KING & SPALDING

Energy Newsletter

April 2015

TRANSACTIONAL

Project Development / Finance

Global Solar Energy – A Bright Future

Tim Burbury, Usman Ahmad

Falling oil prices are no deterrent as the International Energy Agency estimates that by 2020, 2% of the global energy demand will be met by solar power with the figure rising to 16% by 2050. More »

Project Development / Finance

Shared (Common) Facilities in LNG Projects

Kathryn Marietta

LNG project structure varies significantly from project to project. Allowing for disproportionate ownership within an integrated LNG project offers opportunities but also adds complexity to an already complex project structure. Understanding the complexities and addressing them at the onset places project participants in a position to proceed with confidence to project completion and execution. More »

Project Development / Finance

Hydropower Concessions – Long Awaited Reform

Ruxandra Lazar

France is in the midst of altering the manner in which concessions are renewed in the hydroelectric sector. More »

REGULATORY

FERC

FERC's Order No. 807 Addresses Open Access And Priority Rights On Interconnection Customer's Interconnection Facilities

Neil L. Levy, David G. Tewksbury, Stephanie S. Lim

FERC recently issued Order No. 807, which amends certain of FERC's rules with respect to the ownership, control, and operation of Interconnection Customer's Interconnection Facilities, or ICIF. More »

Environmental

Reporting Hydraulic Fracturing Chemicals - New BLM Rules and EPA Study Spotlight FracFocus

Cynthia A.M. Stroman

Recently, the Bureau of Land Management and the Environmental Protection Agency have articulated different views on the utility and effectiveness of FracFocus, a website used by many operators to report the chemicals used to fracture their wells. More »

Visit King & Spalding's Energy Blog at energylawexchange.com

Shortlisted for the CHAMBERS USA AWARDS 2015

Upcoming Events

London Energy Series: Challenges for Europe's Energy Security: Does US LNG or European shale gas offer a solution?

When: **Thursday, 23 April 2015, 5pm – 7pm**
Where: **King & Spalding, 125 Old Broad Street, London EC2N 1AR**

For Further Details Click Here

King & Spalding Hosts FCPA Institute in Houston:

When: **May 4th & 5th, 2015**
Where: **King & Spalding, 1100 Louisiana, Suite 4000, Houston, TX 77002**

DISPUTE RESOLUTION
Construction / Real Estate

Seventh Circuit Court of Appeals: No Coverage under Title Insurance for Mechanics' Liens Arising after Construction Lender Stops Funding

Sarah R. Borders, Jeffrey R. Dutson

A federal appeals court recently entered an opinion interpreting "the most litigated provision" in the standard-form title-insurance policy, Exclusion 3(a), which provides that liens that are "created, suffered, assumed or agreed to" by the insured lender will not be covered under the title policy.
More »

Editorial Contacts
Charles J. (Tim) Engel III
+1 202 661 7800
tengel@kslaw.com
View Profile »

Andrew M. Stakelum
+ 1 713 276 7341
astakelum@kslaw.com
View Profile »

Jeffrey H. Perry
+1 404 572 2702
jperry@kslaw.com
View Profile »

About King & Spalding's Energy Practice
King & Spalding's energy practice has more than 300 lawyers in the U.S., Europe, the Middle East and Asia, giving King & Spalding one of the broadest and deepest benches of energy lawyers in the world. The firm is one of the most active law firms in the global energy industry advising and representing clients on a broad spectrum of transactions and disputes, and has received top rankings from *Chambers Global, Chambers USA, The Legal 500, The International Who's Who of Oil & Gas Lawyers, Euromoney's World's Leading Energy & Natural Resource Lawyers* and *The Best Lawyers in America.* For additional information, visit www.kslaw.com/practices/Energy.

For Further Details Click Here

In The News

King & Spalding Advised on Three Winning Transactions at Infrastructure Journal and Project Finance Magazine Awards Dinner
More »

King & Spalding Recruits Richard Nelson to Its Asia-Pacific Energy Team
More »

Chambers Global 2015 Results Confirm King & Spalding's Standing as One of World's Top International Law Firms
More »

Latin Lawyer Counts King & Spalding Among Top Latin American Practices for 15th Consecutive Year
More »

King & Spalding

Energy Newsletter

April 2015

TRANSACTIONS
Project Development / Finance
Global Solar Energy – A Bright Future
Tim Burbury, Usman Ahmad

In 2013, the total capacity of renewable energy worldwide was 1,560 gigawatts (GW) of which hydropower accounted for approximately 1,000 GW. However, the annual increase in hydropower over the preceding year was 4% while that for other renewables (primarily wind energy and solar energy) was nearly 17%. Even though wind energy is currently far more prevalent than solar energy, there are numerous reasons to be confident that solar energy will grow at a significantly faster rate than wind in the years to come.

This article serves as an initial overview of the trends in the global solar power market. In the coming month, we will publish articles on the various elements of developing solar projects, including PPAs and feed-in-tariffs, construction and O&M considerations, regulatory considerations and financing structures.

Other than hydropower, wind technology has been the mainstay of the renewable energy industry for the last few decades. The investments in this sector have been considerable in both Europe and North America, demonstrated by the fact that wind energy provided a third of Denmark's and a fifth of Spain's energy supplies in 2013. In the United States, investment in wind energy, being the most viable of the renewable technologies, has been driven by the various government subsidies – including tax credits, grants and federal loan guaranties – in place since the early 1990s.

