

Tribal Energy Training Session

Capturing Opportunities

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Overview of Presentation

- **The development process: an overview**
- **Goals and objectives of the tribe in evaluating alternative business structures**
- **Basics of common business structures**
- **Key issues in joint ventures and a few thoughts on leases and rights of way**
- **The Hypothetical (the fun part)**

Historical Paradigm of Energy Projects

- **Energy facilities in Indian Country owned by non-tribal entities**
- **Typical business model**
 - **Lease/royalty arrangement**
 - **Some exceptions, but very few**
- **Tribal employment common, but management less common**
- **Federal control over development of tribal energy resources**

Shifting the Paradigm

- **Tribal owned, operated, regulated energy facilities to serve local and wholesale demand**
 - **Significant tribal investment positions**
 - **Tribal management and labor**
 - **Greater tribal control over development of energy resources**
- = EQUITY AND SHARING OF POLITICAL POWER**
- = BUILDING A DIVERSE AND STABLE TRIBAL ECONOMY**

Building Wealth and Capacity in Indian Country

- **Business development a long-term strategy**
- **Successful ventures, 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 can foster a wide variety of economic opportunities**

Tribal Objectives in Project Development

- **Enhanced tribal capacity for conducting business, attracting investment, and planning options for future economic development**
- **Strengthening sovereignty**
- **Tribal employment and contracting**
 - **Including tribal preference**
- **Protecting tribal assets**

The Six Stages of Project Development

- **“Fatal Flaw” or basic feasibility analysis**
- **Project scoping and team formation**
- **Preliminary engineering, transmission studies; identification of offtakers; site control**
- **Completion of permitting, offtake and transmission agreements, financial Close**
- **Construction**
- **Operation**

Stage One: Feasibility

- **Identify the potential for:**
 - **Demand for power**
 - **Reliable generation (fuel) resource**
 - **Cost effective interconnection capacity**
 - **Ability to obtain site control**
 - **Tribal support and capacity**
 - **Potential partnering opportunities**

Step Two: Project Scoping

- **After reviewing feasibility results and confirming tribal support and capacity:**
 - **Select a project concept**
 - **Select a technology and a technology vendor**
 - **If applicable, select a joint venture partner and development proposals**
- **Development agreement common at this stage**

Step Three: Project Foundations

- **Key investments in:**
 - **Transmission impact analysis**
 - **Demand/offtake analysis**
 - **Detailed financial modeling**
 - **Preliminary site design and engineering**
 - **Initiate permitting and site control activities**

Step Four: Complete Preconstruction

- **Secure everything necessary to start construction:**
 - **Obtain all approvals and permits**
 - **Execute transmission and power sales agreements**
 - **Obtain financing commitments from equity investors and debt/lenders**

Step Five: Construction and Commissioning

- **Once financial close occurs,**
 - **Commence construction**
 - **Project testing**
 - **Complete construction, startup testing and commence operations**
- **Lease payments typically begin here**
- **Project company role evolves from development to operating and management**

A Team Approach

- **Every successful venture requires a team coordinated by the Tribe and motivated by a team leader**
- **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 (joint venture, equity), Indian law, environmental law, government relations**

Top 10 Development Issues

- **Early stage development capital**
- **Efficient tribal business structure with clear, consistent authority**
- **Clear, realistic, and mutual understanding of expectations (e.g., time, cost, return on investment)**
- **Sizing the project correctly**
- **Sharing risk (financial, legal, competition)**

Top 10 Development Issues, Cont.

- **Finding the right offtaker at the right price**
- **Access to transmission**
- **Building and maintaining the right team to get the job done**
- **Streamlining permitting**
- **Funding in a tight market**

Getting Organized

- **Legal counsel and key project advisors play a key role in helping the tribe and/or tribal enterprise get its team together**
- **Understand and Define the Project**
- **Know Your Total Funding Needs**
- **Answer the Questions:** (in plain, short, common English words).
 - **Is this investment “right sized?”**
 - **Can this team execute?**
 - **Can I get a reasonable return in a reasonable time?**

