

New rules for Ukraine's green energy: Feed-in Tariff Auctions, the unification of Power Purchase Agreements

In recent years, Ukraine has created favorable conditions for the development of green energy, most specifically by means of establishing the highest feed-in tariff among countries on the European continent. Moreover, the tariff was fixed in euros, which protected investors from Ukraine's currency fluctuations.

As a result, renewable energy generation has been rapidly developing in Ukraine. As of the beginning of 2019, the total renewable energy sources in operation amounted to 2.2 GW (gigawatt). By the end of 2019, another 1.4 GW capacity is expected to come into operation, with the majority being solar and wind power plants (SPPs, WPPs).

Over the last four years about 2 billion euros have been invested in the Ukrainian renewable energy sector.

As of today, renewable energy accounts for only 2% of the total amount of energy produced in Ukraine. However, the cost of electricity purchased by the green tariff is several times higher than that of traditional energy sources. As such, the green energy sector accounts for 9% of all money in the energy market. Furthermore, Ukraine's outdated electric grid lacks the technical capacity to accept and distribute the energy generated by newly built generating facilities.

Accordingly, in April and May 2019, the Ukrainian government introduced a set of new rules, which will significantly affect both future and current renewable energy generation businesses, as well as their lenders and investors.

The two regulatory and legislative acts in question are:

- Law of Ukraine "On Introducing Certain Changes to Laws of Ukraine Regarding Ensuring Competitive Conditions for Generation of Electricity from Alternative Energy Sources" No. 2712 dated 25 April 2019 (the **Auction Law**). The Auction Law replaces, with some exceptions, the framework of a fixed guaranteed feed-in tariff, and will be applied to solar and wind power plants with a capacity of more than 1 MW (megawatt) and 5 MW respectively, which constitute the majority of the planned and operational renewable power plants in Ukraine. The Auction Law will apply to the plants commissioned after 2019 (with some exceptions as described below and in the Annex 2).
- The Auction Law effectively establishes three groups of solar and wind power plants (WPPs and SPPs) depending on their eligibility for the current framework: those which will be commissioned by the end of 2019 (current tariff), those commissioned after 2019 (auction tariff), and those commissioned after 2019 but still having the right to the current tariff through a so-called "Pre-PPA" mechanism (see below and Annex 2 for details and clarifications).
- Regulation No. 641 "On the Approval of the Normative Acts Governing the Activity of the Guaranteed Purchaser and the Electricity Offtake under the "Green" [Feed-in] Tariff" issued by the National Energy and Utilities Regulatory Commission (the "**NEURC**"). This Regulation, inter alia, introduced a new form of

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the power purchase agreement (the “**Fixed PPA**”), which becomes mandatory for the renewable energy producers acting under the current framework of a fixed guaranteed feed-in tariff. Auction winners will be signing a different form of a PPA (the “**Auction PPA**”), which is yet to be approved by the NEURC.

Earlier energy legislation introduced an important role of the Guaranteed Purchaser, which is to be founded as a separate state-owned company and will be responsible for the purchase of electricity generated by all renewable energy producers both under Fixed PPAs and Auction PPAs. It is expected, that Guaranteed Purchaser will be established till July 1, 2019. As of today, the function of the Guaranteed Purchaser is performed by the State Enterprise “Energorynok”.

The Regulation also establishes a form of Agreement on the expansion of grid capacity to meet the demands of increased renewable energy generation. This Agreement is to be concluded between the Guaranteed Purchaser and electric power distribution company, governing the basis on which the latter will be compensated for expansion or modernization of its electric grid.

The Auction Law: distribution of feed-in tariffs through auctions, introduction of annual capacity quotas

Under the current legislative framework, the feed-in tariff rate is fixed by law¹. There are currently no restrictions on the capacity of the renewable energy generated in Ukraine, and the electricity market operator is obliged to purchase all renewable energy generated by the market. This has resulted in the rapid growth of construction of renewable energy plants and dangerous imbalances in the national electricity grid. The Auction Law introduces competition to gradually bring down the cost of renewable energy and provides a mechanism to limit the quantity of electricity that may be purchased under the tariff.

