# Future Energy M&A Market Monitor 2023

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# Contents


Overview ........ 1

Introduction ........ 2

Parties & completion arrangements ........ 3

Pricing mechanisms ........ 6

Liability ........ 9

Seller limitations on liability ........ 12

National Security and Investment Act 2021 ........ 15

Grid Sharing ........ 16

Support mechanisms ........ 17

Joint ventures or third party process ........ 18

Looking to the future ........ 19

Recent deals ........ 20

Key contacts ........ 21

# Overview

**2022 was another record year for clean energy in the UK with 40% of the UK's electricity coming from renewable energy and this is only set to continue into 2023.**

**Despite global tensions, political instability and economic uncertainty, the UK's future energy sector has remained resilient with M&A activity levels as strong as ever. The UK's clean energy generation market is still seen as a 'safe bet' and investor appetite remains high, creating a competitive market place for assets and opportunities.**

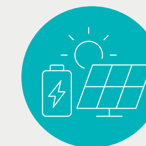
2023 is expected to be another busy year on the M&A front…

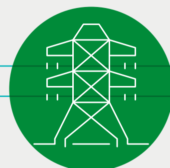
The secondary M&A market for operational wind and solar generation assets remains buoyant as expected and 2022 has seen the following trends:

1. Continued appetite for consented or 'ready to build' solar, battery, co-located assets and onshore wind in Scotland and Wales.
2. A seller-friendly market with high levels of competition and a continued uptake of warranty and indemnity insurance.
3. Project features changing i.e. larger capacity sizes, more transmission connected projects, longer connection dates, future proofing land agreements and planning to encompass future technologies and longer project life, more projects being co-located.
4. Acquirers seeking to transact earlier by either taking planning/judicial review risk or signing transactions at an earlier stage with completion (or put option agreements) conditional on planning.
5. A continued appetite for joint venture arrangements, particularly between investors and developers to develop large scale portfolios with increasing amounts of capital committed.
6. Increased interest in the UK market from overseas investors.
7. Platform sale opportunities increasing where entire development platforms are brought to market.

2023 is expected to be another busy year on the M&A front and is hopefully the year that:

- more investors move beyond just a 'watching brief' on some of the less mainstream technologies and opportunities such as green hydrogen, district heating and heat pumps, CCUS and EV charging infrastructure and other transport decarbonisation opportunities; and
- more large corporates get involved in the clean energy sector in one way or another as part of their own ESG decarbonisation commitments thereby creating a larger market.





# M&A Market Monitor

**This is our first specialist Future Energy M&A Market monitor report, where we look at some of the key trends identified in the negotiation of the acquisition or disposal of future energy projects between 1 January 2022 and 31 March 2023.**

It is based on data captured from 54 M&A transactions* completed by our Future Energy Corporate team and is representative of what we have seen in the Future Energy M&A market more broadly.

The areas on which we focus are:

- Parties & completion arrangements
- Pricing mechanisms
- Seller limitations on liability
- National Security and Investment Act 2021
- Grid Sharing
- Subsidies
- Joint ventures or third party process
- Looking to the future

* Please note: we have not included in the data the asset purchases of project rights.

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2023 could be the year that more investors move beyond just a ‘watching brief’ on some of the less mainstream technologies and opportunities.

# Parties & completion arrangements

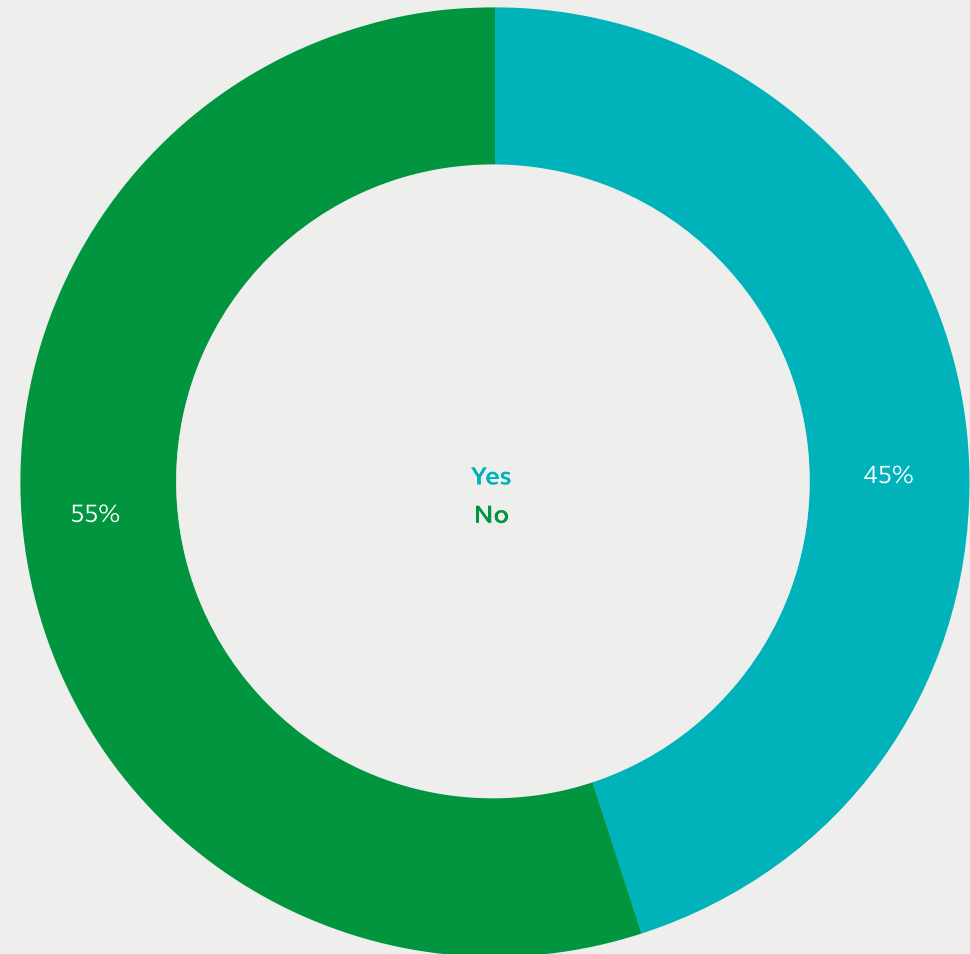
# Deals involving investment fund as acquirer or JV investor

With 45% of the deals that TLT has acted on being backed by an investment fund, what does the other 55% account for?

UK clean energy generation projects continue to be very attractive to investment funds who are particularly keen to acquire operational assets but there continues to be an increasing trend of funds now willing to take construction risk and acquire at 'ready to build' stage.

