

Legal Structures for Project Development

Tribal Energy Projects

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***Tribal Energy Development Workshop
April 21-23, 2009
Denver, Colorado***

A Blessing for this Workshop

Dear God,

- **Bless the people of the Native Nations for giving us a reason to serve. As long as we live, we will never stop learning from you.**
- **Bless our families, who we miss on our journey and who welcome us on our return.**
- **Bless our United States of America, our Tribal Governments and all the staff at NREL for bringing us together.**

Today's Presentation: Focus on Legal Issues

8:30 – 9:00

**The New Energy
Economy and Proposed
Legislation**

9:00 – 10:00

**The Tribal Energy
Development Handbook**

- **Organizational Structure
of Tribal Energy Projects**

BREAK

10:30 – 11:30

- **Key Energy Agreements
Q&A**

Funding Sources for Tribal Energy Projects

- **Energy development costs money – understanding funding sources is key.**
- **Many renewable energy projects would not be financially feasible without federal and state incentives.**
- **Congress has enacted several incentives to encourage the development of renewable energy projects.**

New Energy Economy

- **Concerns about climate change are escalating pressure to develop alternatives to fossil fuel**
- **Economic recovery efforts creating focus on energy efficiency, job creation and solutions for long-term economic prosperity**
- **Increased emphasis on collaboration and development between and among states, tribes, local communities and organizations**
- **Developing vision for the future: energy generated from renewable resources, carried over transmission systems maximized with “smart-grid” technology.**

Clean Energy and Security Act of 2009

- The legislation has four titles: (1) a "clean energy" title that promotes renewable sources of energy and carbon capture and sequestration technologies, low-carbon transportation fuels, clean electric vehicles, and the smart grid and electricity transmission; (2) an "energy efficiency" title that increases energy efficiency across all sectors of the economy, including buildings, appliances, transportation, and industry; (3) a "global warming" title that places limits on the emissions of heat-trapping pollutants; and (4) a "transitioning" title that protects U.S. consumers and industry and promotes green jobs during the transition to a clean energy economy.

New Legislation

- **Retrofit for Energy and Environmental Performance (HR 1778)**
 - **Included in Waxman/Markey draft of American Clean Energy and Security Act of 2009**
 - **Increases efficiency 20% nationally by retrofitting millions of homes and commercial buildings**
 - **30% impact on GHG nationwide**

New Legislation

- **Green Bank Act of 2009 (HR 1698)**
 - **Facilitate development of clean energy**
 - **Clean energy project defined as any electricity, transmission, storage, heating, cooling, industrial process or manufacturing whose primary purpose is deployment, development or production of energy system or technology that avoids, sequesters, reduces GHG's or air pollutants**

New Legislation

- **Cap and Dividend Act of 2009 (HR 1862)**
 - **Sets emission reduction targets at 25% below 2005 levels by 2020 and 85% below 2005 levels by 2050 for covered emissions'**
 - **Places an upstream compliance obligation on the first seller of fossil fuels into the US market**
 - **Auctions 100% of carbon permits and returns 100% of auction proceeds in the form of a monthly consumer dividend to every lawful resident of the US with a valid Social Security number**

New Legislation

- **Energy and Water Integration Act of 2009 (S 531)**
 - **Requires DOE to develop an Energy-Water Research and Development Roadmap and other studies to analyze impact of energy development on water resources**
 - **Water impact analysis for new energy and climate solutions over 18 months**

New Legislation

- **Omnibus Public Land Management Act of 2009 (HR 146)**
 - **Public Law 111-11 on March 30, 2009**
 - **Programs and activities for wilderness preservation, boundary adjustments, national conservation areas, land conveyances and exchanges, watershed management**
 - **Title IV: Forest Landscape Restoration Act includes woody biomass provisions for renewables**

New Legislation

- **Appliance Standards Improvement Act of 2009 (S 598)**
 - **Amends the Energy Policy and Conservation Act to improve federal appliance standards**
- **Restoring America's Manufacturing Leadership through Energy Efficiency Act of 2009 (S 661)**
 - **DOE grants and loans, partnerships to encourage manufacturing technology development**

Other Recent Developments

- **April 9, 2009: Department of Interior Secretary Salazar and FERC Chairman Wellinghoff signed a MOA clarifying each agency's jurisdictional responsibilities for siting renewable energy on the Outer Continental Shelf (OCS).**
- **The MOA should clear the way for wind, wave, tidal, ocean current, and solar energy projects on the OCS.**

Proposed Legislation

- ***Tribal PTC Transfer Bill* introduced by U.S. Senator Tim Johnson (D-SD).**
- **If passed, would encourage joint partnerships between private investors and tribes by allowing tribes to transfer Production Tax Credits to private joint partners on renewable energy projects**

S 802

- **111th CONGRESS
1st Session**

S. 802

To amend the Internal Revenue Code of 1986 to allow Indian tribes to transfer the credit for electricity produced from renewable resources.

IN THE SENATE OF THE UNITED STATES

April 2, 2009

Mr. JOHNSON introduced the following bill; which was read twice and referred to the Committee on Finance

A BILL

- **To amend the Internal Revenue Code of 1986 to allow Indian tribes to transfer the credit for electricity produced from renewable resources.**
- *Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,*

IRC Amendment

- **SECTION 1. TRANSFER BY INDIAN TRIBES OF CREDIT FOR ELECTRICITY PRODUCED FROM RENEWABLE RESOURCES.**
- (a) In General. -- Paragraph (3) of section 45(e) of the Internal Revenue Code of 1986 (relating to production attributable to the taxpayer) is amended to read as follows:
- "(3) PRODUCTION ATTRIBUTABLE TO THE TAXPAYER. --
- "(A) IN GENERAL. -- In the case of a facility in which more than 1 person has an ownership interest, except to the extent provided in regulations prescribed by the Secretary, production from the facility shall be allocated among such persons in proportion to their respective ownership interests in the gross sales from such facility.

