

# Prospects of regulation of renewable energy projects

**VEGAS LEX**

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# Practical business structures of joint ventures in renewable energy projects – current restrictions and way forward

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# Joint ventures in wind power sector: examples\*



## Wind power sector development fund: Fortum-RUSNANO

- ✓ Amount of investments: over RUB 30 billion
- ✓ Year of establishment: 2017
- ✓ Activity: construction and operation
- ✓ Form of incorporation: investment partnership



## FNG-4: Fortum-RDIF

- ✓ Amount of investments: over RUB 21 billion
- ✓ Year of establishment: 2020
- ✓ Activity: construction and operation
- ✓ Form of incorporation: holding structure, LLC



## Redwind: Rosatom-Lagerwey

- ✓ Amount of investments: [confidential]
- ✓ Year of establishment: 2017
- ✓ Activity: supply of turbines
- ✓ Form of incorporation: a company in the Netherlands that has branches in Russia



## WindOGK: Rosatom- Gazprombank

- ✓ Amount of financing: RUB 61 billion
- ✓ Year of establishment: 2018
- ✓ Activity: engineering and construction
- ✓ Form of incorporation: operating company, JSC

# Joint ventures in wind power sector: key participants

## 1. Operational partner

- ▶ *E.g.*, Fortum, Rosatom, Enel
- ▶ Arranges for construction and operation of a wind power plant
- ▶ Provides with co-investments
- ▶ **Is interested in long-term possession of wind power plants**

## 2. Investor / Financial partner

- ▶ *E.g.*, RUSNANO, RDIF, Gazprombank
- ▶ Institutional / major investor, provides with co-investments of up to 50%
- ▶ **Is interested in return of investments:** dividend flow / withdrawals from certain projects / sale of a participatory interest in JV

## 3. Technological partner

- ▶ *E.g.*, Vestas, Siemens, Elawan Energy
- ▶ Arranges for the supply of turbines and other equipment
- ▶ Ensures the local content in equipment
- ▶ **Is interested in gaining a profit from supplies** without technology transfer



# Key features of joint ventures in wind power sector, legal regulation

JV participants: operational partner-  
investor

Corporate legislation generally allows to **optionally** form in JV the management structure, distribution of responsibility and profit of the project in the **interests of JV participants**

Guaranteed proceeds under RES CDA

"Easy-to-understand instrument for investors and financial organizations"\*. Profitability above 12%.

JV may be structured in the manner that the investor be provided additional guarantees; in return, the operational partner becomes entitled to manage freely

Risks of imposition of fines  
under RES CDA

The partners' suretyships, obligations to increase the JV capital and adjustment of investment obligations are used in practice

Risks of imposition of international  
sanctions

The risks of imposition / extension of sanctions related to the Russian partner are regulated through the buyout of a participatory interest in JV

