

## Energy newsletter | Competitive tender for obtaining public subsidies for new renewable energy plants in Spain



## **Energy | Competitive tender for obtaining public subsidies for new renewable energy plants in Spain**

The Spanish Ministry of Energy is going to organize a public tender to select new projects for the construction of new electrical power plants based on renewable energy technologies<sup>1</sup>. Winning bids will be awarded public subsidies, that successful projects will receive in addition to the revenue they will obtain from the sale of electricity in the free market.

The tender will be regulated by a Royal Decree, which will be developed by an Order from the Ministry and a Resolution from the State Secretariat of Energy. Drafts of the Royal Decree and the Order have been published by the Ministry, and the final texts will be issued in the coming weeks. A summary of the regulation and the requirements of this tender is described here. An updated version of this newsletter will be released once the definitive regulations are issued.

Public subsidies awarded to renewable energy projects are regulated in Spain by Law 24/2013, dated 26<sup>th</sup> December 2013, and Royal Decree 413/2014, dated 6<sup>th</sup> June 2014. The system is based on three main principles:

1. Public subsidies will be awarded to those plants which do not cover their costs and therefore cannot compete with other technologies and generate a reasonable level of profitability. For these purposes “reasonable profitability” is the average profitability of the Spanish 10-year sovereign bond within a 24-month period plus a margin. The value of the referred average and the margin are calculated and determined by the Government every 6 years (at present, the average profitability of the bond is €4.503, and the margin is 300 basis points, which makes a total of 7.503%).

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<sup>1</sup> This is not the first tender procedure organized by the Ministry. In January 2016 there was a 700MW auction for wind (500MW) and biomass (200MW).

2. Public subsidies will only be granted to projects selected in public tenders organized by the Ministry of Energy.
3. Public subsidies will consist of economic compensation for the investment made and, in some cases, for the operation costs, and will be paid during the estimated life of the plant. In order to calculate the amount, the Ministry makes estimations of the main parameters which determine the profitability of each type of plant, and compares it with the reasonable profitability which should be reached. The possible gap is covered by the subsidies. The estimations are reviewed periodically in order to adjust them to actual figures.

The aggregated power of the projects to be selected in this tender will amount to 3GW, and eligible projects can be based on any renewable energy technology (pv, thermosolar, wind, biomass, etc.). The projects must be new ones, not definitively registered in the Administrative Register of Electrical Energy Production Plants ("AREEPP"), and the main equipment to be installed must also be new, that is, unused before.

For the purposes of this tender, the draft Order establishes three reference types of renewable energy plants. Each offer presented to the tender will be referred to any of such reference types. Type I is for wind plants, type II for pv projects and type III for the rest of technologies.

A number of parameters are determined for every reference type, such as the estimated life of the plant, the standard value of the initial investment, the number of equivalent hours of operation and the compensation for investment. Basically, the tender aims to select those projects which offer higher reductions in the standard value of the initial investment and, therefore, will receive a smaller subsidy for the investment.

The **estimated life** is the duration attributed by the Order regulating the tender to each reference type of plant: 25 years, during which the public subsidy may accrue. The corresponding figure is final and will not be adjusted or recalculated periodically.

The **standard value of the initial investment** is the estimated value of the initial investment corresponding to each reference type of plant which would be paid by a diligent developer, considering the year of authorization of the plant, its technology and characteristics. This value is €1,200,000/MW for wind and pv plants and €2,000,000/MW for the rest of technologies.

The number of **equivalent hours of operation** is determined for each reference type of plant and is defined as the minimum number of hours which an efficient plant should operate per year. It is expressed as the ratio between the energy produced and sold in the market during such period by a plant (kWh) and its installed power (kW)<sup>2</sup>.

The **compensation for investment (Ci)** is intended to compensate the plant costs which cannot be recovered through electricity commercialization during the estimated life of the plant. Plant costs considered for these purposes are not the actual ones incurred by the developer, but standard costs determined for every reference type of plant. Ci is determined per power unit, as €/MW.

The Government may recalculate most of these parameters periodically in order to ensure that the plant owners receiving the public subsidy will be able to achieve no more and no less than the abovementioned reasonable profitability, in so far as the plants are managed in a diligent way.

In order to participate in the tender, bidders are required to lodge a guarantee, although the amount is not known at present (it was €20/kW in last year's tender). Each bidder will have to offer a percentage of reduction for the standard value of the initial investment corresponding to any of the three reference types of plants. The Ministry

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<sup>2</sup> The minimum equivalent number of hours considered for this tender will be 2,800 per year for wind technology, 2,367 for pv technology and 5,000 for the rest of technologies.

will most likely determine a range of maximum and minimum values for the reduction<sup>3</sup>.

