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# RECENT DEVELOPMENTS IN THE ISRAELI ELECTRICITY SECTOR:

## Focusing on Privatisation and Renewable Energy

The State of Israel is an "energy island" which is not connected to the energy grids of any neighboring country. Security of supply is therefore paramount in the Israeli electricity sector and until recently, competition and privatisation took a back seat, as did renewable energy. Today it is evident that these two trends are rapidly gaining ground.

### A. PRIVATISATION AND UNBUNDLING IN ELECTRICITY SECTOR – AN OVERVIEW

For over eighty years, the electricity sector in Israel was controlled by the Israel Electric Corporation Ltd. (the "**IEC**"), a vertical monopoly that operated throughout all of the sector's segments - generation, transmission, distribution and supply.
With the enactment of the Electricity Sector Law-1996 (the "**ES Law**"), a policy was instituted to gradually open the electricity sector to competition and to grant licenses for each of the main activities in the electricity sector; including a *system management license*, introduced in light of the structured conflict of interests caused by IEC's dominant position in the electricity market and its role as the head of the electricity system administration.

The ES Law provides for transitional reforms, unbundling and privatisation of the various segments. To date, the electricity generation segment has undergone significant transition to the private sector with the entry of Independent Power Producers ("**IPPs**"), whose market share has increased dramatically together with the increased availability of Israeli natural gas. **As of end 2021, 48% of Israeli electricity is generated by the private sector**[1].

[1] including renewable energy IPPs

Privatisation of the Generation Sector

In order to incentivise the entry of IPPs into the market, the provisions of the ES Law and its regulations require the system manager (until very recently, the IEC) to purchase electricity from cogeneration, conventional, and renewable energy IPPs. This critical requirement served as the financial and practical backbone for overhauling the structure of the electricity market by enabling the entrance and rise of IPPs in the generation sector. The IEC in its capacity as transmission system licence holder is also required to provide transmission services and back-up supply to customers of a licensed IPP, in exchange for a tariff. In addition and in light of regional security concerns, related regulation includes provisions aimed at providing security to entities financing IPP projects. During the COVID-19 pandemic, the Electricity Authority ("**EA**") granted relief to certain IPPs who were in the process of constructing their facilities (mainly photovoltaic ("PV") production facilities), by granting an extension of the deadlines of their construction under applicable regulation.

*The first stage* of the generation sector privatisation was carried out by granting **IPP licenses** under the ES Law, including to entities such as Dalia Power Energies (912 MW), OPC Energy (610 MW) and Dorad (860 MW).

*The second stage* was the **IEC Reform** approved by the government in 2018, under which IEC is obliged to sell about half of its natural gas fired power stations (with a total capacity of 4,500 MW), to private operators over a period of five years (the "**Reform**"). To date, the sales of 3 power stations have been concluded and sold to private operators, with the fourth power station in the process of being auctioned off by IEC.

The first two privatisation stages in the generation sector have resulted in IEC's market share of actual generated electricity, as of end 2021, shrinking to 52% of the total market share, with the remainder in the hands of the private sector.

*The third stage* of this privatisation is the recent publication of **a government tender** for a new IPP station, which is detailed below.

The New Generation Tender

In June 2022 the Israeli Government Procurement Administration published a PPP tender for the finance, design, construction, operation, maintenance and transfer to the State of

Israel of a dual fuel conventional power plant, to be located in Sorek, with a capacity between 600-900 MW, including an option to expand the capacity in the future.

Pre-Qualification Process: the tender committee intends to select an entity from the private sector, from Israel or abroad, through a competitive process where in the Pre-Qualification stage the participants will be required to demonstrate their experience and capabilities in specific criteria including, *inter alia*:

(a) demonstrating the applicant's EPC expertise as the main contractor (directly or indirectly) for the construction of at least two power plants qualifying under certain set of criteria and;

(b) demonstration of Financial Pre-Qualification Requirements and Operating Cash Flow thresholds.

The deadline for submitting the Pre-Qualification documents is **October 22, 2022**.

