law 6/2009[589] and the Agreement of the Council of Ministers of 13 November 2009590. These regulations have been deliberately omitted from the Memorial on the Merits but they were introduced, as has been explained in section IV.E, to guarantee the economic sustainability of the SEE.

880. As set out in the Preamble of RD-Law 6/2009:

> *"The increasing tariff deficit, in other words, the difference between the collection from the regulated tariffs set by the Administration and paid by consumers for the regulated supplies and by the access tariffs that are set in the deregulated market and the real costs associated with these tariffs, is causing serious problems which, in the current context of the international financial crisis, is deeply affecting the system and putting at risk, not only the financial situation of the companies in the electricity sector, but also the very sustainability of the system. This imbalance is unsustainable and has serious consequences on impoverishing the security and capacity of financing the investments required for the supply of electricity at levels of quality and security required by Spanish society.*
>
> *To finance this deficit, which will be transferred to future generations through the recognition of long term collection rights, various measures have been adopted that in the current economic situation of the financial markets have proved to be insufficient.*[591] *" (emphasis added).*

881. Indeed, the publication of RD-Law 6/2009 was not correctly appraised by the AEE, which denounced "*the risk of thousands of job losses in the wind power sector through the paralysation of the sector caused by the creation of the Pre-Allocation Register (RD-Law 6/2009 of 6 May 2009) and its resolution*."[592] The documentary proof provided by the Claimants shows that:

[588] Memorial on the Merits, paragraph 890.
[589] Royal Decree-Act 6/2009, of 30 April, which adopts certain measures in the energy sector and approves the discount rate.R-0088.
[590] Agreement of the Council of Ministers of 13 November 2009. R-0116
[591] Preamble of RD-Law 6/2009. R-0088.
[592] News item about the appraisal conducted by the AEE of the enactment of RD-Law 6/2009. R-0229.

"... from 2009 the regulations on renewable energies began to be restrictive. The new warhorse was the tariff deficit".[593]

882. This was the situation that existed when BayWa RE invested in Spain in November 2009. In fact, the Project Nova presentation on 18 August 2009 regarding the potential purchase by BayWa Green Energy GmbH of RENERCO foresaw, within the possible risks of the vendor's business area, inter alia: a) a fall in the demand for electricity for facilities that generate renewable energy and b) a change in the legal conditions such that interests in certain regions or business lines were not attractive. These risks were naturally accepted and understood to be mitigated by investment in different regions and technologies[594]:

4

Risks within the Business Areas

Segment	Possible Risks	Risk
Price changes	- Changes in the prices of hardware components and delivery times - Weakening of the general demand for electricity from installations that generate renewable energy - Availability of project financing - Risk of the failure of individual project developments and of cost overruns for turnkey projects - Changes in legal conditions so that Nova's commitments in individual regions or lines of business become unattractive	Medium to high
Power generation	- The main risk is in the wind level and the irradiation values in the solar area for the relevant periods - Based on readily foreseeable and uniform business performance, funding requirements and return flows from investments are easy to plan for. The compensation models (such as the Renewable Energies Act) make an important contribution to this	Low
Services	- Payment difficulties on the part of project companies constitute a serious risk, and Nova may feel compelled to terminate the long-term contractual relationships - This is a very manageable risk because consulting and support contracts are long-term; moreover, most of the contracts have minimum compensation provisions	Low
Conclusion	Risks can be well-diversified and further reduced by investing in various technologies (wind, solar, etc.) and regions (Germany, Spain, France, Poland, Czech Republic, etc.)	

883. This situation, which existed when BayWa made its first investment in wind farms, has been overlooked by the Claimants. But the purpose of RD 1614/2010 only knowing about this situation can be understood. Its purpose was to extend the regime of RD 661/2007 to the facilities whose entry into operation was deferred until 2009 to guarantee the sustainability of the SEE. Therefore, RD 1614/2010 cannot contain commitments other than those contained in RD 661/2007, which, as has just been explained, did not exist.

884. The Claimants sustain that the Government press release dated 2 July 2010[595], which announced the consensus between the Government and the wind and solar power sectors about what the basic outline of the draft of RD 1614/2010 would contain, also constitutes a commitment to freezing the remuneration regime laid down by RD 661/2007 for investors.

[593] J. López-Tafall, "Wind power, a success story without a happy ending?", Cuadernos de Energía, No. 41, 2013, pp. 108-112. C-0157.
[594] Presentation entitled Project Nova, Potential Acquisition in the Area of Renewable Energies. C-0099.
[595] Official Press Release dated 2 July 2010. C-0152.

885. However, the above-mentioned press release merely informed about the query procedure prior to RD 1614/2010 which, as we have just seen, did not contain any commitment to freeze the remuneration regime of RD 661/2007.

886. Therefore, what the press release showed was that: (i) the situation existing at that time made it necessary to introduce changes to the economic regime established by RD 661/2007 to guarantee the sustainability of the SEE; (ii) both the Government and the system operators were aware of this need; (iii) nothing would prevent new cutback measures from being adopted if the objectives of elimination of the deficit by 2013 were not achieved or if a change to the basic economic circumstances led to an imbalance of the SEE.

887. In fact and after the supposed agreement, the AEE, in its allegations on 2 August 2010 before the CNE, during the procedure followed for approval of RD 1614/2010, reflected a clear understanding of the SEE and of the limits on the regulatory power of the State:

> *The proposed modification to the reactive energy remuneration regimen, if approved, would be retroactive, which, according to Constitutional Tribunal case law, can be considered "minimum grade", as it only has an impact on the economic effects that will occur in the future, even if the basic relationship or situation has arisen as above. It is true that, in relation to these types of retroactive modifications, that the supreme court has declared that there is no "unmodificable right" to the economic regimen remaining unchanged and that "the prescriptive content of Act 54/1997, of 27 November, on the Electrical Sector, neither leads to the setting in stone, or freezing of the remuneration regimen for owners of special regimen electrical energy facilities, nor the non-modificability of this regimen", thus recommending a relatively broad margin to the "ius variandi" of the Administration in a regulated sector in which general interests participate. Now, notwithstanding the foregoing, case law has established limits to this "ius variandi" of the Administration regarding the retroactive modification of this remuneration framework, particularly "the prescriptions of the Electrical Sector Act should be respected regarding reasonable profitability of investments."*[596] *(Emphasis added).*

888. Despite the supposed agreement reached one month earlier, the AEE recognised that the only limit on the ius variandi of the Administration lies in compliance with "*the requirements of the Electricity Sector Act regarding the reasonable profitability of the investments.*"

889. Meanwhile, the official press release of 3 December 2010 concerning the immediate publication of RD 1614/2010597, invoked by the Claimants, does not contain promises of specific treatment other than that provided for in RD 1614/2010 to which it refers. As tautological as it is true.

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[596] Arguments of the AEE before the Electricity Advisory Board for the CNE on 30 August 2010. R-0166. In the same respect, there are other documents provided by the Claimant that show that wind power producers were aware that RD 661/2007 did not contain any regulatory freezing clause. Inter alia, documents C-0169, C-0172 (in which the case law of the Supreme Court on the limits of the Government's regulatory power is also cited) and C-0219 recognise the principle of reasonable profitability.

[597] CNE Press Release of 3 December 2010, C-0190.

890. Therefore, neither the supposed agreement of July 2010, nor its press release, nor the subsequent RD 1614/2010, nor its press release, could serve to legitimately raise in the Claimants the expectation that the remuneration regime contained in RD 661/2007 would remain unchanged throughout the entire operating life of the facilities.

891. Indeed, the Claimant has not accredited that it made its investment in the wind power sector by relying on these elements.

(iii) Lack of existence of specific commitments in RD-Law 14/2010 and its press release of 23 December 2010 on the freezing of the remuneration regime of RD 661/2007

892. It is surprising that the Claimants invoke RD-Law 14/2010 as a regulation that provided even more security in relation to the freezing of the remuneration system contained in RD 661/2007. Rather to the contrary, RD-Law 14/2010 showed that the measures introduced by the previous regulations, whether negotiated or not, had not been sufficient given the appearance of a series of new adverse circumstances.

893. This is shown by the official press release of 23 December 2010 invoked, surprisingly, by the Claimants to provide grounds for their expectations. It does not contain any guarantee of freezing of the remuneration system of RD 661/2007, but it shows that RD 1614/2010 is another "cost reduction" measure and it states that:

> *"The electricity sector is experiencing an exceptional economic situation caused by a sudden fall in the demand for electricity" (...) "The direct consequences of this situation have been a loss of revenue for system as a whole and, additionally, an increase in the total amount of the regulated costs due to the effect of the fall in demand. Since 2009 the Government has adopted a series of measures aimed at rationalising regulated costs and reducing the tariff deficit, among which is the approval of the Royal Decree in 2009 (...)".*[598]

894. The press release itself mentions, amongst the "measures to reduce the costs of the electricity system" that RD-Law 14/2010 incorporates the following: "*all electricity generation companies, both under the ordinary regime and that of renewable energies and cogeneration, will pay a toll of 0.5 euros/MWh.*"[599]

895. Therefore, neither the supposed agreement of July 2010 nor RD 1614/2010 prevented RD-Law 14/2010 from introducing, urgently, new measures to adjust the SEE that affected the economic rights of producers of renewable energies, including wind power, through the imposition of access tolls. These access tolls that the RE producers had to pay involved a reduction of their remuneration.

896. The speech given by the Minister for Industry (Mr Sebastián) in the Congress of Deputies, during the session held for validation of this RD-Law 14/2010 on 26 January, clearly revealed the purpose of this RD-Law 14/2010 (removal of the deficit) as well as the

[598] Press release from the Council of Ministers concerning, amongst other things, the approval of RD-Law 14/2010. C-0164.
[599] Ibid.

absence of any freezing of the remuneration regime in force following approval of RD 1614/2010. Thus, the Minister said:

> *"…since 2009, the Government has been working to adopt a set of measures whose common denominator is the streamlining of regulated costs and the reduction of the tariff deficit (…) All these measures have come about from dialogue, both with the sectors affected as well as with the main political forces. But these measures of 2009 and 2010 have not been enough. The imbalances have been accentuated as a consequence of the appearance of a series of adverse circumstances, in some cases exceptional, of which I should like to highlight two. Firstly, the above forecast growth of some of the regulatory costs during 2010, in particular the premiums of the special regime, and secondly, the evolution of electricity demand, which in 2009 fell by 4.7%. (...) This explains the need to urgently approve new measures (...)."*[600] *(Emphasis added).*

897. In other words, in January 2011 the Government made clear its need and determination to guarantee the economic sustainability of the SEE, which was endangered not only by the deficit accumulated, but also by an unusual fall in electricity demand.

898. The Claimants have not demonstrated, nor are they able to do so, that at this time they were able to legitimately believe in the freezing of the premiums and tariffs set out in RD 661/2007 for the entire life of the wind farms.

899. Furthermore, during 2011 not only had the Government announced its intention to carry out a reform of the renewable energies promotion regime but also, this reform was halted at the last minute as a result of the pressures brought to bear by the AEE, amongst others, since it was contrary to its interests. Thus the AEE itself expressly recognises this:

> *"There are two words that the wind power sector has been tirelessly repeating for the last two years: regulatory uncertainty. And 2011 has been no exception. (...).*
>
> *At the beginning of the year, the Socialist Party was in power in Spain and at the end the Popular Party. In the middle there was a regulatory battle that was hard fought and against the clock. (...).*
>
> *The year began with the approval by Congress of the Economic Sustainability Act. (...). Amongst other things, it established that three months after its approval a Renewable Energies Act should be presented, something that had long been called for by the sector. This never happened.*
>
> *In September and without any sign of the announced dialogue, the Ministry of Industry, Tourism and Trade (the former MITYC) sent the National Energy Commission (CNE) an urgent draft of the royal decree that was unacceptable for the sector, both in terms of model and regarding the economic conditions (...) The parameters proposed by the Government did not guarantee the reasonable profitability of the projects. (...).*

[600] Record of Proceedings of the Congress. Recognition of RD-Law 14/2010. R-0227.

> *The situation experienced was undoubtedly paradoxical: an Association whose purpose was to promote the wind power sector had to carry out intensive educational work with politicians, institutions and the media to stop a regulation that, on the other hand, the sector had been insistently calling for to fill a legal vacuum.*
>
> *On 20 November, a new Government was elected, without anyone knowing for certain what its stance was regarding wind power. However, the Executive did not take long to make clear what its priority was regarding energy: to put a limit on the tariff deficit which, by law, would have to stop increasing from 2013 (...)".*[601]

900. This situation, described by the AEE, highlights not only the lack of conviction in the wind power sector regarding a guarantee of freezing of a specific remuneration regime, but also the imminence of a regulatory change planned since 2011 and the new Government's priority to guarantee the sustainability of the SEE.

901. This was the economic and legal context that existed in September 2011 when Renerco acquired Shell's stake in the wind farms.[602] As a result, it is impossible for the Claimants to have legitimately believed that the remuneration regime of RD 661/2007 was going to remain unchanged.

(iv) Lack of existence of commitments in RD-Law 1/2012, of 27 January and in its official press release dated 27 January 2012

902. RD-Law 1/2012 was the first measure adopted by the new PP Government to recover the sustainability of the SEE. Thus, this regulation was urgently introduced given the insufficiency of the measures adopted in previous years to try to guarantee the sustainability of the SEE. According to its Preamble:

> *"Royal Decree-Act 6/2009, of 30 April, which adopts certain measures in the energy sector and approves the discount rate, established limits to restrict the increase in the tariff deficit (...).*
>
> *Afterwards, and as a result of the appearance of a series of circumstances that occurred, amongst others, the significant fall in demand in 2010 and the increase in electricity production from renewable sources (...) which had a significant effect on the parameters for forecasting the electricity system tariff deficit, new measures were urgently adopted by Royal Decree-Act 14/2010 to address the correction of the electricity system tariff deficit.*
>
> *However, the measures adopted to date have not been sufficient, putting at risk the ultimate target of removal of the tariff deficit by 2013"*[603] *(Emphasis added)*

[601] AEE Yearbook, Wind Power '12. Wind Power Business Association (AEE), the Industry Reference R-0230.
[602] Document C-0196.
[603] Royal Decree-Act 1/2012, of 27 January, which proceeds to the suspension of the remuneration pre-allocation procedures and the elimination of the economic incentives for new electric energy production plants based on cogeneration, renewable energy sources, and waste. R-0090

903. While it is true that this RD-Law 1/2012 does not affect the remuneration regime set out in the legal system for facilities in operation and for those that were recorded in the pre-allocation of remuneration register, in no case does it promise that other future regulations will not affect these facilities. In fact, its Preamble discusses the need for reform:

> *"It is necessary to design a new remuneration model for this type of technologies that takes account of the new economic scenario, promoting the efficient allocation of resources through market mechanisms (...). Furthermore, the new frameworks should encourage cost reduction making use of the learning curve and promoting the capture of maturity of technology so that they are charged back to consumers."*[604]

904. Furthermore, RD-Law 1/2012 showed the willingness and obligation of the Government to adopt any measures necessary to guarantee the sustainability of the SEE since, as stated in its Preamble:

> *"The tariff deficit constitutes in itself a barrier for the proper development of the sector as a whole and in particular the continuation of the policies for promoting electricity production from renewable and high-efficiency energy sources."*[605]

905. The Claimants invoke the press release following the approval of the RD of this RD-Law 1/2012[606] as fundamental for configuring their legitimate expectations. However, it is difficult for the Claimants to have based their expectations on a press release whose purpose was to announce the adoption by the Government of a series of measures for containing the public deficit and which came at a later date than the majority part of their investment.

906. The first measure announced by the press release was the Organic Law on Fiscal Stability and Financial Sustainability.[607] The second one was RD-Law 1/2012. The Ministry of Industry stated at the press conference that:

> *"(...) First of all, there is an unequivocal objective of the entire Government, which is, as Madam Vice-President stated, to reduce the public deficit and no Government policy is unrelated to this objective. In this respect, the energy policy is no exception.*
>
> *Spain currently has a potential electricity generation capacity of 106,295 megawatts (...). Peak demand does not exceed, does not even reach half of this installed capacity, insofar as it is rated at 38,287 megawatts. Therefore, it is obvious that we do not have a problem with production or generation or installed capacity.*
>
> *At the same time, Spain has accumulated a tariff deficit at year-end 2011 that is around twenty-four thousand million euros. As this is a problem, the most important thing is the pace of increase of this tariff deficit at an annual rate which, over the next few years, if we don't do anything, will be around three to four thousand million euros per year (...).*

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[604] Ibid.
[605] Ibid.
[606] Official Press Release dated 27 January 2012. C-0202.
[607] This was Organic Law 2/2012 of 27 April 2012 on Fiscal Stability and Financial Sustainability. R-0135

The Government therefore cannot remain impassive and the Government is not going to remain impassive. This is why this Royal Decree-Law has been drafted (...).

(...) the decision that has been adopted today through this Royal Decree-Act constitutes merely the first step, it is not an isolated measure; it is the first step in solving the problem of the accumulated tariff deficit but, at the same time, to slow down its growth rate (...)."[608] *(Emphasis added).*

907. Additionally, on the same day, 27 January 2012, the Government asked the CNE[609] to draft a report on the regulatory adjustment measures that might be adopted in the energy sector. After receiving over 400 pleadings from interested parties, the CNE issued Report 2/2012 "On the Spanish Energy Sector"[610] on 7 March 2012, the first part of which is dedicated to the "*Measures to Guarantee Economic-Financial Sustainability of the Electricity System*". The report stated the situation of unsustainability in the sector[611], and proposed a series of short-term and medium-term measures on all activities of the electricity sector, including renewable energies, which reflect the urgent need to make changes to the regimes.

908. Therefore, when on 12 March 2012 Renerco (later BayWa AH) acquired the Corporación Empresarial Pública de Aragón S.L. stake[612] in the La Carracha and Plana de Jarreta wind farms and in October BayWa ER acquired 12.2% of Renerco[613], the Claimants were fully aware of the problem of economic unsustainability that affected the SEE and the resolute intention of the Government of Spain to bring this problem to an end through measures which, within the limits set by the consolidated case law of the Supreme Court, might be necessary.

(2.4) The Kingdom of Spain has not violated the legitimate expectations that the Claimants might reasonably have had about the regulatory framework in which they invested.

909. As we have just demonstrated, the regulations, press releases and resolutions that the Claimants mention, as the basis for their expectations, do not contain any specific promise or commitment that the remuneration regime established in RD 661/2007 would remain frozen for the entire operating life of the facilities.

910. The regulatory framework existing at the time when the Claimants made their investment allowed regulatory changes to be made to existing facilities, always maintaining

[608] Official Press Release dated 27 January 2012. C-0202.
[609] Copy of the letter from the State Secretariat of Energy to the Chairman of the National Energy Commission of 27 January 2012. R-0193.
[610] Report on the Spanish Energy Sector Part I. Measures to guarantee the economic-financial sustainability of the electricity system, National Energy Commission, 7 March 2012. R-0131.
[611] The same issues would be declared by the European Commission in its document European Commission guidance for the design of renewable support schemes, Commission Staff Working Document, SWD (2013) 439 final, 5 November 2013. R-0200.
[612] Deed of sale of company shares between "Corporación Empresarial Publica de Aragón, Sociedad Limitada (vendor) and Renerco Renewable Energy Concepts Aktiengesellschaft" (purchaser), of 12 March 2012. C-0197.
[613] Memorial on the Merits, paragraph 285 and Informative Except from RENERCO (C-0074).

the principle of reasonable profitability. The guiding thread of these regulatory changes was motivated by the need to guarantee the sustainability of the SEE, derived from a considerable change to the basic economic elements and avoiding situations of excess remuneration contrary to the principle of reasonable profitability.

911. BayWa AH (formerly Renerco) is an investor that has been present since the promotion of the wind farms. The Claimants' wind farms were the first to be built in Spain. Therefore, Renerco has experienced all the changes to Spanish legislation regarding renewable energies since RD 2818/1998. Renerco must, neccessarilly, have been aware not only that these changes to the remuneration regime were possible, in accordance with the case law of the Supreme Court reiterated since 2005, but it also had to be aware of the leitmotiv behind all of these regulatory changes.

912. Meanwhile, BayWa R.E. (the first Claimant), when it invested in Spain at the end of 2009, could not legitimately have been unaware of the situation of unsustainability of the SEE nor of the Government's intention to adopt the legally required measures to recover the balance of the SEE. All of the measures adopted by the regulator since RD-Law 6/2009 have been governed by this same objective of guaranteeing the sustainability of the SEE and also of avoiding situations of excess remuneration.

913. It is worthy to note that, despite the regulatory indicators, the press releases[614] and the specific warnings of the Spanish Government regarding the need to reduce the deficit and the objectives of the reforms that were implemented to this effect[615], the Claimants are unaware of or underestimate the leitmotiv of the measures that were adopted and that will continue to be adopted until the ultimate objective is achieved: the sustainability of a balanced SEE.

914. In addition, the changes to this regulatory framework that are questioned in these arbitration proceeding were not only possible but they were also foreseeable. In the words of the Supreme Court:

> *"All of these elements of lack of commitment or conclusive external signs from the Administration in relation to the immutability of the regulatory framework, the existence of reiterated case law from this Court which has insisted that our legal system does not guarantee the immutability of the remuneration to owners of renewable energy production facilities, the situation of tariff deficit and threat to the viability of the electricity system and the achievement of the participation objectives of renewable energy prevent the change made to the renewable energy remuneration system from being considered as unexpected or unforeseeable by any diligent operator".*[616]

[614] C-0199, C-0200, C-0201, C-0180, C-0258, C-0259 and C-0316.

[615] PowerPoint Presentation from the Ministry of Industry, Tourism and Trade. C-0180, C-0182, C-0204. These objectives are included in the Report on the analysis of the regulatory impact of the draft Royal Decree which regulates and amends certain aspects concerning electricity production using solar energy and wind technologies (C-0265). Furthermore, the Government proposed to the rest of the parliamentary groups the adoption of an agreement on energy policy based on these objectives (C-0206).

[616] Amongst many others; the Judgement of the Supreme Court of 1 June 2016, 1260/2016 (Appeal 649/2014). R-0149.

915. We also wish to draw attention to various facts that are extremely relevant for the evaluation of the legitimate expectations of the Claimants by the Court.

916. First of all, according to the Claimants:

> *"The existence of certainty is particularly important in the case of investments which, as happens in the present case, are financed on the basis of project finance arrangements, which are repaid with the projected cash flows of the facility."*[617]

917. Therefore, both the project finance, signed in 2001[618], and its respective amendments, signed by La Carracha and Plana de Jarreta in 2006, are prior to all acts which, according to the Claimants, served as a basis for their legitimate expectations, with the exception of the registration of the wind farms with the RAIPRE. In other words, the project finance agreements were signed when RD 2818/1998 was in force and this did not contain any provision for freezing of the remuneration regime existing at the time nor did it contain many of the so-called six rights that the Claimants state were immutable. In fact, the existence of these Project Finance agreements did not prevent the wind farms from requesting and obtaining in 2005 the "modification of Economic Regime" in order to be included under the regime set out in RD 436/2004[619].

918. This happened because in the above-mentioned Project finance agreements it was naturally assumed that there was a possibility of a change to the remuneration regime. In fact, the concept of "total collections" was defined by the financing agreements in the following way:

> *"Total collections means all ordinary and extraordinary income and benefits received in relation to the ordinary operation of the Borrower's business, including but not limited to: a) Revenues derived from any electrical energy sale contract, revenues from the wholesale market, premiums regulated in accordance with the provisions of Spanish legislation that apply, regulated tariffs, revenues derived from the sale of certificates known as "renewables", environmental credits, green certificates or similar products that may be granted to the Borrower by the Spanish authorities (...)".*[620] *(Emphasis added).*

919. In other words, the financing agreements assumed that the remuneration method of the borrower could take on, non-exhaustively, any of the forms mentioned above. The sole condition imposed by the financing banks in the face of the possibility of a change in remuneration was as follows:

> *"27. If any change should occur in the current legislation in relation to the payment systems for energy produced by the Borrower as these are currently set forth in Act 54/97 and Royal Decree 2818/98 or any other system that may come to replace these in the future and provided the Borrower should be entitled to choose between the new system and that previously in force, the Borrower must request prior, written*

[617] Memorial on the Merits, paragraph 910.
[618] Documents C-0068 and C-0069.
[619] Document C-0079.
[620] Ibid.

> *authorisation from the Majority to proceed to change from the payment system it had been using to the new system. Said consent shall not be refused by the Majority without reasonable cause."*[621]

920. None of these provisions contained in the financing agreements were altered when the loans were extended in the year 2006, after the coming into force of RD 436/2004.[622] It was only added that:

> *"In the event that the new tariffs should be equal to or exceed those set out in the Base Case attached as Appendix I at that time, the aforementioned prior, written authorisation shall not be necessary but the Borrower will have to inform the Loan Agent of this fact at least ten (10) working days in advance (...)"*

921. Therefore, an act as essential for the Claimants as the financing of the wind farms took place in the year 2001 and was modified in the year 2006, with express acceptance of the possibility of the modification of the existing payment system, including through a reduction of the tariffs. This is despite the fact that RD 436/2004, valid when the financing was extended, already contained article 40.3 on the subject of the reviewing of premiums and tariffs, which the Claimants are invoking as the predecessor of article 44.3 of RD 661/2007, in the terms in which it was drafted following RD 1614/2010.

922. Secondly, the information booklet published in January 2001 to capture investors for the wind farms[623] estimated an internal rate of return of 6.98%.[624]

923. Thirdly, when BayWa AH (Renerco at the time) acquired an additional share in the projects in the year 2011, its parent company, BayWa AG, applied a discount rate of 6.8% to the cash flows expected to be generated by the wind farms.[625]

924. Therefore, the profitability the Claimants expected to obtain from their investment when they made it was just under 7%, coinciding with the reasonable profitability rate set out in PER 2005-2010 and with the reasonable profitability of 7.398% currently granted by the measures questioned in this arbitration case. This is evidenced by the documents corresponding to the Claimants' investment when this was made.

925. This is something that must be taken into consideration by the Arbitration Tribunal. Pursuant to the Award of Invesmart v. Czech Republic:

> *"a source of contemporaneous evidence of the investor's expectation can be the contractual documents by which it acquired its investment or otherwise dealt with the seller of the investment where it purchased an existing investment."*[626]

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[621] Ibid.
[622] Documents C-0078 and C-0228.
[623] Document C-0022.
[624] This can be seen in the cash flow forecast contained in the booklet, as argued by the Expert Report of Eco One Research Inc of 15 June 2016, figure 11 and par. 112.
[625] Ibid, paragraph 121, with express reference to the document BayWa AG Annual Report no. 2011, p.110. EO-18.
[626] *Invesmart B.V. v. Czech Republic* (UN-0036-01) Award of 26 June, 2009, paragraph 251. RL-0047.

926. In consequence, the Kingdom of Spain has not violated any legitimate expectation of the Claimants' and less so the expectation of the alleged immutability of the regulatory framework throughout the operational life of the wind farms in which they invested.

927. Finally, under no circumstances can the stoppel doctrine, invoked by the Claimants in their Statement, opposed to the Kingdom of Spain.[627] The stoppel cannot be used against the conduct of Spain for several reasons: a) because it is an institution belonging to Anglo-Saxon law that is not known in Spain; b) because the most similar institution in Spanish law is the "*venire contra factum propium non valet"* principle and this principle has not been violated by the Respondent from the point of view of the jurisprudence of the Supreme Court and the constant, unmistakable messages of the Regulatory Body in terms of the need to guarantee the sustainability of the SEE and c) because the Claimants have not shown that they relied on these alleged commitments to immutability in investing in the renewable energy sector in Spain.

(2.5) Spain also has not violated the commitment to provide *stable conditions*.

(a) Introduction

928. The Claimants focus their Legitimate Expectations on the fact that the so-called "Regulatory framework no. 1" "*would be kept stable and consistent over time*"[628]. However, in their explanation of the "*Legitimate expectations in general*"[629], the Claimants identify these expectations with the duty to provide stable conditions for the investment[630].

929. The Kingdom of Spain, in addition to not violating the Claimants' Expectations, also has not violated the obligation to grant stable TEC conditions. As has been shown, the Respondent has granted the Claimants a FET as it has maintained the essential conditions of the Regulatory framework under which the Claimants invested with the challenged measures. Additionally, the Claimants maintain the financial balance of the investment. The new measures were adopted without alterations that were arbitrary, disproportionate or abusive to the existing Regulatory framework.

(b) The ECT requires the creation of stable conditions, but this does not prevent the adoption of justified, non-discriminatory Macroeconomic control Measures.

930. The Claimants interpret the ECT in a biased manner according to which the Treaty would guarantee the freezing of the general regulations in favour of investors. They base this argument on more than fifteen awards, of which only the Case of Plama v. Bulgaria and that of Charanne, relate to the ECT. The rest awards relate to administrative licences or contracts in which the specific legal regulation of any future reforms was clearly stated, being any possible changes to the contract expressly limited or denied.

[627] Memorial on the Merits, paragraph 855.
[628] Memorial on the Merits, paragraph 925.
[629] Memorial on the Merits, paragraphs 872 to 888.
[630] Memorial on the Merits, paragraph 874.

931. Thus, the Memorial on the Merits expressly cites the *Award of BG v. Argentina*[631]. In said Award, the Argentine state committed itself to maintaining the tariffs for 5 years and not modifying the licences without the consent of the licensee[632]. These specific commitments assumed legally and contractually are not comparable to this Case, in which the Kingdom of Spain has not included a specific commitment "not to modify the premiums and tariffs without the consent of the licensee" in its regulations or in any other instrument at any time.

932. Furthermore, some of these awards have been analysed by the report by UNCTAD[633], which the Claimants expressly invoke[634]. The UNCTAD says the following in relation to these awards:

> *"In these cases, tribunals have gone so far as to suggest that any adverse change in the business or legal framework of the host country may give rise to a breach of the FET standard in that the investors' legitimate expectations of predictability and stability are thereby undermined. This approach is unjustified, as it would potentially prevent the host State from introducing any legitimate regulatory change, let alone from undertaking a regulatory reform that may be called for. It ignores the fact that investors should legitimately expect regulations to change over time as an aspect of the normal operation of legal and policy processes of the economy they operate in."*[635] *(emphasis added).*

933. For this purpose, this party considered it more relevant to study Precedents where the standard established in the ECT was applied than the awards invoked by the Claimants.

934. The "stable conditions" referred to by the TEC allow the adoption of reasonable and proportionate macroeconomic control measures, provided these are as a result of a reasonable cause. This has been confirmed by numerous cases of arbitration Precedent which applied the ECT. Thus, the reasoning made by the Arbitration Tribunal in the Case of *Plama v. Bulgaria* is applicable to these proceedings:

> *"the Tribunal believes that the ECT does not protect investors against any and all changes in the host country's laws. Under the fair and equitable treatment standard the investor is only protected if (at least) reasonable and justifiable expectations were created in that regard. It does not appear that Bulgaria made any promises or other representations to freeze its legislation on environmental law to the Claimant or at all."*[636]

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[631] Memorial on the Merits, paragraph 885

[632] *BG Group Plc. v. Republic of Argentina*, CNUDMI, Final Award, 24 December, 2007, Paragraphs 168 to 170. RL-0061.

[633] This is how it has analysed the awards of: TecMed v. Mexico, (RL-0072), Enron v. Republic of Argentina (RL-0019), CMS Gas v. Argentina, (CL-0106), PSEG v. Turkey, (CL-0104), amongst others.

[634] Memorial on the Merits, paragraph 800

[635] United Nations Conference on Trade and Development, *Fair and Equitable Treatment*, UNCTAD Series on Issues in International Investment Agreements II, New York and Geneva, 2012. R-0210.

[636] *Plama Consortium Limited v. Republic of Bulgaria*, ICSID Case No. ARB/03/24, Award of 27 August 2008, paragraph. 219. RL-0034.

935. The Arbitration Tribunal came to the same conclusion in the Case of *AES SUMMIT v. Hungary*. Said Award denied that the existence of a stability clause could be deduced from a general regulatory Framework in the scope of the ECT:

> *"The stable conditions that the ECT mentions relate to the framework within which the investment takes place. Nevertheless, it is not a stability clause. A legal framework is by definition subject to change as it adapts to new circumstances day by day and a state has the sovereign right to exercise its powers which include legislative acts.*
>
> *Therefore, to determine the scope of the stable conditions that a state has to encourage and create is a complex task given that it will always depend on the specific circumstances that surrounds the investor's decision to invest and the measures taken by the state in the public interest."*[637] *(emphasis added)*

936. Said criterion has been reiterated once again in the *Case of Mamidoil v. Albania*[638]. This precedent is clear and conclusive. However, still more relevant is the Precedent that has already examined and assessed Spanish legislation in the years 2007 and 2008, in the Case of *Charanne v. Spain*:

> *"in the absence of a specific commitment an investor cannot have the legitimate expectation that the regulation in place is going to remain unchanged."*[639]

937. Also, the more recent award in the *Electrabel* case establishes that:

> *"the Tribunal considers that the application of the ECT's FET standard allows for a balancing exercise by the host State in appropriate circumstances. The host State is not required to elevate unconditionally the interests of the foreign investor above all other considerations in every circumstance. […] even assuming that Electrabel had an expectation that it would be awarded the maximum compensation [...], once weighed against Hungary's legitimate right to regulate in the public interest, such an expectation does not appear reasonable or legitimate."*[640] *(Emphasis added)*

938. In the application of the ECT to the Spanish SEE, the subsequent Award of *Charanne v. Spain* came to the same conclusion as the cited Awards:

> *"Turning a regulatory provision, due to the limited number of persons that may be subject thereto, into a specific commitment entered into by the State towards each and every one of those persons would be an excessive limitation of the capacity of States to regulate the economy* ***according to the public interest****.*
>
> *[...] "in the absence of a specific stability commitment, an investor cannot have the legitimate expectation that a regulatory framework like the one disputed in this*

[637] *AES Summit Generation Limited and AES-Tisza Erömü Kft v. The Republic of Hungary*, ICSID Case No. ARB/07/22, Award, September 23, 2010, paragraphs 9.3.29 and 9.3.30. RL-0039.
[638] *Mamidoil Jetoil Greek Petroleum Products Societe Anonyme S.A. v. Republic of Albania*, ICSID Case No. ARB/11/24, Award, 30 March 2015 paragraphs 617-618. RL-0046.
[639] *Charanne, Final Award of Charanne BV y Construction Investment S.A.R.L. v. The Kingdom of Spain*, Arbitration No.: 062/2012, 21 January 2016, p. 499. RL-0049.
[640] *Electrabel S.A. v. Hungary* (ICSID Case No. ARB/07/19), Award of 25 November 2015, paragraphs 165 and 166. RL-0048.

arbitration would never be modified in order to adapt it to market needs and the public interest.."[641] *(Emphasis added)*

939. In this sense, the ECT does not oblige the Contracting Parties to maintain a stable and predictable regulatory framework for all investment. Let's not forget that Article 10(1) refers to "conditions", not to a "regulatory framework"[642]. Professor Wälde shows that the obligations imposed on the States in article 10 must be adjusted to the provisions established in part IV of the ECT:

> *"one needs to appreciate that these "primary" obligations are tempered by the miscellaneous provisions of part IV- with reference to sovereignty (Art.18 (1)), presumably an emphasis on respecting the power of economic regulation of states and perhaps equivalent to the reference to "subsidiarity" under the EU Treaty, the – partial and some extent only suspensive- tax veto in Art.21, the exceptions in Art.24 and the hotly contested attribution rules in Art.22 and 23."*[643]

940. For his part, Professor Moshe Hirsch, cited by the Claimants,[644] declares that:

> *"The right of every state to enact legislative or regulatory measures applicable to activities within its territory is one of the basic premises of public international law. International institutions and investment tribunal are well-aware of the basic right (and duty) of governments to legislate and regulate domestic affairs in the public interest".*[645]

941. In the same sense, Prof. Schreuer states that[646]:

> *"At the same time, it is clear that this principle is not absolute and does not amount to a requirement for the host State to freeze its legal system for the investor´s benefit. A general stabilization requirement would go beyond what the investor can legitimately expect. It is clear that a reasonable evolution of the host State´s Law is part of the environment with which investor must contend."*[647] *(Emphasis added)*

942. The Claimant wishes to obtain a legal framework that is non-modifiable for the entire useful life of its wind farms. However, the ECT establishes no more limits on the regulatory power of the States than the minimum standards of international law, with the objective of non-discrimination. And we would reiterate that even this treatment does not apply on the

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[641] *Charanne B.V. y Construction Investments S.A.R.L. v. Kingdom* of Spain (SCC V 062/2012), Final Award, 21 January 2016, dissenting vote, paragraphs 493 and 510. RL-0049.
[642] The Claimant actually identifies both concepts in its interpretation of the Legitimate Expectations protected by the 10(1) TEC in paragraph 1128 of the Memorial on the Merits.
[643] T W Wälde, "Arbitration in the Oil, Gas and Energy Field: Emerging Energy Charter Treaty Practice" (2004) 1 Transnational Dispute Management 2. RL-0054.
[644] Memorial on the Merits, paragraph 884
[645] M. Hirsch, "Between Fair and equitable treatment y Stabilization Clause: Stable Legal Environment y Regulatory Change in International Investment Law", International Law Forum de la Hebrew University of Jerusalem Law Faculty, Research Paper Nos. 07-13, June 2013, pages 2 and 3. CL-0094.
[646] Memorial on the Merits, paragraph 398. The Claimant invokes a publication by Dr Schreuer from 2008 that was subsequently corrected by Dr Schreuer himself in 2012, as we will see later.
[647] C. Schreuer, Fair and Equitable Treatment in Arbitral Practice, 2005, Journal of World Investment & Trade ("Schreuer"), p. 365. RL-0056.

subject of public subsidies or aid. In any case, the TEC allows the adoption of macroeconomic control measures by the signatory States, based on reasons of public interest.

