CLIFFORD

CHANCE

Client briefing
March 2011

Clouds over the photovoltaic sector in Italy

On 3 March 2011, Italy's President of the Republic signed the definitive version of the decree that transposes Directive 2009/28/EC on the promotion of the use of energy from renewable sources in Italy (the "**Decree**"). The Decree will come into force on the date after it is published in the Official Gazette, with publication expected shortly. The Decree varies significantly from the draft version (described in our previous client briefing of February 2011), which had been heavily commented by the industry. The debate and opposition that the draft decree had generated within the industry continues now, again led by energy producers as well as other stakeholders such as institutional lenders and some of Italy's regional and local governments.

In this Client Briefing, we summarise the main provisions of the Decree, and discuss the options open to the participants in the industry.

Key provisions of the Decree

Article 4 allows the Regions and the Autonomous Provinces to decide when two or more projects should be considered, cumulatively, as one single project, for the purposes of the environmental impact assessment, if those projects are located on the same area or on "contiguous" areas. Despite objections during the comment period, the term "contiguous" has been retained, and may be broader than the term "adjacent", which had been suggested as a preferable alternative.

Article 5 mandates that authorities complete their evaluation of an application for a single authorisation within a specific term, not to exceed 90 days if no environmental impact assessment (VIA) is required, or 90 days plus 150 days for the VIA, if the VIA is required. The terms are mandatory, as suggested by the industry, however the Decree does not provide for sanctions for delays by the administration.

Article 6 grants the Regions and Autonomous Provinces the right to allow plants with a capacity of up to 1MW to be authorised by way of a new simplified authorisation procedure, which is very similar to the well known DIA procedure used up to now. This is less than the industry expected, given that Law No.

Key Issues

Key provisions of the Decree

Limitations to the use of agricultural land

Exclusion from the incentives

New incentive mechanisms

Green certificates

Incentives for the photovoltaic sector

Alleged unlawfulness and unconstitutionality of the Decree

If you would like to know more about the subjects covered in this publication or our services, please contact:

Energy, Regulatory and Public Law

Cristina Martorana, Partner

Chiara Commis, Associate

Banking & Project Finance

Charles Adams, Partner

Giuseppe De Palma, Partner

Corporate Law

Umberto Penco Salvi, Partner

Clifford Chance Studio Legale Associato,
Piazzetta M.Bossi, 3, 20121 Milan, Italy
+39 02 80634 1
www.cliffordchance.com

96/2010 (i.e. the parliamentary law of delegation – *legge delega*) required the Italian government to mandate that this exception would be valid on a national scale, and not left to the discretion of each Region/Autonomous Provinces.

Limitations to the use of agricultural land

Art. 10 permits incentives for photovoltaic projects on agricultural sites **only** if:

(a) a plant's nominal power does not exceed 1 MW;

(b) plants on land owned by the same person(s) must be at least 2 kilometres apart; and

(c) the plant covers a surface that is not more than 10% of the total surface of the land owned or held by the plant's owner/developer.

Plants on lands that have been abandoned for at least five years are exempt from the above restrictions. It seems reasonable in this regard to consider 'abandoned' to mean 'not cultivated'. Further, a grandfather clause exempts plants (i) authorised before the Decree comes into force, or (ii) for which authorisation was sought on or before 31 December 2010, in each case on the condition that the plant start operations within one year from the entry into force of the Decree (most likely then by March 2012).

This is already one of the most criticised provisions of the Decree, and the exemptions available are not deemed to be sufficient.

Exclusion from the incentives

Under article 23(3) of the Decree, persons who submitted an application for admission to incentives that was accompanied by any false documents, statements or information are prohibited from gaining access to any such incentives under Italian law for ten years from the ascertainment of such breaches. The prohibition applies to the natural person or company that submitted the application and also to: (a) the legal representative of the company, where a company submitted the application; (b) the person in charge of the plant; (c) the technical director; (d) the partners of general partnerships (*società in nome collettivo*); (e) the general partners of limited partnerships (*società in accomandita semplice*); and (f) directors with powers to represent their firm, with regard to all other kinds of firms and consortia.

