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FOX VALLEY BUSINESS CONFERENCE

Finance Strategies for Corporate Sustainability

September 16, 2024

BRUNSWICK MERCURY

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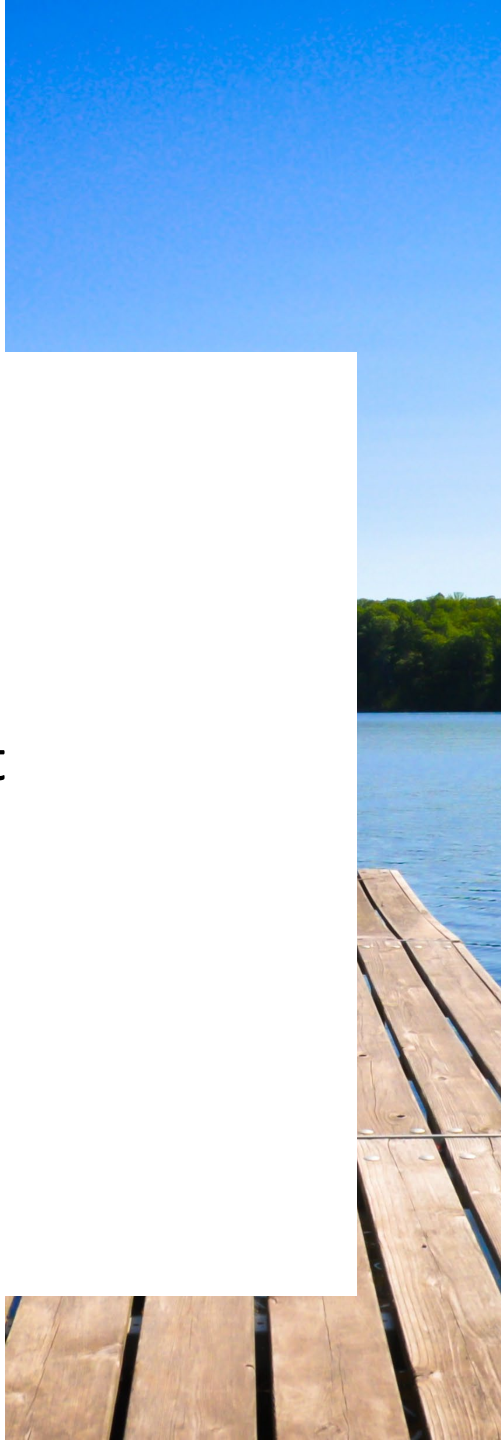
Agenda

- Tax Credit Sales
  - General Overview of Tax Credit Sales
  - Sellers and Purchasers of Tax Credits
  - Payment Amounts and Applicable Requirements of Transferable Credit
  - Risks as Purchaser
  - Tax Credit Agreements: Key Terms
- Virtual Power Purchase Agreements
  - Common Features and Issues for VPPAs



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Tax Credit Sales

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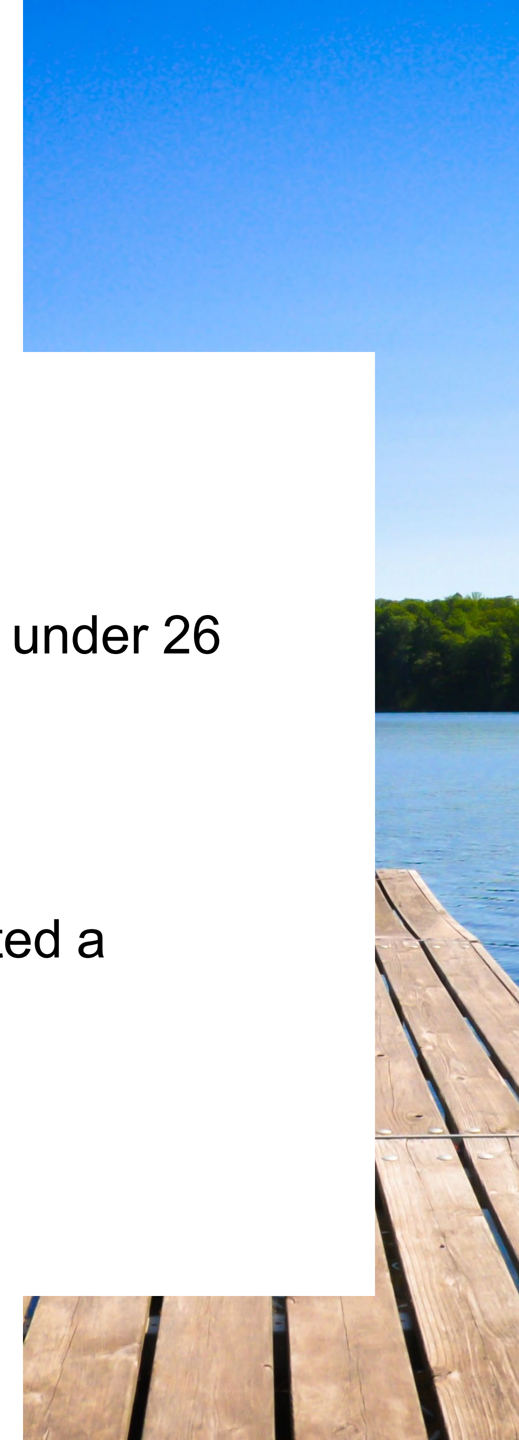
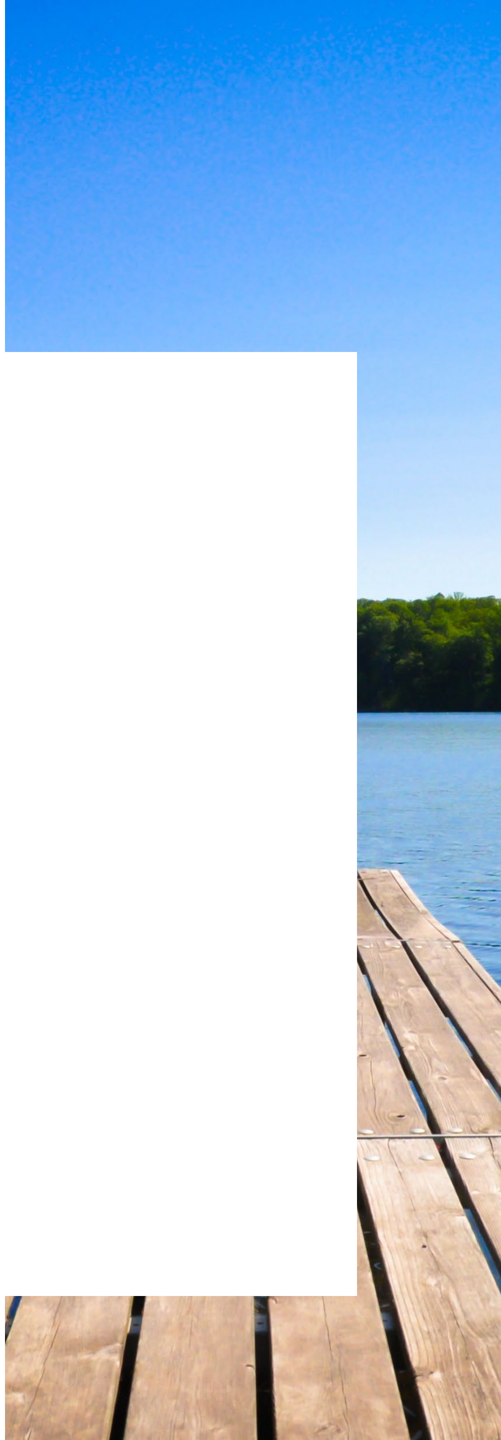
General Overview

