



North American Renewables - Deal of the Year 2007

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Noble NY Wind: Highly co-ordinated

Financing activity in North American renewables reached a heightened pitch in 2007. The previous year featured small, simple financings for established developers. But the last 12 months were marked by increased overseas interest in US wind, more innovative tax structuring and the return of some of the larger sponsors to market.

The year's best renewables financing came not from a large sponsor, nor one of the Iberian utilities making big purchases in the US. The sponsor, Noble Environmental Power, is a JP Morgan Partners-backed developer headquartered in Connecticut that has been operational since 2005. Noble's upper management is liberally stocked with former project finance bankers, and the financing it assembled for its NY wind portfolio demonstrates a keen awareness of banks' soft spots.

It put together an energy hedge, tax-exempt financing arrangements, and a tax equity structure that advance standard market practice, and allow Noble to reap a greater benefit from potential increases in power prices in the region while providing some comfort to lenders. Several developers introduced advances in hedging, technology, and tax structuring in 2006, but few fused them as well as Noble.

Noble, which has no relation with Noble Energy, Noble Group, or Noble Power Assets, has decided from the start to use project-level debt on its farms. This approach recognises that for all the work that sponsors have done compressing yields on tax equity, project debt is still normally cheaper. The three projects are Noble's first, and it decided to finance them in a single process.

The assets are the 100.5MW Noble Clinton Windpark, the 81MW Noble Ellenburg Windpark, and the 100.5MW Noble Bliss Windpark. Clinton and Ellenburg are located in Clinton County, in the northeast of New York State, close to the town of Plattsburgh, while Bliss is located in Wyoming County, to the northwest. They share operations and maintenance contractors.

The two counties are providing incentives to the two projects in the form of breaks on property taxes. The breaks, structured as payment-in-lieu-of-taxes (PILOT) arrangements, do involve some additional structuring, and necessitated two more sets of lawyers, but offer material reductions in the project's tax burden and therefore operating costs. Under the PILOT structure these taxes have to be paid before senior bank lenders, but the sums involved are small enough not to disquiet debt providers.

In May 2006, Noble mandated Dexia Credit Local and HSH-Nordbank to provide the construction and term financing for the three plants. At the same time it lined up GE Energy Financial Services to provide tax equity. The debt and tax equity, together with some sponsor equity, would refinance the hedge fund that refinanced a turbine supply loan for the farms from HVB (now Unicredit).

The tax equity structure for the project is unusual since not only is it levered, or contributed alongside term debt, but it uses a pay-as-you-go (PAYG) structure. Under PAYG, the tax equity provider contributes a lump sum to the project at completion, and then makes additional contributions to the project for a subsequent period. This arrangement allows GE, with its large tax capacity, to receive the production credits to which the project is entitled if it produces electricity, but which Noble and its sponsors cannot use.

The arrangement is not unprecedented, but it is complex, since GE must be held to its commitments, and the sponsor and arrangers must be able to replace it if it defaults on its payments, while keeping the structure intact. Such a degree of coordination between lenders, sponsor and tax equity is difficult to maintain, and explains why GE was selected at such an early stage.

These three participants had to share control of the asset with a fourth party – the energy hedge provider. Financial hedges for wind used to be an exotic niche product, and their providers demanded an enhanced security interest over the assets to which they offered protection. But such hedges were essential to operating in deregulated markets in the northeastern US.

In the last 18 months, though, competition between providers has increased, and terms have become much more competitive. Credit Suisse energy, for instance, won the competition to provide a hedge of 78% of the P50 output of the project, or that that could be expected to happen with 50% certainty, over 10 years. Credit Suisse accepted an unprecedented second lien security interest over the assets. It also allowed the sponsor to use a tracking account mechanism, whereby the projects could fall behind on production commitments provided they made these up within a set period.

The deal took nearly a year to close, while the sponsor negotiated with the large number of landowners involved with the project, and gained the necessary permits. The two banks closed the deal on June 2007, launched syndication in early September, and closed it in mid-October.

The financing consists of a construction loan of \$485 million and sponsor equity of \$85 million. Following completion, the construction debt will reduce by \$210 million, convert to a ten-year term loan, and GE's PAYG contributions will be equivalent to up to a third of project revenue. The loan priced at 125bp over Libor, a generous level by the standards of early that year, but much closer to market reality in early 2008.

Such pricing suggests that banks and the PAYG structure can still be competitive with tax equity only deals. However, the US Internal Revenue Service is considering rule changes that threaten to crimp the attractiveness of the structure. Noble NY could be the apex of this financing type.

Noble Environmental Power	
Status:	Closed 22 June 2007
Size:	\$561 million
Location:	New York State
Description:	Portfolio financing for 282 MW wind portfolio
Sponsor:	Noble Environmental Power
Equity:	\$85 million
Debt:	Construction debt of \$485 million, to be refinanced with term debt and tax equity
Mandated lead arrangers:	Dexia Credit Local and HSH Nordbank
Tax equity:	\$210 million
Tax equity provider:	GE Energy Financial Services
Hedge provider:	Credit Suisse
Borrower legal counsel:	Latham & Watkins
Lender legal counsel:	Chadbourne & Parke
Hedge provider legal counsel:	Milbank Tweed Hadley & McCloy
Tax equity legal:	Bingham McCutchen and McKee Nelson
Legal adviser to PILOT authorities:	Hodgson Russ (Clinton County) and Dadd & Nelson (Wyoming County)
Financial adviser to the sponsor:	CP Energy
Independent engineer:	Garrad Hassan
Insurance consultant:	Moore-McNeil
Turbine surveyor:	Germanischer Lloyd