New incentive mechanisms

Only two incentive mechanisms will be available for renewable power plants that start operations after 31 December 2012. Both are based on the same fundamental principles, that there should be: (i) fair compensation for investments made, and operational costs; and (ii) ongoing financial support over the whole life of the plant. Projects generating less than 5 MW[1] will benefit from a predefined incentive tariff, varying on the basis of the power source used and the plant's capacity. Power plants with a capacity of more than 5 MW will benefit from an incentive awarded through descending-price auctions, which will be managed by the GSE.

The Decree states that secondary legislation in the form of ministerial decrees will provide detailed sets of rules for these incentive systems, which will reflect these fundamental principles, within six

[1] Please note that this power threshold can be modified by subsequent ministerial decrees, but cannot be, in any case, inferior to 5 MW.

© Studio Legale Associato in associazione con Clifford Chance March 2011

months of the Decree coming into force. In financial terms, funding for the incentives will come from the A3 component of the tariff, which is ultimately paid by final customers.

Under article 24(5)(c), the specific terms upon which the transition will take place from the current incentive schemes (in particular, the system of green certificates, which is being abolished – see paragraph below), to the new schemes, will be set out in subsequent ministerial decrees. The article makes clear that all plants currently receiving green certificates will be migrated to the new fixed-incentive scheme, irrespective of their capacity, as means of making returns upon investment consistent.

Green certificates

Article 25 provides for the complete abolition of the green certificates scheme. From 2013, the proportion of electricity generated from renewable sources (or covered by green certificates) under article 11 of Legislative Decree No. 79/1999 will be gradually reduced on a straight-line basis, from its 2012 percentage to zero by 2015. The GSE will be obliged to purchase unsold certificates each year at a price that is 78 per cent of their value as determined under article 2 paragraph 148 of Law No. 244/2007 (i.e., the selling price of certificates put onto the market by the GSE, which is the difference between €180/MWh and the average annual price of sale for electrical power as determined by the AEEG in relation to the previous calendar year).

Incentives for the photovoltaic sector

Articles 25(9) and 25(10) are the provisions of the Decree that have come in for the greatest criticism. They establish that the incentives laid down by the Ministerial Decree of 6 August 2010 (colloquially known as "the third *Conto Energia*") will apply only to photovoltaic plants that start operations no later than 31 May 2011.

The incentives applicable to plants commencing operations after that date will be determined by subsequent ministerial decrees, which should be issued by 30 April 2011, based on a number of fundamental principles, including:

(i) a limitation upon the aggregate annual capacity with access to the incentives; and

(ii) the terms of the tariffs should reflect the gradual reductions in technological and operating costs, and the other incentives applicable within EU Member States.

These principles make no mention of ensuring fair compensation for investments made and operational costs, or of ongoing financial support over the whole life of plants.

The Decree does not abolish article 2-*sexies* of Law No. 41 of 22 March 2010, which provided access to the incentives of the second *Conto Energia*[2] to plants where they (i) had been installed (and that installation duly notified to the authority competent for the issuance of the authorisation, the grid operator and the GSE) no later than 31 December 2010, and (ii) start operation by 30 June 2011.

Inspections by the GSE are currently ongoing to confirm the accuracy of the documentation that operators have submitted and the ascertainment of such breaches may have quite serious

---

[2] Pursuant to article 6 of Ministerial Decree 19 February 2007.

© Studio Legale Associato in associazione con Clifford Chance March 2011

consequences, potentially excluding the breaching operator from all incentives for a period of ten years.

Alleged unlawfulness and unconstitutionality of the Decree

Doubts have been raised in relation to the lawfulness of several of the Decree's provisions, mainly on their possible conflict with some of the fundamental principles set forth in the Italian Constitution and the EC Treaties. Specifically:

(i) The provisions regarding the incentives for photovoltaic plants (article 25) have substantial retrospective effects and severely frustrate the operators' legitimate reliance upon the previous legislation. Many investments and loan agreements were entered into in reliance upon the incentive levels set out by the third *Conto Energia*, which was scheduled to end on 31 December 2013. That its expiry has been brought forward to 31 May 2011, together with the continuing uncertainty over the new incentive tariffs, is certain to have substantial impacts upon the operators' business plans, violating a principle, that of legitimate expectations, that is enshrined in the Italian Constitution, the EC Treaties and the European Convention on Human Rights, and which has been consistently upheld in the case law. The principle implies that, if the Government issued legislative measures providing for benefits, and the citizens have relied upon such benefits to organise their activities, the Government cannot simply withdraw those measures, causing detriment to the citizens to whom an entitlement to those benefits has accrued.

