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A wide variety of timely topics will be addressed during this Seminar, including the provisions of the new energy legislation signed into law by President Bush on December 19, 2007. There are, however, issues of special importance to the Pacific Northwest that deserve comment. One of these issues is how current financial conditions will affect the funding of new renewable energy projects to be built to both meet both state Renewable Portfolio Standards and to supplement BPA allocations to preference customers under the Regional Dialogue Power Sales Agreements to be executed later this year.

I. Factors Driving Renewable Resource Development in the Pacific Northwest

There are several factors that will be driving resource development in the Pacific Northwest in the next decade. The first is the passage of Renewable Portfolio Standards (“RPS”) in Oregon and Washington. Washington’s Initiative 937 requires utilities to use eligible renewable resources to serve at least 3% of their retail load by January 1, 2012, at least 9% by 2016 and at least 15% by 2020. Utilities can comply with these targets in four ways: (1) purchase of power generated with renewable resources, (2) purchase of renewable energy credits, (3) purchase of a combination of renewable power purchases and energy credit purchases or (4) invest four percent of its total annual retail revenue requirement in renewable energy credits or in the incremental costs of eligible renewable resources. Eligible power must be produced by water, wind, solar, geothermal, tidal, landfill or sewage treatment gases, certain biodiesel fuels, and certain biomass sources.

Oregon’s RPS, Senate Bill 838, was signed into law in June 2007. The Oregon RPS seeks to achieve the same goals as Initiative 937, but is structured in a slightly different way. The targets an Oregon utility is required to meet depends upon the size of its retail load. For utilities serving three percent or more of Oregon’s retail load, 5% of their retail load must be served by renewable power starting in 2011. This percentage increases to 15% in 2015, 20% in 2020 and 25% in 2025. Utilities that serve between 1.5% and 3% of Oregon’s retail load must serve 10% of their retail load with renewable power by 2025 and all other utilities must serve 5% of their retail load with renewable power by 2025. Eligible power sources include wind, solar, geothermal, tidal, certain biomass, and certain hydroelectric sources. Ineligible sources include most hydropower, fossil fuels, nuclear power, municipal solid waste incineration, and “green electricity” voluntarily purchased by retail customers.
The second force that will drive resource development in the next decade is Bonneville’s decision to cap preference customer’s entitlement to cost-based power at a predetermined “High Water Mark” (“HWM”). Preference customers with retail load above this HWM will either have to (1) obtain this power from Bonneville at a higher rate or (2) pursue their own generation or contract resources.

II. Public-Private Financing of Renewable Resources

There are two competing trends that will influence the cost and availability of financing for renewable energy projects. The first trend stems from the general financial climate in the United States. A number of the projects that would probably have been privately funded prior to the onset of the mortgage and general credit crisis will now have a significantly more difficult time obtaining access to construction funding. The second trend is that, while traditional venture capital markets may be more difficult to access, financial institutions of all types, as well as Congress and state legislatures, continue to demonstrate support for the construction of renewable resources.

These two trends are creating a new model of public-private resource financing. As traditional private financing becomes harder to obtain, joint development efforts by public and private entities will increase due to the availability of public financing to supplement or replace private funding.

The public-private finance and development model is not a new phenomenon, but the Pacific Northwest has been the trendsetter. Congress, state legislatures and courts in the Pacific Northwest have set up, and authorized, institutions and arrangements that make public-private development possible. Beginning with the Trojan Nuclear Project and continuing with other facilities that were jointly developed and operated, many generation projects are operating to the benefit of regional consumers. Although some of these generation projects have failed, or produced less than favorable results, state legislatures in Oregon and Washington have not abandoned the public-private model. Rather, they responded to these failures by enacting laws that limit the authority of public entities to undertake certain substantial projects and commitments under arrangements that indirectly pledge the financial capability of public and cooperative entities in an unlimited and less than adequately controlled arrangement. At the same time, recent changes to Oregon law, for example, have made it easier for many public entities to enter into the arrangements and institutions necessary for renewable resource project development.

As this finance and development model gains popularity, public entities should be prepared to pursue renewable projects as these opportunities arise. The following principles can help public entities assess whether a resource financing and development project is worth consideration:

1. In assessing the viability of a project, and before exploring financing alternatives, a simple analysis should be undertaken to determine whether the project revenues will provide at least 1.5 times debt service
coverage. In making this determination, it is important to have the monetary inputs and outputs determined under fixed, or at least formulated, returns and prices.

2. Project developers must carefully examine whether tax credits or grants can be obtained to lower the overall capital costs of the project. If the net capital cost of a project can be lowered though tax credits and grant monies, there is a higher probability that favorable debt service coverage ratios can be demonstrated and the interest rates, public or private, lowered.

3. If fuel is required to produce electricity, fuel contracts that fix the price of the fuel and guarantee the delivery of sufficient fuel may be required to obtain financing. The terms and conditions of fuel supply contracts will also affect interest rates.

4. Any commitment to interim financing will require the execution of a development agreement that sets forth the actions that must be taken to obtain permanent financing and establishes a schedule for the interim financing entity or partner to provide a flow of funds.

5. Ownership and equity interest determinations also need to be made prior to negotiation of development agreements. Without serious attention to this determination, the ultimate financing of a project could result in financing entities being accorded most of the ultimate returns on the project to the detriment of the individuals and entities that created the opportunity.