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Pitfalls Still Lurk For Project Developers Seeking Grants

By **Ryan Davis**

Law360, New York (January 18, 2012, 6:04 PM ET) -- The rush to launch renewable energy projects in time to meet a Dec. 31 deadline for a federal government cash grant program is over, but applicants seeking the funds aren't out of the woods yet, attorneys say.

Projects started by the deadline could still be disqualified from receiving the grant — which is not paid until the project is completed — if developers fail to comply with Treasury Department regulations regarding project ownership and costs. That leaves a lot of room for potential problems to creep into the picture, attorneys said.

In order to qualify for the so-called Section 1603 Cash Grant Program, which will cover 30 percent of the cost of a renewable energy project, developers either needed to have started construction by the end of last year or have paid or incurred 5 percent of the total cost of the project. Established in the 2009 stimulus bill, the program has expired and faces uncertain prospects for renewal.

The haste to meet the year-end deadline could lead to problems down the road, attorneys said.

"I'm hopeful that most people did it right, but when when people are trying to do something very quickly to meet the deadline and they haven't done it before, mistakes get made," said John Eliason of Foley & Lardner LLP.

Hitting Completion Deadlines

One problem that could throw a financing bid off track is a failure to meet certain progress and completion deadlines established by the Treasury Department.

Wind projects face an especially tight time frame, since they need to be up and running before the end of the year, while biomass and hydropower projects have until the end of 2013 and solar and geothermal projects have until the end of 2016.

Work also must continue uninterrupted in order to maintain grant eligibility, if the developers have sought that financing.

While the Treasury could be understanding if severe weather or other unforeseen events impede construction, long delays generally could put grant eligibility in jeopardy, attorneys said.

“It’s not enough to start in 2011 and then put the project on the shelf for two years,” Eliason said.

Project developers may also maintain grant eligibility if they have incurred at least 5 percent of the project costs by the end of 2011, per so-called “safe harbor” provisions.

But the determination of whether that threshold was met is up to the Treasury Department, and will be based on the actual final cost of the project, not the developer’s estimates at an early stage in the process, attorneys said.

Because of that, attorneys have advised clients applying for the grant to have spent in excess of the 5 percent threshold by the deadline, just to be on the safe side, said Adam Wade of Foley Hoag LLP.

If it becomes apparent during construction that the project will end up costing significantly more than anticipated, developers may need to scale back the size of the project in order to ensure that it remains eligible for the grant, Eliason said.

“Being conscious of the cost is probably the most important thing you need to think about,” he said.

Watching Out For Ownership Changes

Changes in ownership in a project represent another potential pitfall for ensuring grant eligibility. The Treasury Department has indicated that some types of transactions may disqualify a project entirely.

In a notice issued last year, Treasury said that if an applicant relying on the 5 percent rule sells the facility to an unrelated purchaser after Dec. 31, the buyer may not be eligible for the grant under the safe harbor provision.

That type of deal seems rare, according to Wade, since most developers of renewable energy projects intend to maintain an ongoing ownership interest.

At least two common types of transactions will not run afoul of the 5 percent safe harbor rule, according to Treasury. Sale and leaseback arrangements do allow for some wiggle room. In those situations, the buyer of a property can count the 5 percent for grant eligibility purposes if the property is leased back to the original owner.

Likewise, eligibility may remain intact in a partnership flip transaction, where a partnership interest in a project is sold to a tax equity investor.

As a result of the conditions imposed, caution is a watchword with any transaction involving a renewable energy project under the program, Wade said.

“If you’re planning a deal, look closely at the regulations and discuss with counsel and Treasury how to structure it,” he said.

Making The Grade

While projects were expected to be launched by the end of 2011 to qualify for the grants, the actual applications aren’t due until Oct. 1. Once the government begins evaluating them, it remains to be seen how strict or lenient Treasury will be in determining whether projects measure up.

At this point, Treasury employees overseeing the program have been receptive to corresponding with project advisers about the requirements. That is likely to continue, Eliason said, but the government is expected to stick closely to its written rules.

“My sense is that if you don’t follow the rules, you’re probably not going to get a whole lot of relief,” he said.

--Editing by Kat Laskowski.