Over recent years, and largely due to market competition, we have seen a number of funds either build their own in-house development teams or enter into joint venture arrangements with established developers in order to acquire or invest at a much earlier stage and take development risk.

The usual acquirers remain active in the space including traditional EPC contractors, those who are vertically integrated, utilities and IPPs and energy companies. We also saw increased activity from those not traditionally involved in this sector but are seeking to implement their ESG initiatives. For example, in 2022 we saw projects acquired by local authorities and even a project acquired by a bank.



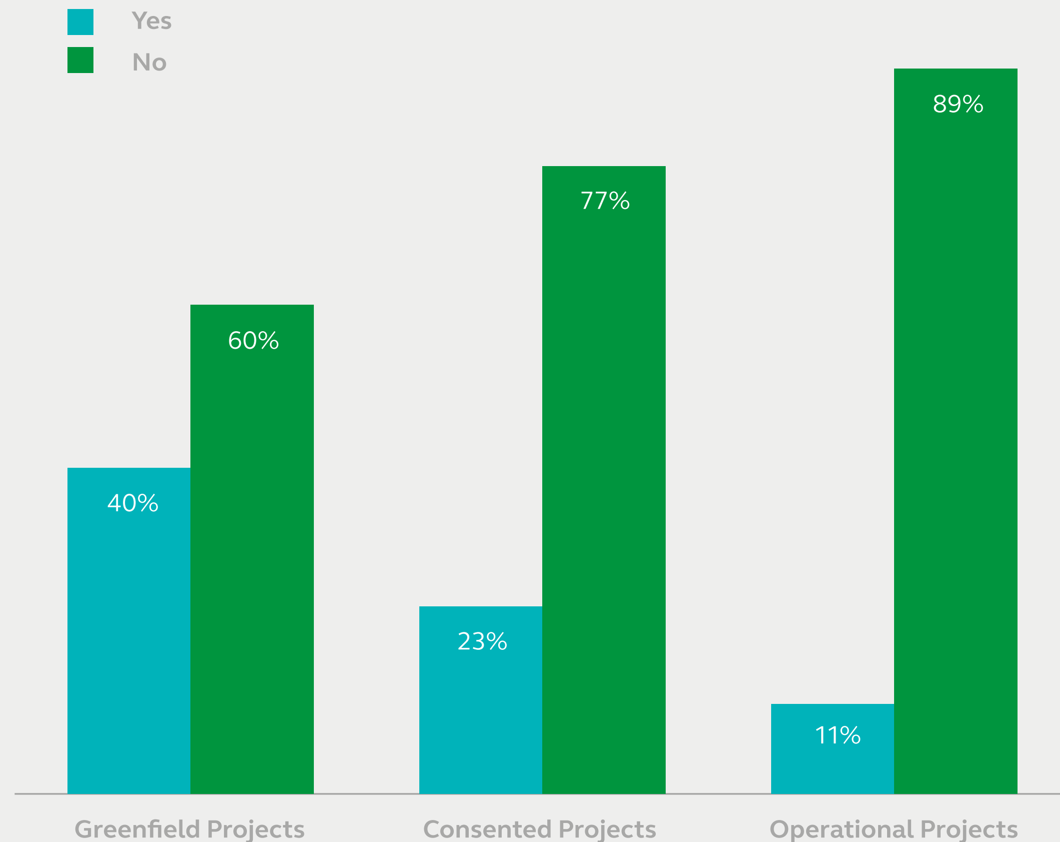
# Was there a gap between exchange and completion?

As expected, the earlier the stage of the project, the more likely there is to be a gap between exchange and completion.

Completion of greenfield sites tend to be conditional upon either planning being granted or, if planning has been granted, the judicial review period expiring without challenge. However, we are seeing an increase in judicial review insurance being acquired to enable an earlier completion.

Consented projects tend to be conditional upon either discharge of certain (more risky) pre-commencement conditions (e.g. satisfactory archaeological studies) or the project reaching 'ready to build' status e.g. any final easements having been secured or any third party consents being received etc.

Operational projects usually involve a simultaneous signing and completion but where this isn't the case, completion has been conditional upon necessary consents e.g. NSIA clearance, lender consent or change of control consents.



# Pricing mechanisms

# Pricing mechanisms

There are three different type of pricing mechanisms – management accounts, completion accounts and locked box – prevalent in the market.

Given greenfield and consented projects are not trading and generating revenue, the pricing mechanism here is, unsurprisingly, management accounts. Management accounts are usually simple in form (given the limited liabilities of the relevant project SPV) and are drawn up to a business day or two before completion.

With operational assets, the most common pricing mechanism is a locked box given a split exchange and completion is less likely (so the locked box period will be known with certainty) and the project revenue, liabilities and permitted leakage will be largely predictable. Key negotiation points will be around an interest ticker and caps on liability/claim period for leakage.

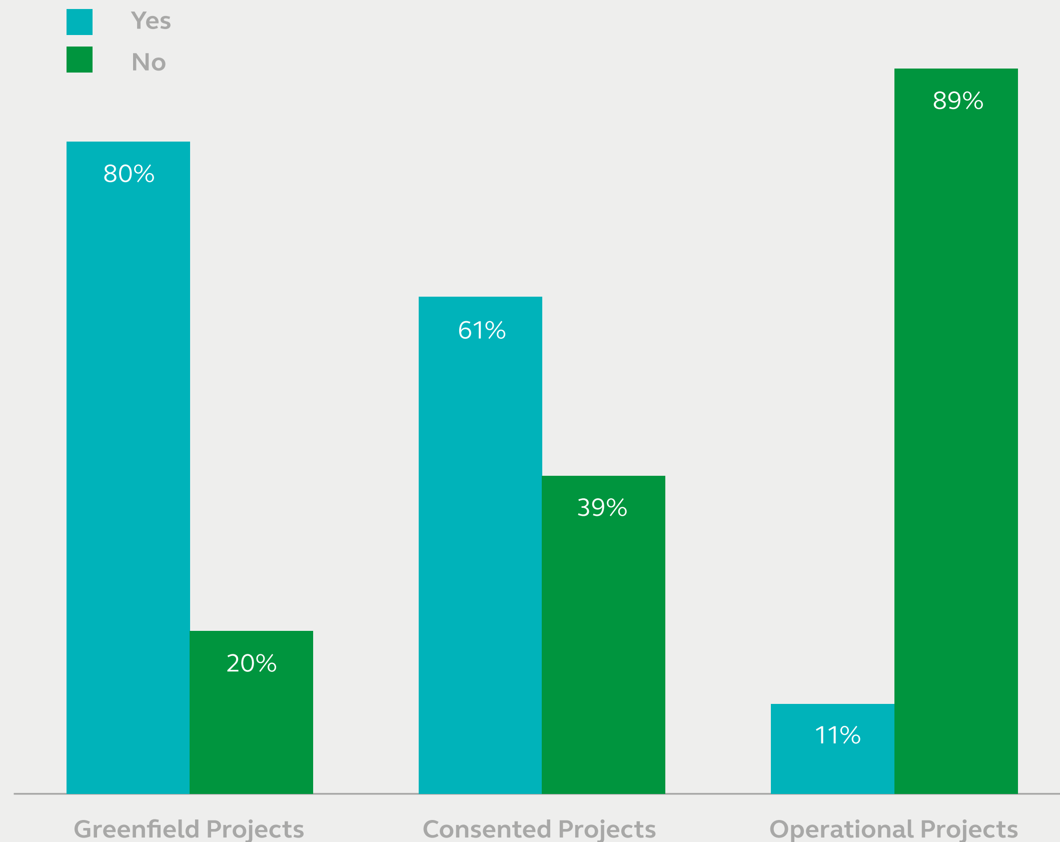
# Deferred consideration – was there any?