- What is a **tax credit** in this context?
  - Tax credits are utilized to **lower tax liability** on a dollar-for-dollar amount
  - Tax credits are generated from certain eligible property and are transferrable under 26 USC Section 6418 of the Code
- Why are tax credits sold?
  - Developers typically do not have the tax appetite to utilize the tax credits
  - The Inflation Reduction Act introduced **tax credit transferability** which created a market for developers to sell tax credits
  - Price per eligible credit varies typically between ~ **$0.92 to $0.95**



Eligible Credits

- Eligible credits include:
  1. the ITC (Section 48) (including for solar, wind and battery storage projects)
  2. the Section 48E clean electricity investment credit (successor to the ITC)
  3. the PTC (Section 45) (including for solar and wind projects)
  4. the Section 45Y clean electricity production credit (successor to the PTC)
  5. the Section 30C alternative fuel vehicle refueling credit
  6. the Section 45Q carbon oxide sequestration credit
  7. the Section 45U zero-emission nuclear power production credit,
  8. the Section 45V(a) clean hydrogen production credit
  9. the Section 45X advanced manufacturing credit
  10. the Section 45Z(a) clean fuel production credit
  11. the Section 48C qualifying advanced energy project credit



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Sellers of Credits

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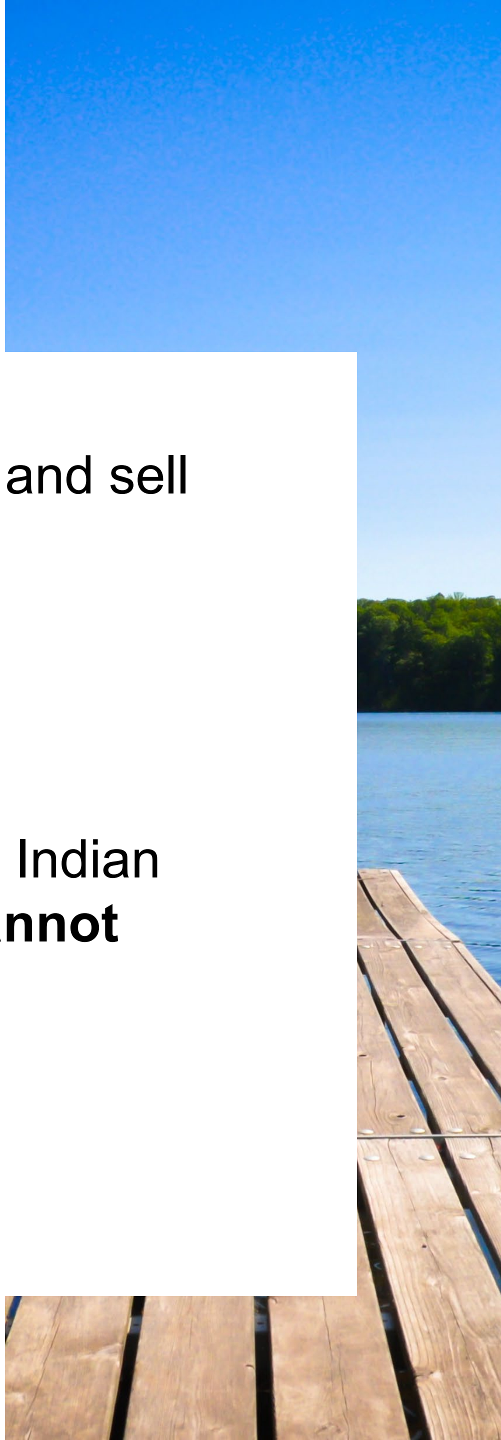
Renewable Energy Sponsors and Developers

- Generally, **any taxpayer** that generates these tax credits may then turn around and sell such tax credits
  - Independent Power Producers
  - Utilities
  - Manufacturers of Clean Energy Technology
  - Tax-exempt entities, states, political subdivisions, Tennessee Valley Authority, Indian tribal governments, Alaska Native Corporations, rural electric cooperatives **cannot**



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Tax Credit Purchasers

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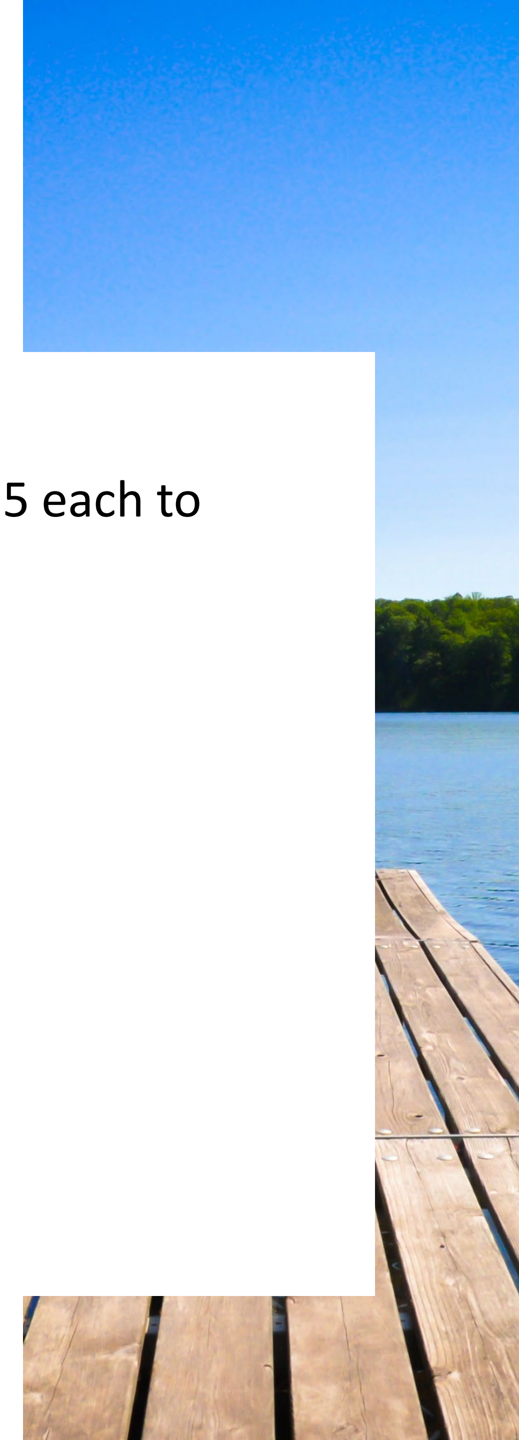
Tax Credit Purchasers

- **Any US taxpayer** can be a buyer, with some restrictions
  - Can have multiple buyers for one credit (i.e., project generates $100 ITC, can sell $25 each to four different buyers).
  - A dollar of credit cannot be sold more than once.
  - Buyer **can’t be related** to the seller.
    - “Related” defined by cross reference to 267(b) and 707(b)(1).
      - Generally, more than 50% overlapping ownership.
      - Complex attribution rules apply.
- Passive activity loss and credit limitations still apply



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Risk of Recapture and the Excessive Transfer Penalty

