Energy Services Coalition (ESC)

Biggest Bang for the Buck
Leveraging Funds

An ESC Webinar
Second Quarter 2009: June 5, 2009

Presented by four Finance Industry Experts:

- Karen Keeler
- Joseph McLiney
- Darin Lowder
- Peter Flynn

See next slide for Technical Difficulties

Technical Difficulties?

An alternative way to view slides:
http://www.energyservicescoalition.org/webinars/2009-06-05/index.html - click on "All"

For audio: you may select Use Telephone after joining the Webinar. United States: 484-589-1010 Access Code: 245-024-916 Webinar ID: 467-416-322

For today's webinar support, please contact Linda Smith at 303-582-5198

The Energy Services Coalition (ESC) presents a national education forum through the use of webinars to enhance the learning and awareness of performance contracting.

What is The Energy Services Coalition?

ESC is a national nonprofit organization composed of a network of experts from a wide range of organizations working together at the state and local level to increase energy efficiency and building upgrades through energy savings performance contracting.

This webinar is hosted by the

Education Committee, a subcommittee of the National ESC Board of Directors.

If you have any questions or need additional information, please contact
Rhonda Courtney at 615-885-0019

Biggest Bang for the Buck
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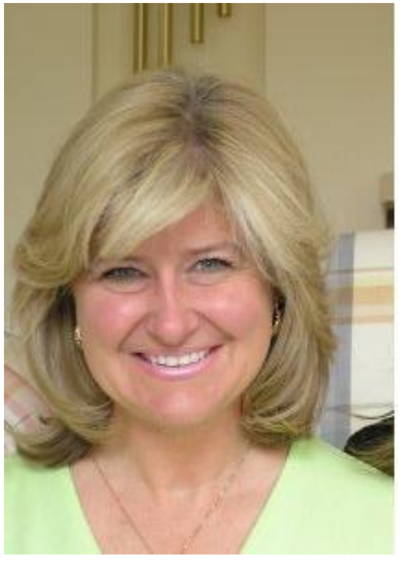
Financing in this New Economic Climate

Karen Keeler, Senior Vice President with AAIG in Denver, is focused on the financing of energy performance contracting transactions. She has been active in the financial industry for over 15 years and has been responsible for the successful origination of over $1 billion in lease and bond financings supporting energy efficiency projects. In addition, Ms. Keeler has been involved in the development of performance contracting legislation in several states and is an active member of NAESCO and the Energy Services Coalition.



Financing
in this New Economic Climate

Lease Purchase Financing

Current Market Trends
Leveraging Grant and Stimulus Dollars
to Develop Projects in Current Economic Climate

Presented By:

Karen Keeler
Senior Vice President
All American Investment Group, LLC

Lease Purchase Financing
Energy Performance Contracts – Current Trends

- Energy Performance Contracts = Self-Supported Debt
- Fewer Institutions Lending = Highly Competitive Market for Available Capital
- Current Focus - Credit Quality (Client & ESCO)
- Banks Trying To Raise Capital = Shorter Terms & Higher Rates
- Lenders have New Exposure Ceilings
- Heightened Interest from Public Sector as Result of ARRA Stimulus funds
- Appeal of Energy Performance Contracting Increasing in Response to Budget Cuts for Capital Projects

Lease Purchase Financing and Leveraging Capital Resources

- Combining Bond Proceeds and Lease Purchase Arrangements on Capital Projects
- Effective Application of Utility Incentives with Lease Purchase Transactions
- Incorporate Traditional Grant Program Dollars to Buy Down Lease Purchase
- Utilize Tax Credits as Part of the Lease Purchase Structure

Lease Purchase Financing – Leveraging Stimulus Dollars

- State and Local Governments can Leverage ARRA funds into much more than a Dollar-Per-Dollar Benefit
- Stimulus Funds Utilized as Incentives for Project Development -- Seed Money
- Leverage Stimulus Dollars with Traditional Sources of Capital- Take Advantage of the Energy Performance Contract paying its own way using a Lease Purchase Arrangement.

Lease Purchase Financing – Leveraging Capital Resources Case Studies

College in Oregon:

Project	$17,000,000
Tax Credit:	$ 2,000,000
State Energy Fund:	$ 2,000,000
Net Project Cost:	$13,000,000
Lease Purchase:	$13,000,000

Customer initially looked at a $4,000,000 project; however, once shown that Energy Savings can cover 100% debt service of Net Project Cost – this is now a $17,000,000 project for the ESCO. A Win-Win scenario.

