

New M&A opportunities in the renewable energy sources

Italian energy policy is changing rapidly. New laws and regulations on renewable energy sources are evolving in quick succession and a brand new incentive mechanism will be announced soon. In this context, on 2 April 2012, a new decree on "burden sharing" was published in the Italian Official Gazette. This may be considered the first step of the Italian government's new approach to renewable energy matters.

Italy implemented Directive 2009/28/EC promoting the use of energy from renewable sources through the comprehensive reform of the incentive system for renewable energy plants set forth in Legislative Decree No. 28 of 3 March 2011 (the so-called "**Romani Decree**"), which set the national target for 2020 for the overall share of energy from renewable sources as 17% of gross final consumption of energy. The Romani Decree expressly stated that (i) a Ministerial Decree would be issued to regulate the incentive scheme for commissioned photovoltaic plants, and further to this the Fourth Conto Energia (as defined below) was implemented, and another Conto Energia (the "**Fifth Conto Energia**") is currently under discussion; (ii) another Ministerial Decree would be issued to regulate the incentive scheme for any other renewable energy source/plant after 1 January 2013 and to abolish the Green Certificate mechanism, replacing it with a feed-in tariff mechanism (the "**Feed-in Tariff Decree**"). In practice these subject matters are regulated by way of Ministerial Decree, but further specifications may be needed due to the highly complex technical elements involved. The entities responsible to issue these further specifications and



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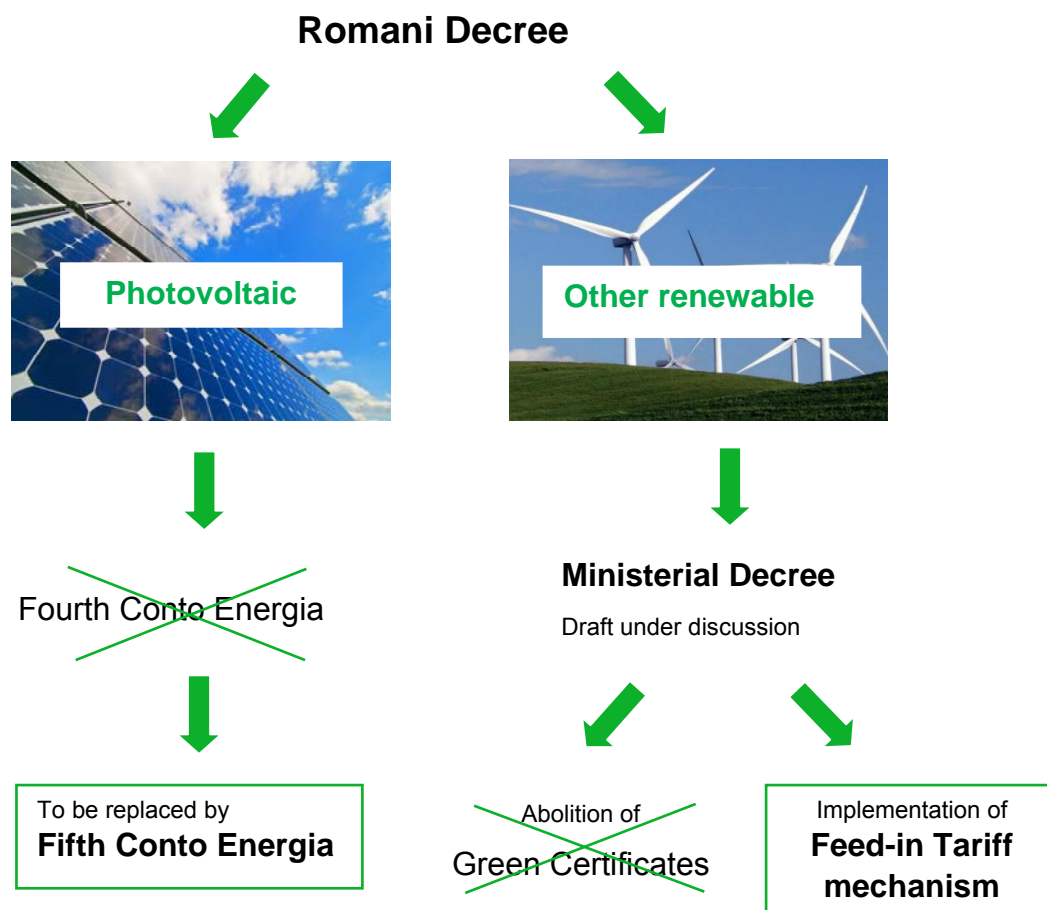
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guidelines are, in principle, the *Autorità per l'Energia Elettrica e il Gas* (the Italian authority for energy and gas, the "AEEG") and GSE S.p.A. (the state-run entity in charge of the implementation of incentive systems to promote the use of renewable sources, the "GSE").



