

## Order of preference and a new capacity allocation regime in the Hungarian green energy market

### Decade-long changes in grid connections

8 March 2024

The latest government package to support further growth in green energy was introduced overnight in mid-week, with an order of preference and changes to the rules of the capacity allocation procedure, to help ensure that increased grid capacity demand is dealt with efficiently and fairly. The published rules will bring fundamental changes to the domestic renewables market, putting some developers in an extremely difficult position and imposing even tighter restrictions on access to the grid until 2030.

According to the announcement published by the Ministry of Energy on 7 March 2024, the total public connection demand in the so-called second publication procedure exceeded 10 GW, which, together with the green power projects already in operation and those already granted with grid capacity but still to be implemented, would represent approximately 20 GW of generation capacity. In comparison, the current average demand is 5 to 6 GW of electricity. Even if consumption growth can be expected in the medium to long-term (mainly due to new, energy-intensive domestic investments such as battery production and processing plants), the pace of grid development is not in line with the increased generation needs. A new framework for the assessment of requested capacity is therefore needed, avoiding the need to cancel the entire second publication procedure and preventing investors from receiving unreasonable technical-economic information sheets ("MGT" in Hungarian) from network operators for the purpose of implementing the requested capacity.

### Order of preference, new capacity allocation procedures and other changes

Government Decree No. 54/2024 (III. 6.) (the "**Government Decree**"), published in the Hungarian Official Gazette on 6 March 2024, which was adopted by the Government under its emergency legislative powers based on the armed conflict in Ukraine, seeks to address the foregoing problems as follows:

- 1 The substantive changes contained in the Government Decree apply to the applications from developers participating in the second publication procedure, which is still ongoing.** The provisions are therefore not of a general nature, unlike the previous, similarly swiftly adopted measures of December 2022. The latest provisions, rather, are aimed exclusively at connection applicants within the individual procedure for the allocation of free network capacity, which started on 30 November 2023 and is still ongoing. Projects that already had a right to connect, or at least a valid MGT before that date, are therefore excluded.
- 2 Capacity requests for grid connection beyond 2030 are generally rejected.** Under the Government Decree, network operators will reject all applications for which, in the judgement of the relevant network operator, the earliest date of connection can effectively be guaranteed only after 2030. In other words, in order to ensure predictability of developments, under the current procedure only applications that can be connected at the latest in 2030 are accepted. Applications that can be scheduled after 2030 are rejected in a uniform manner without any specific assessment, regardless of whether individual applicants would be willing to accept

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the technical conditions set out in the sectoral rules that would otherwise ensure the maintenance of the power balance of the electricity system (such as the ability to provide aFRR services).

The decision on rejection will be taken by the network operator no later than 6 May 2024 for projects in the order of preference and 22 March 2024 for all other projects. However, it is not clear whether Article 27(4) of Act No. LXXXVI of 2007 on electricity will apply to the rejections of the network operator. In other words, it is unclear whether the applicants in question will be able to challenge the rejection before the competent technical safety authority, contesting its legality, and it is also unclear what other remedies will be available to challenge the decision by the network operator. The determination of the year of connection is at the discretion of the network operators, which is something applicants have no control over. It is also not clear what the Government Decree, in its Article 1(5), intends to achieve when it provides that the prohibition does not apply to applicants in third place of the order of preference (see below), while it clearly refers to their investments among the projects to be rejected.

**3 An order of preference has been introduced to prioritise eligible applications.** According to the Government Decree, the following applicants will be the ones for which network operators will issue an MGT and, if necessary, a call for a feasibility study to be carried out among the applications received in the second publication procedure. The list will also indicate the order of connection (i.e., the order of connection year in MGTs will be determined up to 2030 based on this list):

- (a) First and foremost, those who have not made a declaration to maintain the capacity request under the call for applications published at the end of 2022, pursuant to Government Decree No. 526/2022 (XII. 16.), or have made a declaration but have not paid the financial security of HUF 4.5 million/MVA by the deadline; but have, however, resubmitted their request with unchanged technical content by means of an individual application made during the second capacity allocation procedure, and wish to connect their power plant to the medium-voltage grid at most;
- (b) thereafter, wind farms that can be connected to the transmission grid at 400 kV may be connected, provided that they are located at the same site but are presented as several individual projects. Each project must have an individual grid connection application, have a combined installed rated capacity of at least 670 MW and the capability to be connected to the public grid via a single common node, where public transformation is not required (i.e., they can transform the electricity generated to 400 kV on their own);
- (c) lastly, those who, as in lit. (a), have failed to make a declaration or to pay the financial security on time, but who, with the same technical content, have submitted a new individual application and plan to connect their power plant to the high-voltage grid.

In other words, in the still open second publication procedure, new wind power capacities and the remaining applications from previous procedures that can be integrated into the system by 2030 at the latest, can be granted the right to connect until 6 May 2024. The order of preference set by the government will then be taken into account by the network operators as an MGT assessment criteria when determining the year of connection. However, this is somewhat contradicted by the fact that, according to an announcement published on 7 March 2024 by the transmission system operator MAVIR, other projects subsequent to those in the order of preference, in fourth place, may be eligible for connection.

