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PROJECT FINANCE IN THE UNITED STATES

Skadden partner David Armstrong, counsel Megan Kultgen and associate Kirsten Newman focus primarily on the representation of commercial and investment banks, as well as borrowers and issuers, in leveraged and other finance transactions, including project financings, acquisition financings, leveraged leases and other senior secured lending transactions, with a principal focus on the energy and industrial sectors.

GTDT: What have been the trends over the past year or so in terms of deal activity in the project finance sector in your jurisdiction?

"Activity in the oil and gas sector increased slightly in 2017, despite weathering the fourth year of the crude oil downturn."

Lawyers: Skadden's energy and infrastructure projects group advises clients on a broad range of project finance and other energy-related transactions in the United States, as well as in international markets. We will focus here on project finance transactions in the United States, as opposed to US investing and lending worldwide. According to IJGlobal, US project finance bank loans totalled approximately US$37.840 billion in 2017, which represented a 36 per cent increase from the US$27.722 billion of bank loan financings reported for 2016. Though globally the project finance loan market remained relatively stagnant, the United States saw a marked increase, with increased deal flow arising from a variety of factors, including overall economic growth in the United States and liquidity in the loan market fuelled by low interest rates and a continuing influx of commercial banks to the project finance arena. The term loan B market also saw an increase in 2017. Although figures for term loan B transactions vary based on publication (as a result of how certain publications categorise transactions), certain figures show that the total term loan B transactions completed in 2017 broke the US$5 billion mark, which would be a first since 2014. In addition to the increase in loan volumes, there was also an increase in the bond market. The US again led the globe in bond volume, completing approximately US$17.085 billion of project bond issuances (up from approximately US$15.321 billion in 2016). Institutional investors traditionally have played a large role in the secondary market, often as refinancing for commercial bank loans, but institutional investors have increasingly become comfortable assuming construction risk and funding merchant or quasi-merchant projects, resulting in an increased bond volume in 2017. Several hybrid bond-bank deals were completed in 2017, including financing for the AES Southland portfolio (as further discussed below).

Across all US project finance transactions in 2017, the oil and gas sector accounted for approximately 32 per cent of total transaction value (both debt and equity) by dollar volume (consisting of approximately US$24.5 billion of the total approximate US$75.8 billion deal volume), and the power sector accounted for approximately 56 per cent of the total transaction value (approximately US$42.7 billion of the total deal volume), with renewables accounting for approximately US$16.9 billion of that share, in each case as reported by IJGlobal. The transportation sector accounted for approximately 9 per cent of the total transaction value of US project finance transactions, with mining, social defence, telecom and water accounting for the remainder of all transactions. As in 2016, a deep field of commercial banks was active in the US project finance market.

The power sector saw the biggest increase over 2016 figures, with total deal volume by dollar value increasing by approximately 76 per cent and total transactions increasing from 79 to 116, according to IJGlobal. Though renewables accounted for a portion of this increase, the major growth was in the conventional power sector. That said, only approximately one-quarter of the conventional power transactions were primary financings, according to IJGlobal. Refinancings, additional facilities and acquisition financings comprised most of the activity in the conventional power market in 2017. Overall, according to IJGlobal, the total transaction value (both debt and equity) across sectors for primary financings actually decreased slightly in 2017 (down to US$31.4 billion from US$32.2 billion in 2016), while acquisition financings increased dramatically, both globally and in the United States (up approximately 130 per cent in the United States in 2017, accounting for US$13.7 billion of total transaction value, compared to US$5.9 billion in 2016). Although there continue to be new projects coming to market each year across sectors, a slowdown in initial financings could eventually begin to impact the secondary market in years to come.

Activity in the oil and gas sector increased slightly in 2017, despite weathering the fourth year of the crude oil downturn. As we saw in 2016, the days of the mammoth LNG and petrochemical projects seem to have passed for the time being, being replaced with a steadier stream of smaller projects, increasingly in renewables. New pipelines comprised the largest primary financing activity seen in the oil and gas sector in 2017; indeed, the Trans Mountain Pipeline expansion (discussed further below) was the third largest project finance deal in 2017 globally, according to IJGlobal. There was also continued activity in the secondary market from seasoned sponsors such as Cheniere Energy and Freeport LNG.

In the renewable energy sector, financing of solar and wind projects remained steady despite uncertainty regarding proposed tax reform, which clouded the outlook in those industries for a large portion of 2017. According to IJGlobal, despite this uncertainty, total deal volume for renewables increased by 2.4 per cent in 2017, representing US$16.9 billion of total transaction value, up

from US$13.6 billion in 2016. Ultimately, in the final version of the tax bill, production tax credits (PTCs) and investment tax credits (ITCs) were preserved, though the corporate tax rate was reduced to 21 per cent and a base erosion and anti-abuse tax (BEAT) was introduced which, as discussed further below, may limit multinational investors' ability to claim a portion of PTCs/ITCs. As a whole, the proposals which would have most seriously impacted the renewables sector were dropped from the final tax bill, so, while sponsors and investors will still likely need to reassess their investments in renewable assets and determine how best to optimise capital structures, the general consensus in the market is that renewables will remain attractive even after the tax reforms.