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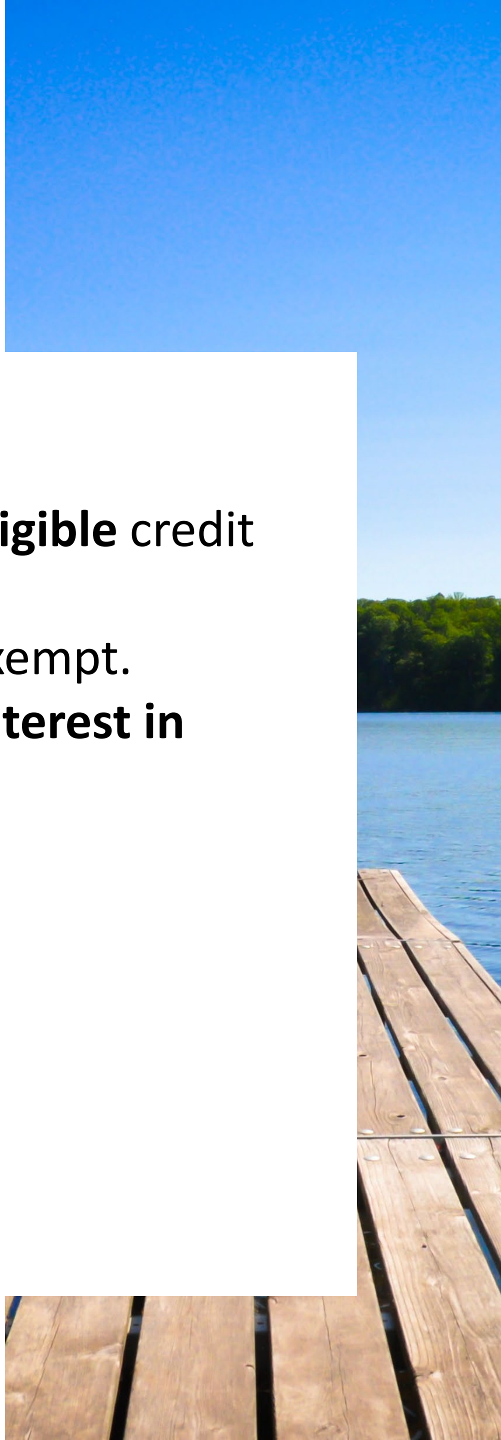
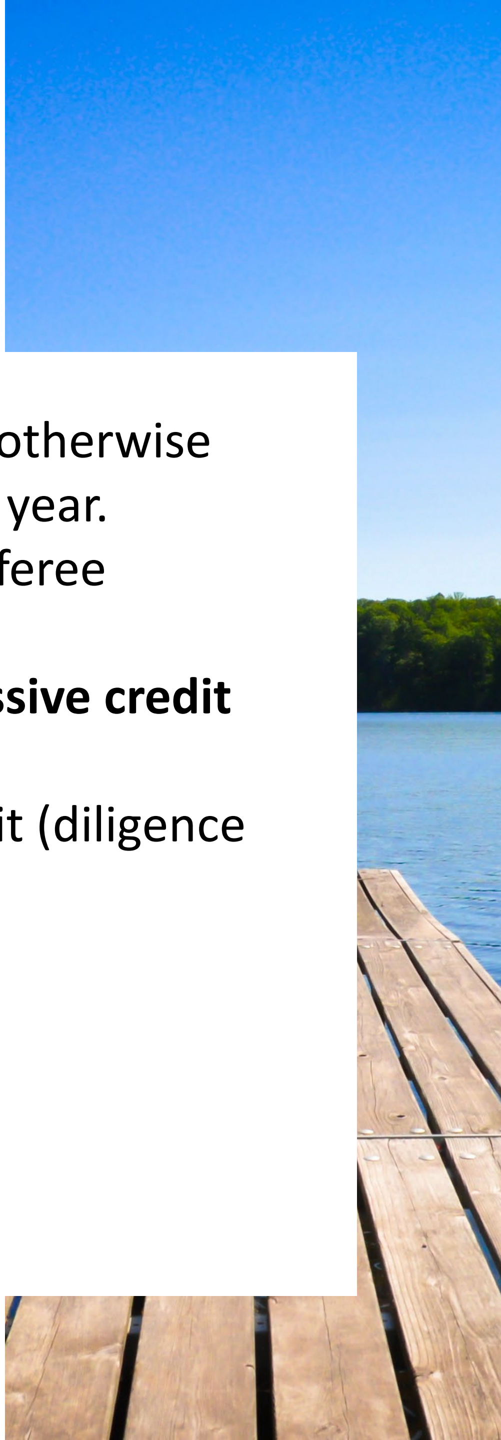
Recapture Risk Post-Transfer

- What is **recapture**?
  - Applies to ITC only (and several other credits, but **not the PTC**).
  - Recapture can occur **if the taxpayer disposes of credit property** or it **ceases to be eligible** credit property.
    - Examples: sale of the project, casualty event, owner of the project becomes tax exempt.
  - Historically, for a partner in a partnership, reduction of their interest below **2/3 of interest in applicable credit year** causes recapture as to that partner.
  - Amount of credit at risk of recapture is reduced by 20% each year for five years.
    - After five years, no more recapture risk.



Excessive Transfers

- The credit may not be transferred in an amount greater than the amount that would otherwise be allocable under the Code with respect to the eligible credit property for that taxable year.
  - The **IRS will impose a penalty** if the specified credit portion claimed by the transferee taxpayer is greater than that amount.
  - This penalty is the **amount of the excessive credit transfer plus 20% of the excessive credit transfer.**
- No excessive credit transfer penalties if buyer has reasonable cause to claim the credit (diligence function)



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Tax Credit Agreements: Key Terms

