

## PORTUGAL: An Introduction to Energy & Natural Resources

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### Energy and Natural Resources – an overview of Portugal

2019 started with the Portuguese Government reaffirming its commitment to reduce the carbon footprint and reach carbon neutrality by 2050. The Government launched the integrated Energy and Climate Action Plan 2030 in articulation with the recently approved Roadmap for Carbon Neutrality 2050 and National Investment Plan 2030. Reaching carbon neutrality by 2050 implies assuming an ambitious target of 85%-90% reduction in GHG emissions. In the context of this launch, the Government emphasised the digital market and its vital role in the energy market in alignment with the European Commission approach.

In this context, renewables investments will need to go ahead, and lack of interest is certainly not the issue. Last year marked a continuing high demand for new renewables projects, including without feed-in tariff.

Indeed, appetite for greenfield projects in renewables continues to grow. On the other side, existing renewables projects for acquisition are in short supply compared with demand from investors. Lack of capacity of the grid has not enabled massive investments and the Portuguese Government even had to select pending projects within the Energy Directorate (awaiting the generation licence) by means of a draw. Further to that, some projects were awarded the right to a generation licence; however, many more await.

Notwithstanding the high interest in renewables licences (in particular for solar projects), smaller projects are having some difficulties in overcoming the market risk and obtaining good conditions for financing the implementation of the projects. The availability of corporate PPAs in the market as a solution for the offtake or hedging of electricity generated under new projects without feed-in tariff is still shy and some projects have been struggling to launch.

To overcome the current situation of uncertainty as to the future outcome of new projects, the Portuguese Government has announced that it intends to reinforce the

investment in the grid and to launch auctions for solar projects. According to public declarations of the Secretary of State, a first auction would be launched in June 2019, for 1,350 MW, and a second one in January 2020, for 700 MW. It is expected that each auction would cover two type of projects, one for smaller projects with a fixed tariff and another one for bigger projects where a contribution would be required from investors, to be used by the Portuguese Government to reduce the tariffs.

Following a steady development of the wind projects, a slowdown on new investment was verified after the Portuguese Government in 2018 subjected the overpowering to a preliminary binding opinion from the energy regulator (ERSE) confirming that these projects would not become onerous for the energy system – several overpowering projects were suddenly stopped. However, in the beginning of 2019, the Portuguese Government exempted overpowering projects from such opinion as long as investors of such projects accepted a remuneration of EUR45/MW, not to be updated, for a 15 year period, and provided the overpowering capacity does not benefit from the protection granted under the extension periods to which most of the windfarms adhered to back in 2013.

Biomass projects were another area of investment in 2018 and additional investments are still expected to take place in 2019.

In 2018, a special highlight should be made to the closing of the financing of the Windfloat project (first offshore wind project in Portugal under a commercial phase); the conclusion of the project and commercial activity is expected for the second semester of 2019. This project involved the setting up of a special legal framework which creates an attractive regulatory foundation for future off-shore projects being implemented.

Energy efficiency will be undoubtedly another crucial area for carbon neutrality to be successfully achieved. In previous years there was undeniably a strong commitment towards energy efficiency; however, measures taken to date have not yet proved sufficient for the ambitions and goals at stake. Further measures are eagerly awaited including special measures focusing on cogeneration projects.

As to traditional power, critical decisions will have to be undertaken swiftly as large thermal power plants are being discontinued in the near future. Visibility on the government strategy in this respect will be important for strategic decisions by investors to take place in due time.

In 2019 the low voltage electricity distribution grid tender for its operation is awaited and, following a public consultation process throughout 2018, the regulator ERSE recommended the launch of a tender for three different concessions areas: north, centre and south of the country.

As to the gas sector, further reforms are required for full practical implementation of EU Regulations. Among others, a change in the tariff year is to take place, with the gas tariff year moving from 1st of July/30th of June to 1st of October/30th of

September. Also, new rules will be applied aiming to improve the relationship between suppliers and customers and enhance protection of the clients.

At the same time reinforced information obligations to clients were already imposed on suppliers of gas, electricity and fuels with the aim to increase transparency in the retail markets.

Offshore oil and gas exploration activities registered a significant decrease due to the lack of a clear political strategy and a wide public opposition to the projects due to alleged environmental and economic detrimental impacts. The market players are waiting to see the outcome of the legislative elections in 2019 and its impact regarding the policy for the sector. In the absence of a clear political strategy, no relevant developments are expected to occur like in the previous year.

2018 was also a year noticeable for changes in the organisation and structure of public sector energy entities – ERSE had previously been attributed competences regarding supervision of the fuels market and this led to various restructurings in the public entities including at the level of the energy directorate.

Tax changes also occurred in the sector and their impact is still to be awaited. The State Budget for 2019 included a relevant development as regards the application of the Extraordinary Contribution on the Energy Sector (“CESE”), extending it to a significant part of the renewables sector. The amendment to the list of exempt entities leads to the taxation of companies covered by guaranteed remuneration schemes (Feed-In Tariffs) but safeguards the position of investors that were awarded projects pursuant to a public tender procedure. This extraordinary contribution has been subject to considerable debate and companies subject to CESE have been questioning its application through tax litigation.

Some energy products (coal, lignite, coke and semi-coke) used in the generation of electricity by entities whose main activity is the generation of energy are now subject to an excise duty on energy and oil products (*Imposto sobre Produtos Petrolíferos e Energéticos* – ISP) and added tax over CO<sub>2</sub> emissions (CO<sub>2</sub> Surcharge), with a phased taxation of 25% of the ISP and CO<sub>2</sub> Surcharge rates in 2019 and increasing 25% each year until 2022. This measure will increase the operational costs of the coal fired plants.

2019 is key for the investment to succeed and for carbon neutrality to become a reality. Investors in renewables are keenly awaiting the possibility of their investments going ahead. It remains to be seen how the Government will ensure market confidence for the implementation of the significant number of renewable projects envisaged and handle the balance of the energy mix with long-term investments in power other than renewables.

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