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Portugal

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PORTUGAL

Trends and Developments

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In the last couple of years, following the European Union policy and directives regarding the energy sector and its internal market, aimed at achieving carbon neutrality by 2050, the market, legislation and regulation of the energy sector in Portugal has been experiencing remarkable changes.

The Portuguese government's policy for the energy sector is currently set out in the National Plan for Energy and Climate 2020-2030 (PNEC 2030). The approach described in the plan establishes the means of achieving the European Union goals and commitments assumed by Portugal regarding the increase of energy generated by renewable sources, energy efficiency, decrease the level of energy prices for the consumer, without losing sight of the economic rationale. The main objectives of this plan are to:

- contribute to decarbonise the Portuguese economy;
- prioritise energy efficiency;
- strengthen the commitment to renewable sources of energy and reduce the country's energy dependence;
- ensure security of supply;
- foster sustainable mobility;
- develop an innovative and competitive industry; and
- ensure a fair, democratic and cohesive transition.

Following a significant standstill mostly due to the economic crisis of 2012 resulting from the IMF/ECB/EU intervention, over the last year Portugal has witnessed significant change in the energy sector (both legislative and commercial) with the country's strategy focussing once again on renewables (without Feed-in Tariffs), new investment in R&D, massive electrification of consumption, the fostering of green hydrogen and market liberalisation, allowing the entry on the scene of new players.

Renewables

Portugal's current electric framework is characterised by a predominance of renewable sources with the goal of achieving carbon neutrality by 2050. The Portuguese Deputy Minister for Energy stated in 2019 that "in the next ten years the country aims for 80% of its electricity production to come from renewable sources. More than realistic goals, these are necessary; I

would say that we have no alternative. This scenario also generates more wealth and jobs in the country."

The PNEC 2030, together with other sectoral policies and strategies, translates the European Union commitments by setting a target of 47% renewable energy and a 35% reduction in primary energy consumption. Moreover, it highlights the importance of promoting sustainable mobility through the decarbonisation of public transport and maintaining a safe and reliable supply system by optimising all energy infrastructure.

All these efforts are a development of the path Portugal has been treading with recognised notoriety worldwide for its remarkable achievements in 2019: not only did the country reach the 100% renewable energy provision goal in December 2019, but it also set a world record in terms of price per MWh through its first solar auction that took place in the summer of that same year.

Another big trend that is emerging in Portugal is the promotion of decentralised production and self-consumption of energy generated from renewable sources. With the publication of Decree-Law No 162/2019, the Portuguese government has set out a new legal framework allowing the emergence of prosumers. The creation of these mechanisms allows citizens as well as public or private entities to produce, consume, share, store and trade the energy produced, thus actively participating in the country's energy transition. This plan will be accompanied by a programme to disseminate information and support the implementation of self-consumption projects, in order to reduce information asymmetries and support businesses, municipalities and citizens in their development.

Furthermore, there is a lot of potential for the Energy sector to become a new Portuguese economic hub, like the tourism and start-up sectors in the past.

The 2019 New Portuguese Framework

There have been some amendments to the Portuguese legal framework for the electricity sector, namely Decree-Law No 76/2019 (the first major systematic revision since 2012).

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Prior to the enactment of this legal novelty, requests made for injection points where grid capacity was unavailable or insufficient would be made by draw. The procedure for the attribution of connection points and licensing of new projects now includes a competitive electronic auction process, through which interested players may bid on lots for the granting of grid capacity.

Another option introduced, for situations where grid capacity is not available, is to enter into an agreement with the grid operator by providing the necessary funds and investments to reinforce the grid so as to connect the project.

Moreover, in an attempt to overcome the scarcity of grid capacity and to put a halt to licence trading, the amendments included a prohibition on transferring the grid capacity reserve and the associated production licence until the project is deemed able to enter into commercial operation.

The first solar auction took place in July 2019 and attracted not only considerable interest but also significant media coverage due to the fact that it resulted in a new world record bid in terms of price per MWh – being one of the lowest tariffs to date and representing a 67% discount compared to the base value.

Following the success of the first auction, the second auction has already been announced, with the final bidding scheduled for the end of August 2020. Despite of the abrupt detrimental effects the COVID-19 pandemic has had on the worldwide economic markets, the Portuguese government is still expecting considerable levels of investor interest in this auction, allowing for the possibility of a slight decrease given the circumstances.

On the whole, the auction and its respective proceedings will be very similar to the one held in July 2019, however, a relevant development must be mentioned, which is the possibility of submitting projects providing storage options, with a new remuneration scheme. Regarding the existing conditions that characterise this very context, Portugal provides very favourable regulatory conditions for investors, with a special incentive on the creation of infrastructures with a longer life time, incentivising participants to adopt a long-term view as regards their ROI.