However, wind energy seems to be running into its current technological limits – recently, there have been few gains in terms of siting or in the design of blades and bearings. Moreover, wind turbines are generally thought to be noisy, unattractive and dangerous to birds.

Solar power, on the other hand, has seen tremendous innovation in the last decade. This has taken two forms. The first (and accounting for about one-tenth of the existing solar energy capacity) has been thermal storage whereby sunlight is concentrated as heat and then can be used for producing steam to power turbines. The second, and more widespread, form of solar energy is electricity produced by photovoltaic (PV) cells. The IEA recently noted that the cost of solar panels has decreased by a factor of five in the past six years. The cost is further expected to halve in the next 20 years making solar a viable long term option as countries explore various avenues to reduce dependence on fossil-fuel-based energy.

Countries with considerable fossil-fuel (specifically petroleum) resources have an incentive to explore alternate energy sources in an effort to preserve their reserves for export and other value added products. Economies importing fossil fuels to meet energy requirements are incentivised to explore other options in an effort to be less susceptible to the vagaries of the global oil market (as demonstrated by the massive price swings since 2007).

Europe, North America and China

Considerable investment in solar energy is expected to occur in Europe and North America in the coming years; however, other regions and countries are likely to be just as active, if not more so, in terms of their solar investments. China, for instance, invested more than US$ 56 billion in renewable energy in 2013 alone (more than all of Europe and more than it invested in fossil-fuel and nuclear capacity combined), including 13 GW of solar energy.

UAE

The UAE has positioned itself at the forefront of the growth of solar energy in the region. The Emirate of Abu Dhabi established the Abu Dhabi Future Energy Company (Masdar) in 2006 with a mandate to reduce the emirate's dependence on oil. Since its inception, Masdar has made considerable investments in renewable energy initiatives including the Shams 1 project, a 100 megawatt (MW) concentrated solar energy project development in conjunction with Abengoa Solar and Total. Abu Dhabi is also home to the International Renewable Energy Agency (Irena).

Dubai has also made significant strides in the development of solar power and is in the process of developing a 1,000 MW solar park of which the first phase (of 13 MW) was commissioned in October 2014. A further 200 MW was awarded in early 2015 in what was the lowest ever bid price for a solar project (5.84 cents/kWh), which was bid by the winning consortium comprising ACWA Power of Saudi Arabia and Spain's TSK. This pricing is, in part, indicative of the technological advances in the PV industry. By 2030, Dubai hopes that 15% of its energy will be produced from renewable sources.

The Dubai Electricity & Water Authority (DEWA) recently announced a rooftop solar net metering program as part of its "Shams Dubai" initiative and further development of the regulatory framework in the UAE can also be expected in the near future.

Saudi Arabia

Saudi Arabia launched the King Abdullah City for Atomic and Renewable Energy (KA-CARE) in April 2010 with the mandate of contributing to development of the renewable energy industry. KA-CARE had the target of procuring 24 GW of renewable energy by 2024. However, the programme stalled before the procurement process commenced and in March 2015, the government gave the responsibility of developing renewable energy to the Saudi Electricity Company (SEC). While no new targets have been officially publicised, there are some indications that the program will initially be of a smaller scale, aiming for projects with a total capacity of 500 MW in the medium term.

The market will be closely watching SEC and the Electricity & Cogeneration Regulatory Authority (ECRA) in the coming months to see how the solar sector will be regulated, how projects will be procured and the framework for any feed-in tariff.

It is instructive to note that Reuters estimates that it costs Saudi Arabia approximately US$ 5/barrel (inclusive of capital expenditures) to extract oil and so using it for the production of electricity domestically displaces oil from other, more value added, uses. This opportunity cost coupled with the vast solar energy potential in Saudi Arabia and the government's drive to diversify the energy mix away from dependence on oil, means Saudi Arabia certainly can be expected to develop its solar energy sector aggressively in the coming years.

Jordan

Jordan has been actively involved in the development of solar energy in recent years to reduce its dependence on imported sources of energy (it currently imports 97% of the energy it consumes). Increase in solar power is a significant part of its strategy and it hopes to connect about 1.65 GW of renewable energy projects to the grid by 2020.

Jordan was the first country in the region to introduce net-metering regulations in 2012 allowing PV owners to sell solar power at a rate of approximately US$ 0.18/kWh and has recently announced plans to install PV systems on the rooftops of each of the 6,000 mosques in the country.

On a larger scale, a consortium led by the European Banks for Reconstruction and Development (EBRD) committed to provide financing of US$ 100 million for the construction of three solar project totalling 40 MW of capacity. This investment comes after the EBRD also agreed to provide financing for a 20 MW project in September 2014.

Egypt

Egypt's geographic location makes solar energy very attractive; however, at the end of 2013, it had only 20 MW of installed solar energy capacity. The government hopes that renewable energy will contribute 20% to the energy mix by 2020.

In recent weeks, the Egyptian Electricity Holding Company (EECH) has entered into a memorandum of understanding with Saudi based ACWA Power and Masdar to explore the growth of renewable energy in the country – 500 MW worth of solar projects are meant to be evaluated in this regard.