(ii) While in formal terms the Italian government is implementing a new EU directive, in substance it is frustrating its spirit and objectives: EU policy in the area is clearly aimed at further development and fostering of the production of renewable energy, while the actions taken by the Italian government seem to go in the opposite direction.

(iii) The Decree also appears unreasonable and discriminatory, where it provides that plants completed by 31 December 2010 and connected by 30 June 2011 are entitled to benefit from the tariffs of the second *Conto Energia*, while those completed in 2011 and connected after 31 May 2011[3] are excluded not only from the second but also from the third *Conto Energia*.

(iv) The Decree also appears to be in breach of Law 96/2010, under which the Government was obliged to "update and bolster the incentive system for renewable energy", whereas the Decree in fact weakens and undermines that incentive system.

(v) The procedure for approval of the Decree has not been properly carried out because of the lack of the opinion of the Unified Conference between the State and the Regions (*Conferenza Unificata Stato-Regioni*). In this case, the Unified Conference examined (and gave its opinion on) a version of the draft decree that was quite different from the one that was ultimately approved by the Council of Ministers, including in some of its most fundamental provisions (which were included afterwards, effectively bypassing the United Conference).

On this basis, the Decree, and any decision taken in implementation of its terms, could be challenged before:

[3] Please note that it ordinarily takes more than six months to obtain a connection to the grid.

© Studio Legale Associato in associazione con Clifford Chance March 2011

(i) the European Court of Justice, by a litigant, on the basis that it breaches both EU policies on renewable sources, environmental protection and climate change, and the European Union's principle of legitimate reliance;

(ii) the European Court of Human Rights, by a litigant, on the basis that it breaches the European Convention on Human Rights;

(iii) the Constitutional Court, by a domestic court requested by a litigant to decide upon the legitimacy of an action taken in implementation of the allegedly unconstitutional provisions; or

(iv) the Constitutional Court, by a regional government, on the basis that it is in breach of the Constitution.

Some regional governments (such as that of Tuscany) have already made statements to the press that they are considering raising the question of the Decree's legitimacy before the Constitutional Court.

Additionally, the major foreign banks operating in the Italian renewable market have intimated to the government that were the Decree to come into force in its current form, it would not only call into question a significant number of current and future loans within the renewable sector, but also be taken as a signal of a wider lack of reliability on the part of the Italian State, which could potentially result in a reduction or withdrawal of investments in other key sectors as well, such as infrastructure, which could have serious consequences, for the wider economy and for employment.

Finally, the operators have pointed out the importance of a rapid definition of the new incentive system, which should be based on such principles as the respect of legitimate reliance and a fair remuneration of the investments.

With respect to these concerns, the Ministry of Economic Development has summoned the major operators and financial institutions that are active in the renewable sector for a meeting on Tuesday 15 March 2011, with the stated intention of clarifying the new framework for incentives as soon as possible (which we take to mean, within the next few weeks).

As a leading law firm much involved in the Italian renewable sector, we are working closely with the operators, the banks and the associations for the amendment of the Decree's key provisions, seeking to restore the stability that such a regulatory framework requires.

This Client briefing does not necessarily deal with every important topic or cover every aspect of the topics with which it deals. It is not designed to provide legal or other advice.

www.cliffordchance.com

Abu Dhabi ■ Amsterdam ■ Bangkok ■ Barcelona ■ Beijing ■ Brussels ■ Bucharest ■ Dubai ■ Düsseldorf ■ Frankfurt ■ Hong Kong ■ Kyiv ■ London ■ Luxembourg ■ Madrid ■ Milan ■ Moscow ■ Munich ■ New York ■ Paris ■ Prague ■ Riyadh* ■ Rome ■ São Paulo ■ Shanghai ■ Singapore ■ Tokyo ■ Warsaw ■ Washington, D.C.

* Clifford Chance also has a co-operation agreement with Al-Jadaan & Partners Law Firm in Riyadh

© Studio Legale Associato in associazione con Clifford Chance March 2011