Transfer and Assignment Rule

- **"(B) SPECIAL RULE FOR INDIAN TRIBES. --**
- **"(i) IN GENERAL. -- In the case of a facility described in subparagraph (A) in which an Indian tribe has an ownership interest in the gross sales from such facility, such Indian tribe may assign to any other person who has such an ownership interest in such facility any portion of the production from the facility that would (but for this subparagraph) be allocated to such Indian tribe. Any such assignment may be revoked only with the consent of the Secretary and shall be made at such time and in such manner as the Secretary may provide.**

Definitions and Effective Date

- **"(ii) INDIAN TRIBE. -- For purposes of clause (i), the term "Indian tribe" means any Indian tribe, band, nation, pueblo, or other organized group or community, including any Alaska Native village or regional or village corporation, as defined in, or established pursuant to, the Alaska Native Claims Settlement Act (43 U.S.C. 1601 et seq.) which is recognized as eligible for the special programs and services provided by the United States to Indians because of their status as Indians."**
- **(b) Effective Date. -- The amendment made by this section shall apply to electricity produced and sold after the date of the enactment of this Act.**

New Regulation

- **EPA announces first step toward GHG regulation with endangerment finding announced April 22, 2009**
- **18 months implementation**
- **Cap and Trade Legislation expected to replace EPA regulation**

Other Agency Action

- **DOE loan guarantee (\$535 million) for solar manufacturing project in California covering 75% of project costs**
- **Pentagon awarded \$20 million contract for cellulosic ethanol project to produce jet fuel, seeking billions more for similar projects**
- **DOE funding for state energy programs require GHG reporting**
- **FERC proposed guidance and Smart Grid development plan**
- **FTA \$100 million in stimulus funds for energy efficiency and GHG mitigation projects**

The American Recovery & Reinvestment Act of 2009

- **Energy Efficiency and Weatherization: \$34 B**
- **Renewable Energy: \$7.9 B**
- **Grid Upgrades/Smart Grid: \$10.9 B**
- **Public Transportation Improvements: \$17.7 B**
- **Alternative Fuel Vehicles: \$1.3 B**
- **Research and Development: \$4.5 B**
- **Green Jobs Training: \$1.15 B**
- **Total: \$113.5 B**

Stimulus Tribal Set Asides

- **\$60 million for Tribal Clean Water Grants**
 - The legislation appropriates \$4 Billion for State Revolving Funds under the Water Pollution Control Act, of which 1.5% is set aside for tribal grants.
- **\$30 million for Tribal Drinking Water Grants**
 - The legislation appropriates \$2 Billion for State Drinking Water State Revolving Funds, of which 1.5% is set aside for tribal grants. Up to 4% may be transferred to the Indian Health Service to support management and oversight of tribal projects.

Tribal Set Asides, Continued

- **\$1.12 million for Tribal Energy Efficiency and Conservation Block Grants. The legislation appropriates \$56 million for Grants, of which 2% is set aside for tribal grants.**
- **\$10 million for the Indian Loan Guarantee Program for Indian-owned businesses.**
- **\$10 million to Community Development Financial Institutions for financial assistance, technical assistance, training, and outreach programs that benefit tribal communities. \$2 million of the allocated amount may be used for administrative expenses.**
- For additional info:
<http://www.indiancountryworks.org/>

The Point of the Stimulus:

- **Double renewable generation by 2011 and reach a 10% renewable penetration goal by 2012**
 - **RES legislation may adopt different market penetration goals**
- **\$134 Billion of new capital investment and renewable energy infrastructure required by 2011; \$217 Billion by 2012**
- **Pace of investment in renewables and efficiency expected to increase dramatically over the prior years**

Tax Based Financing Changes

Tax-Exempt Debt & Tax Credit Bonds

- Tribal economic development bonds**
- Build America Bonds**
- Clean renewable energy bonds
("CREBs")**
- Qualified energy conservation bonds
("QECBs")**
- New market tax credits ("NMTC")**

Federal Tax Incentives – recent changes

What is tax-exempt debt?

- **Tax-exempt debt is a less expensive way for a Tribe to borrow money for a development project.**
- **Less expensive because the interest payments that the Tribe makes in repaying the debt is not treated as taxable income to the person who provides the money**
- **Lender will therefore offer a lower interest rate = savings for Tribe.**

When can Tribes borrow using tax-exempt debt?

- **Before the 2009 Stimulus Act, tax-exempt debt available to tribes and their political subdivisions**
- **To pay for “essential government functions” such as construction of schools, roads, and government buildings**
- **IRS generally concluded that tribes may not issue tax-exempt debt for commercial and industrial activities**

Tribal Economic Development Bonds

- **A tribal economic bond issued by an Indian tribal government is treated as if such bond were issued by a State. This removes the “essential governmental function” limitation that typically applies to tax-exempt bond issuances by tribes.**
- **Tribal economic development bonds may not be issued for facilities that house or that are used in the conduct of gaming or for facilities that are located outside the Indian reservation.**

The American Recovery and Reinvestment Act of 2009 -- Significant Changes

- **Tribes can now use Tribal Economic Development Bonds to finance a wide variety of projects.**
- **Any project that a state government could finance, so long as**
 - **Located on an Indian reservation**
 - **Not related to gaming**
 - **Volume cap allocation**
- **Energy development and transmission projects may be eligible for tax-exempt financing**

The American Recovery and Reinvestment Act of 2009 -- Significant Changes

- **Caveat: The aggregate amount of tribal economic development bonds that can be issued by tribes is capped at \$2 billion and required to be allocated by the Secretary of Treasury in consultation with the Secretary of the Interior.**