Egypt has also created several incentives to encourage investments in the solar energy sector. The most notable of these are (i) government backed 20-25 year power purchase agreements; (ii) a payment of the portion of the price to be based US Dollars (even though the payment would be made in Egyptian Pounds at the prevailing exchange rate) to alleviate currency risk; and (iii) allowing the use of state owned land in exchange for 2% of the energy produced by the project.

A feed-in tariff regime has also been established (the rates for household and commercial users will be different) and projects with capacity ranging from 500 kW and 50 MW will be eligible to participate.

Rest of Africa

Morocco has shown strong growth in solar energy and is targeting 2 GW of solar energy by 2020 and Algeria hopes to have 2.5 GW of renewable energy by 2030. Multilateral agencies have also shown strong interest in the sector, specifically in Africa, with the International Finance Corporation (IFC) announcing the creation of an initiative aimed to develop solar projects. This initiative, expected to be launched later in 2015, will also benefit from World Bank guarantees in respect of delays in connecting with the power grid of the host country as well as political risk.

Tim Burbury
Abu Dhabi
+971 2 596 7001
tburbury@kslaw.com
View Profile »

Usman Ahmad
Abu Dhabi
+971 2 596 7019
uahmad@kslaw.com
View Profile »

King & Spalding

Energy Newsletter

April 2015

TRANSACTIONAL
Transactions
Shared (Common) Facilities in LNG Projects
Kathryn Marietta

LNG project structure varies significantly from project to project. There are, however, some concepts that are common to projects that contemplate ownership of, or interest in, one or more LNG trains being disproportionate across a project. This variation in ownership or interest ("Participation") may arise at the time of project inception, or it may result from project expansion. In addition, regulatory authorities may mandate third party access to some of the infrastructure or the land on which the project is situated. In each case, when Participation is not consistent, integration of the project is typically achieved both contractually and technically through the shared (or common) facilities. In these circumstances, there are defined facilities that are shared across the project to ensure all project participants (irrespective of when they came into the project or the level of project Participation) have reasonable access to facilities that are required to enable each LNG train participant (or participant group) to deliver gas (for liquefaction) and store and lift the resulting LNG. This paper explores a few of the key attributes of a shared facilities agreement and key elements of such attributes. It also illustrates the complexities involved in an integrated LNG project.

Scope of Agreement and Facilities

Each LNG project will vary with respect to the scope of facilities covered by the agreement and the protocols for access and use thereof. The shared facilities typically do not include the LNG trains that process the natural gas into LNG. The facilities defined as shared will vary from project to project. The spectrum ranges from all facilities and equipment (other than the LNG trains) as comprising shared facilities, to only lifting facilities (or LNG storage and lifting facilities) being categorized as shared facilities. Typically, however, gas and LNG processing-related infrastructure (such as pre-treatment facilities) is shared across LNG trains as sharing such infrastructure may significantly increase efficiency and is often fundamentally necessary to include as shared facilities. For purposes of this article, infrastructure will be considered shared facilities. The shared facilities agreement defines clearly specific facilities that are to be shared (specifying interfaces and boundaries, as well as, specific equipment), and the terms upon which sharing will take place. Depending on the LNG site, the initial project plans, and government or other requirements, the agreement may also establish the terms for expansions – the incorporation of future LNG trains into the overall project – and the extent to which facilities existing prior to expansion will be shared with participants in an expansion. Because the lifting facilities and jetty often comprise part of the shared facilities, the shared facilities agreement may contain lifting terms as well.

Governance Committee

Depending on the corporate or similar governance that is adopted by participants in an LNG project, the

significance of the management committee under the shared facilities agreement may vary. Participants within an overall project (across the LNG trains) often look for some level of involvement in the management of the shared facilities. This involvement varies depending upon Participation and can range from informational only Participation to full voting rights. As with most management, coordination and operational committee structures, the agreement typically sets forth specifics about meetings and governance. Project governance structure will drive the depth of scope of the governance committee and related provisions in the agreement. If a project entity has been established, the shareholders agreement may bring definition to governance negating the need for detailed provisions in the shared facilities agreement. It may be that one of the project participants will serve as the entity that operates the shared facilities, and the governance committee is tasked with some level of oversight or given the right to receive information. If this is the case, the operator is often appointed in the shared facilities agreement. Operatorship can become a heavily negotiated term in the agreement. The possibilities are numerous in terms of establishing a governance committee and the breadth of its mandate.

Capacity

Allocating capacity of shared facilities and infrastructure is essential. Project participants develop a methodology for allocation of capacity in the facilities and associated cost sharing. The manner in which capacity is allocated may impact future train debottlenecking and expansions, depending on excess capacity that may exist at the time of initial project completion. In the event the allocation methodology results in the possibility of excess capacity, agreement as to participant access to excess capacity will ideally be reached up-front and documented in the shared facilities agreement.

During the course of operations, the facilities may have under-utilized capacity that has been allocated to one or more parties. Typically, the overriding objective of any integrated LNG project is maximization of LNG output from the project. In order to achieve this objective, the parties may agree to terms that enable participants to have access to each other's under-utilized capacity. These terms often include both capacity allocation and shifting of some, or all, of the cost associated with use of such capacity. Use of under-utilized capacity is typically fully interruptible so that the participant who holds the right to the capacity does not lose it during a period of re-allocation.

