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RECENT AMENDMENTS AND REFORMS TO THE ENERGY SECTOR: LAW 15/2012 AND ROYAL DECREE LAW 29/2012

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Over the past months, the Spanish Energy Sector has suffered the consequences of the Government's attempts to reduce the so called tariff deficit and to reestablish the balance between the costs and revenue within the Electricity Sector.

These attempts have been partially materialized in the following reforms which were finally approved at the end of year 2012: Law 15/2012, of December 27, on tax measures for energy sustainability ("Law 15/2012"), introducing new taxes applicable to energy producers and other entities involved in the energy sector, and Royal Decree Law 29/2012, of December 28 ("RDL 29/2012"), which amends certain parts of the Spanish Electricity Sector Law, particularly those related to how the tariff deficit will be financed.

This report is aimed at providing a brief description of the main amendments contained in such laws and regulations, and is particularly focused on taxes and amendments that will affect renewable energy facilities.

New Taxes Introduced by Law 15/2012

The Official Gazette of December 28, 2012 published Law 15/2012, of December 27, on tax measures for energy sustainability. This is the result of several drafts discussed within the Congress and the Senate which were already subject to prior "Legal Analysis" documents prepared by our Firm.

Law 15/2012 includes the following tax measures that came into force on January 1, 2013. All revenues obtained with these new tax measures will be used to finance certain costs within the Electricity Sector, and thus should help to reduce the current deviation between costs and revenue within the Electricity Sector (the "tariff deficit").

1. Tax on Production Value

Law 15/2012 creates a new tax on the electrical energy production value with the following main specifications:

- *Taxable basis*: The total amount to be received by the taxpayer for the production and injection of energy into the electrical system. It is applicable to all facilities under the ordinary regime and the special regime. The taxable base will amount to all revenues derived from the production/injection of energy, and therefore includes all premiums or other compensations received.

- *Geographical application*: The tax will be applied throughout all the Spanish territory. We understand that this implies that the tax will be applicable to all production facilities located in the Spanish territory but will not apply, for

instance, to energy injected into the Spanish Electricity System by facilities located out of the Spanish territory.

- *Tax rate:* 7%.

- *Payment:* The tax is accrued on the last day of each tax period, which refers to the last day of each calendar year. The taxpayers must present a self-assessment of the tax and pay the tax amount within the month of November of the year following the tax accrual (i.e. 11 months after the end of each fiscal year).

- *Interim tax payments:* Taxpayers are compelled to make interim tax payments in the months of May, September, November and February, based on the value of the electricity production for the 3, 6, 9 or 12 month-period, as applicable. The amount payable will be the result of applying the 7% rate to the value of production measured at the power plant busbar in the period prior to the declaration, deducting interim payments made in prior quarters of the same fiscal year.

  Interim payments are not required to installations whose production value was below 500,000€ in the immediately preceding fiscal year. In the event of installations commencing their production after January 1, the interim payments will be made (if applicable) at the end of the quarter in which the aggregate production value has reached 500,000 €.

2. <u>Levy on the Use of Fresh Water Resources</u>

Law 15/2012 has also included taxes to be applied to hydroelectric facilities. In particular, the law has created a new levy (*canon)* with the following specifications:

- *Taxable basis*: The value of the hydroelectric energy produced, measured at the power plant busbar.

- *Taxpayers*: Concession awardees or entities succeeding these in the exploitation of the hydroelectric facilities. Hydroelectric facilities exploited directly by Public Administration within their public domain administration duties are exempt from the new levy.

- *Tax rate*: 22% of the taxable basis.

- *Payment:* The tax will be payable in the terms established by the relevant concession award. In the case of concessions granted prior to January 1, 2013, the conditions of the concession will have to be updated to include the new levy and the payment terms.

- *Reductions*: Hydroelectric installations of less than 50MW and production facilities over 50MW using hydraulic pumping technology will benefit by a reduction of 90%.