Transmission and the System Manager

By way of providing the full picture in the electricity sector, while the IEC still operates both the transmission and distribution grids almost exclusively and provides back-up services for customers and IPPs, as of November 1, 2021, the system management activity has been transferred under the Reform, from the IEC to Noga – Israel Independent System Operator Ltd ("**System Manager**"), granting independence to the entity that manages the competition between IEC and IPP. This is an important milestone in the privatization of the Israeli electricity sector.

The Supply Segment

The Reform also set the rules for opening up the supply segment to competition, while maintaining stability in this sector. The supply segment for high-voltage, extra-high-voltage and ultra-high voltage consumers (mainly large business consumers) has been fully opened up to competition; with the IEC remaining a default supplier only.

However, the Reform determined that the supply segment for low-voltage consumers (including household consumers) would only be partially opened up to competition.

In February 2020, the EA published a decision setting the principles for opening of the low-voltage supply segment to competition, by allowing new players to apply for a supply license, even if they do not operate a power station. Such new suppliers can only purchase the electricity for their consumers from the System Manager. Recently the EA published

for public hearing its plan to allow such new suppliers to buy electricity directly from small and medium-sized RE facilities.
As of mid-2022, 33 licenses have already been granted by the EA in accordance with this decision.

## B. GENERATION BY RENEWABLE ENERGY

Israel's regulatory framework for renewable energy ("**RE**") has been shaped by a number of government resolutions which set targets for increasing electricity production through RE, by determining quotas for generating electricity using RE, as well as providing incentives for RE initiatives.
As stated above, the IEC and the System Manager must provide IPPs with the appropriate infrastructure, connection to the electricity grid and importantly, purchase the electricity generated by them (via the System Manager) – which has proven crucial in facilitating the entrance of IPPs into the market, importantly including **RE IPPs**.
The main economic mechanism used to encourage individuals and companies installing renewable energy is the Feed-in-Tariff ("FIT"), accompanied by a series of quotas for installations of each technology type. Such FIT is determined mainly by competitive procedures issued by the Electricity Authority.
Currently, the main RE technologies in Israel are solar (PV/Thermo-Solar), wind and pumped storage. As of the end of 2021, the RE installed capacity reached 3.7GW, (17% of the annual installed capacity, with actual production at 8%). RE installed capacity and actual production are expected to reach 35% and 20% respectively by the end of 2025[2].

Renewable Energy Initiatives

The Israeli government has taken steps to increase the use of RE production, in light of its commitments under the Paris Agreement on Greenhouse Gas Reduction, such as setting target renewable energy production rates, passing the decision for the replacement of coal use with natural gas by 2025, promoting green mandatory construction and promoting the development of new RE technologies through, *inter alia*, the granting of tax incentives, provision of financial incentives to promote the financing of renewable enterprises and the revision of various tariffs applicable in the electricity market.

[2] as published by the *EA Annual Electricity Report for 2021*

In December 2016 the Israeli Parliament enacted the Law for Encouragement of Investments in RE (Tax Incentives for Production of Electricity from Renewable Energy) 2016 approving tax reductions to private households producing electricity with RE (an income tax exemption up to NIS 24,200 (approximately US$7,422).
Starting from March 2018, the EA has published a set of decisions that are aimed at incentivizing, the installation of roof PV systems on large roofs and water depots.

In July 2020, the Minister of Energy published a decision to adopt the EA recommendations and set up a policy aimed at increasing electricity production from renewable energy to 30% of all electricity consumption in 2030. Accordingly, Government Resolution 465, issued in November 2020, stipulates that by the end of 2030, the target for electricity generation from renewable energies will be 30% of total electricity consumption, and sets a corresponding intermediate target of 20% by 2025.

In May 2021, the Ministry of Energy together with the Ministry of Agriculture and Rural Development published an invitation to receive proposals from entrepreneurs, examining the feasibility of dual-use of agricultural land for electricity generation from solar energy, while maintaining yielding agriculture. Results were published in November 2021 and the tariff was determined at NIS 0.175 kW/h (about US$0.05 kW/h).
In August 2022 the Ministry of Energy published an investment program promoting the expansion of charging stations for electric vehicles in private parking lots, amounting NIS 8 million (approximately US$ 2.5 million) and the financing of an additional 1,122 charging stations in public parking lots.

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