GTDT: In terms of project finance transactions, which industry sectors have been the most active and what have been the most significant deals to close in your jurisdiction?

Lawyers: While all project finance sectors generally saw growth in the United States in 2017, as mentioned above, the power sector had the most substantial increase, largely due to growth in the conventional power sector. Renewables increased slightly over 2016 figures despite tax reform, and there was modest growth in the oil and gas sector. In the transportation sector, though deal volume fell slightly as compared to 2016 based on total transaction value, the number of completed transactions increased from 8 in 2016 to 13 in 2017, according to IJGlobal.
Turning first to the power sector, AES Corp completed a US$2 billion financing (consisting of a US$1.475 billion bond and a US$492 million term loan) for its two combined-cycle natural gas-fired generation assets totalling 1.284GW and a 100MW battery storage facility, located in southern California, which was the largest power deal in the US in 2017. Though, in many ways, the AES Southland financing reflected a traditional project financing (including the two long-term (20-year) PPAs awarded to AES Corp. by offtaker Southern California Edison), the deal was one of several in 2017 that combined bank and bond debt, evidencing institutional investors increased willingness to expand into the primary financing market, including taking on construction risk. Several merchant deals were also financed in 2017, including the US$1.5 billion financing for the 1,100MW combined-cycle natural gas-fired Cricket Valley project in New York (sponsored by a group of six named investors including JERA, Advanced Power and Blackrock), which will sell power into NYISO. In addition, the Carlyle Group received a US$297 million loan to acquire, and provide working capital for, a portfolio of three simple-cycle natural gas-fired plants in Illinois, which sell power into the PJM market, and Ares-EIF received a US$337 million financing for the 450MW Birdsboro natural gas-fired plant in Pennsylvania, selling into PJM.

In the oil and gas sector, Cheniere Energy again topped the sponsor league tables for 2017 with US$6.4 billion across six transactions – three additional bond issuances for the Sabine Pass liquefaction facility totalling US$3.65 billion, an additional bond issuance for the Corpus Christi liquefaction facility for US$1.5 billion, a US$750 million revolving credit facility to be used by

Kirsten Newman

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Cheniere Energy to provide equity contributions for Corpus Christi, and a US$500 million equity commitment from EIG Global Energy Partners for development of the Midship pipeline in Oklahoma (another US$500 million will be contributed by Cheniere, for a total deal value of US$1 billion). The largest deal in the oil and gas sector, however, was the expansion of the Trans Mountain Pipeline, an oil pipeline running west from Edmonton, Alberta, Canada through British Columbia and into the U.S. state of Washington. Sponsored by Kinder Morgan, the approximate US$3.01 billion financing will be used to nearly triple the pipeline's capacity to 890,000 barrels per day. With a total deal value (both debt and equity) of approximately US$5.58 billion, the Trans Mountain Pipeline expansion was the third largest project finance deal globally in 2017 (IJGlobal).

In the transportation sector, the Virginia Interstate 66 PPP was the largest deal completed in the United States and the sixth largest transaction globally, according to IJGlobal. The total transaction value was approximately US$3.7 billion, consisting of US$1.97 billion of debt, divided across bonds and a Transportation Infrastructure Finance and Innovation Act (TIFIA) loan. Sponsored by a consortium of equity investors led by Meridiam and Cintra, the financing will be used for the widening of 40 kilometres of I-66 to include three regular lanes and two express lanes in each direction. Other significant PPPs in 2017 included the US$1.5 billion Moynihan Train Hall (part of broader renovations and updates to New York City's Penn Station), sponsored 50/50 by The Related Companies and Vornado Realty Trust, and the US$913.2 million reconstruction of Interstate 70 in Colorado, sponsored 60/40 by Meridiam and Kiewit Development Company.

As discussed above, tax reform was a looming concern for the renewable energy sector in 2017, but, despite this, investment in renewables remained steady. As in 2016, interest in yieldcos remained low and two prominent yieldco sponsors signed deals in early 2017 to sell their yieldco investments. NRG Energy agreed to sell its yieldco, NRG Yield, to Global Infrastructure Partners as part of a broader sale of NRG's entire renewables platform, for a total sale price of US$1.375 billion. First Solar and SunPower Corp, owners of yieldco 8Point3, also agreed to sell, striking a deal with Capital Dynamics for US$977 million. Other notable transactions in the renewables sector in 2017 include ArcLight Capital Partners' US$1.065 billion acquisition of TransCanada's New England hydroelectric portfolio, comprised of 13 facilities with a total generation capacity of 584MW, and sPower's US$421.4 million private placement financing of its US solar and wind portfolio, comprised of 39 solar farms and 2 wind projects with a total generation capacity of 565.2MW (as further discussed below).