It is important to point out that according to Law 15/2012, 2% of the revenues obtained with this new levy will be used as a form of revenue by the river basin district organization, while the other 98% will correspond to the Public Treasury and thus will also contribute to financing the costs of the electricity system (rather than contributing to the protection and improvement of the hydraulic public domain, as expressly announced by the Law when creating this levy). Several questions have already arisen with respect to the constitutionality of this new levy.

3. Green Cent

The law creates 3 new special taxes applicable to the use of gas, coal and fuel-oil, as described below (by introducing the relevant amendments in Law 38/1992, of 28 December, on Special Taxes):

	Taxable event	Amount of the tax
GAS	• Natural gas consumption • Production of electrical energy in installations using natural gas as fuel	General Use: 1,15 €/gigajoule Energy Production: 0,65 €/ gigajoule Other profesional uses: 0,15 €/ gigajoule
COAL	Production of electrical energy in installations using coal as fuel	0,65 €/gigajoule
DIESEL AND FUEL-OIL	Production of electrical energy by installations using diesel or fuel oils as fuel	• 29.15 € / 1,000 litres diesel. • 12.00 €/ton fuel-oil.

4. Other Taxes

The law has also introduced 2 new taxes applicable to nuclear installations or activities: The tax on the production of radioactive waste as a consequence of the energy generating activity, and the tax on radioactive waste storage.

The particulars of those new taxes are not analysed in depth in this report due to it being focused on renewable energy activities, but it is important to mention that revenues to be obtained out of such taxes will also contribute to financing the costs of the electricity system, thereby relieving the tariff deficit.

Elimination of Premium-Based Regimes for Installations Using Fuels

Law 15/2012 has introduced important restrictions to the premium-based regimes for the generation of energy based on the utilization of fuels. In particular, according to the Law, the electrical energy attributable to the use of fuels in facilities that use any of the non-consumable renewable energies as primary energy shall not be subject to a premium-based economic regulation.

However, in the case of hybrid installations using both consumable and non-consumable energies, the production of

energy attributable to the use of renewable consumable energy will qualify to receive the premium-based economic regulation.

This affects particularly solar-thermal facilities. Up until now, these facilities were entitled to use support fuel to compensate for the lack of solar irradiation (up to a limit of 12% of the total production per annum if the facility is subject to a regulated tariff, or 15% if the facility combines market price and premium). With this new regulation, the part of the energy production attributable to the use of such support fuels will not benefit from the premium-base regulation (i.e. will be sold on the basis of market prices).

This restriction will imply important consequences in the economic previsions of solar-thermal installations already commissioned or currently under construction. In fact, the consequences for solar-thermal facilities go beyond this restriction: they will suffer the consequences jointly of the new 7% tax, the "green-cent" applicable to use of fuels, and the elimination of premium-based regulations for the energy attributable to use of such fuels.

Finally, the restriction only affects installations using non-consumable energies as a primary energy. Therefore, facilities involving production with biomass or based on the treatment of waste are not affected.

Amendments Related to Provisions Related to the Financing of the Electrical System and the Tariff Deficit

Spanish legal provisions related to the stability of costs and income of the Electricity Sector, and to the so-called tariff deficit, have been amended in several provisions enacted at the end of year 2012.

Up until now, it was generally established that, as of January 1, 2013, the revenues generated by access tolls should be sufficient to cover the entire costs associated with the system. Considering that new taxes have been created to partially finance the deviation between costs and revenue within the Electricity System, certain amendments have been introduced to reflect the fact that part of the costs of the system will be charged to the Public Treasury.

In particular:

- Law 15/2012 has amended Law 54/1997 on the Electricity Sector to state that the costs of the electrical system will be generally financed with both access tolls and amounts allotted in the General State Budget (*vid.* new article 15.2 of Law 54/1997*).* In addition, it includes a provision whereby each yearly General State Budget Law will include financing of the costs of the electrical system up to the following amount: (a) the previsions of tax collection derived from new taxes that, according to the new Law, correspond to the State Public Treasury, plus (b) the estimated revenues in sales of greenhouse gas emission rights up to a maximum amount of 500 million euros.