Lease Purchase Financing – Leveraging Stimulus Dollars Case Study

Texas Municipality

Recipient of $3,500,000 in ARRA funds

Project Size:	$ 7,000,000
Application of ARRA funds:	$ 3,500,000
Net Project Cost	$4,500,000

Customer has numerous “non-energy” saving capital improvements in this $7,000,000 project. Through buy-down of the project, sufficient energy savings exist to cover 100% debt service of balance. In addition, the project has an annual surplus in annual projected savings that can be redirected to cover other capital improvement needs.

Thank you!

Karen Keeler

Bonds
Increasing your Project Size by Decreasing Your Interest

G. Joseph McLiney, President of
McLiney And Company, an investment banking firm that successfully completed over 350 Qualified Zone Academy Bonds, Clean Renewable Energy Bonds and other tax-credit bonds. Mr. McLiney has been in the investment banking business providing funds to municipalities for more than 20 years, is a published writer (economics), and has been a featured speaker for numerous states helping explain complex financial tools to municipalities nationwide.

Bonds
Increasing your Project Size by Decreasing Your Interest

Clean Renewable Energy Bonds

Most recent changes to CREBs

Increase/decrease in tax-credits

Qualified Zone Academy Bonds

"The Original Tax-Credit Bond"

Qualified School Construction Bonds

"QZABs made Easy"

Presented By:

G. Joseph McLiney

President

McLiney And Company

Investment Bankers

Steps

QZABs / QSCBs are like other borrowing instruments. They must follow **<u>all</u>** state and federal rules and regulations. In addition, they have additional federal regulations. To receive a Qs allocation a school district must:

- Create a “Zone Academy”
- Create a Zone Academy Plan
- Find a private partner that gives 10%
- Receive a state allocation
- Find a “Qualified Buyer”

http://www.taxcreditbonds.org, or Wikipedia search, key word: QZABs

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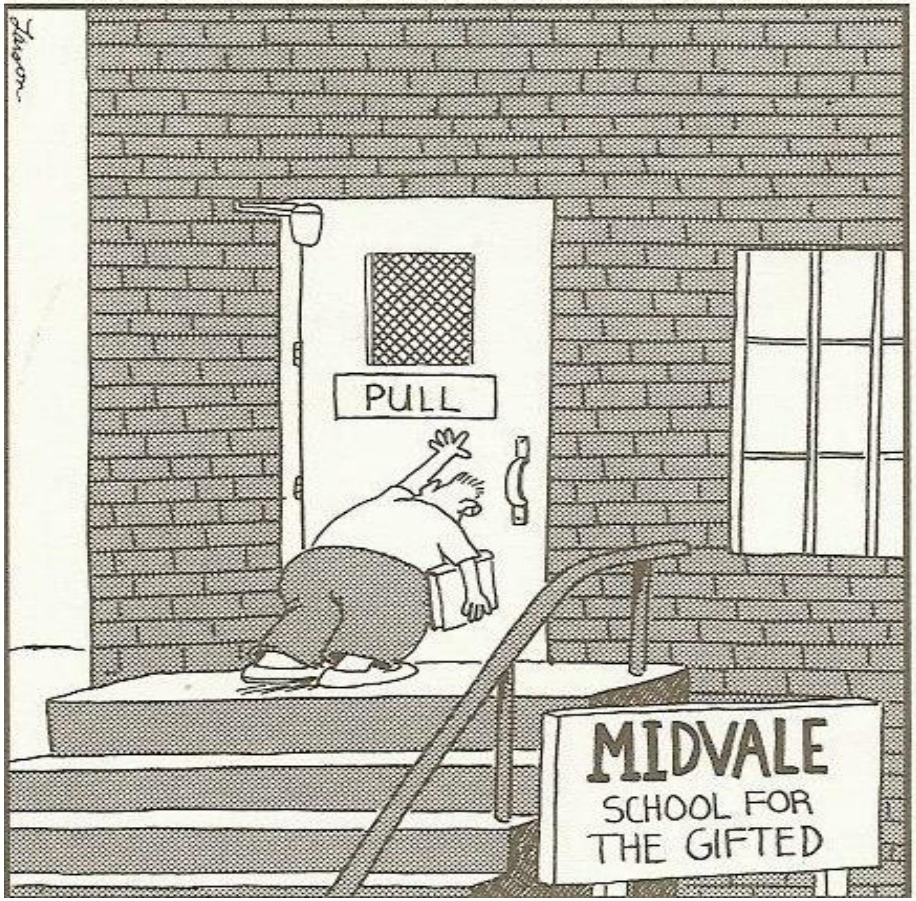
Thank you!

