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# Offshore wind projects with Chinese suppliers: Topics you should think about

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# Navigating the Offshore Wind Industry

## Suppliers and contractors from China: The panacea for the capacity problems and price increases in the European offshore wind market?

The European offshore wind nations – similar to many other nations worldwide – have very recently increased their offshore wind development targets drastically, from the at least 60 GW goal as set out in the EU Offshore Renewable Energy Strategy back in November 2020[1] to an overall goal of installing about 111 GW of offshore renewable generation capacity by 2030.[2]

One of the main bottlenecks for achieving these targets is the limited capacity of the supply chain and of the vessels and further marine spread required. Another issue developers are being confronted with are prices which have risen, coupled with a significant "deflation" of risk appetite on the contractors' side. These are all consequences of the disruptions of the last years, but also of the general movement towards a contractors' market.

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1 "Boosting Offshore Renewable Energy for a Climate Neutral Europe", European Commission, 29 November 2020, accessed at Boosting Offshore Renewable Energy (europa.eu).

2 "Member States agree new ambition for expanding offshore renewable energy", Directorate-General for Energy of the European Commission, 19 January 2023, accessed at Member States agree new ambition for expanding offshore renewable energy (europa.eu).

At the same time, almost decoupled from the international offshore wind industry and development, China has been developing a massive offshore wind supply chain over the last years and has been breaking records with the speed and volume of offshore wind capacity added in its waters. Capacity-wise it is by far the leading nation. In 2022, China reached a total installed capacity of 31.44 GW, which almost equalizes that in the entire rest of the world, which was at 32.86 GW.[3]

As a consequence, international developers are increasingly looking towards China and its huge offshore wind supply chain as a means to still secure required supplies and equipment at reasonable conditions. The offshore wind farm ("**OWF**") Taranto, as developed by Renexia, for example showcases MySE 3.0-135 wind turbines from MingYang Smart Energy. Other European projects which source out to China-based contractors include the 500 MW Greater Gabbard (with ZPMC as supplier) and Moray East in the UK (with CSSC CWHI supplying steel for the jackets and transition pieces flanges). Dajin Heavy Industry is supplying to the 850 MW Moray West by Ocean Winds' (monopiles and transition pieces), RWE's 1 GW Thor in Denmark (monopiles), Ocean Winds' 496 MW Iles D'Yeu et Noirmontier (monopiles), SSE Renewables, Equinor, and Vårgrønn's 3.5 GW Dogger Bank in the North Sea (tower barrels), among others.

However, contracting with Chinese suppliers and contractors still causes a certain, often undefined feeling of uneasiness among many sponsors and financiers. In this publication, after a brief market overview, we will be setting out what the issues and topics are that need to be looked at, when contracting with parties from China, and how to overcome or mitigate relevant risks involved.

Please be aware that these general considerations are not meant to replace or make redundant project specific legal advice.

[3] Cf. Jun Wei and Aldo Boni De Nobili, "China", in Christian Knütel and Anna Leah Tabios Hillebrecht (eds), Offshore Wind Worldwide, Regulatory Framework in Selected Countries (4th ed., 2023), 40, 41 (with further references).

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# 1. Market Overview

The following graphs depict the operational and under-construction Chinese offshore wind capacity in key countries as of the year 2022.

