

## SOLAR BOOM IN HUNGARY

Update on Hungary's solar boom – significant benefit to photovoltaic projects licensed under mandatory offtake system upon applications submitted before 2017

### 1. INTRODUCTION

While no more application for Micro PVPP licenses in the mandatory offtake system can be submitted anymore as of 26 April 2018, it seems that the Government acknowledged that the projects licensed under the mandatory offtake system that are applied before 2017 may not be implemented within the strict deadlines prior set in the regulation. The Government therefore allowed the developers (i) to ask for the extension of the implementation period (additional 3 years instead of the former 1 year) regarding such projects provided that such projects reached a reasonable phase and (ii) cancelled the former 10% cutback on the payback period as well. Projects considered as having "special importance for the Hungarian National Economy" enjoy such extension benefit even if they have not yet reached a certain reasonable phase of the project implementation.

The purpose of this update is to provide an overview on the regulatory changes affecting photovoltaic power plants ("**PVPPs**") licensed under the old regime, to highlight the novelties and potential risks of the "new" system and also to summarize the most recent governmental action bringing an end to the mandatory off-take system.

The supporting system of PVPP projects in Hungary can be divided into three categories:

- a) the "old" mandatory off-take system, relating to the applications submitted until 31 December 2016;
- b) the "new" mandatory off-take and green premium system, relating to the applications submitted after 1 January 2017; and
- c) the "new" tendering system.

### 2. THE "OLD" MANDATORY OFF-TAKE SYSTEM

Although new conditions have been put in place for the support of PVPP projects, every PVPP project licensed upon applications submitted until 31 December 2016 is still covered by the "old" rules.

It is important to recall that the licenses under the old regime terminate in case the PVPP does not start to generate electricity within 3 years (1 year in case of applications submitted after 1 January 2016) counted from the date of commercial operation as set in the license. With regard to applications submitted after 1 January 2016, based on the most recent modification of the relevant decree, the above mentioned deadline (date of

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commercial operation plus 1 year) may be extended with an additional 3 years upon request by the license holder, provided that it fulfils certain conditions (verification of (i) the title over the project land, (ii) the existence of the grid connection agreement, (iii) sufficient funds for the implementation, (iv) construction permit and start of construction by opening the e-construction log). (Small and Major PPs are not subject to these rules of termination if their construction has started before 1 July 2016).

In the second half of 2016, nearly 3,000 applications have been submitted to the Hungarian Energy and Public Utility Regulatory Authority ("HEA") for the support of Micro PVPP projects. We understand that these have been awarded by the HEA, leading to the "solar boom" at the end of the year. However, it is questionable whether the projects with an aggregate capacity of approximately 1.500 MW will actually be implemented. Although the support is attractive and offers compelling business opportunities, the 20-25 years reference period has potential risks as well. In addition, developers have to face unexpected legal uncertainties and problems, such as many of the projects are based on project lands classified as agricultural land in the land registry, therefore the reclassification as "lands out of cultivation" is indispensable, or such as the projects have to take into consideration the environmental protection rules (e.g. Natura 2000 limitations).

In order to support the realization of the projects, the Hungarian legislator adopted certain laws and decrees:

- as mentioned above, the implementation period of the projects licensed under the mandatory offtake system upon applications submitted before 2017, provided that such projects fulfil certain conditions, may be extended by 3 additional years (instead of 1 additional year) upon the request of the developers without any cutback on the payback period;
- the DSO, upon the request of the Micro PVPP, is obliged to establish and develop a medium-voltage grid connection point within 3 years at the frontier of the project land, and the costs of securing the grid connection point shall be borne by the DSO;
- the cost of building and development of cables up to 3,000 meters per network user, as well as other facilities necessary in order to secure the connection of Micro PVPPs to the producer distribution system or the public utility system shall be borne by the DSO;
- the reclassification of agricultural lands became easier for Micro PVPPs, as the land authorities of local municipalities are obliged to make the decision on the reclassification based on the documents submitted to them, without performing site visits, within a maximum of 8 days; as well as the reclassification of agricultural lands with quality above the average quality may also be permitted if the Micro PP is within 1,000 meters from the network with capacity to on-load electricity, provided that the project has been declared as "having special importance for the Hungarian economy" and that the project cannot be realized on another land (or trace);

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- However, it is worth to mention that the Hungarian Parliament is planning to adopt a new act on the unified rules of national and regional spatial planning setting further limitations regarding the construction of PVPPs in Hungary, it is expected that such conditions will be applicable as of 1 September 2018.

### 3. THE "NEW" MANDATORY OFF-TAKE AND GREEN PREMIUM SYSTEM

The new system covers new projects only, i.e. whose implementation has not started until the submission of the application. However, already existing PVPPs may also apply for support under the new regime if they are going through significant reconstruction or development (exceeding 50% of the original project costs).

PVPP Projects shall meet the technical requirements as set out in 55/2016. (XII. 21.) NFM Decree of Hungary and Commission Regulation (EU) 2016/631 on the requirements of grid connection, which has been implemented by the HEA in February 2018. These new technical requirements shall apply to new facilities (i.e. which have already been connected to the network, or in case of which the facility owner has concluded a final and binding contract for the purchase of the main generating assets not later than 17 May 2018).

The new regime differentiates between three categories:

- PVPPs with a peak capacity below 0.5 MW ("**Micro PP**s"),
- PVPPs with a peak capacity between 0.5 MW and 1 MW ("**Small PP**s"), and
- PVPPs with a peak capacity above 1 MW ("**Major PP**s").

