Energy

2019

Seventh Edition

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glg global legal group

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Portugal

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Overview of the current energy mix, and the place in the market of different energy sources

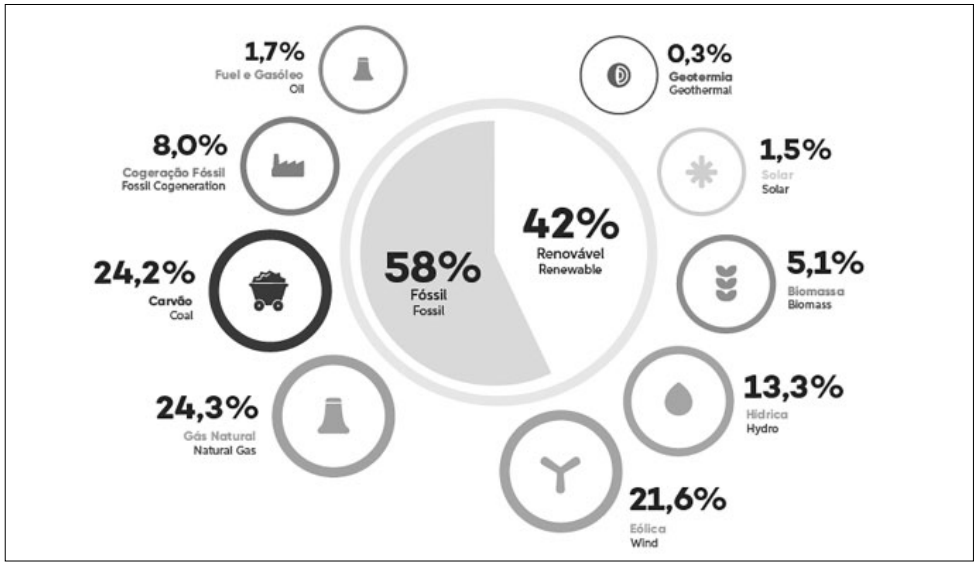
Portugal's dependence on imported energy has been historically high, since the country does not produce oil or natural gas. However, due to an increasing amount of renewable energy in the generation mix, total energy dependence has been declining.

In 2017, energy was produced from biomass (5.1%), hydro (13.3%), wind (21.6%), solar (1.5%) and geothermal (0.3%). Wind and hydro power have been the main drivers in growing energy production in Portugal. Solar power is expected to be the main driver in the future.

National production decreased (54.52 TWh) compared to 2016. The main reason was that 2017 was characterised by a lack of precipitation. The hydrological index was 0.47 (the historical average being 1), which means that the production of electricity from hydro power steeply reduced. Additionally, the wind index decreased by 0.03%.

However, the export balance was one of the best ever (since 1999) with a significant value of 2.684 GWh (only surpassed in 2016 – 5.082GWh).

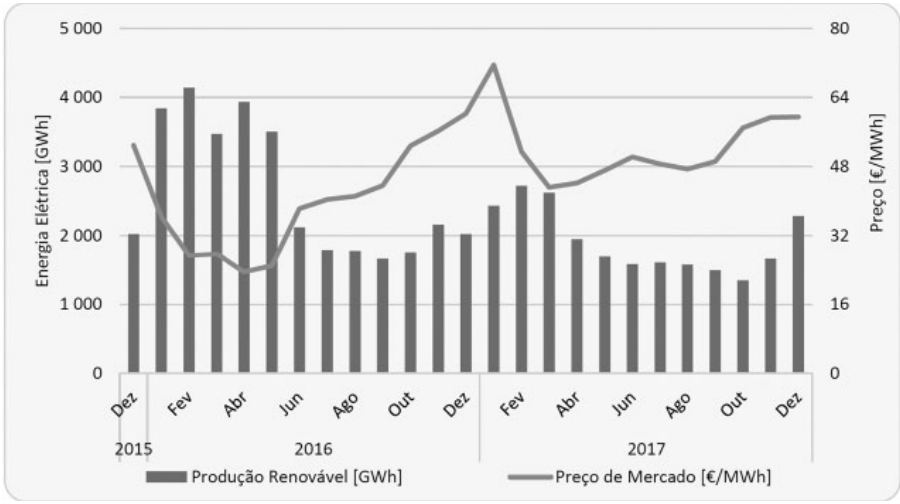
Production of electricity by source 2017[1]



The low representation of renewable sources resulted in an increase in the average annual price of electricity in the wholesale market, which was €52.45/MWh (in 2016, according

to the Portuguese Renewable Energy Association, it was €39.4/MWh). Still, Portugal recorded 122 non-consecutive hours on 100% renewable electricity energy sources.