Deferred consideration can be used as an alternative in some cases to a split exchange and completion.

The conditions for deferred consideration on greenfield projects will largely mirror the conditions that would otherwise be linked to completion such that the majority of the consideration will be held back until planning has been achieved and the judicial review period has expired.

On consented projects, smaller elements of deferred consideration may be held back pending commencement of construction (such that the seller takes some of the residual development risk around discharge of pre-commencement conditions) and (rarely) pending commercial operations and final installed capacity. The latter is less rare where the seller has some residual role in the project in terms of providing development/ construction management services.

Deferred consideration on operational projects is less usual and tends to be linked to snagging items or rectification issues identified in due diligence which are not significant enough to delay the transaction.



# Liability

# Liability/W&I insurance used?

**Number of deals including W&I is 37 out of 60 (62%).**

The current seller's market is driving an increased use of warranty and indemnity insurance on transactions, so that the seller can achieve a clean exit without future recourse (or very limited recourse).

Under the vast majority of W&I deals, the seller caps its liability for breach of warranty and under the tax covenant to £1. Given W&I will also cover fundamental warranties, sellers usually demand that such fundamental warranties are capped at £1 too.

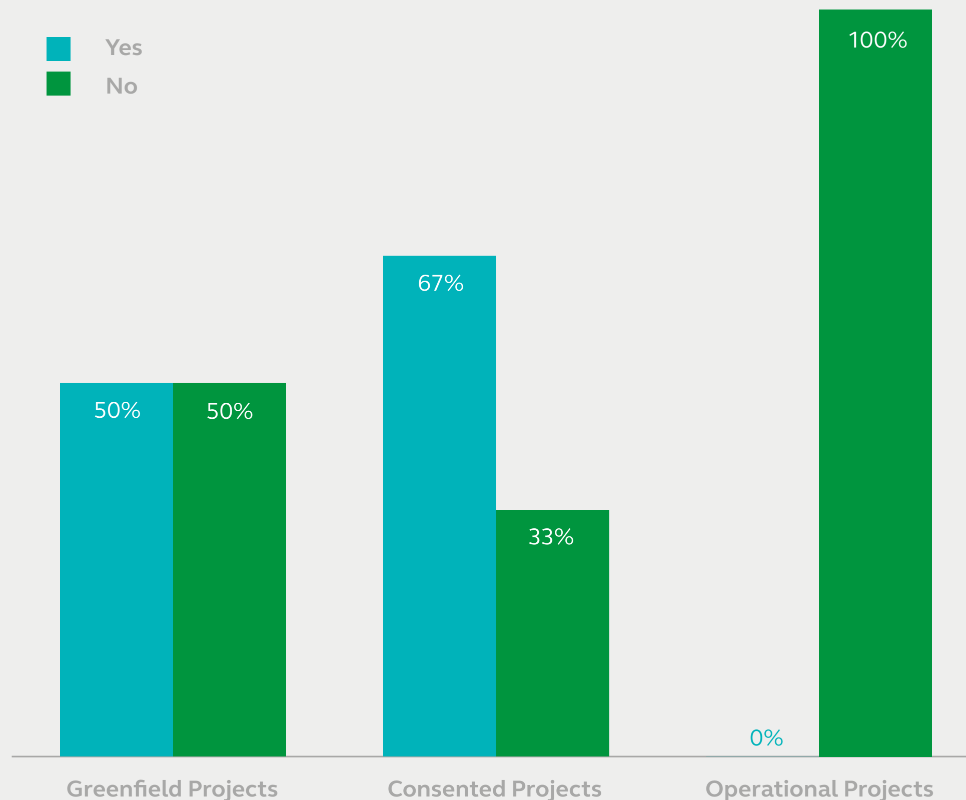
The W&I market is continuing to be very competitive and so incepting a policy is quicker than it traditionally was (i.e. around 14 days) although it is still advisable to engage a broker as early as possible – particularly towards the end of the year where we have seen underwriters' response times slow down due to the volume of policies to be incepted prior to year end. Given the competitive nature of the W&I market, there is also more of an opportunity to negotiate the policy terms than perhaps was the case previously, particularly where the policy premium is high or there is a chance of additional projects coming through the pipeline that will require cover.

Policy premiums are linked to the amount of coverage but, generally, they seem to be in the region of 1% of cover. The level of coverage required will be driven by the buyer's risk appetite but where a portfolio is being acquired, it is unlikely that the buyer will seek coverage for the full purchase price.