#### 3.1. FINANCIAL INCENTIVE SCHEME FOR MICRO PVPPS

Newly built Micro PVPPs are eligible for participation in the mandatory off-take system (similar to the old regime), however, developers applying for entitlements under the new regime are facing less generous conditions than before.

Firstly, the benchmark used to calculate the reference return of investment period for Micro PP was reduced:

- in case of applications submitted before 9 November 2017, the benchmark is 13 years;
- in case of applications submitted between 9 November 2017 and 31 December 2017, the benchmark is 20 years; and
- in case of applications submitted after 1 January 2018, the benchmark is 17 years.

Secondly, the budget for support in the mandatory off-take system is now capped:

- in case of applications submitted before 9 November 2017, between 1 January 2017 and 31 December 2021 only a maximum of HUF 20 billion of support can be

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provided to new entries on a first-come, first-served basis;

- b) in case of applications submitted after 9 November 2017, between 1 January 2017 and 31 December 2016 only a maximum of HUF 1 billion of support per year can be provided to new entries on a first-come, first-served basis.

Further to the above, the new regulation introduced new conditions regarding the determination of the capacity of the PVPP (the capacities of PVPPs considered as neighbouring establishments and which are at the same time operated by linked enterprises or partner enterprises have to be added together). In addition, it is also necessary to include certain information into the applications (i.e. verification of right of disposal over the project land, or written consent by the respective landowner to the establishment of the Micro PVPP on the project land).

Note that Micro PPs are entitled to choose green premium (see below) instead of the mandatory off-take system; however, if so deciding there is no possibility to return to the mandatory off-take system.

On 20 April 2018, the Hungarian Government with Government Decree 81/2018. (IV. 20.) of Hungary declared that **no more applications for Micro PP licenses in the mandatory off-take system can be submitted after 26 April 2018**. The decision was adopted strikingly fast and without any foresight. The underlying reasons are unknown; however, the conventional interpretation appears to be that the high number of applications submitted set a risk on the budget. Such fundamental change may reevaluate the existing Micro PP licenses on the market.

## FINANCIAL INCENTIVE SCHEME FOR SMALL PVPPS

Small and Major PVPPs are no longer eligible to participate in the mandatory off-take system as of 1 January 2017. For them, the new green premium supporting scheme and/or tendering rules apply.

The Small and Major PVPPs sell the electricity generated in the market. The financial support in case of the green premium scheme is the so-called "green premium" which is the margin between the "support price" (defined by the Government which currently equals the supported mandatory offtake prices) and the "reference market price" (based on the prices of the Hungarian Power Exchange, HUPX).

For Small PVPPs, the main difference compared to the old (mandatory offtake) regime is that the operators have to sell the electricity on the market, MAVIR has no obligation to take over such electricity. Additionally, the benchmarks applicable for calculating the reference return of investment period was decreased for 12 years, then raised to 20 years, and later decreased to 17 years, with the timeframes as set out above at the Micro PPs. The budget had also shrunk: at first, only a maximum of HUF 10 billion of support could be provided to new entries on a first-come, first-served basis, then it was changed to a maximum of HUF 0,5 billion of support per year, also on a first-come, first-served

basis.

The rules regarding the determination of capacity also apply to Small PVPPs.

#### 4. THE "NEW" TENDERING SYSTEM

For Major PVPPs, the support price is the subject to competitive tendering. Consequently, Major PVPPs are only eligible to participate in the new financial support scheme if they are awarded upon tender proceedings that aim to select the most competitive and most effective projects. Note that under specific circumstances PVPPs outside the territory of Hungary may also apply for green premium. The premium can be awarded for the period of time as defined in the tender (but in no case longer than 20 years). The budget for entitlements is also capped: at first, only a maximum of HUF 15 billion of support could be provided to new entries, then it was changed to a maximum of HUF 1 billion of support per year.

The limitation on bundling also applies to Major PVPPs, which has significant relevance in case of Major PPs, as the PVPPs with an aggregated capacity above 50 MW is subject to a complex licensing regime.

Although the general rules regarding the tender procedures became effective in the beginning of 2017 already, no tender has been issued since then but there is no indication either that such regulation would be cancelled. The tenders shall be issued by the Hungarian Energy and Public Utility Regulatory Authority upon the request of the Minister. Based on tendering rules such PVPPs would be eligible for support which require the least financial support for the realization of PVPPs. The relevant decree regulates the potential maximum financial support on annual basis which yearly amount shall increase by the amount not granted to tenderers in the previous year.

Although there is no publicly available information regarding when and under what conditions the first tender would be issued, the termination of the mandatory offtake regime may accelerate the process taking also into consideration that the Government's communication concerning the promotion of solar projects has not changed.

However, it cannot be excluded that investors who have already taken certain project development steps (such as securing the lands, evaluating the grid connection possibilities, elaborating their business plans etc.) may be in a better position to provide offers in a most probably very short tendering period.

Wolf Theiss and its highly experienced Energy Regulatory and M&A teams are pleased to assist our clients with any questions in relation to RES investments in Hungary.

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For more information about our services, please contact:



**László Kenyeres**

Partner

[laszlo.kenyeres@wolftheiss.com](mailto:laszlo.kenyeres@wolftheiss.com)

T: +36 1 4848 800



**Zoltán Bodnár**

Senior Associate

[zoltan.bodnar@wolftheiss.com](mailto:zoltan.bodnar@wolftheiss.com)

T: +36 1 4848 800

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Faludi Wolf Theiss  
1085 Budapest  
Kálvin tér 12-13.  
Hungary

[www.wolftheiss.com](http://www.wolftheiss.com)