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Energy Updates in Brief

By Donna J. Bobbish

Court Update: FERC Wins! U.S. Supreme Court Finds Maryland’s New Generation Incentive Program Preempted by FPA and Resurrects FERC Order No. 745 Demand Response Compensation

U.S. Supreme Court Finds Maryland’s New Generation Incentive Program Preempted by FPA

On April 19, in an 8-0 judgment, the Supreme Court affirmed a decision by the U.S. Court of Appeals for the Fourth Circuit, which held that the FPA preempted incentive pricing established by the Maryland Public Service Commission (MPSC) for new generation clearing the PJM market auction that is different from the price the same generation would receive under rules established by FERC.¹

Under its incentive program, the MPSC, through a proposal process, had selected CPV Maryland, LLC (CPV) to construct a new electricity generating facility and required load serving entities in Maryland to enter into a 20-year contract for differences with CPV at the rate CPV had specified in its proposal to the MPSC. Under the contract for differences, CPV sells its capacity to PJM through the PJM auction, but receives the contract rate instead of the auction clearing price for the sales to PJM.

In *Hughes v. Talen Energy Marketing, LLC*, 578 U.S. ___ (2016), the Supreme Court held that the MPSC’s program is preempted because it disregards the interstate wholesale rate required by FERC under the FPA. The Supreme Court found that through the exercise of its exclusive authority over interstate wholesale sales, FERC approved PJM’s capacity auction as the sole rate-setting mechanism for capacity sales to PJM, and has deemed the auction clearing price to be just and reasonable. The Supreme Court further found that the MPSC, through the contract for differences, guarantees CPV a rate different from the auction clearing price for its interstate capacity sales to PJM.

The Supreme Court agreed with the Fourth Circuit that the MPSC incentive program “sets an interstate wholesale rate, contravening the FPA’s division of authority between state and federal regulators.”

The Supreme Court emphasized, however, that it rejected the MPSC program only because it disregards an interstate wholesale rate required by FERC, and that nothing in its opinion should be read to foreclose Maryland and other states from encouraging production of new or clean generation through measures “untethered to a generator’s wholesale market participation.” According to the Supreme Court, “[s]o long as a State does not condition payment of funds on capacity

¹ PPL *EnergyPlus*, LLC v. Nazarian, 753 F.3d 467 (2014).

clearing the auction, the State's program would not suffer from the fatal defect that renders Maryland's program unacceptable."

On April 25, as anticipated in light of its decision on the Maryland incentive program, the Supreme Court denied two petitions for certiorari with respect to a decision by the U.S. Court of Appeals for the Third Circuit, finding that a similar electricity generation incentive program in New Jersey is preempted by the FPA.² States wishing to promote generation will have the task of developing incentive programs consistent with the Supreme Court's ruling.

U.S. Supreme Court Resurrects FERC Order No. 745 Demand Response Compensation

In January, in a 6-2 decision, the U.S. Supreme Court reanimated FERC's Order No. 745,³ which requires market operators, such as regional transmission organizations and independent system operators, to pay the same locational marginal price (LMP) to both demand response providers conserving energy and to generators for producing it, provided a "net benefits test" is met ensuring that accepted bids actually save consumers money.

The Supreme Court reversed the 2014 decision of the U.S. Court of Appeals for the District of Columbia Circuit (D.C. Circuit), which vacated in its entirety FERC Order No. 745 because demand response is "part of the retail market" and "a reduction in consumption cannot be a wholesale sale." Based on these findings, the D.C. Circuit concluded, FERC had "encroach[ed]" on the states' exclusive jurisdiction to regulate the retail market.⁴ Section 201(b) of the Federal Power Act (FPA) gives FERC jurisdiction over the transmission and wholesale sale of electricity in interstate commerce, but does not give FERC authority to regulate intrastate sales and the transmission of electricity.

In *FERC v. EPSA*, 577 U.S. ____ (2016), the Supreme Court held that contrary to the lower court's ruling, the FPA provides FERC with the authority to regulate wholesale market operators' compensation for demand response bids, because demand response "directly affects" wholesale rates and, in Order No. 745, FERC has not regulated retail electricity sales. The Supreme Court found that wholesale demand response is all about reducing wholesale rates, and therefore, rules and practices that determine how those programs operate are all about wholesale rates. The Supreme Court also found that while Order No. 745 affects retail sales, a FERC regulation does not run afoul of Section 201(b) of the FPA just because it affects (as opposed to specifies) the quantity or terms of retail sales.

The Supreme Court further held that FERC's decision in Order No. 745 to provide the same compensation to demand response providers at LMP as to generators was not "arbitrary and capricious," because FERC weighed competing views, selected a compensation formula with adequate support in the record and intelligibly explained the reasons for making that choice.

² States wishing to promote generation will have the task of developing incentive programs consistent with the Supreme Court's ruling. *PPL Energyplus, LLC v. Solomon*, 766 F.3d 241 (3d Cir. 2014).

³ *Demand Response Compensation in Organized Wholesale Energy Markets*, Order No. 745, FERC Stats. & Regs. ¶ 31,322 (2011), *reh'g denied*, Order No. 745-A, 137 FERC ¶ 61,215 (2011), *reh'g denied*, Order No. 745-B, 138 FERC ¶ 61,148 (2012).

⁴ *EPSA v. FERC*, 753 F.3d 216 (D.C. Cir. 2014).

Finally, the Supreme Court observed that the position of the opponents of FERC Order No. 745 – that FERC has no authority under the FPA to regulate demand response at all – would “subvert” the FPA, which has a core objective to “protect against excessive prices.” The Court found that FERC had amply explained how wholesale demand response brings down costs and prevents service interruption in peak periods, and noted that states do not have the authority to regulate demand response either. Thus, the opponents’ position would extinguish the wholesale demand response program in its entirety and create a federal/state regulatory “gap” that the FPA was enacted to eliminate.

LNG Update: FERC Denies Application for Jordan Cove LNG Export Project

In March, in a decision that took most industry observers by surprise, the Federal Energy Regulatory Commission (FERC) denied the application of Jordan Cove Energy Project, L.P. (Jordan Cove) for authorization under Section 3 of the Natural Gas Act (NGA) to site, construct and operate a liquefied natural gas (LNG) export terminal and associated facilities in Coos County, Oregon (Jordan Cove LNG Facility).⁵ FERC denied Jordan Cove’s application after it had denied the application of Pacific Connector Gas Pipeline, LP (Pacific Connector) for a certificate of public convenience and necessity under Section 7(c) of the NGA to construct and operate interstate pipeline facilities that would transport natural gas produced in western Canada and the US Rocky Mountain region to the Jordan Cove LNG Facility (Pacific Connector Pipeline).

In 2011, the US Department of Energy Office of Fossil Energy (DOE/FE) authorized Jordan Cove to export LNG by vessel to countries with which the US has Free Trade Agreements (FTA) that require national treatment for trade in natural gas (FTA Countries). “National treatment” for trade means treating an imported good the same as a locally produced good once it enters a market. As identified by DOE/FE, FTA countries currently include Australia, Bahrain, Canada, Chile, Colombia, Dominican Republic, El Salvador, Guatemala, Honduras, Jordan, Mexico, Morocco, Nicaragua, Oman, Panama, Peru, Republic of Korea and Singapore.

DOE/FE granted Jordan Cove conditional authorization to export LNG to non-FTA Countries in 2014,⁶ but has not yet granted Jordan Cove final authorization to export LNG to non-FTA Countries. Such authorization requires a finding by DOE/FE that the proposed export has not been shown to be inconsistent with the public interest. In October 2015, Jordan Cove amended its application, seeking to increase its export authorization from 292 Bcf to up to 350 Bcf of natural gas per year.

As proposed, the Jordan Cove LNG Facility would include, among other things, four trains that would each process approximately 1.5 million metric tons per annum (MMTPA) of LNG for export to Asia, for transport to southern Oregon and potentially for transport to Hawaii and Alaska, while the Pacific Connector would consist of a new 232-mile-long interstate pipeline designed to deliver up to 1.06 Bcf/d of natural gas to the Jordan Cove LNG Facility.

⁵ *Jordan Cove Energy Project, L.P., et al.*, “Order Denying Applications for Certificate and Section 3 Authorization,” 154 FERC ¶ 61,190 (Mar. 11, 2016).

⁶ *Jordan Cove Energy Project, L.P.*, DOE/FE Order No. 3041 (Dec. 7, 2011) and *Jordan Cove Energy Project, L.P.*, DOE/FE Order No. 3413 (Mar. 24, 2014).

The Sierra Club protested both applications, and an individual landowner affected by the construction of the Pacific Connector Pipeline protested the application for authorization to construct the pipeline. Numerous other entities and individuals intervened in the proceedings and submitted comments, identifying environmental and landowner concerns.