Finally, residential and small commercial and industrial solar developers have continued to find creative ways to finance transactions that would otherwise be too small to interest the large commercial banks that are accustomed to utility-scale power and project finance transactions. For example, many of these developers, including SolarCity, Vivint Solar and others, have been able to take advantage of both economic and

> *"The US energy and infrastructure sector features a broad range of both domestic and international investors and sponsors."*

geographic scale to form tax equity funds with investors, which house residential or small commercial and industrial solar projects. The total investment by tax equity investors in these transactions, which customarily take the form of several tranches before projects reach operations, is typically in the US$50 million– US$100 million range.

GTDT: Which project sponsors have been most active in driving activity? Which banks have been most active in providing debt finance?

Lawyers: The US energy and infrastructure sector features a broad range of both domestic and international investors and sponsors. According to IJGlobal, Arclight Capital Partners (a domestic private equity firm focused on the energy and infrastructure sector) led all project finance sponsors in 2017, with a total deal volume of approximately US$6.5 billion spread across nine transactions. Fitting with the trends noted above, six of Arclight's nine deals were a refinancing or additional facility and two were acquisitions, with only one primary financing (a US$160 million financing for the approximate 139MW Leeward wind portfolio in Nolan County, TX). One of Arclight's most prominent transactions of the year was the acquisition, in partnership with Blackstone, of four natural gas-fired power plants in Ohio and Indiana, comprising 5,200MW of generating capacity, from AEP. The US$1.825 billion financing was divided across a US$1.575 billion term loan B, US$150 million term loan C and US$100 million revolver, with the Arclight/Blackstone partnership providing US$723 million in equity. Cheniere Energy was the second-largest sponsor by deal volume in 2017 with US$6.4 billion across six transactions. The third-largest sponsor was Kinder Morgan with a total deal volume of US$5.76 billion, namely due to its expansion of the Trans Mountain Pipeline. Blackstone and Dynegy rounded out the top five sponsors with US$3.89 billion and US$3.3 billion in deal volume, respectively. In addition to Blackstone's role in the acquisition of the AEP portfolio, Blackstone partnered with Sanchez Energy Corporation to acquire 155,000 net acres in the Western Eagle Ford shale in Texas, utilising a US$1.163 billion financing. Finally, Dynegy's place in the league tables was due to its acquisition of ENGIE's 9017MW US fossil fuel portfolio, increasing Dynegy's generating capacity by approximately 35 per cent. The US$3.3 billion deal was financed through a US$2.2 billion term loan C and approximately US$1.1 billion in equity (US$150 million of which was from a sale of Dyneygy's common stock to Energy Capital Partners, with whom Dynegy had originally intended to acquire the portfolio).

International sponsors ranking high in the league tables included Spanish infrastructure company Ferrovial (a sponsor of the Virginia I-66 PPP through its subsidiary, Cintra), Chinese chemical company Shandong Yuhuang (sponsor of the US$1.5 billion Yuhuang methanol plant in Louisiana), and French utility company ENGIE (a sponsor of the US$1.165 billion Ohio State University utility and energy supply systems lease, and sponsor, through its subsidiary Solairedirect SA, of the US$35.2 million Solaire Holman solar PV plant in Texas).

In the renewables space, NextEra Energy again led the charts with approximately US$1.67 billion in deal volume, consisting of a US$826 million extension and upsizing of the financing for the Silver Slate solar facility, a US$566.3 million extension and upsizing of the financing for the McCoy solar facility, a US$143.62 million initial financing for the 196MW Indigo Plains solar portfolio, and a US$134.75 million initial financing for the 177.5MW Longleaf solar portfolio. Capital Dynamics and Arclight Capital Partners were a close second and third, with US$1.6 billion and US$1.2 billion in deal volume, respectively. Other traditional players in the renewable energy markets, such as SolarCity in residential solar, have continued to play a large role in renewable energy development. In the traditional power sector, several seasoned sponsors remained active in the market, including LS Power, which closed a US$325 million financing for the development and operations of a portfolio of two natural gas-fired projects in PJM.

Among the commercial banks involved in US project finance, Mitsubishi UFJ Financial Group (MUFG) continued to lead the market, with over US$2.89 billion in transaction volume spread across 37 transactions, according to IJGlobal. Rounding out the top 10 most active banks in commercial bank loans were Morgan Stanley, Deutsche Bank, Goldman Sachs, Royal Bank of Canada, Crédit Agricole Group, Sumitomo Mitsui Financial Group, Santander, JPMorgan and Bank of America. Several of these banks were arrangers on the most significant transactions of 2017. For instance, a syndicate of over 20 banks, including MUFG, Bank of America, JPMorgan, Sumitomo and several other large banks involved in US project finance were involved in the Trans Mountain Pipeline project financing, and a syndicate of 19 banks, including many of the same players (MUFG, JPMorgan, Citibank and Société Générale, among others) participated in the financing of the AES Southland portfolio. All of the major banks participating in the project finance market in 2017 were involved in a broad variety of deals across the oil and gas, power and infrastructure sectors. The large US insurance companies, pension funds and institutional investors are also active in the project bond market, both in Rule 144A/Reg S transactions and in more traditional private placements, and institutional investors provide capital for the term loan B market, which saw a slight increase in activity in 2017 over years past.