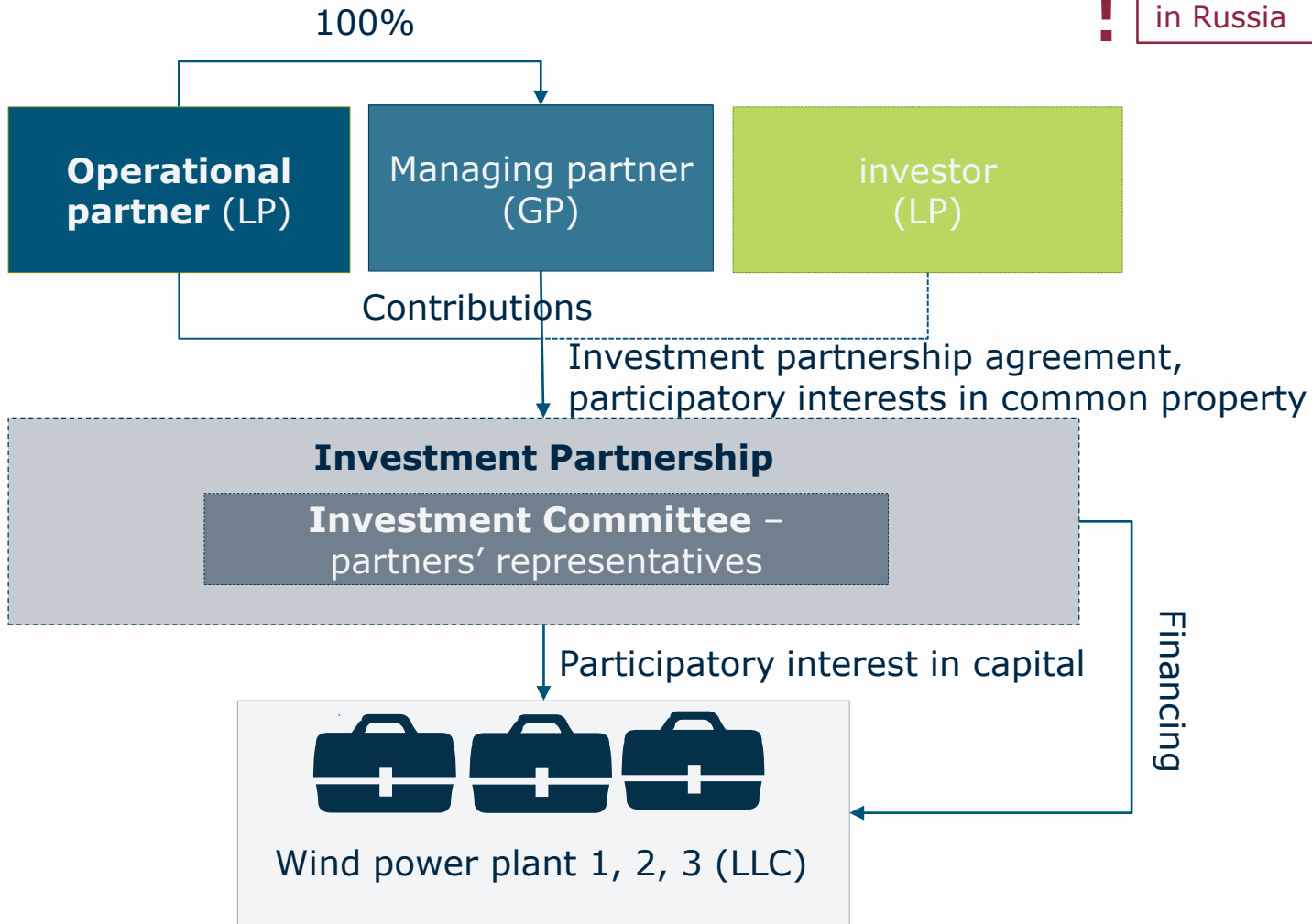
! Generally, the current legislation in Russia ensures the proper regulation of business arrangements in JV, taking into account the specifics of RES.

▪ The basic instruments are: corporate agreement (shareholders' agreement), investment partnership agreement