Main provisions of the Auction Law

According to the Auction Law, from 2020 energy producers wishing to join the renewable energy market will have to compete for the green tariff at auction. Guaranteed Purchaser will organize the auctions according to a specific Regulation to be approved by the Cabinet of Ministers of Ukraine by 22 August 2019. The State guarantees to purchase all electricity produced by the winner(s) of such auctions. The auction procedure will be mandatory for:

- Solar Power Plants (**SPPs**) with a capacity of more than 1 MW, and
- Wind Power Plants (**WPPs**) with a capacity of more than 5 MW.

Other types of renewable energy plants (such as biomass, hydroelectric, etc.) will sell their electricity according to the existing rules under the Fixed PPAs. The law, however, provides that they may participate in the auction on a voluntary basis.

The winner of the auction will execute an Auction PPA with the Guaranteed Purchaser of electricity.

¹ The current green tariff for plants commissioned in 2019 standing at EUR 0,15 per 1 kilowatt for solar energy, and EUR 0,10 per 1 kilowatt for wind farm (depends on the power capacity, etc.)

It should be mentioned, that Fixed PPAs and Auction PPAs are different mandatory documents. As of today, Auction PPAs have not been adopted. NEURC has to adopt them by August 22, 2019 (*see more details in the next section and Annex 1*).

The new rules do not cancel existing green tariffs for existing WPPs/SPPs

Existing SPPs and WPPs will continue enjoying the current green tariff rate as previously stipulated by law until 2030 if they have already been commissioned or will be commissioned by the end of 2019.

Transitional framework for WPPs/SPPs under the Pre-PPA mechanism

The law allows renewable energy producers to sign Fixed PPAs prior to commissioning of their plants, subject to certain requirements. Such PPAs have been named, accordingly, “**Pre-PPAs**”. The significance of the Pre-PPA is that the tariff rate is fixed as of the date of signing of the Pre-PPA and not as of the date of commissioning of the plant and/or commencement of power generation. Accordingly, existing rules will apply to SPPs and WPPs, which are under development, if they conclude pre-PPAs by December 31, 2019.

The requirements for signing a Fixed Pre-PPA are, in short, as follows:

- 1) Land, interconnection and construction permits should be secured before a pre-PPA is signed.
- 2) The plants have to be commissioned:
 - within 2 years from the date of pre-PPA – for SPPs;
 - within 3 years from the date of pre-PPA – for WPPs.

For your convenience, we have classified all types of renewable energy producers according to these criteria (see Annex 2).

Requirements to participate in power auctions

From 2020, if investors would like to participate in a power auction, they must consider the following:

- 1) Renewable power plants that have already received the fixed green tariff cannot participate in the auctions for the same type of renewable energy. Similarly, plants which have already won an auction would not be able to re-enter the auctions for the same type of energy.
- 2) Auction participants must submit documents which confirm either rights of ownership to, or usage of the land plot on which the project is being constructed.
- 3) A grid connection agreement must have been executed with the regional electric power distribution company.
- 4) In order to participate in the auction, participants must provide an irrevocable bank guarantee in favour of the Guaranteed Purchaser/grid in relation to the Auction PPA. The bank guarantee should cover EUR 5 per 1 kilowatt of planned capacity. This irrevocable bank guarantee will be returned to all participants (including the winner of the auction after the signing of the Auction PPA).
- 5) The auction winner must provide an irrevocable bank guarantee in the amount of EUR 15 per 1 kilowatt to ensure fulfilment of its obligations under the Auction PPA. The auction winner also has to pay the auction platform’s fees. The amount of fees will be determined by the Regulation on the auction procedure to be approved by the CMU by 22 August 2019.

Terms of power auctions

The pilot auctions will take place no later than November 22, 2019. In general, the Auction Law provides for auctions to be held from January 1, 2020 until December 31, 2029. Auctions will be held twice per year with the following deadlines: by April 1 and by October 1. The incentive regime (i.e. the fixed tariff in euro) for auction winners will be valid for 20 years.

Auctions will be held via the electronic trading system “Prozorro”. The format of auctions will be closed-type Dutch auctions (price-reducing).

Auction participants shall submit closed proposals containing the technical proposal (capacity) and the price proposal (eurocents per 1 kilowatt hour). The amount of capacity is important for the size of irrevocable bank guarantee for participants.

The proposed price is the only criteria for determining the auction winner. The participant with the lowest bid price is recognized as the auction winner for the declared capacity.