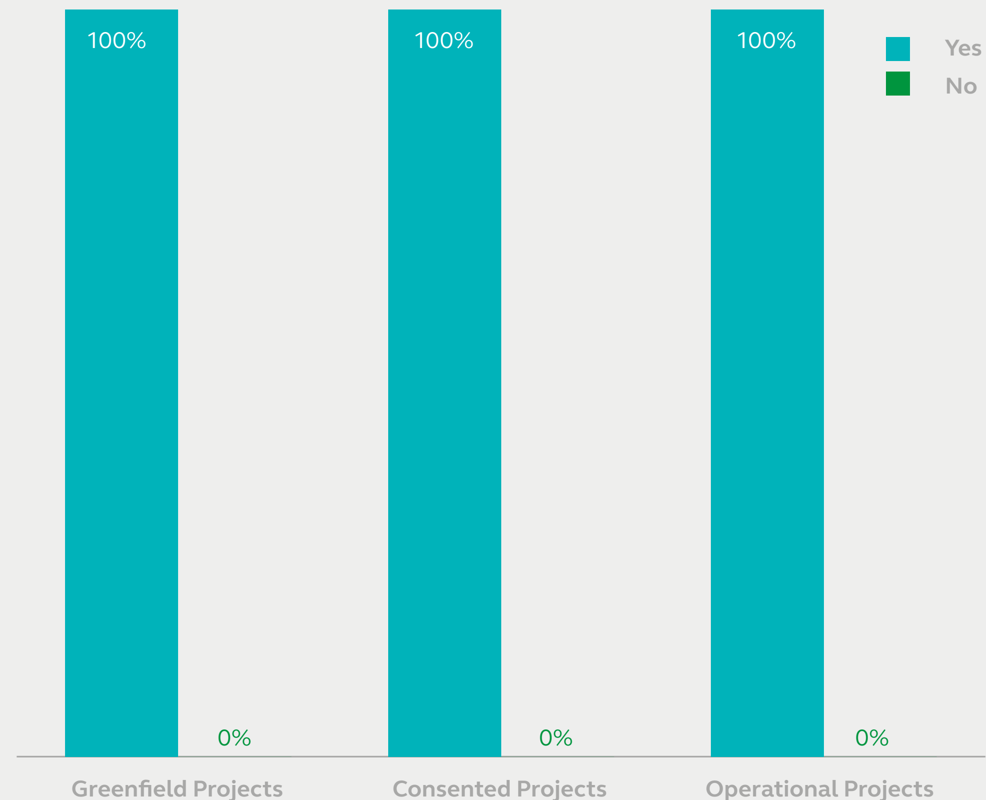
All of the W&I policies obtained on our transactions were buy-side W&I policies.

# Liability/data room/due diligence documents generally disclosed?

## Deals without W&I




## Deals with W&I

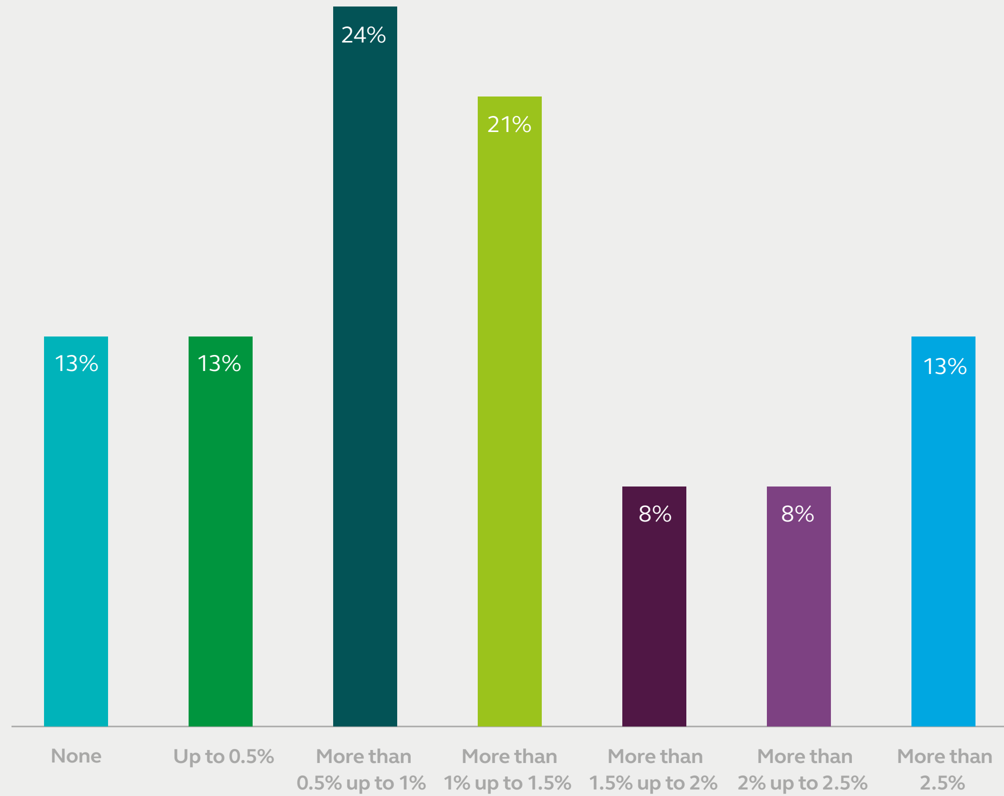



Extensive due diligence is usually undertaken on the project/target entity and whilst general disclosure of the data room tends to come down to the bargaining strength of the parties, on greenfield and consented projects general disclosure of the data room is usually acceptable given the limited volume of documentation expected. This is less the case where the project is operational and depending on how long the project has been operational for, the volume of documentation could be extensive so it is more reasonable for a buyer to insist that a seller carries out a specific disclosure exercise.

Given the current prevalence of W&I, it is not unusual that the buyer will avoid having a negotiation with the seller as regards general disclosure of the data room and instead seeks a policy enhancement under the W&I policy such that the data room is not deemed generally disclosed. The W&I provider will, of course, still need to be satisfied that a reasonable due diligence and disclosure exercise has been carried out.

