Hungarian Energy Market

Notable market changes since the launch of the WT 2022 guide to "Generating Electricity from Renewable Sources"

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Wolf Theiss recently issued its comprehensive guide to "Generating Electricity from Renewable Sources in Central, Eastern, and Southeastern Europe" for 2022 (RES Guide), accessible here. Similar to other countries, there has been some movement in Hungary since the publication of the RES Guide. In a recent conference held to discuss the guide, we focused on these new trends and highlighted some interesting issues, as is summarised below.

1 The Future of Support Schemes

Premium Systems versus Free Market Sale

> As a general trend, statistics show that the financing of renewable projects in Hungary is increasingly shifting towards free market sales.

The feed-in tariff (KAT) system providing mandatory offtake of electricity for a fixed price does not accept new entries since late 2017. The premium system (METAR) resulted in mixed success: in the beginning, developers were enthusiastic, but the trend seemed to slow down after the third and fourth round of the tender. High market prices have also dictated that more consideration should be given to free market sales and financing without state support (for example, by using long-term PPAs).

Simultaneously, more companies have started to opt out of existing support systems and to sell their electricity on the free market instead of the subsidies they had been granted. However, this possibility has been terminated by the legislator in several steps. At first, it was significantly limited, then completely removed a few weeks ago. Thus, those who have been granted state support can no longer leave the support schemes, at least for now.

Industrial and Corporate PPAs

As mentioned above, long-term PPAs are becoming increasingly popular in Hungary. The process is still in its early stages, but there is growing enthusiasm for PPAs on both the producer and consumer side. Investors are also seeing more and more potential in these risk management structures. In our view, those who are at the forefront of this area will have a large advantage in the Hungarian market in the coming years.

Wolf Theiss, Schubertring 6, AT – 1010 Vienna, www.wolftheiss.com

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Tax burdens

Although free market sales are becoming more popular and the general trends point in this direction, projects without state support are still subject to the well-known 31% Robin Hood tax payable after the generated income. This is still a major burden for the non-subsidized projects' cash flow.

2 The Outcome of Grid Connection Reforms

Individual Procedures versus Public Disclosures

The grid connection procedure in Hungary has undergone significant changes in the last year. As transmission and distribution networks have not been developed at the expected pace, the ever-increasing demand for connections has started to pose a serious threat to grid security and system stability.

Therefore, the legislator has introduced a new grid connection procedure for the allocation of available free capacities. Those who want to use these capacities need to go through a tendering procedure and pay a number of cash deposits. However, even after this, it is not guaranteed that they will be granted with grid access.

There is also a so-called individual procedure, but in this case, the developer has to pay for the costs of grid development necessary to deliver the required grid connection capacity.

Moreover, a new limitation can be set by the system operator, which is the absolute maximum for weather-dependent generation capacity to be connected to the system in order not to jeopardise system security. Furthermore, renewable procedures now have to take active part in system stability (by, for example, being capable of centrally organised curtailments, or by providing aFRR services).

Predictability and Transparency

The grid operators communicated there is zero free capacity available in the Hungarian system, and the next publication is expected to take place no earlier than November, so we expect that the individual procedures will gain ground, notwithstanding the fact that it will raise the development costs.

It is also clear that the Government wishes to provide significant financial support for the development of the grid through various funds, and some smart solutions (such as energy storage) are also becoming more popular. So, this temporary phase of grid connection scarcity might change in the long run.

However, it is unclear how these developments will be implemented, and there is no transparency or predictability about the plans of the system operator and the government.

3 The Role of Windfall Taxes in the Spread of Investments

The Obligation to Remain in the Support Schemes

Recently, the Hungarian Government has introduced certain special extra profit or windfall taxes. Some of these affect subsidised power producers. In brief, those who have been granted with feed-in tariff or premium subsidies and decided to leave these support systems while it was possible in the past need to pay a new 65% income tax calculated on the basis of the profit they make by selling the electricity on the free market for the currently very high prices. They also need to pay if they decide not to conclude an agreement with the system operator for the settlement of the subsidies, despite the fact that they have been granted with them.

This new tax and the fact that producers can no longer exit the support systems together will mean that those who were granted with a subsidy will stay in these systems.

Onsite Projects and Consumer-Centred PPAs

Because the tax is calculated on the basis of electricity that is injected into the system, if there is no use of the public grid, there is no obligation to pay such taxes. Therefore, we anticipate that onsite and rooftop projects are going to be more popular in the future.

We also expect that consumers will initiate more PPAs than the developers, so legal support and appropriate project management services will certainly be required for them.

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About Wolf Theiss

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For more information about our services, please contact us:

Laszlo Kenyeres
Partner

E laszlo.kenyeres@wolftheiss.com
T +36 1 484 8800

Adam Lukonits
Associate

E adam.lukonits@wolftheiss.com
T +36 1 484 8800