The Fifth Conto Energia and the Feed-in Tariff Decree are still under discussion; however the drafts that have been circulated allow us a first glance of the Italian legislature's current vision.

This client briefing summarises the state of the art of legislation affecting the renewable energy market in Italy in the context of the evolving legal framework, to identify and to stay ahead of potential trends.

Photovoltaic sources

Status quo: the Romani Decree and the Fourth Conto Energia

The current incentives system for photovoltaic plants in Italy is governed by the Ministerial Decree of 5 May 2011 (the "**Fourth Conto Energia**") which applies to all photovoltaic plants with a capacity exceeding 1kW that start operations after 31 May 2011 and (on or) before 31 December 2016. The incentive to be received by a plant will be determined primarily on the basis of the date on which the plant begins operations and will remain unvaried for the entire incentive period of 20 years.

The incentives available under the Fourth Conto Energia are different for the period until 31 December 2012 from those available for the period thereafter.

Further, the Fourth Conto Energia creates distinctions on the basis of the size of the plant and the date on which the plant is admitted to the incentive system.

Small Plants

- Integrated plants with a capacity of up to 1 MW
- Non integrated plants with a capacity of up to 200 kW which sell their electricity through the net metering service
- Plants installed on buildings and areas belonging to the public administration, irrespective of their capacity



Are admitted to the Fourth Conto Energia without limitations, for the period until 31 December 2012

Large Plants

All plants that are not classifiable as small plants



Until 31 December 2012, admission is restricted by six-month incentive caps, following a registration and ranking process which aims to monitor the incentives payable to the admitted plants to ensure the available incentive caps are not exceeded.

The amount of incentives imputable to large plants admitted to the Fourth Conto Energia will be calculated *ex ante* in accordance with the guidelines issued by the GSE on 15 May 2011, taking into account estimates of (i) the quantity of electricity the plant will produce and (ii) the commissioning date of the plant.

Large plants commissioned by 31 August 2011 are exempt from the registration procedure.



Ranking process

Once each relevant registration session is closed, to determine which plants can be admitted to receive the incentives up to the incentive caps limits, the GSE will rank all the plants admitted to the registry, on the basis of the following priority factors, to be applied in order:

- (i) Plants already operational as at the date of the application
- (ii) Plants already completed at the date of the application
- (iii) Chronological priority of the authorisation
- (iv) Lower capacity of the plant
- (v) Chronological priority of the application

The GSE has announced that the total incentives payable to large plants commissioned by 31 August 2011 and to registered plants have reached Euro 1 billion, which is above the applicable cap (Euro 300 million). Therefore, as allowed under the Fourth Conto Energia, the amount exceeding the cap will be funded using resources deducted from the cap applicable to the second semester of 2012 (Euro 130 million). This means that no registration session will be launched for the second semester of 2012.

Photovoltaic plants installed on the ground over agricultural lands are subject to specific restrictions.

The near future: the "end" of the Fourth Conto Energia and the Fifth Conto Energia

The Fourth Conto Energia has an expiration date of 31 December 2016 and identifies two goals to be reached by this date: one in terms of total installed power (*potenza complessiva installata*), which has been set as 23,000 MW; and a second in terms of envisaged cumulative costs per year of the incentives to the photovoltaic sector, which has been set a Euro 6-7 billion. The Fourth Conto Energia also specifies that when the Euro 6 billion threshold is reached the incentive system may be revisited.