In addition, operational constraints may reduce the capacity available to the participants at any point in time. Consideration should be made in the documentation as to how such a reduction will impact the project participants. If fault for a constraint is not attributable to one or more participants, and no party has a contractual priority that was previously agreed, the reduction in capacity as a result of operational constraints may simply be pro-rata among all project participants.

Liftings

The means and process rules by which LNG is transferred from storage (and therefor the LNG project) into a form of delivery transportation (typically an LNG ship) is of great interest to all project participants. The process itself (called lifting) is operational and many contract terms are operational in nature. However, the scheduling function, allocation methodology for allotting LNG to project participants, measurement parameters, allocation of liability associated with failures to lift, and similar issues are critical project considerations and should be well documented. The lifting terms may be in a standalone document or be part of another project agreement; however, if they are not part of the shared facilities agreement they are typically linked to it. The lifting schedule is established with project participant input and is typically designed to allocate LNG on a non-discriminatory and ratable basis determined on an energy-in (feed gas supplied by a participant)/energy-out (LNG allocated to a participant) basis. Over the course of time, unscheduled or "excess liftings" will need to be accounted for. Assignment of excess liftings to one or more project participants is typically done in accordance with the same allocation methodology (energy-in/energy-out) and same principles of non-discrimination.

Expansions

.

Many LNG projects are sited or planned to allow for additional LNG trains to be constructed and integrated

into the original project at some point in the future. These LNG trains may or may not be specifically contemplated at the time the original facilities are constructed. The tremendous capital expenditures required for infrastructure and ancillary facilities, some or all of which become the shared facilities, during initial project development often result in an opportunity, through expansion, for the original project participants to recoup some of their initial capital investment for excess capacity in such facilities and infrastructure. Principles of expansion are often agreed by the original project participants in an effort to establish the framework by which third parties may enter an existing LNG project by constructing additional LNG trains and utilize the shared facilities without a material adverse effect on existing operations. This framework is often set forth in the shared facilities agreement because, at the time of expansion, the participants in a proposed LNG train will have access to shared facilities, or will contribute new facilities to the shared facilities, as the new train is integrated into the existing project. The allocation of original capital expenditure and credits for contribution of new shared facilities are often formulated in the expansion terms. Principles for expansion may require pre-consent by existing parties to a future expansion (as long as basic criteria are met). Specified liabilities are assumed by the parties having a Participation in the new LNG train as further protection to the original project participants. Typically, terms for an expansion will mandate that the expansion will not adversely impact the then existing project (including capacity), that the expansion will be in compliance with applicable regulations and laws, that the expansion will be in conformity with established gas specifications and other project specific requirements. The post-expansion capacity in the shared facilities will also need to be established based on a pre-agreed formula that is included in the shared facilities agreement.

Other Key Provisions

Other key terms that are generally agreed in the shared facilities agreement include work programs and budgets, modification and capital contribution requirements, decommissioning of facilities, and default provisions.

Conclusion

Allowing for disproportionate ownership within an integrated LNG project offers opportunities to existing and future project participants. Such ownership also adds complexity to an already complex project structure. Understanding the complexities and addressing them at the onset places project participants in a position to proceed with confidence to project completion and execution.

Kathryn Marietta
Houston
+1 713 276 7372
kmarietta@kslaw.com
View Profile »

KING & SPALDING

Energy Newsletter

April 2015

TRANSACTIONS
Project Development / Finance
Hydropower Concessions – Long Awaited Reform
Ruxandra Lazar

France is Europe's second largest hydroelectric producer after Norway and in 2010 initiated a process for renewing hydropower concessions. At the time, several European utilities expressed strong interest in bidding for these concessions; however, the renewal process slowed down and was finally interrupted in 2012 by a change in parliamentary majority. Nine years after the first steps were taken to liberalise the system at the request of the European Commission, this year could mark the difficult birth of a reform which is far from consensual.

Background

About 80% of the current 400 hydropower concessions in France are operated by EDF. The other major generators are Compagnie nationale du Rhône (CNR) and Société hydroélectrique du Midi (SHEM), both GDF SUEZ affiliates.

There are historical reasons for the low number of players in this market. Under the French hydropower concessions regime, established in 1919, a preference right was granted to outgoing concession holders when hydropower concessions were renewed. In 2005, the European Commission opened infringement proceedings against France, stating that this preference right breached EU law. According to the commission, this right could allow existing holders to retain their concessions indefinitely, contravening the principle of equal treatment of economic operators. Moreover, the preference right benefited companies that were already established in France and was thus incompatible with the principle of freedom of establishment. [1] The preference right was repealed in 2006 [2] and in 2008 a decree set out new rules for the renewal of hydropower concessions based on a competitive bidding process. [3]

In connection with the end of preferential rights for historic concessionaires, Parliament established a new royalty mechanism, which applies to new concessions awarded upon renewal. [4]

Renewal process at a standstill

A call for tenders for the renewal of concessions totalling 20% of the country's hydroelectric capacity (5,200 megawatts) was announced in 2010. However, the renewal process has stalled, presumably because of the complexity of this sensitive matter in a pre-election period.

The renewal process was interrupted in 2012 by the new parliamentary majority, which commissioned a report on the various alternative solutions available when renewing hydropower concessions.

