

Merchant solar projects in Portugal: growing interest and challenges

June 25 2018 | Contributed by [Morais Leitão, Galvão Teles, Soares da Silva & Associados](#)

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Investors are increasingly interested in the development of solar energy projects in Portugal. The country's potential for solar energy is substantial and far from fully realised. In fact, most renewable investment in Portugal has traditionally focused on the wind and hydro sectors, leaving solar energy somewhat overlooked. However, Portugal has recently witnessed a significant increase in capacity-licensing requests for solar energy projects, which has resulted in a shortage of grid capacity. This shortage has already resulted in the establishment of capacity assessment tenders and will likely put pressure on the approval of new investments in the Portuguese transmission network.

Another increasingly obvious trend is increasing M&A activity around greenfield solar energy projects. This has been the case despite the fact that these newly licensed greenfield projects will not benefit from a guaranteed remuneration scheme.

Energy generation regimes

Electricity generation in Portugal is divided into ordinary and special regimes. Special regime generation covers:

- generation activity subject to a specific legal framework, such as electricity generation through cogeneration (ie, renewable or non-renewable) or endogenous resources (eg, wind, solar, biomass or biogas), small-scale generation or generation without network injection; and
- the generation of electricity using endogenous resources (ie, renewable or non-renewable) that is not subject to a specific legal framework.

Special regime generators are remunerated through market schemes or guaranteed remuneration schemes. Since 2012 no guaranteed remuneration scheme has been approved for new projects in Portugal, other than for small-scale, self-consumption or renewable cogeneration projects.

Therefore, renewable projects in Portugal:

- benefit from a feed-in tariff granted prior to 2012 (by means of a public tender or pursuant to a generation licence granted on request of the generator), selling energy to the supplier of last resort, through a power purchase agreement (PPA), the content of which is determined by regulation; or
- were licensed after 2012 and thus operate under a market regime, selling energy under organised markets or through bilateral agreements.

Generators benefiting from guaranteed remuneration sell all electric energy by means of a PPA to the supplier of last resort, which is legally obliged to acquire such energy, paying special regime generators the feed-in tariff that corresponds to their generation technology and the date of

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licensing.

Generators that do not benefit from a feed-in tariff may sell the generated energy under organised markets or through bilateral agreements. To facilitate energy trading by these generators, the law was updated in 2012 to provide for a market aggregator, which would trade the energy generated by special regime generators operating under market rules. However, such entity has yet to be established under a public tender procedure.

With the increasing number of projects being licensed under market rules (ie, with no feed-in tariff or other incentive mechanisms), renewable energy generators are now faced with energy trading under organised markets, without a traditional PPA with the off-taker. The new reality of operating without a feed-in tariff (ie, such as would assure a reliable and determinable financial long-term return) is challenging – particularly as regards meeting bankability requirements. Indeed, these requirements presume stability and predictability of cash flows, which the lack of a feed-in tariff can hinder.

However, stakeholders are exploring alternatives. Those that do not intend to resort to bank financing plan to make their way via organised markets energy trading, which is typical for smaller projects. Others are venturing into the new world of the so-called 'virtual PPAs', as a way to mitigate the price volatility risk of spot-market sales and increase cash-flow stability. A virtual PPA is a power-purchase agreement with no physical delivery of electricity to the off-taker, under which the electricity is sold in the spot market and the floating revenue is exchanged by the generator against fixed payments from a corporate off-taker.

Comment

Despite all its challenges, this new and exciting energy landscape does not seem to be overly forbidding to national and foreign investors, which continue to display great interest in deploying solar energy projects in Portugal.

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