It is also important to note that the first auction attracted the attention of foreign investors who placed a large number of the bids. The low tariffs offered at the auction have set a precedent for future projects, making investors readjust business and financial models to secure revenues. Moreover, a large number of capacity attributed to newcomers to the Portuguese market, such as companies from France and the United Kingdom, overcoming major players who have been dominating the market in the past years and even decades.

Guarantees of Origin/Green Certificates

In February 2020, through Ordinance No 53/2020, Portugal adopted the necessary legal steps towards the creation of a mechanism to issue green certificates. While this was already foreseen in the Portuguese legislation in 2010, the legal framework for these certificates has been subject to several amendments regarding the entities bearing power to issue them. With the publishing of this Ordinance regarding the amounts to be charged by the issuing entity of green certificates for the services rendered, the missing piece of the puzzle was found and there are currently conditions in Portugal for the issuing of Guarantees of Origin. The main purpose of these certificates is to provide evidence to the final consumer of the share or amount of energy from renewable sources in the energy mix of a given supplier, not only encouraging the consumer to make a more environmentally conscious decision, but also allowing market players to promote their services more easily.

Self-Consumption and Renewable Energy Communities

The introduction of the legal framework applicable to small production units gave rise to the emergence of prosumers, that is small producers that generate electricity for self-consumption and sell the surplus. This is been possible since the installation of smart metering systems became a reality, as well as the increased development of smart grid systems around the country.

With the enactment of the self-consumption legal framework, multiple businesses engaging in such activities have benefited from support. More importantly, it is also allowed self-consumers and other participants in renewable energy projects to incorporate a legal entity (renewable energy communities (RECs) by means of a SPV or, more precisely, a joint venture) for the production, consumption, sharing, storage and sale of renewable energy.

These self-consumption projects are able to trade the surplus of energy produced:

- through a market participator, with the role of an aggregator;
- through a market facilitator; and
- in an organised market or through bilateral contracts.

The RECs were created to provide centralised operational management of the respective projects, while also allowing the participation of players that have better financing and know-how to carry out the projects, since the development of these kinds of projects would be highly unlikely without this type of support.

This new framework will push market players to develop new strategies and business models to carry them out, as well as bringing new players onto the scene.

Energy Efficiency

In December 2018, the revised Energy Efficiency Directive (EU Directive 2018/2002 of the European Parliament and of the Council of 11 December 2018) entered into force, setting a communitarian energy efficiency target of at least 32.5% by 2030.

One of the primary goals of the PNEC 2030 is to prioritise and boost the development of energy efficiency projects. The government has set the following measures to achieve this in the next couple of years, including:

- ensuring the improvement of efficiency of energy consumption in the various economic sectors;
- reviewing the legal framework for energy management and efficiency and strengthening the monitoring systems;
- promoting the rational use of energy among end users;
- supplying the energy sector with qualified professionals in the area of energy efficiency;
- simplifying procedures and reorienting and strengthening funds and funding programmes;
- encouraging R&D in energy efficiency; and
- promoting increased penetration of more efficient equipment and products through the renewal of existing ones.

The promotion of energy efficiency measures is achieved through various instruments. Since 2006, Portugal's Energy Services Regulatory Authority (ERSE) has been implementing the Consumption Efficiency Promotion Plan (PPEC) in the electricity sector. This is a competitive mechanism to support measures that make a real contribution to reducing consumption.

Under the PPEC, incentives are awarded for the promotion of measures aimed at improving efficiency in electricity consumption through actions carried out by suppliers, operators and organisations that promote and protect the interests of electricity consumers in Portugal. The actions result from specific measures proposed, which are subject to a selection process, the criteria for which are defined in the Rules for the Consumption Efficiency Promotion Plan. This process allows for the selection of the most promising measures for energy efficiency to be implemented by the promoters, considering the amount which is available in the PPEC annual budget, which is approved at the start of each regulation period for each one of its years.

The implementation of the measures approved by the PPEC 2017-2018 was carried out until the end of 2019. The 75 measures supported by that version were selected on the basis of a competitive procedure, with 224 measures being submitted.

The implementation of energy efficiency in buildings promises to be one of the major developments in the years to come.

Hybridisation

Hybridisation was also one of the recent significant developments. Facilities may now produce electricity from different primary sources in the same infrastructure and through the same connection point on the grid. This allows for an increase in generation and a greater energy mix (however, different technologies remain subject to different licensing). Combining wind and solar has already attracted interest from major players in the industry. It would allow the projects to maximise output and efficiency given the different availability of the sources, without requiring more infrastructure investments from the network operator.

