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Federal Ministry of
Food, Agriculture
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of the Federal Republic of Germany



German-Ukrainian
Agricultural Policy Dialogue

Issue #8/2013

at the Institute for Economic Research and Policy Consulting

AGRI-FOOD POLICY REVIEW

Recent amendments of the “green” tariff in Ukraine: new incentives but old barriers

updated (10th of October, 2013)

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Last year amendments to the legislation on stimulating production of electricity from renewable energy sources improve opportunities for biogas projects, photovoltaic systems installed by private households and small hydro-power plants. However, unclear procedures and demanding local component requirements risk counterbalancing the improvements and impeding development of the sector. Unless these problems are fully resolved energy production from renewable sources will grow much slower in Ukraine than in the EU.

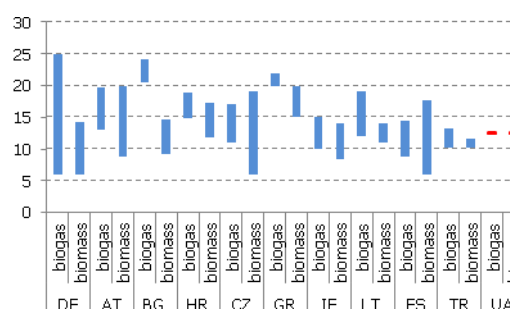
The Law No. 5485-VI "On amendments to the Law of Ukraine "On Electric Power Industry" (promoting electricity production from renewable energy sources) was signed by the President on 29th of November and came into effect on 1st of April, 2013. The Law considerably altered conditions for renewable sector development in Ukraine. In particular, "green" tariff for solar power plants was reduced which is a reasonable decision since "green" tariff coefficient at the level of 4.4 – 4.8 (depending on capacity) was unjustifiably high, comparing it to similar incentives in the EU countries. It is difficult to see any environmental or economic reasoning distinguishable behind such high tariffs, rather than interests of particular companies. At the same time, current amendments extended the tariff to private households which will be able to sell excess power produced by photovoltaic systems fixed on roofs to the grid, though procedures are still to be approved by the National Electricity Regulatory Commission (NERC). This aims to stimulate a wider use of solar energy by private households. In addition, "green" tariff coefficient is increased for small hydro power plants and will be differentiated depending on their capacity. Moreover, biogas projects will be eligible to sell electricity under favourable conditions. Although the "green" tariff coefficient at 2.3 (the same as for the projects on solid biomass) was introduced to support electricity generation from biogas, certain provisions are yet to be clarified and improved to attract investments and ensure sustainable long-term development of biogas sector in Ukraine.

First of all, "biomass" definition should be developed to cover not only waste but also products

and residues from agriculture, forestry and fishery. Current definition excludes raw materials, e.g., silage, which is widely-used in the biogas to energy projects. Additionally, the overall procedure of obtaining a feed-in tariff and connection to the grid should be more simple and transparent.

Secondly, the question whether introduced coefficient for electricity generated from biogas is high enough to guarantee acceptable for investors pay-back period remains open. Currently, no consensus is achieved at the market. Some businesses argue that 2.3 coefficient is better than nothing, while others claim that it is too low to attract investment in biogas projects. For an example, calculations made by Ukrainian Bioenergy Association show that investments under 2.3 green coefficient make up only in 15-20 years, which is too long to attract investors. Notably, the first draft of the Law envisioned green coefficient at 2.7 and this would result in 7-8 years pay-back period. In a number of the EU countries feed-in tariff for biogas projects is differentiated depending on project's capacity and usually higher than for biomass to energy projects (see Figure 1) due to higher construction costs.

Figure 1. Feed-in tariffs for biogas and biomass projects in a number of the EU countries and Ukraine (in Euro cent/kWh)



Source: own presentation based on <http://www.res-legal.eu> data. "Green" tariff for Ukraine estimated based on 2.3 coefficient for the electricity produced from biogas and biomass.

Moreover, "green" tariff for biogas projects in Ukraine is applicable only for the ones which were commissioned as of April, 2013. This creates unfair conditions for biogas projects owners (about 10 biogas plants) which already constructed biogas installations and started electricity production counting for green tariff in their business plans. Parliamentarians voted for green tariff for biogas

projects back in 2011 but the Law was vetoed by the President. Last year the feed-in tariff for biogas was supported by the Parliament and signed by the President but early installations are discriminated. Such inconsistent government policy hampers any foreign investments to renewable sector in Ukraine.

Finally, 30% local component requirement for biogas plants which will start operations as of 2014 and 50% as of 2015 effectively prevents construction of biogas facilities in the near future. Considering that large biogas plants require 2-3 years for construction, project developers will have to meet a 50% local component requirement which is not feasible at the moment. Currently, Ukraine does not have domestic production of biogas equipment to satisfy the local component requirement, thus, imports should not be restricted. Moreover, enforcement of local component requirement to stimulate domestic manufacturing of machinery/equipment in any economic sector is widely criticized in the economic literature since it often creates inefficient capacities and fails achieving desired targets.

Moreover, Ukraine should fulfil its obligations under a number of international agreements. Local component requirement imposes barriers for international trade with machinery/equipment which is clearly against WTO rules (see the AFPR#11 for details). Ukraine also became a member of the Energy Community Treaty in September, 2010ⁱ, and by this had taken obligations to increase the share of renewable energy in gross final energy consumption to 11%. Bioenergy could play an important role in achieving this target but only under condition that feed-in tariffs for biomass and biogas projects are high enough to attract investors and procedures for obtaining the tariff and connection to the grid are simple and transparent. Such conditions will enable access to state support program not only for large companies but also for SME.

Finally, local component requirement is considered to be discriminative against EU producers of renewable energy equipment. Therefore, its elimination is one of the six so called "de Gucht" economic requirementsⁱⁱ to Ukraine which should be addressed before signing the Association Agreement with the EU in Vilnius this November.

In April, 2013, the draft law #2946, which was developed with an expert support of the Ukrainian Bioenergy Association, was submitted to the Parliament. It aims to address the problems described above and contains quite demanding though reasonable suggestions. Unfortunately, not all proposed amendments were accepted by the government bodies and the draft Law was recommended for revision. A compromise version of the draft law was resubmitted in July, 2013.

Following experience of the EU countries, it is reasonable to differentiate "green" tariffs for biogas and biomass projects depending on the capacity and feedstock to create equal opportunities for different project developers. In addition, it is also recommended to abandon local content requirement for renewable energy projects, in particular biogas, since it is economically inefficient policy *per se* and will not stimulate production of green energy. Approval of the draft law #2946 by the Parliament will remove major barriers for development of the domestic renewable energy market in Ukraine.

ⁱ The Protocol Concerning the Accession of Ukraine to the Treaty Establishing the Energy Community was signed in Skopje (Macedonia) on 24th of September, 2010. Ukraine ratified it with the Law #2787-VI as of 15.12.2010 and it came into force on 1st of January, 2011.

ⁱⁱ More information at: <http://forbes.ua/nation/1359018-es-dosammita-v-vilnyuse-ukraine-nuzhno-vypolnit-eshche-shest-uslovij-v-biznes-sfere>