Understand the Risks

- **Input/Technology Risk (e.g., PV solar)**
- **Construction Risk**
- **Operational Risk (e.g., BP)**
- **Output Risk**
- **Sales/growth/reinvestment Risk**

*****A key consideration for creating the right business structure is matching the tribal authority and support (financial, political and legal), to the risks of the venture.***

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 Construction Funding

- **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

- **Long-term offtake agreements (power purchase agreements or “PPA’s”) with credit-worthy third party buyers**
- **Fairly certain in states with RPS**
- **Tribal & non-tribal utilities**
 - **Firm capacity?**
 - **Infrastructure?**

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**

End of Part One

Fundamental Truths About Project Finance

- **Tax incentives alone don't drive the deal**
- **Ready market is vital**
- **Lenders loan to cash flow, and against assets**
- **The investment is secured against the assets**
- **Biggest risks occur BEFORE cash flows**

Types of Risks Managed in the Deal

- **Construction risk**
- **Operation risk**
- **Sales risk**
- **Contract extension risk**
- **Environmental/regulatory risk**

What are Investors Looking For?

- **Specific range for Return on Investment (ROI)**
- **Three essentials/questions:**
 - **1. Project Size: scale and flexibility?**
 - **2. Management Team: can it deliver?**
 - **3. The Plan: will it work?**

Renewable Energy Project Finance

- **Majority of utility scale renewable projects have been financed with a tax equity model**
- **Tax equity model is a combination of:**
 - **Small amount of sponsor equity,**
 - **Bank debt, and**
 - **Tax equity (monetization of tax credits)**

The Goal of Debt in the Deal

- **Non-recourse debt, meaning the lenders do not have any other collateral except for the assets of the project**
- **Loan repayment is from the project cash flows net of operating and capital expenses**
- **Project cash flows will provide scheduled debt repayment**

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.**

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**

Project Finance Basics

- **Non-recourse debt, meaning the lenders do not have any other collateral except for the assets of the project**
- **Loan repayment is from the project cash flows net of operating and capital expenses**
- **Project cash flows will provide scheduled debt repayment**

The Lender's Perspective vs. Equity

- **Debt providers (banks and bond holders) provide more affordable capital but want little or no risk**
- **Lenders look for contracts that shift risk to someone with a deeper pocket and risk appetite (e.g., utility)**
- **Equity providers, by contrast, take the greatest risks but get compensated by getting all the cash available after paying project costs and debt**

Renewable Energy Project Finance

- **Majority of renewable projects have been financed with a tax equity model**
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Effects of the Macro Economy on Projects

- **Dramatic reduction in large tax equity investors**
- **Banks prioritizing financing requests**
- **Terms have returned to conservative**
 - **Long term PPA/PSA's**
 - **Creditworthy counterparties**
 - **Strong EPC contract/parties**
 - **Low technology risk**
- **Strong credit profile is essential**

Economics: Scalable and Flexible Projects

- **Scalability:** projects that can be designed in different sizes, capacities and configurations have a greater chance of capturing a wide range of tax credits and other incentives
- **Flexibility:** projects that offer different and flexible approaches to investor revenues and risks are more bankable

Tribal Energy Legislation Opportunities

- **“Indian Tribal Energy Development and Self-Determination Act Amendments of 2011”**
 - **House Republican staff moving the bill**
 - **Likely to have significant bipartisan support**
 - **Comments and ideas needed now**

Sovereignty

- **Tribes are free to choose the form of governmental or non-governmental organization through which they do business. *Mescalero Apache Tribe v. Jones*, 411 US 145, 157 n 13, 93 SCt 1267 (1973).**
- **As a general rule, state civil laws do not apply to Indians or their affairs within Indian country because either state laws are preempted by federal law, or state laws infringe on Indian self-rule. *White Mountain Apache Tribe v. Bracker*, 448 US 136, 100 SCt 2578, 65 LEd2d 665 (1980).**

The Balancing Act

- **Many business transactions do not rise to a level requiring review and approval by the entire council of a tribe (either elected or general council), but in many instances, the non-tribal party may insist on tribal approval or at least clear lines of authority and support. At most, review and approval of contracts by tribal council may be necessary. In many cases, low-stakes business transactions may be handled entirely by the relevant tribal enterprise.**