Correlation between renewable energy generation (*produção renovável*) and market price (*preço de mercado*), December 2015 to December 2017

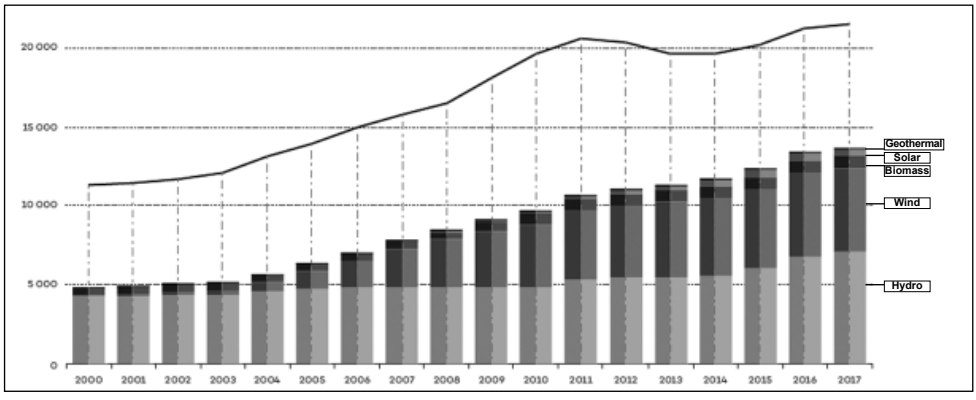


Source: OMIE, REN; Analysis APREN

Installed power in the national electricity system continued to grow. Since 2000, installed power increased from 3.9 GW to 13.7 GW, with average growth of 8% per year. The increase in renewable power was especially noticeable between 2004 and 2011, with the commencement of operations of several wind farms. Since 2011, fossil power capacity has been declining in turn.

Among the new power plants entering into operation in 2017 were: the Foz Tua hydroelectric plant (263 MW); the Pico Alto geothermal power plant (4.5 MW); and large-scale photovoltaic solar power plants (14 MW), in addition to several PV units covered by the self-consumption schemes (UPAC and UPP). On the other hand, the remaining renewable technologies, biomass and wind, have remained practically stagnant.

Evolution of the installed capacity (MW) of the different sources of electricity generation in Portugal between 2000 and 2017



Source DGEG; APREN's analysis

Changes in the energy situation in the last 12 months which are likely to have an impact on future direction or policy

Solar energy projects have increased in the past year, with a significant increase in capacity-licensing requests. Many investors continue looking to this sector despite there being no applicable feed-in tariff or other subsidies.

This is happening despite the implementation of some measures by the current Government which assumed, as a priority, a reduction of the electricity price and the tariff deficit and the burdens of future costs overruns. These measures have included:

- termination of the concession contracts for exploration, research, development and production of oil in the Algarve's offshore areas;
- revision of the power guarantee mechanism (a new scheme, not yet implemented since it awaits a decision from the European Commission regarding State aid) on availability of services;
- a return to the National Electric System of alleged "excessive" amounts received due to the accumulation of feed-in-tariffs and public support funds (determined by Ministerial Order 69/2017 which has not yet materialised);
- revocation of a legal provision which allowed the change of the source of primary energy for generating centres to which the former law was applied;
- limitation of authorisation of over-equipment of power plants to a consultation of the Regulator on the impact on the National Electric System termination of the exemption of excise duty on coal-fired power plants, plus payment of an additional rate over CO2 emissions (starting from 10% up to 100% in 2022); and
- transference of responsibility for payment of social tariff for the supply of natural gas to network operators and suppliers.

These measures notwithstanding, the government is also committed to de-carbonising the economy. The growth of solar capacity is in line with this target.

Micro-generation (self-consumption and small production units) is another area where some developments have occurred, with different schemes being implemented.