FERC issued a final Environmental Impact Statement (EIS) for the Jordan Cove LNG Facility and the Pacific Connector Pipeline at the end of September 2015. The final EIS found that the proposed projects would result in some limited adverse environmental impact, but that these adverse impacts could be avoided or reduced by implementation of mitigation measures proposed by Jordan Cove and Pacific Connector and recommended by FERC staff and other agencies.

In its March 11 order, FERC found that the Pacific Connector Pipeline would affect 157.3 miles of privately owned lands, owned by approximately 630 landowners. FERC also stated that Pacific Connector had presented little or no evidence of need for its proposed pipeline, as it had not entered into any precedent agreements for capacity or conducted an open season soliciting expressions of interest in capacity on the pipeline. Although DOE/FE had found that the export of LNG by Jordan Cove is consistent with the public interest, FERC declined to rely on that decision to support a finding that the construction and operation of the Pacific Connector Pipeline is consistent with the public convenience and necessity. FERC stated that Pacific Connector's generalized allegations of need for the pipeline do not outweigh the potential for adverse impact on landowners and communities. FERC denied Pacific Connector's request for authorization to construct its proposed pipeline because the record does not support a finding that the public benefits of the proposed pipeline do not outweigh the adverse effects on landowners, which could be subject to the exercise of eminent domain if FERC granted Pacific Connector a certificate of public convenience and necessity.

Having denied the application of Pacific Connector, FERC observed that it has not previously authorized LNG export facilities without a known transportation source of natural gas. FERC concluded that the record does not support a finding that the Jordan Cove LNG Facility can operate absent the Pacific Connector Pipeline, and also denied Jordan Cove's application for authorization to construct and operate its proposed LNG facilities.

FERC indicated that its ruling is without prejudice to Jordan Cove and/or Pacific Connector filing a new application should the companies show a market need for its services in the future.

After FERC issued its order, several intervenors in the non-FTA export proceeding before DOE/FE asked DOE/FE to deny Jordan Cove final authorization to export LNG to Non-FTA Countries because FERC had denied Jordan Cove's application for authorization to site, construct and operate the Jordan Cove LNG Facility. DOE/FE has granted Jordan Cove additional time to respond to these comments.

In addition, Sierra Club asked the US Court of Appeals for the District of Columbia Circuit to take FERC's March 11 order into consideration in three cases currently pending before that court. In these cases, the Sierra Club has challenged FERC orders authorizing the construction of LNG export facilities and associated interstate natural gas pipelines.⁷ The LNG

⁷ *Sierra Club v. FERC*, No. 15-1133 (challenging FERC order authorizing Corpus Christi Liquefaction to site, construct, and operate LNG export and import facilities on Corpus Christi Bay, Texas, and to construct and operate related pipeline and compressor facilities), *Sierra Club v. FERC*, No. 14-1249 (challenging FERC approval of requested increase in production capacity of Sabine Pass Liquefied Natural Gas export terminal), and *Sierra Club v. FERC*, No. 14-1275 (challenging FERC order authorizing Freeport LNG to construct and operate LNG export facilities).

project companies in each of the court proceedings opposed Sierra Club's request, arguing that the basis upon which FERC denied the applications of Jordan Cove and Pacific Connector, a lack of demonstrated need for the Jordan Cove LNG Facility and the Pacific Connector Pipeline, is not the basis on which Sierra Club seeks reversal of the FERC orders authorizing the construction of unrelated LNG export facilities and associated interstate natural gas pipelines, which is the sufficiency of the environmental review of those projects.

On April 8, Jordan Cove and Pacific Connector filed with FERC a request for rehearing of the March 11 order. Among other things, Jordan Cove and Pacific Connector argue that FERC should reverse its March 11 decision, and authorize the Pacific Connector Pipeline and the Jordan Cove LNG Facility because, since March 11, five agreements have been reached which demonstrate the need for the Pacific Connector Pipeline and Jordan Cove LNG Facility.

With respect to the Jordan Cove LNG Facility, the request for rehearing indicates that, since FERC issued its order, Jordan Cove has finalized key commercial terms with JERA Co., Inc, a joint venture of Tokyo Electric Power Company, Incorporated, and Chubu Electric Power Co., Inc., for the sale of at least 1.5 MMTPA of natural gas liquefaction capacity for an initial term of 20 years, and also has reached a preliminary agreement with ITOCHU Corporation with respect to key commercial terms for the purchase by ITOCHU of an additional 1.5 MMTPA of natural gas liquefaction capacity for an initial term of 20 years.

With respect to the Pacific Connector Pipeline, the request for rehearing indicates that Pacific Connector has executed precedent agreements with Macquarie Energy LLC, Avista Corporation and Jordan Cove for firm transportation service on the Pacific Connector Pipeline.

Jordan Cove and Pacific Connector also argue on rehearing that requiring them to file a new application is neither an efficient nor commercially feasible approach in light of the approximately \$300 million in project development that has been expended by the sponsors of Jordan Cove and Pacific Connector through the end of 2015.

Enforcement Update: FERC Proposes Penalties for Market Manipulation in PJM and the CFTC Considers Private Rights of Action for RTO/ISO Transactions

FERC Proposes Penalties for Market Manipulation in PJM

In January, FERC issued an order requiring Coaltrain Energy, L.P., a now-defunct financial trading firm, its two co-owners and four of its traders and analysts, to show cause as to why they should not be found to have violated Section 222 of the Federal Power Act and Section 1c.2 of FERC's regulations, which prohibit electric energy market manipulation, by engaging in fraudulent Up To Congestion (UTC) transactions in the energy markets operated by PJM Interconnection L.L.C. (PJM).⁸

⁸ *Coaltrain Energy, L.P., et al.*, Docket No. IN16-4-000, "Order to Show Cause and Notice of Proposed Penalty," (Jan. 6, 2016).

Market participants use UTC transactions as a congestion management tool to hedge exposure to real-time congestion charges between the source and sink of physical energy transactions in PJM, while financial traders use UTC transactions as a “purely virtual project.”

FERC attached to its order a Report and Recommendation by FERC’s Enforcement Staff alleging that from June 15 to September 2, 2010, Coaltrain undertook a fraudulent scheme to inflate trade volumes of UTCs through transactions designed to wrongfully collect large amounts of market credits known as Marginal Loss Surplus Allocations (MLSA) based simply on trading volume. MLSA is the FERC-authorized distribution to market participants in PJM of the surplus revenues that PJM collects for transmission line losses. Specifically, the Enforcement Staff Report alleges that Coaltrain discovered that it could profit from MLSA payments alone if UTC price spreads could be minimized or avoided entirely and devised a scheme called the “Over-Collected Losses,” or OCL, Strategy. The OCL Strategy involved researching and executing sham UTC trades on paths with reliably zero or near-zero price spreads not to profit from price differentials between the day-ahead and real-time markets, but rather to avoid or nullify such price spreads in order to profit from MLSA payments alone. The Enforcement Staff Report alleges that Coaltrain made OCL Strategy trades on 40 separate paths, but made most of the volume of OCL Strategy trades on two paths that FERC had addressed recently in another order assessing penalties.

In its order, FERC further directed Coaltrain to show cause why it should not be found to have violated FERC’s rules through false and misleading statements and material omissions in responding to data requests relating to FERC’s investigation of Coaltrain’s trading conduct. FERC also directed Coaltrain and its co-owners to show cause why they should not be required to disgorge unjust profits of \$4,121,894. Finally, FERC directed Coaltrain’s co-owners and traders and analysts to show cause why they should not be assessed civil penalties totaling some \$38,250,000, and directed Coaltrain’s co-owners to show why they should not be held jointly and severally liable for civil penalties of \$26,000,000 assessed against Coaltrain.

In early March, Coaltrain, its two owners and four traders filed responses to the show cause order challenging the findings of the Enforcement Staff Report and FERC’s proposed penalties.