Due to the strong growth in investments in the photovoltaic sectors it is likely that the Euro 6 billion threshold will be reached as early as June 2012; therefore, the Italian Government has already started discussions to enact a new ministerial decree to replace the Fourth Conto Energia (by way of the Fifth Conto Energia) aiming to reduce the impact of the current incentive system on the final customers (families as well as businesses) also taking in consideration the Eurozone's deepening economic downturn, which cannot currently sustain electricity prices increased by any incentive (as clearly stated by the Minister of the Economic Development, Mr. Passera).

From the drafts circulated during the past few weeks, the Fifth Conto Energia should provide a strong reduction of the incentive tariff starting from 1 July 2012 (or the date on which the Fourth Conto Energia threshold of Euro 6 billion is reached), and provide for a new yearly cap of Euro 500 million for incentives to all photovoltaic plants (irrespective of their size) instead of the cap of Euro 810 million provided by the Fourth Conto Energia for large plants.

The Fifth Conto Energia should also extend the registration and ranking process to all plants having a capacity in excess of 3kW (with priority to integrated plants installed to replace asbestos and fibre cement roofing) and introduce the all-comprehensive tariff (*tariffa omnicomprensiva*) starting from July 2012, instead of January 2013 as provided by the Fourth Conto Energia.

Other renewable energy sources

Status quo: the Green Certificate mechanism

Renewable energy plants other than photovoltaic plants are currently eligible to benefit from the green certificate scheme introduced in Italy by the Legislative Decree No. 79 of 16 March 1999 (the so-called "**Decreto Bersani**") as a result of the implementation of Directive 96/92/EC on common rules for the internal market in electricity.

The green certificates mechanism is based on Article 11 of the Bersani Decree, which - to promote increased use of renewable energy sources to produce electricity and to create a demand for electricity from renewable energy sources - introduced what is known as a "quota obligation", an annual obligation for electricity producers and importers to input into the national electricity system a minimum quota of energy produced using renewable energy sources (the "**Quota Obligation**").

An energy operator may discharge its Quota Obligation by producing the minimum quantity of energy from renewable sources, and/or by purchasing whole or part of an equivalent amount, or the related green certificates, from other producers.

As stated above, the current green certificates mechanism will be abolished in full, in accordance with the Romani Decree: starting from 1 January 2013, the proportion of electricity that must be generated from renewable sources or covered by green certificates pursuant to the Quota Obligation will be gradually reduced on a straight-line basis, from the 2012 percentage to zero by 2015.

The near future: promotion of other renewable energy through a new incentive scheme

Starting from 2015, the Green Certificate mechanism will be replaced by a new support mechanism.

Pursuant to the Romani Decree, a new incentive system will be available for renewable energy plants commissioned after 31 December 2012. This new system will consist of the payment of Feed-in Tariffs on the basis of the following main principles:

- (i) a fair compensation for the investment costs, and
- (ii) an ongoing financial support over the whole life of the project.

According to the Romani Decree, starting from January 2013, projects generating up to 5 MW of power will benefit from predefined Feed-in Tariffs, in amounts varying depending on the power source used and the plant's capacity. Power plants with a capacity of more than 5 MW will benefit from a Feed-in Tariff awarded through descending-price auctions, which will be managed by the GSE.

Renewable energy plants commissioned before 31 December 2012 will continue to benefit from the currently applicable incentive scheme, as amended by the Romani Decree, until the end of 2015. The GSE, which operates on the green certificate market as buyer of last resort of unsold green certificates at maturity, will continue to purchase the unsold certificates relating to the electricity produced during the period 2011-2015, at a price equal to 78% of the price at which the GSE places the certificates on the market pursuant to Article 2 paragraph 148 of Budget Law 2008. Budget Law 2008 (i.e., Law No. 244 of 24 December 2007) specified that the value of each green certificate for the first year was equal to the difference between a predefined value of 180 EUR and the annual average price of electricity defined each year by the AEEG.