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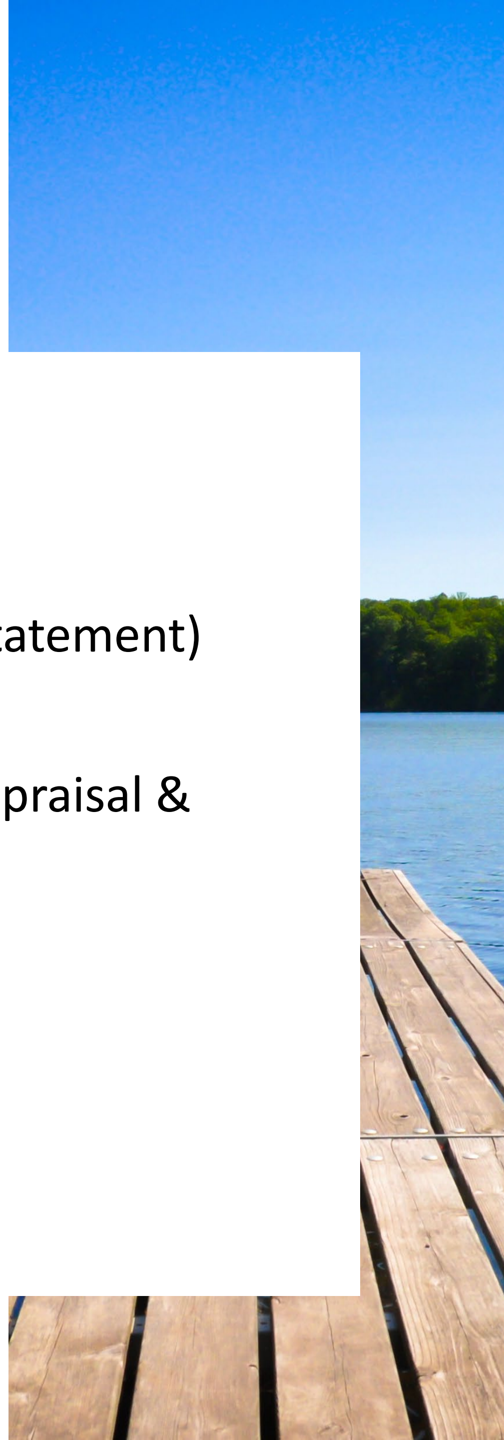
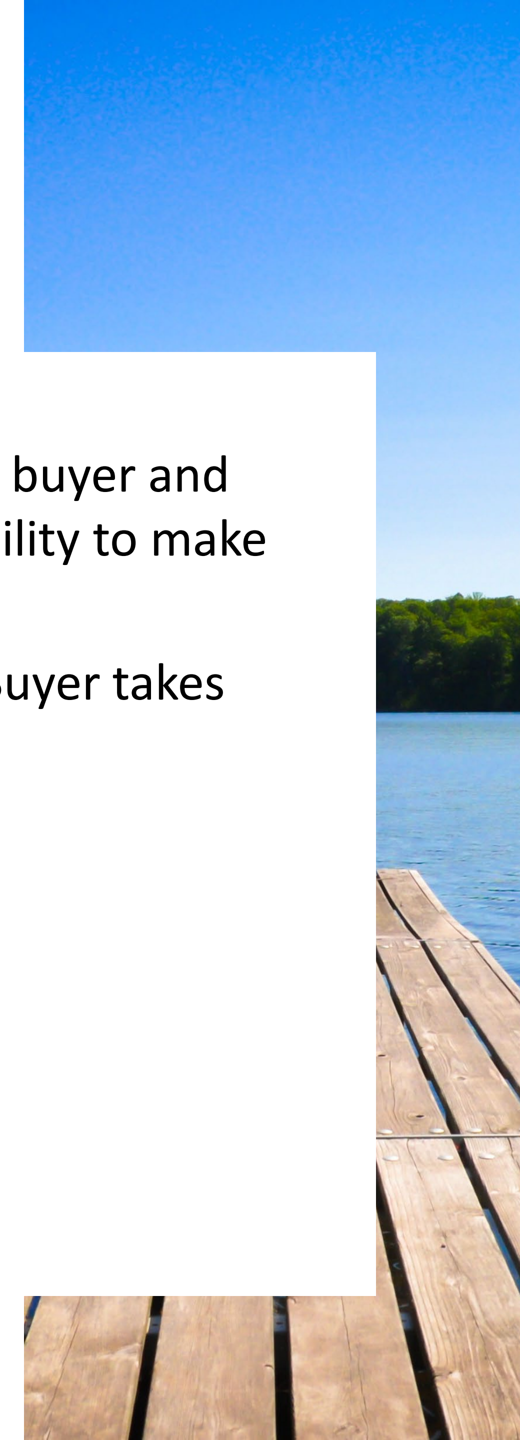
Tax Credit Agreements – Key Terms

- Purchase and Sale
  - Purchase Price, typically between $0.92 and $0.95 per eligible tax credit
  - Transfer of Title (combination of purchase price and exchange of Transfer Election Statement)
- Conditions to Purchase
  - Diligence deliverables may include project contracts, third party reports (Phase I, Appraisal & Cost Seg, IE Report)
  - Achievement of COD or PIS of the Project



Tax Credit Agreements – Key Terms

- Reps and Warranties focused on corporate building blocks and tax status of the seller, buyer and the project, variations on informed purchaser reps (acknowledging no registration, ability to make own investment decisions, etc.)
- Seller indemnity to buyer for recapture, disallowance and excessive credit transfers; Buyer takes risk as to its own status and ability to use credits
- Tax Contests: Rights of seller and buyer to control, or weigh in on, tax contests
- Credit Support
  - Tax credit insurance
  - Corporate guaranty
  - Letters of credit



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Tax Credit Market Snapshot

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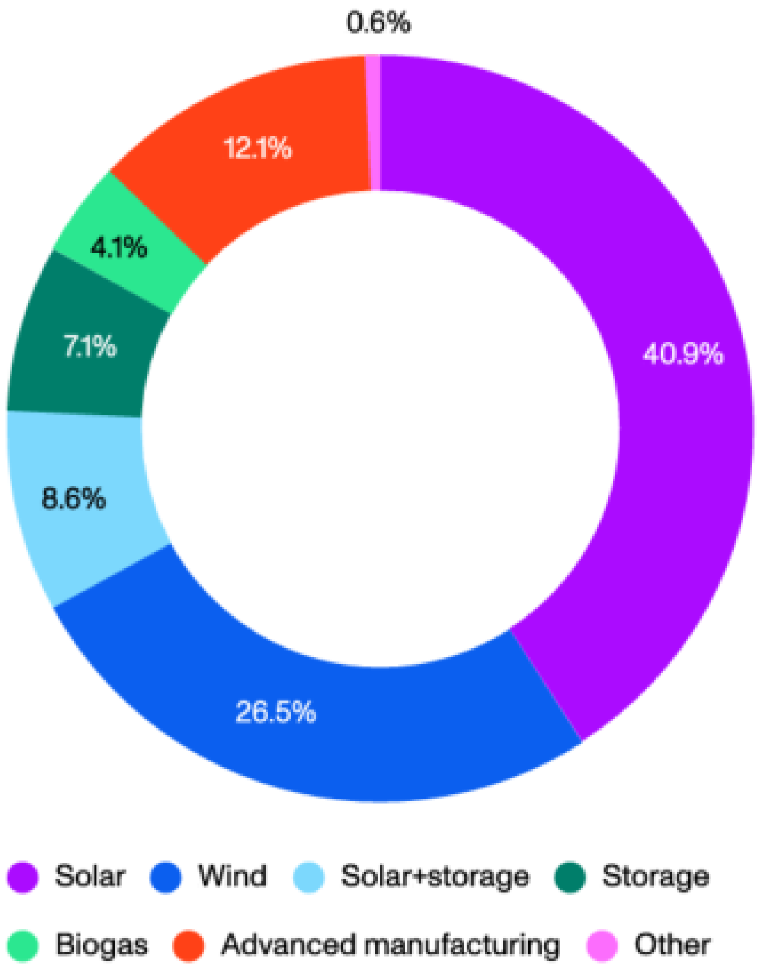
Tax Credit Market Snapshot

- **Demand for energy tax credit transfer deals** is projected to total between **$20 billion and $25 billion in 2024,** according to energy tax credit marketplace Crux. In the second half of 2024, Crux expects “significant growth in 45X advanced manufacturing, 45U nuclear credits and biogas credits” but noted “the supply of 2024 credits from utility-scale wind, solar and storage projects will likely become increasingly constrained.”

