U.S. Incentives to Promote Renewable Energy

The ARRA, cash grants and loan guarantees

November 10, 2009

Travis L.L. Blais

Sahir Surmeli

Mark J. Riedy

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Speakers

Travis L.L. Blais, Esq.

Travis is an associate in Mintz Levin's Tax Section. He focuses on a wide range of federal tax areas, and primarily advises investors and operating companies.

Sahir Surmeli, Esq.

Sahir is a member in Mintz Levin's Corporate practice and is Vice Chair of the Firm's Energy and Clean Technology Practice Group. He has worked on a wide variety of capital-raising projects with aggregate proceeds of more than $8.3 billion.

Mark J. Riedy, Esq.

Mark is a member in Mintz Levin's Corporate and Energy and Clean Technology practices. He has counseled clients doing business in more than 35 countries.

I. American Recovery and Reinvestment Act

- The American Recovery and Reinvestment Act of 2009 ("ARRA") was passed in response to the worldwide economic crisis of 2008-2009.

- It contains various direct spending programs, tax incentives, grants, loans, loan guarantee and bond programs to develop renewable and clean energy technologies.

- $787 billion overall, with more than $50 billion devoted to clean and renewable energy.

II. Two Key Provisions in ARRA

- **The ARRA created a cash grant program for qualified renewable energy power facilities.**
  - *The ARRA provided grants in lieu of Production Tax Credits ("PTC") and Investment Tax Credits ("ITC").*
  - *Directed by the U.S. Department of the Treasury ("Treasury").*

II. Two Key Provisions in ARRA

- **The ARRA also amended the Loan Guarantee Program established in the Energy Policy Act of 2005 ("EPACT").**
  - *The ARRA amends EPACT Section 1705 of Title XVII, providing new loan guarantees for certain "commercial" energy generation projects.*
  - *EPACT created Section 1703 of Title XVII, as expanded by the Energy Security and Independence Act ("EISA") of 2007, providing loan guarantees for new and unique technologies and projects .*
  - *Directed by the U.S. Department of Energy ("DOE").*

III. Key Tax Incentives
A. Overview of Production Tax Credit (PTC)

- A production tax credit is available to certain “producers” of qualified renewable electricity sold over a 10-year period.

- 2.1 cents per kWh of electricity produced by:
  - *Wind.*
  - *Closed-loop biomass.*
  - *Geothermal energy.*
- 1.0 cents per kWh of electricity produced by:
  - *Open-loop biomass.*
  - *Municipal solid waste (landfill gas and trash).*
  - *Qualified hydropower (including small irrigation power).*

A., Continued

- PTC has a 50% reduction penalty if a power-generating facility was financed with any government funding (e.g. grants, loans, loan guarantees, etc.), the so-called "double-dip" penalty.
  - *The ARRA did not remove this penalty for the PTC.*

B. Overview of Investment Tax Credit (ITC)

- The ITC is a one-time, up-front income tax credit for owners of certain qualified “energy property” which is placed in service.
- Generally 10% or 30% of the cost basis of certain specified energy property qualifies for the ITC .
- 5-year recapture period.
- 50% of the credit reduces cost basis: for example, (100% of the cost basis of certain qualified energy property) - (30% credit/2 = 15%) = 85%.

B., Continued

- Accelerated depreciation permitted.
- 50% bonus depreciation allowed through December 31, 2009.
- "Double-dip" penalty was applicable for the ITC, like the PTC, but the ARRA removed it.

B., Continued

- "Energy property" includes:
  - *Solar property.*
  - *Qualified fuel cell property.*
  - *Qualified microturbine property.*
  - *Qualified small wind energy property.*
  - *Combined heat and power system property.*
  - *Geothermal power production property.*
  - *Geothermal heat pump property.*

C. ITC Cash Grants

1. ITC-eligible persons may elect to forego the 30% credit and take a 30% cash grant instead.

2. The ITC Cash Grant Program is uncapped.

3. Treasury already has issued more than $1 billion in ITC cash grants.

C., Continued

4. Eligible Recipients for Cash Grants.

- *Generally, any individual or entity who is the original user of "specified energy property."*
- *Original user may be the first owner <u>or lessee.</u>*
- *Ineligible persons or entities include:*
  - Federal, state, or local governments.
  - Tax-exempt organizations (includes most pension funds).
  - Clean renewable energy bond lenders, cooperative electric companies, or governmental bodies.
  - Pass-through entities having an equity owner who is described above.
  - Foreign persons or entities, <u>unless</u> more than 50% of the foreign person or entity's gross income derived from the property is subject to U.S. federal income tax.
- *"Blocker" corporations may be used to avoid and cure applicant eligibility issues.*