Developments in government policy/strategy/approach

Boom in solar photovoltaic projects

Portugal is witnessing a proliferation of new renewable energy projects, sourced by solar photovoltaic energy. This is together with the promotion of lithium concessions, and measures to reduce energy prices and the tariff deficit, the main vector of this Government's current energy policy.

Many solar photovoltaic plants are being licensed, some of which are already at the construction stage. It is expected that, by 2021, Portugal will grow from the current 572 MW of installed capacity of this energy source to around 1,600 MW, with more than 30 power plants being built.

These projects will be enabled by power purchase or similar agreements freely negotiated with energy traders and suppliers, pursuant to which generators put their electricity at the disposal of a buyer which will then resell it (or sell it on behalf of the generator) in organised markets (notably, in the spot market) or by bilateral agreements. Generators will receive a price per MWh agreed with these buyers.

These projects represent a turning point from the old paradigm of the remuneration of renewable energy projects through feed-in-tariffs set by law or regulation.

Electro-mobility and rush to lithium concessions

Portugal has been active in promoting investment in the electro-mobility sector. A legal framework is in force and a network of charging points of electric vehicles is in place and expanding. At the same time, the Government has also been encouraging the renewal of the fleet of vehicles of the Public Administration by gradually replacing conventional cars with electric vehicles.

In the year 2018, the Government approved the acquisition of 200 more electric vehicles by the Public Administration and the installation of more 250 charging points.

At the same time, Portugal is witnessing a lithium rush, given the growing utilisation of this mineral for the production of batteries used in electric vehicles and in electricity storage. Several companies (mostly multinational companies) have been requesting rights for the research and exploration of lithium. In the period ranging from 2016 until now, more than 30 requests were made for the granting of research and exploration rights of mineral deposits including lithium, in the North and Centre of Portugal.

Due to this volume of requests, the Government has already announced that it will launch public tenders for the granting of rights to research and explore lithium, likely until the end of 2018. However, complementary legislation on these tenders is still awaiting approval.

Developments in legislation or regulation

Regime of prevention of market distortions

In 2013, a legal framework was created with a view to eliminating windfall profits received by Portuguese generators due to the taxes then approved in Spain and which elevated wholesale electricity prices in the Iberian market.

Portugal would afterwards approve its own taxation measures to electricity generators, but would determine that the impact of such measures should be offset against the impact of Spanish measures when measuring windfall profits to be eliminated.

In the second semester of 2017, the current Government has, however, declared this offsetting to be illegal, due to allegedly exempting generators from the cost of Portuguese taxation measures (notably the extraordinary contribution to the energy sector and the burden of social tariffs, which is supported by these generators).

Annulment of possibility of modification of primary energy source of RES

In 2015, the Government approved a regime which allowed for promoters of renewable energy power plants, the installation of which was rendered impossible by reasons not attributable to the promoter, to request the modification of the primary energy source of their installation.

This regime was approved by the previous Government and was seen as a way to allow producers to whom the State had given – through public tender – rights to install mini hydro power plants against the payment of a fee and who, for reasons beyond their control, could not obtain all necessary licences for such installation, to have another way of installing such power (shifting e.g. to solar power, and still receiving a feed-in-tariff, although with a discount to previously set feed-in-tariffs), and for the State to avoid having to return the fees paid.

This regime was frowned upon by the current Government, as it would enable solar photovoltaic power plants receiving feed-in-tariffs at the same time that many solar

photovoltaic projects are being licensed in a market-price regime, and two different remuneration schemes would then coexist at the same time.

In this context, the current Government decided on 31 August 2017 to declare such regime illegal, due to allegedly violating legal principles, such as principles of legality and competition, due to allowing the installation of a different power plant (of a different primary source) than that which was awarded by the public tender. This prevented procedures of shifting of primary sources of licences being successfully concluded.

Attribution of production licences for the generation of electricity from renewable sources

The Ministerial Order no. 62/2018 of March 2, following Law no. 114/2017 of December 29, established that licences for the production of electricity from renewable sources (notably, solar) shall be assigned through a draw when there are applicants whose requests, globally, exceed the injection capacity in the relevant network area.