943. The Respondent has shown in the facts part of this Memorial that the Kingdom of Spain has adopted regulatory measures for various reasonable causes.

(1) The legal obligation to continuously adjust the economic system to the principle of reasonable profitability for investors, avoiding over-remuneration;

(2) The existence of public interest in the sustainability of the SEE, in a context of serious international crisis and with a severe reduction in the energy demand, which reduced the income of the SEE and financially unbalanced such, together with the increased costs of RE; and

(3) The impossibility of allowing consumers to bear the entirety of the economic unbalance.

944. Additionally, this occurred in the context of a set of macroeconomic control measures that were adopted in compliance with international commitments, such as the Council Recommendations of March 2012[648] and the Memorandum of Understanding signed with the European Union on 20 July 2012. In both documents, Spain undertook to adopt macroeconomic measures to deal with a specific unbalance: "*address the electricity tariff deficit in a comprehensive way*". This commitment became binding for Spain from July 2012[649].

945. Furthermore, the challenged measures grant investors (national and foreign) reasonable profitability in the current economic climate, which maintains the economic balance of the investment, with no discrimination whatsoever between national and non-national. They are therefore proportionate, reasonable measures.

946. These measures have been adopted respecting the principle that governed this investment and in accordance with Law 54/1997: to allow priority of access and handling and grant reasonable profitability according to the capital market, which the PER 2007-2010 already declared as being "around 7%".

[648] Council Recommendation of 10 July 2012: "address the tariff deficit of the electrical sector on a global scale, in particular improving the profitability of the electricity supply chain". R-0062.

[649] Memorandum of Understanding signed with the European Union on 20 July, 2012. Sections 29 and 31: "There is a close relationship between macroeconomic imbalances, public finances and financial sector soundness. Hence, [...], with a view to correcting any macroeconomic imbalances as identified within the framework of the European semester, will be regularly and closely monitored in parallel with the formal review process as envisioned in this MoU. [...]
Regarding structural reforms, the Spanish authorities **are committed** to implement the country-specific recommendations in the context of the European Semester. These reforms **aim at correcting macroeconomic imbalances,** as identified in the in-depth review under the Macroeconomic Imbalance Procedure (MIP). In particular, these recommendations invite Spain to: [...] 6) [...] **address the electricity tariff deficit in a comprehensive way**." (Emphasis added). RL-0067.

947. Furthermore, it is not possible to talk about the violation of stable conditions since the profitability ER producers can hope to achieve was determined by Law following RD-Law 9/2013[650]. This had been largely proposed and requested by the sector's Associations[651].

948. In this sense, the judgements of the Supreme Court in relation to the conformity of RD 413/2014 and Order IET/1045/2014 with the law have also analysed the possible violation of the ECT, which forms part of the internal law that the High Court also has the duty of applying. The Supreme Court understands that the ECT has not been violated based on the following lines of reasoning:

> *"(...) even though the Treaty signed in Lisbon on 17 December 1994 encourages Signing Parties to promote and create "stable, fair, favourable and transparent conditions so the investors of other Signing Parties invest in their territory", the concept of "stability" should be understood as referring to the regulatory framework as a whole, not one isolated measure of those that make this up, and also cannot be interpreted as implying the complete freezing of the system approved initially when, as has happened here, there has been a change in the relevant circumstances and there are justified reasons for the regulatory modification applied to photovoltaic technology. Investment in this technology continues to be protected and promoted in Spain by a regulatory framework that is undoubtedly favourable overall."*[652]

949. And it states that the new legal system maintains the essential lines of the above:

> *"the new legal system maintains the traditional incentive measure for the production of renewable energy of guaranteeing reasonable profitability and this guarantee is given greater security by incorporating a calculation system into a regulation with the status of a law, since article 30.4 of Law 54/1997, in the drafting provided by RD-Law 9/2013, now states that said reasonable profitability "will relate to the average profit in the secondary market of ten-year State Bonds before taxes, applying the appropriate differential.*
>
> *For these existing facilities with a prioritised system on the date of coming into force of RD-Law 9/2013, as the value of the State Bonds of reference equates to 4.398 percent, according to the Report of the challenged Measure, once the 300 points established as a differential for the first regulatory period have been added, the reasonable profitability established by the cited RD-Law is 7.398 percent.*

[650] The Third Final Provision of Act 24/2013, of 26 December, the specific figure for facilities already operating is around 7.398 percent profitability for the whole project for a standard facility, as set out in Section IV.D.4.2 of this Statement. R-0076.

[651] "the Spanish FIT scheme has the legal rank of a Royal Decree. Even though it is 'stronger' than for instance a ministerial order, the Spanish renewable energy associations have **long called** for a FIT law."Miguel Mendonça et al., (Powering the Green Economy) in the Feed-in Tariff Handbook (Earthscan, 2010). A complete copy is provided. Page 87. RL-0062.

[652] Amongst many others; the Judgement of the Supreme Court of 1 June 2016, 1260/2016 (Appeal 649/2014). R-0149.

Therefore, the new legal system for renewable energy maintains specific regulated remuneration for the facilities which guarantees reasonable profitability for investment."[653]

950. Indeed, a comparative analysis of the remuneration model established by the current regulation and that in force when the Claimants made their alleged investment allows us to conclude that the pillars of the Spanish remuneration model in place since the year 1997 have been maintained. Specifically:

a. It has maintained the concept of efficiency sought by the SEE since the year 1997 consisting of providing Spanish consumers with electricity at the lowest possible cost.
b. It has maintained the subsidies for renewable energy as a cost of the SEE and therefore linked to the economic sustainability thereof.
c. It has maintained and improved the priority of access and handling for RE.
d. It has maintained the basic structure of the Spanish remuneration system consisting of allowing RE plants to achieve reasonable profitability through the combination of two elements; the market price (pool) and a subsidy.
e. It has maintained the characteristic attributes of the principle of reasonable profitability: the balance and dynamism thereof.
f. It has re-established the balance of the SEE by eliminating situations that generated unjustifiable remuneration such as the indexing of all the elements that make up the subsidy to the CPI or the imbalance caused by the pool plus premium option.
g. It has maintained the dynamic nature of the reasonable profitability. Thus, the reasonability of the profitability continues to be assessed according to the cost of money in the capital market (that of Spanish ten-year bonds). Dynamism that allows the value of the investment to be protected over time, thus giving it greater stability.
h. It has maintained and improved the methodology historically followed by the SEE to establish reasonable profitability consisting of the determination of facility types and standard facilities.
i. It continues to provide RE plants with reasonable profitability. The profitability provided by the Spanish remuneration model is better than the sector's discount rate (opportunity cost) and, specifically, better than the Claimant's discount rate (opportunity cost). As a result, the profitability the Spanish system continues to provide is reasonable.

951. The fact that the Claimants' wind farms are no longer entitled to receive the additional incentive according to the new system is due to the fact that they have already received sufficient remuneration to achieve reasonable profitability. It's enough to examine the annual accounts of the holder companies of the La Carracha and Plana de Jarreta wind farms to see that they have obtained income through sales over their first twelve years of operations, together with the market income, that covers the investment costs, operating costs and reasonable profitability

952. The expectation of obtaining amounts exceeding said Costs and reasonable profitability as maintained in this arbitration would constitute illegal aid according to EU Law.

[653] Ibid.

953. Given all the above, it is clear that the Kingdom of Spain has not violated the obligation of providing the Claimants with stable conditions contained in article 10 (1) of the TEC.

(3) The conduct of the Kingdom of Spain has been transparent.

954. The Claimants[654] maintain that the conduct of Spain has not been transparent, considering that (i) no reasonable justification has been given for the measures adopted and (ii) the correct procedure for the approval of the challenged measures was not followed.

955. In any case, the Kingdom of Spain denies the existence of this lack of transparency both with respect to the lack of justification of the measures adopted and in relation to the correct procedure. Likewise, it denies each and every one of the "alleged defects and errors" the Claimants claim have occurred in the processing of the regulations that make up the current system.

956. The Claimants, once again, in analysing this alleged lack of transparency, focus on specific regulations, as if they were completely separate things. However, all the challenged regulations form part of the SEE, as a dynamic system, and the successive reforms thereof obey a single need: that of guaranteeing the technical and economic sustainability of the SEE, adapting this to the development of the base economic circumstances, with the limit of guaranteeing at all times reasonable profitability according to the capital market.

957. For this reason it will be shown that Spain has been transparent, since in any case: (i) it has justified and publicised the need for reforms, (ii) it has followed the legally established procedures, without unjustified delays, (iii) it has guaranteed the participation of the holders of legitimate rights in the regulatory process (iv) it has not acted retroactively contrary to the legal system, (v) it has not hidden any information that might affect the drafting of the reforms and (vi) it has approved a regulatory system that is predictable and dynamic.

958. Furthermore, as the TEC has been presented, which does not establish any link between the predictability of the regulatory Framework of the signatory States and the standard of transparency. Indeed, this obligation of predictability of the regulatory framework does not apply if there is no specific commitment from the State in this respect.

959. Along these lines, in the case of AES Summit v. Hungary, the company AES Summit alleged the *lack of transparency* of Hungary as it reintroduced administrative prices after signing an agreement with the Claimant. According to AES Summit, this measure was unpredictable. The Arbitration Tribunal examined the Tecmed[655] Award amongst others and concluded that, according to the ECT, Hungary had not violated the transparency conditions since it had acted within the acceptable range of legislative and regulatory behaviour:

[654] Memorial on the Merits, paragraph 960 to 1008.
[655] *AES Summit Generation Limited and AES-Tisza Erömü Kft v. The Republic of Hungary*, ICSID Case No. ARB/07/22; Award of 23 September 2010. Paragraph 9.1.6, bottom of page 28. RL-0039

> *"Respondent's process of introducing the Price Decrees, while sub-optional, did not fall outside the acceptable range of legislative and regulatory behaviour. That being the case, it cannot be defined as unfair and inequitable."*[656]

960. Therefore, the Kingdom of Spain has not infringed its obligation to promote transparent conditions in accordance with art. 10(1) ECT.

(3.1) Justification and publicising of the reforms.

961. The need to reform the legal and economic system of the SEE has been a necessary, ongoing process. In fact, RD-Law 6/2009[657], the MAIN of RD 1614/2010[658], RD-Law 14/2010[659] and RD-Law 1/2012[660] had already made reference to the impact of the global crisis the Spanish economy was suffering and the need to adapt the SEE by means of the necessary reforms in their respective preambles. These same reasons were those that determined the adoption of the measures discussed in this arbitration case.

962. Additionally, announcements for a new Electricity Sector Act were made constantly from December 2011, as mentioned previously[661].

963. In this sense, the general characteristics of the reform announced by the Government are clear and predictable:

- In the announcement of December 2011, the reform was classed as *"Structural"* and *"essential"*, based on a policy of *"slowing down and reducing the average costs of the system"*.[662]
- In January 2012, it was confirmed that the reform of the SEE *"which would avoid the generation of a tariff deficit"* was "*under way"*. [663]
- In February 2012, the CNE performed a Public Inquiry on a "*Regulatory adjustment*", to *"stem the trend of growth of the tariff deficit" in the electricity sector"*[664].
- In March 2012, the CNE brought to light the "*unsustainability*" of the imbalance between the income and the costs of the system[665]. That is, the unsustainability of

[656] *AES Summit Generation Limited and AES-Tisza Erömü Kft v. The Republic of Hungary*, ICSID Case No. ARB/07/22; Award of 23 September 2010. Paragraph 9.3.73. RL-0039.
[657] Preamble of RD-Law 6/2009. R-0088.
[658] RIA of RD 1614/2010. R-0082.
[659] Preamble of RD-Law 14/2010. R-0089.
[660] Preamble of RD-Law 1/2012. R-0090.
[661] Counter-Memorial, Section IV.F.2.
[662] *"Another essential reform is that of our energy system"* Transcription of Mariano Rajoy's inaugural speech as Prime Minister, Congress of Deputies, Monday, 19 December 2011, www.lamoncloa.gob.es. R-0192.
[663] "The complex economic and financial situation, coupled with the situation of the electricity system, make it advisable to temporarily remove the incentives for the construction of these facilities while a reform of the electricity system that will avoid the generation of the tariff deficit is implemented", Press release of the Ministry of Industry, Energy and Tourism, 27th January, 2012. R-0171.
[664] By order of the State Secretary of Energy, the CNE carried out the Public Inquiry on 2 February 2012 to collect proposals with which to produce a report. Paragraph 2 of said public inquiry explains the reason for said report: "*to stem the trend of growth of the tariff deficit and the need to take specific measures in this respect.*" (emphasis added). To do this, it refers to the inquiry on regulatory adjustment measures. R-0131.

the remuneration framework, the immutability of which the Claimant understood as enforceable.

- In April, 2012, the need for a "*thorough reform of the electricity sector*", with the "*firm commitment*" of the Government to address the "*elimination of the tariff deficit*"; with a "*fair distribution of the effort between consumers, the public sector and the private sector*" was recognised. A mention of "*regulated activity cost reduction measures"* was included[666].
- In July 2012, another Document published by the Government made a reference to the *"first step in the thorough reform of the energy system*" [667].
- In September 2012 the "*Energy Reform Law Project*"[668] was announced to solve the tariff deficit, in the increasing of which the premiums on renewable energy had been decisive. In said month "*structural measures to correct the tariff deficit*" and a "*new Law of the Electricity Sector for the first quarter of 2013*" [669]were also announced.

964. Clearly, it is at least noteworthy that despite having access to the monthly information on the reform and the need to adopt such to be able to address the growing trend of the tariff deficit, the Claimants speak of defects as a result of "not informing on the political and legislative changes that could significantly affect investment"[670] and which "took place without sufficient cause"[671].

965. Therefore, contrary to that maintained by the Claimants, we can see that: (i) knowledge of the regulatory framework of the SEE and its fundamental principles, (ii) the studying of jurisprudence that has interpreted the SEE in a constant and consolidated manner, (iii) the reading of the preambles of the regulations and (iv) the monitoring of the information supplied by the Government of the Kingdom of Spain allow any diligent investor to have complete, true information on the reason and need for all the measures adopted.

(3.2) Compliance with the legally established procedures, without the occurrence of unjustified delays.

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[665] On 7 March 2012, the CNE issued the Report on the Spanish energy sector, indicating the following with respect to the tariff deficit*: "the fundamental problem with respect to the electricity sector is that the lack of convergence between the income and costs of the activities regulated in the electricity sector over the last ten years has generated growing debt for the sector. The imbalance between the income and costs of the system is* ***unsustainable****, due to the impact of the accumulated, growing debt on present and future access fees for consumers and the temporary impact on the indebting of those companies forced to finance the deficit of the system." (emphasis added).* R-0131.

[666] National Reform Programme 2012, Government of Spain, 27 April 2012, pages 207 and 208. R-0121.

[667] 9 July 2012, in the document *Six Months of Government: Reform* to Grow, in relation to Royal Decree-act 13/2012, of 30 March. R-0173.

[668] In September 2012, the Document The reforms of the Government of Spain: The determination to face the crisis was published with two objectives: that the cost of energy should not condition the competitiveness of the economy and to provide a definitive solution to the problem of the increased tariff deficit of the energy system. R-0174.

[669] 27 September 2012 with the Document published by the Government: "Spanish Strategy of Economic Policy: Balance and structural reforms for the next six months". R-0122.

[670] Memorial on the Merits, paragraph 963.

[671] Memorial on the Merits, paragraph 1005.

966. In this respect, it should be clarified that the production of various drafts of RD 413/2014, far from being due to the allegedly spurious reasons invoked by the Claimants[672], was the result of the volume of observations received and the high degree of acceptance of the proposals made by stakeholders themselves in the hearing process. This is recognised thus by the Report of the State Council of 6 February, 2014[673]. Therefore, this alleged delay in the processing of RD 413/2014 is actually the result of the transparency and the participation of the affected sectors.

967. At the same time, the time taken for the processing of MO 1045/2014 is also more than justified considering its magnitude and complexity. It's enough to bear in mind that the MO, of 1761 pages, considers 1967 different types of facility.

968. As has been indicated, the definition of such a high volume of types of facility and the calculation of a series of parameters for each of them represented a technical task of much greater magnitude than that initially foreseen.

969. So it is clear that the period of "almost a year" the Claimants[674] claim it took to approve MO 1045/2014 is more than justified and cannot in any way be considered excessive delay. All the more so if we remember that this approval process included a hearing process for all legitimate stakeholders both before the CNMC and before the State Council[675], as will be analysed below.

970. To these effects, it should be noted that, as recognised by the Award of jurisdiction and admissibility of *Phillip Morris Asia Limited v. The Commonwealth of Australia* of 17 December 2015:

> *"The Tribunal wishes to make two further general but at the same time case-specific considerations. First, in this case a period of 19 months passed between the announcement of the intention to legislate and the passage of the actual legislation. However, the length of time it takes to legislate is not a decisive factor in determining whether the legislation is foreseeable. The Tribunal notes that democratic States often have long legislative processes involving consultations with a variety of stakeholders. In this case, the process, which led to the approval of the TPP Act, was transparent, involving preliminary reports and consultations and discussions with all stakeholders, including the tobacco companies. However, this does not make the outcome any less foreseeable than in the case of a State that does not have the same sort of democratic oversight of the legislative process and might enact legislation almost overnight"*[676].

[672] Memorial on the Merits, paragraphs 979 to 982.
[673] Report of the State Council of 6 February, 2014. Said Report shows the process, with the participation of the whole sector and the restarting of the process thereof as a result of the proposals accepted. R-0124.
[674] Memorial on the Merits, paragraph 983, amongst others.
[675] In this sense, see indexes of the documents of MO 1045/2014 before CNMC (R-0086) and that of RD 413/2014 (R-0085).
[676] *Philip Morris Asia Limited vs. The Commonwealth Of Australia*, Award on Jurisdiction and Admissibility, 17 December 2015, Paragraph 567. RL-0037.

971. Additionally, it is interesting that the Claimants should implicitly class the processing of amendments in the Congress of Deputies and the Senate[677] as bad legislative practice. This shows a clear ignorance of Spanish legislative procedure since nothing prevents amendments from being proposed by any political party, including that of the Government.

972. Finally, it states that the original draft of RD 413/2014 was subject to "severe criticism[678]" on the part of the CNE, the National Commission of Competency and the State Council. However, on the one hand, said criticisms turned out not to be due to deficiencies in relation to the transparency in the preparation and approval thereof, so this argument by the Claimants is harmless in relation to the principle of transparency. On the other hand, the very existence of these criticisms shows, contrary to that maintained by the Claimants[679], that the impartiality of said bodies is undeniable, therefore, the Claimant's classing of such as being "closer to the Respondent's positions" is reckless and unjustified.

(3.3) Participation in the regulatory process of the holders of legitimate rights

973. Not only were the reforms announced years before they were enacted but additionally, the drafting of the legal and regulatory standards has been transparent. Prompt information has been provided and access has been granted to all the stakeholders to the projects for the presentation of statements and reports.

974. The processing of Royal Decree 413/2014 and Ministerial Order 1045/2014 complied with the processes required by Spanish legislation for the preparation, processing and approval thereof[680]. Additionally, maximum transparency was offered in the drafting thereof and various hearing processes took place so the sector's companies, associations and individuals could present their opinions and statements. Additionally, a report was requested from the consultant bodies, State Council and the regulator National Markets and Competition Commission[681].

975. In this respect, the Claimants state that: "*During this period, Wind Farms operated in a regulatory limbo without knowing for sure what their definitive remuneration would be in virtue of the New Economic System.*[682]"

976. This statement is emphatically denied. Both in the drafting of RD 432/2014 and that of MO 1045/2014, hundreds of statements from producers, the sector's associations and individuals were taken into account. Even the Claimants themselves have provided documentation[683] that contradicts this statement. Indeed, the Claimants were aware of the

[677] In this respect, the processing of amendments before the Congress of Deputies and the Senate is regulated, respectively, in the Second Chapter, Section 1 of the Regulations of the Congress of Deputies of 10 February, 1982 (R-0111) and the Fourth Section of the Regulations of the Senate of 3 May 1994 (R-0112).
[678] Memorial on the Merits, paragraph 597.
[679] Memorial on the Merits, paragraph 981.
[680] To this effect, we must remember the literal sense of article 24 of the Government Act, transcribed in section IV.E. of this document.
[681] Counter-Memorial, Section IV. F.
[682] Memorial on the Merits, paragraph 29.
[683] The first draft of the Royal Decree, 16 July 2013 (C-0239) and the second draft of 26 November 2013 (C-0241).

draft versions of the regulations and actively participated in the processing thereof, through AEE and APPA[684] [685], so they clearly knew roughly how the final draft of the remuneration parameters would read. It's worth noting that, precisely in response to the statements from the sector, the final result is more beneficial for the plants than the first draft of the regulation, contrary to that maintained completely without foundation in the Memorial on the Merits[686].

977. In light of the documentation provided by both parties, the Arbitration Tribunal will be able to assess and verify if "During this period, Wind Farms operated in a regulatory limbo without knowing for sure what their final remuneration would be in virtue of the New Economic System[687]" or if the process was reasonably transparent. The Respondent understands that compliance with the standard of "transparency and due procedure" has been documented during the processing of RD 413/2014 and MO 1045/2014.

(3.4) Absence of prohibited retroactivity

978. As another of the alleged infractions of the principle of transparency, the Claimants invoke, on the one hand, that RD-Law 9/2013 shouldn't have been approved as a Royal Decree Act[688], as the reasons of urgency and need constitutionally required for the approval of a regulation of this category had not occurred and, on the other hand, that said regulation had retroactive effects.

979. However, before analysing the absence of any retroactive nature of the challenged measures, we should clarify the mechanics of the transitory system of RD-Law 9/2013 which the Claimants are intentionally confusing with a case of prohibited retroactivity.

(a) The transitory system of RD-Law 9/2013 lacks any retroactive scope.

980. The Claimants reiterate on numerous occasions that as a result of the provisional payments made to them during the period of eleven months between the approval of RD-A 9/2013 (July 2013) and the approval of RD 413/2014 and MO IET/1045/2014 (June 2014), they are now returning the Regulated Tariff, received by them during said period of time, in the amount of 460,000 Euros[689]. They refer to said fact implying that this is a retroactive application of the regulation. Nothing could be further from the reality.

981. Indeed and without detriment to that which will be shown below on the absence of prohibited retroactivity in RD-Law 9/2013, with regards to the specific issue of the provisional payments, it should be noted that the clients are confusing the application of a transitory regulation with "retroactivity".

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[684] The Spanish Wind Energy Association presented Statements in response to the proposed draft of RD 413/2014 on 30 July 2013 (R-0232) and 11 December 2014 (R-0233). The APPA also presented statements (R-0241). Likewise, the three producer associations presented statements during the processing of MO ITE/1045/2014, included as R-0204, R-0205, R-0237, R-0238, R-0242 and R-0243.
[685] The association UNEF also presented statements on two occasions in relation to the draft of the Ministerial Order on 25 February 2014 (R-0203) and 26 May 2014 (R-0206).
[686] Memorial on the Merits, paragraph 991 to 995.
[687] Memorial on the Merits, paragraph 29.
[688] Memorial on the Merits, paragraph 584 and 585.
[689] Memorial on the Merits, amongst others, paragraphs 508, 636, 773 and 1019.

982. In this sense, the third Transitory Provision of RD-Law 9/2013 considered the transitory application of RD 661/2007 until the approval of the necessary provisions for full application of the subsequent royal decree which would allow the full application of the new remuneration scheme.

983. The new remuneration scheme was developed by RD 413/2014 of 6 June, which, together with Ministerial Order IET1045/2014 of 16 June, established the remuneration parameters applicable to all the existing renewable energy and cogeneration facilities to determine the remuneration system therefor.

984. In particular, point 2 of the aforementioned 3rd TP of RD-Law 9/2013 stated that the body responsible for making the payments (CNMC) would pay the amounts payable during the transitory application of RD 661/2007 as payments on account. Additionally, it stated that once the enforcement regulatory provisions of RD-Law 9/2013 (which came to be RD 413/2014 and Order IET/1045/2014) should be approved, the payment body CNMC would settle the collection rights or payment obligations corresponding to the facilities, from the coming into force of RD-Ley 9/2013 until the coming into force of the necessary provisions for the full application of the new remuneration system.

985. It should be noted that RD-Law 9/2013 established that the settlement of the amounts received on account would take place in the six payments subsequent to the coming into force of said Provisions. However, the fifth final Provision of Act 24/2013 modified the drafting of point 2 of the 3rd TP mentioned above, making the period for the repayment of the amounts received on account by the owners of renewable energy facilities more flexible by increasing this from six months to nine months and considering a maximum limit of repayment obligations, so that the effect of the monthly amounts to be repaid would cause as little strain as possible on their liquid assets.

986. Therefore, it is clear that the provisional payment system set out by RD-Law 9/2013 has no retroactive effect whatsoever but rather, on the contrary, constitutes a system of transitory law.

987. In fact, the Claimants themselves, aware of the mechanics of this transitory system, provided for the amounts they would have to repay in their annual accounts.

988. Indeed, in the Annual Accounts corresponding to the 2013 financial year of the Wind Companies "P.E. Plana de Jarreta SL" and "P.E. La Carracha SL", produced prior to the publication of RD 413/2014 and Order IET/1045/2014, the administrators of both companies were already considering the repayment obligations of the amounts received on account, in virtue of the application of the provisions of RD-Law 9/2013.

989. Thus, notes 6, 8 and 11 of the "Accounts of "P.E. La Carracha SL" for the 2013 financial year consider, respectively, the following:

Trade debtors and other receivables

The heading "Clients from sales and provision of services" mainly contains the collection rights derived from the sale of energy. The amount owed to the Company on 31 December 2013 came to 1,851,000 euros (1,042,000 euros on 31 December 2012).

The company settles with the market agent, AXPO Iberia, S.L., the collection rights derived from the sale of energy valued at the price plus premium established minus the cost of deviations.

In addition, the company provisionally settles with the Spanish National Markets and Competition Commission the amount corresponding to the net energy effectively produced valued at the price of the premium plus supplements according to repealed Royal Decree 661/2007, of 25 May.

In view of the fact that this settlement is provisional as a result of the application of Royal Decree-Act 9/2013, of 12 July (see Note 1), the Company has recorded a provision for the estimated amount that it will have to return to the National Markets and Competition Commission in application of the new legislation (see Note 8)

8.- Provision for risks and expenses

The Company is the owner of the rights of occupation of the land in the state public domain or private domain situated within the municipal limits of the various places where the wind farms and associated facilities are installed.

The contract of transfer of this land establishes the obligation for the Company to return the land at the end of the transfer period in its original condition, therefore removing all the elements installed on it. The dismantling costs, updated and anticipated by the company directors, which have been recorded in the long term provisions, came to 3,447,000 euros on 31 December 2013 (3,283,000 euros on 31 December 2012).

Furthermore, the Company records in short term provisions, mainly, the amount pending payment to the National Markets and Competition Commission, as a result of the application of Royal Decree-Act 9/2013, of 12 July (see Note 1), according to which the Company estimates that it will have to repay an amount of 1,919 euros (see Note 11.1)

11.- Income and expenses

11.1 Net turnover

The income corresponding to the sale of electricity production in 2013 came to 10,559,000 euros (11,272,000 euros in 2012), with the provisions coming to 645,000 euros (1,648,000 euros in 2012).

Furthermore, it should be highlighted that pursuant to Royal Decree-Act 9/2013, of 12 July (see Notes 1 and 8), a provision has been recorded for the amount to be reimbursed to the National Markets and Competition Commission, which came to 1,819,000 euros.

990. So, having analysed that the provisional payments of RD-Law 9/2013 constitute a system of transitory law, with no retroactive effect, we will now see that none of the challenged measures, including this RD-Law 9/2013, involves prohibited retroactivity: (i) neither in accordance with international law; (ii) or in accordance with Spanish law.

(b) Arbitration precedent on retroactivity

991. What the Claimants call "*retroactivity*" is not really such according to international Jurisprudence. The case of *Nations Energy v. Panama* is particularly illustrative. On said occasion, the Tribunal analysed the concept of *retroactivity* within the protection against illegal expropriation that the BIT granted:

> *"The Arbitration Tribunal does not share this point of view and believes that Act 6 is not retrospective as it does not have the effect of revoking acquired rights and only applies to the future.*
> *Said requirements only apply towards the future and cannot have the effect of retroactively cancelling or reducing deductions already made in relation to income tax for previous years. [...]*
> *In actual fact, the Claimants are **confusing** the principle of non-retroactivity with the principle of immediate effect of the new act for the future. Act 6 does not have the effect of retroactively cancelling acquired rights but rather of modifying the conditions in which the holders of tax credit that has not yet been used may apply this in the future."* [690] (Emphasis added)

992. This Award accurately mentions the concept of "acquired rights", establishing that if these rights are affected by a subsequent regulation then said regulation is retroactive. This is different from regulations that apply to future events, but which do not affect rights already acquired.

993. Indeed, the measures contained in RDA 9/2013 apply towards the future without affecting rights already acquired (the remuneration already received by the investors). As a result, it must be concluded that, according to international Jurisprudence, the concept of retroactivity in international law does not apply to RDA 9/2013.

994. What the Claimants fail to mention when claiming the alleged retroactivity of the measures is that RDA 9/2013 respects the remuneration received by the facilities, which cannot be reclaimed. But the effects of said regulation, the payment of the remuneration according to the new system, take place in the future, as the payments made prior to the coming into force thereof must be respected. The Third Final Provision of LSE 2013 clarifies it thus[691].

995. Therefore, far from acting in a way that would affect the profitability of RD 661/2007, which would imply the possibility of reclaiming that paid by Spain in the past, it is clear

[690] Case of *Nations Energy Inc. and others v. Republic of Panama*, (ICSID Case No. ARB/06/19), paragraphs 642, 644, 646. RL-0040.
[691] Act 24/2013, Third Final Provision. R-0076.

that the effects of the new system take place in the future and that the remuneration received prior to this is intangible and not subject to any reclaiming whatsoever.

996. Indeed, the calculation of the remuneration takes into account the standard values determined by art. 30.4 LSE, guaranteeing said remuneration, together with the market income. This will allow the facility to recover its investment and cover its operating costs and at the same time, obtain the corresponding reasonable profitability over the course of its useful life. But the effects of said regulation, that is, the payment of the remuneration according to the new system, take place in the future, as the payments made prior to the coming into force thereof must be respected.

997. Another case of precedent that has already ruled in relation to the lack of retroactivity of the measures adopted by the Kingdom of Spain, confirming the legal foundation of the Case of *Nations Energy v. Panama*, is worth mentioning. The Award of the Case of Charanne v. *Kingdom of Spain* establishes the following:

> *"In fact, the retroactivity argument raised by the Claimants is a mere rewording of the argument that the State could not alter in any way the regulatory framework from which the Claimants' plants benefited. [...]This stance would, in fact, freeze the regulatory framework, thus restricting any possible regulatory change to new energy plants installed after said changes.*
>
> *It is undisputed that the 2010 regulations applied immediately, from their entry into force, to the plants already in operation, and that they* ***did not apply retroactively to previous time periods****. The Arbitration Tribunal considers that unless there are specific commitments in place such as those stemming from a contract, there is no principle of international law* ***preventing a State from adopting regulatory measures with immediate effect on ongoing situations"***[692].

998. The reasoning of this Award is fully applicable to this case. As a result, it must be concluded that, according to international Jurisprudence, the concept of retroactivity in international law does not apply to RDA 9/2013.

(c) National Jurisprudence applicable to the retroactivity of the measures

999. The Supreme Court and the State Council ratified the legality of the legislative modifications which apply to the future without affecting acquired rights[693]. This Doctrine is the same as that applied by international arbitration precedent.

1000. The Spanish Constitution Court has judged the measures adopted pursuant to RD-A 9/2013 and has ruled that they are not retroactive given that they are effective towards the future without affecting acquired rights. In this sense, the Judgement of 17 December 2015 has declared the following as a clarification:

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[692] *Charanne B.V. y Construction Investments S.A.R.L. v. Kingdom of Spain* (SCC V 062/2012), Final Award, 21 January 2016, and dissenting vote, paragraphs 546 and 548. RL-0049.

[693] Judgements of the Supreme Court of 9 December 2009 Documento R-0002. Likewise, Ruling 937/2013 of the Permanent Committee of the State Council, of 12 September 2013, is cited and presented. General Observation VI, Document R-0123.

