

Long-term power purchase agreements (PPA) with renewable energy generators under Romanian Energy Law

1. Introduction

This article will focus on a presentation of the specific issues related to the sale of the electricity generated from renewable sources through market-based long-term power purchase agreements (“PPAs”), that had been reintroduced in Law 123/2012 on Electricity and Natural Gas (“**Energy Law**”) by Government Emergency Ordinance No. 143/2021 (“**GEO 143/2021**”), that was approved in its final form by Law 248/2022, enacted on 24 July 2022, after being banned for more than eight years.

We consider this topic to be of interest to operators on the current market, for the following reasons:

- energy generation from renewable sources has substantially improved in terms of technology and efficiency, making renewable energy generation competitive with conventional technologies of power generation;
- despite market volatility at the end of 2021, PPAs have continued to be seen as a long-term investment, providing developers with long-term bankability, reflected by cheaper prices for longer contracts, protecting prices against short-term market fluctuations;
- there is no state-sponsored support scheme available in Romania for renewables: the previous green certificates scheme ended at the end of 2016. As a result, the installation of new renewable generation capacities has almost stopped since 2017;
- the significant increase and volatility of wholesale electricity prices increased the demand for longer fixed-price electricity sourcing arrangements. Depending on the pricing formula, a long-term PPA can provide price certainty for a fixed period and thus protection against the volatility in the electricity prices both for the generator and the off-taker. A predictable and stable revenue stream are essential for the bankability of renewable projects

2. Shifting regulations regarding PPA on Romanian Energy market

It is a known fact to the operators on the Romanian energy market that in 2012 directly-negotiated long-term power purchase agreements (PPA), were banned (the Energy Law) under the influence of highly-politicized discussions on the directly-negotiated PPAs concluded by some state-owned power generators with some well-positioned traders in rather unfavourable conditions for the former.

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In order to avoid any discrimination in the market, the ban was general. Thus, art. 23 (1) of the Energy Law imposed after its amendment in 2012 that all electricity transactions have to be carried out in a transparent, public and centralized manner (basically on the centralized markets operated by the authorized market operator, OPCOM).

Even though OPCOM has launched several successful trading platforms, such platforms accommodate contracts with a maximum 1 (one) year term usually and/or are otherwise unfit for long-term contracts (mainly due to firm prices/quantities requirements, competitive auction mechanisms, unavailability of the regulated option to conclude the contract before the operational phase, etc.).

As a result, long-term PPAs have practically vanished from the market and so has the project financing for green field investments and, as such, it negatively affected the development of renewable projects by damaging their bankability.

In May 2020, the Ministry of Economy, Energy and Business Environment announced the reintroduction in Law 123/2012 on Electricity and Natural Gas (the Energy Law), by Government Emergency Ordinance 74/2020, of the right to sell power through directly-negotiated PPAs, as an exception from the general ban, applicable only to any new energy production capacities commissioned after 1 June 2020. This distinction between “new” and “old” power generation capacity was a departure from the directly applicable rules enacted by EU Regulation 2019/943 on the internal market for electricity (“Regulation 943/2019”) which requires Member States, regulatory authorities and system/market operators to ensure that markets are managed in accordance with a number of principles amongst which “long-term electricity supply contracts shall be negotiable over the counter” (the wide definition of the “supply contracts” includes PPAs and the reference to “over the counter” indicates directly-negotiated PPAs).

Therefore, EGO 74/2020 had introduced a restriction on the applicability of Regulation 943/2019 on the matter of freely negotiated PPAs, which is neither provided by the Regulation nor predicted by ANRE’s secondary legislation enacted by Order no. 236/2019, which anticipated the general lifting of the ban on directly negotiated PPAs by expressly allowing electricity transactions to be performed on “non-regulated markets” (in Romanian: “piete nereglementate”), creating another source of uncertainty about the legal framework applicable to PPAs, due to the express ban on PPAs still surviving in the Energy Law.