C., Continued

5. Eligible Property for Cash Grants.

- *"Specified energy property" otherwise eligible for ITC, including "PTC-type" property able to elect ITC.*
- *Tangible property, integral to the facility, for which depreciation is allowed.*
- *Original use of the property must begin with applicant.*
  - But used parts can account for 20% of total cost.
- *Property must be physically located within the U.S. for more than 50% of the year.*

C., Continued

6. Project and Application Deadlines.

- *Construction must begin by end of 2010.*
- *If construction began before 2009:*
  - Property must be placed in service between January 1, 2008 and December 31, 2010.
  - Application must be submitted after placed-in-service date, but before Oct. 1, 2011.
- *If construction began in 2009 or 2010:*
  - Property must be placed in service by the end of
    - *2012 for wind facility eligible for PTC.*
    - *2013 for other property eligible for PTC.*
    - *2016 for property eligible for ITC.*
- *Application submitted after construction begins, before Oct. 1, 2011.*

C., Continued

- *"Construction begins" with "physical work of a significant nature," directly or under written contract.*
  - Preliminary activities do not constitute physical work (e.g., planning, designing, securing financing)
  - Safe harbor: construction begins upon incurring or spending 5% of the total cost of the property (excluding preliminary activities)

- *Property is "placed in service" when it is ready and available for its intended use, i.e., substantially complete and ready to produce energy.*

C., Continued

7. Application Requirements and Funding.

- *Treasury began accepting applications on August 1, 2009.*
- *Applications must be received before October 1, 2011.*
- *Applicants must also register with the Central Contractor Registration at www.ccr.gov/startregistration.aspx.*
- *Applicants must have a Dun and Bradstreet number.*
- *Treasury will notify applicants of an incomplete application and provide 21 days to correct.*
- *Treasury will make payments within 60 days following the later of:*

(1) the date of the completed application; or

(2) the date the eligible property is placed in service.

IV. DOE Loan Guarantees
A. DOE Sections 1703 and 1705

- Section 1703 of Title XVII of EPACT, as expanded by EISA, authorizes loan guarantees for renewable energy and certain other projects that employ "new or significantly improved" technologies.

- Section 1705, added by the ARRA, authorizes loan guarantees under the Financial Institutions Partnership Program (or FIPP) for renewable energy projects that employ "commercial" technologies.

B. DOE Section 1703 Loan Guarantees

1. Overview of Section 1703.

- *Section 1703 authorizes loan guarantees for renewable energy and certain other projects.*
  - Eligible projects must “avoid, reduce or sequester air pollutants” and “employ new or significantly improved technologies” rather than commercial technologies.
  - A principal goal of Section 1703 is to encourage early commercial use in the United States of new or significantly improved technologies.

- *Section 1703 does not specify a deadline by which projects must be constructed.*

B., Continued

2. Eligible Projects for Section 1703.

- *Section 1703 authorizes loan guarantees only for projects that avoid, reduce or sequester air pollutants or greenhouse gases and employ new or significantly improved technologies.*
- *Eligible projects include alternative fuel vehicles; efficient electricity transmission; distribution and storage; energy efficiency projects; solar, wind, biomass, hydro and geothermal power technologies; and advanced biofuels production facilities.*
- *"New or significantly improved technology" is defined as not more than two substantially similar technologies in commercial operation in the U.S. in the past five years.*

3. Eligible Recipients for Section 1703.

- *Private borrowers and project sponsors are applicants, not private lenders.*

B., Continued

4. Eligible Loan Guarantee Coverage.

- *Projects can receive up to 100% loan guarantee coverage for up to 80% of total project costs.*
- *The Federal Finance Bank (Treasury) must be the lender for all 100% loan guarantee coverages.*
- *The Federal Finance Bank will provide loans at interest rates of approximately 22 to 75 basis points over U.S. Treasuries, or approximately less than 4%, and at tenures of approximately 20-30 years.*
- *Where lenders participate in lieu of the Federal Finance Bank, they have a junior lien position to DOE on the covered portion of loans and are pari passu with DOE on the uncovered portion of these loans.*
- *Lenders cannot separate the loan guarantee from the loan when selling paper into the secondary market.*

B., Continued

5. Schedule of Non-Refundable Fees Payable to DOE for Section 1703:

- *Application fee: 25% submitted with Part I; 75% submitted with Part II.*

Loan Guarantee Amount	Total Fee Amount
$0- $150,000,000	$75,000
$150,000,000-$500,000,000	$100,000
Above $500,000,000	$125,000

- *Facility fee: 20% submitted upon execution of Term Sheet; 80% upon closing of Loan Guarantee Agreement.*

