

LAW: Examining the Rules and Risks Surrounding Procurement of Renewable Energy Facilities

BY RICHARD T. HOLLAND

In 2008, Massachusetts enacted the Green Communities Act to promote the development of renewable energy sources, and the market for renewable energy has not been the same since. Municipalities have sought to participate in this market and develop renewable energy sources for any number of reasons, not the least of which is to reduce energy costs. Some have financed and installed their own sources, and others have contracted with a developer to do so on municipal property leased to the developer for that purpose.

It will come as no surprise that there is a tangle of procurement laws that may apply to these installations, as well as a host of legal and contracting issues to consider as part of any procurement.

Procurement Options

There are a number of state laws that may apply to the procurement of renewable energy facilities to be financed and owned by a municipality or by a third party leasing land from the municipality for that purpose. The differences among the laws are many, but the following provides several noteworthy distinctions. Determining which of the laws applies depends on whether the renewable energy facility will be installed on open land or a building, and whether the facility will be financed and owned by the municipality or a third party. More than one law may apply to a procurement, in which event the municipality will need to decide which law best suits its purposes.

• **Chapter 25A** applies to the procurement of energy management services

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contracts, including contracts for energy efficiency improvements to municipal facilities and the installation of renewable energy facilities on municipal property. It is a design-build statute. Thus, it allows a municipality to issue only one solicitation to procure a single developer to both design and build (and operate and maintain) the renewable energy facility. Although more commonly used for the procurement of contracts involving energy-efficiency modifications to buildings, Chapter 25A was recently amended to include the procurement of renewable energy facilities.

Under Chapter 25A, a municipality may issue a request for proposals under Section 11C or a request for qualifications under Section 11I. The primary difference between the two is that a municipality must request the submission of a price proposal in an RFP and use price as a factor in determining the successful offeror; whereas under an RFQ, a price proposal is not requested until all offerors' statements of qualifications have been evaluated, at which time price negotiations with the top-ranked offeror may commence.

Chapter 25A limits the length of the contract to twenty years and requires

that annual reports on the performance of the facility be filed with the Department of Energy Resources. It may be used to procure renewable energy facilities that will be financed and owned by the municipality, as well as facilities that will be financed and owned by a third party on municipal property leased for that purpose, where the municipality and third party enter into a power purchase agreement for the purchase of electricity or “net metering” credits. (If a municipality seeks only to lease its property and does not intend to enter into a power purchase agreement with the third party developer, it would simply procure a lease under Chapter 30B, Section 16, which is discussed below.)

Chapter 25A falls under the jurisdiction of the Department of Energy Resources.

- **Chapter 164, Section 143(d)**, applies only where the municipality will finance and own the renewable energy facility. It was recently enacted specifically to allow municipalities to use the more simplified procedures under Chapter 30B, sections 5–6, for the procurement of renewable energy facilities and to issue a single solicitation for all supplies, services and equipment, including design, construction, operation and maintenance services. Chapter 30B allows for a sealed-bid process (Sec. 5) or an RFP process (Sec. 6) for such procurements. An RFP, however, may be used only if the municipality’s chief procurement officer has determined in writing that, in order to award a contract, it is necessary to consider factors in addition to price, which is typically the situation with the procurement of renewable energy facilities.

Chapter 30B limits contracts to a term of three years, but unlike the twenty-year limitation in Chapter 25A, the three-year limitation may be extended by a vote of the municipality’s legislative body to as many years as that body may decide. (Unlike Chapter 25A, Chapter 30B, Section 12(b), expressly allows for an extension of the term of the contract “by majority vote” of the legislative body.)

Chapter 30B is under the jurisdiction of the office of the inspector general.

- **Chapter 149, Section 44A**, applies to projects involving construction of (or

to) a building, including, for example, installation of solar panels on a rooftop. It is known as a design-bid-build statute, because a municipality procures design services and construction services separately. Design services are solicited through a request for qualifications under Chapter 7, Section 38K, known as the designer selection law, which applies where both the estimated cost of construction is more than \$100,000 and the estimated fee for design services is more than \$10,000; construction services are obtained by sealed bid under Chapter 149. (Sealed bids are required for projects costing more than \$25,000; Section 44A also sets out the procurement requirements for projects costing less than \$25,000.) Chapter 149 also imposes a number of other requirements for projects costing more than \$100,000. It may be used to procure renewable energy facilities that will be financed and owned by the municipality.