CFTC Considers Private Right of Action for RTO/ISO Transactions

In late February, representatives of the US electricity industry, the Public Utility Commission of Texas (PUCT), and regional transmission organizations (RTOs) and independent system operators (ISOs) participated in a public meeting before the Commodity Futures Trading Commission (CFTC) to urge the CFTC to revise a proposed order issued in 2015 exempting certain transactions in the market administered by Southwest Power Pool (SPP), an RTO, from most provisions of the Commodity Exchange Act (CEA) and the CFTC’s rules, but reserving its authority to enforce fraud, manipulation and other scienter-based violations of the CEA with respect to such transactions (the SPP Order).⁹

⁹ *Notice of Proposed Order and Request for Comment on an Application for an Exemption Order From Southwest Power Pool, Inc. From Certain Provisions of the Commodity Exchange Act Pursuant to the Authority Provided in Section 4(c)(6) of the Act*, 80 Fed. Reg. 29490 (May 21, 2015)

The SPP Order has received attention because, in it, the CFTC also has suggested that it intends to permit private parties to bring suit for fraud, manipulation and other scienter-based violations of the CEA involving transactions in the SPP market pursuant to Section 22 of the CEA, which establishes a private right of action for violations of the CEA's provisions. The preamble to the SPP Order also suggested that the CFTC intends the same result — permitting private lawsuits — in a similar final order issued in 2013 exempting from most provisions of the CEA certain transactions offered or entered into on six other RTOs or ISOs (the 2013 Order).¹⁰

As part of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Congress expanded the CFTC's jurisdiction to include swaps as well as futures. It also sought to avoid jurisdictional disputes between the CFTC, FERC and the PUCT over the regulation of ISO and RTO transactions by adding a specific provision to Section 4(c) of the CEA directing the CFTC to grant exemptions from transactions made pursuant to a FERC-approved tariff or a PUCT protocol if the CFTC finds that such an exemption is in the public interest.

The 2013 Order exempts from most provisions of the CEA and CFTC regulations the purchase or sale of specifically defined “financial transmission rights,” “energy transactions,” forward capacity transactions” and “reserve or regulation transactions” that are offered or sold in markets administered by Midwest Independent Transmission System Operator, Inc., ISO New England, Inc., PJM, the California Independent System Operator Corporation, the New York Independent System Operator, Inc. and the Electric Reliability Council of Texas, Inc. (ERCOT) pursuant to a tariff or protocol that has been approved or permitted to take effect by FERC or the PUCT.

The SPP Order exempts from most provisions of the CEA and CFTC regulations contracts, agreements and transactions for the purchase or sale of the limited electric energy-related products offered or enter into a market administered by SPP pursuant to SPP's tariff. The general anti-fraud, anti-manipulation authority and scienter-based prohibitions of the CEA and CFTC's regulations would still apply, however.

The CFTC further said in the SPP Order that “[i]t would be highly unusual for the [CFTC] to reserve to itself the power to pursue claims for fraud and manipulation – a power that includes the option of seeking restitution for persons who have sustained losses from such violations or a disgorgement of gain received in connection with such violations – while at the same time denying private rights of action and damages remedies for the same violations. * * * Thus, the [CFTC] did not intend to create such a limitation and believes that the [2013 Order] does not prevent private claims for fraud or manipulation under the [CEA]. For the avoidance of doubt, the [CFTC] notes that this view equally applies to SPP's proposed exemption. Therefore, the [p]roposed [e]xemption also would not preclude such private claims.”¹¹

¹⁰ *Final Order in Response to a Petition from Certain Independent System Operators and Regional Transmission Organizations to Exempt Specified Transactions Authorized by a Tariff or Protocol Approved by the Federal Energy Regulatory Commission or the Public Utility Commission of Texas From Certain Provisions of the Commodity Exchange Act Pursuant to the Authority Provided in the Act*, 78 Fed. Reg. 19880, April 2, 2013.

¹¹ 2013 Order, 80 Fed. Reg. at p. 29493.

The participants at the February 25 meeting warned the CFTC that permitting private lawsuits with respect to transactions taking place within RTOs and ISOs will undermine regulatory certainty and could result in collateral attacks on the electricity market structure that state and federal regulators have established over the past several decades.

On the same day that the CFTC held its public hearing on the SPP Order, the US Court of Appeals for the Fifth Circuit affirmed an order of the US District Court for the Southern District of Texas dismissing a lawsuit by Aspire Commodities, L.P. and Raiden Commodities, L.P. against GDF Suez Energy North American, Inc. and its subsidiaries for violating anti-manipulation provisions of the CEA.¹² Aspire alleged that GDF Suez had manipulated the LMP on the ERCOT grid to profit on its trades, violating the anti-manipulation provisions of the CEA. GDF Suez moved to dismiss the suit because of the CFTC's 2013 Order which had exempted ERCOT from provisions of the CEA. The district court had granted the motion to dismiss.

The Fifth Circuit affirmed the lower court's decision, finding that while the CFTC's 2013 Order clearly subjected these ERCOT transactions to the anti-manipulation provision of the CEA, and that the CFTC expressly retained the authority to enforce this anti-manipulation section, those ERCOT transactions are exempted from a private right of action under the CEA.

Aspire had argued that under a proper interpretation of the 2013 Order, guided by the SPP Order, the private right of action under the CEA still applies to transactions in ERCOT. The court rejected Aspire's argument, among other things, because it found that the CFTC's statements in the preamble of the 2013 Order "directly contradict" the plain language of the 2013 Order, which exempts agreements, contracts and transactions in the ERCOT market from all provisions of the CEA, except certain enumerated provisions and does not list Section 22 of the CEA, which allows for private actions, as an excepted provision.

¹² *Aspire Commodities, L.P., et al. v. GDF Suez Energy north America, Inc., et al.*, No. 15-20125 (Feb. 25, 2016).



Electrify Africa Act of 2015

by Devin Lei and Ali Hassanali

On February 8, 2016, President Obama signed into law the Electrify Africa Act of 2015 (H.R. 2847/S. 2152), capping an almost two-year effort to pass the legislation. The legislation, which had overwhelming bipartisan support in both houses of Congress, is intended to build on the success of the [Power Africa](#) initiative introduced by President Obama on [June 30, 2013](#). This initiative is aimed at bringing together and leveraging relationships between technical and legal experts, the private sector and governments from around the world to provide access to electricity for 50 million people in sub-Saharan Africa by 2020. The Electrify Africa Act is designed to transform and improve some of the Power Africa initiatives by providing a framework for US government agencies to invest in and promote energy solutions in sub-Saharan Africa.

The Power Africa Initiative

More than two-thirds of the population of sub-Saharan Africa is without electricity, and more than 85% of those living in rural areas lack access to electricity. According to the [International Energy Agency](#), sub-Saharan Africa will require more than \$300 billion in investments to achieve universal electricity access by 2030. According to the US Agency for International Aid (USAID), by combining the expertise of 12 US government agencies and private investors, and with the cooperation of governments in the region, the Power Africa initiative is intended to unlock the substantial wind, solar, hydro, natural gas, biomass and geothermal resources available in the region, with overall goals of enhancing energy security, promoting economic growth and reducing poverty.

The White House, through a press statement issued at the inception of the Power Africa initiative, confirmed that the US had committed more than \$7 billion over five years to support the Power Africa initiative, with additional support and financial commitments provided by USAID, Overseas Private Investment Corporation (OPIC), US Export-Import Bank (Ex-Im), The Millennium Challenge Corporation (MCC), the US Trade and Development Agency (USTDA) and US African Development Foundation (USADF). Now in its third year, this initial \$7 billion commitment has leveraged nearly \$43 billion in additional commitments from the public and private sectors, including more than \$31 billion in commitments from various private sector partners, according to recent [figures published by USAID](#). Other public sector partners, including the African Development Bank (AfDB), the World Bank Group and the European Union, have collectively committed nearly \$12 billion to support the Power Africa initiative and promote sustainable energy activities across the sub-Saharan African region. To date, USAID is tracking 239 transactions across 24 countries in the region which, if successful, would yield more than 26,000 Megawatts (MW) of electricity.

The Electrify Africa Act

The purpose of the Electrify Africa Act is to improve access to affordable and reliable electricity in sub-Saharan Africa through streamlined, coordinated action by US state and governmental agencies under a unified administrative strategy plan. The law's statement of purpose indicates that the US, in partnership with sub-Saharan countries, will support efforts to

promote first-time electricity and power services for at least 50 million people in sub-Saharan Africa by 2020 and will encourage installation of at least 20,000 additional MW of electricity. It also encourages necessary in-country reforms and promotes an energy development strategy for sub-Saharan Africa that includes the use of oil, natural gas, coal, hydroelectric, wind, solar, geothermal power and other sources of energy.

The Electrify Africa Act requires the President to establish and submit to Congress a comprehensive multi-year strategy, consistent with the law's policy goals, to encourage countries in sub-Saharan Africa to implement national power strategies and develop an appropriate mix of power solutions. Its focus is to provide access to sufficient, reliable, affordable and sustainable power in order to reduce poverty and drive economic growth and job creation in the region. This strategy must address ways to attract private investment in the power sector in the region, both on and off the grid, assess the financial viability of power utilities and their current and potential capabilities, and be sufficiently flexible to allow for technological innovation in the sector. The President may also establish an interagency working group to coordinate executive branch agencies involved in implementing the strategy and to facilitate partnerships among executive agencies, the private sector and other development agencies to ensure effective implementation.

