

Mixed fuels

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Since the withdrawal of US IPPs following Enron's bankruptcy, most Spanish CCGT projects are now being developed by incumbents. Iberdrola, Union Fenosa, Endesa and Gas Natural have ambitious programmes, in some cases enhanced by the acquisition of ex-Enron assets in Spain.

Cash-rich and on home ground, none of these companies are likely to project finance.

But the days of the IPP are not completely over. ESB closed a Eu700 million financing for the first IPP plant in the Spanish market early this year (Bizkaia Energía). The AES Cartagena project is now in syndication and Intergen has restarted its 1200 MW project in Catadau (Valencia). Electrabel and Gaz de France are also in the first phases of several projects.

And the approval of Royal Decree 1432/2002 of 27 December creates new opportunities for power plant financings in its attempt to improve the legal framework for electricity producers. This has had already some positive effects. A company that was financed on a corporate basis, with shareholder guarantees, is now likely to seek non-recourse refinancing.

The main features of the new regulation

? The electricity tariff will take into account as a cost the price to be paid to producers in the market, bearing in mind the best possible forecast for gas prices.

? The electricity tariff will be increased or reduced yearly up to 1.40% (the government will consider the increase being equal to 1.40% if it is understood that at the end of the year 2010 the stranded costs ? CTC ? cannot be recovered).

? Additionally the electricity tariff will be increased or reduced yearly up to a 0.60% if certain matters not depending on producers change. The new tariff will include the revision of the assumptions made for the calculation of the tariff of the two previous years in the following cases:

? If the final electricity demand is 1% higher or lower than that forecasted.

? If the interest rate is 50 basis points higher or lower than that forecasted.

? If the premiums for renewal energies are 50% higher or lower than that forecasted.

? If gas price is 5% higher or lower than that forecasted.

In general, several mechanisms are put in place in order for the tariff to be sufficient to pay for all costs of the system including remuneration to producers and to avoid the deficits that existed during the years 2000-2002. While none of these measures give a specific price guarantee to independent producers they do create the adequate framework for a reasonable stability of the revenues of the system. This new tariff methodology has been welcomed as an important tool for supporting new investment.

LNG/regasification

Early this year the first gas infrastructure in Spain reached financial close (Bahia de Bizkaia Gas, sponsored by Repsol, BP,

Iberdrola and the Basque government). The project consists of the construction and operation of an LNG regasification plant with an initial capacity of 400,000 m³/h, plus an expansion of 400,000 additional m³/h. The financing was provided by the EIB through Eu200 million loan, fully insured by MBIA, with a limited guarantee from the sponsors of the project during the construction period. Special attention was paid to the calculation of the system remuneration and settlement system as well as third party access matters. MBIA and EIB shared the security package which was adapted to the specific transaction and Spanish law requirements including, for the first time the choice of Spanish law for the insurance policy.

Financing of the Sagunto regasification plant, sponsored by Union Fenosa, Iberdrola and Endesa, is under way and will follow probably use the same EIB/monoline wrap structure. The Reganosa regasification LNG plant in Ferrol (sponsored by Caixanova, Caixa Galicia, Grupo Tojeiro, Sonatrack and Union Fenosa) will seek financing by the end of this year.

Regasification plants seem to be the choice of the Spanish government for allowing gas supply into the Spanish market due to the difficulties in increasing the France-Spain inter-connection and the uncertainties surrounding the Medgaz project (the new pipeline between Algeria and Spain).

Financing of LNG vessels (gas tankers) has also been extremely active during the last few years. Through a combination of different structures, use of subsidies, tax breaks and lately of the so called tonnage tax, several deals of approximately Eu150 million each have been closed, mainly for Naviera Elcano and Naviera Tapias, on vessels to be used by Repsol and Union Fenosa. There is no doubt that this sector will see the closing of more deals in the near future.

Renewables

Financing of renewable energy projects mainly wind farms is booming. The market has seen the largest wind farm financing in the world the Eu900 million facility for EEE and very sizeable deals like Dyta Eólica (approximately Eu600 million) are expected to close later this year. Likewise, new financing structures are in place, like the financing through securitization of the wind farm business acquired by Nuon from Abengoa. The main features of the legal regime that make possible such financings are the following:

Tariff System

? The main devices of protection created by the Spanish regulator have been: (i) the right of renewable energy producers to receive a premium for the produced electricity, and (ii) the obligation on the nearer distribution company to acquire the electricity produced by the generator.

? In the case of wind farms, the premium shall be fixed by the government, in such a way that the selling price of the electricity produced by these utilities, shall not (i) fall under 80%, nor (ii) exceed 90%; of the average price of electricity, calculated by dividing the total revenue of the supply of electricity by the volume of supplied electricity. This provides wind farm generators with a higher revenue per MW than generators under the ordinary regime, since the price paid by end consumers for the supply of electricity includes some additional elements other than mere generation marginal prices, such as commercialisation, transport and distribution fees, permanent costs of the system, diversification and security costs.

? Utilities under special regime have the option to receive either (i) a fixed premium per produced MW to be added to the market price of the electricity, or (ii) a fixed price per MW for all the electricity produced in one year, regardless of electricity market price fluctuations.

Both systems, the one based on the premium and the one based on fixed prices, need to comply with the 80-90 requirement described above and therefore are updated by the government every month of December with effects as of the following 1 January to ensure that fluctuations occurred in a certain year in the price of electricity for consumers are taken into account in the premiums and fixed prices applicable to utilities under special regime in the following year.

For the determination of the premiums, the government shall take into consideration the voltage of the electricity delivered to the grid, the effective contribution to the improvement of the environment and to the saving of primary

energy, and the investment costs incurred, with the aim of achieving reasonable profit rates with reference to the cost of funds in the capital markets.

Reliability of Royal Decree 2818/1998

? This system of incentives included in Royal Decree 2818/1998, does not have a temporary limit since (i) the environmental benefits of this type of utilities needs to be internalised in the Spanish electrical sector and (ii) their special features and technological standards entail higher costs that make such facilities unable to compete in the free market.

? It is true however that the sixteenth transitory provision of Law 54/97, also instructs the government (i) to set up a ? Renewable Energy Fostering Plan? with the aim to achieve that in 2010, 12% of the total demand of energy in Spain is covered by renewable energy sources and (ii) to bear the Renewable Energy Fostering Plan's goals in mind when determining the precise premiums, but this should not be construed as an absolute temporary/quantitative limit to the premiums, but just as a goal that the government has to pursue in the general energetic policies.

? It is important to take into consideration that EC Directive 2001/77 which determines the basis for the future EU framework of renewable energy production refers to the national targets as ?indicative targets? and has given support to the above said principle of legitimate confidence by establishing that any proposal of EU framework shall, among other goals, foresee sufficient transitory periods of, at least, seven years, for national renewable energies support systems and should also maintain the confidence of investors.

? Additionally the government, in the determination of the premiums, has to consider issues such as the investment costs incurred by the investor, with the aim of achieving reasonable profit rates with reference to the cost of funds in the capital markets, and this principle should also be considered in any amendments to the legal framework applicable to renewable energy generation, at least, for those utilities already in place. All this, in our opinion, protects the investors against arbitrary acts of the government.

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