"so that provisions do not fall within the scope of the prohibited retroactivity that, lacking in ablative or derogatory effects on the past, display their immediate effectiveness in the future even if this involves an impact on a relationship or legal situation that is still ongoing.(...) there is no proscribed retroactivity when a rule governs pro futuro legal situations created prior to its entry into force or whose effects have not been consummated"[694]".

1001. Two subsequent Judgements of the Spanish Constitution Court, dated 18 February 2016, have confirmed this decision[695].

1002. The Supreme Court has also declared that there is no prohibited retroactivity in the measures introduced by RD 413/2014 and Order IET/1045/2014.[696]

1003. In short, the legislator has modified the remuneration system of the facilities establishing reasonable profitability over the whole useful life of the facility. This remuneration allows to take into account the payments already received since the start of operations of the facility, for the purpose of calculating the future subsidies to be received outside of the market, without being retroactive as a result. What's more, this avoids the payment of over-remuneration that could constitute State Aid contrary to the law of the European Union.

1004. It must therefore be concluded that, in accordance with national and international Jurisprudence, the concept of retroactivity does not apply to RDA 9/2013 or the rest of the challenged measures. That is to say, that the Kingdom of Spain has not violated the duty of transparency, because the challenged measures are not retroactive.

(3.5) Absolute transparency with regards to pertinent information

1005. Another of the Claimants'[697] arguments in relation to the alleged lack of transparency relates to the lack of information in relation to the alleged Reports by Roland Berger and the Boston Consulting Group, which would include the calculations in relation to the remuneration parameters.

1006. At this point we would mention that the contract with the Boston Consulting Group was terminated by the Government of Spain due to non-compliance in the execution of the contract, so the Kingdom of Spain did not receive the report cited by the Claimants. Therefore, no Report by the Boston Consulting Group was taken into account to determine the parameters.

1007. As regards the report issued by Roland Berger, this is a report that was issued and received by the Government of Spain subsequent to the approval both of RD 413/2014 and

[694] Judgement of the Constitutional Court of 17 December 2015, delivered in constitutional challenge 5347/2013. R-0154.
[695] Judgement of the Constitutional Court of 18 February 2016, delivered in constitutional challenge 5852/2013 R-0156 and Judgement of the Constitutional Court of 18 February 2016, delivered in constitutional challenge 6031/2013. R-0157.
[696] Amongst many others; the Judgement of the Supreme Court of 1 June 2016, 1260/2016 (Appeal 649/2014). R-0149.
[697] Memorial on the Merits, paragraphs 600 to 608.

Order IET/1045/2014 of 16 June, as recognised by the Claimants[698]. Said report was not intended to be a preliminary step in the drafting of the regulation but rather technical support for the IDAE in the production of the analysis of the costs of the facilities. An analysis that said Institute has also performed with its own means and its direct knowledge as the owner or co-owner of multiple RE facilities[699].

1008. Therefore, the presentation or not of the Report does not affect the transparency referred to in the ECT with respect to the Claimants as it was not a decisive factor in the drafting of the Order, nor is there any record of the presentation thereof having been requested during the processing of the challenged measures.

1009. To sum up, the Kingdom of Spain has complied with the commitments of the ECT in the creation of "*stable, fair, favourable and transparent conditions so that the investors of other Signing Parties invest in its territory.*"[700]

(3.6) Approval of a predictable and dynamic regulatory system, consistent with the linking of reasonable profitability and investment (CAPEX) and operating (OPEX) costs.

1010. Finally, the Claimants argue that the new legal system establishes regulatory periods of three or six years that can be modified at the discretion of the Government, that it does not determine the review methodologies of certain parameters included therein, that the reviewing of the rate of reasonable profitability could affect remuneration already received and that the parameters contained in MO 1045/2014 differ from those in the proposed version of this MO submitted to public inquiry[701].

1011. However, contrary to that maintained by the Claimants, the regulatory periods are not at the discretion of the Government but rather, on the contrary, they are predictable and constitute an element of security for the investor, as they have been outlined in regulations. To this effect and in order to avoid unnecessary repetition, the explanation in relation to the reforms contained in Section IV.G is considered reiterated. (1.7).

1012. On the other hand, the Claimants state that the methodology for the reviewing of certain elements has not been indicated. However, both Act 24/2013[702] and RD 413/2014[703] contain regulations to guarantee that investors receive reasonable profitability in relation to their facilities at all times. Said guarantees are also explained in the statement by Mr Juan Ramón Ayuso[704].

1013. Additionally, contrary to that argued by the Claimants[705], the reviewing of the rate of reasonable profitability, which may take place at the end of each 6 year regulatory period, to

[698] Memorial on the Merits, paragraph 613. (ii)
[699] The means employed for the determination of the costs of each IT are described in detail in the Witness Statement of Mr Juan Ramón Ayuso of 14 June 2016. Section 6. RW-0001
[700] Energy Charter Treaty art. 10.1. RL-0006.
[701] Memorial on the Merits, paragraphs 991 to 995.
[702] Article 14.4 of Act 24/2013, of 26 December. R-0076.
[703] Royal Decree 413/2014. Article 20(1). R-0110.
[704] Declaration of Mr Juan Ramón Ayuso of 14 June 2016. Sections 6 and 7. RW-0001
[705] Memorial on the Merits, paragraph 570.

adapt it to the capital markets, shall only apply for the rest of the regulatory useful life of the standard facilities, but under no circumstances to remuneration already received[706].

1014. As a result, the establishing of regulatory periods gives investors security and guarantees the maintaining of the reasonable profitability, preserving this profitability throughout the regulatory useful life, together with the returning of the investment value.

1015. Finally, as stated in the witness statement by Mr Juan Ramón Ayuso, the historical remuneration calculation parameters up to July/2013 that characterised the wind facilities of the Claimants are exactly the same in the "Proposed Order" and in Order IET/1045/2014. Only the "income per sale" and "operating costs" parameters were different for the future, mainly due to the expected change in the path of market prices in the future[707].

(3.7) Arbitration and academic doctrine also cannot show any violation of the principle of transparency.

1016. The Claimants are trying to justify their claim of the violation of the transparency standard by invoking arbitration and academic doctrine, which can be grouped into three criteria: (i) the interpretation of the principle of transparency under the ECT, (ii) the requirement for "due procedure" and (iii) the reasonable time for the approval of regulatory provisions.

(i) Interpretation of the principle of transparency under the ECT

1017. With regards to the interpretation of the principle of transparency under the ECT, the award of the case of Electrbel v. Hungary[708], the case of Mohammad A. Al-Bahloul v. Tajikistan[709] and that of Gold Reserve v. Venezuela[710] are invoked.

1018. Firstly, the award of the case of Electrabel v. Hungary did not interpret this condition in applying the ECT. Therefore, it is not relevant:

"Electrabel makes no allegations regarding lack of transparency"[711]

1019. Secondly, the award of the case of *Mohammad A. Al-Bahloul v. Tajikistan*, after analysing the awards of Metalclad v. Mexico and Teemed v. Mexico, concluded, in line with that maintained by the award of CMS v. Argentina, that the criterion of transparency must not be interpreted as broadly as to imply the freezing of the regulatory system but rather as the State's obligation to act in an open, consistent manner.

1020. Finally, the award of the case of *Gold Reserve v. Venezuela* found that there was a lack of transparency on the part of Venezuela as it did not inform investors of its changes to its

[706] Declaration of Mr Juan Ramón Ayuso of 14 June 2016. Section 8. RW-0001.
[707] Declaration of Mr Juan Ramón Ayuso of 14 June 2016. Section 8. RW-0001.
[708] *Electrabel v. Hungary*, Decision regarding Jurisdiction. RL-0002.
[709] *Mohammad A. Al-Bahloul v. Tajikistan*. CL-0026.
[710] *Gold Reserve v. Venezuela*. CL-0099.
[711] *Electrabel S.A. v. Hungary* (ICSID Case No. ARB/07/19), Award 25 Nov. 2015, paragraph 115. RL-0048.

mine operating policy[712]. So the non-applicability of this award to this case is clear, not only because it refers to a BIT but mainly because the numerous announcements made by the Kingdom of Spain in relation to the challenged measures, as set out in section IV.F (2) of this document, are undeniable.

1021. Indeed, this party has shown that (i) the RE Sector had been being informed of the need to carry out reforms to allow the rebalancing of the SEE since RD-Law 6/2009, RD 1614/2010, RD-Law 6/2009, RD-A 14/2010 and RD-Law 1/2012 (even in the preamble of RD 661/2007[713] itself) and (ii) that these reforms were processed according to the corresponding legal provisions at all times.

(ii) Due procedure

1022. The collection of arbitration rulings and doctrinal articles in relation to due procedure includes the awards of the cases of *Saluka Investments BV v. Czech* Republic (UNCITRAL)[714] and *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakistan*[715] and the articles of C. H. Schreuer[716] and J. E. Viñuales[717].

1023. As regards the award of Saluka Investments BV v. *Czech Republic (UNCITRAL), Partial award, 17 March, 2006*[718], a careful reading of section VI.2.b) is sufficient to see that the Tribunal, without detriment to the fact that it does not actually analyse the standard of transparency, concludes that the measures adopted by the Respondent were predictable. Thus it states that:

> *"The Tribunal does not find, however, that the Respondent has violated its "fair and equitable treatment" obligation by a failure to ensure a predictable and transparent framework for Saluka's investment. Neither was the increase of the provisioning burden for nonperforming loans unpredictable for Saluka/Nomura, nor could Saluka/Nomura legitimately expect that the Czech Republic would fix the legal shortcomings regarding the protection of creditor's rights and the enforcement of loan security within a timescale of help to Nomura".*

1024. As regards the second of the awards, pronounced in the case of *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakistan*, the Tribunal analysed the application of the standard of transparency to the case in question and concluded that:

> *"More importantly, even assuming for the sake of the analysis that due process and procedural fairness govern the internal processes underlying the exercise of*

[712] *Gold Reserve Inc. v. Bolivarian Republic of Venezuela* (ICSID case no. ARB (AF)/09/1), Award, 22 September 2014, paragraph 591. CL-0099.
[713] Preamble, RD 661/2007. R-0101
[714] *Saluka Investments BV v. Czech* Republic (UNCITRAL), Partial Award, 17 March 2006 (RL-0028).
[715] *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakistan* (ICSID case no. ARB/03/29), Award, 27 August 2009. CL-0114.
[716] C. H. Schreuer, "Fair and Equitable Treatment in Arbitral Practice", The Journal of World Investment & Trade, Vol. 6 (2005). CL-0065.
[717] J. E. Viñuales, Foreign Investment and the Environment in International Law, 2012. CL-0116.
[718] *Saluka Investments BV v. Czech* Republic (UNCITRAL), Partial Award, 17 March 2006 (RL-0028).

contractual rights, the record shows that Bayindir was indeed given the opportunity to present its position on numerous occasions throughout the relevant period"[719].

1025. In short, the Arbitration Tribunal considers the principle of transparency satisfied through the granting of statement collection procedures, a requirement that was more than fulfilled with respect to the measures challenged by the Claimants.

1026. With regards to the article by C. H. Schreuer[720], it should be pointed out that, although the purpose thereof was to perform a systematic study of the standard of fair and equitable treatment, it formulates a conclusion that is particularly relevant to the effects that we are interested in in stating that:

"A general stabilization requirement would go beyond what the investor can legimitately expect. It is clear that a reasonable evolution of the host´s State law is part of the environment with which investors must contend".

1027. So it is undeniable that the reforms of the SEE obeyed a reasonable evolution of the regulatory system, justified by the need to adapt this to the macroeconomic circumstances and fully respecting the limit of reasonable profitability.

1028. As regards the article by J. E. Viñuales[721], the author indicates three milestones that are relevant to assess if the procedure followed by the host State constitutes "due procedure". In this sense, it states that:

"A review of the case-law suggests that three considerations are particularly important in assessing a claim for lack of procedural fairness: (i) a comparison of the administrative process challenged to one identified as 'normal' or 'regular'; (ii) the mandate and scope of discretion of the administrative authority involved and (iii) the conduct of the investors".

1029. The application of these criteria leaves no doubt that the Kingdom of Spain has respected the principle of transparency, as the drafting and approval procedure for the challenged measures took place with full respect of the legally established processes. This procedure included, where applicable, hearing processes for stakeholders.

(iii) Reasonable time for approval

1030. Finally, as regards the doctrine in relation to the reasonable time for the approval of the regulation, the Claimants invoke the award of the case of *PSEG v. Turkey*[722]. A reading of the award shows that the criteria contained therein cannot be extended to this case of arbitration. The difficulties in relation to a contract signed between the investor and Turkey are analysed, with the dual purpose with which the State acts in exercising its regulatory power and simultaneously signing private contracts without specifying the sphere in which

[719] *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakistan* (ICSID case no. ARB/03/29), Award, 27 August, 2009, paragraph 347. CL-0114.
[720] C. H. Schreuer, The ICSID Convention. A Commentary, Cambridge University Press, Second edition, RL-0038.
[721] J. E. Viñuales, Foreign Investment and the Environment in International Law, 2012. CL-0116.
[722] PSEG v. Turkey. CL-0104.

it is operating in each case being described as arbitrary. Therefore, this criterion is not applicable, as the Kingdom of Spain has made it clear that it was exercising its regulatory power at all times.

1031. Furthermore, at this point it is worth once again coming back to the award of *Philip Morris Asia Limited v. The Commonwealth of Australia* of 17 December 2015:

> *"The Tribunal wishes to make two further general but at the same time case-specific considerations. First, in this case a period of 19 months passed between the announcement of the intention to legislate and the passage of the actual legislation. However, the length of time it takes to legislate is not a decisive factor in determining whether the legislation is foreseeable. The Tribunal notes that democratic States often have long legislative processes involving consultations with a variety of stakeholders. In this case, the process, which led to the approval of the TPP Act, was transparent, involving preliminary reports and consultations and discussions with all stakeholders, including the tobacco companies. However, this does not make the outcome any less foreseeable than in the case of a State that does not have the same sort of democratic oversight of the legislative process and might enact legislation almost overnight"*[723].

(3.8) Conclusion

1032. In short, it has been shown that Spain: (i) has justified and publicised the need for reforms, (ii) has followed the legally established procedures, without unjustified delays, (iii) has guaranteed the participation of the holders of legitimate rights in the regulatory process (iv) has not acted retroactively contrary to the legal system, (v) has not hidden any information that might affect the creation of the reforms and (vi) has approved a regulatory system that is predictable and dynamic. Additionally, we have seen that neither the awards or the doctrinal articles invoked by the Claimants back their argument.

1033. Therefore, the Kingdom of Spain has not infringed its obligation to promote transparent conditions pursuant to art. 10(1) ECT. In graphic terms, as the Claimants have obviously not been "*operating in a legal limbo for almost two years*"[724], nor has the Kingdom of Spain violated the FET standard in the way it has acted with respect to the Claimant.

K. The measures of the Kingdom of Spain have granted *full protection and security* to the investment of the Claimant party.

1034. The Claimants sustain that the Kingdom of Spain has infringed the standard of full protection and security for its investment, as laid down by Article 10(1) of the ECT[725]. Nor may it pursue this claim in light of the doctrine and the most relevant arbitral case law.

1035. The Claimants acknowledge that this standard has its origin in preventing physical attacks on investors, "*Having clarified that the MCPS standard and the full protection and*

[723] *Philip Morris Asia Limited vs. The Commonwealth Of Australia*, Award on Jurisdiction and Admissibility, 17 December 2015,Paragraph 567. RL-0037.
[724] Memorial on the Merits, paragraph 29.
[725] Memorial on the Merits, paragraph 1009 to 1028.

security standard are equivalent, and given that the latter obliges the host State to provide investors with both physical protection and a secure legal investment environment, host States bound by the MCPS standard are also under an obligation to create and maintain a legal framework that grants security to the investor."[726].

1036. However, the Claimant party is incorrect in not distinguishing this standard from that of the FET. In fact, it does not add anything different to what is stated in the previous section about legitimate expectations and stable conditions.

1037. Indeed, in this Counter-Memorial, the following has been accredited:

- The possibility of adopting macro-economic control measures, which involve a regulatory change, with the arbitral case law that applies.

- The measures adopted by the Kingdom of Spain have been proportionate and reasonable, in accordance with the socio-economic circumstances in place between 2009 and 2014, which justified them.

1038. Indeed, these two elements are those required by doctrine and by the most recent arbitral case law to deny that the standard of "full protection and security" has been violated, contrary to what is sustained by the Claimants.

1039. In this respect, the opinion of Professors Dolzer and Schreuer determines the compliance of the action of the Kingdom of Spain with the standard invoked by the Claimants:

> *"The standard will not be violated if a State exercises its right to legislate and regulate and thereby takes reasonable measures under the circumstances"*[727]

1040. This opinion is further ratified by arbitral case law. Thus, the arbitral tribunal in the case *AES Summit v Hungary* expressly examined this standard within the framework of the ECT. The Arbitral Tribunal concluded that this standard does not offer protection against the Government's right to legislate and regulate in a way that might negatively affect the Claimant's investment, as long as the actions of the Government are reasonable with the circumstances and with the intention of objectively achieving rational public results.

> *"In the Tribunal's view, the duty to provide most constant protection and security to investments is a state's obligation to take reasonable steps to protect its investors (...) against harassment by third parties and/or state actors. But the standard is certainly not one of strict liability. And while it can, in appropriate circumstances, extend beyond a protection of physical security it certainly does not protect against a state's right (as was the case here) to legislate or regulate in a manner which may negatively affect a claimant's investment, provided that the state acts reasonably in the*

[726] Memorial on the Merits, paragraph 1012.
[727] R. Dolzer and C. Schreuer, Principles of International Investment Law, Oxford University Press, 2012, page 162. RL-0075.

circumstances and with a view to achieving objectively rational public policy goals."[728] *(Emphasis added).*

1041. The Claimant party cites in support of its claims the *Cases CME v Czech Republic*[729] and *Ceskoslovenska Obchodni Banka, A.S. v. Slovak Republic*, 29 December 2004[730]. However, these awards do not apply the standard mentioned in the ECT. Therefore their relevance as a valid criterion for decision is denied.

1042. On the contrary, the relevance and applicability of the *Case AES Summit v. Hungary* to the present Case is not discussed by the parties. The doctrine set out by this Arbitral Tribunal acknowledges the power of Governments to regulate reasonably and in accordance with the socioeconomic circumstances that apply in each case.

1043. Thus, in the present case, the social and economic circumstances that apply have been stated and the reasonableness of the reform that has taken place has been accredited. In addition, the examination at this time of the effects of this reform also make it possible to conclude that it was rational and proportionate since it allowed (1) a rebalancing of the tariff deficit, (2) a halt in the rise of consumer tariffs and (3) maintenance of reasonable profitability for renewable energy producers.

1044. In addition, in the Facts it has been accredited that the method of remuneration was expressly proposed by the majority Association in the RE Sector in 2009, with the legal advice of the Claimants' legal team. Therefore, the reasonableness of the reform that took place is obvious: it is consistent with a request from the majority Association of the RE sector made in 2009. Furthermore, these measures have allowed the tariff deficit to be stabilised and reasonable profitability to be maintained for the renewable energy producers.

1045. As a result, there are grounds for also dismissing the alleged violation of the guarantee of full protection and security in view of (1) the accredited facts, (2) the exercising of the regulatory power of the Respondent and (3) the adoption of reasonable measures in line with the existing economic circumstances.

L. The measures taken by the Kingdom of Spain were reasonable and non-discriminatory.

1046. The Claimants sustain that the Kingdom of Spain has reduced the Claimants' investment with "exorbitant" and "discriminatory" measures. This means, according to the Claimant party, the violation of the FET standard laid down by ECT article 10(1)[731].

1047. For these purposes, the Claimant party invokes the *BG v Argentina* Award. In said Award, the Argentine state committed itself to *maintaining* the tariffs for 5 years and *not*

[728] AES Summit Generation Limited and AES-Tisza Erömü Kft v. The Republic of Hungary, ICSID Case No. ARB/07/22; Award of 23 September 2010; 13.3.2. RL-0039.
[729] Memorial on the Merits, paragraph 1250.
[730] *Ceskoslovenska Obchodni Banka, A.S. v. Czech Republic* (ICSID, Case No. ARB/97/4), Award, 29 December 2004, paragraph 161. CL-0125.
[731] Memorial on the Merits, Section XI.

modifying the licences without the consent of the licensee[732]. The commitments assumed legally and contractually do not apply to this case.

1048. Furthermore, the Claimant is incorrect in considering that it is the Respondent who has to accredit that it has not violated this standard. The literal wording of Article 10(1) does not talk about reasonable or proportionate, but about "*irrational or discriminatory*". Therefore, the Claimant has the burden of proof of accrediting that the measures adopted are "irrational or discriminatory". This burden of proof was declared by the Arbitral Tribunal in the Electrabel Case:

> *"The Tribunal starts with the premise that it is Electrabel which bears the burden of proving its case under the ECT's FET standard."*[733]

1049. However, this standard is related to the FET standard of the ECT, which allows, pursuant to the AES Summit precedent, adoption of reasonable and proportionate regulatory changes.

1050. The facts of this Counter-Memorial have accredited: (1) the existence of an international economic crisis that led to a reduction in electricity demand; (2) the rise in consumer tariffs, (3) the existence of over-remuneration in the RE sector and (4) the existence of expectations of growth of the tariff deficit. All of these circumstances involved the economic sustainability of the SEE.

1051. Such facts will allow, in turn, to demonstrate that the measures adopted are not irrational or discriminatory, pursuant to the various Tests proposed in the arbitral precedents.

(1) Relevant facts for appreciating the reasonable and non-discriminatory nature of the measures being challenged.

(1.1) Economic circumstance of unsustainability of the SEE in 2012.

1052. The facts of this Counter-Memorial have accredited[734]: (1) the existence of an international economic crisis that led to a reduction in electricity demand; (2) the rise in consumer tariffs, (3) the existence of excess remuneration in the RE sector, and (4) the existence of expectations of growth of the tariff deficit. All of these circumstances involved the economic sustainability of the SEE.

1053. Therefore, none of these circumstances is mentioned by the Claimants. They completely omit the economic situation of the SEE after the fall in demand in a context of severe world economic crisis and the foreseeable increase in the tariff deficit due to the costs associated with renewable energies.

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[732] *BG Group Plc. v. Republic of Argentina*, CNUDMI, Final Award, 24 December, 2007, paragraphs 168 to 170. RL-0061.
[733] *Electrabel S.A. V. Hungary* (ICSID Case No. ARB/07/19), Award 25 November 2015, paragraph 154. RL-0048.
[734] Counter-Memorial, Section IV.A, B, C and E.

1054. The Claimants also omit any reference to the international commitments assumed by Spain with the European Union in July 2012 for the adoption of macroeconomic control measures to correct the tariff deficit and for global reform of the SEE.

1055. Moreover, the worsening of these circumstances in 2013 is also omitted by the Claimants when they state the adoption of measures by means of Royal Decree-Act 9/2013, which was introduced for reasons of urgency[735]. Not only do they omit the existing socio-economic circumstances, but they also state that there was no urgent reason to adopt it.

(1.2) These measures were proposed by the RE Sector in 2009.

1056. In the Facts it has been accredited that the method of remuneration adopted for RE was expressly proposed by the majority Association in the RE Sector in 2009, the APPA, in 2009. The *reasonableness* of the remuneration measures being challenged is, therefore, obvious, since it corresponds to what the majority Association in the RE Sector wished to achieve in 2009.

1057. Indeed, the RE Association, APPA, with the legal support of Cuatrecasas, Gonçalves Pereira (the Law Firm that is representing and defending the Claimants in this arbitration), proposed that the remuneration of renewable energies should be determined in 2009 in a similar way to that established in 2013 by RD-Law 9/2013:

> *"The government will establish the amount of the regulated tariffs, premiums and complements, therefore assessing, in all cases,* ***the operating and maintenance costs*** *and the* ***investment costs*** *incurred by the owners of a facility* ***in order to obtain reasonable profitability*** *in reference to the cost of money in capital markets. As a fee for the remuneration of capital, an annual percentage equal to the mean of the preceding year for the remuneration of* ***10-year Treasury bonds*** *will be used****, increased by 300 base points****.*
>
> *"For the preceding purposes, the Government will estimate the investment costs associated with the various* ***classes of facilities****, differentiated by technology and size, such that they reflect the usual values that said investments actually reach"* [736] *(Emphasis added)*

1058. The relevance of this proposal is obvious, because it accredits the fact that the remuneration system laid down in 2013 does not violate the FET standard of the ECT. In other words, these 2013 remuneration measures had to be reasonable and proportionate if the majority RE Association proposed a similar system as the best one (1) for achieving reasonable profitability rates with reference to the cost of money in the capital market, (2) provide "*security and stability for investments*" and (3) allow "*the RE to develop their potential in a sustainable and lasting manner*"[737].

[735] Memorial on the Merits, paragraph 584 to 585.
[736] Article 23.3 and .4 of the proposed Bill presented by APPA-Greenpeace in May 2009. Document R-0187.
[737] Press Release from APPA-Greenpeace on the Draft Bill of the Renewable Energies Development Act, 20 May 2009. R-0167.

1059. On the basis of these criteria, the APPA intended in 2009 to build the reform of the renewable energies remuneration regime for the future.

(1.3) The Claimants omit to state that the measures being challenged have been accepted by national and foreign investors as reasonable and attractive.

1060. The current regulatory regime attracted over 5 billion euros in investment in RE in Spain in 2015. This is due to the stability and security in the receipt of revenues that exist in the current regime. However, the Claimants omitted to mention these facts to the Arbitral Tribunal, giving a biased and incomplete view of the reform of the regulatory framework under discussion. The Claimants have completely omitted to mention the "boom in renewables" that took place in 2015[738].

1061. Furthermore, they omitted all reference to the positive assessments that these measures have received from the European Commission, the International Monetary Fund (hereinafter, "IMF") and the International Energy Agency[739].

1062. Therefore, the economic situation after the measures being challenged and the assessments of international bodies accredit the proportionality and reasonableness of the measures adopted and devalue the Claimants' statements about the sector after the adoption of the measures.

1063. In short, only if the new regulation guarantees reasonable profitability does it seem logical a massive entry of new investors. Furthermore, only if the measures are reasonable, proportionate and effective will they merit the positive appraisal of international bodies.

(2) Failure to meet the requirements of the Test proposed by the Claimant.

1064. The Claimant party invokes the *BG v. Argentina* award to contend that the measures adopted are exorbitant and discriminatory[740]. However, the nature of the commitments acquired by Argentina towards the investor in the Award cited have no similarity with the present case.

1065. It is enough to read the commitments acquired by Argentina, both in the Gas Decree and in the licence granted to the investor, to find that we are dealing with a completely different case[741]. Furthermore, the Claimants invoke the AES Summit award, which will be examined further on.

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[738] "Operations boom in the renewable energy sector after the reform": "The purchase of solar and wind power plants so far this year is already in excess of 1 billion. Experts agree that there will be new operations in the sector in the coming months." News item in the "El Mundo" newspaper, "Operations boom in the renewable energy sector after the reform", dated 22 July 2015.R-0179."The boom in renewables attracts 5 billion in investments": "So far this year, the renewable energies sector has accumulated almost 5 billion euros in buying and selling operations *[...]"* News item in the financial newspaper "El Economista", 17 October 2015. R-0178.

[739] These assessments are outlined in greater detail in section IV.H of this document.

[740] Memorial on the Merits, paragraph 1036.

[741] *BG v. Argentina* The clauses in paragraphs 47 to 50 are included as they are specific and particular. It is worth highlighting the contractual clause contained in paragraph 48: *"The Grantor will not change these Basic Rules, in full or in part [...] except by written consent of the Licence holder and subject to*

1066. In addition, there are grounds for denying that the Test requirements proposed by the Claimants have been met in order to assess the measures as *discriminatory*[742]:

i. *If the reference group of investors for comparative purposes is in a similar situation to that of the investor.*
The Claimant does not accredit the extent to which the different renewable energy subsectors may be treated as a valid reference group for the purposes of application of the Test in 2012 and 2013. In any case, it is denied that the requirements of this Test are met. It should be remembered that, with respect to the wind power and photovoltaic sectors, remuneration reduction measures had already been adopted in 2007 and 2010. Therefore, it is incorrect to merely examine the measures adopted in 2013, when other measures adopted previously to avoid excess remuneration in the same sector and guarantee the sustainability of the SEE have not been examined. In other words, when there had already been adopted measures that were in line with the same guiding thread or reason: economic rebalancing of the system.

ii. *Whether differentiated treatment has been met out to investors in the State receiving the investment.*
The Claimant party does not accredit the extent to which the Claimants or their investment were prejudiced or discriminated against in comparison with the other producers using renewable energies. It is obvious that the macroeconomic control measures challenged have affected all RE producers and the rest of the economic operators of the SEE[743], without any distinction. It is therefore denied that the Claimant or its investment were treated in any differentiated manner.

iii. *Whether said differentiated treatment is reasonably justified.*
It has been accredited in the facts of this statement that the adoption of the measures being challenged was due to the circumstance of economic imbalance of the SEE and excess remuneration to RE. These circumstances are combined with the impossibility of adopting excessive tariff increases for consumers and the existence of international agreements that made it necessary to adopt macroeconomic control measures. All of these circumstances mean that the requirements of this last Test are met since the measures being challenged are reasonably justified.

(3) The Respondent has met the requirements of the Tests referring to the Objectives of the ECT.

1067. As has been stated in section IV.I, the main objective of the ECT is non-discrimination of foreign investors. In addition, Article 10(1) of the ECT establishes an FET standard and, furthermore, when it makes it obligatory to offer to investments a "*treatment no less favourable than that required by international law*", it is recognising the minimum standard of protection guaranteed by international law.

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recommendation of the Regulatory Authority. The provisions that modify the Service Regulation and the Tariff adopted by the Regulatory Authority will not be considered modifications to the Licence in the exercising of its powers, regardless of the right of the Licence holder to demand the corresponding Tariff adjustment if the net effect of such a modification were to change in a favourable or unfavourable way, respectively, the economic and financial balance existing prior to such a modification." RL-0061.

[742] Memorial on the Merits, paragraph 1037.

[743] The text of section IV.F is understood as reproduced here (1).

1068. There are different Tests that are applied by the international arbitral tribunals, which make it possible to assess whether the measures adopted by a State are irrational or discriminatory pursuant to the ECT objectives and standards:

(a) The EDF v. Romania Test, which makes it possible to examine whether Spain has respected the main objective of the ECT, adopting non-discriminatory measures in respect of the Claimants;

(b) The AES Summit v. Hungary Test, accepted by the Claimants as relevant, which makes it possible to examine whether the Kingdom of Spain has respected the FET standard of 10(1) ECT; and

1069. Completion of these Tests will determine the respect by the Kingdom of Spain of the FET objectives and standards laid down by the ECT. This will imply *on the contrary* that no irrational or discriminatory measures will have been adopted:

(3.1) Test of the EDF v. Romania case: non-discriminatory nature of the measures

1070. In the *EDF v Romania Case*[744], the Arbitral Tribunal made use of the verification criteria listed by Rd. Christoph Schreuer in order to assess whether or not the measures adopted by a State are discriminatory. In this respect, Dr. Schreuer considers a measure to be *discriminatory* when:

> *"a) A measure that inflicts damage on the investor without serving any apparent legitimate purpose;*
>
> *b) A measure that is not based on legal standards but on discretion, prejudice or personal preference;*
>
> *c) A measure taken for reasons that are different from those put forward by the decision maker;*
>
> *d) A measure taken in wilful disregard of due process and proper procedure."*

1071. There are grounds for examining each of these criteria separately:

a) *If it is a measure that causes harm to the investor without serving any apparent legitimate purpose.* In this case, it has been accredited that the purpose of the reform is completely legitimate. The measures attempt to address an situation of unsustainable imbalance, in which the international and national economic circumstances determined a reduction in demand which made it necessary to re-balance the system. This

[744] *EDF (Services) Limited v. Romania,* ICSID Case No. ARB/05/13, Award dated 8 October 2009, paragraph 303: "In an attempt to give a content to general expressions such as "unreasonable or discriminatory measures," Claimant relies on the categories of measures that its legal expert, PROFESSOR Christoph Schreuer, has described in his opinion as "arbitrary":
a. a measure that inflicts damage on the investor without serving any apparent legitimate purpose;
b. a measure that is not based on legal standards but on discretion, prejudice or personal preference;
c. a measure taken for reasons that are different from those put forward by the decision maker;
d. a measure taken in wilful disregard of due process and proper procedure.
The Tribunal will consider the claim of "unreasonable or discriminatory measures" according to the terms proposed by Claimant." RL-0035.

legitimate purpose was implemented taking another legitimate purpose into account: not imposing an excessive burden on consumers in order to achieve this re-balance and avoid unjustified excess remuneration.

b) *If it is a measure that is not based on legal regulations or guidelines, but on discretion, discrimination or personal preferences*. The reform carried out was implemented in full compliance with the existing legal regulations and the case law of the Spanish Supreme Court, guaranteeing the reasonable profitability that was and is required by the Electricity Sector Act. The measures questioned in this arbitration are for the purpose of underpinning the principle of reasonable profitability. A principle on which the system of subsidies to production through renewable energies has traditional been built. In addition, the reform being challenged has a general scope. In other words, it is applicable to all operators and to all sectors intervening in the energy market. Therefore, it is not discriminatory with respect to any investor, neither national nor international.

c) *If it is a measure taken for reasons other than those explained by the grantor of the measure*. In the present case, the Preamble of RD-Law 6/2009 and RD-Law 14/2010, as well as the MAIN of RD 1614/2010, warned about the need to reform the electricity sector in order to guarantee its sustainability. These reasons are the same as those on which the measures being challenged were based.

d) *If it is a measure adopted with deliberate disregard for a process with the due guarantees and for the procedure that formally applies.* The Spanish government has followed the legally established procedures to enact the regulatory standard of remuneration in the electricity sector. In the present case it is worth mentioning the effort made by the Government to convey the successive drafts of the measures to the interested parties. Also worthy of mention is the opening of processes for supplementary pleadings, as well as the appraisal and consideration of these pleadings. Under no circumstances were they completely left in the dark, as stated by the Claimants.

1072. Therefore, none of the four criteria explained in the *EDF v Romania Case* for assessing a discriminatory action is met in this case.

(3.2) Test of the AES Summit v. Hungary case: the measures are reasonable and comply with the FET standard laid down by the ECT.

1073. The test set out in the *AES SUMMIT* case is used to determine whether or not an un acceptable (unreasonable) or discriminatory measure exists that does not comply with the FET standard laid down by the ECT. To do this, the Arbitral Tribunal develops the criterion, which in a more limited way had been established by the Arbitral Tribunal in the *Case of Saluka v. Czech Republic*[745]. In the *AES Summit v. Hungary case*, the Arbitral Tribunal stated:

[745] *Saluka Investments B.V. v. Czech Republic*, UNCITRAL of 17 March 2006, paragraph 307. To assess whether the conduct of a State was reasonable it declared: "must be justified by showing that it bears a reasonable relationship to rational policies not motivated by a preference for other investments over the foreign-owned investment." RL-0028.

