



PORTUGUESE SOLAR ENERGY

Regulatory and market outlook

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MACEDO VITORINO & ASSOCIADOS
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Contents

1. Foreword
2. Updated licensing procedures
3. The first solar energy auction
4. The future of solar auctions

Foreword

After mini-hydro and wind, photovoltaic solar energy could become the third wave of the renewable energy revolution in Portugal. By 2030, the power output promises to grow up to 6.6 GW using this technology.

Portugal has been one of the most enthusiastic countries regarding renewable energies. In 2016, 28,1% of the energy produced was by renewable sources, compared to 19,2% in 2004.

This is the eighth highest percentage among European countries and the fifth highest in the Eurozone. Portugal's target for 2020 is set at 31%.

Portugal has a strong solar energy potential, boosting an annual average of 2,200 to 3,000 hours of sun in the mainland, making it the European country with the highest average of hours of sun exposure.

Today, the solar power output in Portugal is of 1.006 GWh. The Amareleja solar plant with its 46MW and annual production of 93 GW is the largest in Portugal.

In 2017, renewable sources represented 41% of the electricity generated in Portugal. Still, more than 30% of the renewable quota was achieved by the electricity generated by large-scale hydro power plants. Solar energy remains very far from what it could potentially be.

The Portuguese Government has, early in 2017, suspended the licensing of any new feed-in tariff photovoltaic plants.

The political motive was not increasing the electricity invoice paid by consumers, but the argument passed to the market players was that the market already offered adequate conditions for the deployment of new projects without a feed-in tariff due to the continuing solar panels' cost reduction.

The lack of stability on promoters' remuneration led to the tightening of the financing conditions and to several licensed projects never being built or operated. The lack of grid capacity has been another challenge to the growth of the Portuguese photovoltaics.

Aiming at solving these challenges, in 2019 the Portuguese government made several modifications on the licensing photovoltaics power plants and changed significantly the solar production ecosystem.

Updated licensing procedures

From 1988 to 2006, under the Old Renewables Law (Decree-Law 189/88, of 27 May 1988) and the Old Renewables Access Law (Decree-Law 312/2001, of 10 September 2001) the licensing procedures for renewable energy power generation were only dependent on the verification of technical requirements following a promoters' request for a grid connection point.

Power generation based on renewable energy is nowadays a strongly regulated activity: initially by Decree-Law 172/2006 ("**Renewables Law**") in its first configuration and, more recently, as amended by Decree-law n.º 76/2019, of June 3, 2019 ("**Auctions Law**"). The Auction Law sets a licensing procedure for the installation and operation of renewable energy facilities divided in four stages:

- Obtaining a title that grants grid capacity ("**Capacity Reservation Title**");
- Obtaining a production license;
- Obtaining an installation authorisation; and
- Obtaining an operation license.

The promotor may obtain a Capacity Reservation Title using one of three of the following methods:

- directly by a grid operator (EDP Distribuição or REN), when there is capacity available and technical conditions are met;
- by entering an agreement with the grid operator, if the promotor agrees with supporting the costs of the grid capacity expansion, or
- by winning an auction organized by the Portuguese government energy office, *Direção Geral da Energia e Geologia* ("DGEG"), for this purpose.

The production license is granted by DGEG, after analysis of the environmental requirements and technical aspects of the project of the power plant, among other elements. The authorization to install the facility is granted by the Ministry of Economy, for facilities whose capacity exceeds 10 MW, or by DGEG, for facilities with capacity up to 10 MW. The operation license is issued after a final inspection conducted by DGEG, serving the purpose of guaranteeing the verification of all technical and safety standards. In addition to these, promoters must obtain a construction permit from the municipality where the solar plant is to be installed as well as a license from the grid operator.

The first solar energy auction rules

The Portuguese Governments announced two auctions per year. Besides a capacity reservation title, these auctions may grant a guaranteed tariff.

The first auction for solar promoters took place in July of 2019 ("First Auction") and it was divided into three different stages: i) eligibility stage, ii) bidding stage and iii) allocation stage. It is likely that the core of future auctions will not change drastically.

In the eligibility stage, the promoters need to provide several information related with their identification and of their projects. Among other duties, the promoters need to reveal a non-binding original intention for acquisition bid (*intenções iniciais de aquisição*) and pay the deposit set in the program of the auction. The bidding stage is the core of the auction, where promoters will present their bid in order to obtain the Grid Title. The bids are made through an online platform, anonymously, through various and successive rounds, using the Japanese method.

In the First Auction, the bids were expressed using a Net Present Value ("NPV").

The calculation of the NPV was dependent of the revenue scheme in which the promoters are interested (either guaranteed revenue or market scheme):

- To calculate the NPV using the guaranteed revenue, the key factor is the discount offered by each promotor to the fixed tariff, previously indicated by the auction jury.
- To calculate the NPV using the market scheme, the key factor is the yearly amount that the promoter is available to pay to the system, as a contribution.

These two methods of remuneration competed among themselves for the same capacity, using different formulas to assess the NPV. The bids were very competitive amongst the investors in the First Auction.

The promoters awarded with the reservation title must comply with several deadlines regarding the remaining steps of the licensing procedure (for example, obtain the land rights for the project's location in 6 months and the production license in 18 months).

In two years, the awarded projects must be ready to operate and those who fail to reach this stage in that period will lose the bond paid to DGEG.

The future of solar auctions

The Auction Law and subsequent launching of auctions for the allocation of grid capacity agitated the Portuguese solar market, which has been dormant until 2019.

In the July First Auction, over 50 eligible promoters applied for 24 different points of connection to the grid, most of them in the range of 10 to 20 MWh. These numbers illustrate the renewed interest in the Portuguese market. The results of this auction also show the promoters' preference for the guaranteed remuneration: 15 out of 24 (equivalent to 75% of the MWs) made their bids using this scheme. The average guaranteed remuneration tariff was 22,22 € p/MWh, while on the market scheme the average tariff to be paid to the electric system is 18.36€ p/MWh.

The profile of this First Auction and its auction rules caught many small promoters by surprise. Some saw their licensing procedure terminated by DGEG as the grid connection capacity they were expecting for their projects was put into auction by DGEG. Those able to participate in the First Auction, were "forced" (after waiting for a production license for years) to offer tariffs as low as 14 euros per MWh and had to restart the licensing procedure under the new Auction Law.

Although they will most likely not repeat in future auctions, where tariffs offered are expected to be closer to the market price of energy, the First Auction's quite surprising tariffs negatively affected the interest of foreign bigger players looking at the Portuguese solar market and were detrimental to the implementation of a "culture of Power Purchase Agreements", non-existent today, as in most cases promoters have chosen a guaranteed remuneration.

Nevertheless, auctions are here to stay and will remain a corner stone of the Portuguese government solar policy. On the positive side, we can say that auctions will allow promoters to obtain the grid capacity before making strong investments in the licensing procedures and land rights. Likewise, the return of the guaranteed remuneration (provided that the tariff is not too low) may give smaller players on accessing to credit, due to economic stability it confers to projects over the years.

In next year's first quarter, the first of two new auctions said to be scheduled for 2020 will confirm or not the Portuguese government belief that auctions will definitively put Portugal in the investors' map. Ultimately, this will depend on the tariffs that will be awarded to the winning bids and on the length of grid capacity that is offered.



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João de Macedo Vitorino
jvitorino@macedovitorino.com

Rua do Alecrim 26E | 1200-018 Lisboa | Portugal
Tel.: (351)21 324 19 00 | Fax: (351)21 324 19 29
www.macedovitorino.com