

RENEWABLES AND THE ENERGY POLICY ACT OF 2005

Fair and Balanced?

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Roger Feldman
Partner
Bingham McCutchen, LLP
Washington, DC
r.feldman@bingham.com

OUTLINE

I. FRAMEWORK FOR ANALYSIS

II. ASSESSING THE BALANCE

III. WINNERS AND LOSERS

IV. CONCLUSIONS

I. FRAMEWORK FOR ANALYSIS

The New Accepted Wisdom:

RENEWABLES ARE AN ASSET CLASS WHOSE TIME HAS COME

- Rising oil and natural gas prices
- More sophisticated focus on environmental benefits capture
- Creation of markets through regulatory incentives
- Focus on “Home grown” resources

**BECAUSE WITH THE ENERGY POLICY ACT OF
2005 PRIOR BARRIERS CAN NOW BE OVERCOME**

I. FRAMEWORK FOR ANALYSIS

The New Realities:

- The Energy Policy Act of 2005 Can Make – But Could Break – The Renewables Market
- The Act's Impact Varies Among Renewables' Heterogeneous Resources

I. FRAMEWORK FOR ANALYSIS

A. ASSET CLASS NEEDS

- Financeability – Scale, Costs
- Relative Competitiveness with Traditional Energy Sources
- Market Sustainability

I. FRAMEWORK FOR ANALYSIS

B. AREAS FOR FOCUS OF ANALYSIS

- Industry Structure of Electric Power
- Competitive Playing Field for Fuels
- Technology Development Incentives
- Glaring Omissions

II. ASSESSING THE BALANCE

NEGATIVE FEATURES

- Greater preponderance of incentives toward central station oriented, non-green technologies – clean coal and nuclear power
- Power industry restructuring – giving way to consolidation and vertical re-integration in the power sector
- Distributed energy and conservation solutions are giving way to large scale utility systems solutions
- Trading solutions are receiving reduced attention relative to technology fixes

II. ASSESSING THE BALANCE

POSITIVE FEATURES

- Clear, enlarged renewable fuels, production and special investment tax benefits covering more assets
- Greening and enhancement of the governmental and building and energy efficiency markets
- Emergence and expansion of ethanol and diverse biofuels incentives loan guarantees grants and R&D programs
- New loan guarantee programs for environmental control and certain related renewable technologies as well as IGCC

II. ASSESSING THE BALANCE

PRINCIPAL CONCLUSIONS

1. Industry Structure - Electricity

The effects of the Title VII of the Act (Electricity) will be to provide favored positions in the industry to existing utilities and to large non-industry players, financial and otherwise. Smaller firms dependent on for support on reliance on regulatory market requirements and ability to capture utility financial credit through structured arrangements will be at a marked disadvantage.

II. ASSESSING THE BALANCE

2. Fuels

The fuels of choice in the future will be driven not only by inherent cost of production economics (as handicapped by the applicable capital and operational requirements imposed by environmental law) but also by exploitation of the Act's special incentives provided for two essentially competing complexes of "clean" technologies: "clean" coal and nuclear power on the one hand, and distributed, renewable "clean" technologies (generally of smaller scale) on the other.

II. ASSESSING THE BALANCE

3. Technology Incentives

There are R&D, grant and in some cases loan guarantees and market creation incentives to incent forecast breakthroughs by newer technologies, e.g., fuel cells, hydrogen, biocellulosic ethanol. The traditional gatekeepers (utilities and oil companies/refiners) will continue to occupy a central position in the realization of benefits from these incentives. As the other “home grown” fuel ethanol is the initial beneficiary of substantial recognition through major excise tax and minimum refiner blending purchase requirements. Longer term, significant technology breakthroughs for biocellulose ethanol may result from incentives.

II. ASSESSING THE BALANCE

4. Glaring Omissions – “Green Tag” Creation and Trading

- *Utility Resource Performance Standards (RPS) – Nothing adopted Federally. Application of State programs remain critical for market creation, particularly given competitive playing field uncertainties potentially created by Act.*

II. ASSESSING THE BALANCE

4. Glaring Omissions – “Green Tag” Creation and Trading (cont’d)

- *No Formal Provision for REC Trading Market Creation – Left to State, Regional & RTO markets*
 - *Efforts to standardize markets*
 - *Efforts to structure developer monetizable programs by State agencies*
 - *Capture and trading of carbon credits*
- *Carbon trading market mechanisms not created*

III. WINNERS AND LOSERS

1. Renewables represent a response to certain perceived Energy and Environmental policy issues
2. Renewables ability to benefit from the Energy Policy Act is a function and the extent to which:
 - a) These issues are addressed
 - b) Renewables play a relatively important role in their address
 - c) The incentives renewables receive actually empower them to play the role

III. WINNERS AND LOSERS

DIFFERENT RENEWABLES – DIFFERENT IMPACTS OF ENERGY POLICY ACT

| <u>Energy Policy Drivers</u> | | <u>Principal Beneficiaries</u> | | <u>Key Incentives for Renewables</u> | | <u>Key Competitor</u> | |
|------------------------------|------------------------------------|--------------------------------|---|--------------------------------------|---|-----------------------|---------------------|
| 1) | Liquid Fuels Strategic Security | 1) | Biofuels | 1) | RFS; Tax R&D | 1) | Coal, Nuclear |
| 2) | Natural Gas | 2) | Alternate Power; Biogasification | 2) | PTC; Market Creation R&D | 2) | LNG; Coal |
| 3) | Industry Structure | 3) | Remote Power Sources; Distributed Generation | 3) | Transmission; Market Creation; Federal Lands Exploitation | 3) | Regulated Utilities |

III. WINNERS AND LOSERS

DIFFERENT RENEWABLES – DIFFERENT IMPACTS OF ENERGY POLICY ACT (cont'd)

| <u>Environmental Policy Drivers</u> | | <u>Principal Beneficiaries</u> | | <u>Key Incentives for Renewables</u> | | <u>Key Competitor</u> | |
|-------------------------------------|-----------------------------------|--------------------------------|--|--------------------------------------|---------------------------|-----------------------|---------------|
| 1) | Air Quality – Pollution Reduction | 1) | Biofuels; Alternate Power | 1) | RFS; PTC | 1) | IGCC; Nuclear |
| 2) | Global Warming | 2) | HydroCarbon Fuel Displacement; Pollution Control | 2) | Tax; Land Management; R&D | 2) | Nuclear |
| 3) | Use of Market Mechanisms | 3) | Conservation; Alternate Power | 3) | Market Creation | 3) | R&D Solutions |

IV. CONCLUSION

- While renewables finance for different project resources continues to be diverse, they are linked by common needs to which current market, legal and regulatory forces are now more responsive. Renewables are becoming a true asset class.
- While the Energy Policy Act of 2005 fosters powerful competitors with renewables, in terms of competitor fuels and electric industry structure, it serves to knit together the diverse policy elements of renewable energy law and on balance should favor renewables finance.

ROGER D. FELDMAN

- Partner, Bingham McCutchen LLP, 850 lawyers; 11 offices (Resident, Washington, DC)
- 30+ years structured and project finance/merger and acquisition/new venture development experience in energy/environment/infrastructure fields
- Advisor on all types of renewable energy projects – development, finance and sale, as counsel to developers, financial institutions, government agencies
- Chair, ABA Renewable Energy Resources Committee; Director, American Council on Renewable Resources; Former Deputy Administrator, U.S. Federal Energy Administration; Member, U.S. EPA Financial Advisory Board; Editor, Merchant Power Monthly; Editorial Board Journal of Structures Finance
- Brown University, Yale Law School, Harvard Business School

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