> *"There are two elements that require to be analysed to determine whether a state's act was unreasonable: the existence of a rational policy; and the reasonableness of the act of the state in relation to the policy.*
>
> *A rational policy is taken by a state following a logical (good sense) explanation and with the aim of addressing a public interest matter.*
>
> *(…) A challenged measure must also be reasonable. That is, there needs to be an appropriate correlation between the state's public policy objective and the measure adopted to achieve it. This has to do with the nature of the measure and the way it is implemented."*[746] *(Emphasis added)*

(a) The Measures were rational and complied with the objective of a public economic policy.

1074. As a first requirement, in the present case the existence of a rational policy is confirmed, adopted by Spain following a logical explanation and for the purpose of addressing a matter of public interest.

1075. The system providing support for renewables is based on the legal principle of reasonable profitability. The Regulator acted for the purpose of redressing the balance required by the applicable legislation. This imbalance, as well as involving an excessive burden for Spanish consumers, was decisively contributing to the generation of the so-called tariff deficit, the correction of which was required by law.

1076. In addition, the imbalance in favour of the producers that the Regulator was trying to stem was taking place in a scenario of acute economic crisis, both in the SEE in particular and in the Spanish economy as a whole. Let us remember at this point that the FADE issues were suspended between March and November 2012, since no foreign financing could be obtained at a reasonable interest rate[747]. These economic circumstances led to the signature by the Kingdom of Spain of a commitment to the EU Member States to adopt macroeconomic control measures[748] that would guarantee the sustainability of the SEE.

1077. The need to protect both consumers, already affected by increases in their electricity bills, and the very sustainability of the SEE compelled the Kingdom of Spain to adopt the measures subject to examination in this arbitration case. Thus, correcting certain costs of the

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[746] *AES Summit Generation Limited and AES-Tisza Erömü Kft. vs. Republic of Hungary*, ICSID Case No. ARB/07/22; Award of 23 September 2010, paragraph 10.3.7 to 10.3.9. RL-0039.

[747] Copy of the certificate of Agreement from the Interministerial Commission regarding article 16 of Royal Decree 437/2010 from the session on 26 November 2012. R-0198.

[748] Memorandum of Understanding signed with the European Union on 20 July, 2012:"*VI. Public Finances, Macroeconomic Imbalances And Financial Sector Reform:*
29. There is a close relationship between macroeconomic imbalances, public finances and financial sector soundness. [...]
31. Regarding structural reforms, the Spanish authorities are committed to implement the country-specific recommendations in the context of the European Semester. These reforms aim at correcting macroeconomic imbalances, as identified in the in-depth review under the Macroeconomic Imbalance Procedure (MIP). In particular, these recommendations invite Spain to: [...] 6) [...] address the electricity tariff deficit in a comprehensive way." (Emphasis added). RL-0067.

System affected by a situation of imbalance constitutes a public policy that fits within the criterion established by *AES Summit*.

1078. In the case cited, the Tribunal, after examining the FET standard laid down by the ECT, declared that the reduction of the excessive profits of investors and the charges to consumers constituted a valid reasonable policy.

> *"the majority has concluded that Hungary's reintroduction of administrative pricing in 2006 was motivated principally by widespread concerns relating to (and it was aimed directly at reducing) excessive profits earned by generators and the burden on consumers.*
>
> *[…] Having concluded that Hungary was principally motivated by the politics surrounding so-called luxury profits, the Tribunal nevertheless is of the view that it is a perfectly valid and rational policy objective for a government to address luxury profits. And while such price regimes may not be seen as desirable in certain quarters, this does not mean that such a policy is irrational. One need only recall recent wide-spread concerns about the profitability level of banks to understand that so-called excessive profits may well give rise to legitimate reasons for governments to regulate or re-regulate."*[749] *(Emphasis added)*

1079. This assessment was expressly confirmed by the Ad Hoc Committee on the application for annulment of the Award, which stated that:

> *"the Committee is also unable to find that the Tribunal's reasoning was either contradictory or frivolous. The Tribunal [...] found, however, that a state can exercise its legislative powers with respect to consumer protection against overly burdensome prices even if this has the consequence that private interests such as an investor's contractual rights are affected, as long as that effect is the consequence of a measure based on public policy that was not aimed solely at affecting those contractual rights. [...] Hungary acted in furtherance of a distinct, legitimate objective. [...] the Committee [...] finds, however, that the distinction is understandable and thus neither contradictory nor frivolous."*[750] *(Emphasis added).*

1080. Furthermore, this criterion has been subsequently ratified by the Electrabel[751] and Charanne[752] cases.

1081. As a result, an action that has as its aims protection of consumers, avoiding remuneration higher than what is reasonable for the investor, is compliant with the FET standard. We should remember that this remuneration is directly supported in the bills to

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[749] *AES Summit Generation Limited and AES-Tisza Erömü Kft. vs. Republic of Hungary*, ICSID Case No. ARB/07/22; Award of 23 September 2010, paragraphs 10.3.31 and 10.3.34. RL-0039.
[750] *AES Summit Generation Limited and AES-Tisza Erömü Kft. vs. Republic of Hungary*, ICSID Case No. ARB/07/22, Decision of the Ad Hoc Committee on the application for annulment, 29 June 2012, paragraph 78. RL-0042.
[751] *Electrabel S.A. v. Hungary* (ICSID Case No. ARB/07/19), Award 25 November 2015, paragraph 179. RL-0048.
[752] Award in the case of *Charanne B.V. and Construction Investments S.A.R.L v. the Kingdom of Spain*, 21 January 2006, paragraph 510. RL-0049.

consumers who, according to the law, have the electricity supply " at the lowest possible cost".

1082. This is thus in line with the first of the parameters considered in the case of *Aes Summit v. Hungary:* the policy implemented by the Kingdom of Spain was perfectly valid and complied with the objective of a public economic policy, which is to correct and avoid, as far as possible, in order to protect consumers, payment of remuneration higher than what is reasonable. The relevance and rationality of the measure is thus beyond all doubt.

(b) The Government's action was reasonable, considering the objective of the state public policy and the measure adopted to attain this objective.

1083. The second criterion assessed by the Arbitral Tribunal in the case of *AES SUMMIT V. Hungary* required the Government's action to be reasonable, requiring proper correlation between the objective of the state public policy and the measure adopted to attain this objective.

1084. In this case, the reform meets this requirement of reasonableness. The reform adopted by the Government affected all subjects involved in the SEE. This reform distributed among consumers and all system operators (producers, distributors and carriers) the measures for increasing the revenues and reducing the costs of the SEE in order to address the tariff deficit[753]. In addition, for the first time since the SEE was created in 1994, financial contributions coming from the General State Budget were planned: Spanish taxpayers were also meeting the costs of the SEE including remuneration of the Claimants.

1085. In the Facts it has been accredited that the method of remuneration adopted for RE was expressly proposed by the majority Association in the RE Sector in 2009[754]. Furthermore, these measures have allowed the tariff deficit to be stabilised and reasonable profitability to be maintained for the renewable energy producers.

1086. As well as reasonable, the measures adopted are also proportionate. The system of subsidies that enabled producers to achieve reasonable profitability of around 7.398% on their investment costs was maintained, at the same time as correcting and avoiding situations of imbalance, which prejudiced Spanish consumers and contributed to endangering the financial sustainability of the SEE.

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[753] These measures are set out in Sections IV.E and G. Among these measures is the fact that a consumer went from paying 370 euros per year for their electricity bill in 2003 to paying a total of 616.20 euros in 2014. The increase accumulated over these years is more than 66.54%. The greatest increases nonetheless took place in 2008 (10%), 2009 (10.1%) and 2011 (17.7%).

[754] Section IV.E(8) of this Statement, the APPA Association proposed that the remuneration of RE in 2009 should be determined in a way that was similar to what was laid down in 2013 by RD-Law 9/2013: "23.3. "The government will establish the amount of the regulated tariffs, premiums and complements, therefore assessing, in all cases, **the operating and maintenance costs** and the **investment costs** incurred by the owners of a facility **in order to obtain reasonable profitability** in reference to the cost of money in capital markets. As a fee for the remuneration of capital, an annual percentage equal to the **mean of the preceding year for the remuneration of 10-year Treasury bonds will be used, increased by 300 base points**.4. For the preceding purposes, the **government will estimate the investment costs** associated with the **various classes** of facilities, **differentiated by technology and size**, such that they reflect the usual values that said investments actually reach." Article 23.3 and .4 of the proposed Bill presented by APPA-Greenpeace in May 2009 (Emphasis added). R-0187

1087. Even the index that was established (Spanish 10-year premium + 300 points) was proposed by the RE sector in 2009. Therefore, the remuneration laid down for the RE Sector was not disproportionate.

1088. This remuneration took place under the financial regime incorporated into RD 413/2014 and Order IET/1045/2014. As has been explained in detail in section IV.F, this system guarantees remuneration for operation, which allows reimbursement of all operating costs necessary to carry out the activity in an effective and well managed manner. The remuneration established after the reform includes the variable and fixed operating costs. The remunerated costs are listed (not exhaustively) in the Preamble of Order IET/1045/2014, of 16 June[755].

1089. Thus, the remuneration system includes and comprises:

a) The revenues from the sale of the electricity generated in the market.

b) Remuneration for operation to supplement the revenues from the sale of energy in the electricity market when they do not cover the fixed and variable operating costs associated with each standard facility, such that in an annual calculation the revenues minus the expenses are at least equal to zero.

c) It also provides the investment with a remuneration that covers, up to the necessary amount, the reimbursement of the initial investment, reduced by the gross annual exploitation margins associated with each IT during its useful regulatory life, when they are positive. To this end, it takes into account the equipment, the facilities and the civil works that are required, together with the costs of promotion, engineering and implementation prior to the plants becoming operational.

1090. In this way, the remunerative parameters for each IT will make it possible to achieve the objective of reasonable annual profitability - established at a rate of 7.398%[756]- on the investment made, from the commissioning of the installation until the end of its useful regulatory life, for those IT that had not previously obtained it. May we remind you that such reasonable profitability is laid down in the Electricity Sector Act and the Jurisprudence of the Supreme Court recognises it as a basic legitimate expectation of the investor.

1091. Such a yield is reasonable and not reviewable until 6 years have gone by from the effective date of RDL 9/2013. The calculation of the remuneration to the investment and of the remuneration to the transaction is established, in an objective and reasonable way, for a typical plant. As is confirmed in the Statement by the witness Mr. Juan Ramon Ayuso, the values applied to all these remunerated concepts are in line with reasonable market value standards[757].

1092. It thus rejects that the remuneration established by the contested measures constitute in the current social-economic reality a *disproportionate or irrational* measure, with regard to

[755] Order IET/1045/2014, of 16 June, Preamble, section III, paragraphs 14 to 21. R-0115.
[756] Its determination is specified in RDA 9/2013, as the average yield in the secondary market of ten-year Government Bonds prior to the effective date of RDL 9/2013, increased by 300 basis points. R-0094.
[757] Statement by Mr. Juan Ramón Ayuso, 14 June 2016, Section 7. RW-0001

the farms in which the Claimant invested. To the contrary rather, in the light of the criteria that have been examined, the reform of the electricity sector carried out by the Kingdom of Spain is a valid and rational policy and it has been carried out by means of a reasonable action, which fits within the standard of FET as laid down in the ECT, as stated by the Arbitral Tribunal in the case *Aes Summit vs. Hungary*.

M. The Kingdom of Spain has not breached the umbrella clause.

(1) Introduction

1093. The Claimants allege that the Kingdom of Spain has breached the so-called umbrella clause in Article 10 (1), last subparagraph, of the ECT.

1094. In this sense, they say that the Kingdom of Spain has failed to fulfil the alleged commitments assumed thereunder and as far as their investment is concerned by virtue of (i) what they call the "Regulatory Framework Number 1" (Act 54/1997, RD 1218/1998, RD 436/2004, RD 661/2007, RD 1614/2010 and RD-Law 1/2012); (ii) certain official statements contained in press releases and (iii) other official statements and facts that demonstrate, in their opinion, the investment climate in the renewable sector in Spain.

1095. As we shall reason below, the arguments of the Claimants cannot be accepted by the Arbitral Tribunal because:

(A) The interpretation of the umbrella clause that is set forth in the Claim Statement is contrary to the literal wording of Article 10 (1) last subparagraph of the ECT and to the concept of the umbrella clause that is dominant in international jurisprudence and doctrine.

B) The Kingdom of Spain has not assumed specific obligations with any investor or investment, neither by dint of Act 54/1997, RD 1218/1998, RD 434/2006, RD 661/2007, RD 1614/2010 or RD-Law 1/2012, nor by dint of press releases, nor by the other acts referred to by the Claimants.

C) The Claimants neither allege nor confirm that any of the sources of the alleged obligations supposedly protected by the umbrella clause played a decisive part in their investment.

D) Even were it to be hypothetically accepted that the Kingdom of Spain had assumed specific obligations by dint of Act 1997, RD 1218/1998, RD 436/2004, RD 661/2007, RD 1614/2010, RD-Law 1/2012 and other unilateral acts cited in the Claim, these obligations would never have assumed with either the Claimant or with their Investment.

E) In any case, the Kingdom of Spain has never made any commitment to guarantee to the Claimants or their Investment the petrifaction of the remunerative regime that was in force when the latter was made. The remuneration was governed by article 30.4 of Act 54/1997, which makes it obligatory to give investors a subsidy which, added to the price of the market, would allow them to achieve a "reasonable profitability" within a sustainable SEE. The aforementioned remunerative regime did not grant any right to a regulatory freeze.

F) The contested measures in this arbitration have respected the essential elements of the Spanish system of remuneration to the plants that generate energy from renewable sources, given that public aid to producers is maintained in order to ensure their competitive position in the market. Thus, subsidies are maintained as a quantity that is added to the market price in order to allow producers to recover: their investment costs, their operational and maintenance costs and to obtain a reasonable profitability from the project. The legal guarantees of priority access and dispatch have also been maintained. Without prejudice to the fact that those plants that have already obtained such reasonable profitability during the previous years, are not goin to receive more subsidies with the new regime. Therefore, the Kingdom of Spain would not under any circumstances have breached the commitments made.

(2) The interpretation of the umbrella clause that is set forth in the Claim Statement is contrary to the literal wording of Article 10 (1)of the ECT and to the dominant concept of what an umbrella clause is, in international jurisprudence and doctrine.

(2.1) The concept of the umbrella clause that is dominant in international jurisprudence and doctrine.

1096. The Claimants allege that the revocation of Regulatory Framework No. 1 by Spain through the successive approval of the Regulatory Framework No. 2 in 2012-2013 and of Regulatory Framework No. 3 in 2013-2014 constitutes a breach of the obligations that the Respondent assumed with the Claimants and with their investment. Accordingly, such revocation constitutes, according to them, a breach of the obligations of the Respondent pursuant to Article 10.1 in fine of the ECT.[758]

1097. However, the Claimants make an erroneous interpretation of the content and purpose of Art. 10 (1) last subparagraph of the ECT, taking the implementation of the "umbrella clause" beyond any reasonable interpretation of the term.

1098. Both the arbitral jurisprudence and the doctrine insist on the importance of the systematic location and the clear wording of umbrella clauses are for their proper interpretation. This is also acknowledged by the Claimant.[759] We must therefore begin by setting forth the wording of Article 10 (1) of the ECT, last subparagraph:

> "Each Contracting Party shall observe any obligations it has entered into with an Investor or an Investment of an Investor of any other Contracting Party". (Emphasis added).

1099. The literal wording of the article obliges one to consider as being included within the protection clause *"any obligations"* that the Contracting Party *"may have contracted"* "with an Investor" or "an Investment". In this regard, in the legal field, if one searches for the meaning of the English expression "*entered into*", the reference shall always address to agreements or contracts.

[758] Memorial on the Merits, paragraph 783.
[759] Memorial on the Merits, paragraphs 786 and 789.

1100. The Claimants stress that the expression "*any*", given its comprehensive nature, would make it possible to include in the concept of an obligation protected by the umbrella clause not only contractual obligations, but also those obligations contracted by means of unilateral acts. Furthermore, the Claimants carry this thesis to the extreme by considering that by dint of the umbrella clause, the precepts of Act 54/1997 and the Royal Decrees issued in its development, which are general provisions *erga omnes*, become commitments that have been specifically agreed with them and with their investment.[760]

1101. Such an approach implies ignorance of the true scope of the umbrella clause, because it ignores that Article 10 (1) last subparagraph of the ECT clearly uses the term "entered into", which necessarily implies the assumption of specific obligations on the part of the State with regard to a particular investor or a specific investment. Thus, in *Noble Ventures, Inc. vs. Romania*, the Tribunal declared that:

> *"[…] considering the wording of Art. II (2)(c) which speaks of "any obligation [a party] may have entered into with regard to investments", it is difficult not to regard this as a clear reference to investment contracts. In fact, one may ask what other obligations can the parties have had in mind as having been "entered into" by a host State with regard to an investment. The employment of the notion "entered into" indicates that specific commitments are referred to and not general commitments, for example by way of legislative acts. This is also the reason why Art. II (2)(c) would be very much an empty base unless understood as referring to contracts.[…]".*[761]

1102. The obligations of the State have to be, therefore, specific, and have to have been assumed by the State with respect to a particular investor, in a *vis-à-vis* relationship, as stated by the Tribunal in *SGS v Philippines:*

> *"[T]he host State must have assumed a legal obligation, and it must have been assumed vis-à-vis the specific investment-not as a matter of the application of some legal obligation of a general character-. This is very far from elevating to the international level all the 'municipal legislative or administrative or other unilateral measures of a Contracting Party*[762]*."*

1103. In fact, in almost every case, the litigation that has grown up around the interpretation and scope of umbrella clauses has had to do with contracts concluded between a State and an investor, but not with the legal framework of the receiving State, which reflects, de facto, the conviction that umbrella clauses are excluded from the scope of legislative acts.

(2.2) Interpretation of Article 10 (1) last subparagraph ECT by Doctrine and arbitral precedents.

1104. The *"Reading Guide of the ECT"* prepared by the Secretariat of the ECT is of relevance, given that it is an element that interprets the ECT. This Reading Guide defines

[760] Memorial on the Merits, paragraphs 830 and 750.
[761] *Noble Ventures, Inc vs. Romania*, ICSID Case No. ARB/01/11, Award dated 12 October 2005, paragraph 51. RL-0026.
[762] *Société Général de Surveillance S.A. vs. Philippines*, ICSID Case No. ARB/02/6, Decision on Objections to Jurisdiction, dated 29 January 2004, paragraph 166. CL-0074.

the provision of Article 10 (1) last subparagraph ECT under the significant heading *"Individual Investment Contracts"* and defines its scope placing emphasis in its foundation, which is none other than the international principle of *"pacta sunt servanda"*[763]:

> *"According to Article 10 (1), last sentence, each CP shall observe any obligations it has entered into with an investor or an investment of any other CP. This provision covers any **contract** that a host country has concluded with a subsidiary of the foreign investor in the host country, or a **contract** between the host country and the parent company of the subsidiary.*
>
> *Respect of the international principle of "pacta sunt servanda" is of particular relevance in the energy sector where most major investments are made on the basis of an **individual contract** between the investor and the state. Article 10 (1) has the important effect that **a breach of an individual investment contract** by the host country becomes a violation of the ECT. As a result, the foreign investor and its home country may invoke the dispute settlement mechanism of the Treaty" (Emphasis added).*

1105. Authors such as Wälde refer to the umbrella clause as the "*pacta sunt servanda clause*", thus underlining its "contractual" nature. In this regard, Wälde notes that:

> *"The umbrella clause and investment treaties target an abuse of the state when situated in its dual role as both contract party and regulator."*[764]

1106. To these effects, the arbitral Precedent of the case *AES Summit Generation Limited vs. Hungary* is conclusive. This precedent, in view of the fact that Hungary features in the list of countries in annex IA of the ECT, denied that an investor could base their claim on Article 10 (1) last subparagraph ECT and argued their lack of jurisdiction:

> *"This Tribunal cannot rule on the scope of contract obligations and consequently cannot determine if the Claimants' contract rights under the 2001 Settlement Agreement – and the 2001 PPA – were eviscerated because it has no jurisdiction to do so."*[765] *(Emphasis added).*

1107. In short, the scope of the umbrella clause in Article 10 (1) last subparagraph ECT covers the contractual obligations that are assumed by the State, we insist, in the framework of a bilateral contract or a similar instrument (administrative contract, concession or license between the State and the investor).

1108. In the present case, the Spanish regulatory framework, including its RD 661/2007, has an *erga omnes* character and, therefore, is not aimed at any collective. Those who had recourse to these regulations were tens of thousands of people, both of this nation and from abroad. The regulations that have been cited and the press releases are not therefore the subject of this final subsection of Article 10 (1) ECT.

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[763] The Energy Charter Treaty: A Reader's Guide, June 2002, page 26. RL-0053.
[764] The "Umbrella" Clause in Investment Arbitration: A Comment on Original Intentions and Recent Cases. Thomas W. Wälde. HEINONLINE 6 J. World Investment & Trade 183 2005, page 226. RL-0055.
[765] AES Summit Generation Limited and AES-Tisza Erömü Kft v. The Republic of Hungary, ICSID Case No. ARB/07/22; Award 23 September 2010. RL-0039.

(2.3) The jurisprudence and doctrine alleged by the Claimants do not support their interpretation of the umbrella clause.

1109. In support of their thesis, the Claimants cite certain arbitral pronouncements. However, it shall be shown below that these quotes do not make it possible to uphold their argument.

(a) The awards that refer to article 10 (1), last subparagraph, of the ECT, do not allow the Claimant's thesis to be to upheld.

1110. In the first place, none of arbitral decisions which refer to Article 10 (1), in fine, ECT, cited by the Claimants, sustain their thesis that the umbrella clause protects obligations deriving from rules and press releases that are *erga omnes* in scope.

1111. With regard to the award in the case *Plama vs. Bulgaria*, the Complainants ignore, when they make reference to it, that the quote they reproduce limits itself to transcribing the reasoning behind the award laid down in the case *Enron Corporation Ponderosa Assets L.P. vs. Argentine Republic*[766], against which they set forth the conclusion reached by the Committee for the Cancellation of the case *CMS vs. Argentina*:

> *"*However, the ad hoc Committee that decided the annulment in the case, CMS v. Argentina, commented that the use of the expression "entered into" should be interpreted as concerning only consensual obligations. In any case, these obligations must be assumed by the host State with an Investor."[767] (footnotes omitted)

1112. The Arbitral Tribunal that made the *Plama vs. Bulgaria* award, after noting the discrepancies in the scope of the expression "any obligations", does not take a position on the matter, given that as the obligation that it is analysing is contractual, and as there are no doubts as to the fact that obligations of a contractual nature are covered by the umbrella clause, no further considerations are required. In short, the award is innocuous for the purposes intended by the Claimants.

1113. With regard to the award in the case *Amto vs. Ukraine*[768], this award arises from the fact that the umbrella clause protects specific obligations contracted *vis-à-vis* with the investor or with their investment (in this case, eleven contracts concluded by a legal entity reporting to the Ukrainian State and a subsidiary of the Claimant). It also reaches the conclusion that Ukraine is not required, neither by virtue of the umbrella clause or by virtue of Article 22 of the ECT, to assume the responsibility deriving from the breach of the contractual obligations of its legally dependent entity. It is hard to see how this award can serve to support the claims of the Claimants.

1114. As for the award made in the case *Liman Caspian Oil vs. Kazakhstan*, not only was it issued in the context of a license that had been granted to Claimant, but also, just before the paragraph that the Claimants have transcribed in their Statement, it says:

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[766] *Enron Corporation Ponderosa Assets L.P. vs. Argentine Republic*, dated 22 May 2007, ICSID Case ARB/01/3, paragraph 274. RL-0019.
[767] *Plama Consortium vs. Republic of Bulgaria* (ICSID Case No. ARB/03/24, Award dated 27 August 2008. RL-0034.
[768] *Limited Liability Company Amto vs. Ukraine* (SCC Case No. 080/2005), Award , 26 March 2008, CL-0069.

> *"(...) the Tribunal considers that it is not clear from the wording of ECT Article 10(1), last sentence, whether the "umbrella clause" also encompasses state legislation concerning the protection of foreign investment such as the Kazakh Investment Laws of 1994 and 2003. The Tribunal notes that the words "obligation the Respondent has entered into with an investor or an Investment of an Investor of any other Contracting Party" in ECT Article 10(1), last sentence, rather seem to suggest that a contractual or similar bilateral relationship must exist between the host state and the investor."*[769] *(Emphasis added).*

1115. That is to say, the Tribunal understands that, in principle, the umbrella clause of the ECT only covers obligations arising from a specific bilateral relationship between the investor and the host state of the investment. Although it also highlights the thesis that has been underlined by the Claimants, is congratulates itself on not having to take a decision in this regard. In the best of cases, in the case tried by the Tribunal, such a decision would involve determining whether the umbrella clause of the ECT also protects commitments made in State legislation that is specifically intended to protect foreign investment, such as the *"Kazakh Investment Laws of 1994 and 2003"*. This circumstance does not concur in the Spanish laws that the Claimants refer to, which are neither rules designed specifically to protect investments nor are they specifically aimed at foreigners.

1116. This same circumstance concurs in the decision on jurisdiction in the case *Khan Resources vs. Mongolia*[770], which analyses the umbrella clause in relation to a Foreign Investment Law. Once again, the obligations analysed by the award did not arise out of rules of a general nature, *erga omnes*, as is the case in this arbitration, rather from rules that are *specifically* designed to promote foreign investment.

1117. For its part, the partial award of the *Mohammad A. Al-Bahloul vs. Tajikistan*[771] case, cited by the Memorial on the Merits[772], also highlights the opinion of the Committee for the Cancellation of the case *CMS vs. Argentina* and, after noting the discrepancies in the scope of the expression "any obligations", comes to the conclusion that it should only take a position with regard to the possible breach of Presidential Decree number 83.r, given that the inclusion of the obligations that have their origin in contracts in the umbrella clause was clear. However, it did not have to take a position on the matter, given that in its opinion, the aforementioned Decree had not been breached.

1118. In short, the Claimant has not cited even a single case in which the umbrella clause has been applied by the Courts without the existence of a contract, a concession or a license that might generate *vis-à-vis* obligations between the State and the claimant investor, with the exception of issues relating to rules designed specifically to promote and protect foreign investments.

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[769] *Liman Caspian Oil vs. Kazakhstan*, CL-0014.
[770] Memorial on the Merits, paragraph 811 *Khan Resources Inc., Khan Resources B.V. and CAUC Holding Company Ltd. vs. The Government of Mongolia and MonAtom LLC* (PCA Case No. 2011-09 (ST-BG), Decision on Jurisdiction, 25 July 2012. CL-0078.
[771] *Mohammad Ammar Al-Bahloul vs. Republic of Tajikistan* (SCC Case No. V (0061/2008)), Partial Award of Jurisdiction and Responsibility dated 2 September 2009. CL-0026.
[772] Memorial on the Merits, footnote 715.

(b) Awards that do not refer to the ECT, do not allow the Claimant's thesis to be to upheld.

1119. The Claimant cites international decisions that apply different treaties of the ECT, in order to try to justify that Article 10 (1), last subparagraph, of the ECT covers obligations arising from rules and other unilateral *erga omnes* acts.

1120. The Claimants use two types of citations: (a) on the one hand, they cite arbitral decisions referring of the implementation of Bilateral Investment Treaties (BIT); and (b) on the other hand, they cite two judgments of the International Court of Justice.

1121. As far as the arbitral decisions referring BITs are concerned, the citations refer to: the decision in the *SGS vs. Paraguay* case[773], the decision of the *SGS vs. The Philippines* case[774], the partial award in the *Eureko vs. Poland* case[775], the decision of the *AEFI vs. Argentina* case[776], the decision of the *Enron vs. Argentina* case[777], the decision of the *Continental Casualty vs. Argentina* case[778], the decision of the *LG&E vs. Argentina* case[779], the decision of the *BG vs. Argentina* case[780] and the decision of the *Noble Energy vs. Ecuador* case.[781]

1122. The first thing that must be made clear is that these arbitral decisions should be discarded when interpreting the umbrella clause of Article 10.1, last subparagraph ECT, given that, as has been recognised by the Claimants themselves, to paraphrase the Institute of International Law "the specific wording of the clause and the instrument in which they are included" are decisive in order to check when a breach of obligation constitutes a breach of the treaty in question[782]. Therefore, arbitral doctrine concerning a specific umbrella clause may not be extrapolated to another clause of a different treaty, unless it is previously credited that both clauses are exactly identical and are contained in similar treaties, with the same systematics, an exercise that the Claimants have completely ignored. In any case, we will show that these awards do not in fact say what the Claimants allege.

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[773] *SGS Société Générale de Surveillance, S.A. vs. Republic of Paraguay* (ICSID, case No. ARB/07/29), Decision on Jurisdiction, 12 February 2010, paragraph 167. CL-0072.
[774] *SGS Société Générale de Surveillance S.A. vs. Republic of the Philippines* (ICSIC Case No. ARB/02/6), Decision of the Court on Objections to Jurisdiction, January 29, 2004. CL-0074.
[775] Partial Award of Jurisdiction and Merits of the case *Eureko B.V. vs Republic of Poland*, 19 August 2005. RL-0043.
[776] *EDFI vs. Argentina*. CL-0019.
[777] *Enron Corporation and Ponderosa Assets, L.P. vs. Republic of Argentine* (ICSIC Case No. ARB/01/3), Award, May 22, 2007. RL-0019.
[778] *Continental Casualty Company vs. Republic of Argentine* (ICSIC Case No. ARB/03/9), Award of 5 September 2008. CL-0064.
[779] *LG&E Energy Corp., LG&E Capital Corp. and LG&E International Inc. vs. República de Argentina* (ICSIC Case No. ARB/02/1), Decision on Liability, 3 October 2006. RL-0020.
[780] *BG Group Plc. vs. Republic of Argentina* (UNCITRAL), Award of 24 December 2007. RL-0061.
[781] *Noble Energy Inc. and MachalaPower Cía. Ltd. vs. Republic of Ecuador and the National Electricity Council* (ICSID Case No. ARB/05/12), Decision on Jurisdiction, 5 March 2008. CL-0082.
[782] Memorial on the Merits, paragraph 789.

1123. In the first instance, the decision in the SGS vs. Paraguay case[783], refers to "(…) oral and written commitments to respect the contract (…)", therefore, this decision does not relate to obligations that originate in regulations or other unilateral acts.

1124. For its part, the decision in the *SGS vs. The Philippines* case[784], affirms the need for an obligation arising from a regulation to also have a contractual side, in order for it to be considered covered by the umbrella clause, when it points out that:

> *"(…) [T]he host State must have assumed a legal obligation, and it must have been assumed vis-à-vis the specific investment -not as a matter of the application of some legal obligation of a general character-. This is very far from elevating to the international level all the "municipal legislative or administrative or other unilateral measures of a Contracting Party." (Emphasis added).*

1125. As for the Partial Award of Jurisdiction and Merits in the case *Eureko B.V. against the Republic of Poland* of 19 August 2005, it should be noted that what it analysed was the alleged breach by Poland of a purchase contract signed with the investor Eureko B.V. The award makes an analysis of the origin (which it places in the "pacta sunt servanda" clause) and the evolution of the umbrella clause. In this regard, it compares the interpretation given in the *SGS vs. Pakistan* award (also cited by the Claimants) with the one made by the *SGS vs. The Philippines* award (cited earlier by the Kingdom of Spain) and it adheres to the latter. Therefore, according to the award in the *Eureko B.V. vs. Poland* case, the umbrella clause only protects obligations arising from specific bilateral investor-state relationships.

1126. As for the award made in the case *EDF vs. Argentina*, it analyses the breach of the concession agreement, under two BITs and affirms that:

> *"Concession agreements granted to foreign investors for specific investments, such as those at issue in this arbitration, fall within the protection of an umbrella clause.*
>
> *This does not mean that all contractual breaches necessarily rise to the level of treaty violation".*[785]

1127. That is to say, not only was the dispute limited to the possible breach of a contract or a specific bilateral relationship but, moreover, the Court held that not every breach of contract has international relevance. Additionally, the concession contract included specific obligations to update rates in dollars and their subsequent conversion into pesos to protect the foreign investment against of Argentinian currency fluctuations, This example is incomparable with the case being heard here.

1128. In the same line, the citation of the decision in the *BG vs. Argentina* case, refers to the existence of an "(…) Information Memorandum (…)[786]", which excludes its application to obligations that originate in regulations.

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[783] *SGS Société Générale de Surveillance S.A. vs. Republic of Paraguay (*ICSID case No. ARB/07/29), Decision on Jurisdiction, 12 February 2010, paragraph 167. CL-0072.

[784] *SGS Société Générale de Surveillance S.A. vs. Republic of the Philippines* (ICSIC Case No. ARB/02/6), paragraph 121. Decision on Objections to the Jurisdiction of the Court, dated 29 January 2004, CL-0074.

[785] EDFI vs. Argentina. (CL-0019).

1129. In similar terms, the decision in the *Noble Energy vs. Ecuador* case[787], alludes to the existence of an "(…) Investment Agreement (…)", so that in this case the requisite as to its application to obligations that originate in regulations, does not concur.

1130. In regard to the decisions in the cases *Enron vs Argentina*[788], *Continental Casualty vs. Argentina*[789] and *LG&E vs. Argentina*[790], referred to in the Memorial on the Merits, it should be noted that they all relate to the BIT between the United States and Argentina. Even if one rejects the analogy between the BIT and the ECT, the criterion contained in the Decisions cited by the Claimants has been contradicted by other arbitral Precedents that apply the same United States -Argentina BIT:

a) The award in the *El Paso vs. Argentina* case[791] sustains that only investment agreements give rise to obligations that are covered by the umbrella clause:

> *"This means that a contract claim is not transformed into a treaty claim by the umbrella clause, while an "investment agreement" claim can be viewed as a treaty claim by virtue of a combination of Articles VII(1) and II(2)(c)"*

b) In the same sense, the Decision of the Ad Hoc Committee for the Cancellation of *CMS vs. Argentina* case[792]:

> *"(a) In speaking of 'any obligations it may have entered into with regard to investment,' it seems clear that Article II(2)(c) is concerned with consensual obligations arising independently of the BIT (…) <u>They do not cover general requirements imposed by law</u>.*
>
> *(b) <u>Consensual obligations are not entered into erga omnes</u> but with regard to particular persons. Similarly the performance of such obligations or requirements occurs with regard to, and as <u>between, obligor and obligee</u>.*
>
> *(c) The effect of <u>the umbrella clause is not to transform the obligation which is relied on into something else</u>; the content of the obligation is unaffected, as is its proper law. If this is so, it would appear that the parties to the obligation (i.e., the persons bound by it and entitled to rely on it) are likewise not changed by reason of the umbrella clause" (Emphasis added).*

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[786] *BG Group Plc. vs. Republic of Argentina* (UNCITRAL), Award of 24 December 2007. RL-0061.
[787] *Noble Energy Inc. and MachalaPower Cía. Ltd. vs. Republic of Ecuador and the National Electricity Council* (ICSID Case No. ARB/05/12), Decision on Jurisdiction, 5 March 2008. CL-0082.
[788] *Enron Corporation and Ponderosa Assets, L.P. vs. the Argentine Republic* (ICSID Case No. ARB/01/3), Award of 22 May 2007: RL-0019.
[789] *Continental Casualty Company v. the Argentine Republic* (ICSID No. ARB/03/9), Award of 5 September 2008. CL-0064.
[790] *LG&E Energy Corp., LG&E Capital Corp. and LG&E International Inc. v. the Argentine Republic* (ICSID Case No. ARB/02/1), Decision on Liability, 3 October 2006. RL-0020.
[791] *El Paso Energy International Company vs. the Republic of Argentina* (ICSID Case No. ARB/03/15, Award dated 31 October 2011. RL-0041.
[792] *CMS Gas Transmission Company vs. the Argentine Republic* (ICSID No. ARB/01/8, Decision on Annulment, 25 September 2007, RL-0031.

