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# Project Finance Client Alert

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## U.S. ARMY CORPS OF ENGINEERS SOLICITS \$7 BILLION OF NEW RENEWABLE ENERGY

On August 8, 2012, the U.S. Army Corps of Engineers posted a request for proposals from renewable energy developers to offer the government up to \$7 billion of total contracted energy from new projects for use on U.S. Army installations over a period of 30 years. The government plans to purchase the energy through long-term offtake contracts, and the companies that win those contracts will be responsible for developing, owning, financing, designing, building, operating and maintaining the plants.

John M. McHugh, Secretary of the Army, announced the RFP as a means to further the Army's goal to deploy a gigawatt of renewable energy by 2025. The RFP followed a recent memorandum of understanding agreed between the U.S. Department of the Interior and the U.S. Department of Defense to identify opportunities to develop renewable energy resources on 16 million acres of "withdrawn" public land set aside for defense-related purposes, and to otherwise facilitate renewable energy projects near military installations, including a dedicated partnership for offshore wind.

In the face of ongoing congressional opposition to traditional federal renewable energy incentives, these Department of Defense initiatives represent a unique and present opportunity for developers of renewable energy projects. Of note, the military spent more than \$17 billion on fuel last year, and accounts for 1 percent of all U.S. energy use – making its activity in the alternative energy market something that energy companies and contractors already involved in energy efficiency projects should closely watch.

### How to Qualify

October 5, 2012 is the deadline for developers to submit proposals to be ultimately awarded an "Indefinite Delivery/Indefinite Quantity" (ID/IQ) contract. If qualified at this initial stage, the developer becomes part of a pool of pre-selected companies that then have three years to bid for "task orders" through which the government will contract to purchase energy from specific projects. The Army will

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determine whether developers qualify for an ID/IQ contract based on the following criteria: (i) corporate technical and management experience in developing, operating and maintaining renewable energy projects and performing PPA obligations, (ii) financial capability to self-finance or obtain third-party financing at competitive rates, (iii) past performance, (iv) small business participation and (v) a reasonable and realistic maximum unit price for the proposed technology.

The RFP, as amended, frequently asked questions, and a link for bidders to submit applications are available at <http://go.usa.gov/Gd6>.

### **Program Details**

Technologies eligible under the RFP include photovoltaic panels and various solar thermal technologies, solar hot water, vertical and horizontal axis wind turbines, geothermal, biomass (including biofuels), and a broad spectrum of other “alternative energy technologies” including ocean power, batteries and micro-grids. Technologies are generally expected to be “commercially ready” – defined as currently deployed in three or more commercial projects in the U.S. that each have been operating for at least five years – but contracting officers will have discretion to accept newer technologies. A new technology’s ability to obtain financing will be a key factor in being specially approved. Consistent with the Army’s energy security rationale for the program, grid-isolation technology is likely to be required so that plants can continue to produce power if the external grid fails.

All projects currently being considered are located on Department of Defense land, but the Army has indicated that projects may be developed on private land as well. The Army will perform National Environmental Policy Act assessments itself when possible, which should streamline development.

In the initial proposals due on October 5, 2012, each offeror must include a maximum price per unit of energy, which is intended to serve as a ceiling in any task order through which the government may later award that offeror a specific power purchase agreement or similar contract (developers with an ID/IQ contract may compete for, and win, multiple task orders). The RFP generally instructs each offeror to base the price in its initial application on the total cost of development, construction, operation and maintenance of a renewable energy power plant at a “suitable”, but not “ideal” (those terms are not further defined), location and size for the proposed technology. Offerors should not include contingency pricing in their bids; interconnection costs, land use fees, environmental compliance and other project-specific costs will be separately priced and evaluated at the task order stage, which may allow for equitable adjustments to price ceilings. While developers will be expected to complete customary site investigations on the ultimate sites for their projects, adjustments for differing or unforeseen site conditions will be made per the applicable provisions of the Federal Acquisition Regulation (FAR).

Task orders for projects that are less than 4 MW will be reserved for small businesses, and preference will be given to small businesses for projects between 4 MW and 12 MW. For projects greater than 12 MW, competition will be unrestricted among bidders.

### **Key Deal Points**

- **Procurement**: The \$7 billion number represents the value of the total contracted energy under the program, not the total project development cost.
- **Financing**: Developers must demonstrate experience in obtaining financing for renewable energy projects at

competitive rates or the ability to self-finance. Not only must the developer demonstrate that it has sufficient capital resources to self-finance or the ability to obtain third party financing, it must also demonstrate its understanding of the financial risks associated with the contract and the ability to recover the investment over the life of the project (which is expected to be no more than 30 years; for the purposes of proposing maximum unit pricing, bidders should assume a 30-year task order period of performance).

- Corporate Structuring & Project Financing Considerations: In a recognition of project financing structures, the RFP stipulates that, in order to establish a special purpose vehicle to receive financing for a project other than the entity that submitted the bid, the government must approve a novation of the applicable contract to the SPV, and it may require a performance guarantee (or satisfactory performance bond) by the original bidder. In order to include parent company experience in a proposal, offerors are required to submit a letter by the parent company guaranteeing contract performance.
- Price: Task orders will be firm fixed-price contracts with fixed escalation rates. Internal regulations allow the Department of Defense to pay a “fair and reasonable” premium for renewable energy, above local utility prices. The contractor will be expected to incorporate available utility rebates and other incentives into its price calculation to offset cost to the government. The contractor may be responsible for determining the source, value, and availability of all applicable financial and tax incentives for the project and shall collaborate with the government to consider incentive options.
- Performance Standards: Contractors are expected to maintain system uptime performance in the top 25% of the applicable technology’s U.S. industry performance, considering site-specific conditions, and sellers may be required to guarantee output, with liquidated damages payable for any shortfall at the monthly average retail rate plus a percentage to account for lost environmental attributes.
- Exclusivity and Renewable Energy Credits (RECs): Larger projects may be allowed to sell excess power to the grid, at a price no lower than that paid by the Army. The Army will determine on a project-by-project basis whether it will retain RECs to meet federal mandates.
- “Most Favored Customer” (MFC) Treatment: Developers must assure the Army of MFC treatment, which prevents the developer from selling energy at a lower price to any other customer with a contract containing substantially similar terms and conditions (if the task order PPA unit price is not lowered to match). This provision is intended to prevent the federal installation which hosts the power production facility from bearing more than its share of cost and thereby subsidizing the cost of renewable energy for other customers.
- End of Term: Each PPA will specify what is to happen to the project and its assets at the end of the term.
- Applicable Laws & Terms: Developers will be required to comply with the Davis-Bacon Act labor standards and the Buy American Act, among other laws and guidelines applicable to military procurement contracts, such as the FAR. The government will also maintain a right to stop construction work if needed, with potential equitable adjustments for stalled contractors.
- Additional Financing Considerations: In order to facilitate typical non-recourse debt financing, the Army may consider including terms to minimize policy uncertainty, such as termination fees payable to the seller in the event of a budget cut, like those featured in multi-year leases that the Army has entered into with real estate companies that supply military housing.

The Army has said that it expects to select its initial pool of eligible bidders by December 2012 and to begin executing contracts for individual projects in 2013.

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