Loan Guarantee Amount	Total Fee Amount
$0-$150,000,000	1% of guarantee
$150,000,000-$500,000,000	$375,000,000 + 0.75% of guarantee
Above $500,000,000	$1,625,000 + 0.50% of guarantee

B., Continued

- *Maintenance Fee: $50,000 to $100,000 per year during the life of the loan guarantee. It shall be either (i) payable each year in advance, commencing upon the closing date of the Loan Guarantee Agreement, or (ii) payable as an one-time fee at the closing in a lump sum amount equal to the aggregate sum of such annual fees specified in the Loan Guarantee Agreement for the entire term of the loan guarantee, discounted to net present value.*

- *Attorneys/Consultants fee: DOE is entitled to payment for additional internal administrative costs and related fees and expenses for its independent consultants and outside counsel.*

- *Credit Subsidy Cost: The Credit Subsidy Cost is the net present value of the estimated cost to the U.S. government of the loan guarantee as determined under the applicable provisions of the Federal Credit Reform Act of 1990, as amended (FCRA).*

B., Continued

6. **July 29, 2009 Section 1703 Solicitation for Energy Efficiency, Renewable Energy and Advanced Transmission and Distribution Technologies.**
   - *7 rounds, 2 parts per round:*

Round	Part I	Part II
1	Sept. 16, 2009	Nov. 13, 2009
2	Oct. 22, 2009	Jan. 15, 2010
3	Dec. 23, 2009	Mar. 12, 2010
4	Feb. 18, 2010	May 14, 2010
5	Apr. 22, 2010	July 19, 2010
6	Jun. 24, 2010	Sept. 17, 2010
7	Aug. 24, 2010	Dec. 31, 2010

B., Continued

- *DOE issued a second and similar Solicitation for transmission infrastructure on July 29, 2009.*
- *Note that for Section 1703 Buy America Act provisions will apply only to public, and not private, sector project.*

C. DOE Section 1705 Loan Guarantees

1. Overview of Section 1705.

- *Section 1705 authorizes loan guarantees for three specific types of projects:*
  - Renewable energy systems.
  - Electric power transmission systems.
  - Leading edge biofuel projects.

- *Examples of eligible projects include wind, closed-loop and open-loop biomass, geothermal, landfill gas, trash-to-energy, hydropower, solar and advanced or leading edge biofuels production facilities.*

C., Continued

2. Eligible Projects for Section 1705.

- *Eligible projects must:*
  - Involve renewable energy generation in the United States.
  - Use a "commercial technology."
  - Commence construction by September 30, 2011.
  - Have a credit rating equivalent to a "BB" from Standard & Poor's or Fitch, or "Ba2" from Moody's.

- *"Commercial technology" is defined as "a technology in general use in any commercial marketplace" (i.e. worldwide) that "has been in operation in each such commercial project for a period of at least two years" from the commercial operations date of that project.*

C., Continued

3. Eligible Recipients for Section 1705.

- *Applications must be filed by a private lender or a "lead lender" representing a consortium of lenders, and not by the borrower.*

- *An "eligible lender" is any person or legal entity engaged in the business of lending money, including:*
  - Commercial banks and investment banks.
  - Savings and loan institutions.
  - Insurance companies.
  - Factoring companies.
  - Institutional investors, venture capital and private equity firms.

C., Continued

4. Eligible Loan Guarantee Coverage.

- *Projects can obtain <u>up to</u> 80% DOE loan guarantee coverage for <u>up to</u> 80% of project costs, or <u>up to</u> 64% of project costs are covered.*
- *Projects, thus, must locate collateral coverage for <u>at least</u> 16% of the loan or obtain additional project equity.*
- *DOE and eligible lenders are pari passu in their lien positions on each of the covered and uncovered portions of the loans.*
- *Lenders can strip off the loan guarantees to sell the paper into the secondary markets.*
- *Eligible lenders generally provide loans with interest rates of approximately 300-400 basis points (or more) over LIBOR and tenures of approximately 7-10 years.*

C., Continued

5. Schedule of Non-Refundable Fees Payable to DOE for Section 1705:

- *Application fee: $50,000, 25% with Part I and 75% with Part II.*
- *Facility fee: 1/2 of 1.0% of guaranteed portion of Guaranteed Obligation, 20% payable upon the signing of a Term Sheet and 80% at closing.*
- *Maintenance fee: Expected to be in the range of $10,000 to $25,000 per year and payable by the Borrower, the amount and payment due dates to be specified in the Loan Guarantee Agreement.*
- *Attorneys/Consultants fee: DOE shall be entitled to payment for additional internal administrative costs and related fees and expenses for its independent consultants and outside counsel.*
- *No Credit Subsidy Cost for Section 1705 loan guarantees.*

C., Continued

6. October 7, 2009 Solicitation for Section 1705 for Renewable Power Projects:

- *Part I may be submitted at any time prior to Part II.*

- *Part II may be filed any time after the DOE notifies the applicant of an accepted Part I evaluation.*

- *DOE evaluates Part I based on:*
  - Eligibility of proposed project and lender.
  - Readiness of project to proceed and consistency with the objectives of the loan guarantee program.

