

STATE OF IOWA
DEPARTMENT OF COMMERCE
UTILITIES BOARD

IN RE: PAUL NEPPEL	DOCKET NO. DRU-06-3
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ORDER DECLINING TO ISSUE DECLARATORY ORDER

(Issued July 24, 2006)

PROCEDURAL HISTORY

On June 7, 2006, Paul Neppel filed with the Utilities Board (Board) a petition for a declaratory ruling on whether eligibility of certain limited liability companies for wind energy production tax credits pursuant to Iowa Code chapter 476C and 199 IAC 15.19 is affected by a time-limited, majority position taken in the limited liability companies with respect to financial rights by an equity investor. Mr. Neppel's proposed answer is that the eligibility for tax credits should not be adversely impacted by use of such a financing mechanism. The Consumer Advocate Division of the Department of Justice (Consumer Advocate) filed a petition for intervention that included some comments on the petition for declaratory ruling on June 21, 2006. Pursuant to 199 IAC 4.3(1), Consumer Advocate qualifies as an intervenor in this proceeding.

On June 27, 2006, the Board issued an order requiring Mr. Neppel to file additional information and setting a comment schedule. The Board noted that, as alluded to in Consumer Advocate's June 21, 2006, filing, the actual terms of the financing arrangement referred to in Mr. Neppel's petition should be filed for the

Board and Consumer Advocate to review. Pursuant to the order, Mr. Neppel filed a non-binding term sheet on July 7, 2006. Mr. Neppel, on the same date, filed a request that the non-binding term sheet be held confidential; the Board granted that request on July 17, 2006.

The Board's June 27, 2006, order allowed Consumer Advocate to file additional comments. On July 12, 2006, Consumer Advocate filed additional comments pursuant to the established schedule. Mr. Neppel replied to Consumer Advocate's comments on July 20, 2006.

MR. NEPPEL'S POSITION

In his petition for declaratory ruling, Mr. Neppel summarized the relevant facts upon which the ruling is requested as follows: Mr. Neppel made application and received certification of eligibility for renewable energy tax credits pursuant to Iowa Code chapter 476C. The Board's staff reviewed the application and requested additional information; Mr. Neppel provided additional information and amended the application as agent for a consortium of ten individual limited liability companies (LLCs) formed and in existence under Iowa law. Each LLC owner will own no more than two eligible facilities. Based on this information, Mr. Neppel received a letter from the Board's Executive Secretary indicating that a preliminary determination had been made that the 21 MW wind facility (consisting of ten individual 2.1 MW wind generators) owned by the ten individual LLCs is an eligible renewable energy facility.

Mr. Neppel is now finalizing arrangements for project development and financing. Mr. Neppel states that a critical element in project financing is attracting

an equity investor to utilize federal production tax credits from each project; Mr. Neppel said the model he wants to use would have the local owner (the Iowa LLC) retain a majority interest with respect to governance rights in each LLC while the equity investor would take a majority position with respect to financial rights in each LLC. After approximately ten years (the specific timeframe has not been determined), the equity investor's entire interest would be bought out by the citizen member of the LLC.

Mr. Neppel asks the Board to declare that the eligibility for chapter 476C tax credits of the ten LLCs is not adversely impacted by the use of the proposed financing mechanism. Pursuant to Iowa Code § 476C.1(6)(b) and 199 IAC 15.1, an "eligible renewable energy facility" must be at "least 51 percent owned" by one or more of a list of eligible entities, which list includes a resident of Iowa and an authorized limited liability company.

Mr. Neppel states that under the financing arrangement proposed, the citizen member retains a majority interest with respect to governance rights and will derive financial benefit via the management services provided. The time-limited equity investment will facilitate the development of renewable energy facilities in Iowa.

The non-binding term bidding sheet that was subsequently filed has been held confidential at Mr. Neppel's request. In his non-confidential response, Mr. Neppel states again that the financier's (equity) interest will be of limited duration and specific provision is made for conversion of the financier's interests in the LLCs.

CONSUMER ADVOCATE'S POSITION

Consumer Advocate notes that when the Board adopted rules for the 476C projects, it said that chapter 476C included a limit on ownership and required an application to include information regarding ownership of the facility. Iowa Code § 476C.3(5) specifically provides that an "owner meeting the requirements of section 476C.1, subsection 6, paragraph b, shall not be an owner of more than two eligible renewable energy facilities." Iowa Code § 476C.1(6)(b) provides the list of persons and entities that may own an eligible renewable energy facility, which list includes residents of Iowa and authorized limited liability companies. Certification of Eligibility for Wind Energy and Renewable Energy Tax Credits, "Order Adopting Rules," Docket No. RMU-05-8 (1/26/2006) (Tax Credit Rules).

Consumer Advocate cites comments filed by Carroll County Projects (Carroll County) on October 13, 2005, that relate to the issues raised by Mr. Neppel. Carroll County commented on a similar statutory scheme in Minnesota, where it said the law also required that at least 51 percent of qualifying projects be owned by certain defined persons (who would presumably receive the benefits associated with that ownership). Carroll County said the Minnesota legislature did not intend that the various permitted ownership structures, such as limited liability companies, be used to divert ownership benefits to persons not listed in the statute; on the other hand, Carroll County recognized that the assistance of outside investors is often required for person who are not independently wealthy to build and own projects. Consumer Advocate agrees with Carroll County that there may be financing structures that meet the Legislature's expectation that a local qualifying owner will obtain the majority of a

project's benefits while also allowing projects to take advantage of available wind industry financing tools.