The American Recovery and Reinvestment Act of 2009 -- Significant Changes

Build America Bonds

- **New type of tax credit bond that tribes can use instead of tax-exempt bonds**
- **Lender eligible for a tax credit equal to 35% of the amount of interest payable by the issuer (Tribe).**
- **In lieu of lender receiving a tax credit, Tribe may qualify to elect to receive a cash payment in same amount.**

The American Recovery and Reinvestment Act of 2009 -- Significant Changes

- **Build America Bonds may be available for development of tribal energy projects, however they are subject to three conditions:**
 - **Must be issued during 2009 and 2010**
 - **Bond proceeds cannot be used by or loaned to private parties**
 - **Cannot be used for refinancings**

Another kind of Tax Credit Bonds: Clean Renewable Energy Bonds

- **As with Build America Bonds, issuers of CREBs only repay the principal amount of the bonds and the bondholder receives tax credits in lieu of interest.**
- **Governmental bodies, including Indian tribal governments, are eligible to issue clean renewable energy bonds (“CREBs”) to finance qualified renewable energy facilities.**

Clean Renewable Energy Bonds . . .

- **A “qualified renewable energy facility” includes a wind facility, closed-loop biomass facility, open-loop biomass facility, geothermal or solar energy facility, small irrigation power facility, landfill gas facility, trash facility, and marine and hydrokinetic renewable energy facilities owned by an Indian tribal government or any political subdivision thereof.**

Clean Renewable Energy Bonds . . .

- **The aggregate amount of CREBs that can be issued is capped and required to be allocated by the Secretary of Treasury. The American Recovery and Reinvestment Act of 2009 increases the cap on CREBs by \$1.6 billion, with one third of that increase allocated to state, local and Indian tribal governments.**

Qualified energy conservation bonds (“QECBs”)

- **Governmental bodies, including Indian tribal governments, are eligible to issue qualified energy conservation bonds if 100 percent of the available project proceeds are used for one or more qualified conservation purposes.**

Qualified Energy Conservation Bonds

- **Like CREBS, qualified energy conservation bonds are tax credit bonds, where the issuer repays the principal amount of the bonds and the bondholder receives federal tax credits in lieu of the interest. However, it may be necessary to issue the bond at a discount or pay supplemental interest.**
- **The tax credit amount is 70 percent of the amount set for CREBs.**

Qualified Energy Conservation Bonds

- **"Qualified conservation purposes" includes the production of electricity from renewable energy resources, including development of a wind facility, closed/open-loop biomass facility, geothermal or solar energy facility, small irrigation power facility, landfill gas facility, trash facility, and marine and hydrokinetic renewable energy facilities.**
- **In addition, tribes must use qualified energy conservation bonds for projects that would otherwise qualify for tax-exempt financing.**

Qualified Energy Conservation Bonds

- **The American Recovery and Reinvestment Act of 2009 increased the volume cap on qualified energy conservation bonds from \$800 million to \$3.2 billion. The volume cap is allocated among the states based on population, and large local governments within a state (which includes Indian tribal governments) are allocated a portion of such volume cap based on population within the state.**

New market tax credits (“NMTC”)

- **The New Market Tax Credit Program is administered by the U.S. Treasury**
- **Permits taxpayers to receive a credit against income taxes for making a qualified equity investment in a designated “Community Development Entity.”**
- **Credit to investor is 39% of the cost, claimed over a 7 year credit allowance period.**
- **Equity must be used by CDE to invest in a low-income community.**

New market tax credits (“NMTC”)

- **Example: Native Times press release about a lender and a Community Development Entity teaming up to provide more than \$12.7 million in NMTC financing.**
- **NMTC financing will be used to “jump start the building of two electrical substations on the Navajo Nation Reservation.”**
- **New substations will double electrical capacity to Shiprock region & bring service to 400 families currently without power.**

Conclusion regarding Bond Opportunities

- This general overview highlights several potential sources of funding for tribal energy projects.
- Each energy project has unique circumstances and the right funding source for one project may not be best for another.
- Tribe should retain bond counsel to advise them on the specifics of these options.

Brief of Review of Recent Changes

Now for a brief review of recent changes to the federal tax incentives

- **PTCs**
- **ITCs**
- **Bonus Depreciation**

Significance of Structuring Tax Equity Investment

- **Typically, 60 to 65% of the economic benefits in US wind projects (on or off tribal lands) are tax benefits; also applies to other energy projects**
- **Two primary benefits**
 - **Depreciation**
 - **Production Tax Credits**
- **Tribe not subject to federal income tax, not eligible for tax credits. Deal needs to structure tax credit investment opportunities**

Institutional Tax Credit Investors

- **Smaller market of institutional tax credit investors – e.g. insurance companies, investment funds, oil companies -- to invest in the equity side of renewable energy projects, particularly for the tax credits.**
- **These investors are primarily interested in the tax benefits, not long-term ownership.**
- **For up-front capital-intensive energy projects, a project's cost of capital and financial structure has a significant impact on the financial performance of the project.**

Variety of Structures for Tax Equity

- **Not all structures work or are appropriate in all transactions. Transaction specific tax advice is critical and must be obtained at an early stage**
- **If flip is used, tribe should negotiate position to acquire PTC share after flip**
- **Majority position usually negotiable after a number of years (typically, but not always the estimated life of initial project installation)**

Production Tax Credit

- **Section 45 of the Internal Revenue Code provides a production tax credit (“PTC”) upon the sale of electricity produced from certain qualified energy resources like wind, biomass, geothermal, and solar.**
- **The PTC is available during the 10 year period (5 years in some cases) beginning on the date the qualified facility is placed in service.**
- **The PTC can be used to offset the federal income taxes of the taxpayer receiving the credit on a dollar-for-dollar basis.**

Qualifications:

- “**Qualified energy resources**” include wind, closed-loop biomass, open-loop biomass, geothermal energy, solar energy, small irrigation power, municipal solid waste, hydropower production, and marine and hydrokinetic renewable energy.
- Generally, a “**qualified facility**” is a facility that produces electricity from qualified energy resources and that satisfies certain other requirements set forth in Section 45, including being placed in service by certain dates.