\* A. Kalanov, RUSNANO: <https://www.kommersant.ru/doc/3873994>

# JV in the form of investment partnership

! New form of JV in Russia



# Advantages and disadvantages of investment partnership



**IP's contract model is more flexible than LLC's contract model**



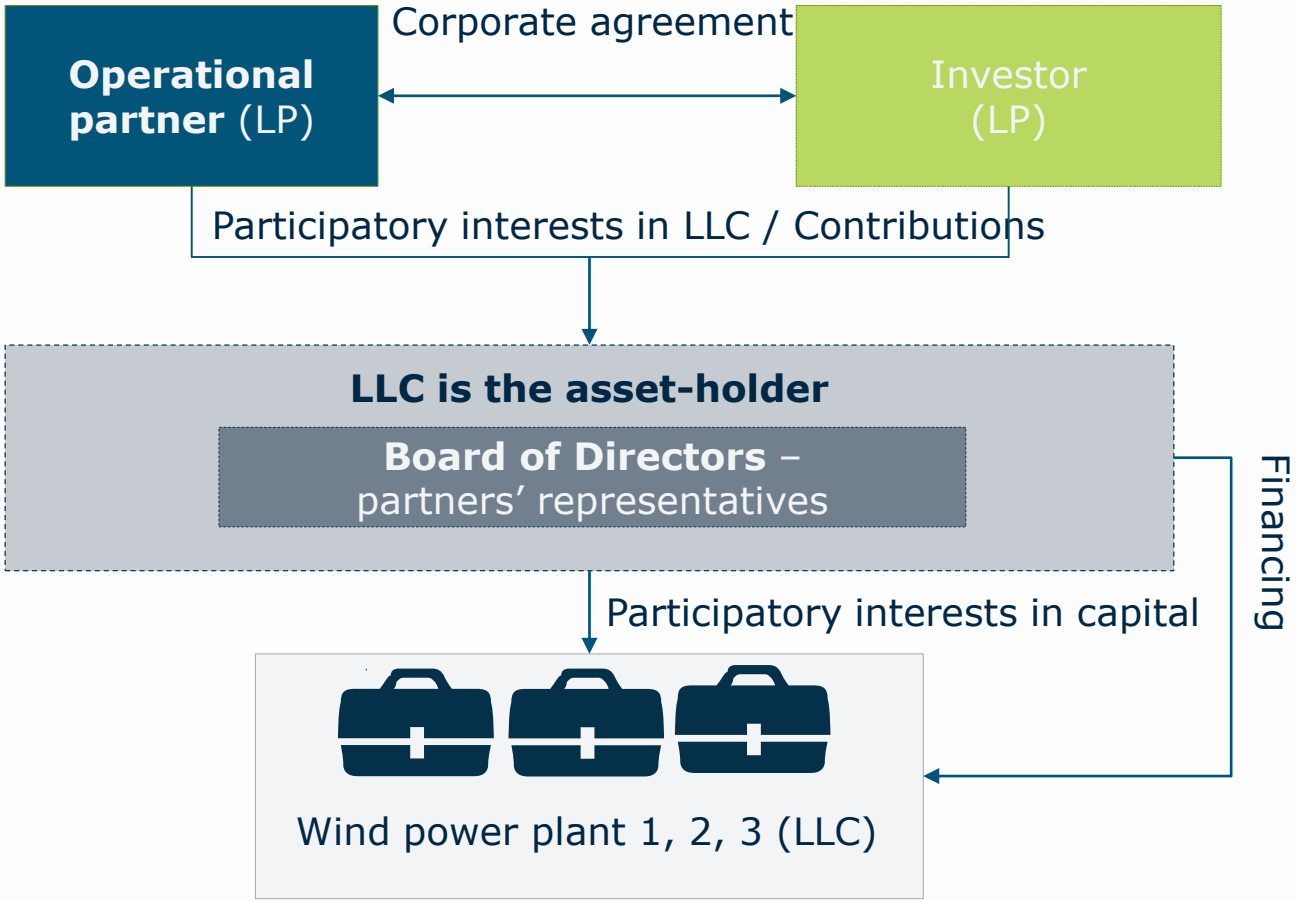
**As compared to LLC, IP has additional risks**

Freedom of contract + optionality = flexibility  
International investment practice (*limited partnership*)  
Regulation is envisaged in agreement only; there is no charter  
Consolidation of various types of contributions  
Monetization of expertise of Managing Partner (GP)  
Flexible management system  
Fine adjustment of distribution of risks and profit (*upside-downside*)  
Additional scenarios for deadlocks and defaults  
Disproportionate distribution of profit  
Different distribution of profit from investments in different facilities  
Engagement of new partners (*deed of adherence*)  
Subsequent amendment of the terms and conditions of IPA  
Confidentiality of participation in IP  
Possibilities for non-consolidation of obligations  
IP participants do not have subsidiary liability

Gaps in tax regulation  
Complex administration  
Absence of judicial practice

# JV in the form of a holding structure that contains LLC

! Traditional form of JV





# Advantages and disadvantages of a holding structure that contains LLC



**It has greater  
predictability  
than IP**



Established positive judicial practice concerning key aspects  
More predictable taxation  
Wide application in practice, including in power industry



**Legal boundaries  
for it are more rigid  
than for LLC**



Mandatory restrictions with regard to LLC  
Less possibilities of managing the consolidation of obligations  
Personal liability of the members of the Board of Directors  
Practice of D&O liability insurance is not developed

# Conclusions

- At present, JVs are established taking into account RES CDAs that ensure investment attractiveness
- Russian corporate legislation is generally compliant with international standards
- Russian corporate legislation does not generally provide for serious obstacles to structure JV in RES
- Investment partnership is the optimum form of JV in RES provided that gaps in tax legislation are filled
- JV in RES may also be structured in the form of LLC
- Further development of corporate legislation and law enforcement practice must relate to “fine adjustment” instruments that meet the needs of investors: certain provisions of the LLC Law and JSC Law

