WINDS OF CHANGE BUFFET GREEN ENERGY SECTOR

By PERRY GOURLEY

SENTIMENT around the renewables industry in Scotland of late has proved as changeable as the Scottish weather on which it relies.

Not long after figures showed renewable electricity had been confirmed as the nation's largest source of power – meeting the equivalent of almost half of its needs in 2014 – the UK election result signalled the start of a shift in policy towards support for green energy which sent a chill through the industry in Scotland.

Chancellor George Osborne used his first budget of the Conservative majority government to remove the exemption of renewable generation from the Climate Change Levy, a step which immediately reduced financial returns from projects. That was followed by a decision to close the Renewables Obligation (RO) subsidy support mechanism to new onshore wind projects and some solar schemes a year earlier than planned.

Major changes to the Feed-in Tariff (FiT) subsidy scheme for smaller renewable projects are also expected to come into force from the beginning of next year. Some of the detail on the changes, including grace periods for projects already being planned, is still to be finalised, but the announcements have been met with broad dismay by the industry north of the border. Trade body Scottish Renewables has warned the early closure of the RO alone could cost Scotland £3bn of investment in larger renewables projects.

Joss Blamire, senior policy advisor for **Scottish Renewables,** also warns the proposed FiT cuts were "quite simply terrible news" for smaller schemes, such as turbines or solar panels installed by businesses to reduce energy costs. "The levels of reduction in support announced will severely curtail development of small-scale onshore wind and solar projects and endanger jobs and investments across the country," he says.

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Nicolas McBride, bto solicitors (below)

Nicolas McBride, a partner at **bto solicitors**, says while it is still too early to tell precisely what the long-term impact of the changes will be, the subsidy cut for onshore wind in particular is likely to hit Scotland hard. "A significant proportion of the UK's generating capacity from wind is located here and of the estimated 3,000 proposed UK wind farms which will be directly affected by the early closure of the RO, over 70 per cent are located in Scotland," he points out.

"The renewables sector in Scotland is also heavily dependent on foreign investment and we may well see a reduction in the availability of investment funds. There are always a small number of projects which, at least initially, would require RO income to meet in order to meet funders' requirements and without it they may well be unable to proceed."

David Cruickshank, partner and head of renewables with **Maclay Murray & Spens**, says there are serious reservations amongst investors that the proposed cuts are too deep and too fast. "Investors in the onshore wind and solar PV [photovoltaic] sectors in particular are looking for clarity around how proposed grace periods for their technologies will operate and whether or not, in practice, this will allow a meaningful number of projects that have achieved certain defined milestones to proceed under the existing RO or FiT."

Timothy Pitt, partner and renewable energy specialist at law firm **CMS**, stresses while the ending of subsidies will undoubtedly have an impact, there will continue to be a market for operational onshore wind farms as investment assets. "There are also other forms of renewable energy options which both Scotland and the rest of the UK can further exploit, including offshore wind, solar and hydro power," says Pitt.

"With the Smith Commission looking at further devolved powers there is a prospect of Scotland taking greater responsibility over energy policy. This could present a real opportunity for economic growth as most renewable energy sources, even solar, are relatively abundant north of the border," he adds.

Andy Drane, partner at law firm **Davidson Chalmers**, also believes the Smith Commission outcome could be one to watch. "On one hand, greater control in this area could enable Scotland to take a different path in committing to onshore wind and other forms of renewable energy going forward. It is, however, questionable whether the Scottish Government could sustain the same levels of subsidy which have been paid by the UK Treasury which have enabled most onshore developments to be viable."

The full impact of the changes for future onshore wind developments won't be known for some time but bto's McBride also believes it may not be as severe as feared. "Previous evidence, such as the closure of the RO for solar projects, would suggest while there may be some investor uncertainty at the moment, in the long term investment will not switch away from onshore wind," he says.