Limits On PTCs

- **The PTC is subject to phaseout and certain adjustments and limitations. If a facility is also financed through certain grants, tax-exempt financing or other credits, then Section 45 reduces the PTC.**
- **The adjustments, limitations and phaseout should be carefully analyzed with respect to each project based on the facts of the particular project and applicable law.**

Recent Changes to the PTC

The American Recovery and Reinvestment Act

- **Extends the period that a qualified facility must be completed and placed in service.**
- **Wind projects will now qualify for PTCs if placed in service by December 31, 2012.**
- **Biomass, geothermal, landfill gas, trash, qualified hydro projects, and marine and hydrokinetic renewable energy projects will now qualify if placed in service by December 31, 2013.**

PTC or ITC, but Not Both

- **If a project is eligible for PTCs and ITCs, then the project owner must choose which credit to take with respect to the project.**
- **So what is an ITC?**

Investment Tax Credits

- **ITCs are tax credits for certain types of renewable energy property, including solar systems and combined heat and power systems provided for in Section 28 of the Internal Revenue Code.**
- **With respect to solar and certain other property, the ITC is equal to 30 percent of the taxpayer's cost basis in the property. With respect to combined heat and power systems and certain other property, the ITC is equal to 10 percent of the taxpayer's cost basis in the property.**

ITCs continued . . .

- **The entire amount of the ITC is available to the taxpayer in the year the energy property is placed in service, whereas the PTC is available over a 10 year period (5 years in some cases) as electricity is produced and sold by the project owner.**
- **If an ITC is claimed with respect to a project and the project ceases to be investment credit property within the five year period after the project is placed in service, then all or part of the ITC is subject to recapture.**

ITCs continued . . .

- **Like the PTC, the ITC can be used to offset the federal income taxes of the taxpayer receiving the credit on a dollar-for-dollar basis.**
- **A project eligible for an ITC can be leased to another party and the lessor can still qualify for the ITC. However, if the project is leased to a tax-exempt party, then it will not qualify for the ITC. This can be a material issue in structuring an ITC transaction involving a tribe.**

ITC in lieu of a PTC

- **The 2009 Act now permits most projects that would otherwise qualify for PTCs to take a 30% investment tax credit in lieu of a PTC. The 30% investment tax credit is available in the tax year the qualified facility is placed in service.**

ITC in lieu of a PTC

- **This is a significant change because PTCs are generated over a 10 year period (less than 10 years with respect to some facilities) and based on the amount of electricity sold by the qualified facility during the 10 year period, whereas the 30% investment tax credit is available in the year the project is placed in service and does not require the sale of electricity, which can be uncertain with respect to many projects (e.g., wind).**

Other Recent Changes to PTCs and ITCs

Under 2009 American Recovery and Reinvestment Act:

- **Certain projects can now claim a cash grant from the U.S. Treasury in lieu of an ITC or PTC.**
- **The amount of the grant is 30% of the cost of certain qualified facilities, including wind, biomass and solar facilities, and 10% with respect to certain other qualified facilities.**

Other Recent Changes to PTCs and ITCs

- **To qualify for the grant, construction on the qualified facility must begin in 2009 or 2010, and the facility must be placed in service by the date required to be eligible for PTCs.**
- **The grant eliminates the need to find investors with an appetite for tax credits.**

Changes to PTCs and ITCs under the American Recovery and Reinvestment Act of 2009

- ***Unfortunately, this grant is not available to projects owned by any federal, state, or local government, including an Indian tribal government, a tax-exempt organization described in IRC Section 501(c), or any partnership or other pass-through entity of which any of the foregoing is a partner or holder of an equity interest.***
- **This is an example of how funding sources may dictate how a Tribe structures its energy project development.**

Challenge: How to Get the Benefit of Tax Credits

- **Developers of renewable energy projects are often unable to fully utilize PTCs or ITCs generated by a project.**
- **Likewise, Indian tribal governments, tribal enterprises and other tribal organizations not subject to federal income tax have no need for PTCs or ITCs.**
- **Federal tax rules do not currently allow the owner of a project to simply transfer a PTC or ITC to a third party in exchange for a cash payment.**

Challenge: How to Get the Benefit of Tax Credits

- **Fortunately, a number of structures have emerged that allow the developer of a renewable energy project to monetize the value of PTCs or ITCs generated by the project. These structures often involve the use of a partnership or a lease and participation by a party with an appetite for the tax credits.**

Partnership Flip Structure

- **Under a partnership flip structure, the renewable energy project is owned by an organization taxed as a partnership for federal income tax purposes, such as a partnership, limited partnership or limited liability company.**
- **A party with a need for tax credits (referred to herein as a “tax credit investor”) makes a cash investment in the partnership. The developer of the project also retains an equity interest in the partnership.**

The Flip Structure Basics

- **LLC agreement provides for percentage interests among investors, usually 90% or more to tax equity investor and remainder to sponsor equity/developer**
- **After 10 year period, or longer period for PTC investor to meet agreed-upon internal rate of return, percentage interests “flip” such that sponsor/developer holds 90+% and PTC investor holds 10%**
- **Usually combined with a purchase option for the PTC investor’s interest after the flip**

Why the Flip Structure Exists

- **In order to claim the PTC, the taxpayer must own the facility and produce the electricity**
- **The party claiming the credit must receive the same proportion of gross revenues and PTCs from the project**
- **PTCs cannot be stripped and sold separately**
- **Other limitations (reduced by federal, state and local credits and grants related to construction of the facility, offsets limits to other taxes, subject to passive loss rules)**