GTDT: What are the biggest challenges that your clients face when implementing projects in your jurisdiction?

Lawyers: While the United States is a mature project finance market, the energy and infrastructure sectors in which project finance is most prevalent have been heavily regulated and have become increasingly complex in recent years. The power, renewables, and oil and gas sectors all must navigate multifaceted regulatory structures, existing at the federal, state and local levels of government. That said, as discussed in more detail below, the proposed changes in legislation and regulatory policy promulgated by the Trump administration have, in certain instances, led to an attempt at reducing and streamlining federal regulations. For example, in March 2017, as part of the Trump administration's 'America First Energy Plan', President Trump signed the executive order 'Promoting Energy Independence and Economic Growth', which requires all federal agencies to review and revise or revoke regulations that burden domestic energy production. In response to this, several federal agencies have already issued rules and recommendations seeking to repeal Obama-era regulations, including regulations governing carbon and greenhouse gas emissions for fossil fuel-fired generation units and oil and gas source performance standards.

However, while certain federal regulatory roll-backs have already begun, several have been only temporary suspensions and others have been (and are expected to be) challenged through the courts. Beyond this, though federal regulations may be repealed, similar regulations

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at the state and local levels may remain in place, and, in response to federal repeals, certain states have recently proposed or enacted regulations on the same issues for which federal regulations have been revoked. California appears poised to be at the forefront of this, last year enacting new regulations curbing methane release during the production and transportation of natural gas, signing a deal with China to lower greenhouse gas emissions, leading an alliance of other states, cities and businesses vowing to fulfil the Paris Climate Accord despite the federal government's withdrawal, and hiring former US attorney general, Eric Holder, to represent the state in potential legal battles against the federal government.

As a result, the proposed federal regulatory roll-backs, and corresponding reactions from state and local governments, may lead to greater uncertainty for sponsors and investors, and may not serve to lessen any bureaucratic red tape. Indeed, it may increase complexity for investors, with increasing variation in standards and regulations across states.

GTDT: Are there any proposed legal or regulatory changes that may give rise to new opportunities in project development and finance? Do you believe these changes will open the market up to a broader range of participants?

Lawyers: In the lead-up to the finalization of the act commonly referred to as the Tax Cuts and Jobs Act of 2017, which was signed by President Trump into law on 22 December 2017 (the Tax Act), there was widespread speculation that the Tax Act would include changes to the existing tax credits for renewable energy; ultimately, however, the tax credits were left in place in the final legislation (and the two-year budget deal signed by President Trump on 9 February 2018 (the Two Year Budget) clarified that certain orphaned tax credits for fuel cells, combined heat and power and small-scale wind projects for which construction began by the end of 2017 will regain their ITC eligibility). Nevertheless, the implementation of the Tax Act will impact what opportunities are available in project development and finance generally in 2018. The Tax Act creates a single corporate tax rate of 21 per cent, reducing the highest corporate tax rate from 35 per cent, and implements a base erosion and anti-abuse tax (BEAT), which is designed to limit tax planning strategies where large companies were previously able to move taxable profits made in one country to another country with lower or no taxes. Although the BEAT is not aimed specifically at renewables or renewable energy tax credits, it may impact the value of tax credits to the extent that a taxpayer is limited in applying the value of renewable energy tax credits against the BEAT. The extent to which this will impact tax equity investors will depend on how much BEAT the investor projects it will have to pay in a year in which it plans to claim tax credits. The BEAT functions like an alternative minimum tax and in determining BEAT liability, the value of the renewable energy tax credits is decreased by 20 per cent, reducing their value for taxpayers subject to the BEAT. This calculus will make investment decisions more complicated for some potential tax equity investors and may impact the capital stack for new solar and wind deals going forward.

Additionally, in January 2018, President Trump approved a 30 per cent tariff (which will decline by 5 per cent each year over a four-year span) on imported crystalline silicon photovoltaic cells and modules (which are key components for solar panels), with the first 2.5GW of imported cells excluded from the additional tariff. Despite this change and an outcry from solar executives as to the dampening effect it could have on the solar industry, the US solar market is expected to continue to thrive in 2018. GTM Research predicts the US will install approximately 10GW of new solar this year. Currently, the US has around 50GW of installed solar capacity and is in line to more than double that total over the next five years.