Subsequently, the Government started in September 2020, a large scale update of the national legal framework in the electricity sector in line with the provisions of Directive 2019/944/EU of the European Parliament and of the Council of 5 June 2019 on common rules for the internal market for electricity and amending Directive 2012/27/EU into the Energy Law, with the purpose of achieving the deregulation of the national electricity market as of 1 January 2021 and to stimulate new investments in green electricity generation.

The legislative changes had been finally implemented by the enactment of GEO 143, as subsequently approved by Law 248/2022, enacted on 24 July 2022.

GEO 143 transposed into Romanian legislation provisions related to national power system flexibility, the possibility to enter into renewable energy power purchase agreements, freely negotiated outside the centralized market, increased interconnection and market liberalization, new concepts as active consumers, citizen energy communities and aggregators, and more facilities to prosumers, among other matters of interest in the energy sector.

3. How PPAs work under the Romanian regulatory framework enacted by ANRE and OPCOM

Although by the changes to the Energy Law mentioned above, there is a legal recognition of the possibility to trade power bilaterally through freely negotiated PPAs, the PPAs conclusion mechanism remains for the time being unregulated by the National Authority for Energy Regulation (“ANRE”).

Some traders argued that it is not necessary that ANRE further regulates a derogatory regime of the PPAs from the trading on the centralized energy market because OPCOM had already regulated the Bilateral Centralized Market for Energy Contracts – Extended Auction (PCCB – LE) where currently there is the possibility of concluding negotiated bilateral contracts with a delivery period of more than one year.

As opposed to a standard bilateral sale transaction perfected on OPCOM administered platforms, a renewable PPA is usually a long-term contract under which an electricity trader or customer agrees to purchase electricity directly from the renewable energy generator.

Therefore, OPCOM-administered trading platforms are not best suitable to accommodate PPAs because of certain specificities related to the contractual term (contracts concluded on such platforms usually have a maximum 1 (one) year term) but also of other specific elements: firm prices/quantities

requirements, competitive auction mechanisms, unavailability of the regulated option to conclude the contract before the operational phase, etc.

Considering that the Romanian energy regulatory framework does not cover the conclusion of directly-negotiated PPAs between renewable energy generators and electricity traders as off-takers, it can be argued that the parties are entitled to freely agree on the content of such PPA.

For such a conclusion we can rely on the interpretation of the provisions of ANRE Order 236/2019 regarding the approval of the rules for eliminating and/or mitigating the impact of some measures or policies that may contribute to restricting the formation of prices on the wholesale electricity market (“**Order 236/2019**”).

Order 236/2019 no longer provides the general requirement that all electricity transactions take place in a transparent, public, organized and non-discriminatory manner and includes “non-regulated markets” (in Romanian: “piete nereglementate”) amongst the markets on which electricity can be traded. This wording could be read as an indication that ANRE is allowing directly-negotiated PPAs outside of a regulated/organized market administered by OPCOM.

4. Types of Power Purchase Agreements

As opposed to a standard bilateral sales agreement, a renewable PPA is usually a long-term contract under which an electricity trader usually named an “off-taker” or customer agrees to purchase electricity directly from a renewable energy generator.

PPAs are used to finance renewable energy projects, as they provide a guaranteed revenue stream for the power producer and help the purchaser meet their renewable energy targets. In addition to setting the price and duration of the agreement, a PPA may also include provisions for the delivery and transmission of electricity, as well as any penalties for non-performance.

There are several different types of PPA, that depend on where the renewable energy project is located and the delivery of the electricity, and each different type falls into long-term and short-term categories of PPA.

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Long-term PPAs are typically used for large-scale projects, such as large-scale solar farms with a lifespan of 25+ years. Short-term PPAs generally are used for smaller projects, such as commercial and industrial solar installations with a smaller budget, and can last from a few months to a few years.

PPAs may be structured as a fixed-price contract for a set period, or they may include a variable pricing component based on market conditions; they usually fall into any of the following contractual types:

- **On-Site PPA**

An on-site power purchase agreement is a contract between a power producer and a power purchaser in which the electricity is generated and consumed on the same site. This type of PPA is often used for small-scale renewable energy projects, such as rooftop solar or carport installations, where the electricity is used to power the facility where it is generated.