G. Joseph McLiney



Bonds, Making Tax Incentives Work for the Public Sector, and More

Darin Lowder, Associate with Ballard Spahr Andrews Ingersoll, focuses on energy, project finance, and related real estate issues. Mr. Lowder has worked with utilities, energy project developers, tax equity investors, engineering and construction firms, project site owners, and power purchasers on a variety of renewable energy and fossil-fuel power projects and financings. Mr. Lowder has also advised clients on multiple financing and regulatory issues affecting the energy industry, including the emerging state and Federal renewable and carbon regulatory regimes.

Bonds, Making Tax Incentives Work for the Public Sector, and More

Qualified Energy Conservation Bonds
Energy Efficiency and Conservation Block Grants
New Markets Tax Credits for Eligible Locations

Presented By:

Darin Lowder
Associate
Ballard Spahr Andrews & Ingersoll, LLP

Qualified Energy Conservation Bonds

- ARRA authorizes a total of $3.2 billion in Qualified Energy Conservation Bonds (increase from last year's $800 million)
- May be issued only by state and local governments
- Should Result in Near-Zero Interest Debt Terms
- May be issued for qualified conservation purposes. Includes:
  - Reducing energy use in publicly-owned buildings
  - Implementing green community programs
- Guidance recently issued
  - No application process
  - Allocations determined by population

Top 10 QECB State Allocations

State	QECB Allocation
California	$381,329,000
Texas	252,378,000
New York	202,200,000
Florida	190,146,000
Illinois	133,846,000
Pennsylvania	129,144,000
Ohio	119,160,000
Michigan	103,780,000
Georgia	100,484,000
North Carolina	95,677,000

Energy Efficiency Grants

- $5 billion to fund grants to states under the existing Weatherization Assistance Program to assist low-income families in reducing energy costs
- $4.5 billion to fund construction, repair, and alteration of Federal buildings for projects focused on increasing energy efficiency and conservation
- $250 million for grants or loans to property owners to upgrade HUD-sponsored low-income housing to increase energy efficiency, including new insulation, windows, and furnaces

Energy Efficiency & Renewable Energy Grants

- Over $2.7 billion in direct formula Energy Efficiency and Conservation Block Grants ("EECBG") available to states, localities, and private entities to reduce fossil fuel emissions and energy use.
  - Cities eligible for direct grants from the DOE include cities with population of 35,000 or the 10 largest cities in each state.
  - Counties eligible for direct grants from DOE are those with 200,000 or one of the 10 largest counties in the state.
  - Cities and counties not qualifying for direct grants may receive sub-grants through their states.
- Up to $456 million in competitive grants
- EECBG funds application deadline: June 25, 2009.

EECBG Eligible Activities

- Eligible activities include:
  - financial incentive programs for energy efficiency improvements;
  - grants to non-profit organizations to perform energy efficiency retrofits;
  - programs to conserve energy used in transportation;
  - energy efficiency building codes and inspections;
  - installing LEDs
- EECBGs may be combined with QECBs for additional leverage

Energy Efficiency & Renewable Energy Grants

- **State Energy Program** - $3.1 billion to the states and state energy offices to address energy priorities and adopt emerging energy efficiency technologies. Includes residential, commercial and governmental building energy efficiency retrofits.
- **Additional grants available** if Governor has "obtained necessary assurances" that state utility commission will seek to implement a decoupling policy

Federal New Markets Tax Credits

- ***New Markets Tax Credit ("NMTC") Program*** is one of the largest economic development incentive programs ever created to stimulate investment in low income communities
- The ***purpose*** of NMTC Program is to encourage private capital investment in low-income communities
- Individual and corporate taxpayers receive a credit against federal income taxes for making qualified equity investments in ***Community Development Entities (CDEs)***
- NMTC totals ***39%*** of the cost of the investment and is claimed over a ***7 year credit period***

Increased NMTC Allocation

- Because the NMTC program results in ***very low cost financing*****,** projects located in an eligible location should considered.
  - Creates a tax credit for equity investments in ***Community Development Entities*** (CDE's)
  - Amount allocated in both 2008 and 2009: **$5 billion**, increased from $3.5 billion in the Stimulus Bill
  - Final **$1.5 billion** of allocations for 2008 were awarded in May 2009

NMTC Tax Investor

- Receives **federal tax credit** equal to **39%** of the amount of the original investment
- Credit taken over a **7-year period**
- May **“leverage” credits** by borrowing for equity investment in CDE
- Mainly banks, insurance companies as **investors**
- Leveraged lenders **include party with interest in QALICB**, commercial lenders to project