The bid selection process will be as follows: the Ministry will determine for each offer the ratio between its Ci (resulting from the proposed reduction) and the number of equivalent hours of the corresponding reference type of plant. The result is defined as the extra-cost per unit for the electricity generation system. The bids will be listed in ascending order according to their extra-cost per unit; the tender will be awarded to those offers with fewer extra-cost per unit, up to an accumulated power of 3GW.

Then, the Ministry will determine the percentage of reduction of Ci for each reference type of plant to be applied to the projects previously selected:

1. First, the marginal extra-cost per unit will be determined for each technology. It is defined (for each technology) as the smaller figure between (i) the marginal extra-cost per unit corresponding to the last successful offer in this tender and the maximum figure for marginal extra-costs per unit established for each technology in the Order regulating the tender<sup>4</sup>.
2. Second, the Ci for each reference type of plant resulting from the tender will be determined by multiplying the marginal extra-cost per unit and the equivalent number of hours of operation established for each reference type of plant in the Order regulating the tender.
3. Finally, the percentage of reduction of the standard value of the initial investment for each reference type of plant resulting from the tender will be that which -once applied to the Ci projected in said Order- equals the Ci resulting

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<sup>3</sup> In the tender organized in January 2016 the percentage applied by the bidders who won the auction was 100%. This meant a renounce to any Ci. This has made difficult the financing of the projects, which construction has not begun yet. The Minister of Energy has expressed the Government's desire to avoid this result in the new procedure, by establishing a maximum percentage of reduction to the offers.

<sup>4</sup> See point 1 in annex to the draft Order.

from the tender (determined in accordance with point 2º above) for each reference type of plant.

The Ministry has designed an execution timetable for the projects selected in the tender, which will have to be finished before 31<sup>st</sup> Dec. 2019. According to this timetable, developers will have to reach specific milestones within a specific period. The first milestone will be the application for provisional registration of the selected offers with the Registry of Specific Compensation Regime (“RSCR”)<sup>5</sup>, which will have to be done within the 45 days following publication of the tender’s results in the Official Gazette (the “Publication”). At the time of applying for registration, developers will have to deposit a bank guarantee of €60/kW, which would replace the guarantee initially lodged to participate in the tender. Applicants will only determine the total power they intend to register (no more than that awarded in the tender) and the reference type of the plant/s they intend to build. Developers of selected bids who do not apply for registration within said time frame will lose their rights and the Ministry will enforce the guarantees lodged for participation in the tender.

Within the 6 months following the Publication, registered developers will have to provide the Ministry with further information on the plant/s they intend to build, whose total power must be equal to the total registered power. Such information will include the exact coordinates of the plant/s and the cadastral data of the relevant plots. In case this milestone is reached on time, the €60/kW bank guarantee lodged will be reduced in €12/kW; otherwise, the Ministry will enforce the guarantee in this very same amount.

Within the 12 months following the Publication, registered developers must submit evidence of the authorization of the executive project/s to the Ministry, as regards the previously identified plant/s. In case this milestone is reached on time, the €60/kW bank guarantee lodged will be reduced in €18/kW; otherwise, the Ministry will enforce the guarantee in this very same amount.

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<sup>5</sup> “Registro en estado de preasignación”.

Finally, not later than December 31<sup>st</sup> 2019 the plants with authorized executive projects will have to comply with the following conditions: (i) be finished (all elements necessary for producing and pouring the energy into the grid will be installed), (ii) be definitively registered with the AREEPP, and (iii) certify the pouring of electricity into the grid. Within one month following compliance with such conditions, developers will have to apply for definitive registration with the RSCR<sup>6</sup>. In case this last milestone is reached on time, the €60/kW bank guarantee will be fully cancelled; otherwise, the Ministry will enforce the guarantee in the amount of €30/kW.

Waiving the construction and connection to the grid of a plant provisionally registered with the RSCR will give rise to the enforcement of the €60/kW bank guarantee. The enforced amount will depend on the time the waiver is notified to the Ministry:

- In case the waiver is notified before 6 months elapse from the date of provisional registration with the RSCR, 50% of the bank guarantee will be enforced, and while the remaining 50% will be cancelled.
- In case the waiver is notified between 6 and 12 months after the date of said provisional registration, 75% of the bank guarantee will be enforced, and while the remaining 25% will be cancelled.
- In case the waiver is notified after 12 months from the date of provisional registration with the RSCR, the bank guarantee will be fully enforced.

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<sup>6</sup> “Registro en estado de explotación”.





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