- **Off-Site PPA**

An off-site PPA is a contract between a power producer and a power purchaser in which the electricity is generated at a different location than where it is consumed. This type of PPA is often used for large-scale renewable energy projects, where the electricity is transmitted to the power purchaser via the grid. Many community solar developers require an off-site PPA, as the electricity that is generated on the solar farm is being consumed off-site.

- **Virtual PPA**

A virtual power purchase agreement (VPPA) is a financial instrument that allows a power purchaser to purchase the renewable attributes of a project, rather than the electricity itself. This allows the purchaser to meet their renewable energy targets without physically taking delivery of the electricity.

VPPAs are often used by companies that are looking to reduce their carbon footprint and increase their use of renewable energy but may not have the physical space or infrastructure to install their own renewable energy generation capacity. By entering a VPPA, the purchaser can support the development of a renewable energy project and receive credits for the energy that is generated, giving them plenty of renewable energy options at low stakes.

- **Physical Delivery Power Purchase Agreement**

Physical delivery power purchase agreements are contracts in which the power purchaser takes physical delivery of the electricity that is generated by a renewable energy project. This type of PPA is typically used for on-site renewable energy projects, where the electricity is consumed at the same location where it is generated.

In a physical delivery PPA, the power producer agrees to sell the electricity to the power purchaser at a fixed price for a set period. The PPA may also include provisions for the delivery and transmission of electricity, as well as any penalties for non-performance.

- **Portfolio Power Purchase Agreement**

A portfolio power purchase agreement is a contract that allows a power purchaser to purchase electricity from a portfolio of renewable energy projects, rather than a single project. This type of PPA is often used by companies that are looking to increase their renewable energy options, but do not have the resources to develop their own projects.

In a portfolio PPA, the power purchaser contracts with a portfolio provider, who is responsible for sourcing and managing the renewable energy projects that make up the portfolio. The power purchaser pays a fixed price for the electricity, and the portfolio provider is responsible for ensuring that the electricity is delivered to the power purchaser.

- **Block Delivery Power Purchase Agreements**

A block delivery power purchase agreement is a contract in which the power purchaser takes delivery of electricity in predetermined blocks of time, rather than continuously. This type of PPA is often used for renewable energy projects with variable output, such as community solar projects, where the amount of electricity generated may vary over time.

5. Key contractual points in PPAs

The PPA establishes the terms and conditions under which the electricity will be sold and defines the responsibilities of each party, amongst which the followings are most notable in the case of a greenfield renewable project:

Conditions precedent to the effectiveness of each party's obligations under the PPA. On the side of the renewable energy generator these may include: (i) receipt of certain governmental authorizations and clearances; (ii) obtaining comfort regarding the receipt of approvals not received as of the date of execution of the PPA; (iii) execution of the construction contract and certain other project agreements.

On the side of the purchaser these may include receipt by the Purchaser of (i) corporate documents (for example, articles of association and board resolutions) and (2) evidence of the energy generator's receipt of the necessary governmental approvals.

The renewable energy generator will usually wish to make financial closing a condition precedent to its obligations, whereas the purchaser will expect that any conditions precedent to the energy generator's obligations be satisfied within a certain period or the purchaser shall have the ability to terminate the PPA without liability.

Lenders will prefer to make all obligations effective as of the date of execution of the PPA. Open-ended commitments for either party can be avoided by including provisions allowing termination if, after specified dates, certain key events have not occurred (such as financial closing).

Sale of capacity and energy. The PPA may require the renewable energy generator both to make available to the purchaser an agreed level of capacity at the power plant and deliver the energy generated in accordance with its provisions.

Pricing. The pricing regime in the PPA typically has two components:

- i. an availability or capacity charge, which is payable by the off-taker in consideration of the power plant operator making generation capacity available to the off-taker, whether or not it actually offtakes electricity from the power plant.

