

# Renewable Energy Financing Incentives

By Fred M. Greguras, partner, K&L Gates

**P**assage of the American Recovery and Reinvestment Act of 2009 paves the way for significant additional funding by the Department of Energy (DOE) to be deployed to start-ups and early stage companies for research, development, demonstration and early deployment of new technologies in the renewable energy field that still have risk in commercialization. Given the current angel and venture capital funding environment, these grants may be the only source of funds for many early stage companies. Such funding can be used to get them through the “chasm” to reach the next validation milestone for investment.

Some of the funding under the Act was specifically allocated for renewable energy activities. Other funding decisions were delegated to DOE or the states. The following is a partial list of earmarked funding under the Act:

- \$2.5 billion for applied research and development activities relating to renewable energy and energy efficiency to be administered by the DOE Office of Energy Efficiency and Renewable Energy, including \$800 million for biomass projects and \$400 million for geothermal projects.
- \$2.0 billion for energy R&D programs at the DOE Office of Science, including the National Renewable Energy Laboratory and other national laboratories. This appropriation includes \$400 million for the Advanced Research Projects Agency.
- \$3.4 billion for the DOE Office of Fossil Energy Research and Development Program, including \$1 billion for fossil energy R&D programs, \$800 million for the Clean Coal Power Initiative and \$1.52 billion for carbon capture and generation efficiency improvement project grants.
- \$4.5 billion for the DOE Office of Electricity Delivery and Reliability for activities related to modernizing the electrical grid.
- \$3.2 billion for the Energy Efficiency and Conservation Block Grant program.
- \$3.1 billion for state energy programs.
- \$2.0 billion for the Advanced Battery Manufacturing grant program to support the manufacture of advanced batteries for hybrids, plug-in hybrids and electric vehicles. This program includes funding for the development of batteries for larger vehicles or devices that have a longer life without recharging and are more robust in difficult environments.

The key issue is whether the grant application and decision-making process will be simplified and shortened so as to make such funds available quickly. We recommend that grant applicants try to convince the funding source that the results of the project could be “game changing” in order to have a competitive advantage over other applicants. Later, we offer a project summary outline which can be used for both early stage and project finance proposals.

In an effort to attract both debt and equity investors back into

the marketplace, the Act provides various incentives for commercial (such as power purchase agreement financings) and private utility project finance. These incentives are discussed below.

*Department of Treasury Grants in Lieu of Renewable Energy Tax Credits.* The current situation in the capital markets has significantly undermined the effectiveness of the production tax credits (PTCs) for electricity produced by certain energy facilities and the investment tax credits (ITCs) for certain energy generating property. The Act attempts to remedy the status quo by providing a set of more beneficial tax provisions for the remaining investors and creating a new program administered by the Department of Treasury that provides grants equal to 30 percent (or 10 percent for combined heat and power or qualified microturbines) of the cost of “qualified facilities” or energy property in lieu of PTCs and ITCs. Qualified facilities eligible for the 30 percent grant include wind, closed- and open-loop biomass, hydropower, municipal solid waste, solar, landfill gas, geothermal, qualified small wind and qualified fuel cell.

In order to qualify for the grant, the facility must be placed in service during 2009 or 2010, or the facility’s construction must commence in 2009 or 2010 and must be completed before the “credit termination date” (which ranges from Jan. 1, 2013 to Jan. 1, 2014 depending on the type of the facility). Treasury is required to make payment of the grant within 60 days of the facility’s being placed in service or, if later, within 60 days of Treasury’s receipt of an application for such grant.

The result of this incentive is to make the ITC refundable for qualifying renewable energy facilities. This incentive is intended to help reduce financing risks by providing the full value of the incentives for renewable energy projects even during the financial crisis. It is anticipated that the grants will provide similar near-term benefits as the ITCs and help reinvigorate the hard hit manufacturing and construction sectors.

*Bonus Depreciation.* The Act extends first-year bonus depreciation for capital expenditures related to property placed in service in the United States in 2009; for example, an owner of qualifying property placed in service in 2009 may deduct 50 percent of the cost of such property (or a reduced percentage if an owner also elects the ITC). The remaining 50 percent would be depreciated over the regular tax depreciation schedule for subsequent years.

*Full Amount of Investment Tax Credit Available Even if Subsidies Used.* The Act also permits the use of the full amount of the ITC even if projects receive subsidized financing (such as below-market-interest loans, state grants, and so on) and allows the full 30 percent credit for small wind generators. In addition, equipment used to manufacture renewable energy components and systems is now eligible for the ITC and accelerated depreciation.

*Investment Tax Credit in Lieu of Production Tax Credit.* Renewable energy facilities that qualify for the PTC may apply the 30 percent ITC instead for facilities placed in service in 2009 or

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2010. This will enable wind power generation project developers to temporarily claim the up-front ITC instead of the PTC, which must be used over 10 years, and thereby help such projects attract financing during the credit crunch. The Act also provides an extension of the energy PTC through Dec. 31, 2012.

**DOE Temporary Loan Guarantee Program.** A new DOE temporary loan guarantee program was established by the new Section 1705 of the Energy Policy Act of 2005 for renewable energy systems (which includes biofuel projects and renewable energy manufacturing facilities) and electric power transmission projects. The underlying purpose was to spur the rapid deployment of renewable energy projects. The DOE is looking for projects that meet reliability needs and have a positive effect on a state's or region's environment and energy needs. Congress appropriated \$6 billion to pay the credit subsidy costs, which should support \$60 billion worth of loan guarantees.

