

New support scheme for renewable energy sources in Poland – results of first auction published

The first pilot auction to support renewable energy projects, scheduled for the end of December 2016, was successfully concluded. Despite controversies caused by technical problems with access to the electronic auction platform, which were to prevent some investors from submitting bids, and in spite of rumours that the auction could be invalidated, on 3 January 2017 the President of the ERO has published the results of 3 successfully completed auctions. As a result of these auctions, support will be given to over 80 new small RES installations ($\leq 1\text{MW}$), whilst over 50 existing small installations ($\leq 1\text{MW}$) will migrate from the green certificates scheme to the scheme based on the guaranteed off-take of energy at the auction price.

When discussing the course and outcome of the pilot auction held in December, it is worth recapping the main principles of the new RES support scheme, launched by that first auction.

Impressions after the first auction

Numerous controversies arose around the first pilot auction for the renewable energy sources ("RES"), which the President of the Energy Regulatory Office ("ERO") was obliged to carry out still in 2016. Narrowing the auction down to limited types of RES installations (only 2

Key issues

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- How long will you get support?
- Stable support but flexible support scheme
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"technological baskets" for the existing migrating installations and 1 "basket" for new projects) caused discontent of the investors whose projects were left out of the auction. The unclear rules on the calculation of the state aid received for the projects, which impacted the auction price calculation, caused a lot of confusion and probably had an impact on the results of the auction. At the same

time, without an express clearance of the new support scheme by the European Commission, the risk of finding the scheme incompliant with the EU state aid regulations still exists.

The auction intended for the existing migrating agricultural biogas plants >1 MW was not held because fewer than 3 valid bids had been submitted by the participants. (It is unclear whether indeed the operators of big biogas plants were not interested in migrating to the new system, or whether the bids were not submitted because of technical issues.)

Under the successfully concluded auctions, the option to migrate to the new support scheme has been exercised by:

- 7 agricultural biogas plants ≤1 MW from the PGB group; and
- 49 other installations ≤1 MW in Basket 3 (mainly small hydropower plants).

All the successful biogas plants offered the auction price of approximately PLN 500/MWh (approximately EUR 114/MWh), whereas the remaining successful installations competing in Basket 3 offered prices ranging from PLN 30/MWh to PLN 468/MWh, which suggests that some investors, whether intentionally or not, decided to sell energy below the prices they could have obtained selling the energy on the market.

Similar doubts as to the bankability of some projects may emerge with regard to new RES projects that won the auction in Basket 7 for installations ≤1 MW (the so-called other small RES installations, in which mainly PV projects ≤1 MW were competing). Under the 84 projects that won the auctions, the prices ranged from PLN 253.5/MWh to PLN 408.8/MWh.

Much controversy surrounds the emerging reports about investors who had been unable to submit bids due to technical problems with access to the auction platform. Depending on the source of the access problems, it cannot be ruled out that some of these unfortunate investors would attempt to challenge the validity of the auctions or seek compensation for the losses incurred.

The entire RES market will now be watching closely the further developments and the progress of the projects that had been granted support under the pilot auction. The owners of the projects who based their offers on solid financial models, having the guaranteed stable 15-year support, will probably not have any problems with financing the construction of the projects. It is also interesting that a large proportion of the successful projects are grouped into portfolios comprising a few, or even a dozen or so, projects

owned by the same Polish or foreign investors. Thus, interesting offers may emerge on the market for investors or finance institutions that get involved only in projects of a certain minimum size.

Two parallel support schemes

The legal framework for the auction-based RES support system was introduced at the beginning of 2015 by the Act on Renewable Energy Sources (the "**Act on RES**") and was substantially amended in December 2015 and June 2016¹. Under the Act on RES, auctions are to be the basic and target support system for RES installations, which is to ultimately replace the existing scheme based on green certificates².

The auction-based system is the exclusive scheme for new RES projects (i.e. RES installations that will begin producing energy after the conclusion of a relevant auction (the "**New RES**"). The lawmakers did not, however, decide on a complete and immediate end to the green certificates ("**GC**") system. Subject to certain modifications and exclusions, the green certificates system will continue functioning for a limited time – in relation to "existing RES installations", i.e. RES installations that began producing energy before 1 July 2016 (the "**Old RES**").