"In fact, the unexpected availability of solar power as a result of the recent growth of solar projects in the UK has been cited as one of the reasons given for the early closure of the RO

A turbulent year for wave energy saw Pelamis Wave Power fall into administration

The Solar Trade Association Scotland says businesses are looking to get projects installed before proposed cuts to the Feed-in Tariff scheme come into force

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Joss Blamire, Scottish Renewables (below)

for onshore wind. Given the fact the solar power sector was subject to the closure of its own RO just a couple of years ago this suggests the outlook for onshore wind is not as bleak as some might think."

But the UK Government's changes could see foreign investors look to get compensation over projects already in the pipeline, according to **Pinsent Masons'** dispute resolution expert John Gilbert. He believes international investors, who have

collectively pumped billions into Scottish renewables, could raise a claim for compensation under the Energy Charter Treaty (ECT) which was introduced to protect the transmission of energy in Europe.

He says: "European investors, and German companies in particular, have invested many millions into Scotland's renewable sector in the belief it was a safe investment with limited risk. Under the ECT, investors can't challenge the government's decision on subsidies, but they may have a good case for seeking damages on the basis their investments have been undermined and devalued."

David Bone of **Harper Macleod** also believes there is a possibility the UK Government could face difficulties with implementing some of the sweeping changes. "This UK Government has, not for the first time on renewables, shot from the hip first and started thinking afterwards.

"European state aid and

discrimination regulations mean they could easily run into trouble with their proposals if they target specific sectors or parts of sectors, so I think there is some way to go yet before there are firm amendments in place."

Bruce Farquhar at **Anderson Strathern** says the severity of the proposed reductions to the FiTs had largely taken the firm's clients by surprise and some were already looking to switch investment to other sectors. "We anticipate a large number of projects which are not capable of being delivered within that timescale will be halted while different funding mechanisms are explored.

"Where the funding models no longer stack up, there is very real risk the projects will simply be terminated and costs incurred to date will be written off. Developers are already looking at other types of projects – which are not necessarily in the renewable energy sector."

Harper Macleod's Bone believes the changes will not mean the end of onshore wind projects. "But they will focus developers' minds on the windiest sites and in trying to develop them as economically as possible, using larger turbines and sophisticated wind data analysis to obtain the maximum output from sites. It will also favour the larger developers who are not totally reliant on subsidies."

Above: The 140-turbine Beatrice offshore wind project is planned for construction in 2016

Ian Williams at **Campbell Dallas** says plans to end a process known as pre-accreditation under the FiTs was also a blow to the sector. "With pre-accreditation it was possible to build a financial model with an agreed FiT rate and have a reasonable idea what the future might hold. Without this, the ability to predict what FIT rate might apply introduces huge uncertainty and is likely to deter many applicants."

Mark Stewart, **Baker Tilly's** head of infrastructure and renewable energy in Scotland, says he believes the proposed cuts to the FiTs "could spell the end of the solar industry in the UK". "There could now be a mad dash to complete renewable deals before the likely closure of the FiT scheme to new applicants post January 2016," he warns.

Ahead of the changes coming into force John Forster, chairman at the recently launched trade body Solar Trade Association Scotland, says there is already evidence businesses are looking to get projects installed before the proposed cuts come into force. "The current returns for commercial rooftop solar are excellent and I think a lot of companies will now be looking to take advantage of that before the cuts take effect."

But he says the huge surge in demand that is the likely outcome of the FiT review "will deliver the worst possible scenario for solar installers and their customers".

"For an industry that has taken three years to rebuild itself from the previous cuts, there simply isn't the capacity to deal with the inevitable demand. The proposals will lead to the cramming of installs into a diminishing window of time that includes a major holiday period and winter weather, putting installers at risk under time pressures to ensure customers don't lose out on the higher tariff before January."

Although the cuts will make solar less attractive, Forster believes they will lead to falls in costs down the supply chain which will mean commercial-scale solar will still be a viable opportunity for many.

