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Regulatory Alert

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MAIN AMENDMENTS ESTABLISHED BY THE ROYAL DECREE 413/2014, DATED 6 JUNE, REGULATING THE PRODUCTION OF ELECTRICITY FROM RENEWABLE ENERGY SOURCES, COGENERATION AND WASTE

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1. Introduction

On June 10, the Official State Bulletin (Boletín Oficial del Estado) published the Royal Decree 413/2014, dated 6 June, regulating the production of electricity from renewable energy sources, cogeneration and waste (**"RD 413/2014"** or the **"Royal Decree"**).

The text serves to outline the methodology of the specific remuneration regime applicable to those renewable energy, cogeneration and waste installations currently up and running or planned for the future. Moreover, it sets the criteria for "reasonable profitability" in order for the renewable plants to make a return on the investment made, something which is not achievable through sales of energy at market prices.

The RD 413/2014 is a regulatory standard which expands on the provisions of the Royal Decree-law 9/2013, dated 12 July, setting forth the new legal and financial regime (**"RD-law 9/2013"**), and Law 24/2013, the Electrical Sector Act, dated 26 December (**"ESA"**).

Moreover, it represents the latest announcement - ahead of the forthcoming approval of the Order of Parameters - in the turbulent reform of the renewable energies financial regime, a process which encapsulates the Royal

Decree's drive under the following arrangements: (i) the Royal Decree-law 1/2012, dated 27 January, putting a stop to the pre-assignment of remuneration processes and the removal of financial incentives for new electricity production installations; (ii) the Royal Decree-law 2/2013, dated 1 February, on urgent measures in the electrical grid and financial sector which, among other things, amended the Royal Decree 661/2007, dated 25 May, removing the option of a more premium market price, determining the remuneration in terms of the tariff for all specially regulated installations and also amending the parameters for updating the remuneration for regulated activities within the grid; (iii) the Royal Decree-law 1/2012, dated 27 January, putting a stop to the pre-assignment of remuneration processes and the removal of financial incentives for new electricity production installations; (iv) the Royal Decree-law 2/2013 dated 1 February, on urgent measures in the electrical grid and financial sector which, among other things, removed the option of a more premium market price, determining the remuneration in terms of the tariff for all specially regulated installations; (v) the RD-law 9/2013 which is subsequently, (vi) picked up in the ESA.

The theoretical justification given by the government for this reform is based on the requirement to guarantee the financial sustainability of the system.

The multitude of legal amendments (immediately springing to mind the well-known work of Professor García de Enterría: *"Justice and legal certainty in a world of unchecked laws"*) and the extensive financial repercussions of the same provoked a huge wave of objection before the Supreme Court's Dispute Chamber, mainly due to their infringement of the principle of interdiction in backdating unfavourable regulations and the principles of legal certainty and legitimate expectation.

In a restated doctrine, the Supreme Court has supported the reforms, consider that the electrical production system is subject to a regulatory alea as opposed to the corporate alea, leading to the legalising of any amendments to the financial regime provided that they respect the principle of reasonable profitability.

The reform of the renewable energy financial regime - until the approval of the Order of Parameters - attempts to align with said Supreme Court doctrine.

Said principle of reasonable profitability *is considered a pre-tax profitability which will be centred around the average performance of the ten-year government bonds on the secondary market, increased by applying the appropriate differential*. And, as in the explanatory memorandum and the press release used to announce the publication of this Royal Decree (www.lamoncloa.gob.es), it attempts to clarify that the new remuneration regime will guarantee the financial stability of the electrical grid.

Notwithstanding that, the process of reform for renewable energies regulation embodied by the RD 413/2014 presents significant areas of doubt.

Although it supposes a significant erosion of the previous financial regime - in fact an entire distortion thereof - that may go beyond the limits set by the Supreme Court, one of the main problems is the application of reasonable profitability with respect to the past.