Eligible projects must generate electricity or thermal energy or manufacture related components and commence construction by Sept. 30, 2011. The new program is available for projects that deploy proven technologies as well as leading-edge biofuel projects that use technologies performing at pilot or demonstration scale. Its value as an incentive will depend on the speed and practicality of its implementation by DOE.

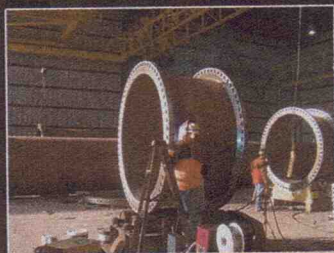
This provision eliminates the significant burdens that had been placed on applicants under the pre-existing DOE loan guarantee

programs. No loan guarantees have been issued under the pre-existing DOE loan guarantee programs as described in Title XVII of the Energy Policy Act of 2005 and at 10 C.F.R. part 609, Loan Guarantees for Projects that Employ Innovative Technologies. Such programs may be used only for projects that employ new or significantly improved technologies as compared to technologies in service at the time the guarantee is issued and there must be a reasonable assurance of repayment of the loan.

In addition, the applicant must pay a credit subsidy fee to create a bad debt reserve to cover the credit risk cost since Congress did not appropriate any funds to support the program. The pre-existing programs are not available for proven technologies and thus do not support projects that involve relatively low risk and have a reasonable assurance of repayment. The existing programs are too slow, too expensive for applicants and too restrictive.

DOE Secretary Steven Chu has promised to reform the DOE and speed up the loan guarantee process. He has committed to streamline the review process and give less scrutiny to each loan guarantee. He expects to start issuing loan guarantees within five months from the date the Act was enacted. Secretary Chu also wants the DOE to spend more than half the appropriation money in the first year.

To have a real impact on financing projects and creating jobs, the new federal loan guarantee program as implemented should have a rolling application process, a streamlined process for making



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decisions on applications and be available for packages of identified, commercial projects in the aggregate amount of at least \$25 million, rather than only for single utility scale projects.

### Strategy for Grants, Guarantees and Funding

The first step in the funding process is to submit a proposal summary to the manager in charge of the funding program and to follow up with a call for initial feedback to confirm the project fits within the program. "Shovel ready" projects (that is, projects that can be started within 90 days) will initially have the highest priority because they will create jobs quickly. The proposal summary needs to address the following business points:

#### Proposal Summary Points

##### Problem and Solution

- What is the problem the project will solve and how will the project solve it? For example, the problem is carbon emissions and the project, the installation and operation of solar energy facilities, will reduce carbon emissions in the case of a request for a federal loan guarantee for a Power Purchase Agreement (PPA) financing.

##### Number of Jobs Created and Speed in Doing So

- Types and number of jobs to be created. For example, solar facility installers who can be trained in entry-level jobs and working on funded projects within 90 days.
- How fast can the jobs be created? For example, for a project to be "shovel ready" all major regulatory approvals must have

been obtained so the project can begin within 90 days.

#### Plan of Action to Carry Out the Project

- Describe how the project will be executed. This point needs to persuade the program manager that a successful outcome is probable as to job creation, project results and staying within the budget.
- What is your "unfair" competitive advantage over others who may propose to do the same type of project? Is it your scientific team, access to certain technology, track record in successfully completing similar projects and so on?

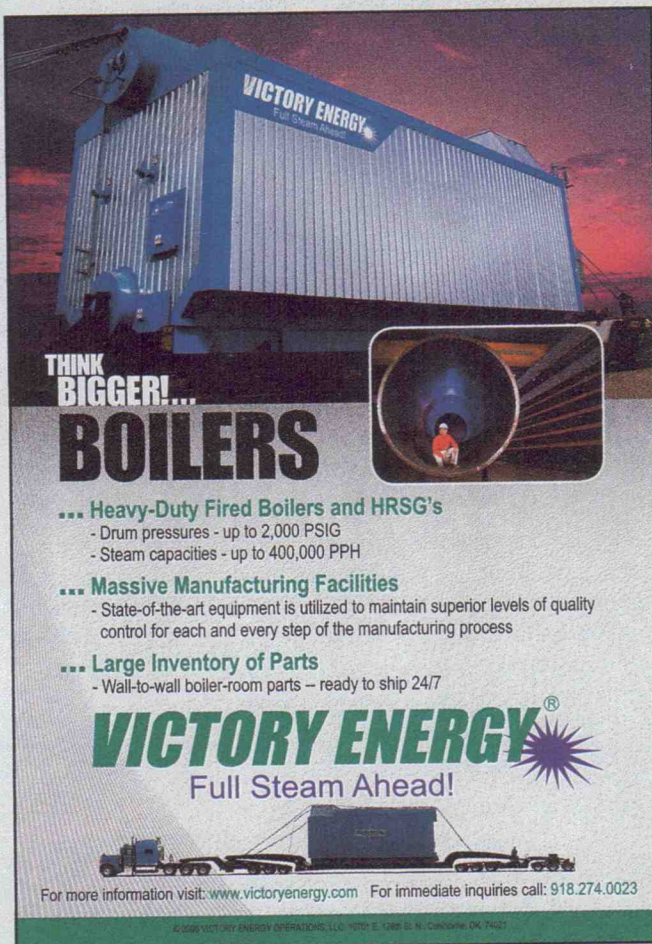
#### Management and Scientific Team

- Why is your team the best team to carry out this project?
- Can the team execute through the project completion stage?
- The team's prior track record can be persuasive in convincing a program manager that the team can achieve success.

#### Project Management Plan

- This includes the financial plan for the project.
- Justify the amount requested. Why is your proposal the "best financial value" for the funding source?
- Specify the schedule for completion with measurable progress milestones.
- Clearly identify the deliverables. **pe**

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