Tax Insurance For Renewable Energy Transactions

With the December 2015 extension of the investment tax credit for renewable energy equipment, the Federal government affirmed tax credits as one of the primary incentives to encourage investment in solar, wind and other renewable energy projects. Institutional investors now have 5+ years to continue to provide a source of funding for the projects involved through tax equity.

As passive participants, tax-equity investors are subject to a number of tax risks. These include the investment structure not being respected, the projects not qualifying for the projected tax benefits (including adjustments to the qualified basis) or the loss of tax benefits through recapture. Tax Insurance is a tool to manage these risks and was identified by the IRS in Rev. Proc. 2014-12 as a preferred vehicle for doing so over guarantees by transaction parties.

Aon Transaction Solutions is the leader in placing tax insurance and our team of 5 former practicing US tax lawyers is active in the use of such policies in renewable energy transactions (over $1.5 b of limits placed since 2013).

Tax Credit Insurance is a Proven Transaction Tool

- Policies have been used for:
  - Solar, wind, clean coal, biomass and other technologies
  - Various transaction structures, including flip partnerships, inverted lease passthroughs and other lease structures
  - Protection of tax equity investors
  - Protection of investors in ABS transactions against the impact of a qualified basis adjustment on a cash sweep mechanism or delays in an IRR based flip date
- Policies have been used in transactions involving major residential and commercial solar and wind developers and have been relied upon by major tax equity investors. Substantial insurance limits are available from high quality insurance balance sheet with ratings of “A” or better
- Policies typically have a term of 6 or 7 years and are issued on a pre-paid non-cancellable basis

CASE STUDY: Solar Investment Tax Credit (ITC) Fund

A tech company sought to invest in a fund sponsored by a solar energy company that would, in turn, invest in a portfolio of residential and commercial projects. Because the investment was outside its core business, the tech company required protection that the projected tax benefits would be received and not lost due to a recapture event.

Tax Insurance was used to assure the investor that the investment vehicle would be respected as a pass-through entity, that the solar facilities would indeed qualify for the credit and the tax basis would be respected, and that there would not be a tax loss due to recapture.

The Tax Insurance policy has a limit equal to the amount of projected tax benefits and provides coverage through the end of the recapture period. Wrapped by the insurance policy, the investment was perceived as prudent for the tech company, and it was approved by the investor’s commitments committee.

We're here to empower results

Aon Tax Insurance Team

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Illustrative Policy Terms & Conditions

Following is a sample illustrative term sheet outlining the terms and conditions applicable to a solar "flip partnership" tax insurance program.

Insurers	Various insurers rated at least "A" by A.M Best, S&P and/or Moody's
Insured	Tax credit investors in specified funds of residential and/or commercial solar projects
Limit of Liability	The policy will specify an aggregate limit of liability. This is determined by the insured, and typically is the amount of expected tax benefits
Retention	The policy will specify an aggregate retention
Policy Term	Typically 6 years. Non-cancellable
Covered Risks	1. Failure of the investment partnership to be respected as a partnership; 2. Failure of the allocation of tax benefits to the Insured (pursuant to a "flip" structure) to be respected; 3. Failure of the solar panels owned by the partnership to be treated as "energy property" within Code § 48 and the "qualified basis" for each of the solar panel systems to be respected; 4. Failure of the projects to be respected as timely placed in service; and 5. Recapture of the investment tax credits within the meaning of Code § 50 Amount of Loss Tax, Interest, Penalties, Contest Costs and a Gross Up, subject to the limit of liability
Key Exclusions	Inability to use the Tax Benefits, Change in Law, Misrepresentations by Insured
Key Underwriting Considerations	Underwriting considerations include the partnership structure and tax opinion, the parties and their financial strength, project level debt and forbearance agreements, the sponsor's obligations and guarantees, the underlying property insurance program and coverage for recapture losses, the mix of residential and commercial installations, the financial strength of end use customers, and the qualified basis analysis and appraisals (if applicable)

Aon Transaction Solutions

Aon Transaction Solutions Includes experts recognized for their experience in developing innovative, cost-effective tax insurance solutions for reducing or eliminating tax risk. The Aon team is unique within the insurance industry in terms of focus on Tax Insurance as an area of specialty and our experience with the product dating back to its earliest use. ATS is the largest transaction liability team in North America, now with 16 professionals on staff, mostly lawyers with previous M&A, Tax and deal experience, in New York City, San Francisco, Washington, DC, Chicago, Houston, Philadelphia, and Toronto. Our professionals also draw on the full resources of our Transaction Liability practices worldwide in Bermuda, the United Kingdom, Australia and Asia.

Aon Renewable Energy Practice

Aon Renewable Energy Practice includes a dedicated team of professionals servicing the renewable energy industry sector worldwide. Working with a client base ranging from the world's largest multinational power companies to small local utilities, Aon has expertise in all types of renewable energy including on-shore and off-shore wind, photovoltaic and thermal solar, biomass, hydro and energy storage.