A first draw was organised and launched by the General Directorate for Energy and Geology (DGEG), the state department responsible for the energy sector, in April 2018. Meanwhile, through Decree-Law no. 57-A/2018, of 13 July, the competence to organise the draw was transferred to the Energy Services Regulatory Entity, which was also bestowed with the power to issue a binding opinion as to the grid connection of new power plants.

The issuance of a production licence or acceptance of prior communication shall be immediate and automatic after the draw, up to the limit of the capacity available in the network zone or set of network areas.

New rules for the licensing of electrical networks

Since 2010, the approval of a regime establishing the maximum levels of human exposure to electromagnetic fields was foreseen in law. However, the complementary decree-law was never approved by the Government.

On 4 May, through Law no. 20/2018, the Assembly of the Republic commissioned the Government to approve legislation establishing these limits to human exposure to electromagnetic fields, applicable to high- and very-high-voltage networks and installations, in a six-month term. Such limits shall be defined in line with the guidelines of the World Health Organization and best practices of the European Union.

The establishing of these limits shall abide by the principle of precaution, avoiding, beyond any doubt, the causing of risks to human health. Also, when minimum distances of electrical networks to households and other buildings cannot be ensured, the possibility of installation thereof underground shall be considered.

This new regime also requires municipalities to issue an opinion as to the network layout before the project is approved.

Social tariff of supply of natural gas

Together with the liberalisation of the natural gas market in Portugal, a social tariff was created in 2011 with a view to providing a discount to the final price of natural gas for supply to especially vulnerable consumers. This discount, which is currently set to 31.2% of the total grid access tariffs paid by these consumers, was hitherto financed by all the clients of natural gas, in the proportion of their consumed energy.

The State Budget Law for 2018 transferred the burden of financing this social tariff to the companies engaged in transportation activity and suppliers of natural gas, in the proportion of the gas delivered the previous year.

Due to poor wording of the law, it is not clear if the reference to the transportation activity only includes the activity of exploitation of transmission networks. According to an opinion of the Advisory Council of the Republic's General Attorney's Office, this burden shall be considered to have been imposed not only on the transmission network operator but also on distribution grid operators, also construed to be encompassed by the concept of "*transportation*" in a broad sense.

Postponement of power guarantee auctions

A power guarantee legal scheme exists in Portugal in order to ensure security of supply in the electricity sector. This scheme aims to do this by ensuring, through payments to the mostly backup electricity generators (or aggregators of generators), such as coal or gas-fired stations, that they are permanently available to commence producing when there is a reduction of renewable energy production, creating the risk of supply not being able to meet demand. As Portugal relies a lot on hydro and wind energy production, which is weather-dependent and volatile, this scheme is a way to eliminate this dependence and volatility.

In 2017, this scheme was amended so as to include an auction mechanism to select chosen generators, in order for the remuneration of the availability service to reflect the market value of this service. An auction was launched for the year 2017.

However, for the year 2018, the Government decided to postpone the auction to select the providers of the power guarantee until the European Commission confirms the compatibility of this mechanism – which was already approved by the Government in 2017 – and for which state-aid provides.

Protection of consumers – new rules for gas bottles

The current Government has been trying to promote competition and transparency in the oil products sector, in order to protect consumers. New measures were taken this year regarding gas bottles.

According to Decree-Law no. 5/2018, of 2 February, new rules were approved for selling, collecting and exchanging bottled Liquefied Petroleum Gas (LPG). These new rules make it mandatory for petrol stations to sell gas bottles and approve mechanisms which facilitate the exchange thereof, requiring any supplier or retailer of liquefied petroleum gas to receive and exchange any gas bottle, irrespective of each brand or original seller. This law prohibited all discriminatory treatment of gas bottles on the basis of their brand.

The new law also subjected retailers of gas bottles to compliance with the legal provisions applicable to essential public services, which until then were only applicable to piped gas.

A 'solidary' tariff for the supply of bottled LPG was also created. The application of this tariff – which will depend on the will of municipalities – will allow the reduction of LPG prices for especially vulnerable consumers.

Judicial decisions, court judgments, results of public enquiries

Components of windfarms not considered as real estate for property tax purposes

Judgments of the Supreme Administrative Court of 10.01.2018 (case no. 01284/17 and case no. 01280/17) considered that each individual component of windfarms cannot be considered real estate for property tax purposes.