Consequently, two RES support systems, the "old" one and "new" one, will for a while function at the same time, independently of each other. However, importantly, the Act on RES provides for the possibility of the Old RES operating under the GC system to migrate to the new system (with respect to full or part of their generation capacity).

How is the new support system organized?

Contrary to the green certificates scheme, where equal

¹ The Act on RES was adopted on 20 February 2015 and published in the Journal of Laws on 3 April 2015 (Journal of Laws of 2015, item 478). The Act on RES was subsequently amended several times, in particular by an Act of 29 December 2015 and an Act of 22 June 2016.

² The current RES support system is based on two main pillars: (i) a system of tradable property rights arising under certificates of origin (so-called "**green certificates**") issued for every MWh of energy produced from a RES installation, and (ii) mandatory purchase of energy produced in RES installations by the suppliers of last resort (now: obliged suppliers) at a regulated price. Pursuant to a recent amendment to the Act on RES, as of 1 January 2018 the second pillar of the existing support (i.e. the mandatory offtake) will cease to apply to projects above 0.5 MW of installed capacity.

support was available for every MWh of energy produced by a RES installation, under the new rules, the support is available only to those RES projects that are successful in a competitive auction.

In a relevant auction, the RES operators will submit bids offering to sell energy from RES for a given price (the "auction price"). The support will be granted to the lowest bidders (until the quantity or value of the electricity specified in the announcement of the auction is exhausted) in the form of a guaranteed offtake for auction price (for RES projects < 500 kW) or quasi-contract for difference model (for RES projects ≥ 500 kW).

In the bid, each investor must specify, among other things, a specific RES project, auction price and the volume of energy planned to be produced in further calendar years of the period of support. The auction price may not exceed the technology-specific reference price, i.e. the maximum price in PLN per MWh, determined annually by the Minister for Energy. (Bids exceeding the reference price are rejected.)

Auctions are to be held at least once a year in electronic form via an Internet Auction Platform. Auctions are conducted separately for:

- New RES,
- modernised New RES,
- migrating Old RES³, and
- modernised migrating Old RES.

Furthermore, each of the auctions is to be conducted separately for large (>1 MW of installed capacity) and small (≤ 1 MW of installed capacity) RES installations. Finally, auctions are to be conducted separately for several overlapping "technological baskets" (created by reference to several different criteria, i.e. the installed electrical capacity factor of a given installation, volume of CO₂ emissions, legal and organizational form of business activity, and natural resources used to produce energy, etc.). This means that theoretically 56 separate auctions can be organized for RES installations.

Technological baskets

Pursuant to the Act on RES, the auctions are to be conducted separately for 7 technological baskets:

- **"Basket 1"** - installations with a utilisation rate of total installed electricity production capacity, regardless of the source of origin, higher than 3,504 MWh/MW/year,
- **"Basket 2"** - installations utilising the biodegradable part of industrial and communal waste, of plant or animal origin, including waste from waste processing plants and waste from water and sewage treatment plants, in particular sewage sludge, pursuant to the regulations on waste as regards qualifying part of the energy recovered from the thermal treatment of waste,
- **"Basket 3"** - in which the emission of CO₂ is not higher than 100 kg/MWh, with a utilisation rate of total installed electricity production capacity higher than 3,504 MWh/MW/year,
- **"Basket 4"** - by the members of an energy cluster,
- **"Basket 5"** - by the members of an energy co-operative,
- **"Basket 6"** - utilising only agricultural biogas to produce electricity,
- **"Basket 7"** - other than mentioned above.

The division into technological baskets is not entirely clear and, except for Basket 6, does not expressly refer to the type of RES technology. As a result, certain RES installations (e.g. hydro power plants) can "fit" in more than one basket and it cannot be unequivocally determined what types of projects will compete against each other in a given basket.

The maximum quantity and value of energy from RES that can be sold in auctions in a given year is determined separately for each basket each year by an ordinance of the Council of Ministers for the following year.

There is no obligation to carry out auctions for all the baskets. The allocation of the volumes between the baskets

³ Except for: (i) multi-fuel fired installations (excluding dedicated multi-fuel fired installations), (ii) hydropower with a capacity above 20 MW, and (iii) biomass/ bioliquids/ biogas installations with a capacity above 50 MW (excluding high-efficiency co-generation units with a maximum thermal capacity in co-generation mode not higher than 150 MWt).

is at the sole discretion of the government. As a result, some baskets may be left "empty", even for several years. For instance, according to the draft auction allocation for 2017, volumes are to be allocated to only 11 out of 56 baskets for existing and new RES projects.