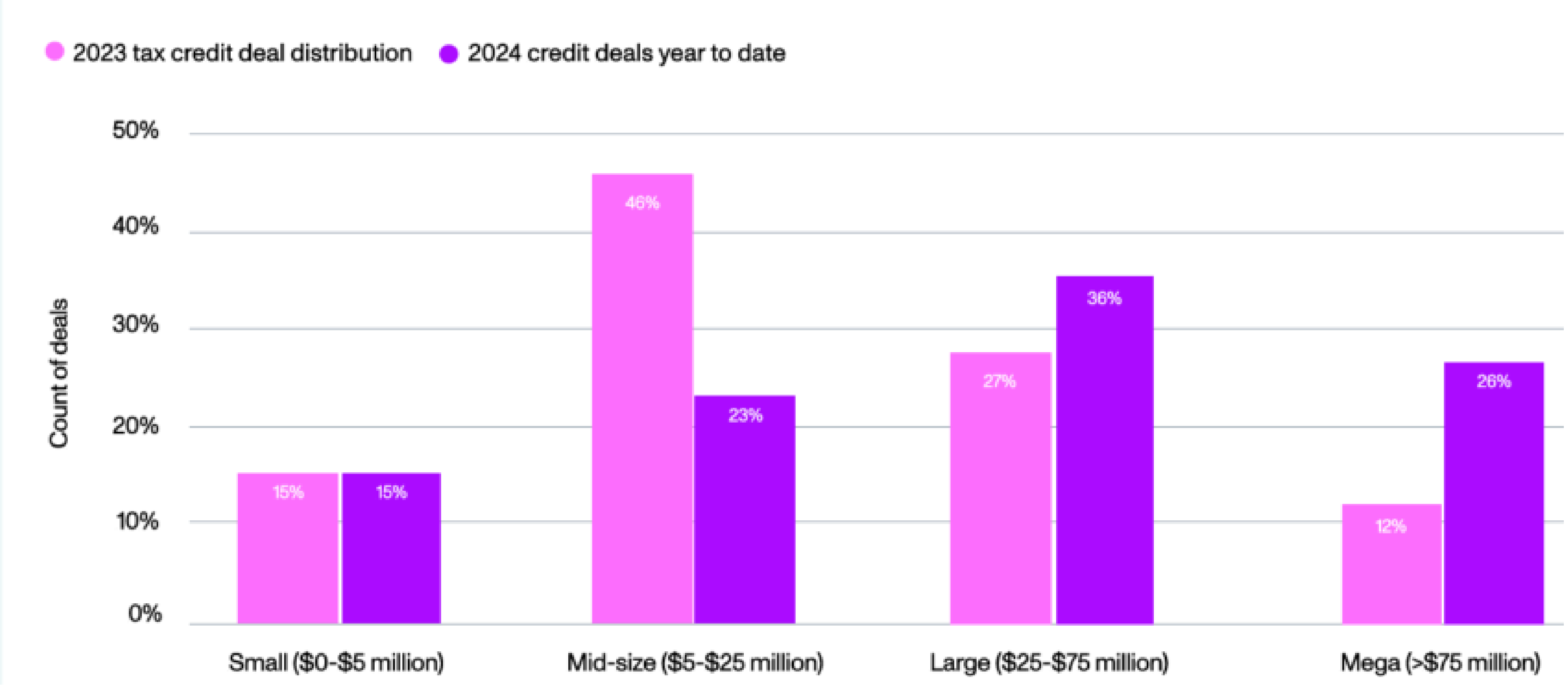
[Source: Crux Climate Inc., which operates a platform for buyers and sellers of the transferable tax breaks]

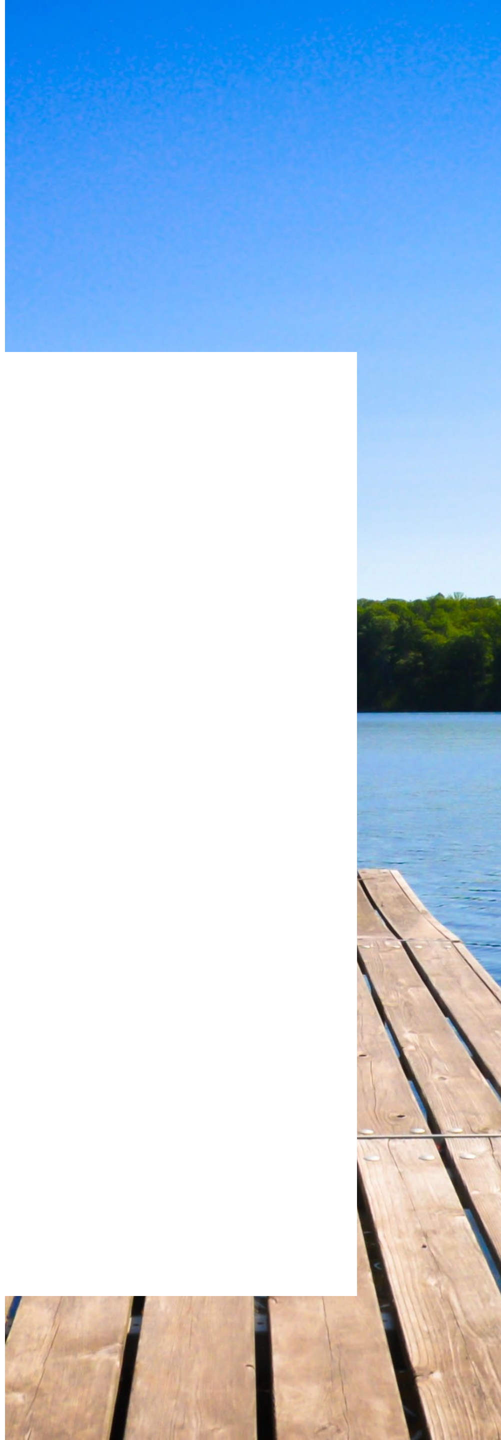
Figure 16. Share of transacted tax credits by technology type



Tax Credit Market Snapshot

Figure 17. Distribution of deals by size, sold year to date 2024 and full year 2023





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Virtual Power Purchase Agreements

