Association of Corporate Counsel

June 20, 2011

QuickCounsel

sponsored by MANKO | GOLD | KATCHER | FOX LLP
AN ENVIRONMENTAL AND ENERGY LAW PRACTICE

RENEWABLE ENERGY: WHAT EVERY GENERAL COUNSEL NEEDS TO KNOW

By Brenda Hustis Gotanda, Dan Reiter and Brett Slensky, Manko, Gold, Katcher & Fox, LLP

Introduction

Energy policies at the federal level and around the nation are undergoing a radical transformation as demand grows at a rapid pace for clean, renewable energy generated from sustainable sources, including solar, wind, and geothermal. This growth in demand is driven in part by a mix of regulatory requirements, government incentives, and voluntary sustainability initiatives adopted in both the public and private sectors.

Whether a client is interested in generating, using, purchasing or selling renewable energy, it is critical for corporate general counsel to understand the broad array of environmental, regulatory, and transactional legal issues raised in the renewable energy context so as to be able to guide the client through the process in a manner that maximizes potential opportunities while avoiding potential pitfalls. While different types of renewable energy present issues unique to the generation technology, there are also many issues in common across technologies. This article highlights several of the macro-level legal issues common to many renewable energy technologies, and which may have significant impacts on project outcomes and client goals.

Structure of the Transaction

The first key issue in any renewable energy transaction is to determine the client's renewable energy goals and assist the client in selecting and creating an appropriate transactional structure to meet those goals. Typical structures to consider may include:

(1) A power purchase agreement ("PPA"), pursuant to which the client purchases renewable power from a third-party-owned generation facility (such as a third-party owned solar energy system located on the client's roof or from a local wind farm);

(2) Ownership of the generation infrastructure, where the client purchases, owns and maintains its own energy generation facilities (such as wind turbines or a solar energy system) and uses the generated electricity for its power needs; or

(3) Leasing arrangements, essentially equivalent to a financing alternative to the ownership option described in (2) above.

- more -

The most appropriate transaction structure for a particular client will generally depend upon the client's energy goals, access to capital, ability to realize the benefits of available financial and tax incentives, and the client's ability or willingness to operate and maintain energy generation equipment. Counsel should discuss with the client the various benefits, burdens, and risks of available structural alternatives and assist the client in selecting and structuring the transaction, including the drafting of legal contracts to implement the project.

Financial Incentives

In today's market, the economic strength of many renewable energy projects is keyed to the ability to obtain tax or other financial incentives. In the renewables sector, some of the most widely-used incentives include:

(i) The federal investment tax credit ("ITC"), which provides qualifying entities with a tax credit equal to 30 percent of the eligible costs of certain renewable energy equipment (e.g., a solar energy system), and

(ii) The grant-in-lieu of ITC, which is an up-front cash grant available from the U.S. Treasury Department in place of the ITC for qualifying equipment purchasers.

Both the ITC and the grant-in-lieu are subject to various rules and guidelines, which counsel should review to help interested clients understand and obtain these incentives. In addition, many states offer grants, rebates, and/or attractive loan programs for qualifying energy projects. The U.S. Environmental Protection Agency (EPA) also offers assistance through programs such as its Re-Powering America's Land initiative, which provides financial and technical assistance to those seeking to use contaminated sites for renewable energy development. Often, a combination of incentives may be used to increase the economic returns on renewable energy projects. Counsel should ensure that client applications for incentives comply with all applicable requirements and are filed timely, and that renewable energy projects themselves comply with all applicable eligibility requirements.

Siting and Permitting

Success in renewable energy projects is often highly dependant upon identifying and securing the use of a suitable installation site for the energy generation equipment. Whether the site is located on a rooftop (roof-mount) as with many solar energy systems, open parcels of land (ground-mount), or parking lot canopies designed to support energy generation equipment, legal issues concerning site selection, zoning and permitting will almost surely come into play.

With roof-mount equipment, some key considerations that should be addressed in the pertinent legal agreements may include the condition of the roof, weight-bearing load limits, impacts on roof warranty, roof pitch, wind conditions, and accessibility for maintenance. With a ground-mount system, key considerations may include environmentally-sensitive areas or land use restrictions, such as the presence of wetlands, floodplains, conservation areas, endangered species habitat, contamination, landfill or soil caps, or other engineering or institutional controls. Parking canopy-mount systems present a hybrid of all of the above, since the canopies themselves are ground mounted while the roofs of the canopies are used for the actual installations.

- more -

In all cases, it is important to ensure that a project can be constructed in compliance with all applicable environmental, land use, and zoning requirements and that all necessary permits to construct and operate the generation equipment can be timely obtained. The availability of liability protections from environmental regulatory agencies may also need to be assessed. In addition, it may be necessary to secure leases, easements, and other access rights when an energy project is hosted on a third-party's property.

