Federal Tax Incentive Opportunities
Waste to Energy Projects

April 27, 2012

Positive energy.

an independent member of BAKER TILLY INTERNATIONAL

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Agenda

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- Renewable Energy Industry Drivers
- Overview of Federal Tax Incentives
  - Renewable Energy (ARRA)
  - New Market Tax Credits
- Tax Incentives' Fit with Funding Options

Baker Tilly Virchow Krause at a glance

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Baker Tilly is the 8th largest accounting network worldwide

- 19th largest in U.S. consisting of over 1,400 Professionals
- Virchow Krause established in 1931
- Eleven years as an established investment banking practice through Baker Tilly Capital, LLC

Baker Tilly Renewable Group U.S. Clientele

- Developers
- Public Entities / Utilities
- Manufacturing
- Real Estate
- Native American Tribes

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Renewable Energy Client Activities

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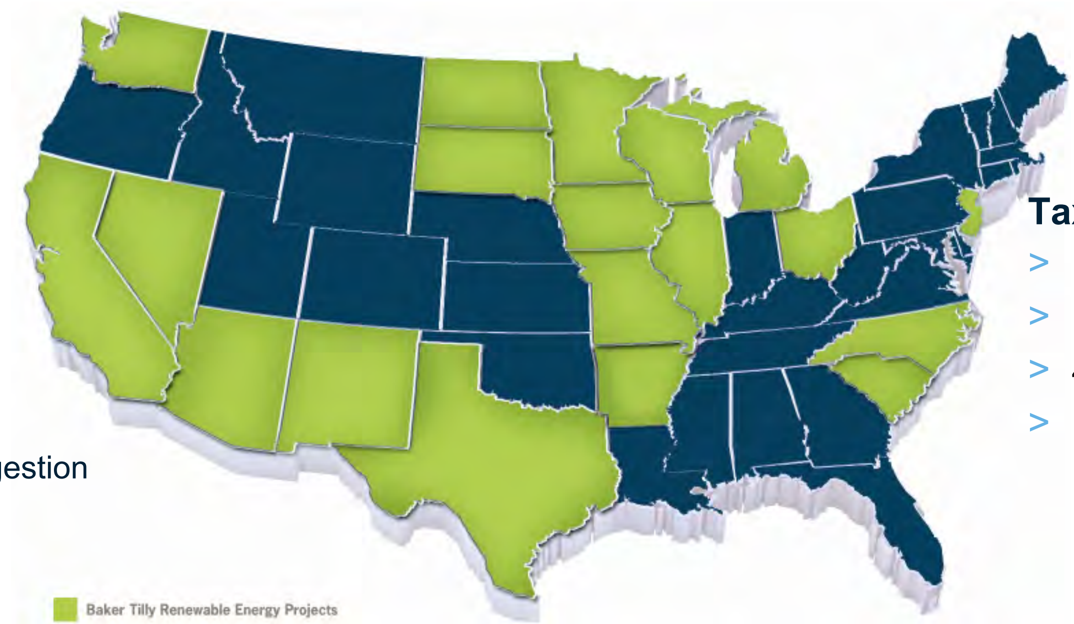
Baker Tilly clients have completed or have ongoing renewable energy projects in the states shaded green.

1,500+ MW
55+ projects

> Wind
> Solar
> Biomass
> Anaerobic Digestion



Tax Credits/Incentives

> 1603 Grants
> ITC/PTC
> 48C Monetization
> New Markets Tax Credits

Primary Drivers of Renewable Energy

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- Renewable Portfolio Standards (RPS) creating demand for renewable power
  - State level incentives
  - Renewable Energy Credits (REC) currently an inefficient market
  - National RPS has been proposed/discussed
- Financial Incentives for Renewable Energy Projects (ARRA most recent)
- Carbon emission regulations and offset markets creating economic incentives to reduce greenhouse gas emissions
  - EPA currently regulates CO2 emissions (fine based system)
  - "Cap and Trade" system has been adopted in California (October, 2011) creating a compliance market for carbon credits from agricultural projects
- Environmental regulations increasing – major impact on agricultural and food processing sectors relating to waste disposal processes

