

The Spanish Government approves Royal Decree 413/2014, on electricity generation by means of renewable, cogeneration and waste facilities

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This document briefly describes the main novelties introduced by Royal Decree 413/2014, which were already anticipated by some of the regulations passed by the Government within the major energy reform being conducted. Assessment of the actual impact of all these measures for the renewable energy facilities will have to wait until approval and publication of the Ministerial Order approving the values that will be used for the calculation of remuneration parameters.

The Cabinet has approved on June 6, 2014 Royal Decree 413/2014 "on electricity generation by means of renewable, cogeneration, and waste facilities" (hereinafter referred to as the "**Royal Decree on Renewables**"), published in the Official Journal of Spain on June 10, 2014, and in force as from June 11, 2014. The approval of the Royal Decree on Renewables is part of the steps that are still pending within the deep energy reform that is being carried out by the Spanish Government.

As anticipated in prior client briefs, Royal Decree-Act 9/2013 on Urgent Measures to Guarantee the Financial Stability of the Electricity System ("**RDA 4/2013**") and the Electricity System Act 24/2013 ("**Act 24/2013**") provided for a specific legal and financial scheme to be established by a further Royal Decree and Ministerial Order, which would contain the specific remuneration applicable to all renewable energy facilities accredited under Royal Decree 661/2007, of May 25, 2007, on the generation of electricity under the special regime ("**RD 661/2007**") and Royal Decree 1578/2008 of September 26, 2008, on remuneration for the generation of electricity using photovoltaic solar technology for facilities after the deadline date for maintaining the remuneration for such technology under RD 661/2007. While RDA 4/2013 and Act 24/2013 had already

established that the reward for renewable energy facilities shall be based on the electricity market price supplemented when necessary to obtain a "reasonable return on investment" by the so-called "specific remuneration", the calculation of the said "reasonable return on investment" is dependant on certain parameters and values that require additional regulatory development.

We have summarized below some of the main aspects contained in the new regulation:

- The Royal Decree on Renewables confirms that a new remuneration scheme, with a goal of achieving for investors a reasonable rate of return on their investments through the specific remuneration in addition to the electricity market price, will apply for those renewable, cogeneration, and waste facilities that benefitted from a recognized feed-in tariff remuneration as of July 14, 2013. These facilities' rates of reasonable, pre-tax return is set as the secondary market average yield on 10-year Government Bonds for the period of July 1, 2003 to June 30, 2013, plus 300 basis points (that is, 7.398% before taxes).
- The specific remuneration that allows to achieve the reasonable rate of return consists of the sum of (i) the "remuneration to the

investment” consisting of a term per unit of the installed capacity to cover, where appropriate, the investment costs for each standard facility that cannot be recovered from electricity sale in the market, and (ii) the “remuneration to the operation” consisting of a term covering, where applicable, the difference between the operating costs incurred and the income obtained from the participation in the electricity market by a standard facility.

- The calculation of the new remuneration regime will be carried out on the basis of the standard costs and revenue (initial investment, operation, and revenue from the sale of power) that would correspond to a *“standard power plant, over the useful regulatory life thereof and based on the business activity that would be carried out by an efficient and well-managed company.”* The costs and investments imposed by laws or administrative acts that are not applicable to the Spanish territory are excluded from the calculation of this specific remuneration, as well as any costs that are not exclusively linked to the activity of producing electrical power.
- The “reasonable rate of return” on the investment refers to the profitability of the project throughout its full regulatory life: the determination of the specific remuneration applicable to facilities already in operation will take into account the (standard) income those projects already received since they commenced operations. Therefore, if the rates of return obtained so far by the

projects have already exceeded a 7.398% rate of return on the investment, the facility in question will not be entitled to receive any further remuneration henceforth, but only the electricity market price.

- The Royal Decree on Renewables establishes the remuneration scheme and the formulas required to calculate the specific remuneration available to various types of facilities, but it does not state the values that will be used for the calculation of the remuneration parameters and consequently of the specific remuneration of the facilities. Those values are to be included in the Ministerial Order that will approve the remuneration parameters for both standard facilities and certain facilities that produce electrical power from renewable energy sources, cogeneration, and waste, which is currently being processed.

On May 20, 2014 the Government sent to the advisory State Council (*Consejo de Estado*) a draft of the aforementioned Ministerial Order for the Council to issue its report (which is non-binding for the Government). The draft Order sets forth 1,492 different formulas of remuneration for standard facilities, depending on technology, date of commissioning, and project size. It is generally expected that the Order (last step for the final implementation of the reform affecting the renewable energy market assets) will be passed shortly once the State Council has issued its report, possibly by the end of week.

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