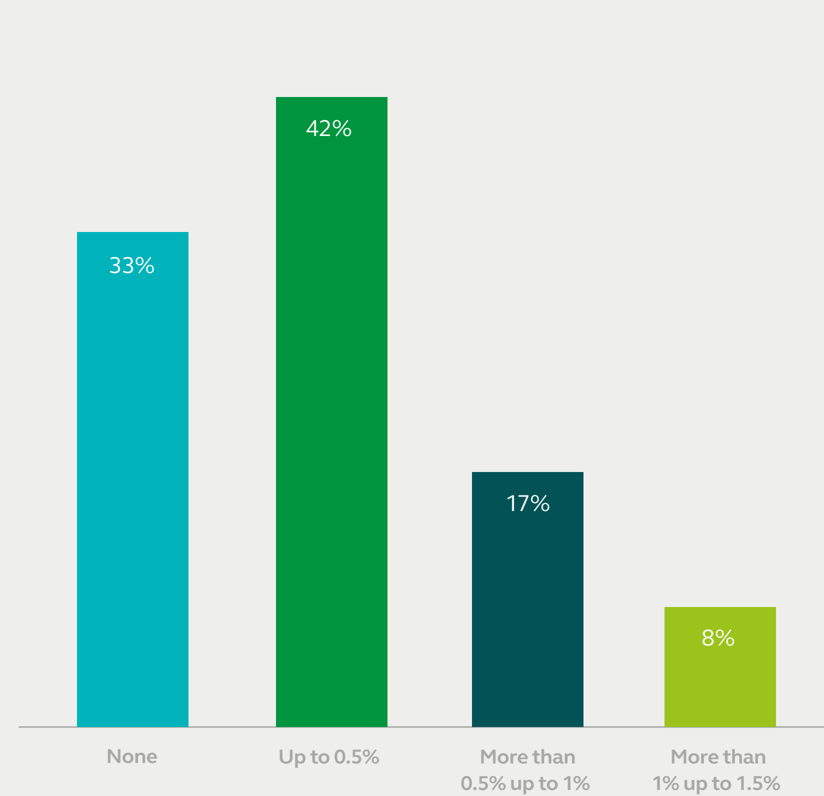
# Seller limitations on liability

## Liability/aggregate claims threshold/basket (% of deal value)



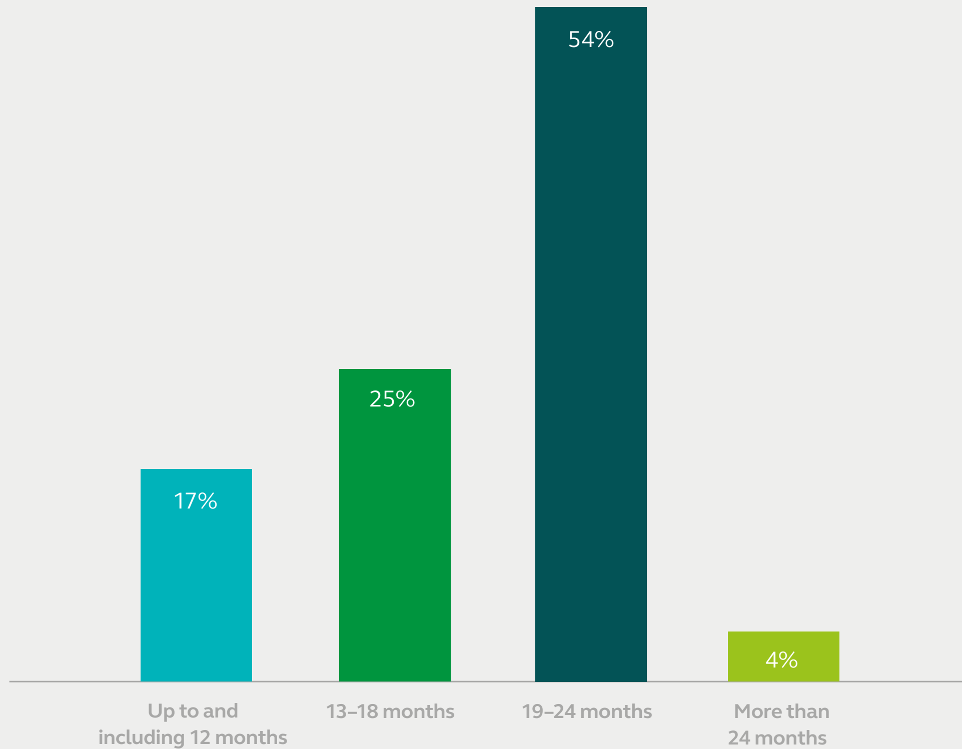

Note: we have only included transactions which did not have W&I insurance

## Liability/aggregate claims de-minimis (% of deal value)



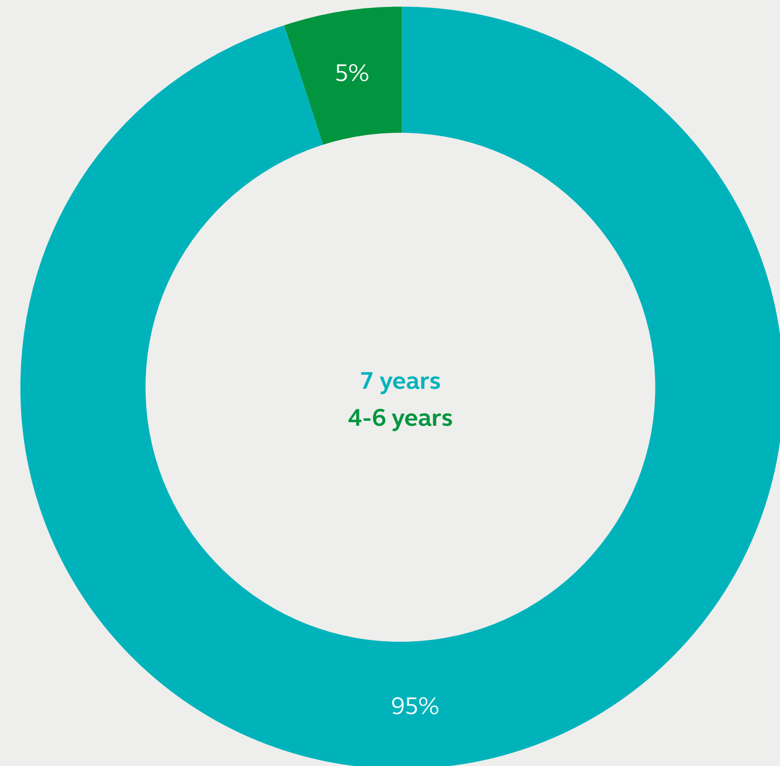

Note: we have only included transactions which did not have W&I insurance

## Liability/limitation period for non-tax warranty claims




Note: we have only included transactions which did not have W&I insurance

## Liability/limitation period for tax claims




Note: we have only included transactions which did not have W&I insurance

The limitations we tend to see on future energy transactions are reflective of the wider M&A market.

As would be expected, under usual transactions without W&I, a seller will seek to include a de-minimis and a basket on claims.

In the majority of cases a de-minimis of up to 0.5% of the deal value is standard and most baskets are agreed at up to 1.5% of the deal value.

Warranty claim periods tend to be 2 years or less and it is not unusual to see the claim period for fundamental warranties to be longer than the claim period for general warranties.

A buyer will usually want a claim period of at least one full accounting period, particularly where a project is operational and therefore trading.

Seven years is the most popular limitation for tax claims given HMRC can look back six full accounting periods.

