

AMERELLER



INVESTING IN RENEWABLE ENERGY IN EGYPT

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Investing in Renewable Energy in Egypt

The Legal Framework



Zafarana Wind Farm, Red Sea, Egypt (360 MW), the largest wind farm on the African continent.

The Market

Egypt has a tremendous potential for renewable energy: the coastal areas on the Red Sea are among the world's finest wind regions and the vast desert areas in the country enjoy intense solar radiation. The Government, moreover, has supported the development of renewable energy for a long time. In 1986, the New and Renewable Energy Authority (NREA) was set up as a specialized government entity, also acting as a project developer, and in 1993 the first wind farm was installed near the beach resort of Hurghada on the Red Sea Coast. At present, the 360 MW wind farm in the Zafarana area (also on the Red Sea Coast) is the largest fully operational project of its kind in Africa and the first Egyptian concentrated solar power (CSP) plant recently commenced operation in Kuraymat, south of Cairo.

While the early projects were exclusively financed through international development cooperation, in 2009 the Egyptian Government has started to tender privately financed wind farms based on a BOO model. It is generally held that private financing will be the key for the future development of the renewable energy industry. The establishment of a feed-in tariff system and the enactment of the new Renewable Energy Law in 2014 conform to this trend. The Government is clearly committed to further developing renewable energy and has set the – ambitious – target that by 2020 renewable energy will provide 20% of the growing electricity demand in Egypt. In addition, the promotion of renewable energy will help to develop an indigenous renewable energy industry.

The Egyptian renewable energy market attracts international suppliers, developers, operators and financial institutions in addition to consultants. In addition, there are a number of Egyptian renewable energy companies, some of them with a strong regional/ African focus.

Investment Climate

Recent political changes have not affected Egypt's long term commitment to renewable energy. Whereas the Revolution of 2011, in the short term, has resulted in a significant decline of foreign direct investment flowing into the country, in the medium and long term there are significant opportunities, in particular in areas such as renewable energy. There is a steadily growing electricity demand. In addition, the energy subsidies are gradually being alleviated. Energy intensive industries, such as cement, aluminum and tourism, are in need of alternative energy sources – and in the absence of subsidies for conventional energy, renewable energy are a reliable, and commercially viable substitute.

The promotion of renewable energy is a political aim that is shared across the political spectrum in Egypt. Renewable energy and climate change further are an important area for economic and development co-operation on the international level.

Energy Law

In December 2014, Egypt has enacted a new Renewable Energy Law (Law 203/2014) which is a major step towards establishing a comprehensive legal framework for renewable energy projects.

The law envisages the following project structures (Art. 2):

- Projects which are tendered and operated by NREA. So far, the majority of renewable energy projects are owned and operated by the state.
- Projects which are tendered by the (state owned) Egyptian Electricity Transmission Company (ETC) on a BOO (Build-Own-Operate) basis. The private investor builds, owns and operates the project and enters into a long term power

purchase agreement (“PPA”) with ETC. Since 2009, BOO models have been used as an alternative to state owned projects.

- The establishment of projects by private investors who sell the electricity generated by those projects to ETC on basis of the feed-in tariff enacted by Decree 1947/2014. This structure is new, and takes advantage of the feed-in tariff enacted in October 2014.
- Private investors can enter into direct PPAs with (large) consumers and will be granted access to the grid for that purpose. This structure is also new and addresses the pressing needs of energy intensive industries in Egypt (in particular cement).

The new law provides considerable flexibility in implementing renewable energy projects. It also permits a gradual move away from state (NREA) administered projects to privately financed projects.

The feed-in tariff was enacted in October 2014 and provides for a sophisticated pricing system, differentiating between solar and wind projects as well as project sizes. The feed-in tariffs will be granted for 25 years for solar projects and 20 years for wind projects. The pricing system is complex. Key indicators which are relevant to international investors are:

Solar:

500 KW up to 20 MW: 0.136 USD

20 MW up to 50 MW: 0.1434 USD.

Wind:

From 0.0957 USD to 0.1148 USD during the initial five years and then between 0.0460 USD to 0.1148 USD for the remaining 15 years of the project, depending on the hours of operation.

Although the prices are determined in USD, the feed-in remuneration will be paid in EGP. According to the formula used, the investor will have to bear part of the foreign currency risk. In addition, a foreign investor will have to manage an EGP revenue stream. This is clearly a compromise.

The government shall provide private investors with project land on basis of a usufruct (manfa'). A private investor establishing a project larger than 500 KW must establish an Egyptian project company under the Investment Law (Art. 3 and Art. 4).

The operation of a renewable energy plant requires a license which is granted by the Electricity Regulatory Authority (ERA).

ETC (or the distribution company), as the case may be, is under a legal obligation to connect a renewable project to the grid (Art. 6 (1)). In addition, they are under an

obligation to purchase the electricity generated by qualifying projects and, if the take off is not possible, the investor is to be compensated (Art. 6 (2)).

The Implementing regulations have yet to be issued by the Council of Ministers.