Chapter 149, Section 44A, falls under the jurisdiction of the office of the attorney general.

- **Chapter 149A, Section 1**, allows municipalities to solicit construction-manager-at-risk contracts for building projects costing \$5 million or more as an alternative to the process set forth in Chapter 149, Section 44A. (A construction manager at risk may perform pre-construction, construction, and construction management services for a project, at a not-to-exceed maximum price.) Chapter 149A, Section 1, may be used to procure renewable energy facilities that will be financed and owned by the municipality. It may be used only with the pre-approval of the office of the inspector general; other than the pre-approval requirement, jurisdiction rests with the attorney general.

- **Chapter 30, Section 39M**, applies to the procurement of construction contracts for non-building (or “public works”) projects, such as roadways or sewer construction. It is also a design-bid-build statute, but unlike under Chapter 149, a municipality is not required to solicit design services under the designer selection law for public works projects. Since the designer selection law does not apply

to such projects, and since contracts with designers are exempt from Chapter 30B [see Ch. 30B, Sec. 1(b)(32A)], a municipality may simply follow sound business practices to procure a designer (e.g., request proposals from three or more designers). Construction services must be procured by sealed bids under Chapter 30, Section 39M. (The advertisement requirements for public works projects under Chapter 30, Section 39M, and building projects under Chapter 149, Section 44A, are the same; they can be found in Section 44J of Chapter 149.) Section 39M may be used to procure renewable energy facilities on open land (not buildings) that will be financed and owned by the municipality.

Chapter 30, Section 39M, falls under the jurisdiction of the attorney general.

- **Chapter 149A, Section 14**, allows municipalities to solicit design-build contracts—where the successful bidder is responsible for both design and construction services—for public works projects costing \$5 million or more as an alternative to the process set forth in Chapter 30, Section 39M. Section 14 may be used to procure renewable energy facilities that will be financed and owned by the municipality and are on open land (not buildings). It may be used only with the pre-approval of the inspector general; other than the pre-approval requirement, jurisdiction rests with the attorney general.

- **Chapter 30B, Section 16**, applies to the acquisition and disposition of public property, including leases to third parties. Therefore, it applies only where a third party will be installing, owning and operating a renewable energy facility on public property leased by such third party from the municipality for that purpose. For the lease of public property, Chapter 30B, Section 16, requires issuance of an RFP when the total fair market rental value of the property (to be determined using accepted appraisal methods) over the term of the proposed lease, including any option years, exceeds \$25,000. Unlike the RFP process in Section 6 of Chapter 30B for the procurement of supplies or services, the RFP process under Section 16 has few requirements to satisfy. This flexibility may be an

advantage, as a municipality may fashion its own rating scheme and rule for contract award, provided it maintains open and fair competition and allows for meaningful comparisons of proposals.

Chapter 30B, Section 16, falls under the jurisdiction of the inspector general.

Between Chapter 30B, Section 16, and Chapter 25A, the former might seem the more flexible, if not appealing, choice for procuring third-party-owned renewable energy facilities to be installed both on open land and buildings, because both installations involve a lease of municipal property; Chapter 25A imposes requirements not found in Chapter 30B, such as the twenty-year contract term limitation and the requirement that municipalities submit annual reports to the Department of Energy Resources; and power purchase agreements are exempt from procurement under Chapter 30B [in Sec. 1(b)(33)] as “energy contracts ... for energy or energy-related services.” There appears, however, to be a general, if unofficial, consensus among the state agencies having jurisdiction over these public procurements—the inspector general, the attorney general, and the Department of Energy Resources—that building installations (as opposed to installations on open land) are best procured under Chapter 25A, because a building installation is more “energy contract” or “building construction” than “lease.” Whether one agrees or disagrees with this reasoning, it reflects the imperfections of the procurement laws, at least with respect to the procurement of third-party-owned renewable

energy facilities on municipal property. For example, although Chapter 25A speaks to energy contracts, it does not address the lease of property; and the reverse is true with respect to Chapter 30B, Section 16, which applies to leases but not energy contracts. (Although Chapter 25A requires developers to provide a performance guarantee, which is commonly mentioned as an advantage for municipalities, such a requirement could be included in a procurement under Chapter 30B, Section 16, simply by writing it into the RFP.)