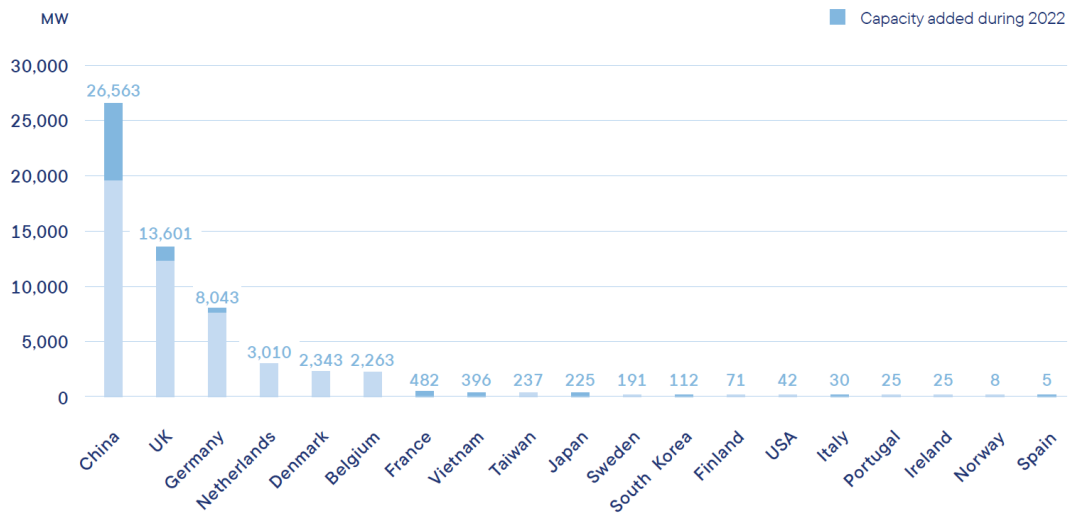


**Figure 1 – Global offshore wind capacity in operation – by country[4]**

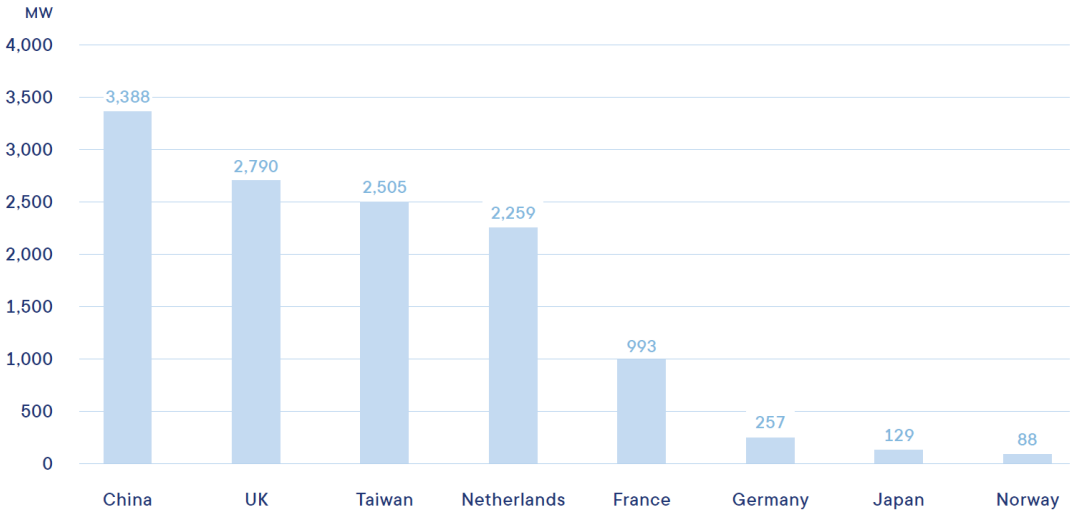


**Figure 2 – Global offshore wind capacity under construction by 2022[5]**

4 "Global Offshore Wind Report 2022", World Forum Offshore Wind (February 2023), p. 7.
5 "Global Offshore Wind Report 2022", World Forum Offshore Wind (February 2023), p. 8.

## 2. Enforcement in China and Arbitration

Offshore wind contracts are very often negotiated heavily, and at length. However, also an offshore wind contract is only worth the paper it is written on if it can be enforced against the respective other party. If not, such party might not feel sufficiently incentivized to indeed comply with the terms agreed.

When one contracts with a counterparty based in China that person will therefore need to consider if and how one can ultimately enforce a decision under the respective contract against such party, should this ever be required.

In offshore wind procurement and transport and installation ("**T&I**") contracts parties almost always agree on arbitration as means of ultimate dispute resolution, as opposed to state court litigation. This approach is of particular importance when contracting with Chinese counterparties.

A Chinese court will only enforce a foreign court judgment if there is reciprocity or if there is a bilateral or multilateral treaty on the enforcement of court judgements in place. Both is typically not the case between e.g., EU countries on one and China on the other side.

As a consequence, there is no reasonable alternative to arbitration. China is party to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards from 1958 (the "**NY Convention**"). Arbitration is preferred by investors, typically in the form of arbitration in Singapore under the rules of the Singapore International Arbitration Centre (SIAC) or in Hong Kong under the auspices of the Hong Kong International Arbitration Centre (HKIAC).