In reality, the RD 413/2014 does not order the reimbursement of any amounts already received, instead calculating future remuneration based on past earnings. Moreover, applying the current concept of reasonable profitability to the past could be deemed, de facto, "unreasonable"; as said profits were not considered such under the previous regulation.

Naturally, these circumstances are different to those analysed at the time by the Supreme Court, reopening the debate around the retrospective nature of the reform as well as the legal certainty and legitimate expectation despite the declarations.

The RD 413/2014 does not only deal with the financial regime of renewable energies. Its scope is much wider, as we assess below.

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2. General Provisions

The concept of nominal power is replaced by installed power, defined as the maximum active power specified in the rating plates. With that, the previous confusion between the concepts of nominal power and limit power has been removed (Supreme Court ruling dated 23 May 2014, article 3 of the Royal Decree).

Nevertheless, the concept of net power remains, which is the one used for the sale of energy in the market (article

9).

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3. Producers' rights and obligations

The priority in terms of dispatch and access and connection to the grid continues to be recognised in the market at equal financial conditions. This is one of the few privileges that remain under the new regulation.

The concept of grouping remains and is defined as a group of installations that (i) connect to the same point of the distribution or transport grid or have a shared discharge line or transformer, with a single point of the distribution or transport grid being understood to be a substation or transformation centre; (ii) those installations with the same land reference, determined by the first 14 digits, will also be considered to form part of the same group.

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4. Specific remuneration regime

The specific remuneration regime is regulated by the Royal Decree replacing the special regulation which was removed by the RD-law 9/2013, dated 12 July, as urgent measures are adopted to guarantee the financial stability of the electrical grid.

Beneficiaries: aside from the remuneration for the sale of energy valued at market price, all renewable energy, high efficiency cogeneration and waste installations shall receive a specific return per unit of installed power allowing the recovery of investment costs which cannot be recovered by the sale of energy in the market.

The objective is to guarantee a **reasonable profit** for the installation: Its value shall be calculated based on the average performance of ten-year government bonds on the secondary market for the 24 months prior to May of the year before the start of the regulatory period, increased by applying a differential.

This remuneration acknowledges the installations which, at the time of entry into force of the RD-law 9/2913, dated 12 July, were deemed eligible for the incentivised financial regime for premiums. New installations may access this remuneration regime by bidding in competitive procedures (2nd Additional Provision).

The remuneration shall be made up of two elements: a return on investment and a return on operation

Return on investment: the value of the return on investment for the installation will be calculated in such a way as to allow for the recovery of investment costs which are yet to be realised according to the net value of the asset as well as the costs which cannot be recovered via the operating income forecasted for the period prior to the installation reaching regulatory useful life.

Return on operation: the return on operation by unit of energy at a standard installation will be calculated by taking into consideration the forecasted operating income by unit of energy generated and the estimated operating costs per unit of energy generated at said installation, with reference to efficient and well-managed companies.

The values of the return on operation and the types of installation which they apply to, as well as the maximum number of equivalent operating hours entitling the installation to receive said remuneration and the rest of the relevant payment parameters will be set by the Order of parameters.

Review by regulatory periods: each regulatory period will last for six years and will be divided into two regulatory half-periods of three years. The first half-period falls between the dates of entry into force of the RD-law 9/2013, dated 12 July, and 31 December 2016.

The payment parameters may be reviewed at the end of each regulatory period and half-period in line with that set forth in article 14.4 of Law 24/2013, dated 26 December, and articles 19 and 20 of the Royal Decree.

As a result of the reviews and updates to the specific remuneration regime, new types of installations may be removed or incorporated into those which come under the application of the return on operation.

Amendments of the installations: these entail the amendment of the remuneration regime, in such a way that (i) the remuneration will not be increased for the investment made, (ii) nor will it bear the right, in the event of a

power increase, to an increase in return on operation. If the amendment entails a change of standard installation, the value of the return on operation will be modified if the revised remuneration is lower. In the event of a reduction in power, the return on investment shall be removed.