While solar power generation remained one of the more active industries within the US project finance market in 2017 and appears poised to continue as such in 2018, the domestic natural gas market has begun to expand. US natural gas production capabilities have grown and we expect such development to continue, positioning the US as a significant exporter of gas, which coincides with an increased global appetite for LNG. This environment has led to greater domestic investment in facilities that convert natural gas to LNG. While, in recent years, the Department of Energy (DOE) has issued a final decision on a very small percentage of the applications for approvals for LNG export to countries that do not have a free trade agreement (FTA) with the US, thereby limiting the number of countries and customers to which LNG exporters can sell their product, the Trump administration has articulated its support for developing and expanding the industry and, correspondingly, the DOE has approved two long-term applications to export additional LNG from the Lake Charles LNG project in Louisiana to non FTA-countries. Furthermore, Congress has introduced two bills to expedite the LNG-export approval process, which are currently under discussion. Regulatory change would help the US achieve the US Energy Information Administration's prediction that the US will have the third-largest LNG export capacity in the world after Australia and Qatar by 2020.

Another noteworthy change has been President Trump's support of the Dakota Access Pipeline and TransCanada Keystone Pipeline and issuance of executive orders seeking to expedite environmental reviews and approvals for high priority infrastructure projects, as well as to promote energy independence and economic

growth (including the reversal of a number of climate and clean energy initiatives, the opening of areas of federal waters, including the Outer Continental Shelf, to energy exploration and production, and an overturn of a moratorium on new coal leases on federal lands). In addition, President Trump's administration has withdrawn from the Paris Climate Agreement (the earliest possible effective date of which would be November 2020) and is seeking public comment as part of a formal process to replace the Clean Power Plan, which mandated a 32 per cent reduction in carbon emissions from existing power plants by 2030 and specific goals for states to decrease use of coal-fired electricity generation and increase reliance on renewable energy and natural gas. The impact of these changes remains to be seen. In the meantime, however, fifteen states and Puerto Rico have joined together to form the United States Climate Alliance and have pledged to uphold the objectives of the Paris Climate Agreement. A number of states have also adopted energy plans to comply with the targets of the Clean Power Plan, regardless of its ultimate legal status.

Although the renewable energy sector continues to thrive and the renewable energy tax credits remain in place, the administration continues to show a preference for supporting fossil fuels and nuclear energy. Energy Secretary Rick Perry has argued that coal and nuclear generation play a critical role in maintaining the reliability and resiliency of the nation's energy grid. As such, the DOE put forward the Grid Resiliency Pricing Rule (the Rule), which would have pushed coal-fired and nuclear generation into a more advantageous market position by providing cost recovery to coal and nuclear power, allowing these power sources to compete more effectively with renewable and natural gas-fired generation. However, in January 2018, FERC rejected the Rule and has ordered a new process seeking more information from grid operators as to whether there is a resiliency issue and what should be done about it. The nuclear industry did benefit directly, however, from the Two Year Budget, which lifted a 2021 in-service deadline for nuclear projects to be eligible for a production tax credit.

Finally, on 23 May 2017, the White House's Office of Management and Budget released a proposed US$4.1 trillion 2018 Budget: A New Foundation for American Greatness (the 2018 Proposed Budget). Highlights of the 2018 Proposed Budget relevant to the DOE include a decrease of US$1.7 billion to the DOE's budget, provision of US$280 million for the Office of Fossil Energy to 'focus on cutting-edge fossil energy research and development, advance domestic energy production, support innovative clean coal technologies and strengthen our energy security' and a reduction in half of the Strategic Petroleum Reserve through a decade of sales. The 2018 Proposed Budget includes a 31.4 per cent

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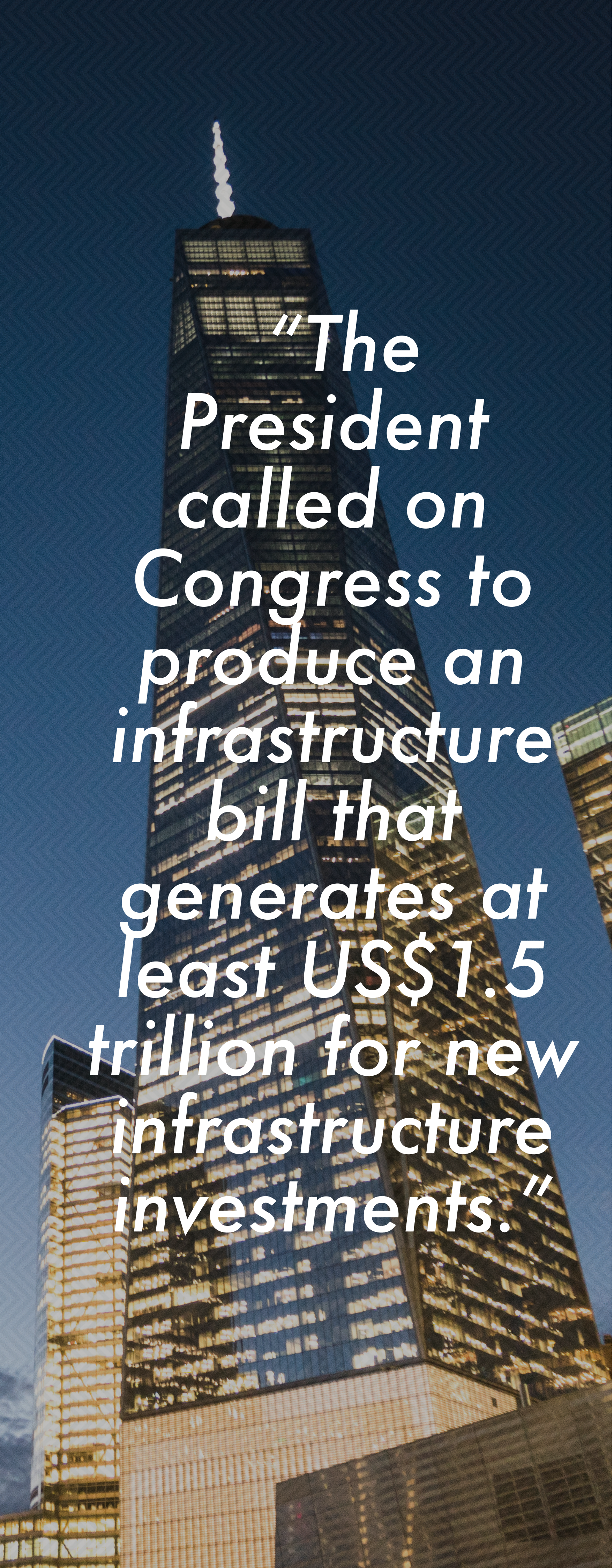