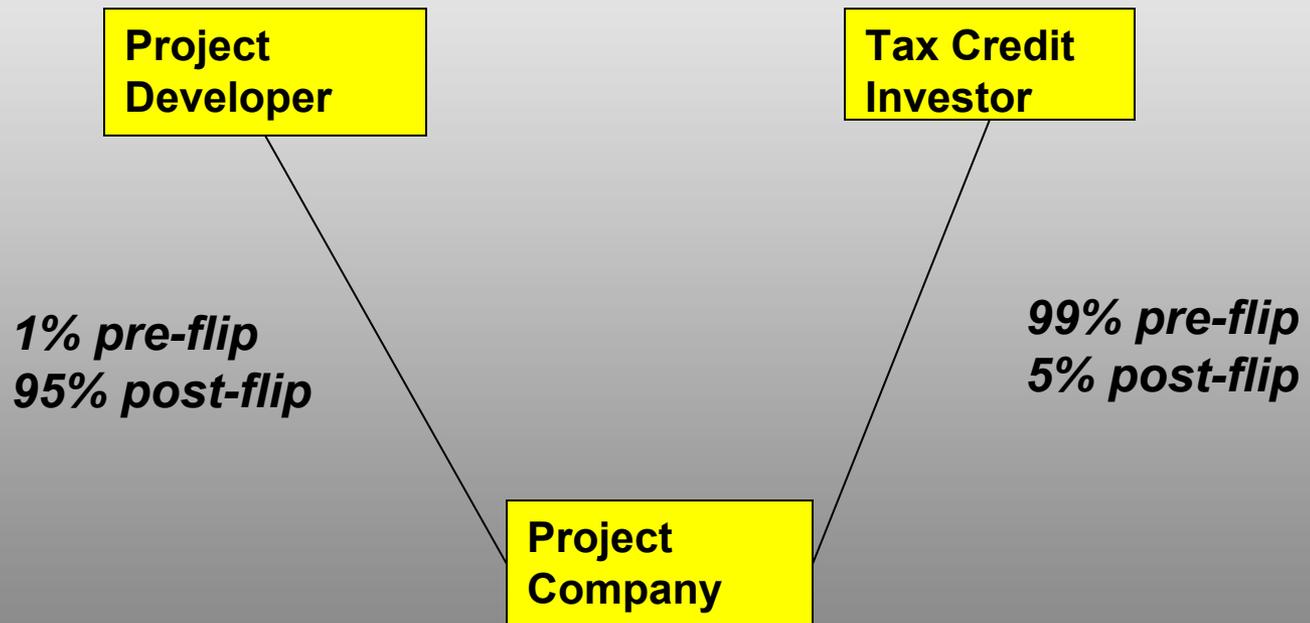
Partnership Flip Structure continued...

- **In exchange for its cash investment, the tax credit investor is initially allocated substantially all of the profits, losses and tax credits generated by the partnership until the tax credit investor receives its negotiated return on its investment, taking into account the value of the tax credits, depreciation, and cash flow.**

Partnership Flip Structure continued...

- **After the tax credit investor has achieved its negotiated return, the ownership of the partnership automatically flips and the developer and other equity investors are allocated substantially all of the profits and losses generated by the partnership. The flip typically occurs at the time of or following expiration of the tax credit period for PTCs or recapture period for ITCs.**

Following the flip, the developer typically has an option to acquire the tax credit investor's remaining equity interest in the partnership.



Another Approach: Sale-Leaseback Structure

- **Projects that qualify for ITCs can utilize a sale-leaseback structure in lieu of a partnership flip structure.**
- **In a basic sale-leaseback transaction, the developer sells the project to the tax credit investor and the tax credit investor immediately leases the project back to the developer.**

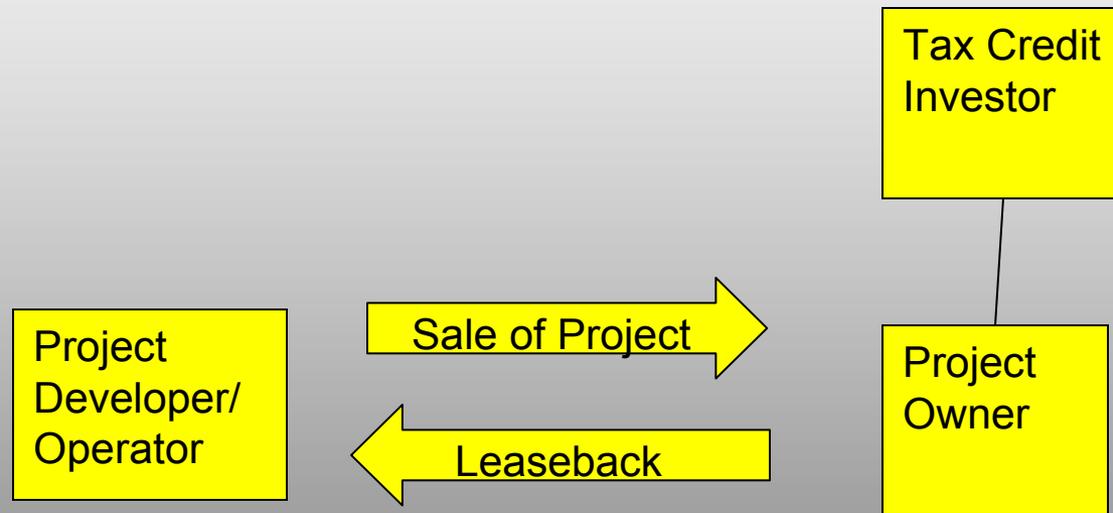
Another Approach: Sale-Leaseback Structure

- **As the owner of the project, the tax credit investor is eligible for the ITCs and the depreciation deductions associated with the project. The sale of the project, including the transfer of the tax credits and depreciation, effectively monetizes the tax credits and depreciation and provides a financing mechanism for the project.**

Sale-Leaseback Structure continued...