The delay in launching the call for tenders prompted criticism from the National Audit Court, which highlighted the loss of fiscal revenues caused by the government's hesitations. [5] Several concessions have expired since 2011; however, in the absence of renewal, they have been extended under the previous royalty scheme. The court estimated that the delay in launching the renewal of the hydropower concessions could result in a loss of fiscal revenues of €600 million by 2020.

Key features of planned reform

Parliament is considering a draft energy transition bill that seeks to implement substantial changes to the hydropower concessions regime.

'Barycentre' method for renewal of concessions

The underlying idea of the 2010 renewal process was to bundle several concessions situated in the same locale, in order to launch tenders for coherent groups of concessions. In order to create these groups, the plan was for the state to purchase some of those concessions before their terms expired, with the incumbent concessionaires being indemnified accordingly. The new administration considered this method to be a barrier to market access, due to the high compensation needed to be paid to incumbent concessionaires by new entrants. Moreover, this financial effort would have penalised both (1) new entrants, who would have reduced their investments accordingly, and (2) the state, which would not have collected the expected amount of royalties.

An alternative solution for the renewal of concessions – the "Barycentre" method – was therefore set out in the draft energy transition bill. This method involves bundling together several concessions located in the same area and setting a single maturity date prior to launch of a bidding process. The single maturity date, set by decree for each concession, would be determined by weighing the maturity dates of the contracts in proportion to the revenues generated by each.

The draft bill sets out the principle that the concessionaire maintains an economic equilibrium, assessed on the basis of all bundled concessions.

The Barycentre method will apply to concessions irrespective of whether these are granted to one or several concession holders. In the latter case, the holders of concessions which are extended shall indemnify the holders of concessions which are shortened, with the amount of such indemnification being established by decree. Concession holders might also be subject to payment of an additional royalty if payment of an indemnification is insufficient to restore the initial economic balance of their concession agreements.

Exceptional extension of some concessions

The maximum duration of hydropower concession agreements set out by the 1919 law is 75 years. Most of the agreements have been for this maximum duration, which has been seen as a barrier to entry to the French market.

A parliamentary amendment has been tabled in order to allow the duration of some concession agreements to be extended beyond this limit. This amendment reflects a provision of EU Directive 2014/23/EC on the award of concession contracts. The directive provides that a concession contract can be modified without having to undertake a new concessions award procedure where additional works or services by the original concessionaire, which were not included in the initial concession, have become necessary. But a change of concessionaire cannot:

- Be made for either economic or technical reasons; and
- Cause significant inconvenience or substantial duplication of costs for the contracting authority.

The concessions which could be extended pursuant to this provision are not yet known.

New royalty scheme

The draft energy transition bill sets out the basis of a newly royalty scheme and provides that:

- A revenue-based royalty shall be paid to the state for all new or renewed concessions; The royalty shall not exceed a ceiling set out by the concession agreement; and

- The holders of concessions which are extended pursuant to the Barycentre method or for the performance of new works shall be subject to this royalty, which shall be set by the grantor, taking into account the need to maintain the economic equilibrium of the contract.

The impact of the new royalty scheme is difficult to assess at this stage, as the amount of the royalty will be set by each concession agreement.

Public-private company system

The draft energy transition bill foresees the possibility for the state to establish dedicated public-private companies – sociétés d'économie mixte hydroélectriques (SEMHs) – held jointly with a private partner and other public entities, which will be awarded concession agreements.

The bill sets out the following rules in this regard:

- Each SEMH will be created for the term of the concession and will be dedicated to a single concession contract.

- Riparian local authorities will be able to participate in the capital of SEMHs, subject to the state's approval.

- The state will be able to require other public entities to make equity investments in the SEMHs.

- Public entities must together hold at least 34% of the share capital and voting rights in an SEMH (*i.e.*, a blocking minority).

- The industrial partner must also hold a blocking minority.

- Before selecting the industrial partner within an SEMH, public entities must specify the main terms and conditions of the envisaged partnership that will be set out in the shareholders' agreements, as well as the share of investments that will be carried out by the public entities.

- Selection of the private partner of an SEMH will be made following a competitive bidding process, as for the award of other hydropower concessions.

The basis on which the state will identify the concessions that will be awarded directly to private partners and those which will be awarded to SEMHs, including a private partner, is not yet clear.

Implementation and next steps

It is expected that the new legal framework for hydropower concessions in France will be based largely on these principles. A consensus is forming along these lines between the two houses of Parliament as the parliamentary process comes to a close.

The implementation of a new hydropower concession regime will require the enactment of several decrees. Therefore, it may take several months to a year before there is clarification as to the duration of the concessions, which concessions will be put to tender, and which will be awarded to SEMHs. Moreover,

implementation of the reform is likely to encounter obstacles. Regional elected officials and energy sector trade unions have already expressed opposition and have denounced the privatisation of the hydropower sector.

This article was originally published in the Energy & Natural Resources – France Newsletter of the International Law Office.

---

[1] "Freedom of establishment: the Commission calls on France, Italy and Spain to amend their legislation on hydroelectric concessions. European Commission", July 13 2005, IP/05/920 (http://europa.eu/rapid/press-release_IP-05-920_en.htm?locale=en).
[2] Law 2006-1772 of December 30 2006 on water and aquatic environments.
[3] Decree 2008-1009 of September 26 2008.
[4] Amending Finance Law 2006-1771 of December 30 2006.
[5] Injunction of the National Audit Court, June 21 2013.