The statute also directs the Administrator of USAID, the Director of USTDA, OPIC and the leadership of the MCC to appropriate, prioritize and expedite institutional efforts and assistance to promote the development of power projects and markets consistent with the goals, policies and strategy of the Electrify Africa Act. US representatives at certain international bodies, including the World Bank Group and the AfDB, are further directed to use the influence of the United States, consistent with its broad development goals, to (a) encourage those institutions to significantly increase efforts in sub-Saharan electrification projects; (b) commit to significantly increase efforts to promote investment in power and electrification projects in sub-Saharan Africa; (c) enhance coordination with the private sector; and (d) provide technical assistance to regulatory authorities to remove legal, political and economic barriers to investment in otherwise commercially viable energy projects in the region.

The President is required within three years to submit a strategy progress report to Congress. This report must include information regarding US programs supporting policy and legislative changes that lead to increased power generation and access in sub-Saharan Africa, and power projects receiving US government support in the region.

Conclusion

The Power Africa initiative was instrumental in directing governmental, institutional and public and private support for promoting investment in the power sector and enhancing access to electricity in sub-Saharan Africa. By spearheading this initiative, and through the enactment of the Electrify Africa Act, President Obama has cemented his legacy in developing a multi-stakeholder partnership among governments and public and private actors to tackle the energy infrastructure void that currently exists in sub-Saharan Africa. Through enactment of the Electrify Africa Act, the Obama administration has also been able to establish the pursuit of such goals as official US government policy for the region.



Indonesia's New Oil and Gas Legislation

by Bill McCormack, Jean-Louis Neves Mandelli and Oene Marseille of ABNR Law, Jakarta, Indonesia

Since November 2012, the Indonesian oil and gas regulatory framework has been in a state of transition. A new Oil and Gas Law, currently under discussion before the Indonesian Parliament, is expected to be enacted during the first half of 2016.

One of the main triggers for the reform was the Indonesian Constitutional Court's decision on November 13, 2012, pursuant to which Badan Pelaksana Kegiatan Usaha Hulu Minyak dan Gas Bumi (BPMIGAS), the state upstream oil and gas regulator, was declared unconstitutional. A key driver for the reform has been the change in Indonesia's oil and gas position. Due to decreasing production and increasing consumption, Indonesia is a net importer of oil and is expected to soon become a net importer of gas. As a result, the Indonesian State has focused on improving the country's energy security, including by increasing control over its oil and gas resources. These drivers are expected to be reflected in the key changes introduced by the new oil and gas legislation.

Although the new Oil and Gas Law is expected to be passed imminently, the final terms of the law are still unclear and may differ from those included in the draft on which this article is based.

New Upstream Regulatory Structure

Until November 2012, BPMIGAS exercised regulatory control over upstream oil and gas operations. BPMIGAS was a non-profit, independent, state-owned legal entity. All upstream production-sharing agreements ("*Kontrak Kerja Sama*") were entered into between investors and BPMIGAS. BPMIGAS and the relevant articles establishing BPMIGAS in Indonesia's current Oil and Gas Law (Law No. 22/2001) were declared unconstitutional pursuant to Art. 33 of the Indonesian Constitution, which requires "all the natural wealth on land and in the waters" to fall "under the jurisdiction of the State." Because BPMIGAS was not directly under the control of the Indonesian Ministry of Energy and Mineral Resources (MEMR), this requirement was held to be breached. As a result, BPMIGAS was disbanded and all its duties, functions and responsibilities were transferred by Presidential Regulation to a temporary work unit known as SKS set up and controlled by MEMR. All upstream oil and gas contracts previously awarded by BPMIGAS remained in full force and effect. SKS was later superseded in 2013 by the Special Task Force for Upstream Oil and Gas Business (SKKMIGAS), also controlled by MEMR.

Under the new Oil and Gas Law, SKKMIGAS will be replaced by a new special state-owned enterprise (BUMN-K) for the oil and gas sector (except in Aceh where this role will be undertaken by a regional specialized state-owned enterprise). BUMN-K is expected to fall under the direct control of MEMR and will have a similar regulatory mandate to BPMIGAS/SKKMIGAS.

As concerns the oil and gas licensing structure, the BUMN-K will, like its predecessors, enter into production-sharing contracts with licensees. However, we understand that MEMR will have a leading role in determining the terms and conditions of these contracts (such as what costs are recoverable).

Under the new Oil and Gas Law, PT Pertamina, Indonesia's national oil company ("Pertamina"), will have a right of first refusal over any new oil and gas contracts so as to increase its role as producer. The draft law included a note to the effect that should Pertamina exercise this right, it would be required to hold a 100% interest in the contract and that farm-ins would not be permitted. This could restrict Pertamina's ability to access private investors' capital and expertise. However, other options to allow private investors to participate in these oil and gas contracts indirectly (such as services contracts) may be available to Pertamina. If Pertamina does not exercise its right of first refusal, the BUMN-K will be entitled to auction the relevant oil and gas contract to private companies.

In a key departure from previous practice, we understand the BUMN-K is intended to operate as a commercial undertaking (rather than as a non-profit organization like BPMIGAS). This is intended to encourage a more commercial approach to the management of Indonesia's oil and gas sector and to allow BUMN-K to develop sufficient financial standing to participate in oil and gas projects without requiring its obligations to be guaranteed by the Indonesian government. However, it is unclear how this will be balanced against the MEMR's rights to direct the terms and conditions of oil and gas contracts. The BUMN-K is expected to hold only minority participations in any oil and gas contracts.

At the end of the term of any oil and gas contract, BUMN-K is required to transfer all rights to the contract to Pertamina. We understand that this would not apply to expiring existing oil and gas contracts.

Reform of Domestic Market Obligation

Since one of the key drivers for the reform of the Indonesian Oil and Gas Law is improving the country's security of supply, the new oil and gas legislation will look to reform the way in which oil and gas produced in Indonesia will be allocated to the Indonesian market, in addition to seeking to increase Pertamina's role as producer upstream.

Indonesian law currently requires 25% of oil and gas produced domestically to be allocated to the Indonesian market. Under the new regime, it is proposed that a state-owned enterprise be appointed to act as "gas aggregator" (*badan usaha penyangga gas*). All of the gas required to meet Indonesia's domestic requirements would be sold by producers to the gas aggregator, which would determine the price at which gas would be sold to it and allocate gas purchased to different sectors based on a gas utilization priority structure set by regulation. It is not clear what the extent of the domestic sales requirements would be and whether the gas aggregator would have oversight over the terms on which Indonesian gas is exported. We understand that the gas aggregator may also be responsible for issuing licenses to conduct midstream activities such as transporting gas through pipelines. Regulations relating to the gas aggregator may be enacted separately to the new Oil and Gas Law.

Conclusion

There has been a significant amount of discussion around the reforms to the oil and gas laws under consideration by the Indonesian State. While the key drivers for these reforms and key initiatives are generally well understood, their detailed terms are still being developed. With respect to many of the reforms expected to be introduced by the new oil and gas laws, such as the reforms to the domestic market obligations, their detailed terms will need to be better understood for investors to fully assess their implications.



Mozambique's New Petroleum Legislation Completed: Toeing the Line in a Challenging Market

by John Inglis and Jean-Louis Neves Mandelli

In 2014, Mozambique reformed the legislation affecting the oil and gas sector by passing a new Petroleum Law (Law No. 21/2014 of 18 August) and a new Petroleum Tax Law (Law No. 27/2014 of 23 September). The impetus for these new laws was to increase Mozambique's share of benefits from its recently discovered vast hydrocarbon reserves, including in the Rovuma Basin.¹³ The details of many of the changes introduced by these new laws were to be set out in implementing regulations that were originally due to be enacted within 60 days of the passing of the new laws. However, they were only published at the end of 2015. In the interim, oil prices have fallen from approximately US\$100 per barrel to less than half that at approximately US\$40 today, significantly changing the dynamics of the oil and gas markets and the economic outlook for petroleum-producing countries.

The new regulations comprise: (a) the New Petroleum Tax Regulations (Decree No. 32/2015 of 31 December) and (b) the New Petroleum Regulations (Decree No. 33/2015 of 31 December). These new regulations replace the previous Petroleum Tax Regulations (Decree No. 4/2008 of 9 April) and Petroleum Regulations (Decree No. 24/2004 of 20 August).

In this article, we analyze the impact of the new regulations and their relationship to the Petroleum Law and Petroleum Tax Law, including in light of the changes in the oil and gas market since the enactment of these laws.

Scope of Application

The New Petroleum Regulations and New Petroleum Tax Laws apply to any undertaking conducting "petroleum operations" (as defined in the Petroleum Law). Neither of these regulations sets out how they are intended to apply to existing concessions. We assume that their application would be considered subject to the grandfathering provisions set out in the Petroleum Law and Petroleum Tax Law. Offshore Areas 1 and 4 in the Rovuma Basin that are currently under development and contain most of Mozambique's discovered non-associated gas reserves would not be affected by these new regulations, thanks to the grandfathering provisions included in the decree-law specific to those projects (Decree Law No. 2/2014 of 2 December).¹⁴

¹³ For further information, see our articles "Mozambique's New Petroleum Legislation: Are Investors Ready to Hit the Gas?," September 19, 2014, and "Mozambique's Decree Law: Worth the Wait," January 30, 2015, which can be made available on request.