Draft auction allocations for 2017

As regards 2017, the draft ordinance on planned auctions announced in November 2016 proposed allocation between the baskets, which in the opinion of the authors of the draft shall allow the construction of:

- agricultural biogas plants -approx. 30 MW of installed capacity of new projects;
- dedicated biomass firing installations - approx. 100 MW of installed capacity of new projects;
- hydro power plants - approx. 10MW of installed capacity of new projects;
- photovoltaic power plants -approx. 300 MW of installed capacity of new projects;
- wind power plants -approx. 150 MW of installed capacity of new projects.

As regards the large Old RES migrating to the auction system, the only auction is to be conducted for hydro power plants.

Because the division of baskets is not transparent and some RES technologies can be assigned to more than one basket, and different types of projects may be forced to compete against each other, the actual allocations with regard to particular RES technologies may differ from the assumptions made by the government.

The above-mentioned allocation plan is a proposal only, and therefore may change.

What support will you get via auctions?

RES projects < 500 kW

A producer of energy from RES with an installed capacity lower than 500 kW who wins an auction is entitled to support in the form of guaranteed offtake for the auction

price: a local energy trading company with the highest volume of energy sold to end consumers (the so-called obliged supplier) is obliged to off-take the energy from the successful RES installation at the (fixed) auction price, in the amount specified in the bid submitted in the auction, based on bilateral contract signed with the obliged supplier.

RES projects ≥ 500 kW

A producer of energy from RES with an installed capacity not lower than 500 kW who wins an auction is entitled to cover the so-called "negative balance" (i.e. the difference between: (i) the net value of the sales of electricity produced in RES and sold in a given month, calculated as specified in the Act on RES and (ii) the value of that electricity determined on the basis of the auction price) in settlements with the state-owned entity responsible for carrying out the settlements of the negative balance (the Renewable Energy Settlements Operator). The funds for the activity of the Renewable Energy Settlements Operator are gathered from the RES payments made by obliged entities.

The individual auction price is subject to annual indexation by the CPI index during the entire period of support.

If in a relevant month the balance is positive, it should be settled with a future negative balance. Such settlements of a positive balance must be made until the end of the support period. If a positive balance is not settled by the end of the support period, it must be returned in six equal instalments, starting from the end of the support period.

Despite the lack of a guaranteed offtake price, the scheme offers a rather stable and bankable model, assuming the RES operator will be able to sell at the level of "market average". The auction system also offers attractive alternative to the unpredictable green certificates scheme for operators of Old RES, provided that the regulator announces separate "migration" auctions, allocates sufficient energy volume to such auctions and that a given Old RES wins an auction.

Are there any penalties for violating auction regulations?

The obligation of a producer who "won" an auction to produce electricity from RES is settled after the end of each three full calendar years in which support was granted, and after the end of the period of support.

If the project fails to produce the electricity in an amount higher than or equal to 85% of the amount specified in the winning bid in the relevant three-year settlement period, the producer is subject to a fine calculated as 50% of the product of: (i) the auction price and (ii) the difference between the energy that was supposed to be produced and energy that was produced by the RES installation.

However, the biggest risk applies to RES projects within Basket 1 or Basket 3, which are qualified by the minimum electrical capacity factor (i.e. 3504 MWh/MW/year). The RES producer whose bid wins an auction within one of these baskets and who does not achieve the installed electrical capacity factor (i.e. 3504 MWh/MW/year) in the period it was eligible for support, will be required to return the state aid it obtained by way of an auction. The Act on RES provides for a narrow catalogue of circumstances not attributable to the producer, in which the limitations in production are considered in favour of the producer. There is no clarity as to when the capacity factor achievement should be tested or how the return of the state aid should be calculated. (Pursuant to the auction by-laws, the capacity factor will be verified separately for each year already at the stage of verification of the auction bid; however, the President of the ERO is entitled to carry out independent control of the achievement of the electrical capacity factor at any time.).

How long will you get support?

The period of support is determined every year separately with regard to all the auctions that are to take place in the relevant year, in secondary regulations (it cannot be longer than 15 years). The period of support for a RES installation that won an auction is calculated from the date of sale of electricity for the first time after the date the auction is closed.