Ruxandra Lazar
Paris
+33 1 7300 3988
rlazar@kslaw.com
View Profile »

KING & SPALDING

Energy Newsletter

April 2015

REGULATORY
FERC

FERC's Order No. 807 Addresses Open Access And Priority Rights On Interconnection Customer's Interconnection Facilities

Neil L. Levy, David G. Tewksbury, Stephanie S. Lim

On March 19, 2015, the Federal Energy Regulatory Commission ("FERC") issued Order No. 807, which amends certain of FERC's rules with respect to the ownership, control, and operation of Interconnection Customer's Interconnection Facilities ("ICIF"). In particular, Order No. 807 addresses the circumstances under which ICIF owners and operators are required to have an Open Access Transmission Tariff ("OATT") on file with FERC, to implement an Open Access Same-Time Information System ("OASIS"), and to comply with FERC's Standards of Conduct.

In the past, FERC has waived the OATT, OASIS, and Standards of Conduct requirements on a case-by-case basis in situations where ICIF owners have been able to demonstrate that their ICIF are limited and discrete and where no requests have been made by third parties to access the ICIF. In circumstances where a third party submits a request for service, FERC has determined that an ICIF owner and its affiliates have priority to existing excess capacity on the ICIF if the owner can demonstrate that there are pre-existing generator expansion plans and that material progress has been made towards meeting construction milestones for the expansion. However, even in situations where the ICIF owner has been able to demonstrate that it should have priority rights to the excess capacity, FERC has required the owner to file an OATT within 60 days of receiving a request for service from a third party.

Recognizing that this existing policy imposes regulatory burdens and unnecessary risks on generation developers, FERC's Order No. 807 grants a blanket waiver of the OATT, OASIS, and Standards of Conduct requirements to public utilities that are subject to those requirements solely as the result of owning, controlling, or operating ICIF. To be eligible for the blanket waiver, the ICIF owner or operator must either sell electricity, or file a statement with FERC that it commits to comply with, and be bound by, the obligations and procedures applicable to electric utilities under Section 210 of the Federal Power Act (the "FPA").

Under the new rules promulgated in Order No. 807, the blanket waiver is not automatically revoked if a third party submits a request for service, but may be revoked upon a third party's application for service under Sections 210 and 211 of the FPA to the extent that the Commission determines that revocation is in the public interest. The rules state that, in any such proceedings, FERC will consider it to be in the public interest to grant priority rights to the owner/operator of the ICIF where it is demonstrated that the owner/operator has specific plans with milestones to use such capacity to interconnect its or its affiliates future generation projects. Moreover, FERC adopted a rebuttable presumption that, for the first five years after the commercial operation date of the ICIF, the owner/operator has definitive plans to use the capacity and that it is in the

public interest to grant priority rights to such owner/operator. Order No. 807 also expressly clarifies that ICIF owners may enter into voluntary agreements that allow other entities to obtain service on the ICIF.

Neil Levy
Washington, D.C.
+1 202 626 5452
nlevy@kslaw.com
View Profile »

David Tewksbury
Washington, D.C.
+1 202 626 5454
dtewksbury@kslaw.com
View Profile »

Stephanie Lim
Washington, D.C.
+1 202 626 8991
slim@kslaw.com
View Profile »

KING & SPALDING

Energy Newsletter

April 2015

REGULATORY
Environmental
Reporting Hydraulic Fracturing Chemicals - New BLM Rules and EPA Study Spotlight FracFocus
Cynthia A.M. Stroman

In the past ten days, the federal government has articulated different views on the utility and effectiveness of FracFocus, a website used by many operators to report the chemicals used to fracture their wells. [1] In its final regulations issued on March 20, the Bureau of Land Management embeds the website as a primary reporting tool. [2] In contrast, EPA issued a study of FracFocus on March 27 that contains a critique of the information collection service, particularly its allowance of confidential business information (CBI) claims. [3] However, provisions in the BLM rule and limitations in the EPA study combine to mitigate the potential use of the study to undermine the continuing utility of FracFocus.

The BLM Rule

The BLM rule, published in the Federal Register on March 26, concludes a three-year rulemaking effort to update regulations in place since 1988. In the rule, operators must submit information about the chemicals contained in fluids used to fracture a well. This information must be submitted through FracFocus or directly to BLM. [4] As expected, the rule contains specific provisions concerning the extent to which operators may assert claims of confidentiality regarding fracturing fluid components. [5] These provisions include the requirement for an affidavit from a corporate officer substantiating the claim. [6] The scope and rigor of the CBI requirements will almost certainly be debated as the rule undergoes judicial review.