1131. In short, the Claimants' reasoning in respect of these awards is mistaken. The Arbitral Tribunal in the Argentinian cases limited itself to analysing to what extent the contractual obligations assumed by the State had been breached, which is why it analyses the regulatory changes. But this does not mean that the umbrella clause includes legislative acts and general provisions, because the obligations for the State arise from the contract, not from the legislative acts. In fact, the regulatory changes were only analysed in relation to their influence with regard to the contract signed between the State and the investor.

1132. As Axel Weissenfels states:

> *"it is worth to note that, although the umbrella clause in LG&E v. Argentina was held in very general terms, the Tribunal limited its scope of application to "specific obligations", excluding "legal obligations of a general nature". The authority arising from these cases is that, no matter how generally an umbrella clause is termed, it is only triggered if the obligations breached are specific ones, i.e., if they concern particularly the investment in question."*[793]

1133. With regard to the judgments of the International Court of Justice, laid down in the cases of the French nuclear tests[794], cited in the Memorial on the Merits, it should also be highlighted that the Claimants do not make any analysis that might allow one to sustain that such decisions uphold their thesis. Moreover, the judgments of the International Court of Justice refer to disputes between two entities that are subject to international Law, two States. And therefore, we are dealing with situations in which any analogy with the present case must be rejected *ab initio.*

1134. The Claimants limit themselves to affirming:

> *"There is no obstacle for the acceptance in international law that a State be bound by the declarations of its Minister/Ministry of Energy as far as issues of representations in the energy field are concerned, because the Minister/Ministry of Energy is undoubtedly an 'organ' for the purposes of attribution of his/her/their actions and omissions to the State (Article 4 of the ILC Draft Articles)."*[795].

1135. However, it is difficult to understand how the judicial doctrine reflected in conflicts between States can be extrapolated, without further ado, to the interpretation of the umbrella clause in investor-State conflicts. This is an exercise that the Claimants should undertake but they have neglected to do so.

1136. Under no circumstances can one uphold that Article 10 (1), last subparagraph, of the ECT, turns subjects of a State into subjects comparable to subjects of international Law, since neither the literal words of the Treaty, nor the most basic reasons of legal logic permit such an argument.

1137. In addition, the Claimants confuse the rules for attributing liability to a State for acts of their representatives with the umbrella clause. As we will see, in order to apply the umbrella

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[793] Umbrella Clauses. Seminar on International Investment Protection. Prof. Dr. August Reinisch. Winter Semester 2006/2007.Axel Weissenfels, page 36. RL-0021.
[794] Nuclear Tests (Australia v. France), Sentence, I.C.J. Reports 1974. CL-0024.
[795] Memorial on the Merits, paragraph 824.

clause, the first thing that has to exist is an obligation that normally arises under the internal laws of the State, which can be invoked at the international level.

1138. Finally, the judgment in the *Mavrommatis* case[796], in which Greece and the United Kingdom confronted each other and which the Claimants have also cited[797], also refers to a conflict between States and does not have the remotest relation with the umbrella clause of the ECT. In that instance, the Court examined to what extent the concessions granted to a Greek citizen by the Turkish Empire before the start of the First World War should have been honoured during the Protectorate implemented by Great Britain after the war. In this case, moreover, there were two concessions. With the British Government having expressly recognised that the subsequent concession holder had not requested the expropriation of the concessions formerly granted to Mr Mavrommatis, the appraisal of the Court was that such concessions should be considered to be existent.

(c) Nor do the doctrinal citations invoked by the Claimants support their broad interpretation of the umbrella clause of Article 10 (1) in fine, of the ECT.

1139. On the other hand, the doctrinal citations invoked by the Claimant lack any manner of endorsement in whatsoever international decision. Therefore, as they have not been admitted by arbitral doctrine, they do not make it possible to state categorically, as the Claimants allege, that official statements may create obligations under the umbrella clause. They do not constitute "applicable international law" to this dispute in accordance with Article 26(6) of the ECT.

1140. What is more, we are going to demonstrate that these citations do not even sustain the claim by the Claimant in this case. In the first place, the Claimant's reliance on the doctrinal opinion of Reisman and Arsanjani[798] is also mistaken, when they conclude the following:

> *"Where statements are made either orally or distributed in writing either hard copy or on-line, clearly promising certain conditions treatment for foreign investors and such statements are made public and are made repeatedly and foreign investors relied on them, and governments do not retrieve or qualify those statements of commitment before the conclusion of contracts with foreign investors, they should, in our view, bind the State[799]". (footnotes omitted) (emphasis added).*

1141. That is to say, according to these authors, unilateral declarations only bind the issuing State in its relations with the foreign investor, when certain requirements are met: (i) they are public; (ii) they have been carried out repeatedly; (iii) they have clearly promised a specific treatment for foreign investors; (iv) the foreign investors have trusted in them when making their investment and (v) they have not been toned down or revoked prior to signing the contract with the investor. That is to say, in addition to other requirements that in this

[796] The Mavrommatis Jerusalem Concessions, Judgment of 26 March 1925, P.C.I.J. Series A, No. 5. CL-0077.
[797] Memorial on the Merits, paragraph 825.
[798] Memorial on the Merits, paragraph 831.
[799] W. M. Reisman and M. H. Arsanjani, "*The Question of Unilateral Governmental Statements as Applicable Law in Investment Disputes*", in P. M. Dupuy et al. (Eds.): Völkerrecht als Wertordnung – Common Values in International Law. Festschrift für / Essays in Honour of Christian Tomuschat, 2006, pp. 409-422, p. 420. CL-0075.

case are not met - such as having promised a specific treatment to the foreign investor and the latter having trusted that promise - the authors require the existence of a contract with the foreign investor.

1142. As far as Maria Cristina Griton Salias[800] is concerned, when expressing her opinion all she does is cite, in the first place, the authors mentioned above (Reisman and Arsanjani), whose opinion has already been commented on. The author goes on to conduct a study of the various arbitral awards that have been made about the scope of the umbrella clause, all of which have been analysed in previous paragraphs of our document. In her summary, she points out that the courts have accepted that the umbrella clause only applies to unilateral acts contained in the legislation or other instruments of States when such acts consisted in obligations specifically assumed with foreign investors.

1143. This last circumstance is not present in this case. The regulatory measures challenged by the Claimants are not aimed at foreign investors, rather to all operators in the SEE, irrespective of their nationality. Furthermore, the author accepts that:

> *"Some tribunals saw difficulties in umbrella clauses that referred to obligations 'entered into' by host States. They read these clauses as being restricted to consensual commitments contained in contracts. This would exclude general commitments, for instance, by way of legislation."*[801]

1144. Finally, the Claimants cite Salacusa to uphold that the umbrella clause can protect obligations arising from:

> *"less formal governmental actions, such as the oral statements by government officials and promises about investments published by a government in the press of promotional literature."*[802]

1145. However, it should not be forgotten that the author is referring to "*commitments and representations to foreign investors*" which, although they may be made less formally than through a contract, a concession or a license, must necessarily exist. Commitments of this nature, to which the author alludes, cannot be found in the acts of the Spanish representatives that are invoked in the Memorial on the Merits, as we have seen when analysing the legitimate expectations.

1146. In any case, if the Claimants cite Salacusa, with this and with the decision of the Annulment Committee on the CMS case invoked by the author, they must concede that:

> *"The effect of the umbrella clause is not to transform a contractual or other obligation governed by domestic law into an international obligation governed by international law. The source of the obligation, as well as its nature and scope, are delineated by the law under which it was originally made –in most cases, the law of the host country- (...) By virtue of the umbrella clause, a host state has an international duty to*

[800] Memorial on the Merits, paragraph 824.
[801] M. C. Gritón Salias, "*Do Umbrella Clauses Apply to Unilateral Undertakings*?", in C. Binder, U. Kriebaum, A. Reinisch y S. Wittich (Eds.), International Investment Law for the 21st. Century. Essays in Honour of Christoph Schreuer, Oxford University Press, 2009. CL-0083.
[802] Memorial on the Merits, paragraph 828.

> *respect its obligations concerning foreign investments despite the fact that those obligations remain subject to the law under which they were originally made."*[803]

1147. From the foregoing, it can be concluded that, once again the doctrine cited by the Claimants does not lead to their intended conclusion in relation to the protection of obligations of legal origin or other *erga omnes* unilateral acts under the scope of application of the umbrella clause.

1148. In sum, general regulatory provisions, presentations and press releases do not, *per se*, create legal obligations for the State under the scope of the umbrella clause. This conclusion is even clearer when such acts do not contain regulations specifically relating to foreign investments. This is a logical consequence of a literal reading ("*entered into*") and of the purposes of article 10(1), final subparagraph, of the ECT. Firstly, such a reading presupposes that there exists a *vis-á-vis* relationship between the State and the foreign investor; secondly, that in this *vis-á vis* relationship the State has undertaken a specific obligation to the foreign investor or to its investment; and thirdly, that the foreign investor has relied upon that commitment when making its investment.

1149. This specific bilateral relationship does not exist in this case, where the Claimant party decided to invest in a liberalised, but regulated, sector. There was no contract, no concession and no permit establishing a consensual bilateral relationship between the Claimants or their Investment and the Kingdom of Spain. There were no specific promises made by the Spanish State to the Claimants or their investment. Moreover, there is no evidence of the Claimants having made their investment whilst relying on the alleged promises which, according the Memorial on the Merits, were made to them and their investment by the Kingdom of Spain.

(3) The Kingdom of Spain has undertaken no obligations covered by the umbrella clause of the ECT to either the Claimants or their investment by virtue of Act 54/1997, RD 2818/1998, RD436/2004, RD661/2007 and RD 1614/2007.

(3.1) Introduction

1150. The Claimants maintain that:

> *"EPA 1997, RD 2818/1998, RD 436/2004 and, in particular, RD 661/2007 and RD 1614/2010, the central pieces or cornerstones of Regulatory Framework No. 1 in terms of rights and guarantees for investors in the Wind subsector, are the Spanish equivalent mutatis mutandis and ratione materiae to the Argentinean gas regulations referred to by LG&E, Enron and other similar awards, the breach of which led many arbitral tribunals to order Argentina to pay compensation to aggrieved investors."*[804]

1151. However, the Claimants do not conduct a comparative analysis of the Spanish and Argentinian legislation that allows them to reach the conclusion that both regulations contain "mutatis mutandis" and "ratione materiae" commitments covered by the umbrella clause. In contrast, as we have seen, the Argentinian regulation refers to the gas sector,

[803] Salacuse, J.W., The Law of Investment Treaties, p. 306. CL-0061.
[804] Memorial on the Merits, paragraph 829

monopolised by the State of Argentina and indirectly exploited through bilateral State-investor acts (concessions). The legislation that applied to these concession contracts contained specific obligations relating to foreign investment, such as tariff calculations in dollars and the update of tariffs in line with US indexes in order to protect the investor from fluctuations in the Argentinian currency[805]. This type of precept cannot be found in the Spanish legislation on renewable energy (which, furthermore, was enacted in a liberalised sector, in which there is no specific relationship established between the State and the investor, regardless of the investor's nationality).

1152. Moreover, the Award in the case of *Continental Casualty v. Argentina*[806], results in the requirement for regulations to specifically refer to foreign investors. More specifically, it states that:

> *"This can include the unilateral commitments arising from provisions of the law of the host State regulating a particular business sector and addressed specifically to the foreign investors in relation to their investments therein[807]".*

1153. It goes on to confirm that two Argentinean general regulations cannot generate obligations under the umbrella clause, expressly stating the following:

> *"Moreover, the provisions of the legislative regime that were changed were addressed either to the generality of Argentina's public or to a wide range of depositors and subscribers of a number of financial instruments[808]".*

1154. For its part, the Award in the case of *BG Group v. Argentina*[809] also analysed the specificity requirement in terms of the link between regulations and foreign investors and therefore resolved the claim presented by the investor on the basis of fair and equitable treatment, instead of on the basis of the umbrella clause, since:

> *"The rules announced by Argentina in the Information Memorandum and materialized in the Gas Law, the Gas Decree and the Bidding Rules were clearly not addressed at MetroGAS alone[810]".*

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[805] *Enron Corporation and Ponderosa Assets, L.P. v. the Argentine Republic* (ICSID Case No. ARB/01/3), Award of 22 May 2007: "Through the Gas Law and its implementing legislation, the Respondent assumed 'obligations with regard to investments': tariffs calculated in US dollars converted to pesos for billing purposes, linked to the US PPI and sufficient to provide a reasonable rate of return were intended to establish a tariff regime that assured the influx of capital into the newly privatized companies such as TGS and ensured the value of such investment."RL-0019. Along the same lines are the opinions issued in the Award in the case of *LG&E Energy Corp., LG&E Capital Corp. and LG&E International Inc. v. the Argentine Republic* (ICSID Case No. ARB/02/1), Decision on Liability, 3 October 2006. RL-0020.

[806] *Continental Casualty Company v. the Argentine Republic* (ICSID No. ARB/03/9), Award of 5 September 2008. CL-0064.

[807] Ibid, paragraph 301.

[808] Ibid, paragraph 302.

[809] *BG Group Plc. v. the Argentine Republic* (UNICTRAL), Award of 24 December 2007. RL-0061.

[810] Ibid, paragraph 365.

1155. In a contrived manner, the Claimants are attempting to attribute to the Spanish regulations governing the special regime on renewable energies, elements that will allow the Court to include them within the scope of protection of the umbrella clause. To this end:

a) They intend to restrict its scope of application to a specific group of subjects: the renewable energies sector and the wind energy sub-sector.[811]

b) It is their intention to attribute to these regulations the purpose of attracting investors.

c) It is their intention to include specific commitments to investors in these regulations.

d) It is their intention that the registration of a renewable facility in the RAIPRE creates a *vis-á-vis* relationship between the State and the renewable energy producing facilities.

1156. However, neither Act 54/1997, nor RD 2818/1998, nor RD 436/2004, nor RD 661/2007 nor RD 1614/2010 contain obligations covered by the umbrella clause since:

a) They are regulations enacted *erga omnes*, which are addressed to the wider public in general.

b) They were not enacted in order to promote foreign investment in Spain.

c) They do not contain specific commitments to the foreing investor or investments.

d) Registration of the facility in the RAIPRE does not determine the existence of a *vis-á-vis* relationship between the Spanish State and the registered facility.

1157. Firstly, and with regard to their scope of application, neither Act 54/1997, nor RD 2818/1998, nor RD 436/2004, nor RD 661/2007, nor RD 1614/2010, nor RD-Law 1/2012 stipulated a specific subjective scope of application. The first four were addressed to the public in general. They merely stipulated the objective requirements necessary for a facility to be integrated within the so-called "special regime" and the legal, economic and technical consequences of said integration. For its part, RD 1614/2010 amended RD 661/2007 in order to introduce measures for the economic sustainability of the Spanish Electricity Sector, wherefore its scope of application is the same as that of RD 661/2007. Finally, RD Law 1/2012 expressly excluded from its scope of application those facilities already registered in the RAIPRE, wherefore under no circumstances could it be addressed to the wind farms of the Claimants nor could it, therefore, contain in its Preamble commitments aimed at said wind farms.

1158. Secondly, none of these regulations were enacted with the purpose of attracting investors, but rather with the fundamental purpose of enabling the correct economic and technical integration of facilities in the Special Regime of the Spanish Electricity Sector. In

[811] Memorial on the Merits, par.830: "*EPA 1997, RD 2818/1998, RD 436/2004 and, in particular, RD 661/2007 and RD 1614/2010 contained unilateral commitments addressed to a particular business sector (renewable energy) and a specific subsector (Wind) for the purposes of attracting investors therein.*"

this sense, it is important to remember that the Spanish Electricity Sector is a closed system and that the integration of new facilities within this system cannot be done in just any manner, but needs to be done in such a manner that guarantees both the economic and technical sustainability of the Spanish Electricity System.

1159. Moreover, under no circumstance do any of these regulations contain any precept whatsoever that can be understood as a specific call for foreign investment. Therefore, these regulations cannot be included under the concept of "foreign investment laws" analysed by the aforementioned arbitration case law. Furthermore, the Spanish regulations are not comparable to the regulations governing the Argentinian gas sector, which were based on the existence of a concession and stipulated that tariffs were to be calculated in dollars and updated in line with US indexes in order to protect foreign investors from fluctuations in the Argentinian currently.

1160. Thirdly, neither Act 54/1997, nor RD 2818/1998, nor RD 436/2004, nor RD 661/2007, nor RD 1614/2010, nor RD Law 1/2012 contained specific commitments freezing any particular remuneration regime.

1161. At this point, however, we must highlight the ambiguity and lack of accuracy employed by the Claimants in determining the obligations which, according to them, would be covered by the umbrella clause of the ECT. In fact, according to the Memorial on the Merits:

> *"A reading in aggregate of the Six Feed-in Rights and subsequent statutory provisions in 2010 and 2012 show the Respondent's unequivocal promise of legal stability of Regulatory Framework No. 1"*[812]

1162. Apparently, according to the Claimants, the obligation that should be covered by the umbrella clause consists of the "stability of Regulatory Framework No. 1". This obligation is extracted by the Claimants from the "joint" reading of the six *feed-in* rights contained in RD 661/2007 and the subsequent RD 1614/2010 and RD-Law 1/2012. However, the obligation covered by the umbrella clause cannot result from a "joint interpretation" of a series of norms. It must expressly, clearly and unequivocally result from a specific relationship between the investor or its investment and the host State of the investment.

1163. Furthermore, it is important to note that the Claimants have not clarified what constitutes said "stability of Regulatory Framework No. 1", which they invoke as an obligation covered by the umbrella clause. Under the scope of the umbrella clause, the obligation must be specific and the Claimants have not specified what type of stability they claim.

1164. If they understand the freezing of the so-called "six rights" set forth in RD 661/2007 as an obligation of stability, this party would like to draw the Tribunal's attention to the fundamental fact that said obligation does not exist pursuant to Spanish law. We have already stated, and we will not insist further, that none of the regulations cited by the

[812] Memorial on the Merits, paragraph 838.

Claimants guaranteed the freezing of a particular remuneration regime. In this regard, we refer to the explanation provided in the foregoing point regarding the FET.

1165. Suffice it to recall that the Tribunal in the Charanne Case clearly established that RD 661/2007 did not create specific commitments regarding the freezing of regulatory provisions, particularly in view of the settled case law of the Kingdom of Spain[813].

1166. Fourthly, in a contrived manner, the Claimants are attempting to make the Tribunal believe that the registration of the special regime facility in the RAIPRE represents the establishment of a specific or *vis-á-vis* relationship between the Respondent and the renewable energy producing facilities.[814]

1167. However, as we have already explained in this Counter- Memorial in both the part relating to the facts and the part regarding Legitimate Expectations, registration in the RAIPRE does not represent the establishment of a *vis-á-vis* relationship between the State and the renewable energy producer by virtue of which the former promises to apply specific and unchangeable economic rights to the latter. This is so because the intention behind the registration in the RAIPRE is that of controlling the Spanish Electricity System and fulfilling the regulator's energy planning objectives. This obligation to register in an administrative register extends to all electricity production facilities, whether renewable or not, as a formal control mechanism. The RAIPRE is nothing more than a subsection of that register.

1168. There are currently over 44,600 owners and more than 64,400 facilities registered in the RAIPRE[815]. Over 5,200 changes of ownership have been recorded in the register[816]. It is unreasonable for the Claimants to claim that the State has undertaken specific commitments to all of these owners and facilities to freeze a particular remuneration regime merely due to the fact that they are registered. The Claimants cannot cite any sentence of the Supreme Court of the Kingdom of Spain that recognises that the State has, through registration in the RAIPRE, granted renewable energy producers any *authorisation* whatsoever, in favour of the facility, that generates an entitlement to a particular remuneration regime. In the same sense, the Arbitral Tribunal in the Charanne case rejected the argument that registration in the RAIPRE generated any type of commitment of the Kingdom of Spain to the investor[817].

1169. Moreover, the fact that registration is a necessary (but not unique) condition for the application of the remuneration regime, does not mean the freezing of said remuneration regime. Moreover, the facts themselves demonstrate that the wind farms in which the Claimants invested, despite being definitively registered in the RAIPRE in 2003, have experienced several changes to their economic regime, as introduced by RD 436/2004, RD 661/2007 and RD 1614/2010. Finally, reading the certificates of definitive registration of

[813] *Award in the case of Charanne B.V. and Construction Investments S.A.R.L v. the Kingdom of Spain*, 21 January 2006, paragraphs 494, 504 and 505. RL-0049.
[814] Memorial on the Merits, paragraph 836.
[815] Report of 26 April 2016 on the number of owners registered under Section 2 of the RAIPRE, of the Sub-Directorate General for Electricity, MINETUR R-0239.
[816] Report of 26 April 2016 on the number of changes of ownership under Section 2 of the RAIPRE, of the Sub-Directorate General for Electricity, MINETUR R-0240.
[817] *Award in the case of Charanne B.V. and Construction Investments S.A.R.L v. the Kingdom of Spain*, 21 January 2006, paragraphs 509 to 511. RL- 0049.

the Claimants' wind farms in the RAIPRE will suffice in order to confirm that no vis-á-vis relationship is generated by virtue of said registration and that no reference is made to the application and freezing of a particular remuneration regime.[818]

1170. In conclusion, the Spanish regulations invoked by the Claimants have no similarity whatsoever with the Argentinean gas regulations. Neither by virtue of said regulations nor of the registration of facilities in the RAIPRE has any *vis-á-vis* obligation been created between the Kingdom of Spain and the Claimants which generates in the favour of the latter any clear, express and unequivocal obligations regarding the freezing of a particular remuneration regime that could be covered by the umbrella clause of the ECT.

(3.2) Press releases and statements issued by the Ministry of Energy do not generate obligations covered by the umbrella clause.

1171. The Memorial on the Merits cites a series of press releases issued by the Ministry of Industry which allegedly would have given rise to obligations covered by the umbrella clause.

1172. Once again, none of these press releases meets the aforelisted requirements for generating obligations protected by article 10 (1) *in fine* of the ECT. In fact, a simple reading of said press releases will suffice to confirm that: (i) they do not include obligations of a specific nature, but rather are general communiques that describe the general thrust of the regulations to which they refer; (ii) at no point do they call for foreign investment or guarantee a particular treatment for foreign investors; (iii) and they contain no promises to freeze the remuneration framework.

1173. On one hand, the Memorial on the Merits refers to a series of communiques that have already been analysed in the section on legitimate expectations. Such is the case with: a) the official press conference after the approval of RD 661/2007, of 25 May 2007, which was limited to a summary of the content of said Royal Decree[819]; b) the official press release of 2 July 2010, announcing the alleged "agreement" between the Ministry of Industry and the AEE and PROTERMOSOLAR[820]; c) the official press release of 3 December 2010, in which the Government announced the approval of RD 1614/2010[821]; the official press release of 23 December 2010 announcing, among other measures, the publication of RD-Law 14/2010[822]; and the official press release of 27 January 2012 announcing the approval of RD-Law 1/2012, among other public deficit reduction measures[823]. Given that these communiques have been studied in the section on Legitimate Expectations, we refer to the part of said section which refers to the absence in these press releases of any commitments specifically aimed at the Claimants or their investments in relation to freezing a particular remuneration regime.

[818] Documents C-0061 and C-0062.
[819] Document C-0097.
[820] Document C-0152.
[821] Document C-0190.
[822] Document C-0164.
[823] Document C-0201.

1174. Notwithstanding, as regards the so-called "agreement with the wind sector" of 2 July 2010 that the Claimants seem to include under the scope of protection of the umbrella clause, it is important to make a clarification. Given its importance in relation to the specificity requirement of the umbrella clause of the ECT, it must be noted that neither the Claimants' wind farms nor the Claimants themselves formed part of the AEE in 2010, wherefore the Kingdom of Spain could hardly have undertaken any specific commitment to the Claimants or their investment by consulting with associations representing the wind and solar thermal sectors with regard to the initial draft of RD 1614/2010.[824]

1175. In any case, the cited "agreement of 2 July 2010" with the AEE and PROTERMOSOLAR associations in order to establish the basis of the draft of RD 1614/2010 did not generate, pursuant to Spanish law, any type of obligation that can be covered by the so-called umbrella clause, given that it is the result of a consultation process aimed at establishing the basis for the draft version of a future regulation. There was not even a guarantee that the subsequently enacted regulation would observe the terms of said alleged agreement. If said agreement had given rise to an obligation covered by the umbrella clause, there would have been no need to process and approve RD 1414/2010. We further insist that the latter also contains no obligations whatsoever covered by the umbrella clause. In fact, neither of the associations that allegedly negotiated the cited agreement of 2 July 2010 have invoked its existence in the claims filed nationally against the measures contested in this arbitration case. In short, the Claimants are attempting to change the nature of the result of this consultation process in order to convert it into an obligation protected by international law, something which, as we have seen, is neither accepted either by the Arbitral Tribunals nor in the doctrine cited by the Claimants themselves.

1176. In addition to the aforementioned statements, the Claimants also cite the statements made by Minister Sebastián on 26 January 2011 in the session of the Congress of Deputies in which RD-Law 14/2010 was validated[825]. In that session, as we have seen in the analysis of the section on Legitimate Expectations, Minister Sebastián expressly advised that all the measures adopted since 2009 (including the so-called "agreement with the wind sector") were aimed at eliminating the so-called tariff deficit, but had been insufficient, due to an unprecedented drop in demand for electricity. This led to the approval of RD-Law 14/2010, which imposed the obligation on all producers to pay an access toll, with the subsequent decrease in remuneration. Therefore, in no way did the Minister undertake, by virtue of his speech, obligations covered by the umbrella clause, but rather expressed the Government's firm intention to end the unsustainable situation of the Spanish Electricity System.

1177. The Claimants state that:

> *"The set of official statements by state officials of the Respondent shows the unequivocal promise of the Respondent of the stability of Regulatory Framework No. 1 for La Carracha and Plana de Jarreta. Such promise included in official statements*

[824] Witness statement of Alberto Ceña dated 18 February 2016. CWS-AC, paragraph 15.
[825] Document C-0166.

(orally or in writing) of Respondent's state officials is a unilateral act binding upon the Respondent as a matter of international law."[826] *(footnotes omitted).*

1178. Once again, we do not know what the Claimants mean by "promise of stability". We do not know if said stability implies the freezing of the so-called "six rights" which, according to the Claimants, were granted by RD 661/2007, or if it is limited to the maintaining of the essential characteristics of the renewable energy remuneration system established by the Spanish legislator in Act 54/1997, as objectives and limits of the regulatory power of the Government.

1179. If, by stability, the Claimants mean the freezing of the so-called "six rights", not even the extracts from the aforementioned communiques selected by the Claimants contain a clear commitment to freeze these "six rights". In fact, no promise to freeze the "six rights" can be found even when the press releases are read in their entirety.

1180. If, by stability, the Claimants mean the maintaining of the essential characteristics of the renewable energy remuneration system established in Act 54/1997 (access and dispatch priority and reasonable return), the press releases guarantee these essential characteristics through a common assumption: the guarantee of the sustainability of the Spanish Electricity System and the principle of reasonable return.

1181. In any case, the press releases invoked by the Claimants have generated no type of obligation whatsoever in Spanish law, wherefore they cannot give rise to obligations covered by the umbrella clause at international level.

(3.3) The other official communiques and acts cited by the Claimants reflecting "the investment climate in relation in renewable energies in Spain" do not contain obligations covered by the umbrella clause.

1182. Finally, the Claimants cite a non-exhaustive series of acts which, according to the Claimants, constituted:

"additional assurances about the legal and economic regime applicable in Spain to renewable energy facilities already registered in the RAIPRE, including that the regulatory framework was not going to be changed for them."[827]

1183. In this sense, the following acts are cited:

i) IDAE leaflets entitled "*el sol puede ser suyo*"[828];

ii) International roadshows allegedly held by Minister Sebastián to attract international investors[829] and

[826] Memorial on the Merits, paragraph 841
[827] Memorial on the Merits, paragraph 842
[828] Documents C-0089 and C-0090.
[829] In this sense they cite: an interview with Minister Miguel Sebastián Gascón on his tour of the United States in 2009 "Q&A: Official details Spain's big green-energy push", Houston Chronicle, November 2007 (C-0279); his trip to California, Colorado and Texas as part of the "Made in/Made by Spain Plan activities in USA - California-Colorado-Texas, 26-30 October 2009", 24 October 2009 (C-0280).

iii) Ceremonies organized for the inauguration of certain facilities such as the Gemasolar solar thermal plant in October 2011.[830]

1184. By citing these "acts", the Claimants demonstrate that they have not understood the nature and purpose of the umbrella clause, since it is their intention to convert any act that alludes to renewable energies, created for any type of technology and at any time, into a "specific commitment" undertaken by the Kingdom of Spain towards the Claimants or the La Carracha and Plana de Jarreta wind farms.

1185. The absence in these acts of specific commitments to the Claimants or their investments which could be covered by the umbrella clause, is evident. Let us see why.

1186. Firstly, two IDAE leaflets dated 24 May 2005 and 6 June 2007, entitled "*el sol puede ser suyo*" and relating to solar photovoltaic and solar thermal energy respectively, could hardly contain specific promises to the Claimants or their investments upon which they would have relied in order to make their investment in the wind sector in 2009, 2011 and 2012. The burden of proof with regard to the existence in these leaflets of an obligation to the Claimants or their investment, which gave them the confidence to invest in the wind sector in 2009, 2011 and 2012, lies with the Claimants and not the Respondent; a burden which has not been met.

1187. The same absence of proof applies with respect to the alleged "*roadshows*", which were supposedly held by Minister Sebastián to promote foreign investment in Spain. In fact, Minister Sebastián's trips to the US were made not with the objective of promoting US investment in Spain, but quite the opposite, rather to open the doors to Spanish businesses that could invest in the US. In particular, in the interview published in the Houston Chronicle, the journalist indicates that:

> *"Miguel Sebastian, the European nation's minister of industry, tourism and trade, recently toured several U.S. cities to encourage companies and governments to work with Spanish renewable energy firms"*[831].

1188. With respect to the programme of activities of the "*Made In/Made By Spain Plan"* in the United States[832], developed in October 2009, the title itself suggests that it is about selling what is made in Spain or by Spain in the United States, which excludes any type of activity for attracting international investment. The purpose of the programme was none other than that of bringing Spanish companies with environmentally friendly activities to the attention of US Public Administrations to increase the possibility that they could be contracted. That is to say, a purpose that had nothing to do with generating obligations that could be covered by the umbrella clause.

[830] In this respect, they invoke the article entitled "Gemasolar ya da luz a la noche" in Diario de Sevilla, 5 October 2011 (C-0283).
[831] C-0279.
[832] "Made in/Made by Spain Plan activities in USA - California-Colorado-Texas, 26-30 October 2009" published on October 24, 2009. C-0280.

1189. As regards the press release referring to the inauguration of the solar thermal plant by the King of Spain[833], which was attended by members of state, regional and local Public Administrations, and the related press articles[834], it should be noted that none of these documents make reference to attracting international investment for similar projects or to the economic regime applicable to its operation, much less to the wind sector. They merely inform of the inauguration of a plant that was considered to be relevant due to its size and significance, in what constitutes a political activity with no connection whatsoever to the present dispute.

1190. Finally, the statement of President Mariano Rajoy on Televisión Española, in the interview given on 26 October 2015, also makes absolutely no reference to the Claimant or their investment. He does not even speak of wind farms in general.

1191. Ultimately, it is clear that no unilateral statement of the Kingdom of Spain exists among the statements invoked by the Claimant that could have created specific obligations with respect to the economic regime applicable to the wind facilities to which the present dispute refers, and that could be covered by the umbrella clause.

(4) The Claimants have failed to prove that they made their investment relying on the promises of "stability" contained in the regulations and other unilateral acts they invoke.

1192. To all of the above, we must add that not a single document exists that proves that the Claimants made their investment relying on the promises of stability that they now invoke as covered by the umbrella clause.

1193. In this sense, the few documents provided by the Claimant in relation to their investment and the *due diligence* process carried out prior to the investment, underline the fact that they accepted the risk that the remuneration regime that existed at the time could change[835]:

[833] Web page of the Royal Household regarding the inauguration of the Gemasolar solar thermal plant on 4 October 2011. C-0281.
[834] These articles merely indicate the identity of the promoters and constructors, as well as some of the technical details of the plant and the innovation it represents.
[835] Presentation entitled "Project Nova, Potential Acquisition in the Area of Renewable Energies", dated 18 August 2009. Documento C-0099t. (original in German).

4

Risks within the Business Areas

Segment	Possible Risks	Risk
Price changes	- Changes in the prices of hardware components and delivery times - Weakening of the general demand for electricity from installations that generate renewable energy - Availability of project financing - Risk of the failure of individual project developments and of cost overruns for turnkey projects - Changes in legal conditions so that Nova's commitments in individual regions or lines of business become unattractive	Medium to high
Power generation	- The main risk is in the wind level and the irradiation values in the solar area for the relevant periods - Based on readily foreseeable and uniform business performance, funding requirements and return flows from investments are easy to plan for. The compensation models (such as the Renewable Energies Act) make an important contribution to this	Low
Services	- Payment difficulties on the part of project companies constitute a serious risk, and Nova may feel compelled to terminate the long-term contractual relationships - This is a very manageable risk because consulting and support contracts are long-term; moreover, most of the contracts have minimum compensation provisions	Low
Conclusion	Risks can be well-diversified and further reduced by investing in various technologies (wind, solar, etc.) and regions (Germany, Spain, France, Poland, Czech Republic, etc.)	

(5) The alleged obligation covered by the umbrella clause was neither addressed to the Claimants nor their investment.

1194. Even if, for merely hypothetical purposes, we were to assume, *quod non*, that the Spanish regulations generated an obligation to freeze the so-called "six rights" contained in RD 661/2007, said obligation would not have been undertaken towards the Claimants or their investments (equity holdings).

1195. Indeed, according to the Memorial on the Merits, the investment that gave rise to the claim filed by Claimants consists of a direct stake in the capital of the companies that own two wind farms (La Carracha S.L. and La Plana de Jarreta S.L.).

1196. The obligations that the Claimants sustain as covered by the umbrella clause would only be enforceable by the companies that owned the facilities, since they refer to regulations RD 661/2007 and RD 1614/2010, addressed to such plant owners.

1197. Said link between the alleged obligations, covered by the umbrella clause according to the Claimant, and the Plants, is also implicitly recognised in the Memorial on the Merits itself when defining what the Claimant refers to as the "Six Rights" which, due to their content, can only apply to or be recognised for owners of wind farms.