However, Tribal Authority Controls

- **A tribe's constitution, treaty, executive order, bylaw or codes are the starting point for understanding the scope of its powers in the business context.**
- **Many tribal constitutions or codes do not spell out the scope of the tribe's authority as applied to particular types of business transactions.**
- **When examining a tribe's constitution the focus should be on express *limitations* on authority rather than on express grants of authority.**

Other Sources of Law

- **When doing business with a particular Indian tribe, it may be important to examine treaties or the specific act of Congress bestowing federal recognition on that tribe. Federal legislation may define the tribe's reservation boundaries, the organization of the tribe, the extent to which state civil jurisdiction applies to the tribe, land use and management issues, and federal rights and privileges, any one of which might have an effect on a particular business transaction.**

Tribal Law Governs

- The power of a subordinate agency, enterprise or corporation is a matter of tribal law. *Navajo Tribe v. Bank of New Mexico*, 700 F2d 1285, 1288 (10th Cir 1993).
- A non-Indian party's claim that it detrimentally relied on a subordinate tribal entity's apparent authority will not save an *ultra vires* contract.

Part of the Tribe, or Not?

- **The enterprise may or may not be a legal entity separate from the tribe. A tribal enterprise which is an integral part of a tribe enjoys all the privileges and immunities of the tribe itself for activities conducted on or off reservation. *Central Machinery Co. v. Arizona Tax Comm.*, 448 US 160, 164 n 3, 100 SCt 2599, 65 LEd2d 684 (1980).**

Distinction between Political Subdivisions

- **In some cases, a tribal authority may constitute a separate political subdivision of the tribe, meaning that the subdivision possesses one of the three commonly recognized attributes of a sovereign: police powers, taxing powers, or eminent domain powers.**

Doing Business With Tribal Government

- **The Tribe**
 - **Many successful ventures have been undertaken directly with the tribe.**
 - **Benefits include sovereign immunity, exemption from income tax, ability to issue tax exempt bonds, direct authority.**
 - **Downside includes exposing tribal assets to liability, delays in approvals due to political processes, lack of experience with business ventures**

Tribal Enterprises or Instrumentalities

- **Still a part of the tribe, but**
 - **Formed by tribal resolution, ordinance or code**
 - **Managed by separate Board of Directors and management staff**
 - **Certain financing options available to the tribe may or may not be available without full tribal approval**
 - **Can incur debt, enter into contracts, be sued without exposing tribe to liability**

Tribal Political Subdivisions

- **Full delegation of sovereign powers to a separate government entity**
- **BIA and IRS confirmation typically required**
- **Exempt from federal income tax, retains sovereign immunity, may issue tax exempt bonds**
- **May be less flexible than a tribal corporate entity, and less attractive to some business partners or investors**

Tribal Corporate Enterprises: Section 17

- **Section 17 of the Indian Reorganization Act (25 USC 477)**
- **Requires tribal resolution, followed by approval of the corporate charter, and BIA ratification of the charter**
- **Must be wholly owned by the tribe, which precludes equity ownership by outside investors**

Tribal Corporate Enterprises: Section 17

- **Assets of the Section 17 corp. may be pledged as collateral**
- **Exempt from federal income tax**
- **May issue tax exempt bonds**
- **Unlike political subdivisions, assets and liabilities are wholly separate from assets and liabilities of the tribe**
- **Can be sued in its corporate form, with tribe retaining sovereign immunity**
- **25 year leasing authority; Section 81 approval of leases/contracts by BIA not required**

Tribally Chartered Corporations

- **Established under tribal law**
- **Separation of corporate assets and liabilities from tribal assets and liabilities**
- **Financing options broad (loans, taxable bond issuances, commercial debt)**
- **Tax status uncertain; may not be able to issue tax exempt debt**

State Chartered Corporations

- **Easy to form**
- **Full separation of assets and liabilities from tribe**
- **Same financing tools as tribal corporations**
- **Subject to federal income tax**
- **Cannot assert sovereign immunity**
- **Subject to state laws and state reporting requirements**