Price proposal may not be higher than the reference rate of the maximum feed-in tariff for a relevant type of renewable energy. The Auction Law provides that the reference rate will be established by reduction of the current feed-in tariff, starting from 2020:

- for solar plants - by 25 % in 2020, with a further decrease during 3 years by 2,5 % each year;
- for wind plants - by 10 % in 2020, without further reduction.

The Auction Law provides a list of documents that are necessary to be filed by the producer to participate in an auction (see Annex 3).

Annual capacity quotas for new SPP and WPP projects

The Auction Law introduces annual capacity limits (quotas) for all renewable electrical power, which will be distributed according to the results of the auctions during a particular year. Quotas are to be set by the Cabinet of Ministers of Ukraine (CMU) for the relevant year. The annual quota has yet to be set for 2020.

Annual quotas will be divided by type of renewable energy.

The law provides for minimum quotas – not less than 15% for each category:

- solar energy;
- wind energy;
- other types (biomass, biogas, hydro, geothermal energy).

The remaining 55 % will be distributed at the discretion of the CMU.

The law provides for two options of the auctioning of the quotas: either through a separate auction for each type of renewable energy, or through a single, “technology neutral” auction available for all producers. The option is to be selected by the CMU.

The rate increase for the use of local components remains

The auction winners will be able to use the existing benefit of an increased feed-in tariff rate of 5-10% in the event that components of the plant were produced in Ukraine. This applies to power plants commissioned before 2025.

The new standard form of Fixed PPA

General provisions

The new form of the Fixed PPA is mandatory for renewable energy producers that have already received the green tariff and which are going to receive it under the current framework (including the pre-PPA mechanism). The new form of PPA is largely based on the previous form, which was a guideline and not mandatory.

The PPA is concluded between a renewable energy producer and Guaranteed Purchaser. It is expected that the Guaranteed Purchaser will be incorporated by July 1, 2019. As of today, the function of the Guaranteed Purchaser is performed by the State Enterprise “Energorynok”.

The procedure for transfer from the present PPAs to the new form of the Fixed PPAs for existing producers

Existing PPAs, which have already been concluded between renewable energy producers and “Energorynok”, need to be brought into compliance with the new form of Fixed PPA by July 1, 2019.

The producer (which has already concluded a PPA or pre-PPA with “Energorynok”) has to file an application to the Guaranteed Purchaser to amend the PPA, submitting the following documents:

- copy of the Charter;
- copy of the order on the appointment of the director;
- a sample of the signature of the director.

Upon completion of this application process Guaranteed Purchaser, “Energorynok” and producer conclude a tripartite Agreement on the change of the PPA’s parties.

Regulation No. 641 establishes essential terms of Agreement on change of the PPA’s parties as follows:

- “Energorynok” is not responsible for any of the Guaranteed Purchaser’s obligations to the producer;
- “Energorynok” and the Guaranteed Purchaser are not responsible for any obligations of the producer towards its creditors.

At the same time, Regulation No. 641 doesn’t clearly establish any liability for failure to change the PPA. However, taking into account requirements of Regulation and the new laws governing the energy market, it can be assumed that, starting from July 1, 2019, “Energorynok” (the old party to the PPA) will not be able to buy electricity, and, accordingly, the producer would need to conclude a new form Fixed PPA with the Guaranteed Purchaser to continue selling electricity.

The new form of Fixed PPA doesn’t allow agreements between creditors and the Guaranteed Purchaser

According to the previous version of the PPA, the producer’s creditors had possibilities to conclude a direct agreement with “Energorynok” (the “**Direct Agreement**”). The Direct Agreement included an obligation of

“Energorynok” not to terminate the PPA during 120 days from the date of a violation of the PPA by a producer, which provided additional comfort to creditors.

Unlike the previous version, the new PPA doesn't provide the possibility of concluding Direct Agreements between the Guaranteed Purchaser and producers' creditors.

Dispute Resolution

The dispute resolution clause provides for an alternative between Ukrainian commercial courts and an ICC arbitration in Paris, at the discretion of the claimant. It is well-known that complex arbitration clauses may complicate the dispute resolution procedure.

Furthermore, the clause includes a provision whereby in case of simultaneous commencement of litigation and arbitration procedures, both parties must submit an application to the Ukrainian court for termination of court proceedings and in support of the arbitration proceedings. It is difficult to see that, in the case of a conflict, the party initiating litigation would really be willing to cancel it in favour of the other party, which prefers arbitration.