RPS Standards

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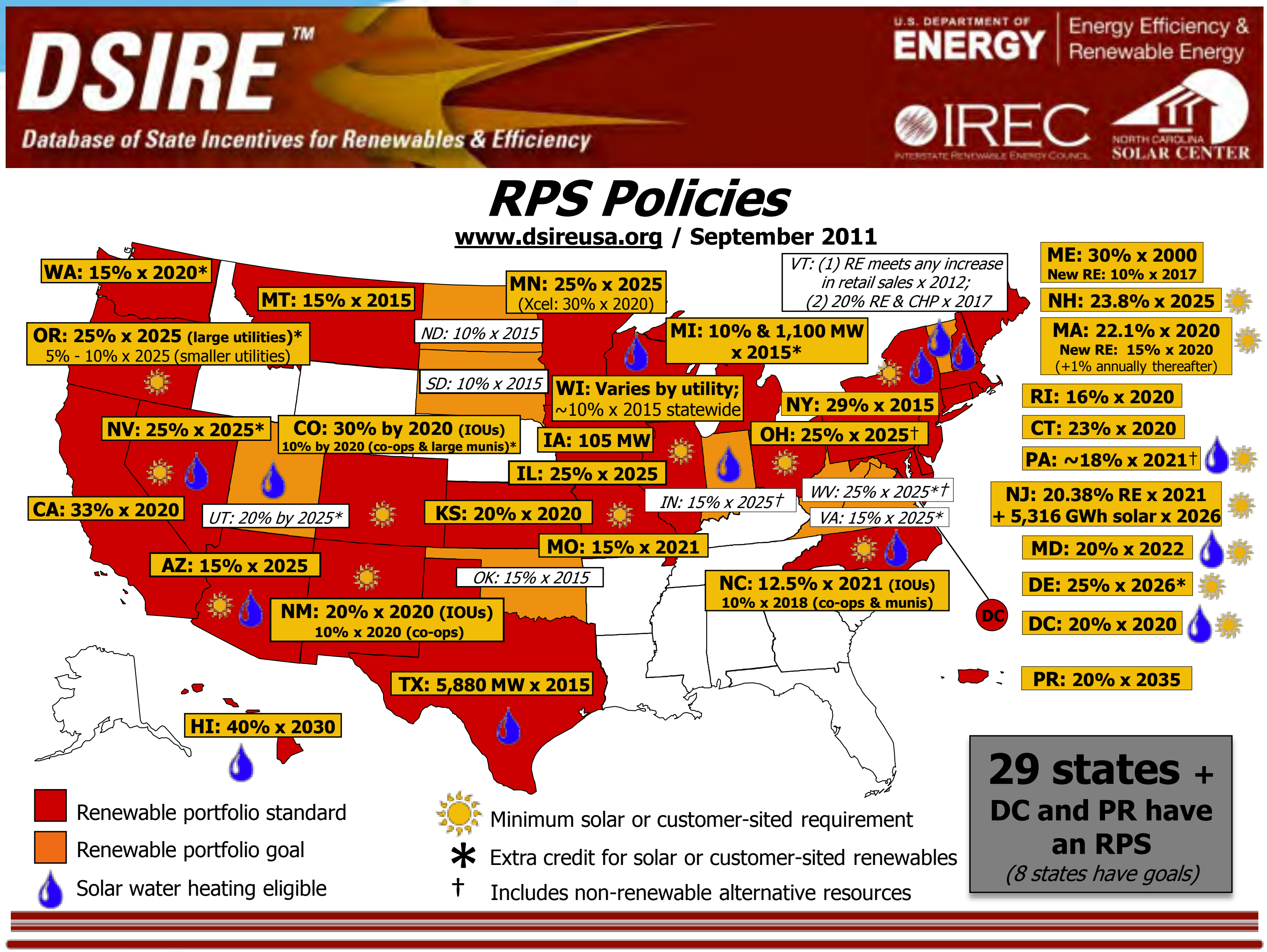