- 4 Capacity requests already submitted may be modified or even withdrawn in their entirety.** Under the Government Decree, for projects in the order of preference, applications may be modified or even withdrawn by 22 March 2024 at the latest, by means of a unilateral declaration addressed to the relevant network operator, in order to reduce the installed rated capacity of the power plant in question. According to the Ministry of Energy, the applicants concerned may benefit from a reduction in the installed rated capacity of some of their projects or from the withdrawal of the entire capacity requirement of a project, as this will give them a better chance of being granted a 2030 connection by the network operator, albeit with fewer projects.
- 5 In terms of amended, withdrawn or rejected applications, a proportionate part of the securities and guarantees previously paid will be refunded or released.** In case of modifications, the full amount of the security, proportionate to the reduced installed rated capacity, or in cases of withdrawal, the full amount of the security shall be repaid. With regard to bank guarantees, these shall be released to the applicant within 15 days of receipt of the unilateral statement of withdrawal or modification by the network operator in question. In cases of refusal, the network operator shall repay the security paid or, in the case of a bank guarantee, release it to the applicant within 15 days of the date of dispatch of the information notice on the refusal.
- 6 Connection rights already granted will be published transparently by network operators.** According to the Government Decree, the Hungarian Energy and Public Utility Regulatory Authority (HEPURA) will henceforth be obligated to publish on its website the feed-in connections available for medium and high voltage weather-dependent generating installations with an installed rated capacity of at least 0.5 MW, which have already been commissioned and have a valid and effective MGT or grid connection contract as defined in the sectoral codes. The publication shall include the main parameters of the connection, including, inter alia, the name of the network user, the feed-in capacity, the type of installation and its primary energy source, the earliest date of connection to the network or the calendar year specified in the MGT and the amount of any connection fee. The first such publication will take place no later than 6 April 2024. Although the new HEPURA database is not a public register with decisive effect, it will make it much easier for future investors to map connection parameters.
- 7 An additional financial guarantee will be introduced for those who have not already provided one.** Applicants who ultimately receive an MGT and, where appropriate, a request for a feasibility study from the competent network operator in the second publication procedure, will be required to make a contribution similar to the additional financial security already introduced in December 2022 for applicants by Government Decree No. 526/2022 (XII. 16.). In other words, in addition to the application and capacity reservation security that is already payable, applicants will be required to provide an additional security of 5% of the benchmark investment amount calculated on the basis of the connection capacity applied for and multiplied by the benchmark investment amount as defined in Annex 1 to Government Decree No. 526/2022 (XII. 16.). This may also be in the form of a bank guarantee. The additional security is payable in instalments in the year determined by the effective date of grid connection and in the four years preceding that date, with the applicant paying 1% of the benchmark investment amount each year. In the event that the applicant can prove the existence of a building permit to the network operator, 50% of the additional financial security already paid shall be reimbursed or released to the applicant within 45 days. It is also essential that all those who, for whatever reason, have already paid the additional financial security provided for in Government Decree No. 526/2022 (XII. 16.), are not compelled to pay the newly introduced counterpart.

- 8 A new capacity allocation regime will be introduced by the end of the year at the latest, entirely at the discretion of the government.** One of the key provisions of the Government Decree is that the current capacity allocation procedure, based on a bi-annual publication, will be discontinued by 31 December 2024, and replaced by a completely new system to be developed by the government. No new capacity allocation is expected to take place before the publication of the relevant government decree, which means that the rest of the year will be spent on setting up the new system.

## Uncertainties and shrinking opportunities

Countervailing influences dominate the domestic renewables market. Despite a recent surge in interest in domestic investment (illustrated by an unprecedented number of applications for grid connection), there are continuing government restrictions. The declared aim of these is to ensure that the green policy objectives set out in the National Energy and Climate Plan are achieved within a reasonable, controlled framework, and that the necessary grid upgrades and balancing regulatory investments are made at the same pace as the increased generation capacity. In other words, the potential increase in grid connections in the coming years will mainly depend on the progress of these grid upgrades and balancing regulation developments (such as investments in storage and gas power plants). It will therefore be worthwhile to monitor where and to what extent grid upgrades and balancing regulation projects will be implemented in the near future, and to align future generation investments with this and with the connection points already built or approved.

Rejected applications for connection and increased connection periods may reopen the problems that developers once faced at the end of 2022, such as how to extend the availability period for their already committed project sites. They may also influence the start of the construction phase, the procurement of equipment, project business plans, and ultimately the feasibility of investments, all of which are key issues from an investment protection perspective.

The changes introduced are likely to slow down the development of new projects and make existing investments that are eligible for connection more attractive. This could have a stimulating effect on the sale of green energy projects. In other words, it could make it possible to sell advanced stage developments where grid connection is already a reality. The new central database managed by the HEPURA will also point in this direction, as it will facilitate the review and assessment of projects for sale by making connection rights transparent. This is, however, significantly overshadowed by the fact that the government has started to squeeze foreign investors out of the domestic market through tightening the rules on foreign investment control. This means that substantial demand is likely to come from buyers with majority Hungarian ownership, as foreign partners face a number of obstacles if they want to buy a renewable energy project in Hungary. Read more on this here: <https://www.wolftheiss.com/insights/on-steep-hills-hungary-tightens-rules-on-the-clearance-of-foreign-investments/>.

As connectivity becomes scarcer, the role of on-site electricity generation may increase. Power plants with feed-in protection (in Hungarian: "visszwatt-védelem") that do not feed into the public grid will remain outside these restrictions. In other words, industrial consumers could see a significant increase in the value of locally implemented green energy projects aimed at reducing self-consumption, which the legislator has recently sought to promote through favorable legislative changes.

If you are interested in the potential of on-site electricity generation, we recommend reading our summary here: <https://www.wolftheiss.com/insights/new-opportunities-for-on-site-electricity-producers-and-suppliers-in-hungary/>.

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