

PROJECT FINANCE

February 2006 -

North American Portfolio Finance Deal of the Year 2005

Invenergy: Green greenfield

The portfolio effect is usually, from a lender's perspective, viewed as a benefit to a financing. But for a sponsor looking to put together a financing for a greenfield wind portfolio, the portfolio effect can mean bringing together disparate construction schedules, working with multiple offtakers and contending with multiple regulatory regimes. All of this must be accomplished within the window afforded by the US production tax credit, which still underpins the economics of US wind projects.

Invenergy's Wind Finance Company (WFC) is the largest bank financing for a wind portfolio in the US to date, and the first fully greenfield construction financing for a wind portfolio. It demonstrates the challenges of portfolio financings, but also their benefits. It also launched the sponsor into the front rank of US wind developers.

Invenergy, based in Chicago, was formed in 2001, ahead of the implosion of the US power market, with a mandate to buy distressed power assets and develop wind projects. Its core personnel come from SkyGen, a cogeneration plant developer bought by Calpine. Before the WFC financing however, Invenergy's record consisted of the purchase of the 370MW Hardee thermal power station from TECO, and the development of the Buffalo Mountain wind project.

Buffalo Mountain was small – a 27 MW wind farm located near Oliver Springs, Tennessee, and financed in June 2004 through a \$31 million loan from Dexia Credit Local. But it introduced Invenergy to the lending community (and Aegon, which provided tax equity), and helped the sponsor develop skills in construction management and wind power purchase agreements.

And timing is everything. According to Jim Murphy, Invenergy's CFO, "one of the most difficult things to deal with for us was that we were counting on development of three separate projects to be concluded in time to construct those projects before 31 December 2005, and to arrange financing that would close before the commencement of construction." The 31 December date was, at that time, the date by which projects had to be installed by to be eligible for a production tax credit, a \$0.018 per kWh tax rebate.

The other looming challenge for developers is the current shortage of high-quality wind turbines. Suppliers, particularly the stronger ones such as GE, can demand upfront payments of up to 50% of the turbines' costs. To deal with these payments, Invenergy closed a \$77 million turbine acquisition loan with Dexia in April 2005, secured on the necessary turbines, as well as project company equity.

The portfolio encompasses three projects – Judith Gap, a 135MW project in Montana, Wolverine Creek, a 64MW project in Idaho, and Spring Canyon, a 60MW project in Colorado. The project uses 173 GE 1.5 MW SLE Wind Turbines. The assets' size and diverse locations allowed for a substantial portfolio financing, even though coordinating their construction schedules presented challenges.

The three projects have signed 20-year power purchase agreements with separate offtakers. Wolverine Creek sells power to PacifiCorp, currently being sold by Scottish Power to MidAmerican Energy, and Spring Canyon sells to Public Service of Colorado, part of Xcel Energy. PacifiCorp is presently Baa1/A- (Moody's/S&P) rated, and likely to improve if it becomes part of MidAmerican, and thus ultimately part of Berkshire Hathaway, and Xcel is rated Baa1/BBB.

Judith Gap's offtaker – Northwestern Corporation – presents more of a problem. Northwestern, recently emerged from Chapter 11 protection and is Ba2/BB rated. This below investment grade credit is not attractive to project lenders, and probably could not be financed on a standalone basis.

The portfolio effect, however, allows the other two projects to bolster the credit of the weaker one, and provide the lenders with comfort that the portfolio's cashflows will be sufficient to service senior debt. The assets' debt facility is provided to the WFC holding company, rather than to each project, thus eliminating any complex cross-collateralisation provisions.

The next phase of the financing was the closing of a construction and equity bridge loan, through Dexia and fellow lead arrangers HVB and HSH-Nordbank. The two loans total \$390.4 million – a \$219.6 million construction loan, a \$153.3 million equity bridge loan and \$17.5 million in letters of credit – and will be refinanced upon completion of the project. The equity bridge loan has limited recourse to the sponsor. The construction package closed in June 2005, and provided enough funding to bring the three projects to completion.

After the projects have been completed the three leads will replace the construction loan with a 15-year term loan, while the equity bridge is taken out using tax equity, again provided by Aegon. The tax equity partially monetises the tax credits to support the term loan, and features a flip structure, whereby Aegon receives the majority of the cash tax benefits up to a targeted return to the investor, at which point the developer realises more of the cash from the portfolio.

According to Murphy structuring the tax equity investment did not feature any novel legal or financial structures. He also notes that using a single funding vehicle minimised the associated legal and financing costs for the project.

The lead arrangers syndicated the debt down to Manulife, Allied Irish Banks, Bank of Scotland, Helaba, Natexis, Royal Bank of Scotland and SMBC. The term loan features a debt service coverage ratio of 1.45x, and is priced at 150bp over libor during construction and until the end of year three, 162.5bp years 4-6, 175bp years 7-9, 187.5bp years 10-12, and 200bp for the remainder of the loan's life.

US wind developers would like to escape the boom-bust cycles that short-term extensions to the tax credit cause. The present environment causes inefficiencies and makes long-term planning difficult. In the circumstances, though, the portfolio financing is likely to stay popular. As Murphy puts it "I think portfolio deals will be a popular financing approach since the wind resource is the biggest variable."

Invenergy Wind Finance Company

Status: Closed June 2005

Size: \$400 million

Location: Montana, Idaho and Colorado

Description: Construction financing for 259MW wind portfolio

Sponsor: Invenergy

Tax investor: Aegon

Lead arranger: Dexia Credit Local

Arrangers: HSH-Nordbank, HVB

Legal adviser to the lenders: Latham & Watkins

Legal adviser to the developer: Foley & Lardner (debt), Winston & Strawn (equity)

Independent engineer: RW Beck/Global Energy Concepts

Insurance adviser: Moore-McNeill