1198. This same conclusion also extends to the obligations that, according to the claimants, result from alleged unilateral statements since, once again, they refer to regulations of the so-called Regulatory Framework No. 1 and it can therefore be concluded that they would only have been undertaken towards wind farm owners.

1199. Ultimately, even if we accept the theory presented by the Claimants, the regulations of Regulatory Framework No.1 were not addressed to third party stakeholders in the facility-owning entities, but only and exclusively to the facility owners themselves.

1200. Consequently, even if, for merely hypothetical purposes, we were to accept the existence of the obligations invoked by the Claimants, the truth is that said obligations could only be recognised for or refer to the renewable energy facilities and, under no circumstances, to third parties who merely hold a stake or debt, not in the facilities themselves, but in the companies that own said facilities.

1201. Therefore, the essential requirements for the alleged obligations that the Claimants claim have be entered into with them or their investment, whatever their origin, have not been met.

(6) The Kingdom of Spain has not breached the umbrella clause.

1202. Finally, if we were to hypothetically accept the theory of the Claimants that the Kingdom of Spain, by virtue of such acts, were to have entered into some type of specific commitment to the Claimants or their investment, *quod non*, said commitment would be limited to the application of the legal regime in force in its entirety and not to two articles of two regulations.

1203. As acknowledged in the Memorial on the Merits[836], Act 54/1997 is the "corner stone" of this legal framework and enshrines two basic guarantees for renewable energy producers: a) the right to priority access and dispatch, and b) the right to obtain a premium which, when added to the market price, allows them to obtain a "reasonable return according to the cost of money on the capitals market", as stipulated in article 30(4). This principle of "reasonable return" is deliberately omitted by the Claimants from their Statement.

1204. This legal regime has been interpreted in several Sentences of the Supreme Court of the Kingdom of Spain, of which the Claimants were aware when they made their investment. Said statements affirm that:

> "The *remuneration* regime analysed does not guarantee, on the contrary, for facility owners in the special regime the intangibility of a particular level of profit or income by virtue of relation with that obtained in previous years, or the indefinite permanence of the formulas used to set the premiums." [837]

1205. The ultimate interpreter of Spanish Law, the Supreme Court, has categorically and repeatedly denied that a regulatory provision can establish the intangibility of a particular level of specific profit or the indefinite permanence of the formulas used to set the same, pursuant to the case law set out in previous sections.

1206. The obligation that the Claimants wish to elevate to international scope, by virtue of the umbrella clause, simply does not exist in Spanish law. The only obligation that Spanish law has generated in favour of renewable energy producers is that of obtaining, as well as access and dispatch priority, a "reasonable return" on their investment. This is how the Supreme Court has interpreted said Law.

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[836] Memorial on the Merits, paragraphs 131 and 135.

[837] Among many others, the Judgement from Chamber Three of the Supreme Court of 25 October 2006, RCA 12/2005, reference case law EDJ 2006/282164. Finding of Law Three. R-0138.

1207. The new measures of the Kingdom of Spain retain the essential lines of the public subsidies system. That system still consists of a market price supplement through a subsidy that places the renewable energy producer in a competitive market position. The subsidies allow renewable energy facilities to recover their investment costs and their operation and maintenance expenses, as well as guaranteeing a return of around 7.398%[838]. Furthermore, the rights to priority access to the network and to the purchase of all energy produced are retain. Spain has fulfilled its guarantee of stability.

1208. The Claimants were fully aware that the energy sector is a regulated sector in Spain, and is therefore subject to regulatory changes, a business risk which the Claimants freely, voluntarily and consciously accepted. We use the term 'consciously' because the very nature of energy regulations (in a regulated sector) makes energy a changing issue, subject to the energy policy of the government and the guidelines and directives of the European Union.

1209. In this sense, in the case of *Perenco v. the Republic of Ecuador*, the Tribunal affirmed that:

> *"Where a State has duly considered a legislative/regulatory policy, as was the case in 1994 when Ecuador resolved that it was in the nation's interest to move from service to participation contracts, governmental decisions taken thereafter must, during the lifetime of such contractual arrangements maintain fidelity to that policy framework. This is not to say that the policy framework is frozen and cannot be changed because this is not so unless the State has expressly stabilised its law vis-à-vis its contractual counterparty".* [839]

1210. In the Plama case, the Tribunal also reached the conclusion that:

> *"the Tribunal believes that the ECT does not protect investors against any and all changes in the host country's laws.(...) It does not appear that Bulgaria made any promises or other representations to freeze its legislation on environmental law to the Claimant or at all."*[840]

1211. Moreover, Wälde understands that the umbrella clause cannot be equated with a sort of clause on the stabilisation or "freezing" of the regulations in force at the time the contract was entered into, stating:

> *"My solution to the question whether the umbrella clause is the equivalent of the stabilization clause but on the level of treaty law (compare Benhamida, supra, footnote 8) is that the umbrella/sanctity of contract clause may not "freeze" applicable law, as some stabilization clause provisions purport to do, but that it prevents the*

[838] Pursuant to the Third Final Provision of Act 24/2013, of 26th December, the specific figure for facilities already operating is around 7.398 percent return for a standard facility, as set out in Section IV.D.4.2 of this Counter-Memorial R-0076.

[839] *Perenco Ecuador Limited v. Republic of Ecuador and Empresa Estatal Petróleos del Ecuador*, ICSID Caso No. ARB/08/6, Decision on Remaining Issues of Jurisdiction and Liability, 12 September 2014, paragraph 562. RL-0032.

[840] *Plama Consortium Limited v. Republic of Bulgaria*, ICSID Case No. ARB/03/24. Award of 27 August 2008. RL-0034.

> *State from invoking its sovereign and regulatory powers in an abusive way to escape from contractual commitments assumed earlier. This is one of the functions of the contractual stabilization clause, but it does not cover the "freezing" automatically. There may be changes in the regulatory context of a project which are of a general nature, non-discriminatory and justified by legitimate public policy adjustment of the legal context to changing circumstances and international standards. Such changes should, as a rule, not be caught by the "sanctity of contract" clause, as they do not represent an abusive reliance on sovereign powers to undermine contractual commitments."*[841]

1212. The fact that the wind farms in which the Claimants invested do not currently receive more subsidies is due to the projects having already received, in previous years, the "reasonable return" guaranteed by the regulator, as it will be explained in detail in the sections on expropriation and damages.

1213. The protection clause of article 10(1) of the ECT, if it were to have applied in this case, would have been fully observed by the Kingdom of Spain.

N. <u>The Kingdom of Spain has observed article 13 of the ECT.</u>

(1) Introduction

1214. The Memorial on the Merits states that the measures adopted by the Kingdom of Spain, the object of this arbitration, constitute the gradual, indirect and unlawful expropriation of the Claimant's alleged investment in our country, based on the provisions of article 13(1) of the ECT.[842]

1215. To this effect, they begin with a partial definition of the concept of indirect expropriation based on arbitral awards which, as it will see, either do not apply to this case or for which the requirements assessed therein have not been proven to exist in this case.

1216. They also consider that their particular case fits with the profile of unlawful expropriation, as two of the four elements contained in article 13.1 of the ECT are absent: "*In this case, the Respondent has offered no compensation whatsoever to the Claimants for the significant deprivation of their rights to peacefully manage and commercially enjoy their investment, two fundamental attributes of rights of ownership. Moreover, the form in which the Respondent has expropriated the investment falls far short of compliance with standards of due legal process in a modern country*"[843].

1217. However, as analysed below, the Claimants fail to include any reference to what that due procedure should have been or what prompt and adequate compensation they understood to be missing. Furthermore, they have failed to include any analysis of the effective presence of a public interest in the measures adopted by Spain and their proportional and non-discriminatory nature.

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[841] The "Umbrella" Clause in Investment Arbitration: A Comment on Original Intentions and Recent Cases. Thomas W. Wälde. HEINONLINE 6 J. World Investment & Trade 183 2005, página 200. (RL-0055).
[842] Memorial on the Merits, paragraph 715 to 782.
[843] Memorial on the Merits, paragraph 721.

1218. Faced with the allegations set out in the Memorial on the Merits, this party will prove that the premises required in order to conclude the existence of a measure equivalent to an expropriation do not exist.

1219. As a starting point, and with a view to clarifying the confusion that the Claimants attempt to generate, it is important to note that their investment, as defined in the Memorial on the Merits itself[844], consisted of the ownership of 74% of the shares in the companies Parque Eólico La Carracha S.L. and Parque Eólico Plana de Jarreta S.L. That is, the subject of the investment was not the wind farms, but a stake in the companies that own said wind farms.

1220. Furthermore, it is important to remember that wind farms receive remuneration for the energy they produce. Said remuneration consists of the market price and a subsidy. Therefore, with respect to the development of energy production activities, the Claimants have not been able to demonstrate a single act of interference by the Kingdom of Spain. This is simply because there has been no interference. Equally, the Claimants have failed to provide any proof whatsoever that the measures associated with this arbitration case prevent the wind farms from producing and selling at market price all of the electricity that they are able to generate.

(2) Non-existence of indirect expropriation due to lack of object.

1221. The definition of expropriation under the ECT is conditional upon the existence of an "asset" owned by the claimant investor which is expropriated by the respondent Contracting Party. This is so according to section (3) of Article 13 of the ECT, which was omitted by the Claimants.

1222. Therefore, in order to demonstrate the existence of an expropriation of an asset, pursuant to Article 13 (3) of the ECT, the Claimant must prove (i) the existence of the expropriable right or asset, in accordance with the law of the host State, (ii) possession or ownership of the same, and (iii) the existence of a causal relationship between the measure adopted by the State and the impact of the same on the ownership of said asset. As shown below, none of said requirements exist in this case.

1223. As regards the expropriable asset or right, the Claimants cryptically consider that "(through) *the approval of Regulatory Framework No. 2 and Regulatory Framework No. 3, the ability to peacefully manage and commercially enjoy the wind farms has been seriously affected, which has generated an effect equivalent to an expropriation by the Respondent, although it has not physically taken possession of the wind farms*"[845].

1224. The alleged powers to peacefully enjoy the profits of the investment and the ability to freely manage and administer the investment do not constitute an expropriable asset in the sense of article 13(3) of the ECT in relation to Article 1 (6).

1225. We must remember that the Claimant's investment consists of a 74% shareholding in Parque Eólico La Carracha S.L. and Parque Eólico Plana de Jarreta S.L., which, in turn, are

[844] Memorial on the Merits, paragraph 49 to 51, Section 2 of Part 2.
[845] Memorial on the Merits, paragraph 731.

the owners of the wind farms. Therefore, the Claimants had no right to directly receive the future subsidies claimed and have not proven that they had the power to directly administer and manage the wind farms. Indeed, the Claimant's investment took the form of shares in the companies that own the farms and not directly in the wind farms and their earnings themselves.

1226. Furthermore, pursuant to Spanish law, it is impossible for the Claimants to hold ownership of possible future earnings, derived from subsidies, that they merely hoped to receive. International case law has recognised, when determining what rights are susceptible to expropriation, that the law of the host State will apply. Along this same line, in *Suez v. Argentina*, the Court stated that:

> *"To assess the nature of these rights in a case of alleged expropriation of contractual rights, one must look to the domestic law under which these rights were created. APSF´s and the Claimants contractual rights in the Concession, which the claimants allege were expropriated, were created by the legal framework and the Concession contract described above*[846]*."* (Emphasis added).

1227. Any investment susceptible to expropriation must consist of a right or asset that is duly constituted, defined, formed and recognised by the laws of the host State, which provides protection under the corresponding investment treaty[847]. This is because international law on expropriations only governs the substantive protections for rights over property or other economic interests, but not the process by which said rights are created[848]. This same theory was adopted by the Tribunal in the case of *EnCana v. Ecuador:*

> *"184. […] for there to have been an expropriation of an investment or return (in a situation involving legal rights or claims as distinct from the seizure of physical assets), the affected rights must exist under the law which creates them, in this case, the law of Ecuador."*[849] (Emphasis added).

1228. It is striking that this Award is invoked by the Claimants[850] in order to raise the dissenting opinion formulated by Professor Grigera Naon with respect to the concept of "*substantial deprivation",* whereas no mention is made, on the other hand, of the parts concerning the concept of "*expropriable asset or right"* as a precept to said "*deprivation".*

1229. In Spanish law there is a clear distinction between an acquired right and an expectation. Therefore, in order to determine whether a compensable harm exists, the injured party must have a right and said right must have been attached to its patrimonial assets. This has been determined to be so on several occasions by the Supreme Court:

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[846] *Suez, Sociedad General de Aguas de S.A., and InterAgua Servicios Integrales del Agua S.A. v. Republic of Argentina*, Decision on Liability, 30 July 2010. RL-0068

[847] UNCTAD Series on Issues in International Investment Agreements, Expropriation, United Nations Series, New York and Geneva, 2012, page 22, ("UNCTAD Expropriation Report"). RL-0070.

[848] Ibid.

[849] *EnCana Corporation v. Republic of Ecuador*, LCIA Case No. UN3481, UNCITRAL (formerly Corporation EnCana Corporation v. Government of the Republic of Ecuador) Final Award of 3 February 2006, paragraph 184. RL-0027.

[850] Memorial on the Merits, paragraph 757.

> *"Another criteria to be applied in order to determine the existence of compensable harm, especially when considering the possible deprivation of rights and interests concerning patrimonial assets, lies in determining whether the rights or interests from which the eventual injured party has been deprived were actually attached to its patrimonial assets, or they constitute mere expectations of rights - not susceptible to consideration from the point of view of their ownership by those who believe they are called to make them effective - or values that belong to the community as a whole, for which the burdens imposed by the legal system in relation to their acquisition have not yet been satisfied".*[851] (Emphasis added).

1230. In particular, the Supreme Court has expressly recognised that the right to receive the premiums and tariffs of the Spanish Electricity Sector cannot be recognised, but that it is a mere expectation not attached to the patrimonial assets of the investors. Thus, the Supreme Court states that:

> *"The argument must be rejected since what would have existed in favour of the appellant would have been an expectation to obtain said right as it had not been included to form part of its patrimonial assets".*[852]

1231. The foregoing has also been confirmed by Spanish doctrine:

> *"The effectiveness requirement demands a harmful effect on the assets or rights of the injured party, as well as being an actual and real damage, excluding future damages and the mere frustration of expectations. And it is precisely at this point where the theory of acquired rights (iura quaesita) enters into play. If we apply to the case the doctrine established by the Constitutional Court in STC 27/1981 of 20 July «we must consider that the concept of individual right cannot be confused with the ius quaesitum», that is, that an acquired right, until it is not consolidated, remains in the sphere of an expectation of a right, and therefore, the frustration or impairment of the same is not compensable by the Administration."*[853] (Emphasis Added).

1232. And international doctrine:

> *"189. Only legitimate, consolidated patrimonial rights will be expropriable; conversely, the legislative effect of the expectations of private individuals effected by a law shall not be compensable. The expectations that private individuals may have by virtue of a law cannot be expropriated by a subsequent law that eliminates them, given that only the deprivation of assets and rights, and even legitimate consolidated interests, can constitute an expropriation. And of the latter, only*

[851] Judgement of the Third Chamber of the Supreme Court of 17 December 1997, RJ\1998\1677. (R-0136) Likewise, Judgement of the Third Chamber of the Supreme Court of 28 May 2001, app. 462/1997. (R-0248), Judgements of the Supreme Court of 11 November 1992 (R-0245); Judgement of the Supreme Court of 16 November 1992 (R-0246); and Judgement of the Supreme Court of 23 November 1992 (R-0247).

[852] Judgement of the Supreme Court, Third Chamber, sect. 3; of 9 October 2007, app. 13/2006. (R-0140).

[853] The scope of application of the principle of legality: a latent and unresolved debate. Regarding the Judgement of the Supreme Court of 13 January 2012 on higher arts education, Xavier Codina García-Andrade, BIB 2010\2824M Civitas, Spanish Journal of Administrative Law No. 155/2012. R-0244.

> *deprivations of certain effective and actual rights will be compensable, but not hypothetical and eventual rights."*[854] (Emphasis added).

1233. Therefore, neither in accordance with international law nor Spanish law is the expropriation of hypothetical and eventual rights possible, but rather, conversely, only certain effective and actual rights are susceptible to expropriation.

1234. As regards arbitral doctrine, it is important to note that in *Nations Energy v. Panama*[855], the Tribunal analysed whether the claimants had an acquired right with respect to the provisions contained in the law. Thus it states that:

> *"641. The Claimants maintain that Act 6 would be retroactive and therefore in violation of the Panamanian constitution.*
>
> *642. "The Arbitral Tribunal does not share this point of view and believes that Act 6 is not retroactive as it does not have the effect of revoking acquired rights and only applies to the future.(...)*
>
> *646. In actual fact, the Claimants are confusing the principle of non-retroactivity with the principle of immediate effect of the new act for the future. Act 6 does not have the effect of retroactively cancelling acquired rights but rather of modifying the conditions in which the holders of tax credit that has not yet been used may apply this in the future."* [856] (Emphasis added). (Footnotes omitted).

1235. The Award in the *Charanne* Case expressly confirms this doctrine:

> *"Thus, the Claimants invested in shares (article 1(6)(b) of the ECT).*
>
> *The Claimants […] claim to have invested in returns (article 1(6)(e) of the ECT) […] According to the Claimants, by reducing the returns of the plants, the 2010 norms would have expropriated such returns. The Arbitral Tribunal is not convinced by this argument. The object of the investment was not the returns, but the company X. […] an investment protected under Article 1(6) must be owned or controlled by the investor, and that the Claimants neither own nor control the future returns of the plants, which do not constitute rights attached to their investment. The Tribunal therefore considers that the Claimants invested in shares (Article 1(6)(b) of the ECT), and not in returns."*[857]

1236. It is remarkable that the Claimants expressly cite the award in the Charanne Case to highlight the concept of indirect expropriation and justify that, in this arbitration proceeding, the "*facts of the claim go far beyond a mere reduction in the value of the*

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[854] El Arbitraje en los litigios de expropiación de Inversiones extranjeras, Iñigo Iruretagoinea Agirrezabalaga, Bosh, 2010, page 291 RL-0069.

[855] *Nations Energy Inc. Electric Machinery Enterprises Inc and Jaime Jurado v. Republic of Panama*, ICSID Case No. ARB/06/19, Award of 24 November 2010, ("Nations Energy"). RL-0040.

[856] *Nations Energy Inc. Electric Machinery Enterprises Inc and Jaime Jurado v. Republic of Panama*, ICSID Case No. ARB/06/19, Award of 24 November 2010, ("Nations Energy"), paragraphs 635 to 648. RL-0040.

[857] Award in the case of *Charanne B.V. and Construction Investments S.A.R.L v. the Kingdom of Spain*, 21 January 2006, paragraphs 458 to 459 RL-0049.

Companies associated with the Project[858]", whereas they completely omit any and all reference to the definition of the object of the investment that must be considered for the purposes of expropriation.

1237. In this regard, the Claimants neither explain nor prove that, on date on which the disputed measures were approved, they held an acquired, constituted and recognised right to receive a subsidy and the power to administer and manage the wind farms, which the claim have been expropriated. They have also failed to demonstrate, therefore, that any legislative measure approved by Spain within the regulatory framework governing renewable energies represents an expropriation.

1238. This therefore leads to the inevitable conclusion that there existed no expropriation whatsoever on the basis of a lack of an object susceptible to said expropriation.

1239. Thus, in the words of the Tribunal in the case of *Nations Energy v. Panama*: "*the Claimants are confusing the principle of non-retroactivity with the principle of immediate effect of the new act for the future*". This is so because the new regulations do not "*have the effect of retroactively cancelling acquired rights but rather of modifying the conditions in which the holders of tax credit that has not yet been used may apply this in the future*[859]".

1240. In conclusion, the object of the investment was not the returns that the wind farms could receive, but the indirect shares in the entities that owned said wind farms. In this respect, the Claimants neither possess nor control the future revenues of the wind farms, much less the expected revenues. Neither do they possess nor control the power to administer and dispose of them, given that these rights have not been attached to their patrimonial assets. Therefore, the rights that have supposedly been invoked do not constitute an expropriable asset in the sense of article 13(3) of the ECT in relation to the concept of protected investment contained in article 1(6) of the ECT.

(3) Under no circumstances can the measures adopted by Spain be considered an expropriation.

1241. Notwithstanding, even in the event that the Tribunal were to understand that the measures have affected the investment, by considering that an expropriable object does exists, the recognition of an indirect expropriation would still not apply. This is so because the contested measures are regulatory acts that generate no obligation to compensate.

1242. Indeed, even if we were to accept, for merely dialectical purposes, that the Claimants hold an asset or right susceptible to expropriation, the macroeconomic control measures adopted by Spain are a consequence of the State's power to legislate, for reasons of public interest, on highly regulated matters.

[858] Memorial on the Merits, paragraph 759.
[859] *Nations Energy Inc. Electric Machinery Enterprises Inc and Jaime Jurado v. Republic of Panama*, ICSID Case No. ARB/06/19, Award of 24 November 2010, ("Nations Energy"), paragraphs 635-648. RL-0040.

1243. The distinction between a regulatory measure with no compensation and an indirect expropriation is a key issue in modern international law on investments[860], as reiterated in all the doctrine invoked, even by the Claimants, despite the fact that they fail to mention such references. Both domestic and international case law and doctrine accept that acts of State are not subject to compensation when they are an expression of their regulatory power (*"police powers").* In fact, as analysed below, this statement is not called into question by the standards invoked by the Claimants.[861]

1244. Furthermore, in arbitral case law we can refer to the case of *Fireman's Fund v. Mexico* in which the Tribunal, when analysing the difference between a regulatory measure not subject to compensation and a measure equivalent to an expropriation subject to compensation, determined the following:

> *"To distinguish between a compensable expropriation and a non-compensable regulation by a host State, the following factors (usually in combination) may be taken into account: whether the measure is within the recognised police powers of the host State; the (public) purpose and effect of the measure; whether the measure is discriminatory; the proportionality between the means employed and the aim sought to be realised; and the bona fide nature of the measure."*[862] (Emphasis added).

1245. In the same sense, in *CME v. the Czech Republic*, the Tribunal determined that the regulatory measures adopted by a State in the proper execution of its domestic law must be distinguished from acts of State depriving of rights and property, and that, indeed, regulatory measures are frequently adopted in order to avoid the use of private property contrary to the general welfare of the host State:

> *"603. Of course, deprivation of property and/or rights must be distinguished from ordinary measures of the State and its agencies in proper execution of the law. Regulatory measures are common in all types of legal and economic systems in order to avoid use of private property contrary to the general welfare of the (host) State"*[863] (Emphasis added).

1246. Likewise, in *Saluka v. Czech Republic*[864] the Tribunal determined that States are not liable to pay compensation to a foreign investor when, in the normal exercise of the regulatory powers, they adopt non-discriminatory and bona fide regulations that are aimed at the general welfare.

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[860] UNCTAD Series on Issues in International Investment Agreements, Expropriation, United Nations Series, New York and Geneva, 2012, page 78, ("UNCTAD Expropriation Report"). RL-0070.
[861] Memorial on the Merits, paragraph 737 to 760.
[862] UNCTAD Series on Issues in International Investment Agreements, Expropriation, United Nations Series, New York and Geneva, 2012, pages 87 to 88, ("UNCTAD Expropriation Report"). RL-0070.
El Arbitraje en los litigios de expropiación de Inversiones extranjeras, Iñigo Iruretagoinea Agirrezabalaga, Bosh, 2010, paragraph 206. RL-0069.OCDE.
"Indirect Expropriation" and the "Right To Regulate" in International Investment Law Working Papers on International Investment, No. 2004/4, 2004, Page 18 R-0231.
[863] *CME Czech Republic B.V. v. Czech Republic*, UNCITRAL, Partial Award, 13 September 2001, paragraph 603. CL-0032.
[864] *Saluka Investments BV v. Czech Republic*, UNCITRAL, Partial Award, 17 March 2006 ("Saluka"), paragraphs 255-265. (CL-0113), also invoked by the Claimants on analysing the FET and Py SC standard (Memorial on the Merits, paragraphs 1202 and 1258).

1247. Furthermore, in *Paso Energy International Company v. Argentine Republic*, the Tribunal ruled that general regulations are not equivalent to indirect expropriations, and that only when said regulations are unreasonable (that is unfair, disproportionate or discriminatory) can they be considered equivalent to an expropriation[865].

1248. In addition, when determining the existence of a measure equivalent to an expropriation, international case law and doctrine also consider whether the adopted measure is reasonable or proportional to the aim or public interest sought[866]. That is to say that there must be a reasonable balance between the measure that affects the investor and the public interest it seeks to protect[867].

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[865] *El Paso Energy International Company v. Argentine Republic*, ICSID Case No. ARB/03/15, Final Award, 31 October 2011, paragraph 240. CL-0062.

[866] *Técnicas Medioambientales Tecmed, S.A. v. United Mexican States*, ICSID Case No. ARB (AF)/00/2, Award of 29 May 2003 ("Tecmed"), paragraph 122 (CL-0061 English version); El Arbitraje en los litigios de expropiación de Inversiones extranjeras, Iñigo Iruretagoinea Agirrezabalaga, Bosh, 2010, pages 304-309. CL-0046.

[867] Tecmed, paragraph 122. "After establishing that regulatory actions and measures will not be initially excluded from the definition of expropriatory acts, in addition to the negative financial impact of such actions or measures, the Arbitral Tribunal will consider, in order to determine if they are to be characterized as expropriatory, whether such actions or measures are proportional to the public interest presumably protected thereby and to the protection legally granted to investments, taking into account that the significance of such impact has a key role upon deciding the proportionality.140 Although the analysis starts at the due deference owing to the State when defining the issues that affect its public policy or the interests of society as a whole, as well as the actions that will be implemented to protect such values, such situation does not prevent the Arbitral Tribunal, without thereby questioning such due deference, from examining the actions of the State in light of Article 5(1) of the Agreement to determine whether such measures are reasonable with respect to their goals, the deprivation of economic rights and the legitimate expectations of who suffered such deprivation. There must be a reasonable relationship of proportionality between the charge or weight imposed to the foreign investor and the aim sought to be realized by any expropriatory measure.[141]

To value such charge or weight, it is very important to measure the size of the ownership deprivation caused by the actions of the state and whether such deprivation was compensated or not.142 On the basis of a number of legal and practical factors, it should be also considered that the foreign investor has a reduced or nil participation in the taking of the decisions that affect it, partly because the investors are not entitle to exercise political rights reserved to the nationals of the State, such as voting for the authorities that will issue the decisions that affect such investors.

The European Court of Human Rights has defined such circumstances as follows:

"Not only must a measure depriving a person of his property pursue, on the facts as well as in principle, a legitimate aim « in the public interest », but there must also be a reasonable relationship of proportionality between the means employed and the aim sought to be realised...[...]. The requisite balance will not be found if the person concerned has had to bear "an individual and excessive burden" [...] The Court considers that a measure must be both appropriate for achieving its aim and not disproportionate thereto.143 ....non-nationals are more vulnerable to domestic legislation: unlike nationals, they will generally have played no part in the election or designation of its authors nor have been consulted on its adoption. Secondly, although a taking of property must always be effected in the public interest, different considerations may apply to nationals and non-nationals and there may well be legitimate reason for requiring nationals to bear a greater burden in the public interest than non-nationals.144 The Arbitral Tribunal understands that such statements of the Strasburg Court apply to the actions of the State in its capacity as administrator, not only to its capacity as law-making body." CL-0046.

1249. Therefore, in order to determine whether a regulatory measure is expropriatory, one must consider whether such reasonableness and proportionality jointly, and not separately, exist in said measure with respect to the public interest sought.[868]

1250. In order to determine or define what the public interest is, international case law indicates that there is a presumption in favour of the State that it acts in good faith and in the public interest[869]. Therefore, the burden of proof that the measure is not in the public interest and was adopted in bad faith rests with the Claimant.[870]. However, in this case it is obvious that the measures adopted by Spain were in the public interest.

1251. As is known, and as we have demonstrated in the present statement, the tariff deficit, which was largely generated by renewable energies, including wind energy[871], is a threat not only to the Spanish Electricity System, which could collapse, but also to the Spanish economy in general, generating an accumulated debt of extraordinary dimensions for all consumers. Indeed, the measures adopted are intended to prevent the collapse of the electricity system and, therefore, have a clear purpose of public interest, deserving of protection.

1252. Furthermore, the measures adopted by Spain were, under no circumstances, discriminatory. The non-discrimination requirement demands that the measures do not affect a single subject and are not adopted for a group of subjects for reasons of race, nationality or other similar reasons[872].

1253. Protecting the public interest led Spain to adopt measures in all sectors of society and for all special regime technologies, so the argument sustained by the Claimants[873] that the measures are discriminatory towards the wind energy sector, is unfounded and lacks any legal basis, without prejudice to later indications in this respect.

1254. Ultimately and contrary to the claims of the Claimants, the disputed measures have, firstly, allowed the wind farms in which the Claimants indirectly invested to obtain a reasonable return on their investment, which has allowed them to cover their investment costs and operating costs and obtain returns in excess of 7.398%, and they are currently still able to sell their energy at pool price, with access and dispatch priority.

1255. Secondly, these measures have allowed the deficit to effectively be reduced, as detailed in section IV. A. (3) of the present Memorial, and have been viewed favourably by domestic courts, international organisations and the markets[874]. Furthermore, it is important to

[868] Ibid . UNCTAD Expropriation Report RL-0070.
[869] UNCTAD Expropriation Report, page 80. RL-0070.
[870] UNCTAD Expropriation Report, page 80. RL-0070.
[871] This recognition of the need to adopt the measures is set out in, among other sources, the APPA-Greenpeace Press Release on the Bill for the Promotion of Renewable Energies, of 20 May 2009 (R-0167) and the Arguments of the AEE to the CNE during hearing proceedings with the Electricity Advisory Board concerting the Draft Royal Decree that regulates and amends certain aspects relating to the special regime, page 2. R-0166.
[872] UNCTAD Expropriation Report, page 96. RL-0070.
[873] Memorial on the Merits, Part IV, Section XI.
[874] Memorial on the Merits, the contents of section IV.H of the present Counter-Memorial are deemed to have been incorporated by reference herein.

highlight that the Kingdom of Spain had already adopted other measures for other sectors of production and of society, which is why the argument that these disputed measures are disproportionate or unreasonable with respect to the intended aim cannot be accepted.

1256. Finally, the measures were adopted in accordance with due process. The Claimant has not called this fact into question, but has merely limited itself to making snide and opinionated criticisms[875].

1257. In conclusion, the measures adopted by Spain are non-discriminatory regulatory adaptations that were approved in good faith, with the aim of protecting the public interest, in a manner that was proportional to the aim sought and in accordance with due process. Therefore, the measures cannot be considered to be expropriatory.

(4) The measures adopted by Spain do not constitute an indirect expropriation according to the substantial deprivation test used by Arbitral Tribunals in relation to international law on investor protection.

1258. In the event that the Tribunal were to understand that said regulatory adaptations are covered by the standard for the protection of investors against expropriation, as stipulated in article 13 of the ECT, in this section we will demonstrate that, under no circumstances, do these measures have expropriatory effects.

1259. The Claimants base their claim on the protection that article 13 of the ECT provides investors against measures having effect equivalent to expropriation, which they refer to as "indirect expropriation"[876].

1260. The ECT does not contain a definition of the term expropriation that provides a clear understanding of the meaning of "*measures having effect equivalent"* to an expropriation. Therefore, in order to determine what is understood by the term indirect expropriation and, consequently, what measures the State can consider to fall within such category, one must refer to the test used in the case law of arbitral tribunals, particularly under the ECT. As discussed below, the Claimants made a biased and interested reference to the afore-mentioned jurisprudence given that it was clearly prejudicial to their position.

1261. International jurisprudence in the field of investment arbitration under the ECT has stated that in order for Article 13 (1) to consider that a measure taken by a State equates to an expropriation, it must necessarily prevent the investor from continuing to trade on his or her investment, or from continuing to make use thereof, or it must limit whatsoever right of ownership thereof.

1262. In fact, the Claimants state that:

> *"arbitration tribunals have concluded that it is acceptable to affirm the existence of an indirect expropriation when the ability of the investor to peacefully manage his or her property has been affected by any of the following circumstances:*

[875] For example purposes, see paragraph 591 of the Memorial on the Merits in which it intentionally qualifies the amendments associated with parliamentary procedure as amendments to the Act, in order to create the sensation that there were more legislative changes.
[876] Memorial on the Merits, paragraph 737 to 760.

(i) the investor retains control of his or her investment; (ii) he or she carries out their daily operations; (iii) their agents and employees have been detained by the State; (iv) the State supervises the work of the agents and employees of the investor; (v) the State has apprehended the yields from sales above and beyond the payment of taxes; (vi) the State interferes in the management or in the activities of the administrators or shareholders; (vii) the State prevents the distribution of dividends to the partners or shareholders; (viii) the State interferes with the appointment of directors or administrators; (ix) the State has taken a certain action to taken away from the investor his or her full ownership and control of the investment"[877].

1263. Actually, none of these requirements concur, nor have any of them been accredited in this arbitration. On the contrary, as the Claimants themselves acknowledge: "*there is no discussing on the fact that the Claimants have not lost the final, direct or indirect ownership of the shares in the Parque Eólico La Carracha, S.L. and in the Parque Eólico Plana de Jarreta, S.L., the Companies in the Project that own the La Carracha and the Plana de Jarreta (Wind Farms). Furthermore, the Claimants acknowledged herein that they currently retain ownership of the aforementioned shares*[878]".

(4.1) Substantial deprivation

1264. In effect, in *ELECTRABEL S.A. vs. the Republic of Hungary*, cited by the Claimants[879], the Tribunal determined that the measures taken by Hungary, even though they implied an economic impact on the profit of Electrabel, given that they did not prevent it from continuing to work with the plant, nor from operating in the electricity market in Hungary, could not be considered as measures tantamount to an expropriation, under Article 13 ECT. The Tribunal specifically determined the following:

"As regards indirect expropriation, the Tribunal considers that the wording of Article 13(1) ECT requires Electrabel to establish that [...] its investment lost all significant economic value with the PPA's early termination. […]

In short, the Tribunal considers that the accumulated mass of international legal materials, comprising both arbitral decisions and doctrinal writings, describe for both direct and indirect expropriation, consistently albeit in different terms, the requirement under international law for the investor to establish the substantial, radical, severe, devastating or fundamental deprivation of its rights or the virtual annihilation, effective neutralization or factual destruction of its investment, its value or enjoyment. […]. Conversely, arbitral tribunals have rejected claims for expropriation under international law where the investor has failed to meet this test for "substantial" deprivation,[...]

the Tribunal also interprets the terms of Article 13(1) ECT as requiring Electrabel to meet the test for substantial deprivation both for direct expropriation and

[877] Memorial on the Merits, paragraph 723.
[878] Memorial on the Merits, paragraph 731.
[879] Memorial on the Merits, paragraph 1135.

indirect expropriation having the equivalent effect to direct expropriation or nationalization.." [880] *(Emphasis added)*

1265. Also in the context of a dispute that originated in the midst of the ECT, once again cited by the Claimants[881], in *Nykomb Synergetics Technology Holding AB vs. the Republic of Latvia*[882], the Tribunal decided that although the measures taken by Lithuania (sic) did reduce the rate the Claimant was to receive, as they did not imply any interference in the rights of the shareholders or in the control or management of the company, they could not be considered to be tantamount to an expropriation.