Public Tenders

Public tenders are governed by the Tender Law (Law 89/1989). The Tender Law by and large conforms to international standards and government projects normally are awarded on basis of a public tender. The Tender Law however is not in all respects tailored to the requirements of large scale projects:

- The Tender Law does not explicitly permit deviations from the tender documents, although in practice bids will often contain certain deviations and this has been accepted by the tendering authorities in the past. In particular, with regard to the legal conditions of a tender, there often is only limited room for amendments. This makes a proper risk analysis upfront even more important.
- The Tender Law does not envisage contract negotiations with the successful bidder. However, it is customary to hold a “clarification session” where certain contractual terms are also discussed.
- A tenderer without a legal presence in Egypt must appoint an Egyptian “tender agent” which acts as point of contact for the tendering authority.

If and to the extent the project is financed through international development co-operation, the procurement rules of the relevant financing institution will apply in addition to the Tender Law. Often, the financing institution would also support the tender process, e.g. through a consultant.

Contracting with the Public Sector

Under Egyptian law, special rules apply to “administrative contracts” which are, broadly speaking, all contracts which are entered into with the Government and government agencies and are related to a public good or service. The rules on administrative contracts are contained in the Tender Law and are supplemented by the case law of the Egyptian administrative courts. The rules applicable to administrative contracts can differ substantially from the provisions governing private contracts:

- Administrative law provides for certain “privileges” of Government, including the right to terminate the agreement “in its discretion.” If the termination is not based on “just reasons”, the private partner must be compensated. In addition, Government may impose certain fines in case of delay and there are rules which permit for an adjustment of the contract in the light of “changed circumstances”.

- Contracts with government entities are reviewed and must be approved by a special entity of the State Council.
- Disputes arising out of administrative contracts fall within the competence of the administrative courts.

In the case of renewable energy projects, many agreements qualify as administrative contracts, whether because the project as such is carried out by a state developer (NREA) or because the Government is a party to the concession and land use agreements.

Land Use

Most of the land used for renewable energy projects is Government owned. The allocation process can be lengthy; in particular if several Government entities are involved. The land is allocated to the investor on basis of a usufruct (manfa'). The usufruct is a real right attached to a piece of land permitting the beneficiary to use and exploit the land. It is advisable to register the manfa' in the land register, although in remote rural areas this tends to be a difficult process. More recently, the Government has started to allocate land to NREA which is designated for renewable energy projects. This should facilitate the allocation process (as the investor will only be dealing with NREA instead of a multitude of different government entities).

EPC Contracts

EPC and supply agreements regularly are based on the FIDIC models, supplemented by Egyptian law. The rules on supply and construction contracts are contained in the Egyptian civil and commercial codes, which are derived from French law. Egyptian law, in particular, provides for "decennial liability" attaching a 10 year warranty to the design and construction of "fixed installations". Although it is questionable whether a wind farm or CSP plant which will be dismantled at the end of the contractual period qualifies as a "fixed installation", there is no court precedent that would support this view. The rules on decennial liability are mandatory. Egyptian courts apply them to all projects located in Egypt, irrespective of the law determined as the proper law of the contract.

Project Finance

Egypt has a long history of project finance. The structures and techniques developed in the oil and gas sector can be applied, with certain modifications, also to renewable energy projects. Large projects tend to be financed (and syndicated) on the international market, with loan documents based on the LMA model (often governed by foreign law). Smaller projects also can be financed locally, on basis of credit agreements governed by Egyptian law. Egyptian law sets caps on interest rates. Egyptian courts hold that the

respective provisions are mandatory and that they also apply in cases in which foreign law has been determined as the proper law of the contract.

Taking security can raise complex issues, among them:

- There are restrictions on the mortgaging of government land. This means that in many instances the project site cannot be used as security.
- Direct agreements are fairly common but can take long to negotiate, depending on the counter party.
- Under Egyptian law, a pledge over assets normally requires possession. This also can be constructive possession which is exercised through a trustee. This structure, however, makes enforcement of the security more difficult.
- A retention of title provision provides limited protection to a supplier. The supplier risks losing its rights over an asset when the asset is firmly and permanently attached to a piece of land. In addition, retention of title does not always have effect vis-à-vis third parties if the buyer becomes insolvent.
- Egyptian law does not prevent an assignment of future claims. The law, however, requires that the claims assigned can be precisely determined.
- Shares in a project company can be pledged. Enforcement proceedings, however, can be cumbersome.

Designing an acceptable security package thus requires careful planning.

CDM and Export of Green Electricity

Both the Clean Development Mechanism (CDM) and electricity export can provide additional funding for renewable energy projects. The potential, however, so far has not been fully developed.

Egypt ratified the United Nations Framework Convention on Climate Change in 1994 and appointed the Egyptian Environmental Affairs Agency as DNA. The number of CDM projects however is low. Even in times where carbon prices still were high, the bureaucratic hurdles made the use of the CDM in Egypt not very attractive.