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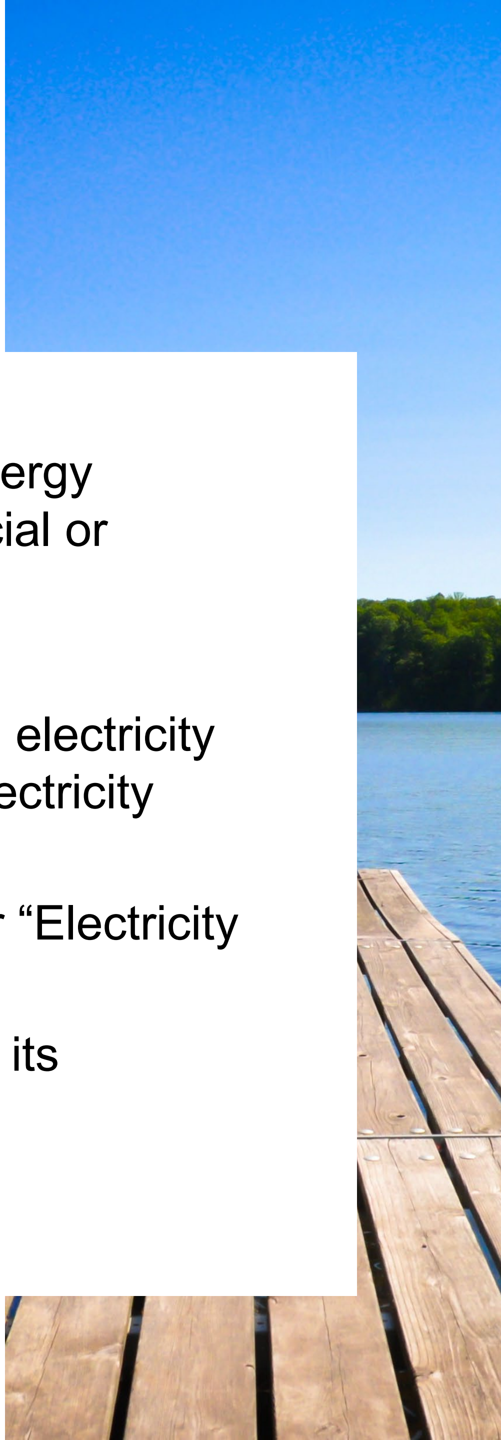
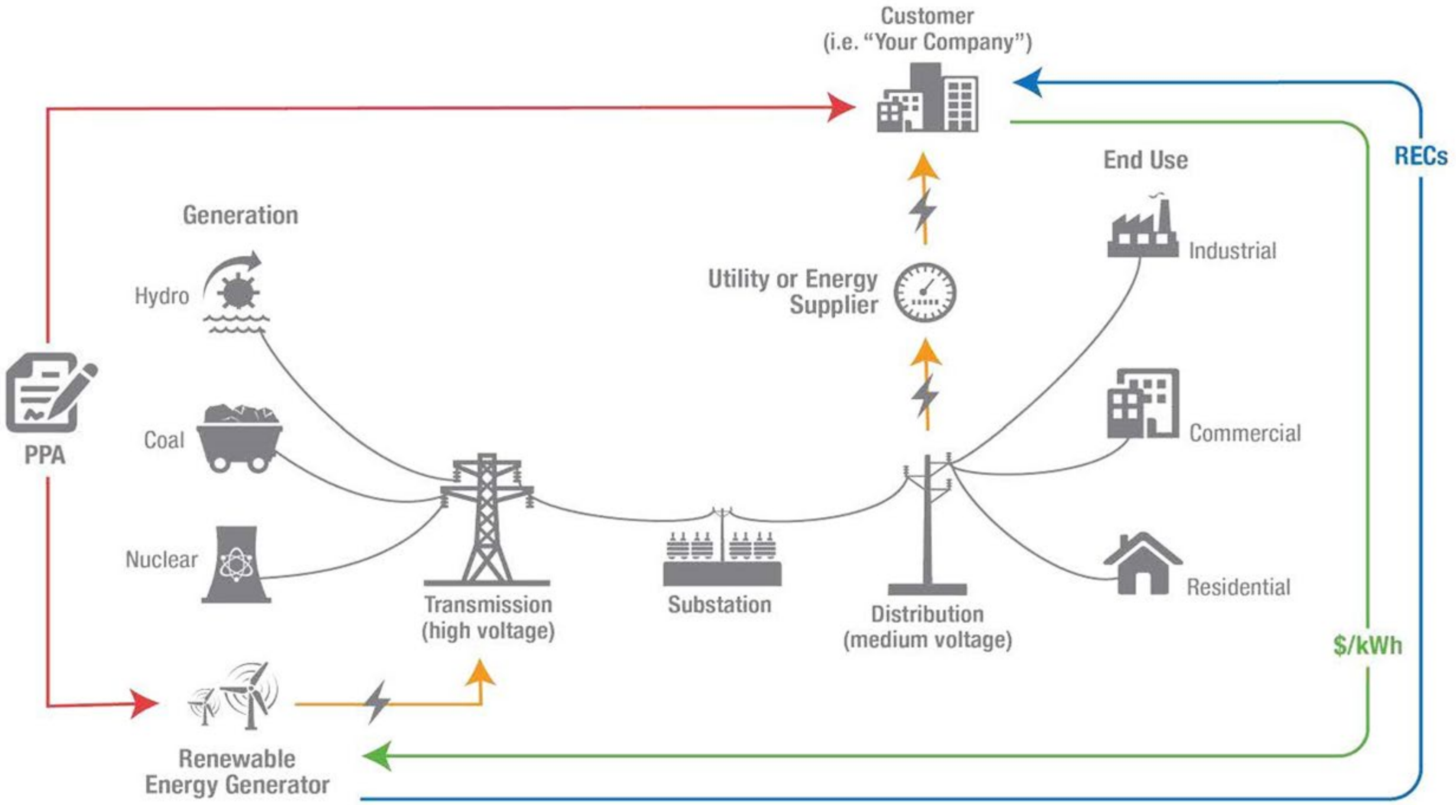
What is a Virtual Power Purchase Agreement?

- A Virtual Power Purchase Agreement (VPPA) is a contract for the “sale” of renewable energy between a project developer/owner (the Seller) and an offtaker, usually a large commercial or industrial user of power (the Buyer).
  - Most commonly used for wind and solar projects (the Project)
  - The Seller **does not** actually deliver electricity to the Buyer. Rather, the Seller delivers electricity **to the power grid** at a “point of interconnection” and the Buyer continues receiving electricity from its local utility.
  - Also known as a “Synthetic Power Purchase Agreement”, “Contract for Differences” or “Electricity Hedge Agreement”.
- Renewable Energy Credits (RECs) are delivered to the Buyer, who retires them to offset its consumption of non-renewable energy.



How Does a VPPA Work?



Source: U.S. Environmental Protection Agency, Green Power Partnership

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VPPA Pricing

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Settlement – Determining the price under the VPPA

- **Settlement** – The process for the parties to determine the net payment due from Seller or Buyer to the other. Typically occurs monthly.
- **Settlement Interval** – A short-term period used for each settlement calculation. Typically based on pricing intervals in the regional energy market. Often hourly.
- **Settlement Amount** – For each Settlement Interval, the difference between the Fixed Price and Floating Price, multiplied by the electricity generated by the Project.
  - Floating Price < Fixed Price → Buyer pays Seller the difference.
  - Floating Price > Fixed Price → Seller pays Buyer the difference.
- **Fixed Price** – A set price (set forth in the VPPA) upon which the parties agree to base their determination of the Settlement Amount for each Settlement Interval.
- **Floating Price** – The market price for electricity from time to time in a determined energy market. Often a real-time or day-ahead price at a certain trading hub.

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Renewable Energy Credits (RECs)

