
Key points on PPAs or long-term renewable energy power purchase agreements

Legal Flash - Energy

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Power purchase agreements (“PPAs”) are becoming a reality in our electricity market. They enable (i) energy consuming companies (particularly those that are energy intensive) to rely on green energy at a predictable long-term price, and (ii) producers to ensure the sale of all or part of the energy produced at a fixed price. Royal Decree 24/2020 reflects this reality and sets out a legal framework necessary to cover the risks of medium- or long-term energy supply agreements.



Highlights

- > The current regulatory framework offers ample scope to the autonomous will of the parties to establish the terms of the agreement based on their interests.
- > This contractual arrangement enables energy producers or marketers to obtain stable revenue and facilitate project financing.
- > PPAs enable companies that consume energy and, particularly energy-intensive sector companies to ensure a long-term supply of energy from renewable sources, and at fixed and competitive prices
- > The measures adopted under Royal Decree 24/2020 will therefore facilitate PPAs being negotiated and implemented.
- > At the same time, long-term supply schemes are beginning to be developed under the form of self-consumption, in accordance with RD 244/2019.



What is a PPA?

- > A power purchase agreement or **renewable energy power purchase agreement** is a bilateral agreement for buying energy from renewable resources at a set price, for an established period and generally long term.
- > Currently, the most widespread type of PPA agreement in Spain is an agreement signed between energy **producers and marketers**, but PPAs may also be signed between energy **producers or marketers and end consumers**, specifically companies requiring large amounts of energy, based on the specific needs of both parties.
- > PPAs signed directly between producers and end customers are scarce, because there are difficulties to match supply and demand and to adjust these to production and consumption curves. However, the mediation of a marketer provides that flexibility through its customer portfolio, in purchases as well as sales, with the addition of its ability to absorb deviations
- > Mixed agreements are beginning to take shape to develop a renewable plant and supply, in which a large consumer assigns a part of its land to a company that constructs and operates a renewable plant, and the two parties sign a long-term direct supply agreement. This type of agreement is governed, as mentioned, by RD 244/2019 of April 5, which regulates the administrative, technical and economic conditions for self-consumption of electrical energy.

Types of PPAs

There are several possible structures for implementing a PPA, which can lead to different classifications depending on the criterion chosen. For the purposes of this legal flash, we classify them by the following main types:

- > **Physical PPAs:** There is a supply in the legal sense: there is a purchase and sale of electricity, but (despite its name) this does not entail a physical energy transmission. These correspond to “traditional” supply agreements, in which the marketer sells energy that is delivered by the distributor. The major difference between these physical PPAs and the traditional agreements lies in the term (medium or long-term, as compared to terms that are typically shorter) and fixed price that, until now, was not standard practice on the market.



- **Direct PPAs (self-consumption):** There is a direct supply: there is a physical delivery of electricity between producer and consumer, connected by a power line. These agreements could fall, at least partially, under the form of self-consumption, based on the specific circumstances (physical, technical and legal) of the plant. Specifically, under this arrangement, the producer would sell the energy to the consumer. If the generation plant falls under the system of self-consumption without surpluses, the only destination for the energy produced would be the consumer's plant. In this case, the plant would be held in the consumer's own name. But if the plant registers for the system of self-consumption with surpluses, it could sell as much energy to the consumer as he requires, but it could offload any surpluses onto the grid. Equally, the consumer will be able to continue to receive energy (through its energy marketer) to cover any consumption needs which cannot be met by the renewable plant.
- **Financial PPAs:** These do not entail the physical delivery of energy. In the case of PPAs between producer and marketer, the producer sells its energy to the market and the parties arrange to settle the difference between the agreement and market price. In the case of PPAs between marketers and consumers, the consumer is supplied the energy through any ordinary channel and arranges the settlement with the marketer by differences between the fixed price and the resulting market price.

PPA regulatory framework

- There is no complete and specific **regulatory framework** in Spain that regulates the form of PPA between the producer and the end consumer, although regarding the purchase of energy through **physical PPAs**, it is generally necessary to address issues such as the provisions on bilateral energy purchase agreements established in: (i) [Directive \(EU\) 2018/2001](#), of the European Parliament and of the Council, of December 11, 2018, on the promotion of the use of energy from renewable sources; (ii) [Spanish Act 24/2013, of December 26, on the Electric Sector](#); and (iii) [Spanish Royal Decree 2019/1997](#), on December 26, organizing and regulating the market for the production of electricity.
- **Financial PPAs** are the most flexible in operational terms, although they are subject to specific financial legislation (European Market Infrastructure Regulation) and to certain accounting and tax features, so we recommend a specific analysis of the parties' situations before opting for this type of agreement.