Off-peninsular territories: in territories where the cost of conventional generation is much higher than that of the electrical grid within the peninsular, until the point at which the costs of generation for photovoltaic and wind technologies is lower than that of conventional thermal technologies, further incentives for investment due to a reduction in generation costs shall be established (5th Additional Provision).

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5. Accrual and payment of the specific remuneration regime

The specific remuneration regime shall begin to accrue as of the latest date from the following:

- The first day of the following month after the authorisation of the installation's start-up licence.
- The first day of the following month after application for recording in the register for the pre-assignment of remuneration.

The return on investment and operation will extend throughout the regulatory useful life of the standard installation, whose value shall be published on the orders of the Ministry of Industry, Energy and Tourism.

The amounts corresponding to the specific remuneration regime shall be subjected to the general payments process as prescribed in the ESA and the subsequent development thereof. Said payments will be made on a monthly basis in accordance with that stipulated in the ESA, without prejudice to any subsequent adjustments.

It should be reminded that provisional payments have been made in line with the former special regime, in accordance with that laid down in the third transitional provision of the RD-law 9/2013 for which urgent measures have been adopted to guarantee the financial stability of the electrical grid.

Moreover, it was established that the payments owed on the energy produced due to the application of the new remuneration regime from the entry into force of the RD-law 9/2013, until the entry into force of the new remuneration regime, would be made in nine instalments, with a maximum limit imposed resulting from the adaptation of the provisional payments to the new financial regime.

Thus, the eighth transitional provision of the RD 413/2014 determines the process to be applied to these transitional payments which have been made.

Firstly, the payment of the amounts corresponding to the specific remuneration regime for the period to which each payment refers will be made in accordance with the general procedure foreseen in the ESA.

Subsequently, one-ninth of the payments owed resulting from the application of the methodology prescribed in the RD 413/2014 to the energy produced will be included, from the entry into force of the RD-law 9/2013 [1], until the entry into force of the necessary regulations for the full application of the new remuneration regime.

Nevertheless, a payment limit has been established as foreseen in the RD-law 9/2013: this may not surpass 50% of the payment relating to the new specific remuneration regime and the payments owed in the market for the month to which the payment refers. If due to said limit it is not possible to recover the entire amount owed by an installation in nine payments, the remaining amount will be included in the following payments.

This payment process will be applied from the seventh payment of the 2014 financial year, assigning itself to the 2013 financial year until the supplementary payment of the 14 relating to the 2013 financial year is made and subsequently assigns itself to the following years.

Aside from the above, the processes to be applied in the event of failure to make payments corresponding to the electrical grid or its representatives have been established.

6.- Administrative procedures and registers

Register of electrical energy production installations

The electrical energy production installations included in the scope of the application of the RD 413/2014 must be formally registered in the register of electrical energy production installations (**"RAIPRE"**) based on their power rating (article 37). Those with a power rating of higher than 50 MW are registered in the first section and those with an installed power equal to or less than 50 MW are registered in the second section.

This replaces the former Register of specially regulated production installations governed by the Royal Decree 661/2007 as the special regulation element has been removed.

The registration process is very similar to the former: it comprises a prior and definitive registration (article 39 and 40). The latter shall entail the obligation to evidence the gross, net and minimum power in line with that established in the hibernation capacity regulation (article 37.3).

The pre-registration shall be cancelled if the applicant fails to submit the definitive registration within a period of three months (article 41). On the other hand, the cancellation of the definitive registration will result, of its own accord or at the request of the applicant, from the ceasing of energy production or the withdrawal of the installation's licence (article 42).

Specific remuneration regime register

The specific remuneration regime register (**"RRRE"**) has been created ex novo under the approval of the RD 413/2014 with the aim of awarding and tracking the specific remuneration (article 43.2).

