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### International Arbitration

## Chile Energy Bill Provokes Regulatory Risks for Investment in Renewables Sector

### *Timely Assessment of Investment Protections May Shape Navigation of New Developments*

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The Chilean Congress is currently considering a legislative proposal introduced by the Chilean Government aimed at subsidizing electricity costs for approximately 4.7 million households. The proposed bill introduces a temporary measure that would reduce profits for three years from small- and medium-sized distributed generation assets of less than 9 MW (locally known as PMGD). In a written statement, Energy Minister Diego Pardow stated that “we have identified a gap between the efficient cost of development and the income that a group of generators is receiving” and that “there is a space to contribute to the expansion of the subsidy.”

Many international sponsors have invested in the development of PMGD portfolios, with many international creditors providing financing. On October 1, 2024, ten financial institutions sent a letter to the Chilean Government indicating that the approval of the legislative proposal “could be a significant disincentive to investment in renewable energy.”

Key features of the proposed law include:

- **Modification of Revenue Structure for Distributed Generation Assets.** In an effort to manage energy costs for low-income families and increase subsidies, the bill proposes to cap for three years the revenues that PMGDs receive. This adjustment could generate approximately \$150 million in subsidies from 2025 to 2027, which represents approximately 30% of projected PMGD revenues for the same period, according to commentators. S&P Global explains that the cap would impact PMGDs by reducing cash flows and by making it harder to make debt payments.

- **Expansion of Powers of the Regulator and Increase in Fines.** The proposed law seeks to provide the regulator, the Superintendency of Electricity and Fuel, with the power to require corrective action plans from entities operating in the generation, distribution, transmission, transportation, and storage subsectors in cases of “inefficient performance.” Companies that fail to comply with the action plans could face significant fines through punitive proceedings. In the message submitted to Congress along with this initiative, the Chilean President stated that the “bill increases the amount of sanctions that the agency can impose,” aiming to double the current fines established in the regime.

Through Supreme Decree 244 of 2005, Chile implemented a framework to calculate a stabilized price per megawatt for PMGDs. This was revised through Supreme Decree 88 of 2019, by which Chile adjusted the framework for the stabilized price. The Government implemented a transition period for projects being developed at that time, allowing them to enjoy government support until 2034. However, the latest bill now threatens to change the structure that has attracted many investors to the renewable energy sector in Chile.

Chile has been known for being one of the most politically stable countries in Latin America. However, recent years showed rising levels of social unrest, political polarization, a more nationalist economy, and measures that mark a departure from long-standing policies in the country. New measures, like the proposed bill introduced by the Chilean Government, could further cause uncertainty in the legal and regulatory framework of other sectors in which international companies and creditors invest in Chile.

Chile has been a respondent in seven investment arbitrations before the International Centre for Settlement of Investment Disputes (ICSID) at the World Bank. New measures that affect investor rights could lead to more investment disputes involving Chile as the respondent state under investment arbitration frameworks that did not exist decades ago, but are now firmly established in Chile and the region. Chile currently has over 60 international treaties in force with investment protections, including treaties with various countries from the Americas, Europe, and Asia.

In a similar situation, and in response to the global financial crisis, Spain modified its renewable energy regime in 2010 by reducing incentives that attracted investment into the country. This led to over 50 arbitrations under the Energy Charter Treaty, with claims exceeding €8 billion from foreign investors, showing the possible consequences if Chile adopts the proposed bill.

The Chilean Government’s proposed legislative changes aimed at subsidizing electricity costs raise significant concerns for the renewable energy sector and investor confidence. Investors and creditors could face different risk management implications depending on the type and structure of their investment. Investors who put the right level of emphasis on the management of risk factors from the outset usually achieve the best outcomes to protect their investments. Arbitration is a key mechanism to protect investments in disputes that arise from changes in legislation.

*The Paul Hastings team is active in the Chilean renewables market and has decades of experience with Chilean investment and arbitration.*

Relevant sources of information:

Proposed Bill presented on August 26, 2024, Bulletin No. 17064-08, available at <https://www.camara.cl/legislacion/ProyectosDeLey/tramitacion.aspx?prmID=17680&prmBOLETIN=17064-08>

“News Analysis: Proposed revenue cap threatens Chilean distributed generation’s foreign investment”, available at <https://ionanalytics.com/insights/infralogic/chile-proposed-revenue-cap-threatens-distributed-generations-foreign-investment/>

“Dangerous Precedent’ Rattles Chile’s Renewable Energy Market”, available at <https://financialpost.com/pmnbusiness/pmnb/dangerous-precedent-rattles-chiles-renewable-energy-market>

“S&P Global dice que la ley de subsidio eléctrico es perjudicial para los PMGD, el sector de Energía y la imagen de Chile”, available at <https://www.latercera.com/pulso/noticia/sp-global-dice-que-la-ley-de-subsidio-electrico-es-perjudicial-para-los-pmgd-el-sector-de-energia-y-la-imagen-de-chile/SA5OMISIPNFSHB3DAPWLUMWUN4/>

“La carta de 10 instituciones financieras a Pardow y Marcel por los PMGD: proyecto de subsidio ‘podría significar un desincentivo relevante a la inversión”, available at <https://www.df.cl/empresas/energia/la-carta-de-10-instituciones-financieras-a-pardow-y-marcel-por-los-pmgd>

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