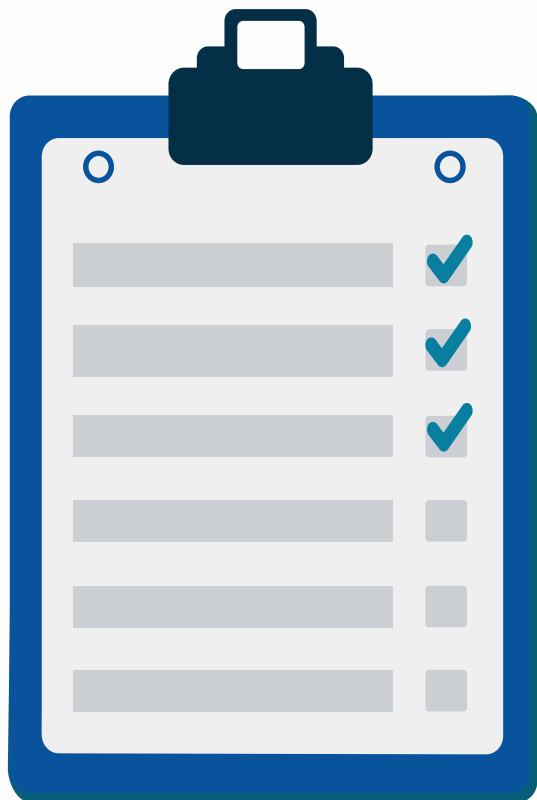
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# Local content of equipment in the renewable energy projects – status and prospects

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# Relevance of localisation issues in renewable energy projects



- 1** **Toughening** of the requirements to local content in RES\*
- 2** **For wind power generation facilities:** from 2025 to 2030 – 87 points; from 2031 to 2035 – 102 points (in 2020–2024 – 65%)
- 3** **For solar power generation plants:** 110 points of local content from 2025 to 2030; 120 points till 2035 (at present - 70%).
- 4** **The volumes for the new support programme** of new plants and facilities to be put into operation in 2025–2035, have not been approved yet
- 5** **Should the volumes of support programmes reduce,** the ROI in localisation may collapse

# Regulatory framework for localisation of power facilities in renewable energy projects

- Decree of the Government of the Russian Federation No.426 "On Qualification of a Generating Facility Operating on Renewable Energy Sources (RES)" of 03.06.2008
- Resolution of the Government of the Russian Federation No.449 "On the Mechanism for the Promotion of Renewable Energy on the Wholesale Electricity and Capacity Market" of 28.05.2013
- Order of the Ministry of Industry and Trade (Minpromtorg) of the Russian Federation No.3788 "On Setting up the Procedure for Localisation of Power Generating Facilities Operating on Renewable Energy" of 24.09.2018
- Order of the Government of the Russian Federation No.1-r "About Main Public Policies in Enhancement of Energy Efficiency of the Electric Power Industry in terms of Using Renewable Energy for the Period up to 2035" of 08.01.2009



## JV Establishment

Establishing a JV with a technological partner who will ensure that locally made equipment is supplied.

## Supplier's Obligations and Warranties

- Detailed obligations in localisation, including a localisation plan
- Independent warranties of capitalised affiliates
- Loss Recovery

## SPIC

- "Made in Russia" status
- Grandfather clause
- Specific terms and conditions for public land plot lease, etc.

