

Renewable energy in Ukraine

With its accession to the Energy Community in February 2011, Ukraine has undertaken to ensure that by 2020 12% of Ukraine's electricity supply comes from renewable sources. To accomplish this, Ukraine will need to attract a significant amount of investment into the renewable energy sector ("RES").

This client briefing contains an overview of the key incentives available in Ukraine to those engaged in renewable energy generation and certain challenges related to investment in the RES in Ukraine.

What are the regulatory incentives?

Regulatory incentives are available in Ukraine for the major types of renewable energy, such as biomass, wind, solar and hydro generated energy.

The key regulatory incentives applicable to the RES include:

- guaranteed off-take of the electricity;
- linking minimum green tariff rates to EUR;
- "grandfathering provisions" to ensure that green tariff rates are not reduced until 1 January 2030; and
- tax benefits (e.g. a qualified exemption from corporate profit tax until 1 January 2021 and VAT exemptions on the imports of certain equipment for an indefinite period of time).

Guaranteed off-take

Alternative energy producers may sell electricity directly to customers under bilaterally negotiated sale and purchase agreements or to the operator of the Ukrainian wholesale electricity market, State Enterprise "Energoynok" (the "**Electricity Market Operator**"), who is obliged by law to purchase, at the applicable green tariff rate (discussed in more detail below), all electricity that a producer wishes to sell to them. The law requires that settlements between the energy producer and the Electricity Market Operator under power sale and purchase agreements be made in a timely manner and for monetary consideration (as opposed to barter arrangements).

Green tariffs

What are the green tariffs?

The green tariff (also known as the feed-in tariff) is a special tariff for the purchase of electricity generated from renewable energy sources by the Electricity Market Operator.

As of 1 July 2013, more than 90 RES companies were operating under the green tariff regime in Ukraine.

Key issues

- What are the regulatory incentives?
- Guaranteed off-take
- Green tariffs
- Local content requirement
- Green tariff "grandfathering" provisions
- Tax benefits available for RES companies
- Challenges for RES investors

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Which entity assigns green tariffs?

In Ukraine, green tariff rates are assigned by the National Commission for the Regulation of Energy ("NERC") for each energy generation facility of an energy producer.

What green tariff rates apply?

The green tariff rates are set by NERC in UAH based on a statutory formula and are adjusted by NERC on a monthly basis to ensure that the applicable green tariff rates do not fall below the statutorily established minimum rates linked to EUR.

The statutorily established minimum green tariff rates are set out in the table below:

Type of energy generating facilities		Green tariff rate, approx. EUR / kW x hours*
Wind power plants	comprising wind turbines with an individual capacity of more than 2 MW	0.1131
	comprising wind turbines with an individual capacity of 0.6-2 MW	0.0754
	comprising wind turbines with an individual capacity of less than 0.6 MW	0.0646
Solar plants	facilities located on the ground	0.3393
	facilities assembled on a roof or a facade with a total capacity of more than 100 kW	0.3490
	facilities assembled on a roof or a facade with a total capacity of up to 100 kW	0.3587
Hydro power plants	small hydro power plants	0.1163
	mini-hydro power plants	0.1551
	micro-hydro power plants	0.1939
Biomass power plants		0.1239
Biogas power plants		0.1239

* VAT not included

How long will the green tariff rates apply?

Once an energy producer has had it confirmed that a green tariff rate will apply in respect of a certain energy facility, that rate cannot be reduced until 1 January 2030.

Will green tariff rates decrease over time as applied to new energy producers?

Green tariff rates which will be offered to new energy producers will gradually decrease by 10%, 20% and 30% from the current rates starting from 1 January 2015, 1 January 2020 and 1 January 2025 respectively.

What is the condition for assigning a green tariff?

Any new energy producer wishing to obtain a green tariff rate, where construction of the relevant energy facility commenced after 1 January 2012, needs to comply with the local content requirement. A more detailed overview of the local content requirement is set out below.

Local content requirement

What is the local content requirement ("LCR")?

The LCR is the requirement that a certain portion of the raw materials, equipment, works and services used in setting up the applicable facilities must be of Ukrainian origin.

Rules on LCR

Under the currently effective rules on LCR ("**LCR Rules**"), the LCR applies to all energy producers in the RES, other than hydro power plants and household solar energy producers.