However, in the context of capacity attributed by means of an auction, the possibility of hybrid electricity generation continues to be available as long as the obligations arising from that auction are strictly complied with.

Hydrogen

The Portuguese government has announced its strong commitment to maximising the renewable capacity installed by developing large-scale projects for the production of hydrogen, which also benefit from certain infrastructure which already exists, notably pipelines. A cluster of companies is being formed to realise a fully dedicated large-scale solar pv plant (1 GW), and a large hydrogen electrolysis plant, both located to the south of Lisbon, in Sines, to be operational as early as 2023. This is intended to be the first of several projects which will allow the future use of idle renewable capacity through an alternative process of storing energy and introducing that energy back in the market as "green fuel".

Recently, in May, the Portuguese Ministry of Environment and Climate Change published a preliminary National Hydrogen Strategy, under public consultation, available to the market, looking forward to hearing any contribution the players could have in connection with that strategy.

Portugal has favourable conditions for the development of a hydrogen economy ecosystem, namely the existence of a modern natural gas infrastructure, competitive renewable electricity production prices and an excellent geographic location for exports.

The government strategy is part of the promotion of an industrial policy surrounding hydrogen based on the definition of public policies that guide, co-ordinate and mobilise public and private investment in projects in the areas of production, storage, transmission and consumption of renewable gases in Portugal. Moreover, there are several main initiatives that will see further development in the next couple of months, such as:

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- the setting up of a mechanism to support and encourage the production of green hydrogen;
- the regulation of hydrogen in the gas infrastructure (the gas legal framework is set to be amended shortly);
- the setting of targets for hydrogen incorporation;
- the provision of financial support for hydrogen-based projects; and
- the incorporation of a collaborative lab (COLAB) for R&D for the hydrogen supply chain and new industries.

The government places hydrogen at the centre of its strategic planning for the 2030 horizon as regards decarbonisation, making it possible to achieve the objectives and targets set in strategic economic sectors that currently have few technological alternatives and where electrification is not the best option.

A policy framework and significant measures will be adopted shortly in the legislative and regulatory field, in R&D and in the promotion of projects which sponsor green hydrogen.

Lastly, it is worth mentioning that the assets producing renewable electricity and trading of electricity with the supplier of last resort (“CUR”), namely wind or solar pv, which are operational and benefit from a Feed-in Tariff, can be fully or partially converted to green hydrogen production by adding the appropriate technology (electrolysis plant) at the location where the installed and licensed powerplant operates. This mechanism will continue to be studied for the remainder of 2020 but the shift to hydrogen production would be through a sole purchase scheme, where the owner of the asset receives a payment equivalent to the net present value (“NPV”) of expected cash-flows equivalent to the duration of the current Feed-in Tariff. In the long term, this mechanism is aimed at making these promoters shift to 100% production of green hydrogen, by which time they will be able to access other support mechanisms.

Storage

There have also been amendments to the Portuguese legislation which are aimed at creating a new market niche in this sector: storage of electricity. It was through the aforementioned Decree-Law No 76/2019 that storage activity was better developed in the Portuguese legal system. While it requires further legislation to be implemented, it marks a step towards the opening of the market to the energy storage options, which until lately has been nearly impossible. Moreover, the experience gathered from the Gracióllica project (located in the Azores archipelago), which uses a combination of solar and wind power and has a storage facility, will bring a new focus and investment in storage options, allowing for more efficient facilities in the future.

At present, storage activity carried out autonomously is subject to a storage licence (like production and operation licences).

Furthermore, it should be noted that the solar auction set to take place in August 2020 has established a specific remuneration scheme for those players which intend to store energy produced in their powerplant.

Market Liberalisation

The full transition to a liberalised market is still a work in progress. The starting point was the publication of EU Directive 2003/55/EC which established the ground rules for the internal energy market and which has consequently facilitated the opening up of the market, giving all customers the right to choose a supplier. After being pushed back several times, the process of phasing out end-user regulated tariffs is still under way. Decree-Law No 75/2012 approved the timetable for the gradual phasing out of such tariffs for normal low-voltage electricity consumers. After numerous delays, the deadline for the end of all regulated tariffs is set for the end of 2025. In the meantime, however, transitory tariffs with a gradually increasing component will be applied by ERSE.

For natural gas, since the beginning of 2010 all consumers have had the right to choose their supplier freely. The process of natural gas’ market liberalisation has already allowed all large consumers to join the free market. Additionally, most industrial consumers have opted for more favourable conditions offered by market traders and the evolution of the residential customer segment has shown a very significant and growing adherence to offers in the market.