Energy Regulation

As with conventional energy, the renewable energy sector is highly regulated at the federal, state and local levels. Inherent in all energy projects are questions such as: at what point does the owner of electricity generation equipment become a regulated utility? To whom can such an owner sell power? Are any compliance filings, disclosures or other documentation required in connection with a given energy project? These questions can be jurisdiction-specific and it is important for corporate general counsel to evaluate and resolve these and other similar regulatory questions up front. Likewise, the process of physically interconnecting electricity generation equipment with an energy customer's electrical infrastructure or the applicable electricity grid operated by a regional transmission organization ("RTO") can be highly regulated and the parties involved must understand the applicable regulatory framework, RTO interconnection rules, and requirements of the local public utility.

Renewable Energy Credits

State Renewable Energy Portfolio Standards ("RPS") have significantly driven the recent development and growth of renewable energy generation capacity across the country. Many state compliance schemes are based on renewable energy credits ("RECs"). RECs are environmental "credits" that evidence the generation of clean, renewable energy by voluntary market participants, and which are typically sold to regulated load-serving entities (e.g., utility companies) that need to generate a specified percentage of their power from renewable sources pursuant to their state's RPS. RPS compliance is typically satisfied through ownership of RECs to evidence the required amount of renewable generation.
Thus, it is the REC, and the price a seller may obtain for this commodity-like credit, that has in large part dictated the success of state efforts to promote the use of renewable energy resources as part of a state's energy mix.

Various state REC-related rules and regulations—such as a requirement that all RECs used for RPS compliance purposes within a given state be generated within such state as opposed to accepting out-of-state RECs for compliance purposes—as well as general market dynamics such as the classic interplay between supply and demand, affect REC pricing and therefore impact a given market's success. Currently the most well known and valuable REC is the solar renewable energy certificate ("SREC"), a type of REC created through solar generation, although RECs are generally available to evidence the generation of energy from a broad array of renewable resources. Often a key component of renewable and alternative energy development is the ability of a project to generate RECs, the sale of which can secure a significant revenue stream. Likewise, if intending to use a REC for purposes of meeting above-code programs such as for LEED-certified green building projects, it will be important to ensure compliance with those program requirements. As with all commodities, monetizing REC values can require both business and legal expertise.

- more -

Identification, Assessment and Allocation of Risk

An inherent component of any renewable or alternative energy transaction is risk, both operational and regulatory. Generation equipment owners rely on their equipment's performance, yet a variety of factors, such as component or installation defects, shade from neighboring buildings or foliage, or even severe weather, may adversely impact performance. A generation system's failure to perform as predicted can have significant economic impacts, and anticipated cost savings for the power consumer, and profits for the power producer, can quickly vanish. In addition, if the regulatory programs or incentives fueling a given REC market are modified or revoked, any assumed financial benefits may not be realized. Energy market participants cannot wholly eliminate these and other types of operational and regulatory risk, however informed parties can and should identify and evaluate such risks, allocate them accordingly as between the interested parties through carefully drafted and negotiated project documentation, and underwrite deal pricing accordingly.

Conclusion & General Recommendations

Overall, numerous external factors may affect renewable energy projects at some point in the lifecycle of the transaction or project. Counsel should assist clients by staying up to date on marketplace, legislative and regulatory developments, and as relevant factors evolve, counsel should consult with their clients on any potential impacts to their existing and future energy projects. Aided by such ongoing diligence, counsel can help clients make informed predictions regarding the renewable energy markets and tailor their involvement accordingly to maximize the chances of economic and environmental success.

ACC Resources

- ACC Compliance Training Portal (2011): FERC Standards of Conduct
- ACC Leading Practices Profile (2011): Leading Green Practices in Sustainability Compliance and Marketing: How Companies Embrace Environmental Responsibility
- ACC QuickCounsel (2010): FERC Enforcement and Compliance
- ACC InfoPAK (2010): FERC 101: An In-House Lawyer's Guide
- Presentation (2010): Where Do I Start? Environmental Permitting and Reporting for the Non-Specialist
- ACC/MGKF Green-house Counsel (2010): Learn About "Green" Projects for Which Funding Through Energy and Environmental Programs May Be Available

Sponsors Resources

- Fueled by the Sun: 10 Sizzling Legal Issues in Solar Energy Projects (2011)
- 2011 Regulatory Guidance and Policy Initiatives Expected to be a Positive Impact on Development (2011)
- U.S. Treasury Grant in Lieu of Tax Credit Program Extended Until December 31, 2011 (2011)
- Wind Power Projects, Nuisance Claims and Right-to-Farm (2010)
- Financial Incentives for Installing and Maintaining Solar Photovoltaic (PV) Systems (2009)
- Solar Power: The Long-Term Advantage (2008)

- more -

Other Resources

- Flett Exchange (2011)
- SRECTrade (2011)
- Regional Transmission Organizations, FERC (2011)