¹⁴ For further information, see our article "Mozambique's Decree Law: Worth the Wait," January 30, 2015, which can be made available on request.

Purpose and Content

The new regulations generally follow the structure and content of the regulations they replace but include certain new provisions, mostly to reflect the additional requirements imposed under the Petroleum Law and Petroleum Tax Law.

A. New Petroleum Regulations

Domestic Petroleum Allocation

One of the key concerns arising from the Petroleum Law was the requirement that at least 25% of all oil and gas produced in Mozambique is to be allocated to the domestic market. It was hoped that the New Petroleum Regulations would clarify this allocation requirement, and in some respects they do. First, the amount to be allocated to domestic consumption is to be agreed upon as part of the development plan. This is helpful as it seems to allow more leeway to discuss how the 25% is calculated (e.g., whether net of royalties or not). All sales will be done through the Mozambican state-owned national oil company Empresa Nacional de Hidrocarbonetos (ENH), and while the terms of such sale will be set by the Government, they will be on “market terms.”

Listing on Stock Exchange

The Petroleum Law required all “oil and gas companies operating in Mozambique” to be listed on the Mozambican stock exchange. The New Petroleum Law clarifies that this listing is only required of the entities holding oil and gas concessions and must occur after the approval of any development plan in accordance with applicable law. We assume the applicable law in question is Law No. 15/2011 of 10 August (also known as the “PPP Law” or “Mega Projects Law”), which requires a listing of 5-20% of shares in the concessionaires. The timing of the listing is not very clear, but it would need to be done within five years of commercial operations, assuming existing legal requirements apply.

Clarification of Regime for Infrastructure Concessions

One of the key changes expected to be introduced by the Petroleum Law relates to the creation of a regime for concessions involving LNG projects and other upstream and midstream infrastructure, as only pipelines were provided for under the previous Petroleum Law of 2001. While the Petroleum Law introduced a concept of “infrastructure concession” to cover these types of assets, it failed to provide any details as to the terms of such concessions. Under the New Petroleum Regulations, however, infrastructure concessions can be granted for a maximum of 30 years and may be granted through a direct award. The application process and content requirements for infrastructure concessions are also detailed and are very similar to those applicable to pipeline concessions.

Under the Petroleum Law, holders of infrastructure (and pipeline) concessions are required to grant third parties access to their facilities. While this has been a requirement of Mozambican petroleum legislation since its inception, there were concerns as to its practical implications. The New Petroleum Regulations clarify that tariffs that would apply to third-party users should cover all costs plus a margin.

Local Content and Participation

As with the Petroleum Law, the changes introduced by the New Petroleum Regulations focus on increasing local content and the Mozambican state’s oversight over petroleum operations. The New Petroleum Regulations describe the obligations of foreign persons to associate themselves with Mozambican persons when supplying goods and/or services in Mozambique and to give preference to Mozambican goods and services that are set out in the Petroleum Law. Despite concerns raised

(and addressed in the Decree Law for Offshore Areas 1 and 4) with respect to the impact of these obligations on the availability of export credit agency financing, no exception is made for these under the New Petroleum Regulations. The New Petroleum Regulations also reflect the requirements imposed in the Petroleum Law as concerns the training and hiring of Mozambicans. However, no further information is provided as to the minimum terms of such local content efforts. These will need to be discussed and agreed under each concession. Helpfully, the Petroleum Law and New Petroleum Regulations do not change the rules applicable to the hiring of foreign nationals.

Natural Gas Resources

Unlike pre-existing legislation that was focused on oil extraction, the New Petroleum Regulations introduce specific provisions addressing the sale of associated and non-associated natural gas that concession holders are encouraged to pursue (although the terms of any such sale are subject to the approval of the Government). With respect to associated natural gas, under the New Petroleum Regulations, if concession holders elect not to sell associated natural gas, the Government may (without compensation to the concessionaire) collect such associated gas and sell it itself.

Alignment to Concession Practice

The New Petroleum Regulations codify certain terms typically included by the Mozambican government in its oil and gas concessions. These include: (a) the joint and several liability vis-a-vis the Mozambican government of concessionaires comprising more than one legal entity; (b) the creation of a decommissioning fund; and (c) the Mozambican government's right to require immediate transfer of the concession interests to it and without compensation in the event of concessionaire breach. The termination regime under the New Petroleum Regulations imposes specific—and quite short—cure periods and time limits to exercise termination and transfer rights. No provision is made for lender direct agreements. However, it should be possible to amend this regime in the specific concession contracts as, once approved and executed, these would typically prevail over conflicting regulations.

The New Petroleum Regulations also clarify that the responsibility for managing the concessions rests with the concessionaire (previously this was stated as being the responsibility of the operator) and provides Mozambique's National Petroleum Institute (Instituto Nacional de Petróleo) with day-to-day management responsibilities previously vested in the Ministry of Mineral Resources.

B. New Petroleum Tax Regulations

The Petroleum Tax Law included detailed provisions regarding the calculation and payment of taxes for undertakings in the petroleum sector. As a result, the New Petroleum Tax Regulations mostly reflect the terms of the Petroleum Tax Law. One notable clarification relates to the circumstances in which a lower petroleum production tax rate applies (50% of the headline rate). Under the New Petroleum Tax Regulations, this reduced rate would only apply to sales to ENH in fulfilment of the concessionaire's domestic petroleum sales obligations. The tax will be calculated on the revenues generated from sales to ENH.

Conclusion

The New Petroleum Regulations and New Petroleum Tax Regulations provide some helpful clarifications as to some of the new requirements introduced by the Petroleum Law and Petroleum Tax Law. As we understand that they will only apply to new petroleum concessions, they will be relevant to new investors in Mozambique or investors seeking to increase their

footprint in that jurisdiction. The Petroleum Law and Petroleum Tax Law were developed at a time of high oil and gas prices with a view to helping monetize and control these resources for Mozambique, often resulting in less favourable terms for investors. Due to current market conditions, new investor interest in Mozambique is likely to be more limited—as may have been evidenced by the fact investors only bid for eight of the 15 blocks tendered during Mozambique’s last licensing round in 2015. While the new regulations do not impose materially more stringent requirements than the laws they are implementing, they also do not purport to temper those new requirements to reflect less advantageous market conditions.



RTO Update: Panda Power Sues Ercot Over Capacity Forecasts

by Donna J. Bobbish and Jonathan Tompkins

In March, Panda Power Funds and certain of its subsidiaries (“Panda Power”) filed a lawsuit against the Electric Reliability Council of Texas, Inc. (“ERCOT”) in the District Court, Grayson County, Texas, 15th Judicial District. The lawsuit alleges that in 2011 and 2012, ERCOT committed negligent misrepresentation, fraud and breach of duty by sponsoring false and misleading market reports and other statements concerning the need for capacity in the ERCOT market that induced Panda Power to invest nearly \$2.2 billion in constructing new electricity-generating facilities.¹⁵

Panda Power invested in, financed and constructed three large-scale, natural gas-fueled electricity generation projects within the market operated by ERCOT. ERCOT is an independent system operator that administers an electricity transmission grid located solely within the state of Texas and not synchronously interconnected to the rest of the United States.

Panda Power contends that in 2011 and 2012, ERCOT issued a “false and misleading” report on Capacity, Demand and Reserves (“CDR”), which projected a serious and long-term scarcity of power supply in the market. The companies allege that these CDRs presented a picture of market conditions that ERCOT knew would lure investors, such as Panda Power, to construct generating facilities based on the belief that the price for power in such short supply would be high enough to cover the cost of construction without any need for a capacity payment. Panda Power further alleges that these CDRs, along with public statements by ERCOT officials supporting the CDR results, induced Panda Power to invest nearly \$2.2 billion to build three generating facilities in ERCOT — the Sherman Power Plant, the Temple I Power Plant and the Temple II Power Plant. But for ERCOT’s representations concerning the need for capacity in the market, Panda Power maintains it would not have invested in or built the three generating facilities.

Panda Power asserts that after its investments had closed and the generating facilities were substantially under construction, ERCOT published new CDRs showing a market having extreme overcapacity rather than a need for capacity. In addition, the companies allege that new information showed that ERCOT’s methodology and data used to prepare the 2011 and 2012 CDRs were “either seriously flawed or rigged.” As a result, the energy market reflected in the new CDRs depressed the market price for power both in the short and long term, making it more difficult to hedge against temporary market distortions through selling power into the ERCOT forward markets.