The concept of producing solar electricity in the Mediterranean “sun-belt” and then to export it to Europe is intrinsically linked with the DESERTEC initiative. The idea is to generate the green electricity at the place where the natural conditions are best – and to permit producers from non EU member states to sell green electricity at attractive prices. The EU Renewable Energies Directive 2009/28 for the first time permits the “import” of green electricity from non-member countries and to offset it against the national quotas imposed under the Directive. The import into the EU however requires a *physical* interconnection and it does not permit virtual trading schemes or barter structures (e.g.

“gas swaps”). So far no connection to the European grid exists and Egyptian projects therefore cannot benefit from exporting electricity to Europe. Moreover, in view of the electricity shortage in many parts of the country, the idea of exporting electricity presently is viewed rather sceptically.

Investment Protection

Egypt has ratified the ICSID Convention and has entered into bilateral investment treaties with many countries, including Germany (2005), Denmark (1999), Italy (1989), Spain (1994) and the UK (1975).

Dispute Resolution

Disputes arising out of administrative contracts fall into the competence of the administrative courts. Civil disputes are heard by the civil courts. In 2008, specific Economic Courts were set up as a specialized branch of the judiciary, as being competent to hear commercial disputes.

Arbitration clauses are widely used. In administrative contracts, an arbitration clause requires the consent of the competent Minister. Many agreements with the Egyptian state envisage arbitration according to the rules of the Cairo Regional Centre for International Commercial Arbitration (CRCICA). The CRCICA rules of arbitration are by and large based on the UNCITRAL Model.

Egypt has ratified the New York Convention (1958).

Amereller Legal Consultants

The Firm

AMERELLER LEGAL CONSULTANTS is an international law firm with offices throughout the Middle East and Germany. The firm specializes in corporate and commercial law in the Middle East and is one of the few law firms with a direct presence in key markets in the region. This enables us to keep our finger on the pulse of this dynamic legal environment and provide tailored advice to clients consistent with evolving practices in the Arab World.

We have had leading roles in some major transactions in the Middle East, especially in Egypt, the UAE, Libya, Iraq, Saudi Arabia, Syria, Oman and Yemen. Clients consult us for expert advice and commercial guidance that we provide. Our personalized focus on supporting clients across country borders and industry sectors is central to our firm's culture. We aim to provide our clients with the professionalism, depth of expertise and quality offered by top-tier international law firms, together with the personal attention and practical knowledge available only through on-the-ground presence.

AMERELLER LEGAL CONSULTANTS has offices in Cairo, Damascus, Dubai, Ras Al Khaimah, Tripoli, Baghdad, Basra and Erbil, as well as in Berlin and Munich. Our eight partners lead a team of 40 internationally trained, multilingual and experienced lawyers, who are sensitive to the cultural and legal nuances of conducting business successfully in the Arab World. Through our network of best friend firms we cover all jurisdictions in North Africa and the Middle East – including Iran and Afghanistan.

Our Renewable Energy Practice

We regularly advise project sponsors, contractors, suppliers and financial institutions on renewable energy projects across the region and have been involved in many of the significant projects to date. Due to this experience, we are at the forefront of legal developments in the field of renewable energy. We have advised on the first privately financed renewable energy project in Egypt. Among our projects are initiatives such as DESERTEC, that aim at promoting the large scale installation of renewable energy projects across North Africa or investors active in MASDAR City and other eco-friendly mega projects.

We are regularly called by international organizations and governments to advise on renewable energy regulation and related legal issues. We follow policy debates closely and are familiar with both the international standards and local business customs. Our regional presence provides us with contact to government authorities and regulators.

We further advise clients on the legal aspects of the CDM and the structuring of energy trading schemes.

Recent Transactions

AMERELLER LEGAL CONSULTANTS have been active in the MENA markets for many years. Our recent experience in the field of renewable energy and climate change includes:

- Advising an international consortium in Egypt on the bid for two 50 MW windfarms to be operated under the new feed-in tariff;
- Advising an international supplier of wind turbines in connection with the market entry in Egypt (commercial law, corporate law, energy law, environmental law);
- Advising an international technology company on the bid for a 300 MW windfarm located on the Egyptian Red Sea;
- Advising a German solar company in relation to the bid for a 100 MW photovoltaic plant in Abu Dhabi;
- Advising Desertec Industrial Initiative (dii) GmbH across the MENA region;
- Advising the Regional Centre for Renewable Energies and Energy Efficiency in Cairo on the organisational structure, international legal status and financing structure (donor coordination);
- Advising a Middle Eastern government entity on legal issues arising in connection with the tendering of wind farms on a BOO basis;
- Advising an international construction company on the bid relating to the construction of a barrage on the Nile financed by an international development bank;
- Advising a consortium of energy companies on the structuring of gas swaps for the export of green electricity;
- Advising an international technology company on trade law aspects of importing components for solar plants in various Middle Eastern jurisdictions;
- Advising an international chemical company on complying with the ecological standards in connection with setting up in Masdar City, UAE.

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