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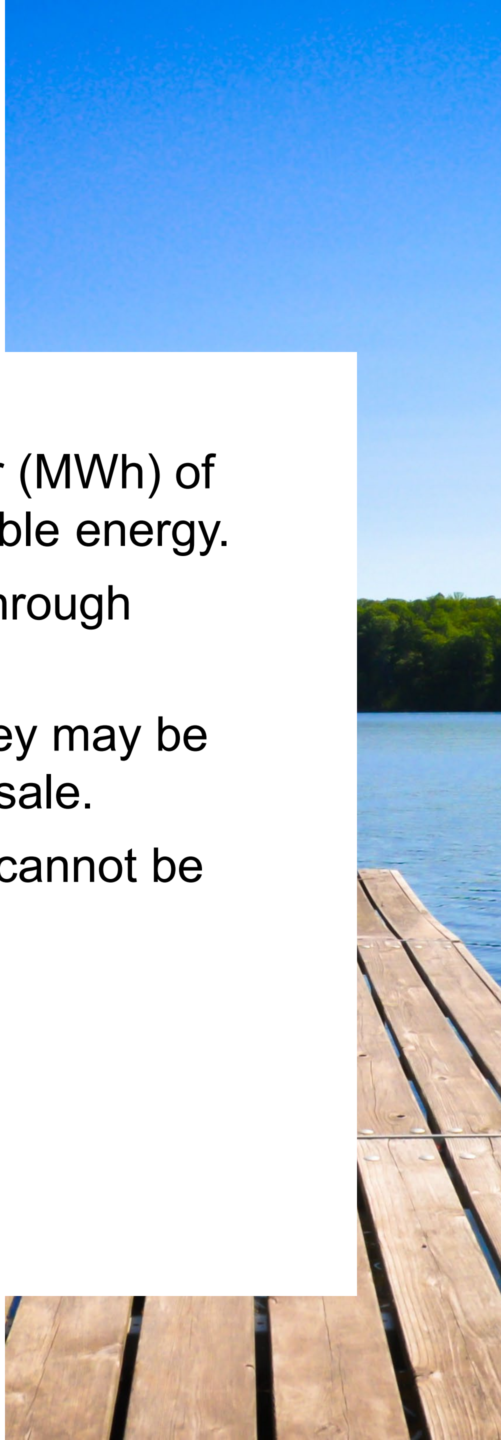
What are RECs?

- RECs represent a fixed quantity of renewable energy generation (often 1 megawatt hour (MWh) of electricity). They represent the environmental and other non-energy attributes of renewable energy.
- RECs are generated by qualifying, registered projects and are tracked and transferred through several regional tracking systems.
- The RECs sold under a VPPA may be the specific RECs generated by the Project, or they may be an equivalent number of similar RECs from other projects purchased by the Seller for resale.
- Companies “retire” RECs to achieve their sustainability goals. Once a REC is retired, it cannot be used again or transferred to another owner.



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Key Items to Consider for VPPAs

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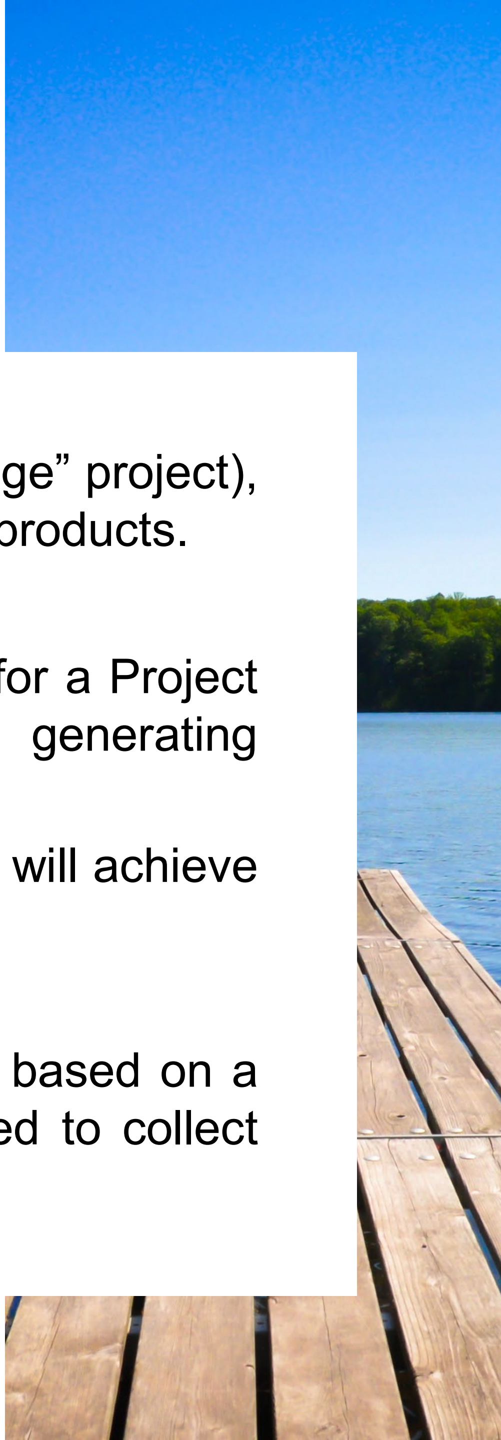
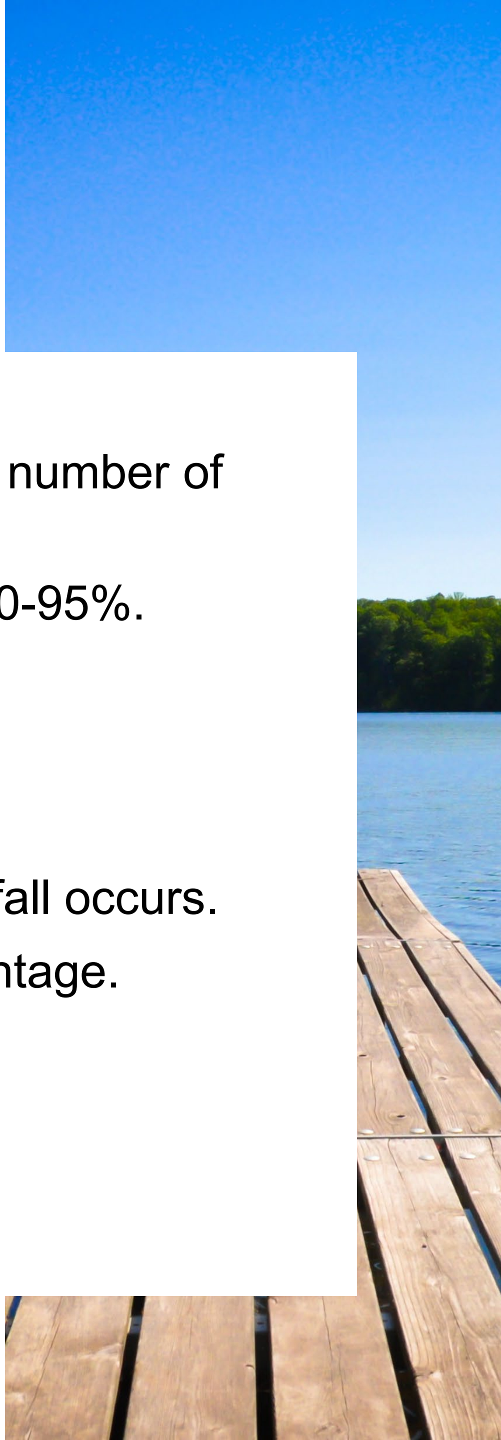
Project Development Timelines

- Once a site is selected and preliminary interconnection work is completed (an “early-stage” project), the developer will begin to seek offtakers for the Project electricity, RECs and any other products.
  – VPPAs are likely to be negotiated and executed at this stage.
- From the time that a VPPA is signed, the total development and construction timeline for a Project may be **2-4 years** before the Project achieves commercial operation and begins generating electricity and RECs.
  – Guaranteed Commercial Operation Date (GCOD): Seller guarantees that the Project will achieve commercial operation by a fixed date or period of time after signing the VPPA.
    - Usually subject to extension for force majeure events and interconnection delays.
  – Liquidated damages are payable for a limited period of time (often up to 180 days) based on a price per MW per day of delay. After the “outside” GCOD, Buyer is typically entitled to collect maximum liquidated damages and terminate the VPPA.