> "The President called on Congress to produce an infrastructure bill that generates at least US$1.5 trillion for new infrastructure investments."

reduction to the budget of the Environmental Protection Agency (EPA), which is the largest percentage funding decrease of any agency under the 2018 Proposed Budget. The Department of the Interior (DOI) received a 10.9 per cent decrease to its budget, but received US$791 million to boost US energy production and amounts to support onshore oil and gas permitting, offshore production efforts and oil and gas leases in the Arctic National Wildlife Refuge beginning in 2022. While many departments saw reductions to their budgets, one of the 2018 Proposed Budget's key spending priorities is support for US$1 trillion in private and public infrastructure investment. The 2018 Proposed Budget included a request for US$200 billion over 10n years, beginning with US$5 billion in 2018.

As a follow-up to the 2018 Proposed Budget, in President Trump's 30 January 2018 State of the Union address, the President called on Congress to produce an infrastructure bill that generates at least US$1.5 trillion for new infrastructure investments. Then, on 12 February 2018, the White House issued an outline of its plan for federal infrastructure policy entitled "Legislative Outline for Rebuilding Infrastructure in America" (the Infrastructure Plan). In line with the 2018 Proposed Budget, the Infrastructure Plan included spending US$200 billion of federal funds to spur state, local and private investment. Of the US$200 billion, 50 per cent of the total appropriations will be used to create an Incentives Program that would provide grants (of no more than 20 per centof required new revenue) based on established criteria to encourage infrastructure investment (in surface transportation and airports, passenger rail, ports and waterways, flood control, water supply, hydropower, water resources, drinking water facilities, wastewater facilities, stormwater facilities and Brownfield and Superfund sites) and accountability, with federal funding conditioned on meeting certain milestones. 10 per cent of the total appropriations will be allocated to expanding existing infrastructure programs (including TIFIA, the Water Infrastructure Finance and Innovation Act, the Railroad Rehabilitation and Improvement Financing program and the Department of Agriculture Rural Utilities Lending Programs) and broadening the use of private activity bonds. Ten per cent of the total appropriations will be made available to a Transformative Projects Program that, according to the Infrastructure Plan, is focused on 'ambitious, exploratory, and ground-breaking project ideas that have significantly more risk than standard infrastructure projects, but offer a much larger reward profile' and would include, but not be limited to, the transportation, clean water, drinking water, energy, commercial space and broadband sectors. Additionally, 25 per cent of the total appropriation is allocated to developing a new Rural Infrastructure Program to rebuild and modernise infrastructure in rural US communities. The Infrastructure Plan also sets forth a proposal

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THE INSIDE TRACK

What three things should a client consider when choosing counsel for a complex project financing?

First, clients should consider breadth of expertise. In addition to project finance capability, complex financings often require tax, real estate, environmental, regulatory, cross-border and intellectual property specialists, to name a few. Thus, it is imperative that the firm has wide-ranging experience. Secondly, specific industry knowledge and understanding of the core business are important. This applies on the lender side (where designing covenants to address industry-specific risks is essential) and on the sponsor side (where ensuring the company has flexibility to run its business effectively is a must). Finally, clients should consider whether the firm's style aligns with the client's approach to the transaction.

What are the most important factors for a client to consider and address to successfully implement a project in your country?

While it is difficult to narrow the factors in a market as diverse as the United States, we consider the following to be among the most important: knowledge of, and adequate legal counsel in respect of, regulations at all levels (federal, state and local) applicable to the project; adequacy of funds to support project development, particularly given the long lead time in many industries; understanding of the debt market in which the project is expected to be financed, and structural considerations to ensure that risks associated with that project will be financeable; and tax considerations, to ensure the project achieves optimal tax savings.