Net Metering Policies

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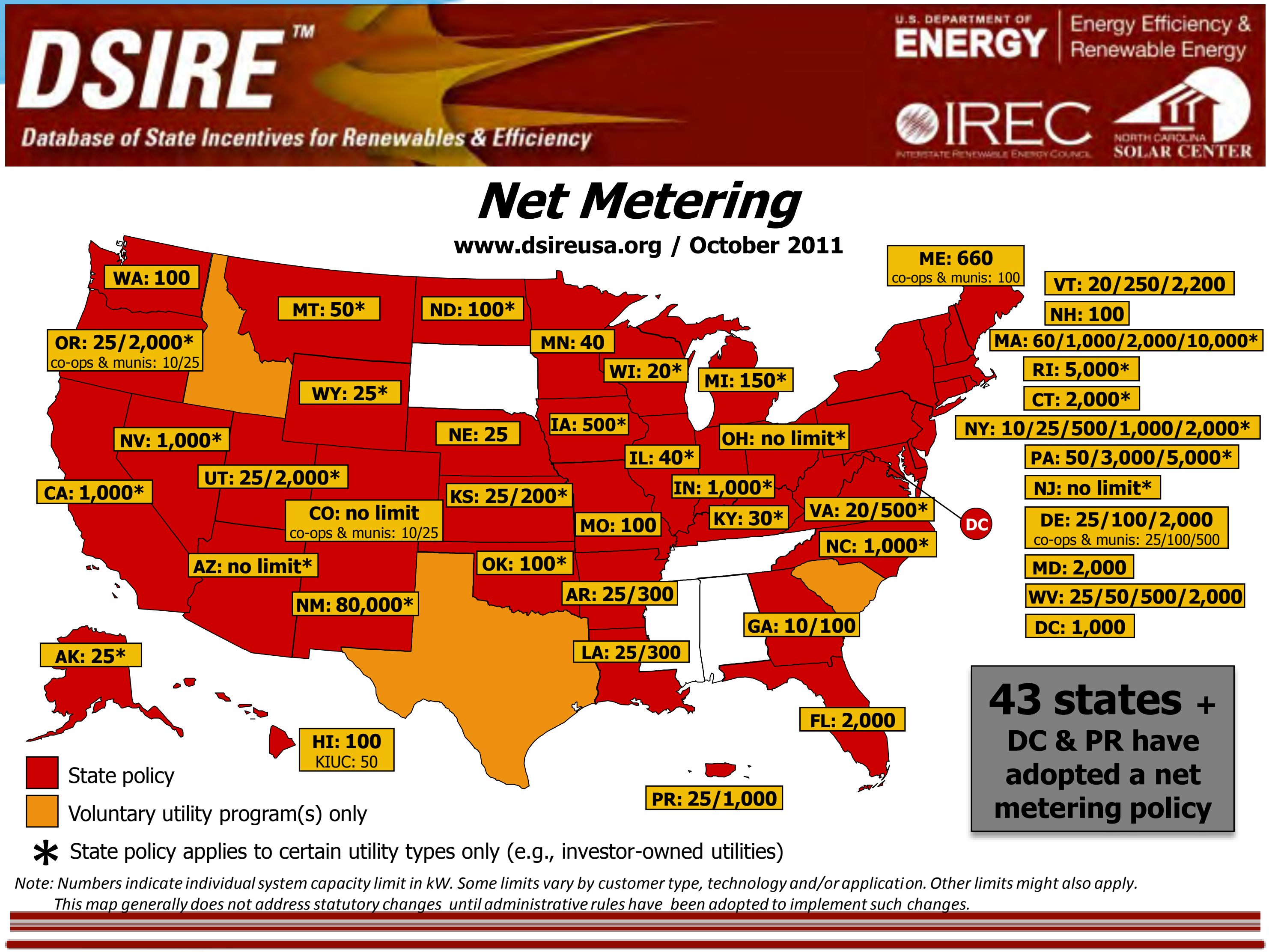

ARRA Qualified Facilities

- Section 1603 Program Guidance defines several "Qualifying Facilities". Most waste to energy projects qualify under one of the following:
  - "Trash facilities: A trash facility is a facility, other than a landfill gas facility, that **uses municipal solid waste to produce electricity**…"
    - "Municipal solid waste" is defined in IRC section 45[c][6]. By reference this term is defined in section 2(27) of the Solid Waste Disposal Act (42 USC 6903) as it relates to "solid waste". This Act defines solid waste as "**any garbage, refuse…and other discarded material, including solid, liquid, semisolid, or contained gaseous material resulting from industrial, commercial, mining, and agricultural operations**…"
  - "Open-loop biomass facilities: An open-loop facility uses open-loop biomass to produce electricity. Open-loop biomass is **any agriculture livestock waste nutrients or any solid, nonhazardous, cellulosic waste material or any lignin material that is derived from qualified sources.**"
    - **Agricultural livestock manure and litter**
    - Qualified sources from which solid, nonhazardous, cellulosic waste material or any lignin material must be derived are:
      - **Forest-related resources**
      - **Solid wood waste materials**
      - **Agriculture sources, including orchard tree crops, vineyard, grain, legumes, sugar, and other crop by0products or residues**