In essence, it replaces the former Pre-assignment Register which gave access to the feed-in tariff regime under the regulation of the RD 661/2007.

Registrations in the RRRE may have pre-assignment (article 45) or operating status (article 46 and 47). Registration under pre-assignment status shall require the advanced deposit of a financial security whose amount is determined by ministerial order, and may be executed in the event of suspending construction of the installation unless due to preventative circumstances which are not attributed to the applicant (article 44).

The holder of the RRRE registration under pre-assignment status must submit the operating status registration within one month of the deadline date for completion of the installation (article 47.1), as ordered by the MINETUR (article 46.a).

In the event that the operating status registration is not submitted within said timeframe, or is rejected/dismissed, the registration of pre-assignment status shall be cancelled (article 48).

In terms of the cancellation of the operating status registration and the subsequent denial of access to the financial regime, a series of circumstances are foreseen (article 49).

Among those are: (i) closure, (ii) revoking of authorisation, (iii) withdrawal, (iv) amendment or inaccuracy in the hybrid installations register, (v) failure to comply with registration requirements, (vi) failure to notify the receipt of public aid, (vii) amendments which entail a reduction in the value of investment without a reduction of power, (viii) repeat failure to comply with the efficient energy conditions, (ix) repeat failure to comply with the limits established for fuel consumption, (x) it is declared that the conditions required for entry into the RRRE are not being maintained as a result of an inspection, (xi) inaccuracies in any declarations, and (xii) any non-fulfilment of the obligations and requirements laid down in the Royal Decree.

A new element with regards to the draft of the Royal Decree dated 10 January 2014 is the provision that the owner of the installation who appears in the RAIPRE must also be the owner of the RRRE registration.

Attributes of the inter-temporal law

The arrangements of the inter-temporal law of the RD 413/2014 stipulate that the installations which were deemed eligible for the incentivised financial regime for premiums at the time of entry into force of the RD-law 9/2013, will be automatically registered in the RRRE (DT 1ª) under the following conditions.

The registration under pre-assignment status shall be carried out for installations which at the time of making the registration are not registered in the payment system, but were deemed eligible for a remuneration premium. On the other hand, if they were already registered in the system, such registration would enjoy operating status.

The information included in the payment system or in the pre-assignment register, whichever applies, will be used at the time of making the automatic registration in order to determine the power for which the installation had been

awarded the Feed-in tariff regime.

By order of the MINETUR the equivalences between the new standard installations and the former categorisation in force shall be established. In the event that it is not possible to determine the categorisation of standard installation, it shall be assigned by default.

Within a period of three months from the entry into force of the order, the owners will be able to submit a request to amend the assignment of standard installation by default together with the documentation which it deems appropriate for proving said change.

Within a period of six months from the publication of the MINETUR's order these installations shall send (via electronic media) the UTM coordinates of the polygonal line where the installation is located to the General Directorate for Energy Policy and Mines.

Installations registered under pre-assignment status must have been registered definitively in the RAIPRE and have begun to feed energy back by the deadline in order to be able to move to operating status (6th Additional Provision).

In the case of those installations automatically registered on the RRRE, and that had previously been registered on the pre-assignment register under the protection of the Royal Decree 1578/2008, a cancellation procedure for specific non-fulfilment is laid down (7th Additional Provision) in the same way as that for those registered under the protection of the Royal Decree 6/2009 (8th Additional Provision).

The obligation for the installations to submit (via electronic media) a declaration regarding any aid received within a period of six months from the automatic registration in the RRRE is included as a new element with respect to the previous draft of the Royal Decree.

If you are interested in obtaining more information on the content of this Alert please contact Félix Plasencia, Javier Torre de Silva and Jaime Almenar on tel: (+34) 91 451 93 00

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These comments contain general information only, not representing any professional opinion or legal advice.

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*Footer:

1) The entry into force occurred on 14 July 2013 (Tenth final provision of the Royal-Decree law 9/2013)

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