# National Security and Investment Act 2021

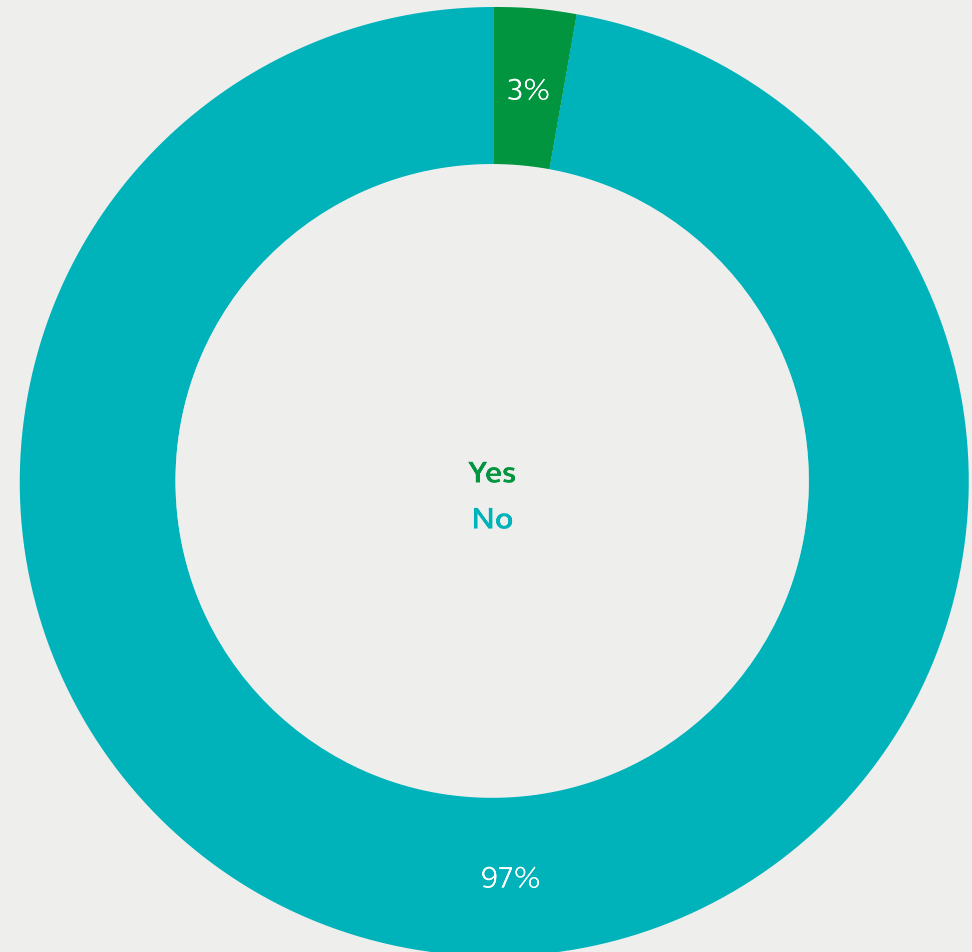
A new national security regime came into force in the UK on 4 January 2022 pursuant to the National Security and Investment Act 2021 (NSIA), and this has become a significant consideration in a number of transactions.

The NSIA captures a wide range of transactions and focuses on entities and assets which operate in 17 'sensitive sectors'.

Energy is one of the 17 sensitive sectors and so NSIA requirements should be considered on each future energy transaction. A detailed summary of trigger events is beyond the scope of this report but particular care should be taken where the target entity is a transmission, distribution or interconnector licence holder (or would need to be a licence holder save for an exemption); where the target entity involves an operational project of at least 100MW; or where the buying group holds (inclusive of the target entity) generation assets or aggregates at least 1GW.

Where transactions are caught by the regime (either by way of a voluntary or mandatory notification) we are finding that the new Investment Security Unit (ISU) which reviews the clearance applications is typically taking the full review period to which it is entitled to respond and make its assessment. This is something which parties need to factor into their transaction timetables. We are seeing the approval period often being dealt with as part of a split exchange and completion with the parties agreeing to the terms of the transaction subject to confirmation from the ISU that the clearance has been given (or given with conditions to which both parties are happy to comply). It is also not unusual for the SPA to be negotiated ahead of an NSIA application being made, and only entered into once clearance is received (so as to avoid the more complex mechanics of a split exchange and completion), especially where the risk of clearance not being granted and/or transaction risk are low.

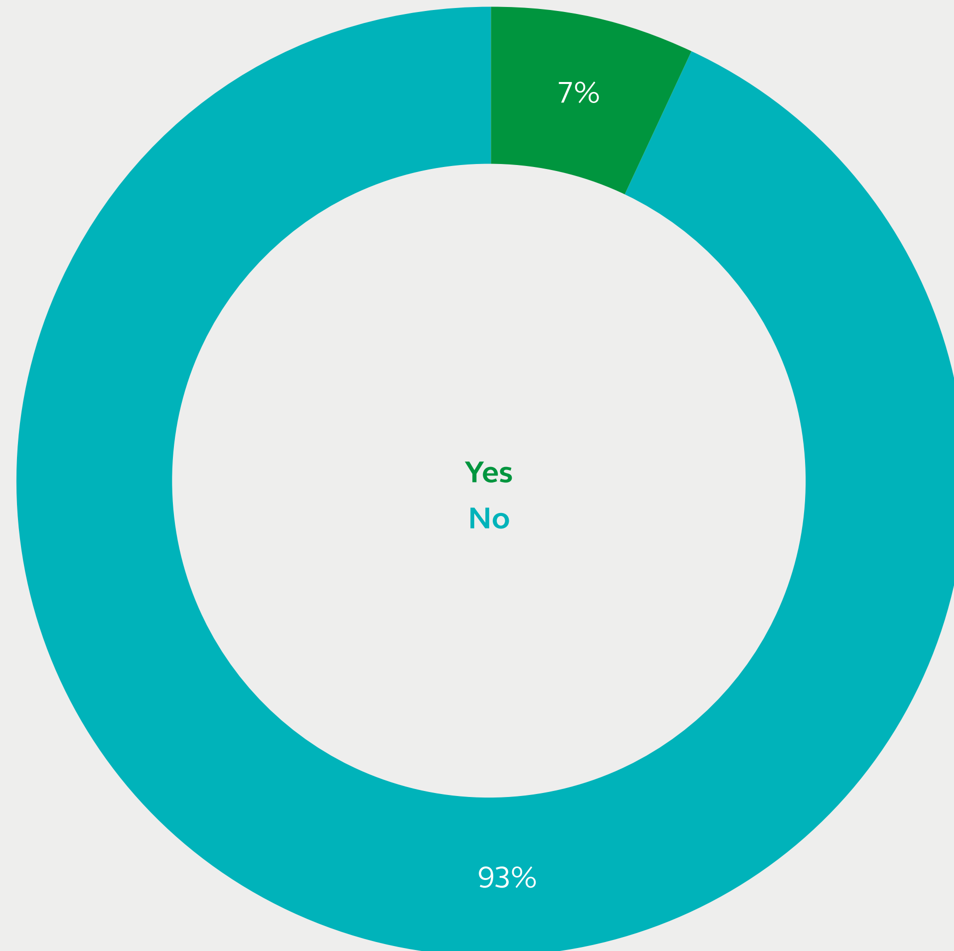
For more information on the regime and how it relates to Future Energy transactions please do refer to this article: **The NSI Act 2021 – implications for clean energy transactions – TLT LLP**



# Grid Sharing

Whilst grid sharing arrangements remain a feature on only a minority of transactions, we expect this to become an increasing trend going forward in light of grid constraints and the increasing need to utilise all spare grid capacity as well as an increasing trend in co-located assets.