1266. What is more, in response to the international jurisprudence, which has ruled in other treaties concerning the reciprocal protection of investments, many courts have rejected the existence of an indirect expropriation, whenever investors have maintained control over the entire investment (even in those cases in which the investor has been deprived of specific rights or benefits deriving from the investment), as occurs in this case.

1267. In *CMS vs. Argentina*, the State of Argentina, in the context of its financial and economic crisis, decided to unilaterally suspend the scheme used to adjust tariffs in the gas transport sector. CMS argued that Argentina's suspension of the scheme used to adjust tariffs constituted an indirect expropriation of its investment in the gas sector. However, the Tribunal determined that the measures taken by the Government of Argentina could not be regarded as tantamount to an expropriation, because they did not involve a substantial deprivation of the investment. In particular, the Tribunal noted that:

"262. […] […] What is essential, therefore, is to establish whether the enjoyment of the property has been restricted (…). The Government of Argentina has argued convincingly that the aspects that should be taken into account in order to establish the existence of substantial deprivation, as was established in this case, are not found in this dispute. Indeed, the Respondent has explained that the investor exercises the control of the investment; the Government does not manage the daily operations of the company; and the investor has the full ownership and control of the investment."[883] *(footnotes omitted) (emphasis added).*

1268. The Tribuanl in the case *Pope and Talbot vs. Canada* (an award to which the Claimants refer[884] without proving that the assumptions of that case concur in their case), rejected the idea that the Canadian export control regime constituted an expropriation, considering that, even when the interference of the State had led to a reduction in the benefits of the investment, the fact was that the investor was still exporting substantial quantities and was receiving sufficient profit from said sales. It laid down that:

[880] *Electrabel S.A. vs. the Republic of Hungary*, ICSID Case No. ARB/07/19, Decision on Jurisdiction, Applicable Law and Liability, of 30 November 2012 ("Electrabel"), paragraph 6.53-6.62, 6.63. RL-0002.
[881] Memorial on the Merits, paragraph 737.
[882] Nykomb Synergetics Technology Holding AB vs. the Republic of Latvia, award of 16 December 2003, paragraph 4.3.1. CL-0051.
[883] *CMS Gas Transmission Company vs. the Republic of Argentina* (ICSID No. ARBI/01/8, award of 12 May 2005 ("CMS"), paragraph 262-264. CL-0106.
[884] Memorial on the Merits, paragraph 740.

> *"While it may be uncertain whether a specific interference in the activities of the business can constitute an expropriation or not, the test consists in seeing whether that interference is so sufficiently restrictive as to conclude that the owner's property has been confiscated. Therefore, the Harvard Draft defines - the standard that requires an interference that "would imply that the owner might not be able to use, enjoy or dispose of property". The Restatement, dealing with the question as to whether the regulation can be considered expropriation, talks about "an action that is confiscatory or prevents in an unreasonable manner, interferes, or unduly delays the effective enjoyment of a property to a foreigner". In fact, in the hearing, the Adviser to the Investor correctly pointed out that under International Law, the expropriation requires a "substantial deprivation." The Export Control Regime has not restricted the Investment in this way."*[885] (footnotes omitted) (own translation) (emphasis added).

1269. Similarly, in *Feldman vs. Mexico*[886], the Claimants claimed that the measures taken by Mexico, as they deprived them of certain tax deductions, were measures tantamount to an expropriation. The Tribunal found that there was no such expropriation, because although the measures affected the profits from the activity, they did not deprive the Claimants of the control of their investment nor did they prevent them from continuing with their professional activity.

1270. For its part, in *Sempra vs. Argentina*, the Tribunal stated that in order to determine whether a measure is tantamount to an expropriation, something more than "adverse effects" is required, so that the measure can only be considered as tantamount to an expropriation if it implies that the investor no longer holds control of the investment or that the value of the investment has been completely eliminated:

> *"285. [...] More than adverse effects are needed to decide that this is an indirect expropriation. It would be necessary for the investor no longer to have control of the operation of his or her company, or for the value of the enterprise to have been virtually destroyed. But this is not the case in this dispute."*[887]

1271. In *AES vs. Hungary*, the Tribunal determined that since AES retained control of the company and continued to receive profit from its investment, the measures taken by Hungary could not be considered as measures tantamount to expropriation:

> *"14.3.1 It is clear that many of the actions or measures taken by the State may affect the investments, and the modification of an act or regulation is probably the most common of these actions or measures. However, an act of a State that has a negative effect on an investment may not be automatically considered to be an expropriation. In order for there to be an expropriation, it is necessary that the investor be deprived completely or significantly of the property or the effective control of his or her investment: or that their investment lose all or a significant part of its value (...).*

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[885] Pope and Talbot, Inc vs. Government of Canada, UNCITRAL/NAFTA, Interim Award of 26 June 2000, paragraph 102. CL-0053.

[886] Marvin Roy Feldman Karpa vs. Mexico, ICSID Case No. ARB(AF)/99/1), Award of 16 December 2002, paragraph 152-153. RL-0073.

[887] *Sempra Energy International vs. the Republic of Argentina*, ICSID Case No. ARB/02/16, Award of 28 September 2007 paragraph 285. RL-0074.

> *14.3.3 Furthermore, the Claimants continued to receive substantial income from their investment during 2006 and 2007, which proves that the value of their investment has not been radically diminished and that they were not deprived of all or a significant part of the value of their investment."*[888] (free translation) (emphasis added).

1272. In short, the "substantial deprivation" test requires that there must be a loss of control of the investment or an elimination of its economic value; the fact that the investment may have suffered adverse effects is not sufficient.

1273. Yet again, the Claimants' analysis is incomplete and confusing in this regard since, on the one hand, they claim that the hypothetically expropriated "asset" is their right to receive future yields from the farms and their ability to manage them and, on the other hand, they state that they have been deprived of their holdings (the real purpose of their investment). In other words, they change their investment depending on whether they analyse the "expropriable object" or the existence of "substantial deprivation". An obvious contradiction that demonstrates the unsustainability of the claim for compensation based on a hypothetical expropriation.

1274. However, we will accredit, for the sake of argument, that not even when the Claimants' theory is accepted is there "substantial deprivation". If they contend that the "expropriable asset" is their right to receive future profits and to manage the Plants, they should have analysed the effect of the substantial hardship from the point of view of the impact that the regulations have had on the profitability of the Plants.

1275. Thus, the Claimants have not proved that with the subsidies received so far they have not covered their investment costs, the operating costs and obtained reasonable profitability. Nor have they even proved that the Plants have received profitability of less than 7.398%. Furthermore, they have not proved that they are not in a position to compete in the market and that the pool price does not cover their operating costs. On the contrary, it is confirmed that the Plants continued to be in operation, receiving reasonable profitability and under the control and management of their owners at the time of adoption of the measures under dispute.

1276. On the contrary, if we understand that the "asset" affected by the expropriation is: (i) the financial value of their shares in the wind farms and (ii) the ability to manage and administer them, nor have they suffered any "substantial deprivation" at all.

1277. Regarding the supposed financial impact on the wind farms, it is worthy of note that the Claimants base the "substantial deprivation" on the witness statement from Mr Schulz, which states that operational cash flow after the financing fell from 9.5 million euros to 3.5 million euros per year.

1278. This comparison omits the fundamental issue that the cash flow for a specific year cannot be compared to the financial profits of a project. Therefore, the unit of measurement used to assess the deprivation, for the purposes of expropriation, is not representative.

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[888] *AES Summit Generation Ltd. and AES-Tisza Erömü Kft vs. Hungary*, ICSID Case No. ARB/07/22; Award of 23 September 2010; paragraph 14.3.1 - 14.3.4. RL-0039.

1279. However, even assuming that this unit of measurement is valid, for the sake of argument, we have to remember that (i) these 9.5 million euros net per annum had been obtained since 2003 in the form of subsidies, (ii) these subsidies allowed the plants to recover the investment costs and obtain profitability of more than 7.398%, (iii) the plants had reached their "level playing field", since without receiving any subsidy, in other words, only obtaining revenues from the sale of energy at pool price, they were able to cover their operating costs and receive around 3.5 million euros in net operating cash flow, (iv) the plants continued to enjoy priority of despatch and access to sell all the energy produced.

1280. In this respect, as stated in the Econ One Research report of 15 June:

> *"51. We note that KPMG does not present any economic analysis that would support the statements of Claimants and their witnesses. To the contrary, KPMG's own projections show that the Projects are currently projected to generate substantial positive cash flows from their operations, even under its Prevailing Scenario (that is, with the Measures in place) in which they are not expected to receive any financial incentives above market prices.*
>
> *52. Mr. Schultz acknowledges that the Projects are currently generating an operating profit. He states "the expected net operating cash flow is now going to be in the range of 3.5 million euros."*
>
> *53. According to KPMG's own projections with the Measures in place, the Projects will continue to generate operating profits. KPMG projects operating profits (before depreciation) of about € 4 million per year, a figure that is projected to increase to about € 7 million over time (…). This represents a margin of about 50%.*
>
> *54. Furthermore, the cash flows projected by KPMG in its Prevailing Scenario, together with all of its assumptions, mean that the Enterprise Value of the Projects as of December 31, 2015 was about € 59 million. Given that the debt of the Projects as of that date was about € 29 million, this means that the Equity Value of the Projects, according to KPMG's own calculations and assumptions, is about € 30 million, 74% of which belongs to Claimants. As we explain below, we disagree with some of the assumptions used by KPMG. But the values resulting from KPMG's calculations and assumptions are sufficient to prove that Claimants' assertion that the Projects have been rendered worthless by the Measures is simply incorrect"*[889]*. (footnotes omitted).*

1281. Furthermore, the Claimants argue that they have suffered substantial deprivation , based on their statement that:

> *"i. Since 2011, the Project Companies have not been able to allocate dividends;*
>
> *ii. The Project Companies have stopped paying interest and capital on the shareholders' subordinated loans; and*

[889] Econ One Research Report of 15 June 2016, paragraphs 51-54.

iii. Since 2014, the Project Companies have not complied with the debt service coverage ratios required under the loan agreements[890] *".*

1282. However, regardless of what is added later, the conclusion resulting from the witness statement of Mr Schulz is immediate: if the plants have 3.5 million of annual operating cash flow after the financing, but even so they cannot meet the cover ratios, they are not paying the interest and capital on subordinated loans to shareholders, nor are they able to allocate dividends, the reason for the economic and financial situation of the plants lies in their financial structure and not in the measures under dispute.

1283. In other words, their economic and financial situation is the result of a free business decision by the Claimants since, as has been stated throughout this document, the reasonable profitability guaranteed by the Kingdom of Spain has always been based on projects funded 100% with own funds, with each facility assuming the risks for the chosen financing option.

1284. Regarding the powers of administration and management of their investment, the Claimants once again show confusion between their real investment and the wind farms. Indeed, the Claimants repeatedly invoke the loss of the power of administration and management, not of their investment (shares), but of the wind farms[891].

1285. In this respect, the Claimants state[892] that they no longer enjoy the peaceful management of their investment, due to the fact that they have been obliged to refinance their loans. However, these functions clearly correspond to the management and administration of an entity. Obviously, the Claimants are confusing "*substantial deprivation*" of these faculties with the fact that they supposedly have to managed the wind farms instead of merely receiving excess remuneration charged to subsidies.

1286. In addition, it is worth highlighting that, in line with what has previously been stated, that "need to refinance" their bank debts does not arise from the measures under dispute but from a misguided decision to refinance their debt in 2006. Indeed, as stated in the Econ One Research Inc. report of 15 June[893]:

"As we explain in this section, the current difficulties in servicing the Projects' debt are the direct consequence of refinancing decisions made in 2006. Had those refinancing decisions not been made, the Projects (which, as we saw earlier, are generating significant operating cash flows) would not be having any problems servicing their debt according to the original schedule. Thus, it is would be incorrect to blame the Measures for any difficulties servicing debt that the Projects may be experiencing currently (…).

The initial financing for the Projects followed a similar structure with a high percentage of loans relative to equity shares at the outset, with € 77.7 million in

[890] CWS-ES, paragraph 35.
[891] Memorial on the Merits, paragraphs 715, 716, 721, 726, 731, 745, 748, 759, 773 and 775.
[892] Memorial on the Merits, paragraph 774.
[893] Econ One Research Report of 15 June 2016, paragraphs 57 to 77.

debt,[894] *and the remainder of the upfront costs funded through € 26.6 million in shareholder contributions (…).*[895]

The original debt of the Projects consisted of three tranches of bank loans, referred to as the syndicated loans, while the shareholder contributions include both equity holdings and shareholder subordinated loans.[896] *As a condition of the syndicated loan agreements, a ratio of approximately 25% equity to total capital was required.*[897] *Due to this highly leveraged structure, the 2001 prospectus for the Projects projected that the Projects would not pay corporate tax until 2012.*[898]

In 2006, the Projects' owners chose to refinance its debt.[899] *The Project used this inflow of funds to distribute € 17.3 million to shareholders.*[900] *Thus, by the end of 2006, and including prior distributions, the Projects had distributed at least € 22.6 million to its shareholders, greater than their initial equity contribution.*[901] *Without the refinancing, that cumulative distribution to shareholders would not have been achieved until several years later.*

The large distribution to shareholders after refinancing means that, despite several years of debt repayment, at the end of 2006 the Projects owed € 75.4 million in bank loans, nearly as much as had been originally borrowed to build the Projects.[902] *Mr. Schulz in his witness testimony states that when the refinancing took place in 2006, "an agreement was reached with the syndicate of banks, which maintained a similar*

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[894] **¡Error! No se encuentra el origen de la referencia.**, Financial Structure of the Projects, Table 1.

[895] As shown in the table, the companies that owned the majority of the Projects when they were built sold their shares shortly after the Projects were commissioned. Falck Renewables acquired its share from Blue Energy A.G. in June 2003, Shell from TXU Energy in July 2003, and BVT merged with other entities to form Renerco in July 2003. **C−0071**, Deed of SPA between Blue Energy AG and Falck Renewables Limited on the shareholding interests in the SPVs, July 21, 2003, p. 26 of PDF; **C−0073**, "*Shell acquires 40% of La Muel*a Wind Farm", El Periódico de Aragón, 24 July 2003; **CWS−MT**, Witness Statement of Mr Matthias Taft, February 24, 2016, ¶ 44.

[896] **C−0228**, Deed of the Modifying Novation of the Credit Agreement entered into with Parque Eólico [Plana de Jarreta], dated 30 June 2006, pp. 12-13 of PDF.

[897] **CER−0002**, **Exhibit 2**, Audited Annual Accounts of Parque Eólico La Carracha S.L. and Parque Eólico Plana de Jarreta S.L. (2003 to 2014), pp. 19-22, 810-814 of PDF.

[898] **C−0022**, Windparks La Muela, Zaragoza (Aragón), Project Information Brochure dated January 2001, p. 23 of PDF.

[899] **CWS−MT**, Witness Statement of Mr. Matthias Taft, February 24, 2016, ¶¶ 55-56.

[900] The funds were distributed in the form of dividends, reduction in share capital, and principal payments on shareholder loans. **¡Error! No se encuentra el origen de la referencia.**, Financial Structure of the Projects, Table 2.

[901] Error! Reference source not found., Financial Structure of the Projects, Table 2. This figure understates the amount of funds that shareholders received. As noted in Error! Reference source not found. below, we have been unable to calculate precise figures for the amount of interest paid on shareholder loans through 2006.

[902] **CER−0002**, **Exhibit 2**, Audited Annual Accounts of Parque Eólico La Carracha S.L. and Parque Eólico Plana de Jarreta S.L. (2003 to 2014), pp. 76, 897 of PDF; **CWS−ES**, Witness Statement of Mr. Errol Schulz, February 1, 2016, ¶ 25.

level of project leverage."[903] *However, after the refinancing, the debt represented 91% of the total capital as opposed to 74% initially.*

As of the time of the regulatory changes in December 2012, the Projects were highly leveraged, with debt accounting for 91% of the total capital structure. As we explain in more detail below, high leverage tends to increase the risks of a project, since it is more difficult to cope with unexpected business downturns when the project has high debt servicing commitments that, unlike a dividend distribution, cannot be simply reduced or postponed (…).

The decision to refinance and distribute the funds to shareholders in 2006 represents a turning point in the financial health of and risk to the Projects. As noted above, the Projects were self-contained nonrecourse entities.[904] *That means that they must rely on internal cash flows to pay back debt.*

Under the original financing terms, the bank debt would have been fully paid off by 2018, which was the original accounting estimate of the end of the useful life of the Projects, 17 years from commissioning (…).

Thus, the current difficulties in servicing the Projects' debt are a direct consequence of the refinancing decision. In 2006, the Projects' shareholders used the Projects as a piggy bank, causing the Projects to incur additional debt so that they could obtain a very sizable distribution that had not been contemplated originally. As stated at the beginning of this section, had that refinancing decision not been made, the Projects (which, as we saw earlier, are generating significant operating cash flows) would not be having any problems servicing their debt according to the original schedule. Thus, it would be incorrect to blame the Measures for the any difficulties servicing debt that the Projects may be experiencing currently" (footnotes partially omitted) (emphasis added).

1287. Therefore, having accredited that the measures adopted do not involve "substantial deprivation" for the Plants, which are the recipients of them, and that the Claimants do not have any "expropriable asset or right", under the terms of ECT Article 13(3) in relation to Article 1(6), the existence of an expropriation can only be denied.

(4.2) Permanent nature of the expropriation

1288. Meanwhile, international case law requires that the measures in question, in order to be considered equivalent to an expropriation, are likely to be permanent[905].

[903] CWS−ES, Witness Statement of Mr. Errol Schulz, February 1, 2016, ¶ 26. Given that the share of debt increased to 95% in 2006, this statement appears to be incorrect

[904] **CWS−MT**, Witness Statement of Mr. Matthias Taft, February 24, 2016, ¶ 56, referring to C−0228, Deed of the Modifying Novation of the Credit Agreement entered into with Parque Eólico [Plana de Jarreta], dated June 30, 2006

[905] UNCTAD Series on Issues in International Investment Agreements, Expropriation, United Nations Series, New York and Geneva, 2012, page 22, ("UNCTAD Expropriation Report"), page 69. RL-0070. *Principles of International Investment Law* Rudolph Dolzer and Christoph Schreuer, Oxford University Press, 2012, page 124. RL-0075.

1289. Thus, in *Suez v. Republic of Argentina*, the Tribunal rejected the statement from the Claimants that the measures adopted by Argentina constituted measures equivalent to an expropriation, since the requirements of substantial and permanent deprivation regarding the claimants' investment did not apply:

> *"140. Analysing the measures taken by Argentina to address the crisis, the Tribunal considers that, in view of the major crisis with which the country is faced, these general measures are within the powers of the State and they do not constitute substantial or permanent deprivation concerning the Claimants' investment. Although they may have had a negative effect on the profitability of the AASA concession, they did not lessen or reduce the rights of the AASA or its investors and they did not affect the ability of the AASA to maintain the Concession and run its own operations and activities."*[906] *(Own translation) (Emphasis added).*

1290. Furthermore, in *BG Group Plc. v. Republic of Argentina*, after recognising that a State can impose regulatory measures that affect private property in the public interest, it was determined that the measures adopted by Argentina, despite being harsh and affecting the claimants' investments, were not permanent. Therefore, it was considered that they could not be considered to be equivalent to an expropriation because the claimants' investment still existed and they had not lost its management and operation:

> *"268. The tribunal contends that the State may exercise its sovereignty in order to issue regulatory measures that affect private property in order to benefit the public welfare. Compensation for expropriation is required if the measure adopted by the State is "irreversible and permanent and the assets or rights subject to these measures have been affected in such a way that "..." there is no way of operating them". As a result, a measure cannot be compared to being equivalent to an expropriation if "the investment remains operational, even if the profits are reduced (...).*
>
> *270. Specifically, the impact of the measures in Argentina on the value of the BG stake in MetroGAS was not permanent. It may be that the measures adopted by Argentina were causing major fluctuations in BG's investment during the crisis. However, the business of MetroGAS was not interrupted, it continues to operate and it has an asset base that is recovering..."*[907] *(free translation).*

1291. The Tribunal in *Ulysseas, Inc. v. Ecuador* also determined that the evolutive nature of the changes to the electricity sector prevent the measure that affected Ulysseas from being characterised as equivalent to expropriation, since they were not of a sufficiently permanent nature:

> *"189. The evolutive nature of the changes to the order of priority due to the need to guarantee improved stability in the conditions of the electricity market deprives the supposed substantial deprivation of the value necessary for the Claimant of the necessary permanent nature"*[908] *(emphasis added).*

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[906] Suez, Sociedad General de Aguas de Barcelona S.A., and InterAguas Servicios Integrales del Agua S.A v. Republic of Argentina, ICSID Case No. ARB/03/17, Decision on Liability, 30 July 2010, paragraphs 134 and 140. CL-0068.

[907] *BG Group Plc. c. la República de Argentina*, CNUDMI, Final Awrad of 24 december 2007, par. 268-272. RL-0061.

[908] *Ulysseas Inc. v. Ecuador*, UNCITRAL, Award of 12 June 2012, paragraph 189. RL-0076.

1292. In similar terms to those included in the aforementioned awards, the disputed measures have been adopted by the Kingdom of Spain in the exercise of its regulatory powers. The adoption of these measures is a response to the need to guarantee the sustainability of the Spanish Electricity System by reducing the deficit and adapting the reasonable return to the capitals market. The freezing of the Spanish electricity system which, due to its inherent nature, must be dynamic in order to adapt to the macroeconomic conditions in each circumstance, whilst always limited to guaranteeing reasonable returns, is unwarranted. That dynamism has not prevented the Claimants from maintaining the control and economic value of their investment, on the contrary, it constitutes a guarantee for the stability of the investment's value, in line with the capitals market.

(4.3) Transfer of assets.

1293. Finally, international case law has also understood that when measures adopted by a State involves a benefit for the society as a whole, and there is no economic benefit or clear transfer of assets to a private entity, no expropriation exists[909].

1294. Thus, in *SD Myers v. Canada*, the Tribunal determined that since the measures adopted by Canada did not represent a benefit for Canada or a transfer of benefit or property to others, they could not constitute measures equivalent to an expropriation[910].

1295. In *Olguín v. Paraguay*, the Tribunal determined that for a measure to be considered equivalent to an expropriation, the subject performing the allegedly expropriatory acts must acquire control or the fruits of the expropriated assets:

> *"84. For an expropriation to occur, there must be actions that can be considered reasonably appropriate for producing the effect of depriving the affected party of the property it owns, in such a way that whoever performs those actions will acquire, directly or indirectly, control or at least the fruits of the expropriated property. Expropriation therefore requires a teleologically driven action for it to occur; omissions, however egregious they may be, are not sufficient for it to take place*[911]" (Emphasis added).

1296. In summary, international case law is consistent in sustaining that the test to be applied for cases of indirect expropriation is that of the *substantial deprivation* of the investment. In this sense, in order to consider whether said substantial deprivation exists, the tribunals have determined that state measures must prevent the operation from continuing, involve the taking of control of the actions or the management of the investment, or permanently annihilate the value of the investment. Furthermore, if the measures adopted by the State involve a benefit for the society as a whole, and there is no economic benefit or clear transfer of assets to a private entity, no expropriation exists.

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[909] UNCTAD Series on Issues in International Investment Agreements, Expropriation, United Nations Series, New York and Geneva, 2012, page 22, ("UNCTAD Expropriation Report"), page 104. RL-0070.
[910] S*.D. Myers, Inc v. Canadá*, UNCITRAL, Partial Award of 13 November 2000, paragraph 287. CL-0131.
[911] *Eudoro Armando Olguín v. Paraguay*, ICSID Case No. ARB/98/5, Award of 26 July 2001, paragraph 84. RL-0077.

1297. The measures adopted by Spain cannot be considered as falling within the aforementioned expropriatory parameters.

1298. Firstly, the disputed measures in no way imply that Spain has taken control of the actions or the management of the Claimant's investment in the wind farms or that it has annihilated the value of the investment. It is obvious in this case that: (i) the Claimants continue to have full, day to day control of their shares in both companies; (ii) the wind farms continue to operate, producing and selling energy on the renewable energies market, and of course; (iii) all the companies continue to receive a reasonable return.

1299. Secondly, the measures have at no point resulted in any saving whatsoever for Spain, and neither have they involved a "transfer of wealth" or benefit of any kind for Spain or third parties.

1300. Thirdly, the measures do not affect the Claimants investments permanently. In this sense, the regulatory standards promoted by any State - such as Royal Decrees and Royal Decree-Laws in Spain- are not, by nature, either permanent or irreversible. Furthermore, as stipulated in section IV. G (1.7), the current remuneration model includes periodic reviews to be conducted every 3 and 6 years, therefore, although the regime is unquestionably stable, it is neither unchangeable nor permanent.

1301. Ultimately, applying the parameters established by the arbitral case law on the matter, one must conclude that the measures adopted by Spain (i) did not deprive the investor of its investment; and (ii) are measures that represent a benefit for society in general, with no economic benefit or transfer whatsoever of assets to the Government of Spain or to a private entity.

(5) The measures adopted by Spain do not constitute an indirect expropriation, even under the standard set out by the Claimants.

1302. Here follows an analysis of the doctrinal and arbitral references invoked by the Claimants, demonstrating that, not even under said standard, does the alleged expropriation exist.

(5.1) Awards invoked with respect to the concept of "indirect expropriation".

1303. Firstly, the Claimants mention the Award in the case of *Mamidoil v. Albania*[912] in order to demonstrate that the indirect expropriation applies.

1304. However, the Claimants fail to mention that the award does not stop at acknowledging the possibility of an indirect expropriation, but goes beyond outlining the concept, establishing the evident difference between mere damages and an expropriation. Thus the award in question states:

> *"566. The Tribunal holds that the decisive criterion for most tribunals that find expropriation is not the fact of having incurred a damage and/or the loss of value as such, but the finding – as stated in Santa Elena v. Costa Rica – "that the owner has truly lost all the attributes of ownership". As the tribunal in El Paso v.*

[912] Memorial on the Merits, paragraph 722.

> *Argentina expressed in its award, which has been upheld in annulment proceedings, "at least one of the essential components of the property rights must have disappeared for an expropriation to have occurred".*
>
> *(...) In its literal translation, expropriation describes a specific effect on property itself and not a damage inflicted to property. The effect can be a direct taking as it can be an indirect deprivation of one or several of its essential characteristics. These are traditionally defined by its use and enjoyment, control and possession, and disposal and alienation. If one of these attributes is affected, the resulting loss of value and/or benefit may lead to a claim for expropriation.*
>
> *570. (...) Thus, a mere loss of value or a loss of benefits that is connected to and caused by the dissolution of at least one attribute of property, does not constitute indirect expropriation".*[913]

1305. Secondly, the Claimants cite the case of *Metalclad v. México* to illustrate that an indirect expropriation can be produced by regulatory measures[914] and that said expropriation can be identified with the substantial deprivation of the attributes of rights of ownership[915].

1306. Before entering into an analysis the extension of the criteria of this award to the present case, it is important to note that in the Metalclad case the dispute centred around the permit granted to Metalclad, which allowed it to conduct hazardous waste storage activities, resulting in Metalclad commencing the construction of a storage plant. Once Metalclad had completed a substantial part of the work on the construction of the plant, Mexico passed a decree for the closure of the plant, withdrawing permission for the construction of the plant from Metalclad. The Tribunal ruled that the measures adopted by Mexico where equivalent to expropriatory measures because:

> *"[This] decree had the effect of barring forever the operation of the landfill"*[916] *and "effectively and unlawfully prevented the Claimant's operation of the landfill."*[917] (Emphasis added).

1307. It is plain and evident that the measures adopted by Spain are not even comparable with the measures adopted by Mexico in the Metalclad case. The measures of Spain have not forever barred the companies in which the Claimants hold a stake from conducting their economic activities, which consist of the production of electricity through wind farms. In fact, the Claimants acknowledge that they continue to operate on the market. Furthermore, the measures have not meant that the plants have had to close or cease operation. In fact, both wind farms continue to operate, producing electricity and having the privilege of being the first to sell their energy.

1308. Moreover, the Claimants invoke the award in the case of *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakistan*[918]. This Award in particular contains an

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[913] *Mamidoil Jetoil Greek Petroleum Products Societe Anonyme S.A. v. Albania* (ICSID, Case No. ARB/11/24), Award, 30 March 2015, pages 105 to 107. RL-0046.
[914] Memorial on the Merits, paragraph 738.
[915] Memorial on the Merits, paragraph 754.
[916] *Metalclad Corporation v. Mexico*, ICSID Case No. ARB (AF)/97/1, Award of 30 August 2000, paragraph 109. CL-0052.
[917] *Metalclad Corporation v. Mexico*, ICSID Case No. ARB(AF)/97/1, par. 106. CL-0065.

exhaustive description of the steps for assessing the existence of an unlawful expropriation, stating that:

> *"The first step in assessing the existence of an expropriation is to identify the assets allegedly expropriated (...).*
>
> *Having identified the assets, the next step is to identify the allegedly expropriatory conduct. As stated in the Decision on Jurisdiction, expropriation may arise out of a simple interference by the host State in the investor's rights with the effect of depriving the investor of its investment. A critical issue in this regard concerns the intensity or the effect of such conduct with respect to the investor's property (...).*
>
> *The third step in this inquiry consists in examining whether the alleged interference with the property or the rights of the investor has been made in the State's exercise of its sovereign powers (...).*
>
> *The fourth step in assessing the existence of an expropriation in breach of the Treaty is the analysis of the conditions specified in Article III(1), namely (i) the lack of a public purpose, (ii) discrimination, (iii) the absence of payment of prompt, adequate and effective compensation, and (iv) a breach of "due process of law and the general principles of treatment provided for in Article II of this Agreement.*[919]*"*

1309. In the present case, the Claimants have not demonstrated the existence of any of these steps. In fact, (i) they have failed to identify any expropriable asset, (ii) they have not demonstrated the intensity of the "expropriatory conduct", that is, the existence of a substantial deprivation, (iii) they have failed to demonstrate that said deprivation is the result of the State's exercise of its sovereign powers, (iv) that the disputed measures are discriminatory, and (v) that due process was not followed during the approval of the measures.

(5.2) Awards regarding expropriation not necessarily having to involve a deprivation of the possession of the expropriated asset.

1310. The Claimants state that expropriation does not necessarily have to mean the dispossession of the expropriated asset, and that mere interference with rights of ownership will suffice[920]. This general statement is not disputed by this party. However, the regulatory standards adopted by the Kingdom of Spain in no way involve the taking of control of the actions or the management of the Claimants facilities or the annihilation of the value of the company. This maxim is even confirmed by the awards invoked by the Claimants themselves.

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[918] Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakistan (ICSID case no. ARB/03/29), Award of 27 August 2009. CL-0114.
[919] Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakistan (ICSID case no. ARB/03/29), Award of 27 August 2009, paragraph 442 to 446. CL-0114.
[920] Memorial on the Merits, paragraphs 726 to 731.

1311. Firstly, in the case of *Plama v. Bulgaria*[921], careful reading of the award shows that, in the final instance, the determination of an expropriation in contravention of article 13 of the ECT requires the existence of the following assessed requirements: (i) substantial deprivation and complete elimination or annihilation of rights of enjoyment of the investment, (ii) the irreversibility of the contested measures, and (iii) the extent of the loss of economic value. Thus, the cited award states:

> *"The Arbitral Tribunal considers that the decisive elements in the evaluation of Respondent's conduct in this case are therefore the assessment of (i) substantially complete deprivation of the economic use and enjoyment of the rights to the investment, or of identifiable, distinct parts thereof (i.e., approaching total impairment); (ii) the irreversibility and permanence of the contested measures (i.e., not ephemeral or temporary); and (iii) the extent of the loss of economic value experienced by the investor*[922]*".*

1312. In the same sense, with respect to the cases of *Starret Housing Corporation v. Islamic Republic of Iran and Tippetts et al. v. TAMS-AFF*[923], resolved by the Iran-US Claims Tribunal, although they hold that an expropriation can occur without the need for a material dispossession, they also hold that, in such cases, the deprivation must be substantial and not ephemeral[924], as this party sustains.

1313. Furthermore, the Claimants invoke the award in the case of *Waste Management v. Mexico*[925]. However, the purpose of this award is to assess cases in which the breach of a contract can be considered equivalent to an expropriation and is therefore innocuous for the purposes of the present arbitration.

1314. Finally, reference is made to the Decision on Jurisdiction and Liability of 6 June 2012 in the case of *SAUR International SA v. Republic of Argentina* (ICSID Case No. ARB/04/4). However, the Claimants have maintained silence with respect to the final award, which rejects the claim of indirect expropriation, considering that:

> *"No evidence has been presented to persuade us that Claimants were substantially deprived of their investment by operation of the Emergency Measures. To the contrary, they continued to own and operate EDEMSA and later sold the company, albeit at an unfavorable price"*[926].

1315. As demonstrated in the present arbitration: (i) there has been no substantial deprivation or interference with the Claimant's management and investment powers, (ii) the contested

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[921] *Plama Consortium Limited v. Republic of Bulgaria*, (ICSID Case No. ARB/03/24), Award, August 27, 2008. RL-0034.
[922] *Plama Consortium Limited v. Republic of Bulgaria*, (ICSID Case No. ARB/03/24), Award, August 27, 2008, pág. RL-0034.
[923] *Starrett Housing Corporation v. Islamic Republic of Iran*, Case No. 24, Interlocutory Award No. ITL 32-24-1, 19 December 1983, paragraph 154 (CL-0041) and *Tippetts, Abbett, McCarthy, Stratton v. TAMS-AFF*A, Award No. 141-7-2, 22 June 1984. CL-0043.
[924] *Tippetts, Abbett, McCarthy, Stratton v. TAMS-AFF*A, Award No. 141-7-2, 22 June 1984, page 5/7. CL-0043.
[925] *Waste Management, Inc. v. United Mexican States* (ICSID, Case No. ARB(AF)/00/3), Award of 30 April 2004, paragraph 171. CL-0044.
[926] *EDF International S.A., SAUR international S.A. and Leon Participaciones Argentinas S.A. v. Republic of Argentina* (ICSID Case No. ARB/03/23). RL-0078.

measures are not unchangeable as they form part of a dynamic regulatory system, and (iii) the extent of the loss suffered has not been proven, as we will demonstrate in section V. Therefore, these awards do not serve to uphold the position of the Claimants.

(5.3) Awards invoked with respect to the concept of gradual expropriation.

1316. Once again, the Claimants invoke a series of awards that accept the concept of "gradual expropriation". However, there is no justification whatsoever for applying said concept to the present arbitration.

1317. Indeed, the award handed down in the case of *Philips Petroleum v. Iran*[927], considers the possibility of a gradual expropriation. However, the Claimants once again fail to mention that this award also requires the demonstration of the substantial deprivation of the expropriation with respect to the proportionality of the measure[928].