Based on these allegations, Panda Power claims that ERCOT negligently, as well as knowingly or recklessly, made or caused to be made false representations to induce Panda Power to invest and construct electricity-generating facilities in Texas, and further claims that ERCOT breached its fiduciary duty to Panda Power, causing substantial damages.

¹⁵ *Panda Power Generation Infrastructure Fund, LLC D/B/A Panda Power Funds, et al., v. ERCOT*, No. CV-16-0401.

Panda Power has requested a jury trial and seeks to recover, among other things, actual, consequential and incidental damages from ERCOT.

In order to prevail in its suit against ERCOT, Panda Power will need to demonstrate, among other things, that a fiduciary relationship existed between Panda Power and ERCOT and that it justifiably relied on any representations made by ERCOT. These will be fact-intensive inquiries.

In early April, ERCOT filed a motion to dismiss Panda Power's lawsuit, and in the alternative, a motion to transfer the case to Travis County, Texas, and an answer to Panda Power's lawsuit.

In its motion to dismiss, ERCOT argues that Panda Power's suit should be dismissed based on improper venue. Specifically, ERCOT argues that a forum-selection clause entered into by Panda Power mandates that any suit be filed in Travis County, Texas. In the alternative, ERCOT argues that Panda Power's case should be moved to Travis County, because none of the events or omissions that form the basis of Panda Power's claims occurred in Grayson County, Texas, and transferring venue to Travis County would be more convenient for the parties and witnesses.

ERCOT characterizes Panda Power's lawsuit as the result of having "gambled on future increased demand for power," having "apparently lost," and "regretting" its investment decisions.

In its answer to Panda Power's lawsuit, ERCOT raises a number of affirmative defenses, including that Panda Power's claims are barred by its failure to exhaust or utilize available administrative remedies, its own acts or omissions that caused or contributed to its purported injury, its failure to comply with applicable statutes of limitations, and its failure to mitigate any purported damage; as well as the express disclaimers contained in the CDRs that are the basis of Panda Power's claims; the doctrines of waiver and estoppel; and contractual damage waivers and limitations found in the agreements entered into between Panda Power and ERCOT. ERCOT further argues that Panda Power's claim for breach of fiduciary duty is not cognizable under Texas law and that Panda Power has not specified the maximum damages it seeks to recover from ERCOT.



Physical Protection Convention Amendment to Enter Into Force With Hopes It Will Prevent a Black Swan Nuclear Event

by Helen Cook

“There once was a time when the world thought that swans were only white. Then in 1697 the Dutch explorer, Willem de Vlaming, discovered black swans on the west coast of Australia. He took two specimens back to Europe and the zoology world said of course, it was obvious black swans would exist.”¹⁶

This was the opening section of Australian Foreign Minister Julie Bishop’s address to the 2014 Nuclear Security Summit in The Hague, The Netherlands.¹⁷ The Minister continued that today, “a black swan event is a metaphor for an event that is highly improbable, highly unlikely, highly unusual, and yet, should it occur, it may be said that in hindsight it may have been foreseen.” She said, “Our presence in The Hague should be seen in the context of a black swan event, a nuclear terrorist attack, that may be unlikely, improbable, unthinkable. However, we cannot allow a failure of imagination to ignore the possibility of such a catastrophic event.”

With the aim of preventing a nuclear security-related black swan event, global leaders met again in April 2016 in Washington D.C. for the final Nuclear Security Summit. Since US President Obama launched his nuclear security initiative in Prague in 2009, a multifaceted approach to global nuclear security issues has been pursued. One focus has been to strengthen the international legal basis for nuclear security, including achieving the entry into force of the Amendment to the Convention on the Physical Protection of Nuclear Material (CPPNM Amendment). At the end of the Nuclear Security Summit, it was announced that this objective has been fulfilled, and the CPPNM Amendment will enter into force for all contracting states within a few months.

The Convention on the Physical Protection of Nuclear Material (CPPNM) was signed in 1980 and, in 2005, a Diplomatic Conference was held to strengthen the CPPNM. The result was the CPPNM Amendment. However, ratification of the CPPNM Amendment by two-thirds of the contracting parties to the CPPNM was required to bring the CPPNM Amendment into force. Prior to the Nuclear Security Summit, the White House said that over 80 countries had ratified the CPPNM since 2009. On April 1, 2016, it was announced that as a result of 10 new ratifications in the lead-up to and during the final

¹⁶ Australia’s Foreign Minister’s address to the 2014 Nuclear Security Summit in The Hague, The Netherlands. Available at: http://foreignminister.gov.au/speeches/Pages/2014/jb_sp_140325.aspx?w=tb1CaGpkPX%2FISoK%2Bg9ZKEg%3D%3D

¹⁷ Available at: http://foreignminister.gov.au/speeches/Pages/2014/jb_sp_140325.aspx?w=tb1CaGpkPX%2FISoK%2Bg9ZKEg%3D%3D

Nuclear Security Summit, the CPPNM Amendment reached the 102 ratifications needed to bring it into force.¹⁸ The CPPNM will enter into force on May 8, 2016.

Together with the International Convention on Suppression of Acts of Nuclear Terrorism and certain UN Security Council resolutions, the CPPNM and CPPNM Amendment contain the primary international obligations in the area of nuclear security. The CPPNM, as amended, is intended “to achieve and maintain worldwide effective physical protection of nuclear material used for peaceful purposes and of nuclear facilities used for peaceful purposes; to prevent and combat offences relating to such material and facilities worldwide; as well as to facilitate co-operation among States Parties to those ends.”¹⁹ The scope of the CPPNM is restricted to nuclear material used for peaceful purposes while in international nuclear transport,²⁰ while the CPPNM Amendment expands the application of the CPPNM to nuclear facilities and material in peaceful domestic use, storage and transport.²¹ Together, the CPPNM and CPPNM Amendment require contracting parties to:²²

- **Physical protection regime:** Establish, implement and maintain an appropriate physical protection regime applicable to nuclear material and nuclear facilities under its jurisdiction, with the aim of protecting against theft, ensuring measures are in place to locate any missing or stolen nuclear material, protect nuclear material and facilities against sabotage and mitigate any radiological consequences of sabotage. This commitment includes establishing a legal and regulatory framework to govern physical protection and requires application of specific levels of physical protection (with such levels being set out in Annexes I and II). In implementing these obligations, contracting parties are to apply, if reasonable and practicable, a set of “Fundamental Principles of Physical Protection of Nuclear Material and Nuclear Facilities.” These “Fundamental Principles” are introduced via the CPPNM Amendment and include principles relating to the responsibilities of the State and the license holders, security culture, defense in depth, quality assurance and confidentiality.²³
- **Import and export assurances:** Undertake not to export or import nuclear materials or to allow transit through their territories of such materials unless they have received assurances that these materials will be protected during international transport in accordance with the levels of protection determined by the Convention.
- **Criminalize acts:** Criminalize specified acts, including unlawful possession or transport of nuclear material, theft, using or threatening to use nuclear material to cause harm and interfering with operations of nuclear facilities with the intent to cause harm. Each contracting party is to establish jurisdiction over these offences in the following circumstances (i) where the offence is committed in its territory or on board a ship or aircraft registered in the state; (ii) where the alleged offender is a national of the state; (iii) where the alleged offender is present in its territory and is not extradited; or (iv) when the state is involved in international nuclear transport as the exporting or importing state (optional).

¹⁸ In 2016, 10 States ratified the 2005 Amendment to the CPPNM allowing it to reach the required two-thirds necessary to enter into force: Azerbaijan (Mar 31), Cameroon (Apr 1), Côte d'Ivoire (Feb 10), Kuwait (Apr 1), Marshal Islands (Mar 30), Montenegro (Apr 1), New Zealand (Mar 18), Pakistan (Mar 24), Paraguay (Mar 11) and Serbia (Mar 30).

¹⁹ Article 1.A, Unofficial English version of the text of the Convention on the Physical Protection of Nuclear Material, adopted on 26 October 1979, reflecting the Amendment adopted by the States Parties to the Convention on 8 July 2005, produced by the IAEA.

²⁰ Article 2.1, CPPNM.

²¹ Article 3, CPPNM Unofficial Consolidated Text produced by the IAEA, available at: <https://ola.iaea.org/ola/documents/ACPPNM/Unofficial-consolidated-text-English.pdf>

²² Article 2A, CPPNM Consolidated Text.

²³ Article 2A.3, CPPNM Consolidated Text.

- ***Prosecution and extradition:*** Prosecute or extradite those accused of committing such acts. Importantly, the offences listed in the CPPNM, as amended, will be deemed to be included as extraditable offences in any extradition treaty existing between contracting parties. The CPPNM Amendment strengthens the extradition provision by stating that none of the offences are regarded as a political offence and, as such, a request for extradition cannot be refused solely on the grounds that it concerns a political offence.²⁴

In 2009 in Prague, President Obama classified the risk of nuclear terrorism, however unlikely to occur, as the most immediate and extreme threat to global security. Upon entry into force of the CPPNM Amendment, international nuclear security obligations will be further strengthened, with hopes they will aid in the prevention of a nuclear security-related “black swan event.”