Based on the NY Convention, Chinese courts must, as a matter of principle, help enforcing foreign (final) arbitral awards. Foreign tribunal's decisions on interim measures are not recognizable or enforceable because they are not considered as final and conclusive awards

(other than interim measures ordered by tribunals seated in Hong Kong, see below). Still, under the NY Convention, enforcement is generally subject to certain defences and exceptions, including the "public policy" exception. China has tended to use such exception quite sparingly in recent years. According to public sources, from 2012 to 2022, over 90% of the foreign arbitration awards brought before the Chinese courts were finally recognized and enforced, with more than half of which being settled within one year.[6] This is also because the Supreme People's Court consent is required for a local court to refuse to enforce a foreign arbitration award under the New York Convention.

Upon China's resumption of sovereignty over Hong Kong, the New York Convention became inapplicable between Hong Kong and (Mainland) China. To fill this gap, Hong Kong and China entered into an arrangement allowing the mutual enforcement of arbitral awards in June 1999, implemented since 1 February 2000. Additionally, in 2019, Hong Kong and China reached an agreement wherein Chinese courts would grant interim measures in support of arbitration seated in Hong Kong (making Hong Kong the first and only jurisdiction outside China with such an agreement). Accordingly, parties to arbitral proceedings administered by certain eligible arbitral institutions set up or established in Hong Kong will be in a position to apply to the Chinese courts for interim measures before the arbitral award is issued. This agreement might provide a boost for Hong Kong in its attractiveness as an arbitral seat when compared with other seats in Asia such as Singapore for transactions involving Chinese entities.

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[6] Cf. an article by Sam (Ronghui) Li, Michael (Haomin) Zhang, Lucas (Zhouquan) Lu, Tina (Yanfei) Qian, Zhong Lun Law Firm (Shanghai Office), 12 September, 2023, quoted from Kluwer arbitration blog (https://arbitrationblog.kluwerarbitration.com/2023/09/12/recognition-and-enforcement-of-foreign-arbitral-awards-in-china-between-2012-2022-review-and-remarks-part-i/).

## 3. EU trade policy and economic sanctions

Sanctions can include restrictions on trade in goods and services, restrictions on engaging in commercial activities, targeted financial sanctions (including asset freezes) on designated persons and entities or travel bans on certain persons. Sanctions have become an important and widely used tool to change a political behaviour of states, companies, and persons.

In an offshore wind context, it cannot be ruled out that China or relevant Chinese suppliers or contractors become the object of trade or financial sanctions with the effect that it becomes forbidden to contract with Chinese suppliers in general or certain suppliers in particular, or to continue performance under an existing contract.

However, the actual risk of this happening and causing issues specifically in an offshore wind supply context appears to be limited.

To date, relevant Chinese OWF suppliers or contractors are not targeted or captured by any relevant US or EU sanctions.

The EU does not currently maintain a sanctions regime against China, though it has designated a number of Chinese persons and entities under its Global Human Rights regime in relation to the persecution of ethnic minority. Additionally, certain restrictions imposed through its sanctions against Russia may affect trade with China or certain Chinese entities. Additionally, the EU has imposed an import ban on Russian iron and steel products, which extends to third country iron and steel products that are manufactured from restricted Russian iron and steel.

It is difficult to predict though what type of US or European sanctions against China or a Chinese act of aggression against Taiwan could trigger. Given the substantial impact of any ban of Chinese products on the US and EU economy the risk of a general ban on Chinese products appears to be low, but ultimately impacts on offshore wind related products and the ability to pay for such products cannot be ruled out, in particular if the Chinese counter parties are ultimately state owned.

It is therefore prudent to exercise caution, especially in relation to state-owned entities which could face higher risk and implement a proactive approach to compliance.

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*"Even with topics that occur at short notice, Hogan Lovells makes support possible at any time."*

Chambers Europe, 2023

## 4. Intellectual property (IP) issues

While in recent years Chinese suppliers have become increasingly present in renewable energy markets outside of China, intellectual property ("**IP**") issues concerning products supplied by Chinese companies have attracted increasing attention.

Renewable energy equipment has to implement current state of the art technology and needs to comply with current grid requirements. Numerous technologies used in wind turbines, wind farms, converters and other equipment and utilities required for the installation and operation of offshore wind utilities are protected by IP rights, most importantly patents.

The current IP landscape poses several challenges to Chinese suppliers of renewable energy equipment, the most important being:

The supplied products must not violate the IP (patent) rights of competitors in Europe.

In addition, the supplied products must not violate IP (patent) rights of competitors that are validated in China or the respective home of the supplier.

Chinese manufacturers currently have fewer and less important IP rights in their technologies, which gives them a weaker position to negotiate license agreements with their US-based or European-based competitors.