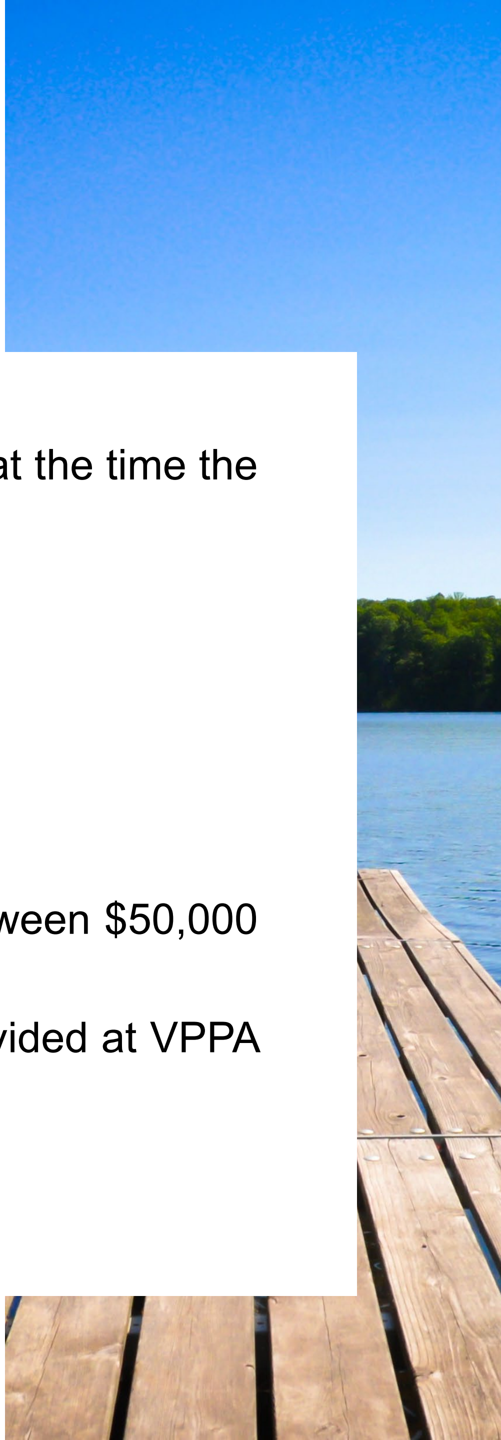
Availability Guaranty

- Seller guarantees that the Project will be ***available*** to generate electricity for a minimum number of hours rather than total amount of electricity generated.
  - Usually measured annually or biennially with a typical guaranteed availability rate of 90-95%.
    - Sometimes lower in the first year to account for start-up issues.
- Liquidated damages are typically payable for availability shortfalls.
  - **Simple**: Fixed dollar amount per 1% shortfall per MW of Project capacity.
  - **Complicated**: Based on Buyer's replacement cost for RECs at the time that the shortfall occurs.
- Buyer is usually entitled to terminate the VPPA if the availability falls below a floor percentage.



Credit Support

- The Seller is almost always a “project company” with few or no assets, and no source of revenue, at the time the VPPA is signed so Seller credit support is a key consideration.
  - Common forms of credit support are:
    - Cash collateral
    - Letter of credit
    - Parent guaranty
    - Payment and/or performance bond (uncommon for VPPAs)
- Amount of credit support depends on the value of the underlying contract, but are often set at between $50,000 and $150,000 per MW of Project capacity.
- Amount of credit support can vary over time but it is critical that the initial Seller credit support provided at VPPA signing is substantial.
- Buyer credit support may be required in the form of a parent guaranty in some instances.



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Thank You

Questions?

September 16, 2024

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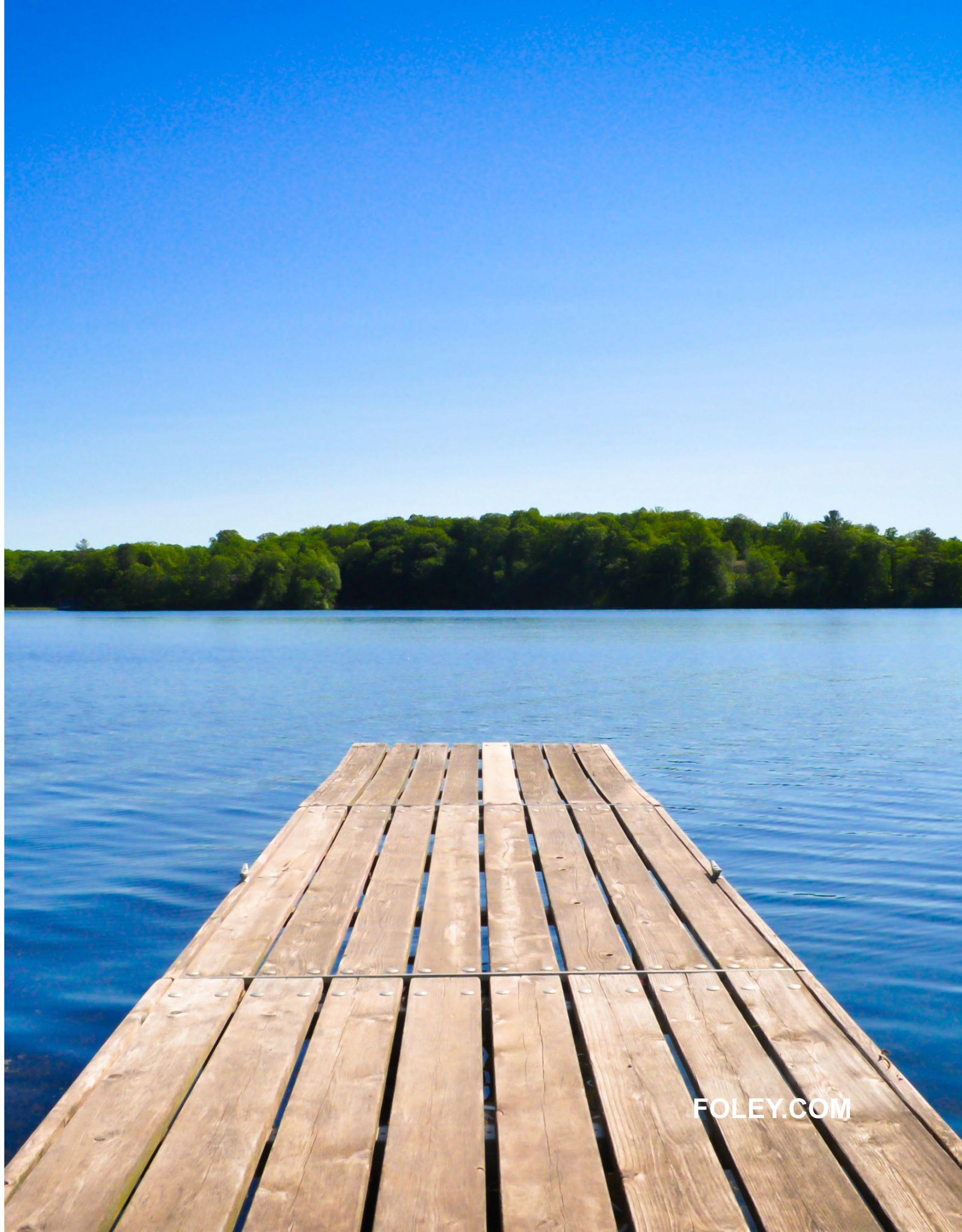

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