Grid sharing arrangements need to be carefully thought through to mitigate risk to the sharing parties, maintain bankability and to future-proof any future exit arrangements. TLT is experienced in grid sharing arrangements and how best to structure such projects, and is advising a number of developers with grid sharing arrangements between different projects held by different SPVs in order to ensure bankability, especially where there is a timing gap in the stage of development of the projects. We have also advised a number of lenders and acquirers in carrying out extensive due diligence on projects sharing grid rights.

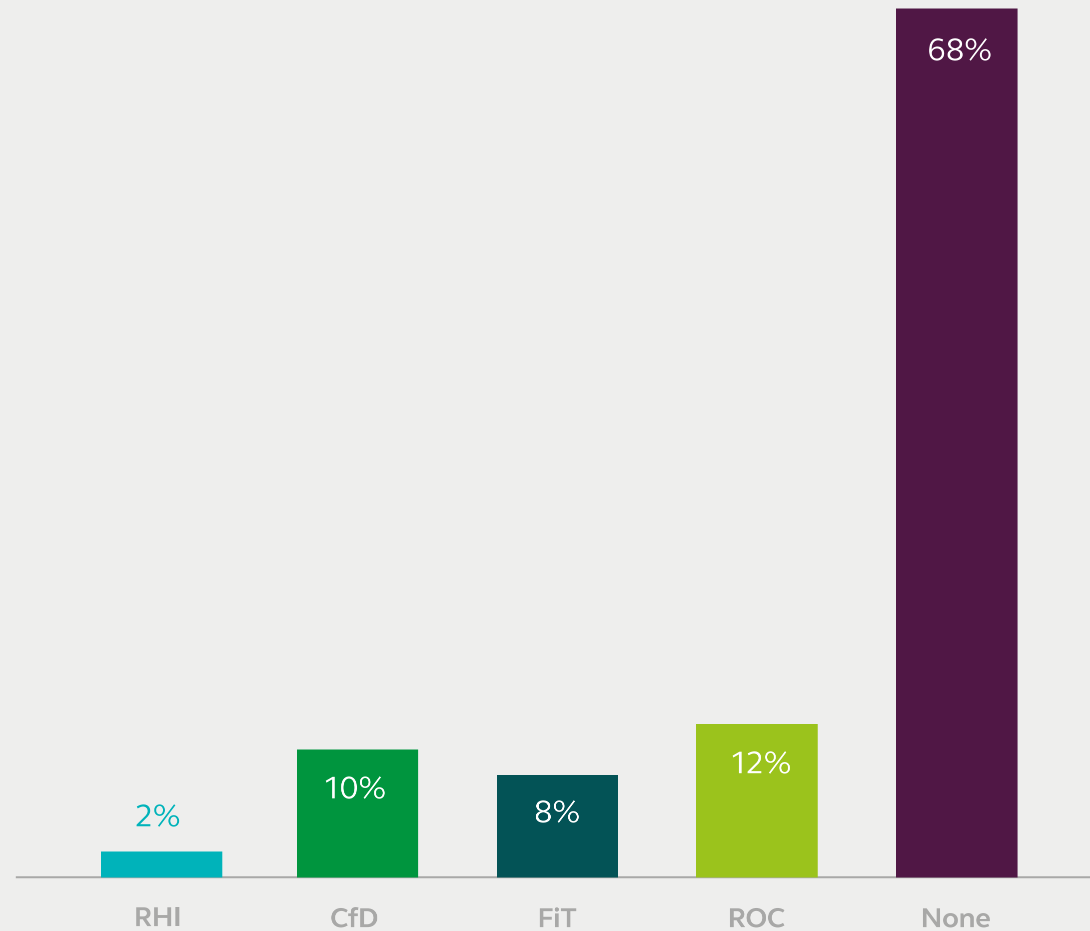


# Support Mechanisms

As is to be expected, the majority of the transactions we have worked on this year have involved projects that do not attract any form of support mechanism and the market is mature enough in terms of onshore wind, solar and battery storage that projects are developed on a subsidy/support free basis as a matter of course.

There will continue to be ROC and FiT projects coming to market as investment periods mature and assets are to be sold. Projects that attract a subsidy are still viewed favourably and there is no shortage of buyers for such assets.