C., Continued

- *10 rounds in Part II.*

Part II Submission Rounds	
1. November 23, 2009	6. July 8, 2010
2. January 7, 2010	7. August 23, 2010
3. February 22, 2010	8. October 7, 2010
4. April 8, 2010	9. November 22, 2010
5. May 24, 2010	10. January 6, 2011

C., Continued

- *Construction must commence by September 30, 2011, and is defined as the borrower having:*
  - Completed all pre-construction engineering and design.
  - Received all necessary licenses, permits and local and national environmental clearances.
  - Engaged all contractors and ordered all essential equipment and supplies.
  - Begun or resumed physical construction at the primary site of the project.

C., Continued

- *DOE is expected to issue Solicitations for (i) manufacturers of commercial renewable energy property and (ii) leading edge biofuels.*
- *DOE is expected to issue rules for small businesses to better enable their program participation.*
- *DOE may issue a solicitation enabling venture capital, private equity, infrastructure and other funds to obtain DOE loan guarantees to secure debt to leverage existing fund equity for investments (and possibly loans) into clean technologies and renewable energy projects in the U.S.*
- *Note that for Section 1705 Buy America Act provisions will apply only to public, and not private, sector projects.*

D. DOE Sections 1703 v. 1705

- **Section 1705 projects must employ “commercial technologies.”**
  - *Section 1703 projects must employ “new or significantly improved technologies.”*

- **Section 1705 projects must commence construction by Sept. 30, 2011. The ability to implement a project expeditiously takes on greater importance.**
  - *Section 1703 projects have no construction deadline.*

D., Continued

- **Section 1705 projects must comply with the Davis-Bacon Act, which requires payment of “prevailing wage” to all laborers.**
  - *Section 1703 has no such requirement.*

- **Section 1705 projects are not required to pay the “credit subsidy cost” of a loan guarantee, which is the cost to the federal government of assuming the risk of a default on a loan.**
  - *Section 1703 requires the borrower to pay the credit subsidy cost at closing for loan guarantees on qualified projects.*

D., Continued

- **Section 1705 lender interest rates are generally higher than those under Section 1703, while Section 1705 loan tenures are generally shorter than those under Section 1703.**

- **Note that for Sections 1703 and 1705, Buy America Act provisions will apply only to public, and not private, sector projects.**

E. Tax Credit Extensions

- **Discussions are underway in the Congress to extend various programs enacted or modified by the ARRA.**
  - *Deadlines for Cash Grants and Loan Guarantee Programs may be extended.*
- **The recently proposed Solar Manufacturing Jobs Creation Act (S. 2755) would add equipment for solar power manufacturing to the list of properties eligible for an existing Solar Investment Tax Credit of 30%.**
- **Funding for the Section 48C advanced manufacturers tax credit may be expanded by an additional $2.3 billion, and critical dates may be extended.**
  - *The $2.3 billion currently allotted for 48C is fully committed.*

E., Continued

- *The Section 48C tax incentive is for manufacturers of advanced energy property, not generators of renewable electricity, and is designed as a tax credit, not as a grant.*
  - Each of the incentives are independently are measured against 30% of the qualified costs of the specified energy property.
- *The same taxpayer cannot take advantage of both tax incentives for the same specified energy property.*
- *The Section 48C incentive is designed to be obtained through a competitive process, if extended/re-appropriated, with evaluation and scoring by each of DOE and Treasury, and ultimate selection and approval by Treasury.*

Thank You!

- Travis L.L. Blais, Esq. **Mintz, Levin, Cohn, Ferris, Glovsky and Popeo, P.C.,(617) 348-1684, TBlais@mintz.com.**

- Sahir Surmeli, Esq. **Mintz, Levin, Cohn, Ferris, Glovsky and Popeo, P.C., (617) 348-3013, SSurmeli@mintz.com, Twitter.com/EnergyCleanTech.**

- Mark J. Riedy, Esq. **Mintz, Levin, Cohn, Ferris, Glovsky and Popeo, P.C., (202) 434-7474, MJRiedy@mintz.com.**