In reality, no matter the statute followed, these procurements will be hybrids—basing an award of contract on, among other things, the lease and energy prices offered by developers. If there is any lesson here, it is that municipalities should consult with legal counsel and the relevant state agencies before and throughout the procurement of any renewable energy facility.

Power Purchase Agreements

The purpose of a PPA, like any other contract, is not only to memorialize a transaction or arrangement, but to allocate risk between the parties. Of the risks involved with a PPA, perhaps the most pronounced are the long-term nature of the contract, which may span twenty or more years, and the lack of certainty over energy prices and the energy needs of the municipality many years into the future. Before embarking on a PPA, therefore, municipalities are well advised to seek the assistance of experienced profession-

als in the procurement and negotiation of such contracts. These will include legal counsel and technical (energy, engineering and/or financial) consultants. Many municipalities have established energy committees and appointed experienced volunteers, used in-house expertise, procured technical consultants pursuant to the provisions of Chapter 30B, or employed some combination thereof.

Under a PPA, a municipality will be purchasing the energy produced by the renewable energy facility, whether that energy is consumed by an onsite facility or delivered into the electric distribution grid, or both. When electricity is delivered into the grid and the municipality has successfully applied for net metering services, the municipality will receive from the utility “net metering credits,” which represent the monetary value of, and the utility’s payment for, that electricity. Net metering credits are calculated pursuant to net metering regulations (220 CMR 18.00) promulgated by the Department of Public Utilities and implemented through the utility’s DPU-approved net metering tariff. A municipality will use net metering credits, which will be reflected on the invoices it receives from the utility, to offset the costs of electricity charged by that utility. (For facilities having a capacity of more than one but less than two megawatts, the utility may, at its election, pay a municipality cash for the electricity rather than provide net metering credits.) If the net metering credits received from the utility exceed the total annual electricity costs eligible

Procurement Options for Renewable Energy Facilities

PROJECT TYPE	FACILITY OWNED BY MUNICIPALITY OR THIRD PARTY	G.L. Ch. 149 Sec. 44A	G.L. Ch. 149A	G.L. Ch. 30B Sec. 16	G.L. Ch. 30B Secs. 5-6 (G.L. Ch. 164)	G.L. Ch. 30 Sec. 39M	G.L. Ch. 25A Sec. 11C and 11I
Building	Municipality Owned ≥ \$5 M	X	X		X		X
	Municipality Owned < \$5 M	X			X		X
	Third-Party Owned						X
Open Land	Municipality Owned ≥ \$5 M		X		X	X	X
	Municipality Owned < \$5 M				X	X	X
	Third-Party Owned			X			X

for offset, such credits will accumulate for later use, unless the municipality allocates those credits to another municipality or other governmental entity (which is allowed under 220 CMR 18.05[1]). If the facility is to be owned by a third party and is expected to produce excess credits, the PPA must address the allocation of those credits. For facilities that will feed electricity back to the grid, a municipality must, therefore, determine the total annual electricity costs that are eligible for offset and whether it desires a facility only large enough to offset those costs or a larger facility that will produce and allow for the allocation of excess credits.

In addition, the municipality should consider whether it may, in the future, develop its own renewable energy facilities or undertake other energy conservation projects, which may reduce future electricity costs. Any plans for such projects should be taken into account when determining the size of a renewable energy facility, especially in light of the regulatory cap for municipal net metering services, currently set at 10 megawatts for each municipality or governmental entity.

Price and Other Considerations

Power purchase agreements are complex, lengthy documents. The following are some key provisions that may be included in a PPA.

A municipality must decide whether to require a developer to guarantee a certain level of production of electricity. Although a developer interested in maximizing revenue will have a strong incentive to maximize electricity production, the municipality should request a guarantee of a certain level of electricity production each year. (In fact, a performance guarantee, so called, is a requirement under Chapter 25A.) It is expected that, in establishing such a guarantee, a developer will account for periods when the facility is not producing electricity, such as during routine repairs, or as a result of extraordinary events beyond the developer's control (known as "force majeure" events), including the absence of fuel (no sun or wind, for example), or due to the degradation of equipment over time. For example, in New England, due to climate conditions, it can be expected

that a photovoltaic facility will produce electricity at maximum capacity only 12 to 15 percent of the time.