State Chartered Limited Liability Company

- **Easy to form**
- **Full separation of assets and liabilities from tribe**
- **Structure familiar to lenders and potential business partners**
- **LLC members achieve tax benefits of a pass through entity**
- **No sovereign immunity**
- **May not issue tax exempt debt**

Choosing an Entity for Joint Development

- **Most common types of entities for creating a joint venture between a tribe and a non-tribal business partner include:**
 - **Corporation**
 - **Limited Liability Company**
 - **Partnership**

Corporation as a Joint Venture Entity

- **Corporate owners enjoy complete protection from personal liability for the activities of the corporation.**
- **Unless a wholly-owned Section 17 or wholly-owned tribal corporation, the corp. is subject to federal income tax.**
- **Non-tribal owners may also be required to pay income taxes on any income received from the corp in the form of dividends or distributions.**

Partnership as a Joint Venture Entity

- **General and limited partnerships**
- **Both types enjoy the same tax status:**
 - **Partnership not directly subject to federal income tax**
 - **Each partner reports its share of the partnership's income or losses as part of its own annual income or losses (“flow-through” taxation)**
 - **IRS clear that tribal partners not subject to federal income tax**

LLC as a Joint Venture Entity

- **Most common between tribes and non-tribal businesses because it combines the limited personal liability of corporate status with the pass through tax feature of partnerships.**
- **Does not have the attributes of the tribe (e.g., sovereign immunity) and cannot issue tax exempt debt.**
- **Tribal participation may make certain types of federal tax credits and depreciation benefits difficult or prohibited.**

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**

Many Responsibilities of the project company...

- **Initial project design and layout**
- **Regulatory and permitting analysis**
- **Negotiation of key agreements (e.g., land, water, fuel supply, offtake, interconnection and transmission, EPC, financing, shareholders)**
- **Market analysis for power sales**
- **Selection and management of advisors, EPC contractors**
- **Community and government relations**
- **Finance (projections, debt, investors, etc.)**
- **Operation and maintenance plans and budgets**

Joint Venture Process

- **Usually begins with a non-binding Letter of Intent (LOI) 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.**

The Term Sheet

- **Could be in the form of an MOU, an MOA, or even in the LOI**
- **This is where you should reach consensus on major issues**
- **You will have a much better idea who your potential partner is, and whether the deal is right for the tribe, upon completion of the term sheet**
- **Don't be afraid of detail here; but make the parties expectations clear on whether the terms are concepts or precise contract language**

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**

Other Critical Issues

- **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**

Preconstruction Development Budgets

- **Recovery of tribe's expenses prior to execution of development agreement**
 - **Upon execution or financial close, or both**
- **Internal costs (personnel and overhead), third party costs, fees, litigation expenses**
- **Flexible mechanisms to update and revise the budget**
- **Earned fees and success fees**

Hammer this out up front or it will be trouble down the road...

Ownership of Assets and Work Product

- **Data, studies, reports, analyses**
- **Typically property of the project company or if contributed by one party, held in trust for the company until certain conditions met (e.g., payments, milestones, etc.)**
- **Disclosure to third parties restricted?**
- **Ownership upon termination**

Equity Participation

- **Ownership of the project and ownership of the project company should be clarified**
 - **Some parties may seek to participate as equity partners in the project without an ownership share of the company**
 - **Some parties propose different structures before and after financial closing**
- **The equity rights of the tribe should be clear and specific**
- **Rights to sell, add partners, in-kind contributions, carried equity**

The Minority Shareholder Position

- **Retain rights to approve certain matters, such as sale of the project, admission of additional partners, or dissolution of the joint venture**
- **Right to participate in issuance of additional equity interests**
- **Caps on required contributions**
- **Rights to participate in material decisions**
- **Contributions in kind**

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)**

Leasing and Rights of Way 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 and rights of way 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.**
- **Support new federal legislation.....**

Select Features of Lease & ROW 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**

Ideas for Next Steps

- **Establish a Tribal Energy Entity**
- **Find a project to start that has some elements in place: success begets success**
- **Consider a “Request for Qualifications” or RFQ process to interview companies, technologies and project proposals**
- **Get commitments in writing**
- **Build on the great relationships already established**

For More Information

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