- **At the end of the lease, the project developer will typically have the right to repurchase the project at fair market value.**
- **There are variations on this basic sale-leaseback structure.**
- **If the project is leased to a tax exempt party, then it will not qualify for ITCs. This materially limits the application of sale-leaseback transactions where a tribe or other tax-exempt party is directly participating in the project.**

Sale-Leaseback Structure



Bonus Depreciation for Renewable Energy Projects

- **Property used in renewable energy projects is often eligible for a 5 year MACRS depreciation recovery period.**
- **In 2008, taxpayers were permitted to deduct 50% of the cost of certain “qualified property” acquired and placed in service during the year (“bonus depreciation”), in addition to regular depreciation on the remaining cost of the property.**

Bonus Depreciation for Renewable Energy Projects

- **This allowed in excess of 50% of the cost of qualified property to be deducted in 2008. Qualified property includes property that has a recovery period of 20 years or less, like wind turbines, solar panels, and other equipment.**
- **The American Recovery and Reinvestment Act of 2009 extended bonus depreciation to qualified property acquired and placed in service in 2009.**

Accelerated Depreciation for Tribal Projects

- **Section 168(j) of the Code provides certain accelerated depreciation schedules for “qualified Indian reservation property,” e.g. project costs may be recovered over an accelerated 3-year period instead of 5-year.**
- **Generally, “qualified Indian reservation property” is property that is used by the taxpayer predominantly in the active conduct of a trade or business within an Indian reservation.**

Accelerated Depreciation for Tribal Projects

- **The Code imposes a number of conditions on the above definition of “qualified Indian reservation property.” For instance:**
 - **The property must not be used or located outside the Indian reservation on a regular basis;**
 - **Unless the property is an infrastructure project (such as roads, power lines, water systems, or communication facilities), the taxpayer must not have acquired the property directly or indirectly from a related party;**
 - **The property must not constitute tax-exempt use property or tax-exempt bond financed property, among others; and**
 - **The property must be placed in service by the end of 2009.**

Conclusion: Sources of Funding

- Renewable energy incentives are changing fast.
- Tribe should retain counsel to advise them on the specifics of these options.
- Source of funds for a project may impact how tribe approaches organizational structure for project development . . . Next topic.

The Tribal Energy Development Handbook

- **Original concept**
 - **Model agreements**
 - **Five basic issues of primary importance to tribal energy deals**
 - **Tribal ownership**
 - **Land issues**
 - **Joint ventures**
 - **Capturing the benefit of tax incentives**
 - **Energy agreement essentials**
 - **Training materials**

Today's Presentation: Select Highlights

- **Additional features:**
 - **Addressing recent legislative changes to regulation and funding**
 - **Adding a project development guide that can be referenced throughout the Handbook**
 - **Reorganization to flow from early to late stage development processes and issues**

Part II: The Development Process

- **Goals and objectives of the tribe in developing a renewable energy project that influence legal structures**
- **Goals of the deal structure**
- **Elements of key deal agreements**

Building Wealth in Indian Country

- **Energy development a long-term strategy**
- **Successful energy projects, no matter how large or small, require 3 elements:**
 - **Efficient business structures**
 - **Standardized and fair regulatory processes administered by reliable, stable and transparent government authorities**
 - **Enforceable, fair and balanced contracts**
- **Once a level playing field is established, these three elements will generate a wide variety of economic opportunities for the tribe**

A Team Approach

- **Every energy project requires a team coordinated by the Tribe**
- **The team must have financial, legal, political and public relations experience**
- **Within each discipline, certain subject matter expertise is essential**
 - **Legal: e.g., tax, real estate/land, finance, contracts (PPA's, joint venture, equity), Indian law, environmental law, government relations**
 - **Energy development experience key**

Should the Tribe be a Passive or Active Player?

- **Pros and cons of each approach**
- **Assess tribes resources and willingness to commit to the project regardless of choice**
- **Long-term partnership with non-Indian parties on Indian lands in both cases:**
 - **Tribal-owned/operated: PPA's, investors**
 - **Not tribal owned/operated: long-term presence and partnership**
- **DOE Tribal Energy Program can help tribes evaluate this issue**

From Grants to Long Term Resources

- **Attracting private capital for renewable resource projects generally requires five essential elements:**
 - 1. **Renewable resource**
 - 2. **Site control**
 - 3. **Buyers for the energy**
 - 4. **Transmission to market**
 - 5. **Incentives (production tax credits, other tax incentives)**

Have Energy Resources Been Assessed?

- **Type and amount/magnitude of resource**
- **Economic feasibility of development**
- **Will resource(s) meet demand (both on and off the reservation)**
- **Ability to meet other tribal objectives**
 - **Tribe as sponsor of renewable energy projects**
 - **Tribes as utility owners/operators**
 - **Tribes as regulators**

Land Control

- **Site control and fair market valuation early in the development process**
- **Assumption by some private energy developers that obtaining third-party control of Indian lands may be simpler and cheaper than non-Indian private land**
- **Budget and schedule must factor:**
 - **Tribal land-withdrawal processes**
 - **Federal lease requirements**

Buyers

- **Fairly certain in states with RPS**
- **Price increase predictions driven by climate change issues changing the demand and supply outlook**
- **Tribal & non-tribal utilities**
 - **Firm capacity?**
 - **Infrastructure?**
- **Long-term offtake agreements (power purchase agreements or “PPA’s”) with credit-worthy third party buyers**

Transmission

- **Distance to transmission system**
- **Market factors for creative transmission contracts**
- **Load capacity to deliver to market**
- **Ballpark overview a fairly simple exercise for qualified energy consultants**
- **Regional transmission coordinating agencies manage regional transmission grid and maintain data, require reliability and capacity studies**
- **Other DOE agencies, private and public utilities with transmission info**