What was the most noteworthy deal that you have worked on recently and what features were of key interest?

One noteworthy transaction we have worked on recently is representing Citigroup Global Markets, Inc, as lead placement agent, and Credit Agricole Securities (USA) Inc, KeyBanc Capital Markets Inc, Rabo Securities USA Inc, SG Americas Securities, LLC and Wells Fargo Securities, LLC, as co-placement agents, in connection with the 4(a)2 private placement of US$421.4 million of senior secured notes issued by an indirect subsidiary of FTP Power LLC (doing business as sPower), and Coöperatieve Rabobank UA, New York Branch and Wells Fargo Securities, LLC, as joint lead arrangers, and Coöperatieve Rabobank UA, New York Branch and Wells Fargo Bank, National Association, as issuing banks, in connection with a related US$100 million letter of credit facility. The proceeds of the notes were used to finance the operations of a portfolio of 39 solar and two wind generating facilities (which were grouped in nine existing tax equity funds) and to refinance three back-leverage debt facilities in place for the construction and early operations of many of the facilities. The letters of credit issued under the letter of credit facility support collateral and reserve obligations of the relevant sPower subsidiaries. The facilities are located in seven states across the U.S. and total 475.6MW AC/565.2MW DC in aggregate capacity. The transaction was awarded Americas Renewables Deal of the Year for 2017 by Project Finance International.

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to establish authority to allow for the disposal of federal real property and the creation of a Federal Capital Financing Fund to address inefficiencies in the current process related to appropriations for real property purchases. Finally, the Infrastructure Plan delineates an approach whereby revenues generated from energy development on public lands would be applied to a new Interior Maintenance Fund that will be used to pay for capital and maintenance needs of public lands infrastructure. To the extent this program moves forward, it will generate a number of new opportunities for developers, investors, lenders and other providers of capital to the industry. There is concern, however, on both the Democratic and Republican sides of Congress as to how feasible the plan is and how it will be financed. Furthermore, the timing of implementation of any such plan remains up in the air, in particular in the wake of the signing of the Two Year Budget, which could increase deficits past the US$1 trillion mark by 2019. As such, it is not clear whether the administration's plans will result in any actual opportunities in the near term.

GTDT: What trends have you been seeing in terms of range of project participants? What factors have influenced negotiations on commercial terms and risk allocation? Are there any particularly innovative features?

Lawyers: As mentioned, according to IJGlobal, US project finance loan volumes increased by 36 per cent to US$75.830 billion (across 159 transactions) in 2017 from US$56.934 billion (across 105 transactions) in 2016. This increase in activity was consistent across the oil and gas, renewables, conventional power and mining/social defence/telecom/water industries, with only the transportation industry showing a decrease in dollar value as compared to 2016-levels. Furthermore, on the lending side, the sources and structures of funding remained diverse across all industries in the project finance space. In 2017, the total number of commercial bank finance deals in the US was US$37.840 billion (across 122 transactions), up from US$27.722 billion (across 93 transactions) in 2016, according to IJGlobal. Similarly, the number of bond financed deals was US$17.085 billion (across 38 transactions) in 2017,

> *"Historically, the inverted lease structure has been more attractive than the partnership flip in a scenario where owner-level debt is contemplated."*

up from US$15.321 billion (across 28 transactions) in 2016, according to IJGlobal.

Perhaps the greatest determinant of commercial terms and risk allocation in US project finance is the lending market in which a particular project is being financed. For instance, in commercial bank transactions, the covenant packages and deal structures tend to be tighter than in term loan B and Rule 144A/Reg S project bond transactions. Among the rationales for this distinction is that amendments and waivers are more manageable in commercial bank transactions because of the traditionally closer relationship between sponsors and commercial bank lenders. Accordingly, although covenants may be tighter, sponsors believe that they have greater flexibility to seek amendments and waivers to such covenants. Commercial banks also tend to have less appetite for risk than term loan B lenders (which is reflected in the rates and fees paid by borrowers in each of those markets), which results in riskier projects (including less sponsor support, increased merchant risk and heightened technology, permitting or other risks) being financed in the term loan B or high-yield bond markets.

Given the breadth of the US project finance market, it is difficult to discuss with any specificity the innovative structures and relevant risk allocations being used and applied. Instead, we will focus for illustrative purposes on the solar industry and the diversity of debt and equity activity seen in the market in 2017. In 2017, solar tax equity remained a popular revenue generating approach, with partnership flips and inverted (or pass-through) leases continuing to provide a consistent source of tax equity investment into the solar space. In a partnership flip, the solar developer and the tax equity investor form a joint venture and the allocation of upside (profits, cash, tax benefits) flips between the parties during the life of the investment. With an inverted lease, the solar developer leases projects to the tax equity investor and assigns its rights under the power purchase agreement and related agreements to the investor, who then contracts the servicing of those projects back to the solar developer or its affiliate. Historically, the inverted lease structure has been more attractive than the partnership flip in a scenario where owner-level debt is contemplated, as a foreclosure on a project owned by a partnership flip during the ITC recapture period would result in recapture, so tax equity investors would typically seek complete forbearance from the lenders. In contrast, a foreclosure on a project owned by a lessor in an inverted lease during the recapture period results in recapture only if the project is transferred to a disqualified person, so investors seek a limited forbearance, which has been viewed more favourably by lenders in the market.