All of these challenges pose a potential threat to the supply of renewable energy equipment from Chinese suppliers.

The most imminent challenge is to avoid any violation of IP rights of competitors which are valid in Europe. As relatively new players in the European market, it is particularly challenging for Chinese suppliers to identify all potentially relevant IP rights of competitors and to implement a proper patent monitoring, which are effective tools to mitigate infringement risks.

If IP rights are infringed by the products of Chinese suppliers, this may result in a suspension of the supply or even mean that operation of the supplied equipment or even the wind farm has to be stopped. In addition, also the European operator of the equipment may be liable for compensation payments to the IP owner. The recently established European Unified Patent Court (UPC) makes enforcement of patents across several countries even more efficient and faster, including in the coastal waters and in the Exclusive Economic Zone (EEZ).

In addition, competitors may also own IP rights in China. In our experience, Chinese courts have displayed a readiness and expedited process in enforcing IP rights against Chinese suppliers.

In the global wind power patent applications, Chinese manufacturers find themselves in a position that lacks competitive advantage. In particular, many EU based competitors have a significant portfolio of IP rights that is tailored to European requirements which gives them a strong enforcement position. This disparity between China-based manufacturers and their EU counterparts remains substantial and make it challenging for China-based suppliers to negotiate necessary IP licenses.

Given this context, EU project developers need to allocate specific focus to the verification of intellectual property rights held by Chinese suppliers to proactively mitigate potential IP disputes. It is imperative to conduct a comprehensive assessment of licensing prerequisites as well.

The IP challenges faced by Chinese suppliers operating within the EU underscores the urgency for robust cross-border cooperation. As economic ties between China and the EU continue to evolve, stakeholders must collaboratively strive to strike a balance that fosters innovation, safeguards IP rights, and nurtures a conducive environment for sustainable business growth. By addressing these challenges proactively and collaboratively, both regions stand to unlock the potential of a more secure and mutually beneficial trade landscape.

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## 5. Product safety and compliance

Relevant offshore wind farm components and their constituent parts need to comply with European product safety and product compliance laws. In particular, manufacturers need to conform with the so-called CE framework, i.e., the need to successfully complete the applicable CE conformity assessment procedure, need to draw up the respective documentation and issue a (signed) CE declaration of conformity, explicitly stating that the relevant product indeed complies with the applicable CE laws, especially with the respective essential product safety requirements. For WTGs, such requirements typically include those under the Machinery Directive (MD), the Electromagnetic Compatibility (EMC) Directive, and the Radio Equipment Directive (RED) (including planned updates such as the forthcoming new Machinery Directive), as well as technical standards (e.g., on functional safety and EMC).

Depending on permitting and certification requirements in the relevant jurisdiction, CE violations can have severe consequences and can, in the worst case, lead operations not being permitted, WTG recalls, work accidents with criminal exposure, etc.

The product safety requirements apply to produces and offshore wind farm components irrespective of where they are produced or sourced from, including to components sources from China. And insofar no particularities apply in relation to Chinese products as opposed to European products. However, since at this moment in an offshore wind context Chinese end products are not being sourced on a regular basis or in notable volumes, there is a certain risk that such products do actually not comply in all aspects with the applicable requirements. This applies in particular to WTGs, electrical equipment used on offshore substations, etc., but less to products such as sea cables, towers, or foundations.

In relation to such critical components, developers and project owners will need to apply a thorough diligence and ensure that also from a contractual perspective product safety compliance is properly dealt with, including consequences of non-compliance.

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*"Under enormous time pressure the team is always fully on top of the topics and gives best advice on how to continue and finalise a deal."*

Chambers Europe, 2023

## 6. Anti-dumping

In the EU, anti-dumping measures constitute a vital trade policy tool aimed at addressing unfair trade practices and protecting domestic industries from the detrimental effects of dumped imports. Dumping occurs when foreign (i.e., non-EU) producers export goods to the EU market at prices lower than their production costs or below the selling prices in their home markets, creating an uneven playing field and potentially causing harm to European industries. To counteract injurious dumping, the EU can impose anti-dumping duties, usually for a period of 5 years. The duties are paid by the EU importer. In an offshore wind farm context, this would be the buyer of the relevant component such as the developer or project company buying foundations or wind turbines.