Moreover, Ukrainian law provides for an international arbitration only in case there is a foreign party in the dispute, and, accordingly, if the power plant operator would be a Ukrainian-registered company, international arbitration's jurisdiction may be substantially undermined.

Applicable Law

Ukrainian law should govern the PPA.

Amendment of the Fixed PPA by changes in the law

Requirements of the Fixed PPA can be amended only in the case of legislative changes. The Regulation strictly establishes that changes cannot limit the scope of the producer's rights under the green tariff (which probably aims to mean that whatever changes may be introduced to the Fixed PPA by the law, the original rate of feed-in tariff should not be affected by the changes).

The Regulation also establishes the procedure and time limits for making changes to the PPA. In the event of changes in the Fixed PPA form, the Guaranteed Purchaser should publish the relevant amendments on its website and send a new version of the PPA to the producer.

The producer should provide a new version of the signed PPA to the Guaranteed Purchaser within 1 month from the date that it was sent by the Guaranteed Purchaser. Failing to do this will be interpreted as the producer's will to terminate the PPA.

Overall, the introduction of a uniform, standardized Fixed PPA will provide benefits in terms of standardization, in particular, it would save costs for renewable project analysis, create equal rules for all market players, and provide predictability with regard to changes to the Fixed PPA.

However, the Fixed PPA will lose its flexibility, including the options of creditors to have a direct contractual relationship with the Guaranteed Purchaser. Furthermore, it will make the Fixed PPA more sensitive to the

political influence, as both the regulator responsible for the PPA's form and the Guaranteed Purchaser will represent the state.

Finally, there remains an issue of the legality of compulsory conversion of all existing Fixed PPAs into the new standard Fixed PPAs. Concerned investors may potentially claim the government is imposing less favourable conditions for investment and therefore potentially violating the guarantees provided by a relevant bilateral investment treaty.

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Annex 1.

Pilot auction: the timeline

The pilot auction will determine the winners eligible to connect to the grid during 2020.

April 26, 2019	Regulation No. 641 was adopted (PPA's form was approved)
May 22, 2019	Auction Law entered into force <i>"Energorynok" performs as Guaranteed Purchaser</i>
July 1, 2019	Start of the New Electricity Market Expected date of incorporation of the Guaranteed Purchaser
August 22, 2019	Deadline for the adoption of Regulation on the procedure of conduction of the auction (by CMU) Deadline for the adoption of Auction-PPA's form (by NEURC)
	<i>expected period for filing applications for participation in the pilot auction</i>
<u>November 22, 2019</u>	<u>Deadline for the pilot auction to take place (by CMU)</u>
Date of pilot auction + 15 days	Deadline for concluding Auction-PPAs with the auction winners
December 1, 2019	Deadline for setting annual quota for 2020 (by CMU)
December 31, 2019	Deadline for concluding pre-PPA (according to existing rules)

Annex 2.

Classification of renewable energy producers*.

No.	Pre-PPA date	Commissioned date	Auction	Tariff (EUR/1 kW)		Green tariff term
				SPP	WPP	
I	Has already concluded	Has already commissioned	-	0,15	0,10	2030
II	Till Dec 31, 2019	For SPPs - within 2 years from the date of pre-PPA; For WPPs - within 3 years from the date of pre-PPA	-	0,15	0,10	2030
III	After Jan 1, 2020	After Jan 1, 2020	+	As determined by the auction, but not higher than 0,11 **	As determined by the auction, but not higher than 0,09	Date of commissioned + 20 years

* – only for SPPs with a capacity more than 1 MW, and WPPs with a capacity more than 5 MW.

** – a tariff for solar energy will be reduced for 3 years by 2,5 % each year.

Annex 3.

List of documents which are necessary to be filed by the producer to participate in the auction.

To participate in the auction, participants have to file:

1. Application.
2. An irrevocable bank guarantee in favour of a Guaranteed Purchaser.
3. Documents, which confirm either rights of ownership to, or usage of the land plot on which the project is being constructed.
4. A grid connection agreement.
5. Information about the final beneficial owner.
6. Extract from Register of Legal Entities.
7. Information on the management bodies of the entity and their personal composition.
8. Information on affiliated persons.