Main obligations for the parties to a physical PPA

Below we list the **main general obligations** for the parties to a PPA:

- › **Registering in the corresponding administrative registry** considering its nature or accreditation of the capacity of its representatives through the corresponding notarized power of attorney. Specifically, energy producers should be registered in the administrative registry of electricity production plants, and in the registry for the specific remuneration system, if applicable. Direct consumers should be registered in the registry of direct consumers in the electricity market.
- › **Meeting technical requirements** of the operating procedures approved by the system operator, Red Eléctrica de España (“REE”).
- › **Providing REE with the appropriate guarantees** to meet any financial obligations arising from the operations under the PPA and meeting the requirements in the operating procedures approved by REE in relation to the payment guarantees.
- › The following are **obligations for parties to PPAs with the physical delivery** of energy: (i) notifying REE of the affected production and acquisition units, as well as the maximum energy covered by the bilateral transaction; (ii) notifying REE daily of the PPA execution in the manner and means established in the operating procedures; and (iii) meeting REMIT legislation (market transparency).
- › A specific authorization system is envisaged for agreements signed between subjects and companies located outside Spain that are authorized to buy or sell electric energy, providing these entail a flow of electric energy over the **international interconnections** of the Iberian Peninsula.

Content of the physical PPA

- › Within the regulatory framework of the PPAs, **ample margin exists for the autonomous will of the parties** to establish the terms governing the agreement.
- › The fundamental **content** of the PPA includes the quantity of energy supplied, the duration of the agreement and the price, energy measuring and delivery point, as well as any guarantees established for cases of risk of nonpayment, regulatory changes, possible



price review formulas, penalty system and system for agreement termination. It is also essential to regulate any deviations.

- › There are no minimum or maximum periods for contractual **durations**, although in keeping with the nature of the PPA, commitments are generally established for a prolonged period (between 5 and 12 years).

Content of the financial PPA

- › Financial PPAs are **agreements settled by differences**, essentially of financial content. Many companies offer PPAs in the form of an ISDA agreement (standard agreement for financial transactions, normally under English law) or Financial Transaction Framework Agreement or "CMOF" (same structure, but subject to Spanish law). However, it is possible (in our opinion, it could be recommendable) to implement this through a specific *ad hoc* agreement
- › The main **content** of financial PPAs refers to the settlements and the means of performing these, as well as to the approach to discrepancies. They do not usually contain references to a specific plant, nor to physical or regulatory aspects of the energy system. However, as this is tied to the development of the electricity market, it will also be important to establish the content of the change-in-law clause, as well as the causes and consequences of early termination.

Guarantees of Origin

- › Guarantees of Origin (GOs) certify that a given amount of electricity has been produced from renewable sources. In Spain they are regulated by Circular 1/2018 of the CNMC (National Commission for Markets and Competition).
- › PPAs usually include the GO's transfer from the producer to the energy marketing company or to the end consumer, in which case it is called a redemption.
- › Physical PPAs permit direct transfer of GOs to the purchaser, whether marketer or consumer. In the case of financial PPAs, in contrast, the consumer cannot receive the GO directly because redemption is only possible through their energy supply company. Therefore, in the case of financial PPAs, mediation mechanisms should be set up, to



allow consumers to continue enjoying the schemes that officially guarantee consumption of renewable energy.

Advantages of PPAs

- › PPAs offer important advantages for producers and for energy-intensive companies.
- › The main **advantages for energy-intensive companies** are as follows: (i) the setting of the costs for the long-term supply of electricity; (ii) the decrease of the risk of volatility of the electricity market price; and (iii) the accreditation of consumption through green energy guarantees-of-origin certificates.
- › We highlight the following **advantages for energy producers**: (i) a guarantee of stable and foreseeable revenue for a long period, and (ii) the possibility of financing for their projects and plants.

Changes introduced by Royal Decree 24/2020

- › Royal Decree 24/2020 sets out the legal system for the state to cover the risks derived from buying electrical energy with medium- and long-term agreements, entered into by electrical energy suppliers and consumers certified as high-intensity energy consumers at the moment the concession is granted.
- › It creates the **Spanish Reserve Fund for Guarantees for Energy Intensive Entities** (“**FERGEI**”), a body registered at the Ministry for Industry, Commerce and Tourism. It will cover, on behalf of the state, the risks derived from medium- and long-term purchases of energy supply between certified energy-intensive consumers and the various electrical energy suppliers on the production market. FERGEI will be managed by the Insurance Compensation Consortium, whose initial provision of funds will be at least 200 million euros.
- › The Spanish Company for Export Credit Insurance S.A. and the Insurance and Reinsurance Company S.M.E. (**CESCE**) is appointed as the exclusive managing agent, acting as an insurer or guarantor on behalf of the state to cover any insolvency risks in contracts signed by energy-intensive consumers for the medium- and long-term acquisition of electrical energy.



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