The EPA Study

For the past several years, EPA has been engaged in an assessment of the potential impacts of hydraulic fracturing on drinking water. Completion of the assessment was originally scheduled for 2014, but progress has not kept pace with the Agency's target deadlines. [7] As an installment, EPA issued the results of its analysis of over 38,000 disclosures posted to FracFocus between January 1, 2011, and February 29, 2013. A prominent finding of the study is that "[o]perators designated 11% of all ingredient records as confidential business information, [and] [o]ne or more ingredients were claimed confidential in more than 70% of disclosures." [8]

Implications

Some stakeholders have interpreted the finding as evidence that FracFocus should not be used in the BLM rule for reporting. [9] However, such claims ignore several points, many of which are noted in the study report itself. First, the data do not constitute a complete picture of all fracturing chemicals, because not all wells are covered by the database and many of the states covered in the analysis did not have mandatory reporting

during the entire 2011-2013 time frame. [10] Second, EPA studied FracFocus 1.0, a version superseded in June 2013 by 2.0, which in turn will be replaced by version 3.0, both of which have substantial upgrades that yield more robust reporting. [11] Third, while specific ingredient identities may be withheld, FracFocus provides information about the general classes of chemicals reported as CBI. [12] More importantly, the BLM rule provisions bolster FracFocus' reporting requirements and raise the threshold for claiming information as CBI. [13] Moreover, the rule requires disclosure of a general chemical class for each CBI claim. [14]

The BLM believes that the generic chemical name that was or should be provided to the EPA under TSCA or other statutes and published in the Federal Register would not constitute a trade secret because it is or should be public, and the operator can still withhold the specific chemical identity. . . . Therefore, final section 3162.3-3(j)(6) requires the operator to include the generic chemical name for each such chemical. The BLM expects that the generic chemical name submitted pursuant to this rule will be the same as that submitted to EPA; if the generic chemical name is less descriptive than that submitted to EPA, the owner of the information should have a credible explanation for the difference. [15]

These reasons suggest that the EPA study should serve as an informative retrospective, not as evidence that undermines BLM's reliance on FracFocus as a centerpiece in its regulatory scheme.

---

[1] FracFocus provides public access to information about the content of fluids used to fracture wells. The website is a joint effort of the Ground Water Protection Council and the Interstate Oil and Gas Compact Commission.
[2] 80 Fed. Reg. 16,128 (Mar. 26, 2015).
[3] EPA, Analysis of Hydraulic Fracturing Fluid Data from the FracFocus Chemical Disclosure Registry 1.0, Doc. No. EPA/601/R-14/003 (Mar. 2015) (hereinafter EPA Study) .
[4] *See* 43 C.F.R. § 3612.3-3(i). BLM intends to load to FracFocus any data it received directly from the operator.
[5] 43 C.F.R. § 3612.3-3(j).
[6] *Id.*
[7] EPA currently estimates that it will complete its assessment in "spring 2015."
[8] EPA Study, at 2.
[9] *See, e.g.,* BNA, Daily Environment Report, "Most Oil, Gas Drillers Keep Fracking Chemicals Secret in FracFocus, EPA Says" (Mar. 27, 2015) (quoting NRDC spokesperson).
[10] *See, e.g.,* EPA Study, at 32.
[11] *See* EPA Study, at 1; *see also* http://www.fracfocus.org/major-improvements-fracfocus-announced (Feb. 26, 2015) (announcing additional upgrades in version 3.0).
[12] *See* EPA Study, Appendix B.
[13] 80 Fed. Reg. at 16,171 ("An operator may withhold information as exempt from public disclosure only if it identifies a Federal statute or regulation that would prohibit the BLM from disclosing the information if it were in the BLM's possession."); *see also* Law360, "Feds, States Must Clear Regulatory Air on Fracking Rules" (Mar. 20, 2015) ("It will be tougher for operators to shield chemicals from public disclosure through a trade secrets claim process.").
[14] 43 C.F.R. § 3162.3-3(j)(6) ("The generic chemical name must be only as nonspecific as is necessary to protect the confidential chemical identity, and should be the same as or no less descriptive than the generic chemical name provided to the Environmental Protection Agency.").
[15] 80 Fed. Reg. at 16,172.

Cynthia A.M. Stroman
Washington, D.C.
+1 202 626 2381
cstroman@kslaw.com
View Profile »

KING & SPALDING

Energy Newsletter

April 2015

DISPUTE RESOLUTION
Construction / Real Estate

Seventh Circuit Court of Appeals: No Coverage under Title Insurance for Mechanics' Liens Arising after Construction Lender Stops Funding

Sarah R. Borders, Jeffrey R. Dutson

On March 12, 2015, the United States Court of Appeals for the Seventh Circuit entered an opinion interpreting "the most litigated provision in the standard-form title-insurance policy purchased by real-estate lenders to protect their security interests in ongoing construction projects." [1] Exclusion 3(a) in the standard-form construction lender's title policy provides that liens that are "created, suffered, assumed or agreed to" by the insured lender will not be covered under the title policy. In *BB Syndication Services, Inc. v. First American Title Insurance Company*, the Seventh Circuit held, in the context of a failed construction project, that this exclusion applies to mechanics' liens arising as a result of a construction lender's decision to declare a default and stop funding additional loans. [2]

Background

Like most large construction projects, the "West Edge" project in Kansas City, Missouri was funded by a combination of a cash contribution from the developer, Trilogy Development Company (the "Developer"), and a construction loan from the lender, BB Syndication Services (the "Lender"), secured by the development. [3] The Lender's loan documents contained the customary provisions whereby the loan proceeds were disbursed only as the project progressed and the Lender had the ability to stop funding if the loan became "out of balance" —*i.e.*, if it became apparent that the cost of the project would exceed available funding. At closing, the Lender obtained a lender's title insurance policy from First American Title Insurance Company ("First American"). As the project progressed, the Lender obtained an updated title policy each time it disbursed new loan proceeds. [4]