With respect to existing RES installations migrating from the green certificate system, the period of support received under the green certificates system should be included.

Pursuant to the Act on RES, the auctions are to be organized by 30 June 2021. It is unclear how the RES support system is to be organized after that date.

Stable support but flexible support scheme

Although support, once granted, offers solid and stable conditions (fixed period of support, foreseeable income stream, solid contractors, and indexed prices, etc.), the scheme through which the support is granted is designed in a very flexible way, allowing the government full discretion to decide, by means of secondary regulations, on the volumes, values and directions of support granted in a particular year.

In particular, the following issues are to be regulated by way of secondary regulations:

- maximum volumes and budgets for energy to be sold by auction (and the basket allocation) and the order in which auctions are to be held (*ordinance of the Council of Ministers to be issued by 31 October of the preceding year*);
- the reference prices and the period of support (ordinance of the Minister of Energy issued no later than 60 days before the start of the first auction in the relevant year);
- the rules on calculation of the value of state aid (*ordinance of the Minister of Energy*);
- the detailed conditions of emergency auctions (*ordinance of the Minister of Energy*);
- date of the auction (announcement of the President of the ERO made no later than 30 days before the start of the auction).

No long-term commitment with respect to volumes for future auctions is the main headache for developers and investors with pipeline RES projects. Also the lack of clarity with respect to the reference prices and length of support in future auctions makes future investment decisions more difficult. However, this should be less challenging once the government publishes the Energy Policy until 2050 and, within it, the desired energy mix for Poland, which is expected in 2017.

Reference prices

There are different reference prices determined for different RES technologies (not corresponding to the technological baskets), separately for installations ≤ 1 MW and >1 MW, and separately for new and modernized RES installations. The following reference prices were determined for 2016:

- for large on-shore wind installations - 385 PLN/MWh, and for small ones - 300 PLN/MWh;
- for off-shore wind installations - 470 PLN/MWh;
- for agricultural biogas installations - 550 PLN/MWh (for small and large ones);
- for installations utilising biomass, biogas or agricultural biogas in a dedicated multi-fuel fired plant - 310 PLN/MWh.

The reference prices have not been determined for 2017 yet.

When determining the reference prices, the Minister of Energy should consider a number of factors, in particular: the material technical and economic parameters of the functioning of the RES installation, the capital expenditures incurred during the period of preparation of the project and its construction together with the necessary technical infrastructure, the operating costs and additional capital expenditures incurred during the operating period when the RES installation is subject to support mechanisms and instruments, and the costs of equity.

Are there any other formal requirements?

Old RES migrating to the auction system from the green certificates system are exempt from pre-qualification.

Any new RES project intended for an auction must the complete pre-qualification procedure carried out by the President of the ERO. During pre-qualification, the investor must evidence the ready-to-build status of the RES project and show the schedule of works and costs for the construction. A certificate of admission to an auction is issued within 30 days of the date an application is submitted and remains valid for 12 months from the date of issue.

Furthermore, a deposit is required in the form of a bank guarantee or cash deposit of **PLN 30 per kW** of the installed capacity of the RES installation put to auction. The deposit is returned within 60 days of the date of the first production of electricity from the RES installation that won the auction, or within 14 days of the date the auction closes with respect to installations that were not awarded support.

New RES installations that "win" an auction must begin producing electricity by a prescribed deadline, which is:

- 24 months after the closing date of the auction - in the case of PV installations
- 72 months after the closing date of the auction - in the case of off-shore wind farms; and
- 48 months after the closing date of the auction - in the case of any other RES installations.

Planned amendments

According to market rumours, yet another amendment to the Act on RES is planned probably for Q1-Q2 2017. Although there are no clear indications as to the scope of the potential amendment, it may be used to fine-tune the auction regulations, introduce more precise basket definitions and qualification criteria and implement the lesson learned from the first pilot auction.

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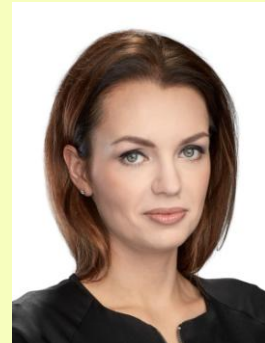
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