Key Drivers for Energy Investment

- **Tax benefits: Accelerated depreciation and Production Tax Credits**
- **Serve local energy demands and/or economic development with utility scale projects with revenues to tribe**
- **Cash flow to equity investors**
- **Affiliate contracts**
- **Economic Development and Other Policy**
 - **State/federal incentives**
 - **Environmental/social benefits**

Understanding the Investors

- **Strategic investors**
 - **Capacity to develop investment in the sector**
 - **Capacity to accept project risks because of knowledge and active management**

Institutional Equity Investors

- **Mainly passive investors, motivated by tax benefits and overall return**
- **Experienced in other energy tax credit regimes**
- **Will not accept significant development risk**
- **Requirements similar to lender requirements**

Early Stage Development Equity

- **Substantial development costs required to reach a financeable project**
- **Sponsor and developer may lack adequate capital, development expertise and ability to arrange additional financing**
- **Alternatively, sponsor finds developer with capital, expertise and financing ability**

Late Stage/Construction Stage Equity

- **Made through purchase or joint venture/limited liability company**
- **Required to support power purchase agreements (PPA) or interconnection agreement security, turbine purchase order and construction loans**

The Formation of the Deal – One Model

- **Sponsor (including the tribe and/or a tribal entity such as an enterprise, tribal corporation or Section 17 corporation)**
- **Developer (could be tribe or non-tribal entity)**
- **Project company formed to carry out:**
 - **Development**
 - **Construction**
 - **Operation**

Joint Venture Process

- **Usually begins with a non-binding Letter of Intent coupled with a Confidentiality and Nondisclosure Agreement**
 - **Sets the basic tone for discussions between the tribal sponsor and developer**
 - **Allows both parties to share information without fear of disclosure to competitors**
- **Most non-tribal third parties will accept dispute resolution at this stage pursuant to tribal law**

Joint Venture/Joint Development Agreement

- **Guides the parties through the pre-construction development process**
- **Sets the tone and the “template” for future agreements between the tribal sponsor and the developer**
- **Establishes the business relationship, and the allocation of project development risk between the tribe and non-tribal project entities**

Major Issues in Joint Venture Structure

- **Preconstruction development budget**
- **Project schedule and milestones**
- **Delineation of development activities and responsibilities between tribal sponsor and developer**
- **Rights of compensation before and after financial closing**
- **Allocation of development costs**
- **Property rights**

Critical Issues for Tribal Parties in Joint Ventures

- **Shareholder rights, especially minimum proposed minority shareholder protections (e.g., anti-dilution, rights to acquire interests in the project and project company, management issues)**
- **Tribal employment and contracting preference**
- **Compensation for use of tribal lands, taxation**

Key Sticking Points

- **Dispute resolution, governing law, choice of forum are not the roadblocks they used to be, but must be discussed early**
 - **Waiver of defense and right of sovereign immunity**
 - **Exhaustion of remedies in tribal courts**
 - **Arbitration vs. litigation**
- **Indemnification, limitation of liability, remedies on default and termination**

Negotiating the Sticking Points

- **Limited waiver of immunity to suit essential - limit to specific assets, protect tribal officials and individuals, tie to dispute resolution**
- **Binding arbitration to avoid state court jurisdiction**
- **Authority to compel arbitration, enforce awards, protect parties during arbitration in any court of competent jurisdiction**
- **Insist on clear terms preserving tribal jurisdiction (covenant not to contest tribal jurisdiction on tribal status as Indian nation)**

The Road to Financing: Key Agreements



Project



Interconnection



Buyer

In order to move forward with a project and secure financing, certain key pieces need to fall into place: technical designs, agreements for interconnection and transmission, and **a long-term power purchase agreement (PPA)**.

Power Purchase Agreements (PPA's)

- **An agreement**
- **between a power producer and end-user/
purchaser**
- **for the sale of the output of an energy
project.**

Overview of a PPA

- **A Power Purchase Agreement has the same basic structure as any contract for the purchase and sale of goods.**
- **Some of the provisions are provisions you would see in any purchase and sale contract, some are unique to the purchase and sale of power.**
- **Parties need to understand and be comfortable with all provisions in the PPA.**

Overview of a PPA

1. Preamble – identifies the Parties to the Agreement (the seller and purchaser) and the nature of the Agreement

2. Definitions

3. Effective date

4. Industry terms such as

- Capacity
- Capacity Factor
- Curtailment
- Commercial Operation Date (COD)
- Energy
- Forced Outage
- Megawatt hour (MWh)
- Renewable Energy Credit (REC)

Overview of a PPA . . .

- 5. Conditions precedent to the Parties' responsibilities**
- 6. Party "corporate" approvals**
- 7. Government approvals – land use, construction, environmental, utility regulators**
- 8. Supporting agreements secured – such as transmission and interconnection agreements**
- 9. Requirement to produce power**

Overview of a PPA . . .

10. Required Commercial Operation Date

- This may be especially critical to the party receiving the Section 45 federal production tax credit

11. When and how power is to be delivered

- Transmission scheduling
- Which party arranges and pays for reserve and support requirements
 - Reserves provide backup for unexpected loss of energy production or transmission transfer capability
 - Shaping adjusts the project output over a given time period – for instance, to ensure that the output of a wind project is flat even if the wind is variable or stops, which usually requires a separate agreement with another generation project that operates on fossil fuel

Overview of a PPA . . .

12. MWh delivery expectations

13. Delivery points

14. Capacity Factor (the percentage of potential output expected to be realized in actual operation)

15. Requirement to purchase power

16. Price

- Payments – how and when made
- Whether “green attributes” are included in the purchase price or priced separately
- Mechanism to change price over term of agreement

Overview of a PPA . . .

17. Term – length of the agreement

- Initial length – usually at least 20 years**
- Renewal – short periods, usually no more than 5 years**
- Number of renewals**

18. Operational parameters

19. Curtailment by either party, circumstances allowed and effect on parties responsibilities

20. Communication – with Parties, transmission providers etc.

Overview of a PPA . . .