Starting from 1 January 2015, the right of the renewable energy plants commissioned before 1 January 2013 to receive Green Certificates will be converted into the right to receive a Feed-in Tariff, in accordance with the new incentive system.

The Feed-in Tariff Decree - secondary legislation in the form of ministerial decrees - will be promulgated to provide detailed sets of rules for the new incentive system, including rules governing the interim period and the transition of existing plants eligible to receive green certificates to the new incentive scheme.

The Burden Sharing Decree: first step of the new energy policy

A significant step toward the reorganisation of the national renewable energy policy was taken by the Italian Government with Ministerial Decree 15 March 2012 (the so called "**Burden Sharing Decree**") which was published in the Italian Official Gazette No. 79 of 2 April 2012.

The Burden Sharing Decree, as provided for in Article 36, sixth paragraph, of the Romani Decree, sets and quantifies the targets for use of energy from renewable sources at the regional level. These targets are the bases to achieve, by 2020, the national objective in accordance with the requirements set forth by the European Directive 2009/28/EC. The Burden Sharing Decree also sets out the procedure to monitor the progress towards achievement of the targets and the remedies available if those targets are not achieved.

The regional targets vary greatly from region to region and have been set on the basis of each geographical area's current usage of renewable sources, and its ability to deliver expanded use.

In order to achieve their respective targets, the regions and autonomous provinces must augment the tools available for local government and for the support of business innovation, introducing specific local legislation that favours energy efficiency and the use of renewable sources.

The Burden Sharing Decree should be followed by a new national energy plan for Italy, which in turn will allow Italy to benefit of a comprehensive legal framework in this vital and key sector.



M&A market opportunities

As shown above, the current situation is quite fluid. What clearly emerges is that the incentive schemes which have characterised Italy so far will be amended again, and significantly.

Nevertheless, this could lead to circumstances favourable for investors. The Fifth Conto Energia and of the Feed-in Tariffs will be ready soon and they will certainly be in line with the above economic policy. This will give access to a new world for incentives with a completely new environment of opportunities for investors.

In fact:

- The vast number of plants already connected - to which the current incentive scheme applies – is very fragmented. Hence, there will be a high number of transactions - with no discount on prices considering the low level of risk – to allow a fewer number of players to consolidate the market (on plants to be connected the risk profile is of course higher but there will be a high number of "low cost" opportunities as a consequence of the risk profile);
- The consolidation process has already started: a number of key players own and operate fleets of high quality solar and other renewable energy plants and may consider selling minority stakes to venture capital and other investors (also in the form of debt-equity hybrid instruments) considering that the capital market track seems unavailable in the short-medium term;
- The market will likely be driven by a few high calibre professional investors which see a great opportunity for investment in Italy as well as the opportunity to reshape Italy's energy landscape;
- Foreign investors, in particular, are welcome by the Italian Government, which has recently enacted new rules on golden shares to reduce the discretionary authority of the State and to minimise the intervention of the State in key sectors such as the energy sector (for more information on the new "Golden Share" please see our Briefing Note of March 2012);
- Lastly, the proposed reductions in the incentives schemes is likely to be mitigated because of the significant reductions of the price of solar panels. So particularly in the Southern regions of Italy it should be possible to implement projects on a "grid parity" basis.

In terms of general economic politics, it is quite clear that the Italian Government is taking a rigorous approach, while keeping in mind the importance of the renewable energy in a country where natural resources of energy are far less than sufficient to cover internal need and where nuclear power has been definitively banned. In this frame, it is not surprising that Minister of Environment Clini has declared that the incentives for photovoltaic plants should be continued and added that *"renewable energies are a key element to reach the Government's targets. New incentives will be introduced for high efficiency green technologies. However, the cost of the photovoltaic modules has decreased by 75% since 2004: the current incentive system grants excessively high revenues and this may lead to speculation."*

This publication 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.

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