The LCR Rules require that the LCR be calculated by looking at the raw materials, equipment, works and services of Ukrainian origin used in each element of the construction of the energy facilities (such elements of construction being defined in the law). Certain elements of construction may then account for a certain fixed percentage share of the LCR. For example, as applied to wind farms, the use of blades of Ukrainian origin will equate to 15% for the purposes of calculating the LCR, and the use of construction works of Ukrainian origin will equate to 20%.

According to the procedure for the application of the LCR Rules, that were adopted on 27 June 2013 (and will take effect upon being officially published), each element of construction may only account for the LCR if the relevant element does not have any foreign content (i.e. that of a non-Ukrainian origin). This means that in order to comply with the LCR certain elements of construction would need to contain goods or services of Ukrainian origin only.

According to the LCR Rules, in order to qualify for a green tariff rate:

- electricity producers generating electricity from wind, solar and biomass energy will need to ensure that, where construction commenced after 1 January 2012, the facilities comply with the following LCRs:
 - 30% for energy facilities that are put into operation before 1 July 2014; and
 - 50% for energy facilities that are put into operation after 1 July 2014;
- electricity producers generating electricity from biogas will need to ensure that, where the construction commenced after 1 January 2012, the facilities comply with the following LCRs:
 - 30% for energy facilities that are put into operation after 1 January 2014 but before 1 January 2015; and
 - 50% for energy facilities that are put into operation after 1 January 2015.

Decision making on the LCR compliance

The Ukrainian origin of goods needs to be confirmed by a certificate from the Ukrainian Chamber of Commerce and Industry or another relevant foreign authorised body.

The Ukrainian origin of construction works will be confirmed if the energy producer retains contractors registered in Ukraine (as confirmed by relevant extracts from the Ukrainian registry of companies).

The NERC will make its decision on the compliance with the LCR based on the relevant confirmation documents submitted by the energy producer which, among others, include certificates of origin issued by the authorised bodies.

Green tariff "grandfathering" provisions

Ukrainian law contains a grandfathering provision in relation to the application of the green-tariff regime. The law provides that the green-tariff regulations effective as of the date of commencement of energy generation for a particular facility will continue to apply for the life of such facility or until 1 January 2030, whichever is earlier. If the relevant regulations are subsequently amended, renewable energy producers may, at their discretion, opt to comply with the new or amended regulations or continue to work under the old regulations.

Further, the law provides that for the period during which the green tariff is applicable, the Electricity Market Operator must purchase all of the electricity generated (in excess of that supplied to customers and/or gas distributors directly) at the applicable green tariff rates.

Tax benefits available for RES companies

Corporate profit tax (CPT)

The Ukrainian tax code provides that any profits generated by alternative energy producers, to the extent derived from energy generation activities, are exempt from CPT until 1 January 2021.

In order to qualify for the relevant tax exemption, the energy producer must spend its non-taxed profits on the improvement and/or acquisition of production facilities, increasing the production capacity, implementation of modern technologies and/or repayment of credit facilities taken out for these purposes.

Value added tax (VAT)

A VAT exemption is available to companies in the RES for imports of certain materials and equipment, including equipment and materials for the production of alternative energy.

The following requirements should be met in order to qualify for the above tax benefit:

- the relevant goods imported are used by the tax payer for its own production; and
- identical goods with similar quality parameters are not produced in Ukraine.

Land tax

RES companies enjoy the benefit of paying reduced land taxes, i.e. 25% of the land tax calculated based on the applicable tax rules.

Challenges for RES investors

Any potential investor in this sector must be aware of the regulatory hurdles which exist in Ukraine, including the following:

- the complicated procedures for obtaining a licence for the production of electricity in Ukraine;
- the inability to secure green tariff rates and long term power purchase agreements at the initial stages of an RES project;
- legislative uncertainty, as evidenced by the frequent changes that have been made to the law and regulation since its adoption (we note that the "grandfathering" provisions only apply once a green tariff rate has been obtained, which occurs once the project is put into operation);
- the land allocation process, which can be complex and time consuming, and there can be difficulties with rezoning certain types of land;
- the existing electricity transmission infrastructure in Ukraine, which requires upgrading; and
- the connection of high capacity generating facilities to the grid may be a challenge in certain regions of Ukraine.

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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