21. Planned outages/Forced outages

22. Metering, testing meters, project performance reporting

23. Project equipment (primarily turbine and generator) maintenance requirements

24. Defaults and remedies

25. Indemnifications

26. Insurance requirements

- For the project**
- For the Parties**

Overview of a PPA . . .

Other miscellaneous provisions:

- **Handling of confidential information**
- **Assignment**
- **Force majeure events (acts of nature)**
- **Governing law**
- **Requirement to cooperate**
- **Entire agreement**
- **Further assurances**
- **Dispute resolution**
- **Amendments**
- **Waiver**
- **Notices**

Development Process: Three Concurrent Paths



Project



Interconnection



Buyer

In order to move forward with a project and secure financing, certain key pieces need to fall into place: technical designs, **agreements for transmission**, and a long-term power purchase agreement (PPA).

Transmission Agreements

In practice, transmission consists of three separate agreements:

- **Interconnection**: Project and transmission provider enter into an agreement for connection to provider's system.
- **Transmission**: Project or power purchaser and transmission provider enter into an agreement for the transport of power to the purchaser's delivery point.
- **Interconnection**: Purchaser and transmission provider enter into an agreement for connection to provider's system.

Transmission Interconnection Agreement

- 1. Preamble – identifies the Parties to the Agreement (the Project and Transmission Provider) and the nature of the Agreement**
- 2. Definitions (such as Effective Date and Industry Terms)**
- 3. Conditions Precedent to Parties' responsibilities – responsibility for design, construction, etc.**

Transmission Interconnection Agreement

- 4. Construction of Interconnection Facilities**
- 5. Party “corporate” approvals**
- 6. Government approvals required and which Party is responsible for securing them (land use, construction, environmental, utility regulators)**

Transmission Interconnection Agreement

7. Term – Length of Agreement

- Initial length as long as PPA with all renewals**
- Renewal Terms**

8. Operational Requirements and Impact on Power Deliveries

- Curtailment by provider (when, how)**
- Communication**
- Outages/Safety/System Protection**

Transmission Interconnection Agreement

9. Indemnifications

10. Insurance Requirements

11. Other Miscellaneous Provisions

- Handling of Confidential Information**
- Assignment**
- Force Majeure events**
- Governing Law/Choice of Forum/Sovereign Immunity**

Transmission Services Agreement

- **The Agreement for transmission is very similar to the Interconnection Agreement.**
- **Rates will be determined by the provider's tariff, which may provide for "market based" negotiated rates.**
- **FERC regulations require that all parties are treated in a similar fashion and have open access to the transmission system.**

Transmission Services Agreement

- **Reservations of capacity, and information about the transmission system, are made on the provider's OASIS (Open Access Same Time Information System) web site.**
- **There may be a queue for service because transmission capacity is only added in "stair step" increments.**
- **The provider may require that a system study be performed, at the project's expense, to determine availability & conditions.**

Land Agreements

- **Most tribal land held in trust, where fee title is vested in the US on behalf of and for the benefit of the tribe.**
- **Trust lands may not be sold or transferred.**
- **Tribal authority to authorize use of tribal lands is set forth in various provisions of the U.S. Code**
- **Energy development will most likely require tribal government to enter into some land agreements (e.g., lease to tribal entity or developer; right of way for transmission)**

Leasing Tribal Lands

- **Trust lands MAY be “encumbered” – lease most common form.**
- **25 U.S.C. 81 provides that no contract with a tribe that encumbers Indian lands for 7 years or more is valid without approval of the Secretary of the Interior.**
- **Section 81 lists specific required contract terms**

Long Term Leases– 25 U.S.C. section 415

- **“Any restricted Indian lands, whether tribally or individually owned, may be leased by the Indian owners, with the approval of the Secretary of the Interior, for * * * business purposes, including the development or utilization of natural resources in connection with operations under such leases * * *. All leases so granted shall be for term of not to exceed twenty-five years (many tribes have exceptions)**

Long Term Leases– 25 U.S.C. section 415

- **Prior to approval of any lease, BIA must consider whether adequate consideration has been given to, among other things:**
 - **The use of the leased lands**
 - **The height, quality & safety of any structures or facilities to be constructed**
 - **The effect on the environment of the uses to which the leased lands will be subject.**

Right of Ways

- **Transmission across tribal lands also brings with it some unique considerations.**
- **Bureau of Indian Affairs has extensive regulations regarding “Rights-of-Way Over Indian Lands.” 25 C.F.R. Part 169**
- **25 C.F.R. 169.27 specifically relates to right of ways for “power projects” -- transmission provider and tribe must be sure that negotiated agreement is consistent with BIA regulations.**

Leasing Issues

- **Critical early issue due to importance of site control in permitting, negotiations for PPA's, transmission interconnection**
- **Joint venture or development agreement should guide sponsor and developer with general goals of project site lease to avoid surprises during the development process**

Suggestions to Improve the Leasing Process

- **Evaluate tribal code provisions, if any, and consider adopting business site leasing regulations under BIA authority**
- **Consider creation of tribal energy authority (e.g., Dine Power Authority of the Navajo Nation) with leasing powers**
- **Talk with the local BIA officials *early* about the approval process, timelines, federal appraisal requirements, etc.**

Select Features of Lease Structure

- **Permitted uses**
- **Compensation, alternative tax structure**
- **Term (primary and renewal)**
- **Assignment and transfer**
- **Rights on termination, default**
- **Removal of improvements; reserve account**
- **Approved encumbrances**
- **Liability allocation**
- **Dispute resolution**

Structures for the Tax Motivated Equity Investor

- **Recap:**
 - **Joint venture or joint development agreement provides rights of equity investment for tribal sponsor and third party equity investors, including tax credit investors**
 - **Joint venture and lease provide for rights of third party investors as approved encumbrances**

For More Information

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