The municipality may also consider including within the PPA an option to purchase the facility. For tax reasons and in order to maximize revenue from solar renewable energy certificates that will be generated by a facility, a developer may be unwilling to agree to the exercise of an option to purchase before the tenth year of the agreement. The parties may agree, in advance, on a schedule of purchase prices based upon reasonable estimates of the future fair market value of the facility; or they may agree that,



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upon the exercise of the purchase option, an independent appraiser selected by the parties will determine the fair market value of the facility, which will then serve as the purchase price. Given the difficulty in determining the price so far in advance and the likely advantage of the developer in establishing such a price, the use of an independent appraiser at the time of purchase is recommended. (In its recent *Guide to Developing Solar Photovoltaics at Massachusetts Landfills*, the Department of Energy Resources states that the purchase price should not be predetermined, but should instead be based on an independent appraisal at the time of purchase.)

[A note on solar renewable energy certificates, or SRECs: They represent the positive "environmental attributes" of the energy generated by a qualifying facility. One SREC is minted for each mega-

watt hour of electricity generated. The Massachusetts Renewable Energy Portfolio Standard requires regulated utilities and competitive suppliers to obtain a percentage of electricity from renewable energy sources. To comply with this requirement, utilities and suppliers may purchase SRECs on the open market.]

Another important issue is "liquidated damages." The theory of liquidated damages is that, in certain instances, in the event of a breach of contract, a non-breaching party's actual damages will be difficult to calculate. As a result, the parties may agree in advance on an amount of damages that the non-breaching party will be paid in the event of a breach, and then include that amount in their agreement. This amount is called "liquidated damages" (sometimes called a "terminal value" or "termination fee" in PPAs). Provisions for liquidated damages present a serious risk for municipalities and should be avoided if possible. A municipality may prohibit, in its procurement document, the inclusion of a liquidated damages provision in the PPA, though this may affect the number of offers received in response to its solicitation. If, however, a liquidated damages provision is not prohibited and is proposed by the developer, the developer should be required to explain in detail how the damages were calculated. Such a provision, like any other contained in the PPA, should be negotiated. Even without a liquidated damages provision, however, a municipality should anticipate that a breach of the PPA may result in significant damages. For this reason, the municipality should insist on language that expressly requires the developer to use all commercially reasonable and diligent efforts to mitigate its damages (in the event of a breach of contract by the municipality) by, for example, selling electricity and net metering credits to all other willing purchasers at the highest price, or similar language.

The PPA should include provisions on insurance. Whenever a municipality leases property to another party it should consult with its insurer or risk advisor about the insurance to require of the lessee and whether existing municipal insurance should be adjusted. Municipalities should also consider whether to require a developer to furnish surety bonds (or

other security) to ensure that the facility will be properly installed, operated, maintained and/or removed at the end of the term of the PPA and lease. The PPA should also include a requirement that the developer indemnify (pay) the municipality for damages arising from the developer's activities on municipal property. The requirement should include payment of the municipality's costs and expenses—including attorneys' fees—incurred in connection with any action to recover such damages. It should also include payment of any regulatory fines or penalties imposed against the municipality, such as those assessed by the Department of Environmental Protection in connection with damages arising from a facility installed on a municipal landfill.

Last but not least is the issue of price. The price for electricity and/or net metering credits generated by a renewable energy facility may be fixed or indexed, or a hybrid. A fixed price might be, say, 8 cents (flat or adjustable) per kilowatt hour. The risk of such a pricing structure is that electricity prices and the value of net metering credits could, over time, dip below the fixed price paid by the municipality. An indexed price, on the other hand, may require payment of a certain percentage (say, 75 percent) of the value of a net metering credit at any given point in time. Such a structure ensures that the municipality will never pay more than the value of the credit, shifting the risk of declining prices to the developer. It is likely, however, that the developer will insist, even with an indexed price, on a minimum floor price to satisfy the facility's financiers, who will expect a steady, uninterrupted stream of income—hence a hybrid pricing structure. In any event, shifting the risk of declining prices to a developer will likely result in a higher energy price for the municipality.

Taxes

A dilemma for municipalities and developers has been the issue of taxes. Although municipal and other publicly owned land is exempt from real estate taxes, if public land is leased to a private party for a private purpose, the land will be taxable to the lessee as if the land were privately owned. The Department of Revenue has taken the position that

municipal land leased to a private entity for a renewable energy project becomes subject to taxation pursuant to Chapter 59, Section 2B, even if the municipality receives a benefit from the lessee's use of the land in the form of a reduced price for electricity. In addition, the developer will likely be required to pay taxes on the electric generating equipment incorporated into the facility. Whether the equipment will be taxed as personal property or as part of the real property is a determination to be made by the local assessor. Although the taxation requirement will invariably result in a higher energy price for the municipality, it must be remembered that these taxes are still "new money" for the municipality. In any event, a municipality should include in its procurement document and PPA the requirement that the developer pay all personal property and real estate taxes for the property and renewable energy facility.