# Localisation and other benefits\*



## "Made in Russia"

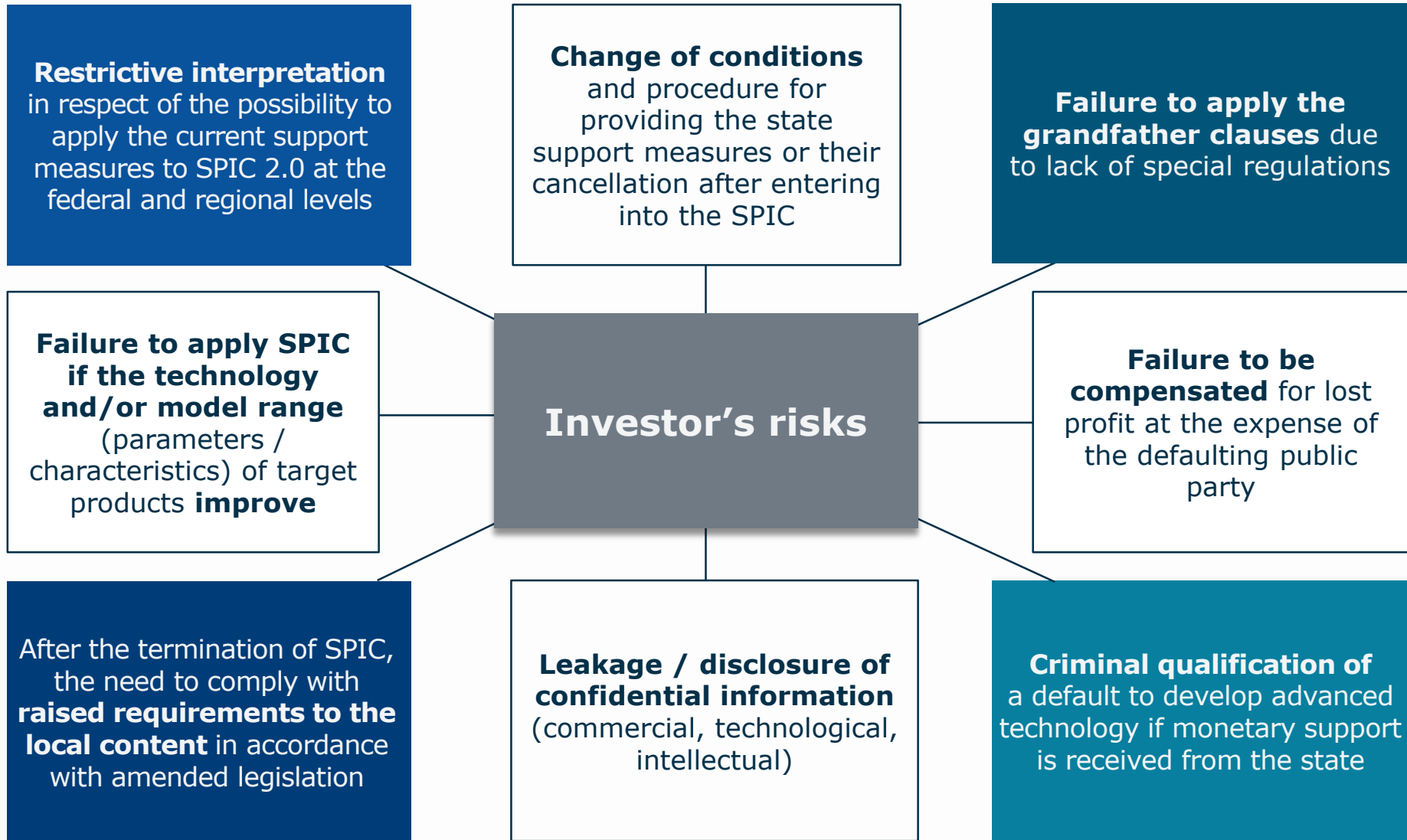
- An investor may obtain such a status "in advance": upon concluding a SPIC (Special Investment Contract), even before launching target products manufacturing
- Required localisation must be achieved within 3 years from the starting date of target products manufacturing
- After SPIC expiry, it is necessary to comply with the localisation requirements in accordance with the amended legislation



## Grandfather clause

- No new federal and regional regulations introducing restrictions on exercising rights related to SPIC performance will be effective
- Specific "non-deterioration" procedure is provided for by the federal and regional legislation, accordingly, as at the date of SPIC conclusion
- There are exceptions (performance of international agreements, EAEU instruments, protection of the foundations of the constitutional system, defence and security)

# Risks of the private party to SPIC 2.0





# Instruments to mitigate the risks

## Wordings of contract

Caveats and definitions in the contract, minutes and correspondence



## Explanations

of the competent authorities with regard to SPIC and the contractual terms and conditions



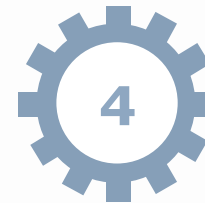
## Planning

Evaluation of the results of investment project under the average-weighted or moderately negative scenario



## Post-planning

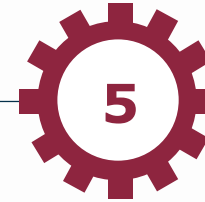
Before the expiry of SPIC, development and implementation of a plan to achieve the statutory local content



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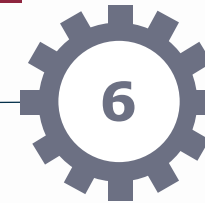
## Legislation

Initiating and providing a rationale for amending, clarifying or supplementing it



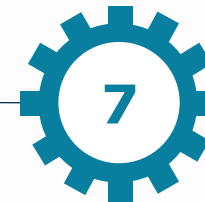
## Deviations

Specifying the extent of deviations from the project parameters where a breach of contract will not be deemed material



## Data protection

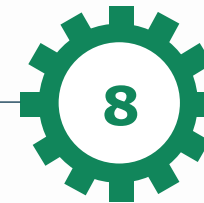
Non-disclosure and other means to keep any sensitive information confidential



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## Evidence

Documenting of specific performance of the obligation to develop technology and, in case of failure to perform such obligation, immediate cash refund to the public party



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# Regulatory agreement as an alternative to Renewable Energy Sources Capacity Delivery Agreements (RES CDA)

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# What is regulatory agreement?