With the goal of liberalisation in mind, PNEC 2030 already anticipates new challenges that might arise in this context, as given the existence of several significant changes, the responsibility for ensuring security of supply is shared by the various players, and the role of each will therefore have to be redefined. In this new model, all agents, including producers, operators, suppliers, customers and political and regulatory institutions are key elements in the process of ensuring supply efficiency and security.

As such, the Portuguese electric sector focuses its efforts on the end-consumer, making sure that all relevant information is available and that consumers have a free choice available to them, facilitating the possibility of changing supplier whenever the customer sees fit.

The legal framework applicable to self-consumption already envisages the transition to a fully liberalised market, setting the general process for determining the prices freely by each supplier and not by the Regulatory Authority for Energy Services (ERSE).

Although the Feed-in Tariff scheme was reintroduced, it was under special conditions, at significantly lower prices, and provided that such remuneration is either secured through a public auction or in the context of overpowering, or for projects using hybrid production to combine a different primary energy source to an existing powerplant.

Thus, it is expected that market aggregators will carry out the purchase and sale of electricity generated by powerplants. Even though this legal figure was first foreseen in the Portuguese legal system in 2012, no entity has yet carried out such activity. Recent amendments enacted in 2019 determined that that activity shall remain subject to a specific licence to be attributed by means of a public tender. As soon as the tender is launched, it is expected that new entities will take on that role.

Electric Mobility

Electric mobility – green transportation – is one of the most newsworthy themes worldwide and, as such, it should be no surprise that it assumes an important role in Portugal's energy development goals. As the transport sector is one of the most important sectors for GHG emissions (due to its size and necessity), Portugal has identified concrete measures to progressively eliminate fossil fuels in this context.

The Electric Mobility Network, an integrated network linking more than 1,000 charging stations, managed by MOBI.E, enables electric cars to recharge using a simple card. The Portuguese government has been covering some of the costs associated with the usage of electricity grids for electric mobility and even providing a very competitive framework of incentives for the purchase of electric vehicles, as well as exemptions from vehicle tax, autonomous taxation and other applicable taxes.

Considering the overall tendency towards sustainable and shared transport, the focus on electric mobility and advanced biofuels should be the most cost-effective decarbonisation option in the transport sector, but other mobility alternatives will emerge including low carbon vehicles such as hydrogen powered vehicles.

For the transport of goods, Portugal's transition to decarbonisation encompasses not only the use of alternative fuel sources (such as electricity and hydrogen) but also the optimisation of routes for both small and large vehicles. At the maritime level, the investments will be directed towards new forms of energy while simultaneously prioritising transport for short distances and reinforcing interoperability with commercial ports.

Additionally, given the existing issue of urban congestion, investment in a good quality and energy-efficient public transport system is seen as one of the essential steps towards not only achieving environmental targets but also improving the quality of life of a large part of the population. In order to promote the increase of the high-capacity public transport network and to maintain the expansion of these systems, Portugal has already started to work on numerous initiatives, such as: the expansion of Lisbon and Porto's metro infrastructures, reinforcing the charging networks in both public and private buildings as well as the creation of a charging network for electric buses, night shipments and complementary shipments at terminal stops or parking areas, covering public transport and tourism services.

At present, renewable sources account for 10% of the total energy utilised in Portugal's transport sector, however, the PNEC 2030 sets the ambitious goal of doubling this percentage by that very same year.

Regulatory Sandboxes

At the beginning of March 2020, the Portuguese government, through Resolution No 29/2020 of the Council of Ministers, established general principles for the creation and regulation of technological free zones (ZLT), a regulatory sandbox project. Portugal intends to adopt a flexible and innovative approach to new technologies, businesses and products in the energy field in order to foster innovation and increase the attractiveness of Portugal as a hub for testing. This will be done through the creation of digital innovation hubs as collaborative networks that include specific competence centres brought to the table by companies, for their development, testing and experimentation. The goal of the government is – in collaboration with regulators, universities and market players, among others – to set the conditions to gradually create new business models and solutions in the energy field. The Internet of Things, the development of smart cities and the enhancement of the smart grid are some of the topics that ought to be considered in these sandboxes. It is expected that by the end of 2020/early 2021 the government will focus on this new reality.

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TELLES Advogados is a full-service law firm with national coverage and a local presence in the two main cities of Portugal: Lisbon and Porto. The firm is represented by a range of departments that work in many areas of expertise, namely, finance, projects, corporate and M&A, tax, energy and natural resources, real state and litigation. The finance, projects and capital markets team is comprised of eight members: one part-

ner, four associates and three trainees. In addition, other practice areas involved in blockchain work are digital, privacy and cybersecurity; tax; and litigation/arbitration. In the last couple of years, the firm has built on its sustained growth and has been achieving higher presence in international markets. It has also gained the necessary expertise to provide services regarding new technologies and business models.

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