This component is typically designed to provide a revenue floor for the project and is the primary channel through which each project proponent would recover its fixed costs (including its capital investments, financing costs and a return on equity); and

- ii. an output charge – this is usually referenced to the volume of electricity actually delivered and is intended to cover the energy generator's variable costs.

Third-party sales. The ability to make third-party sales can enhance the commercial viability of a renewable energy generating project and provide it with a degree of cushioning against demand side risks under the primary long-term PPA.

However, purchasers are often reluctant about allowing third-party sales as they want to be sure that all capacity is available to them at all times and so the PPA may include an exclusivity period during which all power produced is to be supplied to the purchaser. The practical feasibility of third-party sales (both in terms of demand and access to physical infrastructure to deliver electricity to third parties) will also need to be considered carefully.

Underperformance and delays by renewable energy generator. The PPA may provide sanctions or require the renewable energy generator to pay liquidated damages if it fails to deliver power as promised. Common examples include liquidated delay damages, if the construction of the renewable project is not completed on schedule or tariff abatements where the renewable power plant does not meet agreed performance standards during the operational phase.

Renewable energy generators and their lenders will be concerned to ensure to limit the impact of liquidated damages on their ability to recover their capital investments and earn a return. A commonly argued point is whether the renewable energy generator may be required to pay liquidated damages as a result of disruptions which are not within its control. It is also useful to note that in the event that the renewable energy generator is not able to make capacity available due to risks that the off-taker has agreed to bear, then the capacity will be deemed to be available to the off-taker. Examples of such risks include risks related to the availability of the transmission system to take energy from the power plant, the availability of fuel (if the off-taker is responsible for providing fuel), and political force majeure events.

Force majeure or purchaser breach of contract. The renewable energy generator is typically relieved from complying with its contractual obligations (and liability to damages) for disruptions arising from force majeure events.

However, the scope of force majeure relief available can often be a key negotiation point as it is a key contractual mechanism for allocating risk between the parties to the PPA.

One frequent issue is to what extent a renewable energy generator can obtain force majeure relief due to inability to obtain relevant government approvals.

The force majeure regime is often closely linked to the change in law regime. The scope of force majeure relief may also need to be adapted to different technologies. For example, a gas fired power plant is exposed to different disruption risks than a wind farm.

Renewable power plant operation. Issues in this respect typically include scheduled outages and maintenance outages, operation and maintenance, emergencies, and keeping of accounts and records.

Change of law. PPAs should address the impact on tariffs in the event of a change in applicable law and the mechanism for tariff adjustment. The private off-taker has significant less ability and appetite to absorb change in law risks (compared to a government entity).

6. Conclusions

The Romanian energy regulatory framework does not contain any specific restrictions on the conclusion of PPAs between renewable energy generators and electricity traders as off-takers, which means that the parties are entitled to agree freely upon the content of their contractual relationship.

However, if the renewable energy generator intends to sell electricity directly to customers, it must comply with certain regulatory provisions, but still in this scenario the freedom of the parties to determine the commercial content of their contract is relatively broad. Most notably, the pricing under a renewable PPA is liberalized and is based on free negotiation between the contracting parties without any intervention in the form of regulated product tariffs.

Notwithstanding the foregoing, the relevant energy sector specific rules and the industrial codes of the Romanian electricity system, such as the regulations enacted by the power transmission system operator, Transelectrica, also apply to PPAs. In practice this means that the renewable energy generator and the off-taker are entitled to agree freely upon the specific terms and conditions of the PPA as long as their agreement does not contradict a specific provision of the aforementioned sector-specific regulation.

The predictable and stable revenue stream secured by the directly-negotiated PPAs is a major bankability factor, therefore the lifting of the ban on renewable energy generators to conclude PPAs should help them secure project financing more easily. This is, therefore, a much-awaited correction of the regulatory framework.

In addition to the key commercial conditions of the renewable PPAs, on which we have intended to provide an insight above, the technical and legal aspects should also be carefully considered, since such clauses also have relevance from a bankability perspective.

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PETERKA & PARTNERS Romania remains at your full disposal to provide more information and any related legal assistance connected to this topic.

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