I It is an agreement between the state and regulated organization whereby:



- **the regulated organization** shall assume the obligations to operate, construct, reconstruct and modernize the network infrastructure facilities as well as other property used for carrying out the regulated activity in accordance with the target values of reliability, quality and energy efficiency approved by the investment and production programs
- **the authorized government agencies and (or) local government authorities** shall provide the conditions for carrying out the relevant activity as well as take into account, in accordance with the basic principles of pricing in the regulated areas when establishing tariffs of such organization, the long-term parameters of tariff regulation and costs for implementing the measures envisaged by the production and investment programs, the obligation for the performance of which is envisaged by the agreement

# Agreement concerning the conditions of carrying out the regulated activity

## Federal Law No.35-FZ "On Electric Power Industry" dated 26 March 2003

The government regulation of prices (tariffs) in electric power industry for a period of not less than five years may be carried out on the basis of the long-term parameters of regulation of the relevant organizations' activity **or on the basis of agreements concerning the conditions of carrying out the regulated activities concluded according to the procedure established by the Government of the Russian Federation (Clause 4 of Article 23)**

Agreements shall be concluded between the state and regulated organizations (Clause 1 of Article 23.4):

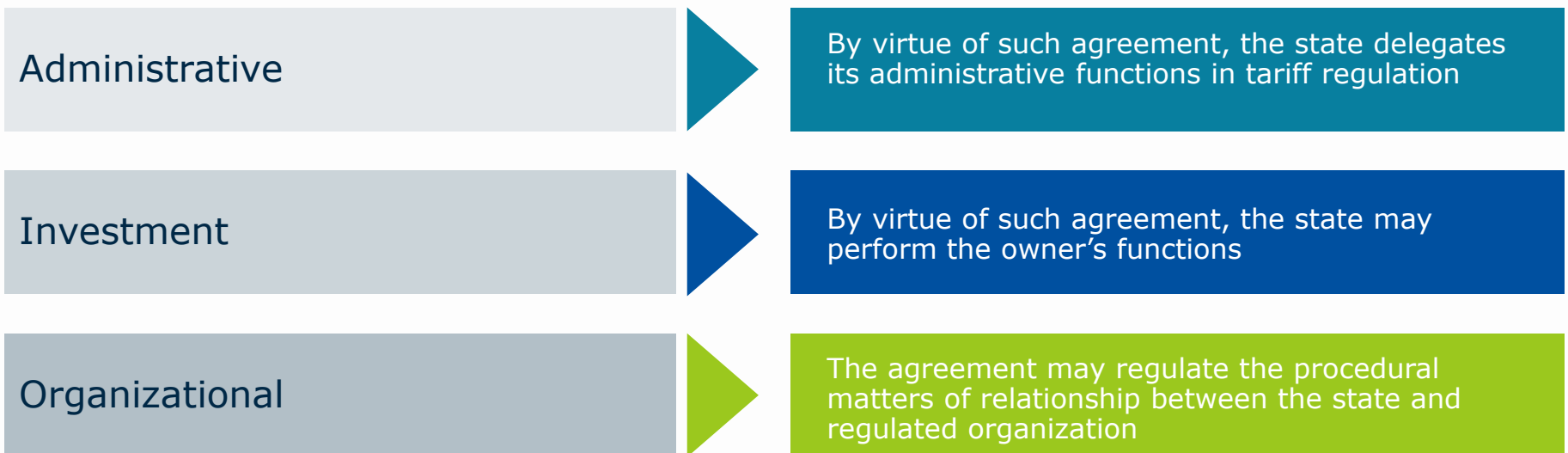
- at the federal level – between FAS Russia (as the federal government agency in tariff regulation) and organization for operating the Unified National (All-Russian) Power Grid
- at the regional level – between the government agency of the constituent entity of the Russian Federation in government regulation of tariffs and a local grid company

The procedure for conclusion, alteration and termination of agreements concerning the conditions of carrying out the regulated activities and a list of essential conditions shall be approved by the Government of the Russian Federation (Article 24) **(a decree has not been adopted)**