ARRA Tax Incentives

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- Tax Incentives :
  - Production Tax Credit equal to $.011/kwh produced for 10 years (inflation indexed)
  - Investment Tax Credit (“ITC”) equal to 30% of eligible project costs
    - Eligible project costs are those related to “**Specified energy property**”, which is in turn defined as “**only tangible property (not including a building) that is an integral part of the facility**”
  - 1603 Grant in Lieu of ITC
    - Grant proceeds available 60 days after Commercial Operation Date (COD)
    - Project must have “commenced construction” by December 31, 2011

For PTC, ITC or 1603 grant, Project must reach COD prior to December 31, 2013

  - Accelerated Depreciation (5-7 Year MACRS) applies as well (basis reduced by 50% of the 1603 grant)

ARRA Qualified Facilities…

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- Combined Heat & Power ("CHP") Facilities
  - System uses the same energy source for the simultaneous or sequential generation of electrical power, mechanical shaft power, or both in combination with the generation of steam or other forms of useful thermal energy (including heating and cooling applications):
    - Produces at least 20% of its total useful energy in the form of thermal energy, <u>and</u>;
    - Produces at least 20% of its total useful energy in the form of electrical or mechanical power, <u>and</u>;
    - Meets energy efficiency (at least 60%) and capacity (50 MW or less) standards
  - <u>ITC is equal to 10% of eligible costs</u>
  - Project must reach COD prior to December 31, 2016

Need to carefully plan and apply when thermal energy generation is involved. IRS has indicated that some thermal does not automatically cause a project to have 10% ITC/ 1603 Grant eligibility.

Structures Used for Tax Investment

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- Structures
  - Sale-leaseback
    - Term of lease must be meaningfully shorter than useful life of equipment
    - FMV requirements
  - Flip Structure (Section 45, Revenue Procedure 2007-65)
    - Investor owns 99% of project, sponsor owns 1% but is managing member
    - Automatically shifts to 5/95 split at pre-arranged “flip point” (based on IRR for tax investor)
    - Sponsor has option to purchase remaining 5% at FMV
  - Preferred membership class for tax investor
    - Preferred equity holders would receive preferred return and their original capital in advance of distributions being made to the common equity holders.
    - Tax benefits from losses included in definition of “cash flow” for purposes of calculating distributions to preferred members
- Requirements in all cases
  - Must be investor at time qualifying equipment is placed in service (Sale-leaseback provides 3 month cushion)
  - Economic substance guidelines

Tax Investor will have similar underwriting perspective to senior lenders

New Markets Tax Credits

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- New Markets Tax Credits (NMTC)
  - Brings additional low cost capital to fund a project
  - "Typical" NMTC deal ($10 million of allocation) provides approximately $2.0 million of benefit to the project
  - Total allocation of $33 billion since program's inception in 2000

Can be combined with renewable energy tax incentives

NMTC Overview

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What are New Markets Tax Credits?

- First tax credit program to stimulate commercial investment in rural and "low-income communities"
- The program is administered by the US Treasury Department through a division called the CDFI Fund, in a unique "public/private partnership" with Community Development Entities (CDEs)

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Community Development Entities (CDE)

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What is a "community development entity"?

> CDEs come in a variety of forms:
  - An affiliate of a municipality to promote economic development
  - An affiliate of a bank to help meet the bank's community reinvestment goal
  - Non-profit and for-profit entities with a mission to serve low income communities

> CDEs have defined geographic service areas and are charged with evaluating each potential NMTC transaction for community impact

> CDEs can be found using a search engine on the CDFI Fund website at www.cdfifund.gov

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Community Development Entity

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- CDEs have a primary mission of providing investment capital for low-income communities and are accountable to the residents of that community through a governing or advisory board
- Delegated authority by US Treasury to sell NMTCs to fund Qualified Low-Income Community Investments (QLICIs)
- Responsibility for ongoing monitoring and maintenance of Sub-CDE
- CDEs earn fees from obtaining and deploying the allocation and those affiliated with banks earn Community Reinvestment Act (CRA) credit

Low Income Communities

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What is a "low income community"?

