Case Study

Financing of a Hydroelectric Project

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The Borrower/Project Owner:

- An irrigation district, and quasi municipal corporation, located in the State of Oregon.

The Project:

- A single turbine 5 MW hydroelectric facility located on an irrigation canal, together with pipeline infrastructure. Total project cost = $26,000,000

The Financing Sources:

- Senior Secured Debt
  - Loan from OR Department of Energy: On-lending of proceeds of tax-exempt bond issuance by the State of Oregon to finance small scale local energy projects. $17,000,000, 19 years, at an interest rate equal to the bond yield + 1.5%.
- Unsecured Debt
  - Loan from OR Department of Environmental Quality: Loan from the Clean Water State Revolving Fund of proceeds of an ARRA capitalization grant to construct a pipeline to replace the existing open canal. $4,000,000 (of which 50% is forgiven, resulting in a net loan amount of $2,000,000), 20 years, at 0% interest.

- Grants
  - PGE Pelton Dam Fund: Established to protect and enhance habitat for the Deschutes River fish passage. Grants awarded for water rights and habitat improvements where salmon and steelhead will migrate, spawn and rear. Grant of $250,000.
  - Local city grant: Funded through the American Recovery and Reinvestment Act and available to eligible entities that implement strategies to reduce fossil fuel emissions in a manner that benefits local communities and improves energy efficiency. Grant of $278,000.
  - DEQ Grant: $2,000,000, representing the loan principal forgiveness described above.
  - Oregon Watershed Enhancement Board Grant: Funded from the Oregon Lottery and other sources to support Oregon's efforts to restore salmon runs, improve water quality, and strengthen ecosystems that are critical to healthy watersheds and sustainable communities. Grant of $935,000.
  - Deschutes River Conservancy/Bureau of Reclamation – grant to improve water quality in the Deschutes Basin and restore watershed. Grant of $1,000,000.
- Monetization of Tax Benefits
  - OR Business Energy Tax Credit: A tax credit offered by the OR Department of Energy to investors in energy conservation and renewable energy. Equals 50% of eligible project costs and can be taken over 5 years or, in the case of a public entity with no tax liability, transferred to another entity in exchange for a lump-sum cash payment. Expected value upon project completion of $4,350,000.
  - Energy Trust of Oregon: Cash incentive of $1,000,000 in exchange for RECs generated by the project.

The Issues:

- Collateral Sharing – the District purchased a parcel of land from the State of Oregon Parks and Recreation Department, which financed the purchase and took a deed of trust as collateral for the loan. The District needed to negotiate and balance the lien priority of Parks (with a small, short-term loan) and DOE (with a large, long-term loan).
- Inability of a tax-exempt/governmental entity to utilize typical tax incentives – Because the District is a governmental entity, it was unable to use or monetize the 30% Investment Tax Credit or grant often available to renewables projects, nor bonus depreciation.
- Balancing of federal and state funding sources – The District was limited in the amount of 0% interest rate loan proceeds that it could take from the federally funded DEQ program due to restrictions in applicable state loan and grant programs relating to the balance of state and federal funds financing the project.

The Lessons:

- Check with your state for unique tax incentives, grants and subsidies.
- You may have to do some research, but there are multiple sources of long-term, low fixed rate financing that will allow your project to achieving a low-cost financing structure with an adequate investor return, even if traditional tax incentives are not available to you.