²⁴CPPNM Amendment para.10, inserting a new art.11A.



Dispute Resolution Trends: Salient Developments and Opportunities (Part 1 of 2)

By Nils Eliasson, Mark S. McNeill and Robert L. Nelson, Jr.

Given turbulent times in world energy markets, companies look for ways to protect themselves against unwelcome surprises and to give themselves an edge over the competition. The ability to prevent disputes from arising, and turn them to your advantage when they do, can be critical. However, important considerations for achieving these goals, and key methods for meeting them, are often neglected. Relevant points to consider in energy projects and transactions include the following:

Project Construction Phase: Nip Problems in the Bud Through Multi-Tier Dispute Resolution Provisions That Deploy Dispute Review Boards (DRBs) or Dispute Adjudication Boards (DABs)

Too often, minor disputes in the field mount up, with snowballing effects as small problems turn into large ones. Critical path schedules and owner-contractor relations can be disrupted as tempers fray and work goes undone: the bridge between issues in the field and formal disputes at the arbitration table becomes all too easy to cross.

Experience in recent years suggests that new ways of approaching construction issues in the field can go a long way toward reducing the number, and harmful effects, of field construction disputes. In particular, the use of standing DRBs (which issue recommendations as to how incipient disputes should be resolved) or DABs (which render binding decisions about incipient disputes and which decisions may be appealable in arbitration for matters involving amounts above a certain monetary threshold) in projects can ward off many issues and ensure that others are resolved to mutual satisfaction before they cause appreciable cost or schedule effects.

Typically, for both DRBs and DABs, the parties select a neutral expert prior to the commencement of a project to serve as an on-call third party when minor disputes arise. For large, complex projects, the expert may be full-time on site; multiple experts may also be engaged, particularly where various types of experience and expertise would prove helpful (additional experts may be party-nominated, but must be impartial). The empowered neutral(s) are then provided with background information about the project, and periodic updates and reports, to ensure that they maintain keen awareness of project nature and progress. As issues emerge that the parties cannot resolve quickly among themselves, the parties engage the dispute board to render its opinion on a “real-time” basis. A DRB decision represents a recommendation to the parties; a DAB decision binds them. However, the technical difference between DRBs and DABs often proves illusory, as experience suggests that the parties typically adopt decisions by either entity. Quick resolution of disputes also keeps owner and contractor positions from hardening, thereby ensuring that the parties maintain a generally constructive working relationship – which in turn can reduce the incidence of further disputes arising.

Major procurers of construction services often find DRBs/DABs invaluable. For example, dispute resolution procedures enabled the massive CERN particle accelerator project to save substantial time and money in the construction process, including through the avoidance of ripple effects that otherwise would have resulted from small, lingering problems

disrupting critical path schedules. CERN constituted a panel of five experts (based on its own research and feedback received from potential contractors during the bidding process) authorized to hear disputes between or among CERN, the contractor(s) and the independent engineer. The panel's decision bound the parties until the conclusion of the construction process, at which point a party could, if still aggrieved, invoke arbitration.

Many governmental authorities and other project sponsors require the use of DRBs/DABs in significant projects. Use of DRBs/DABs also facilitates financing: diminished concerns about potential cost and delay issues mitigate project risk profiles for lenders. Thus, the relevant question for dispute boards becomes not whether to use them, but how they can best be crafted to work optimally for you.

Complex Transactions: Ensuring Integrated and Consistent Dispute Resolution

A variety of issues can arise in the implementation of complex transactions, affecting various stakeholders in a number of different ways. Not infrequently, however, parties learn to their chagrin that dispute resolution procedures that were drafted late in the negotiation process and implemented inconsistently across various documents result in diffuse and uncoordinated dispute control mechanisms that also pose the risk of yielding inconsistent results in proceedings related to the same set of core facts. For example, improper coordination of dispute control mechanisms between a guaranty and the contract(s) containing the guaranteed obligations can lead to the guarantor being found liable in one proceeding while its subsidiary defeats the relevant contention in a separate proceeding (this being an unfortunate real-life situation involving a major company).

Thus, careful thought needs to be given as to how best to coordinate dispute resolution proceedings in a complex, multi-stakeholder transaction. A standard dispute resolution clause – often involving multi-stage proceedings starting with negotiations by senior corporate officials, followed by mediation/conciliation, with arbitration as the final stage – provides a solid foundation, but may not adequately address all coordination issues that can arise in a multi-contract/multi-party setting. Unfortunately, however, the dispute resolution clauses in many transactions never proceed beyond this necessary, but often insufficient, stage. In a complex multi-contract/multi-party transaction or project, disputes can arise among different parties under different agreements, even though the core facts and legal issues may be common to those disputes. Without streamlined dispute resolution clauses across all relevant transaction documents that include provisions to address these overlapping issues in a meaningful and expeditious way, various proceedings can be launched and prosecuted in an inefficient and costly manner, all the time posing tactical and strategic challenges relating to inconsistent results. These problems can be obviated, if not eliminated, through the employment of contractual dispute resolution provisions that empower, or even direct, arbitral tribunals to consolidate the hearing of any two or more parallel arbitrations arising under any of the transaction documents involving any such common issues of law or fact. Similarly, it may sometimes be desirable to include provisions that empower an arbitral tribunal to join additional parties to the transaction documents to a pending arbitration even though such party was not originally named a party to the proceedings.

In this regard, parties drafting dispute resolution clauses often overlook the fact that the arbitration rules of most arbitration institutions (including frequently used rules such as the ICC rules, the LCIA rules, and the UNCITRAL rules) do not contain comprehensive provisions on consolidation and joinder. Parties that wish to ensure that related parallel arbitration between different parties arising under different transaction documents can be consolidated, or that additional parties may be joined even though they are not parties to the agreement that gave rise to the primary dispute, therefore must add express provisions on consolidation and joinder to their contractual dispute resolution clauses. One notable exception involves the Hong Kong

International Arbitration Centre (HKIAC), whose Administered Arbitration Rules include comprehensive provisions on consolidation and joinder that obviate the need for including equivalent procedures in the contractual dispute resolution clause.

Providing mechanisms for efficient and rational treatment of complex, overlapping issues in advance yields successful results far more often than trying to accomplish this after disputes have already arisen and parties are already at loggerheads. The presence of clear procedures can also ward off potential gamesmanship by parties seeking to exploit differences between different agreements and parties involved in the transaction. Energy-related disputes can be difficult enough without their being aggravated by – rather than having their solution facilitated by – dispute resolution clauses.

Cross-Border Transactions: Consider Potential Treaty Applicability and Provisions, and Avail Yourself of Opportunities Presented

Over the last decade, disputes under bilateral investment treaties, regional trade and investment agreements like the North American Free Trade Agreement (NAFTA), and specialized treaties like the Energy Charter Treaty (to which the EU, most European countries, and some Central Asian and Asian countries (like Japan) have become parties) have proliferated, and the amounts involved have soared. In a recent Energy Charter Treaty arbitration proceeding involving former Yukos shareholders and the Russian Federation, for example, Shearman & Sterling partners Emmanuel Gaillard and Yas Banifatemi helped the claimants win the largest arbitration award in history by a factor of twenty: over \$50 billion. In cross-border transactions, energy companies typically give considerable attention to tax strategies, and to ensuring that they design project ownership structures to implement those tax strategies properly. Until recently, however, ensuring that project ownership structures took proper advantage of treaty-related opportunities on the investment front received much less attention. Given the uncertain levels of legal and investment regime stability and neutrality in many countries where significant energy and natural resource opportunities are located, as well as issues that can arise even in countries with much more sophisticated governmental and legal frameworks (the recent solar project experience in Spain and the phase-out of nuclear power in Germany come to mind), companies need to devote considerably more time and attention to examining the opportunities, and issues, posed by investment treaties that may be relevant to their contemplated projects and transactions, including structuring their investments in a way that ensures investment treaty protection, as well as seeing how those treaties can be employed once disputes have arisen.

In the next article, we will turn to additional salient opportunities for energy industry stakeholders, as well as other dispute resolution issues that merit their attention and awareness.



US Efforts to Meet Paris Climate Agreement Obligations and Their Impact on Future Sources of Domestic Energy Production

By Jason Pratt

The United States and China Commit to Signing the Paris Agreement

UN Secretary General Ban Ki-moon is hosting a Paris Agreement signing ceremony at the UN headquarters in New York on April 22, 2016. It is anticipated that up to 130 countries will sign the agreement that day. If 130 countries do sign the agreement on April 22, 2016, it will represent the highest number of countries that have signed an international treaty in a single day (in 1994, 119 countries signed the Law of the Sea Treaty in a single day).