# Functions of regulatory agreement

- Agreement shall be concluded between the state and a regulated organization
- The term of the agreement may not be less than 5 years
- The agreement shall be concluded according to the model form approved by the Government of the Russian Federation
- When carrying out the government regulation on the basis of the agreement, cost saving may not be excluded from the required gross proceeds throughout the period of such regulation
- The amount of the saving, which is not subject to exclusion from the required gross proceeds (RGP), shall be determined according to the procedure established by the Government of the Russian Federation

## Contingent classification



# Types of regulatory agreements (RA)

- A regulatory agreement as a contractual form of making investments must ensure the principle of the parity (of parties)
- Depending on its purpose, the regulatory agreement may contain:
  - ▶ limitation of the regulator's authorities
  - ▶ procedure for tariff approval or change
  - ▶ methods of tariff regulation (including those not named in laws and regulations)

## Autonomous agreement

- ▶ Establishes a particular tariff rate and procedure for its change for the duration of the term of the agreement. It does not require administration by a regulator.

Tariff shall be approved at the time of conclusion of the agreement. Tariff may not be abolished or changed during the period of validity of the agreement. Tariff calculation procedure shall be regulated by the parties to the agreement and shall not depend on the existing laws and regulations

## Administered agreement

- ▶ Establishes the tariff calculation procedure or formula and periodicity of tariff approval. It requires administration by regulator.

RA establishes the tariff calculation procedure, the method of tariff regulation or compilation of methods, the periodicity of tariff approval and grounds for tariff revision or abolishment

# Contents of regulatory agreement

**1**

Purpose of conclusion of regulatory agreement

**2**

Project part of the agreement: description of obligations and roles of all parties to the agreement in the project. Time limits, target values, etc.

**3**

Principles, methods, time limits and parameters of tariff regulation. Procedure for tariff approval and revision