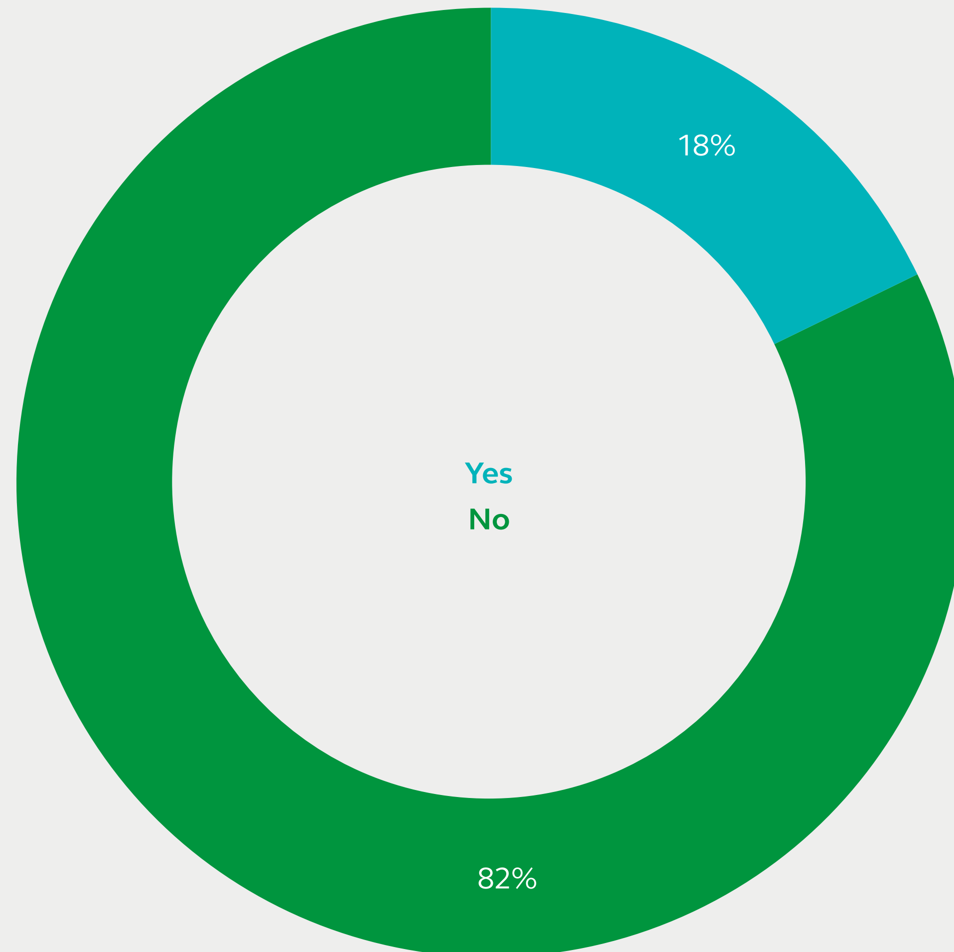
With more CfD allocation rounds being created (and hopefully on a more regular basis), the number of projects benefiting from a CfD contract should continue to increase.



# Joint ventures or third party process

One in five of the transactions we worked on in 2022 involved creating a joint venture which would most likely be an investor-developer joint venture.

Given the competitive nature of the market, investors are using joint venture structures to gain a form of exclusivity with reputable developers and secure a conveyor belt of projects. Developers too are benefitting from joint venture structures given the guaranteed funding line and they are capitalising on the competitive tension in the market by securing joint venture terms that are much more favourable than those we have historically seen for developers. For example, developers are retaining a higher equity stake, are demanding returns earlier than would have traditionally be seen and are seeking more rights (in terms of control, options to co-fund and early exits).



# Looking to the future

**Investors' appetite for the more mainstream technologies (being wind, solar and battery) remains strong and we'll see continued deployment and M&A activity surrounding those technologies.**

Given these are the cheapest to fund and quickest to develop and build forms of clean electricity generation, it makes sense that the focus should remain on these technologies. The UK's targets to achieve 70GW of solar by 2035 and 50GW of offshore wind by 2050 along with NGESO's desire to bring connection dates for energy storage systems forward are all helpful and will promote investor confidence. However, more detailed roadmaps are needed and, in addition, a change in policy for onshore wind is urgently needed given this feels like low hanging fruit in terms of contribution to the UK's target for net zero.

In the short term, at least, the market is expected to continue to be a seller/developer's market with competition remaining high for mainstream assets coming to the market. Investors will continue to identify good quality developers to team up with in order to secure large project pipelines or to diversify into other technologies – either by way of a platform acquisition or in respect of a joint venture arrangement.

The market has seen a significant increase in pricing for mainstream technology projects over recent times but there is a growing view in the market that such pricing will calibrate to what is considered to be a more normal level in the short term particularly with increasing interest rates, increasing supply chain costs and lead times, longer grid connection dates and an expected reduction in power prices. Nevertheless, investors' appetite for the traditional technologies is expected to remain high, and we expect overseas investor involvement to continue to increase. Given the continued pressure on the grid and ever-longer grid connection dates, the trend towards utilising all spare capacity will increase through the development of more multi-technology hubs and the implementation of more grid sharing and private wire arrangements.

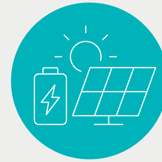
The need to decarbonise our heat and transport is now becoming urgent and so it is hoped that in the short term we will start seeing increased activity and investment into district heating schemes, the deployment of heat pumps and CCUS schemes and that we will see more momentum behind green hydrogen and electric vehicle charging infrastructure. Most equity investors remain cautious of these technologies which can be expensive and can be more challenging in identifying the revenue streams to generate the returns needed. More incentive schemes and/or regulation is needed from Government to help these technologies gather pace.

The green agenda and ESG movement is bringing sustainability to the forefront for many large corporates who are increasingly providing a market for further investment into the sector, whether that is through the use of corporate PPAs or private wire arrangements, using green fleets or actually acquiring generation projects themselves. There is only one direction of travel as the number of companies seeking to develop and implement ESG strategies snowballs.

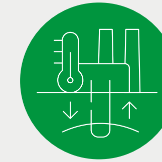
There is a lot to play for and it is easy to see that despite the political and policy challenges that the sector continues to face, 2023 and into 2024 is going to be another buoyant year for investors in the future energy sector.

# Recent deals

Cero Generation's joint venture with Enso Energy – Enso Green Holdings Limited (EGHL) – on the sale of a 720MW ready-to-build co-located solar and battery project portfolio to DIF Capital Partners.

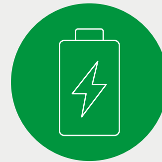


JBM and Susgen on the sale of JBM Solar, one of the UK's largest independent solar and co-located battery developers, and its 6.1GW solar and battery portfolio to RWE.

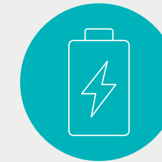


Thrive Renewables PLC on its investment in United Downs Geothermal Limited ('UDGL') in connection with the construction and development of the UK's first ever commercial geothermal power project.

Ecotricity in relation to securing the site for the country's first 100% vegan biogas plant that literally creates "gas from grass".



TagEnergy on its £300m partnership with Balance Power to build, own and operate 500MW of battery energy storage system projects across the UK.



BlackRock Global Renewable Power III on its £200m joint venture with battery storage developer KX Power Limited.

Capital Dynamics on its £146m disposal of a 97MW wind portfolio to Vantage RE.

Low Carbon (and Waste Energy Power Partners) on the sale of Doveryard Limited to funds managed by Octopus Renewables which will see the construction of the 185,600 tonne Oldhall Energy Recovery Project – the first large-scale, subsidy free energy recovery project in western Scotland.

Innova Renewables on a strategic partnership with funds managed by Schroders Greencoat LLP, which aims to fund and develop 5GW of energy generation and battery storage projects across the UK in the next three to five years.

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