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Offshore wind – a rise in disputes in an industry at the crossroads

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Ambitious targets for the development of offshore wind have locked horns with global inflation and other adverse events, leaving stakeholders at risk of a range of potential disputes.

Offshore wind is an industry at the crossroads. Recent welcome developments include the Biden administration's action plan and the EU's pledge to further increase its support for the industry. But although the industry is central to energy transition and decarbonisation efforts by States (*e.g.*, the Ostend Declaration in the EU and the Advancing Offshore Wind Energy strategy in the United States) it also faces tight deployment timelines and deteriorating market conditions, putting a strain on stakeholders and making disputes more likely.

This article explores recent developments and identifies the most acute dispute risks for stakeholders.

1 DISPUTE RISKS IN OFFSHORE WIND PROJECTS

Building, operating, and integrating offshore wind projects in the current energy system requires extensive cooperation between stakeholders. Ambitious targets mean accelerating deployment – and achieving this in the face of spiking energy prices, global cost inflation, heavy reliance on imported raw materials, and already low margins for suppliers is likely to stretch all stakeholders, increasing the likelihood of disputes.

1.1 Construction and engineering disputes

Developing and constructing offshore wind farms entails substantial risk of dispute, since such projects:

- require new technology (increasing the risks of design errors impeding performance);
- take place in a difficult environment (at sea both the weather and the nature of the seabed are unpredictable);
- involve complex maritime logistics (*e.g.*, availability of offshore vessels);
- involve disaggregated procurement featuring multiple contracts with different equipment manufacturers (generating interface risks such as knock-on delays and inconsistencies in liability and warranty provisions); and
- must be completed within a short deadline to meet ambitious capacity targets.

Potential areas of dispute include claims for additional compensation and extension of time for alleged variations of the works, but also disputes over responsibility for design defects or defective performance.

1.2 Supply chain disputes

In 2022, the following factors led most major wind turbine manufacturers outside China to operate at a loss:

- **Cost inflation of raw materials**: Since early 2020, the prices of key raw materials used in the manufacturing of offshore wind turbines and balance of plant ("**BoP**") components (*e.g.*, foundations, array and export cables and substations) have significantly increased.
- **R&D race:** Designing ever larger wind turbines in an already strained economic environment may have triggered quality issues, since mechanical breakdowns, component failures and serial defects seem to be on the rise.
- **Rise in shipping costs:** The impact of Covid on the shipping industry and a surge in container demand has led to a substantial increase in shipping costs since 2020 – exacerbated by the war in Ukraine.

All this has seriously affected the profit margins of wind equipment manufacturers, while they are being asked to rapidly expand manufacturing capacities across the supply chain to reach ambitious development targets –without any dip in quality. This makes the likelihood of disputes over delays or defects in the delivery of wind turbines and BoP components, or requests for price review by manufacturers (either under their relevant agreements or pursuant to statutory law), more probable.

1.3 Disputes relating to power offtake agreements

The current economic climate is also affecting offshore wind developers themselves since recent cost inflation has seriously reduced the expected profitability (or even called into question the economic viability) of several projects for which power purchase agreements ("**PPAs**") or Contracts for Difference ("**CfDs**") were entered into prior to the recent spike in electricity prices.

In the last few months, major wind developers terminated their power offtake agreements, or respectively sought revision thereof. Others suspended works on projects in development or indicated that they would consider abandoning projects for which no final investment decision has yet been made.

If price volatility persists, this may trigger further disputes as wind developers attempt to renegotiate, adapt, or terminate power offtake agreements, relying on various legal doctrines depending on their specific agreements and the applicable law (*e.g.*, hardship, *clausula rebus sic stantibus*, force majeure, frustration).

1.4 Regulatory disputes

States have designed various incentive schemes to promote offshore wind: the United States offers fixed levels of subsidy, mainly in the form of production tax credits or investment tax credits, whereas EU States grant aid through competitive auctions in which wind developers vie to offer the lowest subsidy required to initiate the project (to comply with strict EU state aid rules).

If States amend or retract these incentives in the current context of rising global supply costs, offshore wind developers may reconsider certain projects in development, refuse bidding for new projects or, in the worst-case scenario, raise claims against such States, including under bilateral investment treaties (if and when possible).

Developers recently warned European countries that "negative" bidding – in which developers receive no subsidies and instead pay the State for the right to build an offshore wind farm – will likely generate additional costs that will have to be borne by suppliers and/or final consumers in the form of lower prices for components and/or higher electricity prices.

1.5 Disputes during the operational phase

Dispute risks persist even after an offshore wind farm has become operational. Developers generally enter into operation and maintenance ("**O&M**") agreements and while these often include availability warranties, various long-term factors outside the O&M contractor's control can affect a wind farm's overall availability (*e.g.*, the development of adjacent structures or actual average wind speeds being less important than initially anticipated). Since there may be multiple O&M agreements (*e.g.*, for wind turbines, substations and foundations), coordination between the various O&M contractors is of critical importance.

2 INTERNATIONAL ARBITRATION

International arbitration is particularly suitable for adjudicating potential disputes in the industry since it caters to both the features and characteristics of offshore wind projects and the types of disputes that may arise:

1. Parties to construction, engineering, supply and O&M contracts are often based in different jurisdictions.
2. Projects are capital-intensive, long-term and complex ventures in which disputes can arise at any stage – from initial concept to decommissioning.
3. Technical disputes involving performance and engineering issues, as well as pricing disputes relating to price review claims, require extensive expert evidence.
4. A variety of actors (*e.g.*, turbine and BoP suppliers, installation vessels, wind developers, grid operators) and contracts, as well as disaggregated procurement (often leading to joinder and consolidation of claims), are involved.

If States are to reach their ambitious targets for energy transition by 2050, offshore wind projects cannot grind to a halt because of ongoing legal disputes. International arbitration has stepped up with recent procedural features adopted by prominent arbitral institutions – including expedited proceedings and the new SCC Express Dispute Assessment – which may prove useful tools in the disputes arsenal.

For further questions or comments about this topic, please contact the author.