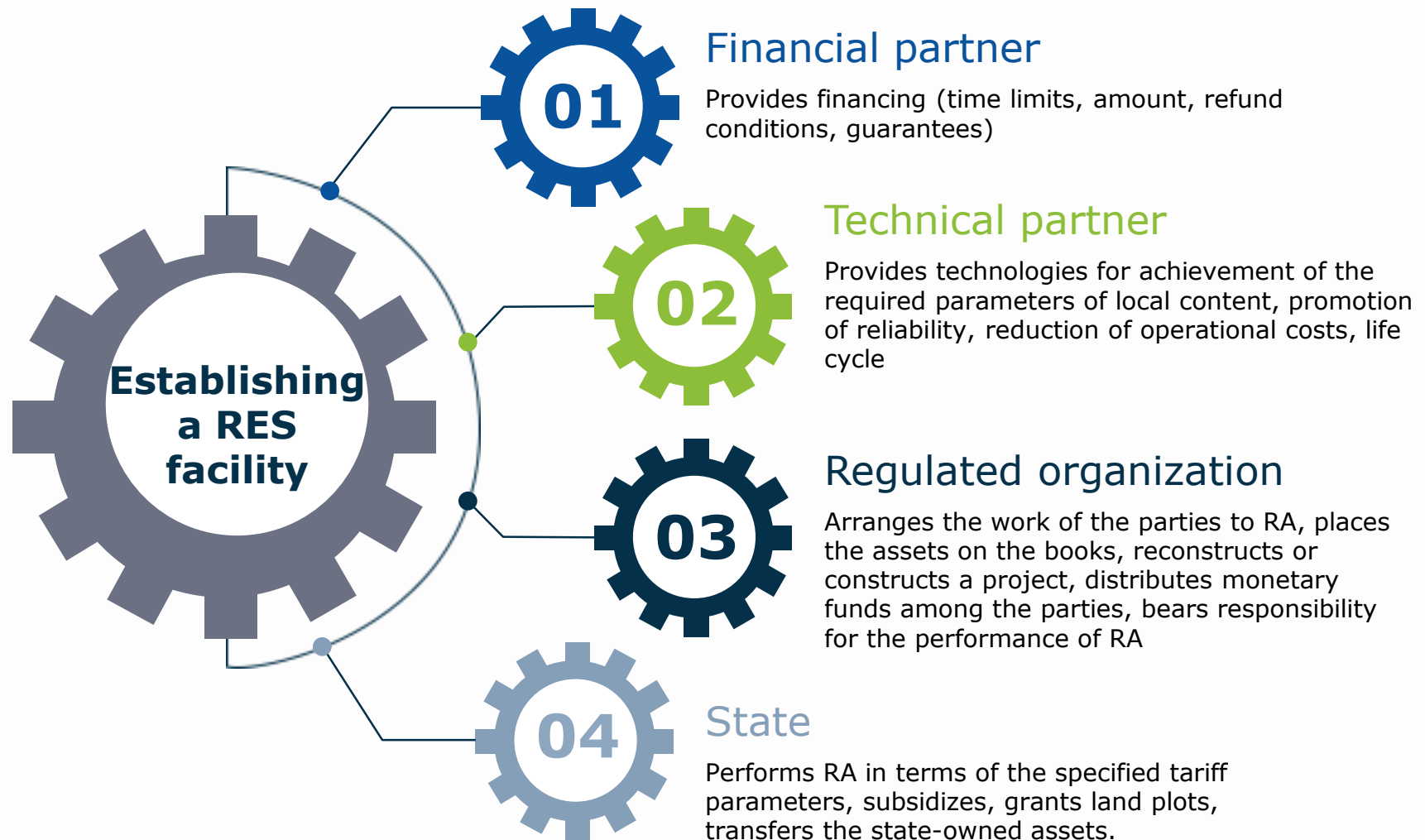
**4**

Principles of relationship of the parties to the agreement: information exchange, implementation control, reporting, document management, liability, etc.

**5**

Dispute resolution and settlement procedure

# Who may be a party to regulatory agreement?

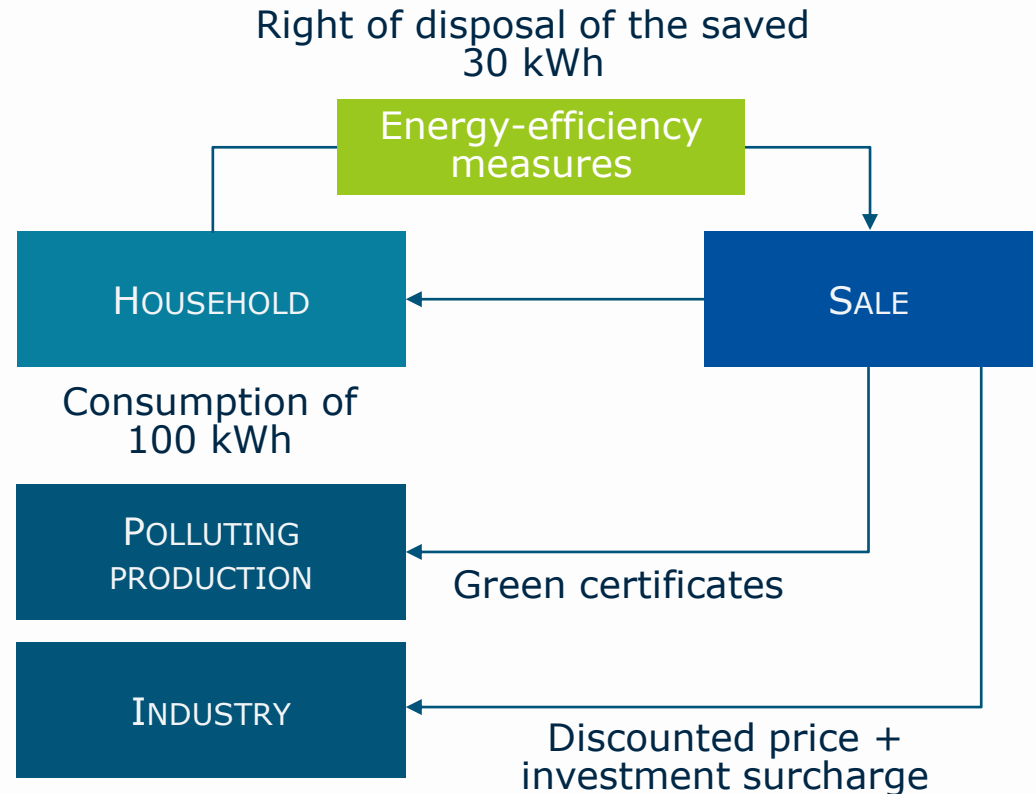




# Microgeneration and RES



What if the ratio of the households' costs for electric power supply would be maintained by volumes rather than prices?



! The slide presents a conventional scheme of consumption and relationship of the parties

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