The European Commission will initiate an anti-dumping investigation after having a received a complaint from the EU industry with prima facie evidence of dumped imports resulting in injury to the domestic industry. However, the European Commission can also initiate an investigation ex office, irrespective of a complaint.

These investigations involve a thorough examination of factors such as sales, pricing, production costs, and market dynamics. If the European Commission finds that imports were dumped causing injury to the EU industry, it will impose anti-dumping duties, effectively raising import prices to a fair level and restoring fair competition in the market.

The imposition of anti-dumping duties significantly increases costs as the anti-dumping duties must be borne by the EU importer. It is not possible to contractually agree that e.g., the foreign supplier pays the anti-dumping duty. Such practice is referred to as "absorption" of the anti-dumping duty, which would likely lead to a re-opening of the investigation resulting in a higher duty.

Generally, anti-dumping measures do not apply retroactively, though in certain exceptional circumstances the European Commission may impose anti-dumping measures retroactively (for a limited time period of no longer than 90 days during an ongoing investigation).

To mitigate risks associated with Chinese suppliers, we recommend carefully evaluating offers from Chinese suppliers that are significantly lower than EU market prices. Additionally, the TARIC database provides an overview of possible duties applicable to goods when imported from China (on the basis of CN codes). Initiation of anti-dumping investigations are published in the Official Journal and the European Commission maintains a database with information on past and ongoing investigations.

When dealing with Chinese suppliers, it is prudent to consider including a contractual clause allowing for unilateral termination of the contract if anti-dumping duties are imposed in relation to the Chinese supplier.

To our knowledge, there is only one EU anti-dumping measures currently in force that is potentially relevant for offshore wind projects. These are anti-dumping measures on imports of steel wind towers from China (Commission Implementing Regulation (EU) 2021/2239 of 15 December 2021). Definitive anti-dumping duties have been imposed in relation to Penglai Dajin Offshore Heavy Industries, ranging from 7.2 to 19.2%.

However, recently Brussels had been considering whether to investigate China's use of subsidies to promote the country's wind turbine manufacturers. But according to subsequent press releases this investigation did not proceed due to lack of "very clear evidence" of unfair practices.[7]

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[7] https://www.reuters.com/business/energy/eu-not-ready-formal-probe-into-chinas-wind-industry-source-2023-10-24/.

## 7. Cabotage

Cabotage laws are rules that restrict foreign-flagged vessels from engaging in domestic shipping (e.g., "Jones Act" in the US). As such, cabotage laws are only relevant if Chinese transport and installation (T&I) contractors or vessels were to be engaged with the transport and installation of EU offshore wind farm (OWF) projects.

The extent of the ban on Chinese T&I vessels to operate within a country and its territorial waters or in the EEZ is different in each country and will need to be investigated for each country separately.

In Germany, the *Verordnung über die Küstenschifffahrt* (KüSchV) applies, which provide that in coastal waters the ban applies, while none applies in the EEZ.

The EU cabotage liberalization (Regulation 3577/92) only applies to EU flagged vessels.

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*"[Christian Knütel] absolute specialist for offshore wind farm development", client*

JUVE handbook, 2023/2024

## 8. Supply chain act (*Lieferkettengesetz*)

In Germany, the German Supply Chain Act (*Lieferkettengesetz - LkSG*) requires companies to actively monitor and mitigate human rights and environmental risks within their respective supply chains.

This obligation is not exclusive to Germany; rather, it aligns with an international trend, evident through legislations such as the UK's Modern Slavery Act, California's Transparency in the Supply Chain Act, the 'conflict minerals' provisions in section 1502 of the US Dodd-Frank Act, and the broader context of National Action Plans focusing on Business and Human Rights. However, the LkSG follows a more comprehensive approach in contrast to most of the other legislation.

As of 2023, the LkSG applies to companies (legal entities) headquartered or having branches in Germany with a workforce of at least 3,000 employees in Germany. From 2024 onward, this employee threshold will be lowered, extending the Act's coverage to companies with a minimum of 1,000 employees in Germany.

The entire process of the supply chain is covered in the law's scope of application, spanning from the extraction of raw materials to the distribution of the final product to the end costumer. The obligations for supply chain due diligence are staggered, covering the company's own business area, its direct suppliers, and – to a limited extent – even the indirect suppliers.