After reviewing Mr. Neppel's non-binding term sheet, Consumer Advocate filed additional comments on July 12, 2006. Consumer Advocate states it is unable to conclude, based on a review of the document, that the terms of the proposed arrangement will provide the majority of financial benefits to the citizen member owners. Consumer Advocate notes the terms of the non-binding term sheet do not support Mr. Neppel's assertion that the citizen member will always retain a majority interest with respect to the LLC's governance rights. Consumer Advocate argues the eligibility requirements for chapter 476C renewable energy credits reflect a clear legislative intent that the majority of ownership benefits accrue to specified Iowa persons and entities.

Consumer Advocate concludes that the financing arrangement which is the subject of Mr. Neppel's petition for declaratory order could adversely affect the eligibility of the ten LLCs for chapter 476C tax credits and that Mr. Neppel's original application for tax credits, submitted on behalf of the ten LLCs, would have to be modified if this type of financing arrangement were pursued. Consumer Advocate states that because there has not been a clear demonstration that majority ownership benefits remain with the original LLC applicants, the Board should decline to issue a declaratory order finding that the proposed financing arrangement would not adversely impact the eligibility of the ten LLCs for chapter 476C tax credits.

APPLICABLE STATUTE

The issues raised by Mr. Neppel relate to ownership of and benefits flowing from facilities eligible for Iowa Code chapter 476C tax credits. The Legislature has specifically defined an eligible renewable energy facility. Iowa Code § 476C.1(6)(b) provides that any eligible renewable energy facility must be at least 51 percent owned by one or more of any combination of the following:

1. A resident of this state;
2. Any of the following, as defined in section 9H.1:
 - a. An authorized farm corporation;
 - b. An authorized limited liability company;
 - c. An authorized trust;
 - d. A family farm corporation;
 - e. A family farm limited liability company;
 - f. A family trust;
 - g. A revocable trust; or
 - h. A testamentary trust.
3. A small business as defined in section 15.102;
4. An electric cooperative association organized pursuant to chapter 499;
5. An electric cooperative association that has members organized pursuant to chapter 499;
6. A cooperative corporation organized pursuant to chapter 497 or a limited liability corporation organized pursuant to chapter 490A and meeting other requirements; or
7. A school district.

DISCUSSION AND RULING

In 2005 the Legislature enacted legislation establishing two types of energy tax credits, one for wind energy production tax credits (Iowa Code chapter 476B, often referred to as the large wind credits) and one for renewable energy tax credits (Iowa Code chapter 476C, often referred to as the small wind credits, although a portion of the credits are reserved for other renewable energy facilities). A history of

the administrative rules adopted to implement the two pieces of legislation is set forth in the order adopting the Tax Credit Rules and will not be repeated here; however, ownership issues were some of the primary issues in the rule making, and the Administrative Rules Review Committee encouraged the Board to adopt strict ownership limits for chapter 476B projects.

Chapter 476C differs from chapter 476B in that chapter 476C includes a specific list of eligible types of owners. Therefore, unlike the rules applying to chapter 476B projects, the Board found no statutory authorization to pierce the corporate veil and look through the listed entities when applying the ownership limits of section 476C.3(5), which provides that an owner meeting the eligibility requirements of the chapter shall not be the owner of more than two eligible renewable energy facilities; for chapter 476B projects, the Board considers the equity owners of the application, in addition to the applicant itself, when applying the ownership limit.

The issues raised by the petition for declaratory order are similar to those debated in the rule making because they involve statutory construction and a determination of legislative intent in establishing the ownership requirements and restrictions contained in chapter 476C. While the Board recognizes creative financing may be necessary for some wind projects to reach fruition, that creative financing must satisfy the ownership criteria of chapter 476C or the facility will not be eligible for the tax credits. Mr. Neppel seeks to create two types of ownership, at least for a certain time period, with one "owner" (the non-eligible owner) having an equity interest and the other owner (the Iowa LLC) having a much smaller equity interest (at least for a certain time period) but having "governance" rights.

The difficulty with the financing arrangement proposed by Mr. Neppel is that at least for a certain and substantial time period, the equity investor (who is not an eligible owner as defined by chapter 476C) appears to retain the majority of project ownership benefits. Like Consumer Advocate, the Board cannot determine from the petition and term sheet whether the Iowa-eligible LLCs will receive a majority of the project ownership's benefits over the life of the projects. If this condition is not satisfied, the project would not qualify. Finally, it appears from the filed information that, contrary to the assertion in the petition, the eligible Iowa LLCs may not always retain a majority interest with respect to governance rights in the LLCs.

Because the Board cannot determine that the 51 percent ownership threshold (using financial and governance criteria) is satisfied by the proposed financing arrangement, the Board will decline to issue a declaratory ruling. If Mr. Neppel decides to pursue this type of financing, he must modify his application for tax credits and provide the actual financing documents (not a non-binding term sheet) for Board review. However, without significant changes, it is unlikely that such an arrangement would satisfy the requirements of chapter 476C, which indicate a legislative intent that Iowa individuals or Iowa entities retain a majority of the financial benefits from these projects and that the receipt of such benefits not be suspended and retained by non-qualified entities for a substantial period that could approach or even exceed ten years. From the information provided, it appears that legislative change would be necessary for the ten LLCs to retain their eligibility for state tax credits using the financing method described by Mr. Neppel.

ORDERING CLAUSES

IT IS THEREFORE ORDERED:

1. The Utilities Board declines to issue a declaratory order pursuant to the request for declaratory order filed by Paul Neppel on June 7, 2006.
2. Any argument in the pleadings not specifically addressed in this order is rejected as not being of sufficient persuasiveness to warrant comments.

UTILITIES BOARD

/s/ John R. Norris

/s/ Diane Munns

ATTEST:

/s/ Margaret Munson
Executive Secretary, Deputy

/s/ Curtis W. Stamp

Dated at Des Moines, Iowa, this 24th day of July, 2006.