One and a half years after construction began, the project's general contractor, J.E. Dunn Construction Co. ("Dunn"), asserted that design changes made by the Developer would likely increase the construction costs by $20 to $30 million. The Lender had only extended about $5 million of its $86 million loan commitment. [5] Notwithstanding Dunn's estimates of cost overruns, the Developer continued construction and the Lender continued funding. One year (and $56 million in loans) later, the Developer acknowledged that funding for the project was short by about $37 million. The Lender declared a default and stopped funding, and the Developer filed for bankruptcy. [6]

In bankruptcy, the Developer commenced litigation to determine the amount and priority of the liens of its various creditors. In addition to the Lender's $61 million secured claim, Dunn and several subcontractors held claims in excess of $17 million secured by mechanics' liens on the project. Because a substantial portion of the asserted mechanics' liens related to work done prior to First American's last update to the title policy, the

Lender looked to First American to defend the litigation and cover any loss. [7] However, First American denied coverage, asserting that the Lender caused the mechanics' liens to arise by cutting off funding for the project and, therefore, the liens were subject to Exclusion 3(a). [8] The Bankruptcy Court held that the mechanics' liens took priority, the project was sold to a third party for approximately $10 million, and the Lender, after reaching a settlement with the other claimants, received only $150,000 on its $61 million claim. [9]

Following First American's denial of coverage, the Lender sued First American in Wisconsin state court alleging breach of the title policy and bad-faith denial of coverage. First American subsequently removed the case to federal court, where the District Court held in a split ruling that: (a) First American breached its duty to defend and thus was required to reimburse the Lender for its attorneys' fees in the bankruptcy litigation; but (b) First American did not have an obligation to indemnify the Lender for the mechanics' liens because coverage was excluded under Exclusion 3(a). [10] The Lender promptly appealed the latter ruling to the Seventh Circuit Court of Appeals.

Seventh Circuit Opinion

Exclusion 3(a) excludes from coverage any liens "created, suffered, assumed or agreed to" by the insured lender. On appeal, the Seventh Circuit reasoned that the application of this exclusion turns on whether the Lender was at "fault" for the lien. Because the liens at issue here arose from work that went unpaid as a result of the Lender's decision to stop funding, the Court concluded that the liens arose directly from the Lender's actions and thus fell squarely within Exclusion 3(a). [11]

Noting that various courts have come to differing conclusions regarding the application of Exclusion 3(a), the Court reviewed authorities from the Eighth and Tenth Circuits supporting the exclusion and authorities from the Sixth and Eighth Circuits refusing to apply the exclusion in similar (although factually distinguishable) circumstances. The Seventh Circuit concluded that Exclusion 3(a) applies to mechanics' liens arising when a construction lender declares a default and stops funding. The Court reasoned that it is appropriate for the Lender, not First American, to bear the risk of unpaid subcontractors because "construction lenders have significant ability to ensure that the projects they finance remain economically viable—both at the beginning when deciding whether to finance a project and how much money to commit, and also throughout construction." [12] In support of this conclusion, the Court noted that construction loan documents, like the ones at issue in this case, usually give a lender broad rights to monitor the project and significant discretion when advancing funds throughout the course of the project. [13]

In light of a construction lender's ability to monitor the project and any cost overruns, the Court concluded that "when liens arise from insufficient funds, the insured lender has 'created' them by failing to discover and prevent cost overruns—either at the beginning of the project or later." [14] The Court held that the Lender can be said to have "created" or "suffered" the mechanics' liens that arose from insufficient project funds because the Lender, not First American, "had the authority and responsibility to discover, monitor, and prevent" such a loss. For these reasons, the Court affirmed the District Court's conclusion that the mechanics' liens were not covered under the title policy.

Lessons Learned

The Seventh Circuit's interpretation of Exclusion 3(a) in the standard-form construction lender's title policy places the risk of loss associated with unpaid subcontractors arising from a lender's decision to stop funding squarely on the construction lender, not the title insurer. There are, however, steps that a construction lender can take to mitigate this risk of loss. For example, a construction lender can request that the standard-form title insurance policy be modified to include the so-called "Seattle endorsement," which expressly protects a lender from intervening liens in situations in which it ceases funding as a result of the borrower's default. However, this type of endorsement is increasingly difficult to obtain and often requires state-by-state approval from the title insurer's senior management. Additionally, the lender can take steps to decrease the likelihood of default and non-payment by the borrower (*e.g.*, obtain a third-party guarantee or a performance bond). Finally, a construction lender must remain vigilant and closely monitor the progress of construction, outstanding balances

owed by the borrower to subcontractors, and potential cost overruns.

---

[1] *BB Syndication Servs. Inc. v. First Am. Title Ins. Co.*, No. 13-2785, 2015 U.S. App. LEXIS 3956, *1 (7th Cir. Mar. 12, 2015).
[2] *Id.* at *35–*37.
[3] *Id.* at *6.
[4] *Id.*
[5] *Id.* at *7.
[6] *Id.* at *7–*8.
[7] *Id.* at *8.
[8] *Id.*
[9] *Id.* at *9.
[10] *Id.*
[11] *Id.* at *15.
[12] *Id.* at *24–*25.
[13] *Id.* at *25.
[14] *Id.* at *29.

Sarah R. Borders
Atlanta
+1 404 572 3596
sborders@kslaw.com
View Profile »

Jeffrey R. Dutson
Atlanta
+1 404 572 2803
jdutson@kslaw.com
View Profile »
