

The Basics of a Power Purchase Agreement

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A power purchase agreement (PPA) is a long-term agreement between the owner of a biomass-fueled electric generating facility and the wholesale energy purchaser. A PPA allows the facility owner to secure a revenue stream from the project, which is necessary to finance the project. Typically, PPAs address issues such as the length of the agreement, the commissioning process, the purchase and sale of energy and renewable energy attributes, price, curtailment, milestones and defaults, credit and insurance.

The term of a PPA may be for five or more years. A PPA is usually legally binding once it has been executed by the seller and the purchaser, but may be subject to early termination rights. Early termination rights may allow one or both parties to terminate the PPA early if certain events occur, including the seller's failure to obtain financing.

Price terms vary, reflecting the cost of the project financing, quality and cost of the biomass resource, prevailing market prices and many other issues. Market prices for biomass energy have increased over the past few years, reflecting the increase in input, equipment and labor costs. Price terms are very important to project development, as the PPA

allows investors to estimate the total revenue available over the life of the project. In addition, the price may include all of the project's renewable energy credits, including carbon credits.

Most PPAs recognize that there will be times when either the purchaser, transmission owner or transmission authority may curtail the facility's production of energy because of constraints on the transmission system, emergency or other reasons. The parties must decide who will bear the financial risk for losses that arise when the purchaser, transmission owner or transmission authority exercises its curtailment right. Often the purchaser will pay the seller for the energy that the project would have produced as a result of a purchaser's ordered curtailment.

PPAs often provide development milestones to commercial operation. Construction or development milestones track the project's development progress and provide the buyer with liquidated damages in the event the seller fails to construct the project within the agreed upon milestone dates. Development milestones may include acquisition of all permits, execution of a construction contract, commencement of construction, and ultimately, commercial operation.

Sellers and purchasers face risks associated with the credit of the other party. Many purchasers require sellers to provide some form of credit enhancement to cover expected damages to the purchaser if the project does not meet construction milestones or is not commercially operational by the agreed upon date. This credit enhancement may take several forms, including guaranties by credit

worthy affiliates, cash collateral or escrow accounts, irrevocable standby letters of credit, or performance bonds.

The PPA will usually require that the seller maintain, at the seller's expense, specific insurance policies and name the purchaser as an additional insured.

Negotiating and securing an acceptable PPA is an essential step in developing a biomass-fueled electric generating facility and should not be entered into without the advice of experienced legal counsel. PPAs include many critical terms and conditions beyond just the price for energy generated by the project. PPA terms and conditions warrant careful analysis and consideration, and parties nearing negotiations on a PPA should confer with counsel to ensure that the PPA meets the needs of the specific project. BIO

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