In addition to the activity in the tax equity market, we saw back-leverage debt facilities put into place to fund construction costs and early operations of solar projects. In addition, we saw initial inroads into the 4(a)2 private placement market (discussed more fully below) for solar financing, the proceeds of which are being used to fund operating expenses of existing projects and to refinance underlying debt facilities.

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Furthermore, the number of successful solar securitisations completed in 2017 increased from those that closed in 2016. The partnership flip, however, remains a more challenging structure for securitisations. While some of the risk in the partnership-flip structure can be mitigated by the introduction of insurance to cover tax basis risk, which arguably could make investors more comfortable in opening themselves up to another risk-foreclosure exposure (particularly as with basis risk covered by insurance instead of the sponsor interest in the partnership indemnifying for that risk, more money remains in the system and lessens the chance of default on debt (therefore indirectly mitigating foreclosure risk)), this remains a less popular securitisation structure.

We expect solar securitisations, which bundle and sell loans for distributed solar projects to investors, to gain further momentum as the newest financial product to dominate at least the residential solar market. In a solar securitisation, a bankruptcy-remote special purpose entity is used to combine thousands of rooftop solar projects and the monthly cash flows related thereto. The special purpose entity issues new debt securities based on these cash flows and investors buy the securities and receive interest payments. Furthermore, to satisfy the Security Exchange Commission's newly applicable credit risk retention rules, the originator, either directly or through a majority-owned affiliate, must retain a membership interest in the issuer, known as 'horizontal' risk retention, or in each class of assets issued, known as 'vertical' risk retention (or a combination thereof). In the early stages, SolarCity/Tesla dominated the solar securitisation market; however, with SunRun, Mosaic, Sunnova and Dividend Finance all successfully completing solar securitisations, it is clear that other players are interested in and capable of entering the field. There are also additional players who have completed property assessed clean energy securitisations. The increase in solar loan securitisations is tied to a shift from third-party owned systems to customer-owned systems, which trend we expect to continue.

GTDT: What are the major changes in activity levels or new trends you anticipate over the next year or so?

Lawyers: With the implementation of the Tax Act, the rollback of the Clean Power Plan, the tariff on imported crystalline silicon photovoltaic cells and modules and the nascent stages of the Infrastructure Plan, there is still a great deal of uncertainty in the US project finance market.

As previously noted, however, the US solar market is expected to continue to thrive in 2018. Furthermore, the US wind market is forecast to install approximately 10GW per year for the next several years as the production tax credit phases out. With renewable tax credits left undisturbed by the Tax Act, we anticipate activity levels in the solar and wind tax equity space to remain fairly consistent with or to increase as compared to 2017 levels and for the partnership flip to remain the most popular structuring tool for unlevered tax equity financings. We note that the Tax Act may have created issues for the use of partnership flips in some levered structures, so we may see their prevalence begin to decline in the context of wind tax equity financings. Nevertheless, this will position the wind and solar markets, as well as new gas-fired plants, to compete for shares in the US power market.

As mentioned, we anticipate continued increased activity in the 4(a)2 private placement market throughout the energy industry. In 2017, we continued to see a shift from Rule 144A/Regulation S transactions to 4(a)2 private placements. Historically, 4(a)(2) transactions were primarily used for smaller transactions in the energy space; however, with the massive amount of liquidity currently available in the 4(a)(2) market, we have seen many larger transactions completed in the past year (including the Sabine Pass transaction, which was the first such transaction completed by Sabine Pass after many Rule 144A/Regulation S issuances, the Tenaska CSolar IV West transaction, with Tenaska having historically accessed almost exclusively the Rule 144A/Regulation S market for the refinancing of its construction debt, and the sPower portfolio financing (discussed in greater detail below)).

Finally, we expect to see a greater number of LNG transactions completed that are much smaller in overall capital costs. Typically, an LNG project requires a massive amount of capital, as evidenced by the Cheniere, Freeport and Cameron LNG projects, among others. However, in the past year, as the competition for offtake contracts increased, resulting in reduced offtake pricing and greater risk for developers, we saw a trend towards smaller projects, including the Elba Island project, which completed its financing in the first quarter of 2017. Given their smaller size, such projects are seen as less risky to lenders (and third party equity providers), and are better able to fill their (relatively smaller) offtake requirements. Accordingly, we expect smaller LNG projects to continue to make headway in a market that has thus far been dominated by giant projects.