  However, this provision was completed by Law 17/2012, of 27 December, approving the General State Budget for 2013, which has established that items to finance the costs of the electrical system included in the General State Budget for each year shall be used for the promotion of renewable energies in the amount of (a) the tax collection under Law 15/2012, plus (b) 90% of the estimated revenues in sales of greenhouse gas emission rights up to a maximum amount of 450 million euros. The remaining 10% of greenhouse emission rights will be used for the fight against climate change.

- Final Provision 4 of RDL 29/2012 has amended Law 54/1997 on the Electricity Sector in the part related to the tariff deficit. First paragraph of the Additional Provision 21 of Law 54/1997 has been eliminated. The erased provision established that as of January 1, 2013, the access tolls should be sufficient to finance all the costs of the system, thus avoiding a tariff deficit being accrued *ex ante.* The truth is that such provision, aimed to avoid the appearance of deficit in the system, proved to be useless to prevent the deviation between income and costs of the electricity sector.

  With the new regulation, the Government will not be forced to increase the access tolls when necessary to assume all the costs of the electricity system. If the Government finds it appropriate, it can freeze the access tolls and charge the tariff deficit to the Annual Public Budget (Additional Provision 2 of Law 15/2012).

- Law 17/2012, of 27 December, approving the General State Budget for 2013, has suspended the compensation against the General State Budget of the extra-costs of generating energy on the island and non-peninsular systems (i.e. Canary Islands, Baleares, Ceuta and Melilla) corresponding to year 2012. Therefore, there is an additional extra-cost of the system that is no longer financed through specific items of the budget, but will have to be added to the costs of the system that have traditionally and continually increased the tariff deficit.

Other Amendments Introduced by Royal Decree Law 29/2012, of December 28: Finalization of the Construction as a Requirement to Qualify for the Premium-Based Regimes

RDL 29/2012 has additionally introduced certain clarifications related to the finalization of the construction of installations under the Special Regulation to qualify for the feed-in tariff or the premium-based regulation.

In particular, it states that premium-based regulations will not be applicable if upon conducting an inspection or by using any other legal means, it is confirmed that an installation previously registered at the pre-allocation registry (and thus applying for premium-based regulations) is not completely finalized at the end of the legal deadline for construction.

It further states that, regardless, the installation cannot be considered as finished:

a) If all the evacuation infrastructure necessary to inject energy into the distribution or transport grid have not been finalized;

b) If all the equipment to generate energy has not been installed and is in service;

c) If all the solar farm is not installed and is operative, if applicable;

d) If the storage capacity contemplated in the construction project is not operative, when applicable.

The above amendments were probably not strictly necessary since the previous regulations did already require finalization of the construction for the installations registered under pre-allocation registries to qualify for the premium-based regulations. However, such clarifications were probably found necessary by the Government to avoid interpretation fights and particularly considering that a considerable amount of MW of wind facilities reached the deadline for construction on December 31, 2012.

Finally, RDL 29/2012 states that the equipment not included in the construction projects approved by the public administration cannot be considered part of the installation nor can they begin operation, except if the relevant amendment has been approved by the administration. In such case (i.e. if the amendment is approved), the installations will correct their premium-based regulation in the part of the energy attributable to the new equipment (that will be sold on the basis of market prices). This may help to clarify the possible consequences in the case of additional power being installed in plants awarded with premium-based regimes: the amendment can be done and the power related to the additional installations would not benefit from the premium regulations or feed-in tariffs. But the Royal Decree also states that the specifications of the economic regulation of installations that, after being awarded with premiums have been subject to such amendments, can be established by the Government in future regulations. We will have to wait to see the real impact of this amendment and if it really brings full comfort in the event of substantial technical amendments made to installations awarded with premiums / feed-in tariffs (which up to now could affect the economic regulation of the whole installation).