Critically for the prospects of the Paris Agreement coming into effect, the United States and China issued a joint presidential statement on March 31, 2016, confirming that both countries will sign the agreement at the April 22, 2016 signing ceremony. The United States and China were two of 195 countries that approved the agreement at the Paris summit (also known as COP21) on December 12, 2015. The agreement will not become binding unless and until it is adopted by 55 countries that, in the aggregate, account for at least 55 percent of greenhouse gas emissions. The ratification process formally begins in April 2017, one year after the April 22, 2016 signing ceremony. China and the United States are the largest and second largest emitters of greenhouse gases.

For the United States, the agreement is not a treaty, and therefore will not have to be ratified by the US Senate. The pertinent provisions of the agreement will become effective within the existing United Nations Framework Convention on Climate Change, a treaty which was ratified by the Senate in 1992.

Once in effect, the United States and other participating countries will be required to establish greenhouse gas reduction commitments and to submit new commitments every five years. The goal, as announced at COP21, is to ensure that the ongoing warming of the planet stays “well below” 2 degrees Celsius above pre-industrial global temperatures, and to “pursue efforts” to limit the temperature increase to 1.5 degrees Celsius.

The agreement does not specify the methods of emission-reduction that countries must implement – this is left up to each participating country.

The US Supreme Court Stays Implementation of the Clean Power Plan

Assuming the Paris Agreement goes into effect, the ability of the United States to meet its obligations might pivot on how the US Environmental Protection Agency’s (“EPA”) Clean Power Plan fairs in the courts. The Clean Power Plan, President Obama’s signature initiative to control greenhouse gas emissions under the US Clean Air Act, established standards to limit the emission of carbon dioxide pollution from existing power plants. The plan promulgated interim and final statewide goals

for carbon-dioxide emission reductions. Under the plan, states would be required to submit implementation plans by 2018 and show carbon dioxide emission reductions by 2022.

The Clean Power Plan suffered a setback, although potentially only a temporary one, when on February 9, 2016 the US Supreme Court voted five to four to stay its implementation pending the resolution of challenges to the plan in the D.C. Circuit Court of Appeals. At least five separate stay applications had been lodged by dozens of states and various affected industry groups prior to the Supreme Court's issuance of the stay.

As a practical matter, the issuance of the stay will preclude the EPA from taking actions to enforce or implement the plan pending resolution of the challenge. Most likely, power plants will now refrain from making expensive investments in carbon-emission control efforts until the legality of the plan is decided in court. The D.C. Circuit has scheduled oral arguments for June 2, 2016, and a decision would most likely come in the Fall of 2016 or later.

A writ of certiorari petition could follow the D.C. Circuit ruling, placing the ultimate fate of the Clean Power Plan back in the US Supreme Court. In considering this scenario, it is potentially significant that the five-judge majority that voted in favor of the stay included the late Justice Antonin Scalia. Justice Scalia died on February 13, 2016, four days after issuance of the stay. If a new Justice is not seated when the Clean Power Plan comes before the Supreme Court, and the remaining eight justices split the vote four-four, whatever the D.C. Circuit rules will be automatically upheld.

If a new Justice is seated, then he or she might break a tie between the four conservative Justices and four liberal Justices. Merrick Garland, President Obama's nominee to fill Justice Scalia's seat, has in past rulings evinced an inclination to defer to federal agencies, including the EPA. For instance, in April 2014 he was part of the D.C. Circuit majority that upheld the EPA's Mercury and Air Toxics Standards rule that limited mercury emissions from power plants.

The Clean Power Plan is the first initiative to limit heat-trapping gas emissions from existing power plants. Notably, the stay will not affect the EPA's regulations that limit carbon emissions from new or modified fossil fuel-fired power plants.

Other Federal Developments

The fate of the Clean Power Plan is likely the most significant factor that will impact both US efforts to comply with the Paris Agreement and the United States' future energy-generation mix – what percentage of energy generation will be fired by coal and oil, and what percentage will be fired by natural gas or nuclear fuel, or will otherwise be derived from renewable sources such as wind and solar. That said, there are other Federal initiatives that will likely impact these issues. As of this update, many of the initiatives tend to favor natural gas, nuclear and renewables over coal and oil.

On the renewables front, in December 2015 Congress extended the production tax credit and the investment tax credit that incentivize the development and production of wind and solar energy. One initial estimate by Bloomberg New Energy Finance suggested that the net result of the extensions could be to spur on \$73 billion in new investments and to provide access to renewable energy to more than eight million additional households.

In March 2016, the US Department of the Interior's ("DOI") Bureau of Ocean Energy Management announced that Trident Winds LLC is qualified to develop its proposed 800-megawatt wind farm, and that going forward DOI would ascertain whether other companies were interested in the subject lease area. The Trident proposal calls for 100 floating turbines. If DOI determines other companies are interested, it will initiate a competitive bidding process. The lease area is located approximately 33 nautical miles northwest of Morro Bay, California. The project, if followed through to completion, would be the first offshore wind project in California. The DOI has also awarded 11 wind energy leases in federal waters off the

Atlantic Coast. The first wind farm in federal water, located off the coast of Rhode Island, is expected to be completed in 2017.

Also in March 2016, the US Bureau of Indian Affairs released a final Environmental Impact Statement (“EIS”) for a proposed 100-megawatt solar energy plant. The plan, proposed by the Moapa Band of the Paiutes, would be located on the tribe’s reservation near Las Vegas, Nevada. The EIS addressed the consequences of the project’s construction and operation on soil, water resources, air quality and wildlife in the vicinity of the reservation. The tribe would lease the land to First Solar. It is anticipated that construction would take 12 to 15 months, and First Solar would operate the plant for 30 years with a possible 10-year renewal.

Just as there are Federal initiatives that tend to incentivize and green light renewable projects, other Federal developments would appear to hamper more greenhouse-gas intensive energy production, in particular energy derived from coal. For example, in January 2016 the Secretary of the DOI announced a three-year moratorium on coal leases on federal land while it reviews the federal coal program. The review will include an evaluation of the royalties it charges and the program’s impact on global warming. Given that approximately 40 percent of United States coal is mined on federal land, this development will likely put upward pressure on the cost of coal just as the price of natural gas, a chief competitor, remains at historically low levels.

With respect to methane regulations, new Federal initiatives will likely increase costs for extracting both oil and natural gas. Methane is a potent greenhouse gas; it remains in the atmosphere for a shorter time than carbon dioxide, but traps a proportionately greater amount of heat. In March 2016, the US EPA announced it would develop rules to reduce methane emissions from existing oil and gas infrastructure. As a first step, the EPA will issue a formal Information Collection Request to enable it to gather information regarding the hundreds of thousands of existing sources, including information relating to reduction technologies and their costs and feasibility. The Obama administration intends to reduce methane emissions from the oil and gas sector by 40 to 45 percent from 2012 levels by 2025. The US EPA’s new methane initiative is mirrored by similar Canadian initiatives.

State Developments

Apart from Federal initiatives, States continue to propose and implement measures that affect the economic prospects of various energy sources, including passing laws that limit or eliminate their utilities from obtaining electricity from coal-fired power sources and that expand their Renewable Portfolio Standards, or RPSs. For instance, in March 2016 Governor Kate Brown of Oregon signed a law that, starting in 2030, bars coal-fired generation plants from contributing electricity to the State’s two major utilities. Under the law, the phase out of coal-fired power would be complete by 2035. The law also increases the scope of the State’s RPSs. The RPSs had directed State utilities to obtain at least 25 percent of their electricity from renewable sources by 2025; the law increases this percentage to 50 percent by 2040.

The Oregon law could lead to intra-State litigation, pitting states such as Oregon that wish to eliminate coal-fired power from their energy mix against states such as Kentucky that are more reliant upon and committed to coal mining and coal-fired energy production. Opponents of efforts to regulate or eliminate obtaining power from coal-fired plants, including those in other States, argue that such efforts violate the Commerce Clause of the US Constitution preventing a State from unduly regulating commerce with a sister State.

Both proponents and opponents of the Oregon law are following a dispute between Minnesota and North Dakota that is currently being contested in the Eighth Circuit Court of Appeals. Minnesota in effect bars new coal-fired plants from

supplying electricity to its utilities; the Minnesota law mandates that new power plants that produce 50 or more megawatts of electricity and increase carbon dioxide emissions are barred from supplying the State electricity. Much of Minnesota's power has traditionally been generated in coal-rich North Dakota. Minnesota lost round one; a US District Judge ruled that Minnesota's law directly regulated commerce with North Dakota in violation of the Commerce Clause. Minnesota has appealed to the Eighth Circuit.

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