The LkSG offers robust safeguards against both environmental and human rights concerns. On the environmental front, it addresses issues such as soil, air, and water contamination, excessive water usage that adversely affect human well-being, the use of mercury and specific chemicals, as well as the import and export of hazardous waste. Regarding human rights, the Act guards against unfair wages, forced labor, child labor, infringement upon labor rights and freedom of association, unequal treatment under labor laws, forced eviction, land expropriation ("land grabbing") affecting livelihoods, and the utilization of security forces in business operations.

In cases where due diligence and reporting obligations are not met, fines ranging up to EUR 8 million can be imposed, depending on the severity and nature of the violation. For companies with an annual turnover surpassing 400 million EUR, fines can reach up to 2% of the average global yearly turnover of the economic entity (i.e., group).

Undertaking a risk analysis as key due diligence of various obligation involves identifying, assessing, documenting, and reporting potential risks and – considering the risks identified – implement preventive and/or remedial measures as warranted. Continuous updates to the risk analysis are required. The law emphasizes conducting risk analyses in an "appropriate" manner, allowing companies a degree of flexibility in their approach. The choice of specific methods is left to the discretion of each company. The risk analysis extends to the company's own business area, direct suppliers, and, when substantiated knowledge dictates, even indirect suppliers.

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## 9. ESG in general

There are no Chinese-specific environmental, social, and governance ("**ESG**") supply chain requirements. Nevertheless, a lot of related scrutiny are to be expected from lenders.

Traditional ESG requirements do apply to the "on the ground" impact of the project itself and less to supply chain issues. Chinese supply chains, however, need to be able to demonstrate the ability to satisfy (or cause the developer to satisfy) Western ESG standards and laws.

Hence, supply chain legislation in the wider sense, as set out above, is probably the most relevant to scenarios involving China-based suppliers. This is so, as lenders and advisers typically consider supply chain risk as part of their wider commercial and technical due diligence. Thus, this may very well include KYC checks in case of Chinese suppliers.

Suppliers, operators, and developers alike do need to consider that certain risk of ESG topics is being (mis)used to discriminate in global West vs. East trade issues.

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*“Very experienced and capable team, very knowledgeable.”*

*“Very good cooperation; pragmatic approach to solutions.”*

Legal 500, 2021 - 2023

## 10. Cybersecurity

In today's digital world, cyberattacks rank as the most important risk for companies, regardless of size or industry. Lack of or insufficient protection against cyberattacks has led to a number of serious incidents in the recent past, resulting not only in significant financial and reputational damage, but also potential liability of both, the company and management. However, in particular operators of critical infrastructures – including energy producers and network operators – are currently being put to test, as threats are manifold.

Following the increasing risk, operators of critical infrastructure are also facing increasingly stringent regulatory requirements in the area of cybersecurity. While the EU's first Network and Information Security Directive (2016/1148, also known as "NIS") introduced common minimum standards already in 2016, many Member States have established new and stricter requirements in recent years. Responding to the growing threats, the EU's second Network and Information Security Directive (2022/2555 – NIS2) is further strengthening security requirements and in particular addressing the security of supply chains. It is accompanied by the Critical Entities Resilience Directive (2022/2557 – CER), which focuses on physical measures to increase resilience. While Member States have to transpose both Directives into national law by October 2024, operators must provide for adequate cybersecurity standards to both prevent and react on incidents. Furthermore, operators must comply with information obligations as well as reporting, certification and audit requirements.

In addition, some Member States, such as Germany, have introduced legislation which stipulates special security requirements for critical components, i.e. certain crucially important IT products used in critical infrastructures. The use of such components requires a notification and may even be prohibited if necessary to protect the national public order or security. In Germany, however, applicable provisions of the Act on the Federal Office for Information Security (BSI Act – BSIG) and the Energy Industry Act (EnWG) provide that critical components need to be explicitly determined as such which only has been done for certain IT products for 5G networks to date.

*"Hogan Lovells always gets in the details of the project structure and helps with complex issues during the processes."*

Chambers Europe, 2023

While none of the above regulation is specific to China, special attention is required in the context of increasing calls for EU self-sufficiency and decoupling. The use of Chinese IT products could have an impact on audits or certifications of cybersecurity measures. There is also a risk of a broader application of the present legislation as well as additional restrictions on critical components, in particular with respect to products supplied by companies that are controlled by foreign governments.

Companies should therefore take a pro-active approach to cybersecurity compliance and carefully monitor legal developments and authority guidelines. Particular focus should be given to equipment for which a malfunction could have a material impact not only on individual turbines, but on the wind farm or the secure grid operation as a whole.

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