It is possible for a municipality and a developer to execute a payment-in-lieu-of-taxes (PILOT) agreement under Chapter 59, Section 38H(b), or, if the property is located within an economic opportunity area, a tax increment financing plan under Chapter 40, Section 59. A PILOT agreement provides for fixed annual payments throughout the term of the agreement. Although these payments are negotiated, they must be based on the full and fair cash valuation of the real and personal property. A TIF agreement, on the other hand, exempts from taxation a portion of the increased value of the real property resulting from the renewable energy facility. PILOT and TIF agreements require approval by the municipality's legislative body.

Statutory and Regulatory Compliance

The applicability of prevailing wages must be considered. For facilities financed and owned by the municipality, prevailing wages will apply. For third-party-financed and -owned facilities, whether prevailing wages will apply will depend upon the circumstances of the procurement. The more control a municipality seeks to exercise over the means and methods employed by the third party in the construction of a facility—by, for

example, requiring a certain level of quality in the materials and equipment incorporated into the facility, as a municipality may do if it anticipates that it may purchase the facility in the future—the more likely that the Department of Labor and Workforce Development and/or the attorney general will find the prevailing wage law applicable. Where applicable, a municipality will be expected to obtain the prevailing wage rate sheets and include them in its procurement document, or, for third-party financed projects, require the developer to do so at the time of construction. Municipalities, therefore, should include a provision in their procurement documents and PPAs requiring the developer to comply with all applicable local, state and federal laws in the financing, construction, operation and maintenance of the facility, including the prevailing wage law.

There will also be various permitting and approval requirements for a renewable energy facility, including zoning approvals. In some instances, a more complicated regulatory approval process will be required. For example, if a facility is to be located on a capped landfill, the post-closure use of the site must be approved by the Department of Environmental Protection. DEP approval will also be required if a facility is to be installed on water supply land. The PPA should require the developer to obtain (and pay for) all governmental and non-governmental permits and approvals.

Other possible concerns include whether the property was acquired for water supply protection purposes or open space or recreational uses, commonly referred to as Article 97 purposes, a reference to the applicable provision of the Massachusetts Constitution. If so, approval of the local board having custody of the property, the local legislative body (by a two-thirds vote), and the Massachusetts General Court (two-thirds vote of both Houses) will likely be required for the property to be leased to a developer and used for the purpose of a renewable energy facility.

Prior to advertising its procurement, the municipality should consider conducting a review of the property to determine what, if any, approvals may

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be required, and whether there are any easements, restrictions or other encumbrances that may complicate or prohibit use of the property for the installation of a renewable energy facility.

Moreover, in order to connect a facility to the electric grid for net metering services, the developer must obtain approval from the utility in accordance with the utility's DPU-approved interconnection tariff. The PPA should require the developer to obtain (and pay for) such approval, as well as for any upgrades to the electric distribution grid that may be required by the utility as a condition of any such approval. Since the municipality will be the "host customer" on the meter installed for the facility and, as such, will be required to enter into a host customer agreement with the utility, the municipality should require the developer to pay for all costs incurred by the municipality under that agreement.

Furthermore, local legislative approval will likely be necessary for most if not all third-party financed facilities. Such approval will be required in order to lease open land for the installation of such facilities and may be necessary for building installations, though a municipality may, generally, lease a (non-school) building for a period not to exceed thirty years without legislative approval (see Ch. 40, Sec. 4). As for a PPA, although exempt from Chapter 30B, due to the length of, and significant risks presented by, such an agreement, it is generally recommended that municipalities obtain local legislative approval to enter into the agreement. Since the municipality will likely need to obtain such approval to lease the property, it may simply include language in the appropriate legislative vote for approval of the PPA as well.

Conclusion

There are myriad factors, risks and potential pitfalls that should be considered when procuring renewable energy facilities to be installed on public property. With careful drafting and attention to detail, however, it is possible to procure such facilities in a manner that reasonably protects the municipality while affording maximum benefit from both environmental and financial perspectives. ❁