1318. Likewise, in the case of *TecMed v. Mexico*[929], the Claimants continue to insist on the same standards described throughout this section, the existence of which has not been demonstrated by the Claimants. Thus, the award states that:

> *"To establish whether the Resolution is a measure equivalent to an expropriation under the terms of section 5(1) of the Agreement, it must be first determined if the Claimant, due to the resolution, was radically deprived of the economical use and enjoyment of its investments, as if the rights related thereto —such as the income or benefits related to the Landfill or to its exploitation— had ceased to exist. In other words, if due to the actions of the Respondent, the assets involved have lost their value or economic use for their holder and the extent of the loss. This determination is important because it is one of the main elements to distinguish, from the point of view of an international tribunal, between a regulatory measure, which is an ordinary expression of the exercise of the state's police power that entails a decrease in assets or rights, and a de facto expropriation that deprives those assets and rights of any real substance. Upon determining the degree to which the investor is deprived of its goods or rights, whether such deprivation should be compensated and whether it amounts or not to a de facto expropriation is also determined. Thus, the effects of the actions or behavior under analysis are not irrelevant to determine whether the action or behavior is an expropriation*[930]*"*
> (footnotes omitted) (emphasis added).

1319. Ultimately, even if we were to accept that expropriation can take place gradually, in any case, the allegedly expropriatory measures must be proven to be disproportionate and unreasonable with respect to the public interest they seek to protect that gave rise to the same and it must be demonstrated that said measures involve the substantial and permanent deprivation of the Claimant's investment. These premises do not exist and have not been proven in the present arbitration case.

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[927] *Philips Petroleum Co. v. Iran*, Award of 29 June 1989, reprinted in 21, Iran-US Claims Trib. Rep. CL-0047.
[928] *Philips Petroleum Co. v. Iran*, Award of 29 June 1989, reprinted in 21, Iran-US Claims Trib. Rep. Pages 3 and 4. CL-0047.
[929] Técnicas Medioambientales Tecmed, S.A. v. United Mexican States (ICSID, Case No. ARB(AF)/00/2), Award of 29 May 2003. CL-0061.
[930] *Técnicas Medioambientales Tecmed, S.A. v. United Mexican States* (ICSID, Case No. ARB(AF)/00/2), Award of 29 May 2003, paragraph 115. CL-0046.

(5.4) Awards involving a substantial deprivation of the attributes of rights of ownership.

1320. In this final section the Claimants indiscriminately invoke a series of awards, which apply to both the ECT and to bilateral treaties, with the aim of demonstrating that expropriation can be understood not only as a substantial deprivation of the economic value of the investment, but also as that of the essential attributes of rights of ownership.

1321. On one hand, the Claimants cite [931]the award in the case of *Compañía del Desarrollo de Santa Elena, S.A. v. Republic of Costa Rica*[932] of 17 February 2000 in order to sustain that when assessing whether a measure is equivalent to an expropriation, the criterion of the neutralisation of other attributes of ownership rights should be used. This award does not apply to the present case, since its object is limited to: "*This is, at the end of the day, a case of expropriation in which the fundamental issue before the Tribunal is the amount of compensation to be paid by Respondent, Costa Rica, to Claimant, CDSE. While a host of sub-issues were raised by the parties in the context of the written and oral procedures, both parties agree that such matters are relevant only insofar as they tend to affect this central issue*[933]".

1322. On the other hand, the Claimants invoke the award in the case of *CME Czech Republic B.V. v. The Czech Republic*, Partial Award of 13 September 2001, without making the slightest argument with regard to its applicability to the present arbitration case. The cited award indicates the need to distinguish the expropriation from acts of the State in the execution of their laws. Thus, it states:

> *"Of course, deprivation of property and/or rights must be distinguished from ordinary measures of the State and its agencies in proper execution of the law. Regulatory measures are common in all types of legal and economic systems in order to avoid use of private property contrary to the general welfare of the (host) State. The Council's actions and inactions, however, cannot be characterized as normal broadcasting regulator's regulations in compliance with and in execution of the law, in particular the Media Law"*[934].

1323. In the present case, as described in detail in sections IV. E and G, the Kingdom of Spain has limited itself to adopting amendments to the regulatory framework governing the regime for the promotion of renewable energies, with respect to the essential conditions of said regime and with the aim of guaranteeing the sustainability of the Spanish Electricity System and a reasonable return for investors, in accordance with the capital markets.

1324. Finally, the Claimants cite the award in the case of *Les Laboratoires Servier, S.A.S. Biofarma, S.A.S. Arts et Techniques du Progres S.A.S. v. Republic of Poland* of 14 February 2012. Simply reading the portion extracted by the Claimants will suffice to confirm that the

[931] Memorial on the Merits, paragraph 749.
[932] Compañía del Desarrollo de Santa Elena, S.A. v. Republic of Costa Rica (ICSID, Case No. ARB/96/1), Award of 17 February 2000. CL-0054.
[933] Compañía del Desarrollo de Santa Elena, S.A. v. Republic of Costa Rica (ICSID, Case No. ARB/96/1), Award of 17 February 2000, page 188. CL-0054.
[934] Compañía del Desarrollo de Santa Elena, S.A. v. Republic of Costa Rica, Award of 17 February 2000, paragraph 603. CL-0054.

cited award does not apply in this case. In fact, it requires a "*substantial interference*" which involves "*depriving the investor of its ability to benefit from the relevant asset*" and in the present case, the Claimants, (i) continue to own their shares[935], which constitute the true investment in this case, despite the Claimants' attempts to create confusion between the investment and the future earning of the wind farms, and (ii) retain the power to administer, enjoy and dispose of said shares.

1325. It is important to note that the power to administer the wind farms has not been restricted either, given that, as acknowledged by the Claimants and as detailed ut supra, said administration activity currently centres on negotiating loans, due to the erroneous refinancing decision adopted in 2006. Another issue entirely is that the Claimants intended to limit themselves only to receiving an over-remuneration and found it an inconvenience to have to re-negotiate financial contracts in order to save costs.

(5.5) The doctrine invoked by the Claimants does not uphold their theory on expropriation.

1326. Finally, we will demonstrate that the doctrine invoked by the Claimant does not uphold their theory given that, firstly, they present a biased and partial assessment of the same, and, secondly, they fail to prove the existence of the premises required by the cited doctrinal articles for expropriation in the present case.

1327. In fact, the Memorial on the Merits[936] invokes the position of M. Reisman and R. Sloan[937] as set out in "*Indirect Expropriation and its Valuation in the BIT Generation*". More specifically, they refer to a quote in which they sustain that, in order to determine a creeping expropriation, one must consider the joint effect of all acts and omisions contemplated retrospectively. In this case, one can see that, despite said joint effect, the Claimants (i) maintain ownership of their shares, which constitute the true investment, and (ii) retain the power to administer, enjoy and dispose of the same. All of this without prejudice to the fact that the wind farms continue producing energy and selling on the market with access and dispatch priority.

1328. Furthermore, the doctrine of Professors L. Y. Fortier & Mr S. L. Drymer, also does not allow the Claimants to sustain their claim of expropriation. Indeed, it is surprising that the Claimants invoke this doctrinal article in which the authors describe the difficulties of distinguishing between the non-compensable effects of legislation and expropriation, through a study of several awards. It is even more surprising if we note the final conclusion of the authors, who highlight the need to refer to the specific circumstances of the case, concluding that:

> *"So, where does this leave the foreign investor wishing to understand the state of the law with respect to protection from expropriation? How can a foreign investor know whether and which conduct by the host State, affecting an investment, is compensable? Given that the law is, truly, in a state of flux, the best answer to the*

[935] Memorial on the Merits, 731.
[936] Memorial on the Merits, paragraph 732.
[937] M. Reisman & R. Sloane, "*Indirect Expropriation and its Valuation in the BIT Generation*", 74 British Yearbook of International Law 115, 2004, page 123. CL-0056.

> *question "when, how, or at what point does otherwise valid regulation become, in fact and effect, an expropriation?" may be: "I know it when I see it."82 However, even then the answer in many instances will not be crystal clear, as so much depends on the context. The law can provide a basis for answering the question; the circumstances in which the question arises, however, remain critical to the determination. Certain governmental measures, in certain instances, will almost always give rise to a finding of indirect expropriation, and hence to compensation. Others will not. In between lies a "rough and sketchy" area of "large lacunae" in the law.*
>
> *When it comes to understanding precisely when and how State conduct that interferes with an investment will be found to comprise an expropriation, the foreign investor would be wise to heed the credo: "caveat investor."[938]"*

1329. Moreover, the Claimants refer to the doctrine of *Mr Abdala & Mr Spiller*[939], with respect to the possibility of indirect expropriation taking place by means of regulations, unlawful interpretations of contracts, administrative procedures or ordinary decisions. In this same sense, the Claimants cite *Mr Nathanson*[940]. However, the Claimants yet again fail to make the necessary argument or provide evidence to prove that the measures contested in the present arbitration case meet the requirements (disproportional, discriminatory and illegitimate) and produce the essential effects (substantial deprivation or complete elimination) for classification as expropriatory. It is important to remember that, as highlighted by the arbitral doctrine, even that invoked by the Claimants, the distinction between non-compensable regulatory powers and expropriation is not a simple matter and can only be considered after studying the particular circumstance in each case.

1330. Furthermore, reference[941] is made to the article entitled "*Partial Expropriation" by U. Kriebaum*[942], with regard to the consideration that losses, reduced profits, profits substantially lower than expected or the need to close a business may constitute an indication of indirect expropriation. However, as with all indications, these must be accompanied by proof of the other requirements or premises of the expropriation. Proof which, in this case, does not exist.

1331. Finally, the Claimants bring up[943] the article "*The Concept of Expropriation under the ECT and other Investment Protection Treaties*" of *D. C. Schreuer*[944]. In particular, the Claimants emphasise the citation of the author that the essential criterion to assess the substantial deprivation is economic impact. However, the Claimants forget to point out that,

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[938] L. Y. Fortier y S. L. Drymer, "*Indirect Expropriation in the Law of International Investment: I Know It When I Vid It, or Caveat Investor*", ICSID Review – Foreign Investment Law Journal (2004), Vol. 19, Nº 2.CL-0060.

[939] M. A. Abdala & P. T. Spiller, "*Damage Valuation of Indirect Expropriation in International Arbitration Casos*", American Review of International Arbitration, (2003), Vol. 14 Nº 4. CL-0062.

[940] R. A. Nathanson, "The Revocation of Clean-Energy Investment Economic-Support System as Indirect Expropriation Post-Nykomb: A Spanish Caso Analysis", Iowa Law Review, vol. 98:863 (2012). CL-0063.

[941] Memorial on the Merits, paragraph 756.

[942] U. Kriebaum, "Partial Expropriation", The Journal of World Investment & Trade, Vol. 1 Nº 8, Ginebra, February 2007. CL-0072.

[943] Memorial on the Merits, par. 726.

[944] C. Schreuer, "The Concept of Expropriation under the ECT and other Investment Protection Treaties". CL-0050.

also D. C. Scheurer requires that: "*The deprivation would have to be permanent or for a substantial period of time*". The non-attendance of this requirement has been credited ut supra.

1332. In short, this party, which has analysed in detail the concurrent circumstances, has established that (i) the measures discussed are due to the State's regulatory authority, exercised in an extensively regulated economic sector and in accordance to ensuring the sustainability of the system, reducing the tariff deficit and eliminating the over-remunerations, with full respect for the "reasonable return", (ii) that there has not been any substantial deprivation or the economic value of the investment of the Claimants or their powers of administration and management, (iii) that the measures do not have a permanent nature and (iv) that there has not been a translation of value of the investment of the Claimants to the State or a third party.

1333. The Claimants, on the contrary, are limited to a biased and unmotivated citation of a series of doctrinal rulings and articles, which cannot but strengthen the evidence that the Kingdom of Spain has complied with article 13 of the ECT.

(5.6) Conclusion

1334. The Claimants do not demonstrate how the measures analysed affected their alleged investment. In fact, the Claimants have not even been able to define, in a minimally consistent way, which is the asset or right that they have been expropriated from. On the one hand, they argue that they have been expropriated of the right to receive future subsidies and to manage the wind farms. On the other hand, they argue that the impact of the expropriation has occurred on their stakes in the companies that own the facilities. This is, they do not know what is the object of their investment, nor do they know what has been hypothetically expropriated from them.

1335. In addition, with regard to the right to receive subsidies and the authority to manage and administer the Wind Farms, the Claimants have not established that there is a right to receive a certain level of subsidies nor have they demonstrated that their indirect stake in the parks attributes them with powers of management and direction on the same.

1336. Therefore, pursuant to Spanish law, there is no right to receive benefits in the future, since they are mere expectations. Such expectations cannot be included in the investment concept of Article 1(6) ECT, nor can they benefit from the protection of Article 13 ECT

1337. On the other hand, they argue that the impact of the alleged expropriation has occurred on their shareholdings, as well as on their powers to administer and manage the wind farms.

1338. Well, the implementation of the "substantial deprivation" test leads to emphatically rejecting the existence of an expropriation. In fact, the measures adopted by the Kingdom of Spain (i) did not signify a substantial deprivation of the investment (they do not imply cessation of operation, nor take-over of the facilities, nor destruction of the value of the investment for ever); and (ii) are measures that represent an improvement for the society in general, without incurring economic benefit or transfer of assets to the Government of Spain or a private entity.

1339. It must therefore be concluded that the Kingdom of Spain has not expropriated the investment of the Claimants, so that it is not necessary to pay any type of compensation in this regard.

V. THE CLAIMANTS HAVE NO RIGHT TO THE REQUESTED REPARATION

1340. The alleged obligation Spain would have to repair the damages is briefly set forth in paragraphs 1066 and following of the Memorial on the Merits *"caused to the Claimants as a consequence of the Respondent's violations of its obligations under the standards of protection of Part III of the ECT…"*[945]. According to the Claimants, *"the damages for which full reparation is sought have been caused by Spain's internationally wrongful actions and omissions, namely, the adoption of Regulatory Framework No. 2 and Regulatory Framework No.3"*[946].

1341. In the first place, we have to stress that the earlier request contains a contradiction in itself: the legal and regulatory regime, from 1997 to the present, has always awarded the same thing, a reasonable return. Therefore, something that has not been dispossessed cannot be claimed and there can be no talk of damages.

1342. Secondly, since in the previous sections it has been demonstrated that Spain has not engaged in any violation of the provisions of the ECT, the Respondent has no obligation to pay compensation to the Claimant.

1343. Therefore, this section V presents subsidiarily, for the case that, in the first place, the Tribunal were to accept to have jurisdiction over this dispute and, additionally, secondly, the Tribunal were to understand that there is a breach on the part of the Kingdom of Spain of any provision of the ECT.

1344. On the other hand, this section is complemented by the report of the experts of Econ One Research of 15 June 2016.

1345. It should also be noted that the lack of provision of information (which will be required in the relevant proceedings) limits, at this time, the legitimate right of defense of the Respondent. In this regard, the experts of Econ One reference on repeated occasions the provisional nature of the calculations and estimates and include an annex[947] to their report with information that would be necessary, among other.

1346. Accordingly, we must carry out a full reserve to formulate further objections on the calculation of the compensation requested, including: the impropriety of the different parameters considered; the contributory fault of the Claimant; the Flow-Through of hypothetical damages; the incorrect determination of the dates of valuation considered for the FET standard; the inappropriate immunity against business risk; or the necessary discounts for marketability, for lack of control, or other.

[945] Memorial on the Merits (footnotes omitted) par. 1066.
[946] Memorial on the Merits (footnotes omitted) par. 1069.
[947] Econ One Report, Appendix B.

1347. Regardless of the foregoing, in this section, the following arguments will be developed (all of them, we reiterate, subsidiarily, and with reserve of subsequent objections to the *quantum*):

a) The alleged damages are totally and absolutely speculative.

b) The DCF method is inappropriate for the concurrent circumstances, in accordance with the doctrine.

c) The rates of return obtained reflect the speculative nature of its claim and the absence of any damage.

d) Subsidiary calculations using DCF: positive financial impact for the Claimant.

e) Subsidiarily: incorrect claim of interests.

A. The alleged damages are totally and absolutely speculative

1348. In the first place, the alleged damages estimated in the KPMG report are not compensable, as they are totally and absolutely speculative.

1349. In the Memorial on the Merits, it is indicated that the loss of historical and future cash flows must be compensated, distinguishing the cash flows supposedly generated until 31 December 2015, incorrectly called "Past damages"[948] and those that are alleged to be generated from that date onwards.

1350. Well, this approach opposing the distinction between “historical” flows and future flows ignores the basic concept of regulatory useful life and omits the joint consideration of cash flows, past and future, to ensure the reasonable return of the investments undertaken. Accordingly, such an approach must be rejected outright.

1351. The wind farms are guaranteed by law the enjoyment of a reasonable return, protected from the uncertainties and fluctuations in the market. Precisely for this reason, it is a paradox that, in the context of an investment that has a reasonable return guaranteed by law, a privilege that few entrepreneurs enjoy, the Claimant claims for violation of the FET standard.

1352. Against this guarantee, the Claimant intends to contend a claim based on a simplistic comparison of scenarios (actual and butfor), assuming that the “actual” one is going to be maintained in the coming decades, ignoring that the guiding principle of the system is constituted by the reasonable return guaranteed. It is for this reason that the projection of the existing parameters is hypothetical and illusory.

1353. We, as the Supreme Court of the Kingdom of Spain in similar situations, understand that the alleged damages have not been substantiated even minimally. The time horizon, together with the fact that there is no guarantee that the remuneration is petrified in the present form, always ensuring a reasonable return, makes the calculation of damages made speculative.

[948] Memorial on the Merits, par. 1091.

1354. A reasoning that will surely not be novel for the Claimant (nor, probably, its experts), considering that the same was clearly embodied in almost a hundred of sentences in which the Supreme Court has known of amendments to the remuneration scheme of renewable energies. Among them, mention can be made of Sentence of 24 September 2012 that, in its Legal Ground Six, declares the following:

> *"To sum up, with regard to the expert's report provided with the statement of claims to quantify the impact of the application of Royal Decree 1565/2010, of 19 November, on the return of the projects, we shall limit ourselves to reiterating that its conclusions cannot be accepted from the moment when its extrapolations were based on a future of thirty years of magnitude, the calculation of which lacks the necessary rigour and security. A "time horizon" of limitation to 30 years for the right to receive the regulated tariff, the loss of "equity value" of the photovoltaic plants affirmed in said reports is not proven. As on previous occasions, we refer to the dispositions already made in the judgement of 19 June 2012 (appeal 62/2011) and subsequent sentences"*[949].

1355. Therefore, speculative and hypothetical damages are being invoked. To sum up, the Claimants do not comply in any way with the burden of proof required of them.

B. <u>The DCF method is inappropriate due to the concurrent circumstances, in accordance with the doctrine</u>

1356. As the damages are merely speculative, the Claimant has had to resort to a method that is also speculative for its calculation.

1357. Thus, the Claimant has used the DCF method to calculate the market value, considering the future cash flows of the wind farms. As expressed in its Memorial on the Merits:

> *"KPMG has determined the expected free cash flows by way of the Discounted Free Cash Flow Method ("DFCFM"). Under this valuation technique, the expected free cash flows are discounted at an appropriate rate at the Valuation Date"*[950].

1358. Without prejudice to, obviously, the wide dissemination of the DCF method, in the present case there are a series of circumstances which manifestly discourage its use. In this sense, arbitral case law is clear and unequivocal on vetoing the implementation of the DCF when the same is excessively speculative.

1359. In this section, we will show how the doctrine and arbitral case law reject outright, under certain circumstances, speculative methods like the DCF and, in contrast, are inclined to give more credibility to more reliable methods such as those based on assets.

1360. That is to say, the doctrine and arbitral case law are inclined to check that the investor receives the repayment of its investments plus an adequate return on the cost of the same.

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[949] Sentence of the Third Chamber of the Supreme Court of 24 September 2012, Legal Ground Six. R-0147.
[950] Memorial on the Merits, par. 1096.

1361. In this regard, *Ripinsky* warns about the effect that often would lead to using the DCF, overestimating financial impacts based on future ones:

> *"[…] the future is uncertain and looking into the future requires one to make numerous assumptions and subjective choices regarding future market conditions, sales, costs, additional capital requirements, currency fluctuations, rates of inflation, levels of risk, etc. The end-result is thus inherently somewhat speculative. This explains why litigating parties' experts frequently produce DCF valuations with diverging results. Noting this tendency, Stauffer has warned against a 'Cinderella effect', that is, overvaluation of assets by claimants in their DCF valuations"*[951] *(emphasis added).*

1362. Well, in this case certain circumstances coincide that demonstrate both the inappropriateness and the impossibility of applying the DCF method:

(a) The fact that this is a capital intensive business, with an important asset base. Virtually the whole of its costs are investment costs in tangible infrastructures. There are no relevant intangibles to assess.

(b) The high dependence of the cash flows on volatile and unpredictable exogenous elements, such as the price of the pool, inter alia.

(c) The financial weakness of the Project Finance structures without recourse agreed, that excessively levered the wind farms, compromising and conditioning their viability.

1363. Bearing in mind the above elements, we will see different doctrinal pronouncements in this regard. Hence, we see that the DCF has been rejected on numerous occasions for cases such as the present one in which a series of characteristics arises:

> *"The DCF method has been rejected by tribunals on several grounds including:*
>
> *(i) lack of sufficiently long performance record;*
> (ii) *failure to establish future profitability of the investment;*
> (iii) *lack of sufficient finances to complete and operate the investment; and*
> (iv) *large disparity in the amount actually invested and the FMV claimed.*" (emphasis added).

1364. Consequently, given the inadmissibility of the DCF, the Arbitration Tribunals have frequently used, to assess the existence of damages, methods based on the costs of the assets, analysing if the latter are recovered and a reasonable return is obtained on them:

> *"The method of calculating FMV by reference to actual investments has proved quite popular in arbitral practice. […] they have turned to the historic costs of investment*

[951] *Damages in International Investment Law*, Sergey Ripinsky with Kevin Williams, British Institute of International and Comparative Law (BIICL), 2008, pages 200 and 201. RL-0057.

as the relevant approach to valuation when the evidence necessary to apply an income base method has been considered insufficient"[952]*. (Emphasis added).*

1365. For his part, *Marboe* stresses the advantages of methods based on assets, less speculative and more simple to apply:

"The advantage of this approach is that, in comparison with the income capitalization approach, it appears to be much easier and less speculative. It looks into the past and not into the future and is seemingly much simpler to apply than the highly complex forecasting and discounting processes"[953] *(Emphasis added).*

1366. Again, *Marboe* refers to the normal returns and the book value as an obligatory reference, particularly when the investment is very recent. Likewise, he refers to the reasonable rates of return:

"Experienced economists point to the fact that the significance of the ABV usually works with companies with normal rates of return. Extraordinarily high or low rated are rather rare and cannot be explained or be appropriately reflected by this method. Stauffer notes that extraordinarily high and 'abnormally poor performance must be explained, since, by definition most firms or ventures realize "average" rates of return'. This is also confirmed by Lou Wells who supports the use of the book value method for recently established businesses […]"[954]*(emphasis added).*

1367. Going into further detail on the same idea, Sabahi talks about the recovery of the costs plus a return on the same as an appropriate method of compensation:

"In Metalclad v Mexico, for example, […] considering that the investment was made recently and lacked a history of profitability, held that the investor could only recover its actual investment […] sunk costs in this case may have approximated the fair market value, because the investment was made recently.

Another example is the case of Wena v Egypt […]. The tribunal […] did not consider DCF appropriate because the ventures were new and the claimant has not proved satisfactorily that they would have become profitable. Instead, the tribunal awarded the value of the investment actually made […]."[955] *(Emphasis added).*

1368. In short, when the factual elements mentioned above coincide, we understand that all of them have to be considered by the Honourable Tribunal, in order to rule out any valuation based on a DCF in the present case.

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[952] *Damages in International Investment Law*, Sergey Ripinsky with Kevin Williams, British Institute of International and Comparative Law (BIICL), page 227. RL-0057.

[953] *Calculation of Compensation and Damages in International Investment Law*, Irmgard Marboe, Oxford, Oxford International Arbitration Series, 2009 , page 267. RL-0058.

[954] *Calculation of Compensation and Damages in International Investment Law*, Irmgard Marboe, Oxford, Oxford International Arbitration Series, 2009 , pages 275 and 276. RL-0058.

[955] *Compensation and Restitution in Investor-State Arbitration* – Principles and Practice, Borzu Sabahi, Oxford, International Economic Law, 201, pages 132-133. RL-0059.

C. The rates of return obtained reflect the speculative nature of its claim and the absence of any damage.

1369. In this section we are going to check with figures how the return obtained by the facilities of the Claimants exceed reference rates, and therefore no damage to the investments can be argued. To do this, we will primarily refer to what is reflected in paragraphs 113 et seq. of the Econ One report.

1370. In this way, the experts of Econ One have calculated, starting even with the data and the model of KPMG, that the wind farms of the Claimants grant, in the "actual" scenario (i.e., after the measures in dispute) a rate of return of 8.19%.

1371. It is clear that the return figures are extremely high, especially if compared with rates such as the reasonable return established in the current standard at 7.398%, or other rates reflected in the Econ One report, all of them around 7%.

1372. Therefore, talking about damage, when the rates of return obtained are higher than those expected in the market, is unfounded.

D. Subsidiary calculations using DCF: positive financial impact for the Claimants

1373. In this respect, it is necessary to recall that the Memorial on the Merits calls for the reparation of the damages with the following wording: "*the damages for which full reparation is sought have been caused by Spain's internationally wrongful actions and omissions, namely, the adoption of Regulatory Framework No. 2 and Regulatory Framework No. 3*"[956].

1374. The above claim comes from the false premise that the regulatory amendments have necessarily caused a damage.

1375. For this reason, and despite the fact that we understand that the DCF is inappropriate for this case, we will compare the results that a DCF would give from the difference between an Actual scenario and a But-for scenario, in such a way that we obtain a hypothetical financial impact.

1376. The discrepancies between the different DCF (KPMG's and Econ One's) derive for this exercise from the discount rates applicable to the cash flows and from the definition of the But-for.

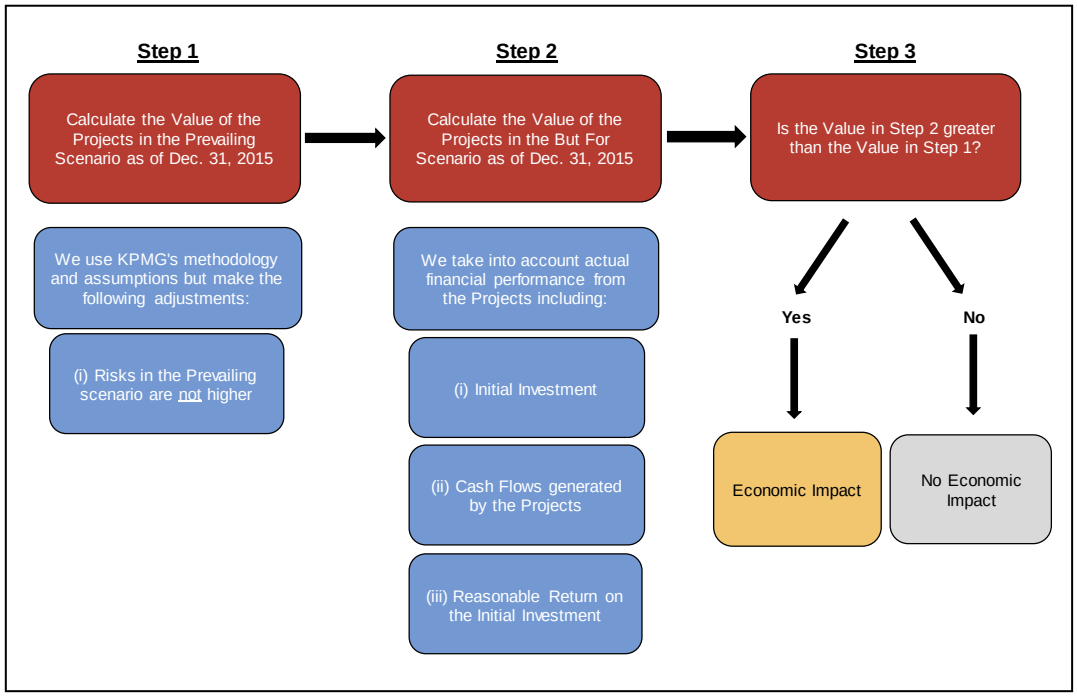
1377. In this regard, Econ One has considered (as opposed to KPMG) that the conditions of the Actual scenario would not entail a greater risk and greater uncertainty than the But-for scenario. In fact, in the Actual scenario, under the current regulations, we are faced with an stable framework that is more predictable and has less risk. This is demonstrated without reservation by the assessments of the market players and the numerous transactions that have occurred since the adoption of the disputed measures.

1378. With regard to the But-for scenario, it should be recalled that once the investor amortises its investment and the market price is sufficient to cover operating costs,

[956] Statement of Claim (footnotes omitted) par. 1069.

obtaining in this way the so-called "level playing field", it cannot continue to obtain subsidies.

1379. The methodology used in this subsidiary exercise is summarised in the following graph[957]:



1380. Applying the appropriate discount rate for the cash flows (eliminating the unjustified risk premium that KPMG adds), the Current scenario, using the own figures of KPMG, we obtain a value for the projects of the Claimant of EUR 71.4 million.

1381. With regard to the But-for scenario, the value of the investment in the same is obtained from the following table[958]:

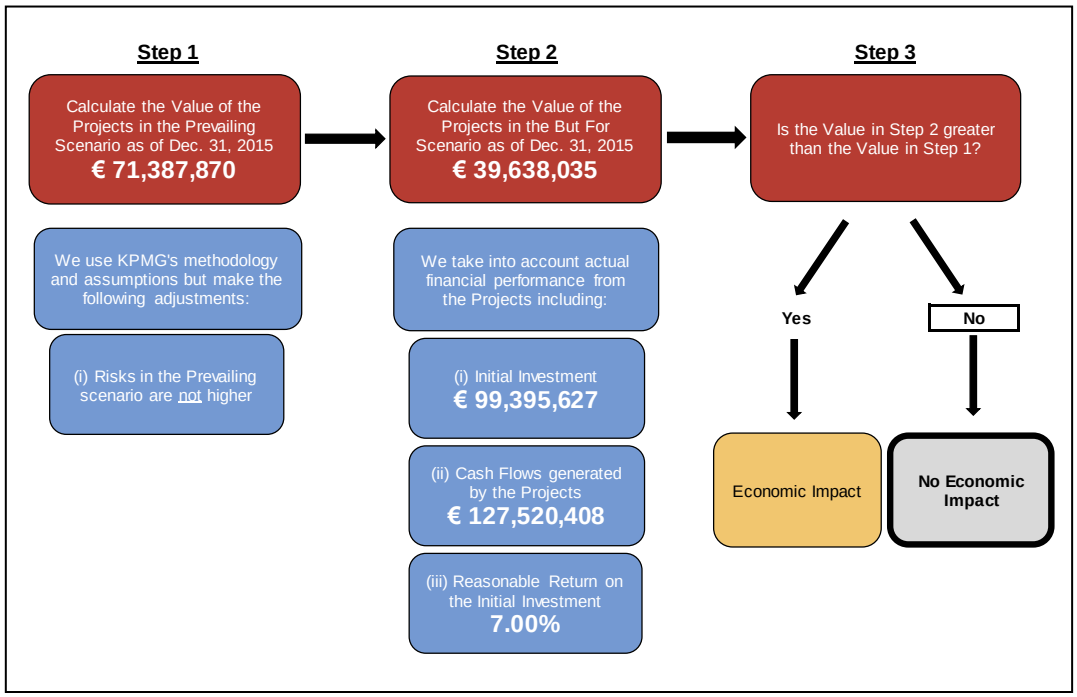
	Amounts (€)
1. Initial Investment	99,395,627
2. Reasonable Return on Investment	67,762,815
3. Cash Flows Generated by the Projects (2003-2015)	127,520,408
4. "But For" Value of the Projects (R1 + R2 − R3)	39,638,035

1382. As the Econ One experts note, "the "But For" value of the projects as of December 31, 2015 is €39.6 million. This means that if the Projects had been sold on this date at this amount, the Projects would have yielded a project IRR of 7%, meaning that the Projects'

[957] Econ One Report, Figure 14.
[958] Econ One Report, Table 10.

funders would have recovered their initial investment plus the reasonable rate of return for renewable energy projects"[959].

1383. The result we obtain is that there is no negative economic impact, but rather the opposite: the measures in dispute have increased the value of the investment of the Claimants in EUR 23.5 million[960].



E. Secondarily: incorrect identification of the interests.

1384. By logic order, we must now address the treatment that the Claimant gives to interests. With regard to the interests, the Econ One experts considered that, for the hypothetical case in which the Arbitration Tribunal would consider a damage, the interest to be considered would be very different from the one chosen by KPMG.

1385. In this way, KPMG has calculated interests between the appraisal date (31 December 2015) and the date of its report. And to this end it has considered two alternatives: a) a "commercial rate"; and b) a hypothetical wacc.

1386. On the contrary, the Econ One experts consider in their report more appropriate a "risk-free short term rate", taking into account the lack of default risk of the borrower, not assimilable to a risk paid by a "commercial rate".

1387. According to the foregoing, the inappropriateness of the interests calculated is evident.

[959] Econ One report, par. 196.
[960] Econ One Report, Figure 15. The EUR 23.5 million are calculated as (EUR 71.4 billion - EUR 39.6 million) x 74%.

VI. PETITUM AND RESERVATION OF RIGHTS

1388. In view of the arguments put forward in this writing, the Kingdom of Spain respectfully requests the Arbitration Tribunal that:

a) It declares to lack jurisdiction to hear the claims of the Claimants, or where appropriate, the inadmissibility of the same, in accordance with what is stated in the Objections of Jurisdiction contained in this writ.

b) Secondarily in the event that the Arbitration Tribunal were to decide that it has jurisdiction to hear the present controversy, it rejects all the claims of the Claimants on the merits, since the Kingdom of Spain has not breached in any way, the ECT, in accordance with what is set forth in section IV of the present Writ, regarding the Substance of the Matter.

c) Secondarily, that all of the recisionary claims of the Claimants are dismissed in as much as the latter do not have a right to compensation, in accordance with what is set forth in section V of this Writ; and

d) It condemns the Claimants to pay all costs and expenses derived from this arbitration, including ICSID administrative expenses, arbitrators' fees, and the arbitrators' fees and the fees of the legal representatives of the Kingdom of Spain, their experts and advisors, as well as any other cost or expense that has been incurred, all of this including a reasonable rate of interest from the date on which these costs are incurred and the date of their actual payment.

1389. The Kingdom of Spain reserves the right to supplement, modify or complement these pleadings and present any and all additional arguments that may be necessary in accordance with the ICSID Convention, the ICSID Rules of Arbitration, procedural orders and the directives of the Arbitration Tribunal in order to respond to all allegations made by the Claimant in regards to this matter.

Madrid, 15 June 2016

Respectfully submitted,

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