Baker Tilly's Stewart says the latest raft of announcements will inevitably affect sentiment over investing in Scotland and the rest of the UK. "In the global fight for finance, the UK will lose out in the short to medium term as investors seek to deploy their funds in jurisdictions which are certain, stable and supportive of a long-term commitment to carbon reduction. The only certainty in the UK at the moment is the uncertainty and there are no signs of this changing."

David Gilchrist, energy partner at **DWF**, agrees investors could well move their focus to overseas markets. "The recent changes to renewables subsidies will have a huge impact on future developments as it creates uncertainty. In a competitive global market investors will look elsewhere to invest so we need to deliver a sustained commitment to renewables to encourage international investment into the UK.

"Less investment and development in the renewables sector will also have a knock-on effect on the wider capacity market," he adds. "In order to deliver secure, sustainable and affordable electricity, the UK needs to invest in new generation projects to provide back-up power that will ensure the lights stay on when demand is high."

While the debate over the subsidy cuts for mature renewable technologies rages on, those at early stages of development have also not had their troubles to seek.

The wave energy sector in Scotland in particular has seen turbulent times over the past year with Pelamis Wave Power – probably its best known name – falling into administration and rival Aquamarine Power also suffering significant job losses amid a downsizing process.

The Scottish Government responded to the sector's crisis by establishing **Wave Energy Scotland** to provide funding packages for the sector and through Highland and Islands Enterprise (HIE) it acquired the intellectual property of Pelamis.

Tim Hurst, who was appointed managing director of the body in May, says the organisation was looking to "create the conditions which will allow the private investors to re-enter the sector and take it through to commercialisation".

"There are always significant challenges in the development of new technology and the wave energy sector is no different. Wave Energy Scotland seeks to learn lessons from the sector to date, but also to draw on the experience from a range of other industries which will help us produce engineering solutions for the cost effective and reliable generation of wave energy," he says.

While wave energy has suffered setbacks, Scotland's role in the development of tidal energy has continued to develop. In the Pentland Firth, progress on a major tidal energy project, MeyGen, is now progessing apace with work on the initial four turbines being installed on the seabed well under way. Atlantis, the company behind the project, believes the total figure could eventually rise to 269 turbines.

The stock market listed company recently raised £2.5m in a placing to accelerate its plans and is in talks with ScottishPower Renewables over a deal which would bring together their tidal power project businesses in Scotland.

While much focus in recent months has been on mainstream renewables, Peter Bachmann, a director at **Scottish Equity Partners**, says it is also important to bear in mind the wider context of the clean energy market.

Last year the Glasgow-based fund investment firm raised £135m for the launch of the Environmental Capital Fund to invest in UK-based clean energy projects. As well as small-scale wind and hydro, the fund, backed by Perth-based energy group SSE and a syndicate of financial investors led by Lexington Partners, invests in projects include those addressing energy efficiency and heating.

"There is great diversity and breadth within the clean energy market, in particular within small scale infrastructure," points out Bachmann. "These projects have less reliance on government subsidy and have struggled to source flexible funding to enable their growth.

"We launched the fund to specifically address this opportunity, backing innovative projects which may be individually too small for traditional sources of infrastructure capital, but taken collectively within a carefully structured platform, become attractive."

The Beatrice project in the Outer Moray Firth was granted an investment contract by the UK Government in May 2014

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IN FOCUS: Offshore wind

WHILE much uncertainty surrounds the onshore wind sector, the offshore industry is making significant strides.

Earlier this year the 448MW Neart na Gaoithe wind farm planned for the Firth of Forth was one of 11 Scottish renewable projects successful under the first auction under the new Contracts for Difference (CfD) subsidy scheme.

Developer Mainstream Renewable Power has spent the last seven years working on plans for the project, which will be the first large-scale offshore wind farm constructed and operated in Scottish waters to be directly connected to the Scottish electricity system.

Neart na Gaoithe joins the 140-turbine Beatrice project in the Outer Moray Firth, which was granted an investment contract by the UK Government in May 2014, and is planned for construction in 2016.

Between them the two projects represent over 1GW of offshore wind in Scottish waters with funding secured and moving towards a final investment decision.