- Based on census tract data – median income, poverty rate and unemployment
- Qualifying vs. "Higher Distress"
  - Includes rural areas, brownfield areas, designated Hot Zones, medically underserved areas, food deserts, Colonias and HUB Zones
- Qualifying census tracts in non-metropolitan counties automatically qualify as "higher distress"
- Qualifying census tracts can be located using a mapping tool on the CDFI Fund website at www.cdfifund.gov

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Baker Tilly NMTC experience

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- Involved with NMTCs since the program's inception in 2000
- One of nation's foremost experts in NMTCs
  - We operate our own CDE (The Valued Advisor Fund), which has received allocations totaling $102 million in NMTCs
  - Assisted in closing 100+ NMTC transactions to date, bringing investment value of over $1 billion to distressed communities nationwide
  - Worked with more than 50 CDEs on successfully structuring and closing transactions
  - Authored 25 award winning allocation applications totaling more than $1.3 billion in NMTC awards
- Strong relationship with country's leading tax credit investors
- Working relationships with 7 governmentally controlled CDEs

The most comprehensive NMTC consulting practice in the country

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NMTC Program Benefits

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Economic benefit to recipient

- Capital to fund projects, business expansion or debt refinancing
  - Tax credits are monetized to bring additional capital to the capital structure
- Low cost of capital
- Flexible loan terms including longer amortization and higher LTV ratios
- Debt forgiveness
  - At the end of the 7-year compliance period a significant portion of the NMTC benefit is permanently forgiven.

NMTC Program Benefits

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Community benefit

- Create additional economic development for the local community
- Attract and retain skilled workforce
- Bring new goods or services to underserved communities
- Capital investment to underserved, qualified Low-Income Communities (LIC)

Historical Allocation

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Round	Year	Awards	Amount ($ bil)	Avg. Award ($ mil)
1	2001-2002	66	$2.5	$38
2	2003-2004	63	$3.5	$56
3	2005	41	$2.0	$48
4	2006 *	63	$4.1	$65
5	2007 *	61	$3.9	$64
6	2008	70	$3.5	$50
7	2009 **	32	$1.5	$47
8	2009	99	$5.0	$50
9	2010	99	$3.5	$35
10	2011	70	$3.5	$50
TOTAL		**664**	**$33.0**	**$49.7**

Critical Distinction

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NMTC Allocation

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Tax Credits or Cash

The Math

NMTC Allocation	$10,000,000
NMTC Rate	39%
Tax Credits	$3,900,000
Investor Discount & Costs	49%
Net NMTC Cash to the Project:	$2,000,000

What makes a good NMTC candidate?

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- Located in a “highly distressed” census tract – any one of the following:
  - Poverty > 30%
  - Median Income < 60% of statewide
  - Unemployment > 1.5 times national average
  - Non-metropolitan county
- Community impact
  - Tangible community benefit – measured by quality job creation, providing unmet goods & services to low income communities (grocery stores), environmentally sustainable construction, etc.
  - Part of an existing plan for economic revitalization
  - “But for” test – NMTC fills a real funding gap that would otherwise not happen
- Ready to go
  - Other sources of funding are committed
  - Approvals all in place

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Funding Options

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Potential Funding Options	Cost of Funds	Comments
1603 Grant Funds*	Nearly 0%	Need to have met "start of construction" requirement prior to December 31, 2011
NMTC Proceeds	Nearly 0%	Not an "entitlement program", must secure allocation from CDE
Utility Rebates/Grants	Nearly 0%	Depends on project deliverables and timing for "yearly" program goals/funding
Federal Loan Guarantees/TIF/Other	4-8%	Specific to project location, availabilty and owner's overall profile of need
Foundation Investments	5-8%	Depends upon fit of project with "Program Funds" available
Senior Debt	6-9%	Depends upon Sponsor's background and contractual "de-risking" of the project
Tax Equity**	10-15%	Supply/demand driven and is a fluid market
Equity	12-20+%	Depends upon technology's stage of development

* Requires a bridge investment (funds received post COD).
** Cost of funds represents cost to project owner with tax liability of its own.

Observation:

- Having well established partners and clear communication is critical. Not easy to bridge varying perspectives that exist between engineers, energy, financial and agricultural communities