The court concluded that each component of a windfarm (wind turbine, rotor, etc.) does not have economic autonomy from the windfarm in its entirety, and cannot therefore be subject to evaluation and taxation individually (i.e. in the absence of the full windfarm).

Therefore, the court annulled the settlement of the property tax for the wind turbines of a given windfarm individually. However, the reasoning of these judgments will not prevent windfarms (in their entirety) being considered real estate and subject to property tax.

Major events or developments

Transference of regulation of the oil sector to the Energy Services Regulatory Entity (ERSE)

Pursuant to Decree-Law no. 57-A/2018, of 13 July, the sector of oil products, biofuels and LPG become subject to ERSE's regulation. This change was anticipated since it was foreseen in the State Budget Law for 2017.

Thus, ERSE, which is the regulatory entity for the electricity and natural gas markets, will acquire these duties with the regulation of the oil sector (downstream), including oil products, LPG and biofuels.

It is unclear if this change of competent authority will be accompanied by a material change in regulatory activity itself, notably if a more active and intense regulation will follow. Although the listing of ERSE's new competences in this sector, as well as its vocational and customary approach (its intervention occurs in economically regulated sectors, such as electricity and natural gas), point in this direction, the legal framework of the development of downstream activities of the oil sector, was not amended with this change. According to this legal framework, activities in the oil sector – including transportation, storage and distribution activities developed in infrastructure qualified as being of public interest – are not public activities developed under a concession, nor strictly regulated as the regulated activities of the electricity and natural gas sectors.

This decree-law also provides for the creation of a new advisory body to advise ERSE on carrying out its functions in the oil sector.

Proposals for changes in laws or regulations

Overpowering of windfarms

In the last few years, windfarms existing in Portugal have carried out overpowering actions, through the installation of additional wind turbines and injection of additional energy to the grid, according to the existing legal framework.

There were also some overpowering projects carried out in Portugal before 2017. The existing legal framework allowed for the overpowering of windfarms up to a limit of 20% of their connecting power, surplus electricity produced being remunerated at €60 / MWh.

However, in August 2017, the Government determined that any overpowering shall not have negative effects for the National Electrical System, and that this evaluation shall be carried in each case by the regulator (ERSE). The approval of a new legal regime for the overpowering of windfarms, replacing the existing one, is foreseen and may happen in 2019.

The approval of a legal framework regarding the repowering of renewable energy power plants – modernisation of power turbines, by replacing old wind turbines with new wind turbines with more efficient technology, capable of generating more electricity and at much lower cost – is still expected in this sector, in order to provide legal certainty to investors in windfarms reaching the end of their lifespan.

Consumers to be exempt of subsoil occupancy charges?

Currently, part of the price of natural gas supply to final consumers in some municipalities is formed by subsoil occupancy charges, a type of charge levied by municipalities for the

installation and passage of pipelines in subsoil of their public and private domain.

These charges are primarily charged to distribution network operators and are passed thereon to suppliers and, finally, to end consumers.

In its struggle to lower energy prices, the current Government has already tried to prevent companies passing on this charge to consumers and has even approved legislation for that purpose. However, it seemed to hesitate later, and such legislation was never applied. In fact, this legislation runs the risk of incentivising municipalities which do not yet levy this charge (or levy it in small amounts) to charge it, as the possible dissatisfaction of consumers is the main disincentive for their collection of high values.

However, the Government has already announced that it intends to review existing legislation on subsoil occupancy charges with a view to achieving a balance in the levying of these charges and prevent end consumers having to pay them.

Tenders for concession of low-voltage distribution networks

Tenders for the new concession agreements of low-voltage distribution networks are also expected to be launched in 2019.

In principle, tenders shall be launched at the intermunicipal level. However, municipalities may launch separate tenders if they can demonstrate that there are powerful reasons, technically or economically, which support or recommend it, and this does not result in global losses of efficiency, equity or territorial cohesion.

* * *

Endnote

1. http://www.apren.pt/contents/documents/anuario-apren2018ebook-spreads-1-4410.pdf.

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A Partner since 2007, Mónica has a strong and well-known professional carrier as a lawyer. She is the co-author of the first publication launched in Portugal with comments to the Natural Gas Legislation enacted in 2008, and frequently publishes opinion articles.

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