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Japan's New Feed-in Tariffs: Government's Model Contract Available Now

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I. Introduction of FIT in July 2012

On July 1, 2012, the Act on Special Measures concerning Procurement of Renewable Energy Sourced Electricity by Electric Utilities (Act No. 108 of 2011) (the “**RE Act**”) came into effect and a feed-in-tariff (“**FIT**”) system was introduced in Japan in an effort to promote the use of renewable energy.

The RE Act imposes an obligation on electric utility operators (“**Utilities**”) to purchase electricity generated using renewable energy sources including solar energy (“**Renewable Electricity**”) from renewable energy electricity suppliers (“**Suppliers**”) at prices and for time periods designated by the Ministry of Economy, Trade and Industry (“**METI**”).

The length of the procurement period under the power purchase agreement (the “**Procurement Period**”) (which is currently twenty years) and the prices (the “**Procurement Price**”) payable during such Procurement Period as currently determined by METI are quite favorable to Suppliers, and thus, there has been a recent flood of companies building large solar and other power plants based on renewable energy.

In response to the introduction of FITs, each Utility prepared standard terms and conditions (yakkan) (“**Utility Terms**”) as part of the grid connection agreement (“**GCA**”) and a form of power purchase agreement (“**PPA**”) which the Utility expected to be accepted by Suppliers without any amendments. However, Utility Terms are typically drafted in favor of Utilities and may not be consistent with the RE Act. For example, under many Utility Terms, despite the 20-year Procurement Period, the contracting term was only one year with an option to renew each subsequent year, which technically enabled the Utilities to terminate the contract before the expiration of the Procurement Period. The more serious concern was that many Suppliers faced difficulties in obtaining bank financing for their projects because Utility Terms do not allow the Supplier to assign any of its rights and/or obligations under the GCA and PPA.

II. Model Contract

On September 26, 2012, METI released a model contract to be used for GCAs and PPAs (the “**Model Contract**”). The Model Contract can be found here

http://www.enecho.meti.go.jp/saiene/kaitori/dl/2012denki_keiyaku.doc (only in Japanese).

In its press release, METI described the Model Contract as complying with the RE Act and “other provisions defined in the related laws and regulations, while considering practical requirements and other procedures related to fundraising activities” of suppliers. According to METI, it released the Model Contract because Utility Terms (i) vary in terms of contents, some of which included terms that were not always consistent with the RE Act; and (ii) were not drafted for Suppliers to be able to obtain financing from banks.

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The Model Contract was drafted for use under the following circumstances:

- The Supplier sells Renewable Electricity to the Utility with which the Supplier acquires grid connection (in other words, the Supplier enters into the GCA and PPA with a single Utility);
- The subject project has a capacity to generate 500kW or more Renewable Electricity;
- The Supplier and Utility enter into the contract before starting the construction of approved facilities for power generation; and
- The Supplier intends to obtain finance from banks for the project.

As METI notes, the Model Contract is an example of a GCA and PPA and can be modified as appropriate to reflect the nature of energy sources, sizes of facilities for power generation and other circumstances of a particular project as long as the contract is in compliance with the RE Act and other applicable regulations.

III. Key Provisions of the Model Contract

Below are some of the key provisions of the Model Contract:

1. Contract Term (Article 1.2)

The contract term is to be a specified period (e.g., 20 years) that does not exceed the Procurement Period and does not allow the Utilities an option to terminate the contract after one year.

2. Compensation for Supply Suspension (Article 3.2)

Under the RE Act, Utilities are allowed to require a Supplier to suspend its Renewable Electricity supply without any compensation under certain limited circumstances such as, for example, a force majeure event, an accident, or a periodic check. However, if the total suspension period exceeds the maximum period (i.e., 30 days) permitted by the RE Act, the Utilities are required to compensate the Suppliers for the suspension. The Model Contract provides more details, in particular, the method of calculating such compensation.

3. Assignment of Rights and Obligations (Article 7.2)

Under the Model Contract, the Supplier is, upon obtaining prior consent from the Utility, allowed to assign the Supplier's rights and obligations under the GCA and PPA to lenders for financing purposes. This provision was incorporated specifically to allow Suppliers to satisfy the conventional condition imposed by banks and other lenders providing project financing that they receive an assignment of the rights and/or obligations under the GCA and PPA.

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