NMTC CDE

- For-profit entities established specifically to obtain NMTC allocation.
- CDEs must have a primary mission of serving or providing investment capital for, low-income communities (“LIC’s”) or Low-Income Persons and be accountable to LICs they serve
- Sample of entities that have set up CDE and received allocations: PNC Bank, Wachovia Bank, ESIC (Enterprise), Trammel Crow Company, Prudential Insurance, McCormack Baron, Morgan Stanley
- List of Allocatees: www.cdfifund.gov

NMTC Qualified Active Low-Income Community Business (“QALICB”)

- An energy efficiency project located in low income census tract may qualify as a QALICB
- Interest only loans for 7-year credit period
- CDE required to provide loan on more favorable terms, such as below market interest rates, lower organization fees, more flexible borrower credit standards, higher than standard amortization period
- Portion of the value of the NMTC to investor passed on to QALICB (forgiveness of debt, very long amortization period)

Thank you!

Darin Lowder

Build America Bonds and Alternative Financing Structures

Peter Flynn, Principal, Bostonia Partners LLC, has over 15 years experience in law and finance and is a co-founder of the firm. Mr. Flynn is experienced in structuring and funding federal, municipal and commercial energy efficiency and renewable energy projects, contract finance, securitization and public/private partnerships. Mr. Flynn is a graduate of Boston University School of Law and Syracuse University where he graduated Magna Cum Laude and Phi Beta Kappa.

Build America Bonds and Alternative Financing Structures

Presented By:

Peter Flynn
Principal
Bostonia Partners, LLC

Overview of the Build America Bond Program

- The American Recovery and Reinvestment Act of 2009 (the “Act”) creates two types of tax advantaged municipal securities known as Build America Bonds (“BABS”).

  Issuer Subsidy BABS. Municipal issuers can sell taxable BABS and receive a subsidy directly from Treasury equal to 35% of the interest on the bonds.

  Investor Subsidy BABS. Alternatively, municipal issuers can sell taxable BABS and the investor receives a tax credit equal to 35% of the interest received. Since the tax credit is transferable, the investor is permitted to sell the credit to a third party.

Structuring Considerations

The Act provides significant debt structuring flexibility and places no restrictions on size, amortization, maturity, coupon type or callability of BABs

- **Size:** The taxable market prefers large transaction sizes which facilitate liquidity; a premium may be required for transactions below $100 million.
- **Amortization:** The taxable market prefers bullet maturities; traditional term bonds with mandatory sinking fund payments will sell at a slight yield premium to bullet maturities.
- **Maturity:** BABs can be sold with maturities up to thirty years in the taxable market.
- **Coupon Type:** BABs can be issued as current interest bonds (fixed floating, put bonds, floating rate notes), zero-coupon bonds and convertible zero-coupon bonds.

Additional Structuring Considerations

Bond Indenture:

- Principal Amortization
  - In light of the taxable market's preference for bullet maturities, issuers and bankers will need to work with counsel to determine how bullets, or 'balloon' maturities, are treated for the purposes of calculation debt service for a Rate Covenant, an Additional Bonds Test ("ABT") or a Debt Service Reserve Fund ("DSRF") requirement.

- Interest Rate
  - For Issuer Subsidy BABs, issuers and bankers will need to work with counsel to determine how the subsidy from the Treasury is treated for the purposes of defining pledged revenues or calculating debt services for a Rate Covenant, an ABT or a DSRF requirement.
  - For Investor Subsidy BABs, the coupon at which the bonds are sold would likely apply to such calculations .

- Such issues will need to be analyzed on a case-by-case basis.

Tax Considerations

- BABS can only be issued for purposes that are otherwise tax-exempt eligible. Therefore, BABs needs to comply with all arbitrage regulations, e.g. spend-down requirements, yield rebate and restriction rules, limits on DSRF funding, etc.
    - The issuer will need to file a Form 8038 and execute a form of tax compliance certificate given the requirement to comply with arbitrage regulations.

- Arbitrage yield calculation
    - For Issuer Subsidy BABs, interest is calculated at the applicable bond rate, less the amount of expected subsidy.
    - For Investor Subsidy BABs, interest is calculated at the applicable rate.
    - A blended arbitrage yield will be calculated when BABs are issued as a common plan of finance with tax-exempt bonds

- The interest on any Issuer Subsidy BABs and the tax credit on any Investor Subsidy BABs are treated for state income tax purposes as being exempt from Federal income taxation.

BABs Buyers

- BABs will expand and diversify the investor base for municipal bonds and help to replace lost market capacity from leveraged buyers who reduced their municipal holdings over the past year.

- Issuers of BABs will be able to capitalize on the relative credit strengths of, and low default rates associated with, municipal bonds versus corporate equivalent securities.
  - The best candidates for BABs are medium to large, highly-rated (strong ‘A’ or higher) issuers.

- Domestic corporate bond buyers, the most active purchasers of BABs, have seen a dramatic reduction in taxable investment grade new issues.
  - This lack of supply has driven recent tightening of spreads in this market.

- Major targeted investors in BABs include mostly domestic corporate investors, such as bond funds, insurance companies and asset management companies.

Recent Issuances

- Approximately $10 billion of BABs have been sold since February
- **May 28**
  - New Jersey Transportation Trust Fund - $270 million, 30-year taxable bonds priced to yield 240 basis points over benchmarks, or 7 percent
  - The Metropolitan Transit Authority of Harris County, Texas (rail car purchases) - $83 million, 30 year final maturity, priced at 240 basis points over the comparable-maturity Treasuries, or 6.984%.
    - $137 million in twenty-year tax-exempt bonds offered a 4.69% yield.
  - Denver Water - $44 million, 30-year taxable bonds priced at 6%.
    - Denver Water will pay 3.94 percent interest. That is less than the average 4.23 percent that Denver Water pays on its outstanding tax-exempt bonds.

BABs Criticisms

- 35% formula may not benefit the Government
  - Top federal income tax rate is 35% and many buyers are in lower tax brackets (i.e. municipal bond mutual funds)
  - If tax rates go up – BABs will be more attractive
- State of California sold $20 billion of BABs at above 7%
  - Effective borrowing rate of 4.7% versus G.O. bonds at 5.5% or more.
  - Looks good, but will the rebates last?
- Yields in secondary trades of BABS were approximately 25 basis points lower – huge profits for underwriters.

Alternative Contract Structures: Energy Performance Contracting

- Leverage: Investing time and resources to implement energy performance contract structures without borrowing money thus providing for infinite returns at no risk.
- Private ownership of public sector projects allows developers/vendors to realize the full value of Stimulus tax benefits.
- properly structured deliver the maximum leveraged benefits to the public and private Sectors

Alternative Financing Structures: Typical terms and conditions

- Performance-based operating agreement for energy efficiency (and renewables) – PPA's, Shared Savings
- Vendors must install, operate and maintain assets
- End users pay for commodity generated – i.e. electricity, energy savings
- Customer payments are based upon measured, realized savings or services delivered
  - Nothing stipulated
- Contract terms range from 5 to 20 years
- Contracts for efficiency and/or renewables
- Assets are privately owned
- Environmental benefits can be assigned to the customer
- Contracts typically contain end of term purchase or renewal options.

Alternative Financing Structures: Advantages to both Public and Private Sectors

- Operating Agreement vs. Balance Sheet Liability
- Preserve existing debt ratings and capacity
- "No risk" alternative to existing performance contracting structure
- Vendor shares commodity risk with its customers
- Vendors are tied to performance on a long-term basis
- Unlimited return on zero investment
- Private ownership allows for utilization of all available local, state and federal tax benefits
- Preserve or maximize available clean energy or Stimulus funds through leveraging

Alternative Financing Structures: Unique economic advantages to the Public Sector

Private Sector ownership provides additional local economy stimulus through:

- Properly structured ownership of energy assets allows for the maximum realization of all Stimulus tax benefits
- 'Sales Tax' states and municipalities will realize additional revenues through private ownership
- 'Income Tax' states will realize the benefits of additional income taxes paid by developers and manufacturers
- Local property/excise taxes on private asset ownership
- Public/Private sector balance sheet/debt ratings will not have any current or future consequence
- Increased job creation
- Contracting for new technologies will reap local benefits
- Power Purchase Agreements/ Shared Savings Contracts properly structured deliver the maximum leveraged benefits to the Public and Private Sectors

New Technologies in the Public Sector

- Procurement regulations have not fostered implementation or acceptance of new or innovative technologies
- New companies with great new ideas lose their appetite for the prolonged approval and sales cycles
- Public entities now have the tools and funding to foster new energy efficiency and renewable energy technologies
- Consideration for innovative financial and contract structures for both new and old technologies
  - Must be a technology that can be measured and verified annually
  - Single technology contracts work best
- Public entities can become "investors" and reap significant rewards
- Public leverage should reap "private" rewards

Thank you!

Peter Flynn

Energy Services Coalition (ESC)

On behalf of ESC's Education Committee and the ESC National Board…

Thank you!

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