

# Montalto di Castro PV: Debt in a cold climate

---

19/10/2009

At the end of 2008 SunRay Renewable Energy, a relatively new solar developer backed by private equity firm Denham Capital, approached banks with the biggest PV project in Italy to date – the Eu145 million (\$214 million) 24MW Montalto di Castro photovoltaic plant in Lazio.

Given the confluence of global financial crisis, the reluctance of banks to lend outside established sponsors, and the litigation and permitting headaches that often hinder Italian projects, the financing has been an unlikely success – so successful that SunRay already has permitting approval to increase capacity at Montalto di Castro to a world-beating 100MW and will be in the market for further project debt.

The choice of Lazio as the site for Italy's biggest PV project is unusual given Puglia is normally favoured by solar developers because of its southerly location and fast-track permitting laws for developments under 1MW. "We're located in Lazio for a combination of reasons. In the North of Lazio there is a sun trap that gets only slightly less solar radiation than Puglia, while the proximity to Rome ensures that the political environment is extremely stable," says Sean Murphy, chief technology strategist at SunRay. "Puglia has ample sunshine and initially offered rapid permits for smaller projects, but recent changes to the legislation have hindered the speed of development. Nonetheless, the South of Italy remains a very serious target for SunRay's development team."

SunRay's site also benefits from being only a few hundred metres away from one of the largest power distribution lines in Italy, with easy connection to the grid unlike most rural sites in the South.

Successful permitting, partial construction and project financing of the Montalto project validates SunRay's community-based development model, where professionals on the ground build relationships with key local stakeholders in the community, municipality and region.

Extensive legal due diligence by SunRay and regulatory clarity from the Lazio regional authorities significantly de-risked the project from a litigation standpoint and SunRay owns the land for the plant, preventing any security or legal issue arising from a tenancy agreement.

"We took an early decision to build an incredibly robust project with strong contractual risk allocation," says Tim Corfield, head of project finance at SunRay. "Banks were impressed by the extent of our own due diligence across all aspects, particularly on the project contracts and legal issues. We were focused on quality and value rather than necessarily cost in terms of our EPC contractor, SunPower, and our advisers Allen & Overy and Fichtner. We weren't trying to push the technology at all. We returned to old-fashioned project finance values – for instance, we issued a detailed information memorandum to banks, something that hasn't been done in the market for about five years!"

The Eu120 million debt is provided by BIIS, SG and WestLB, has a tenor of 19 years (construction plus 18.5-years amortization period) and features a cash sweep at year eight. Italian export agency, SACE, is guaranteeing part of SG's portion. The deal is levered between 80% to 85% and debt margin (unconfirmed by the deal's participants) is believed to start at between 275bp and 300bp. The banks also provided the project company, Cassiopea, with hedging against

interest rate fluctuations.

The financing should set a template for future large solar deals – particularly where multiple project companies are located near the same site and use the same substation and interconnection with the grid. The deal features a complex cost sharing mechanism for the substation, which is capable of handling up to 150MW, that allows future project companies to contribute to its cost on a pro rata basis depending on the project companies' power capacity.

Building a captive substation only makes economic sense for developers with larger plants. While SunRay plans to develop further phases of the project at Montalto di Castro to a total of 100MW, the project companies will be separate entities.

Other complex site-sharing issues such as the sharing of borders, rights of access and apportionment of insurance liabilities were also worked through by SunRay's legal counsel Allen & Overy. This structure, including agreements reached with the high-voltage grid operator Terna in relation to the substation's operation, is the first of its kind in Italy in the solar sector.

SunPower is the EPC contractor and is supplying back-contact mono-crystalline modules and single-axis tracking technology. SunRay also commissioned a high-voltage substation from Terna which will evacuate power from the full-scale 100MW plant directly onto the 150kV high voltage grid. Construction began in February funded from equity.

Lenders took comfort from a suite of guarantees provided by SunPower. The lump-sum turnkey EPC contract contains liquidated damages to cover delays and a specific compensation package if the plant is not connected to the grid by the end of year and is therefore ineligible for 2009-level tariffs. The project is on track to be connected to the grid by the end of 2009 and for full commissioning in Q1 2010.

SunPower is also providing availability guarantees for the entire duration of its 20-year operation and maintenance contract. The credibility of the availability guarantee is supported by the average operating performance of its solar units (used extensively in the US and Spain). Banks were comfortable with the relative credit strength of SunPower compared with its peers, some of which are struggling due to overcapacity in the production of solar panels and associated equipment.

As a ground-based tracking plant above 20kW the project also benefits from a tariff of Eu0.35 per kWh. This tariff is fixed for 20 years – a key issue for SunRay given the 2009 tariff fell 2% from 2008 and is due to fall by 2% in 2010.

On top of the tariff, the project revenues include the merchant sale of electricity to GSE, an arm of the Ministry of Economy and Finance. SunRay, on approval from the lenders, also has the ability to negotiate power purchase agreements with end users.

While SunRay has benefited from locking in a 2009-tariff, after 2010 there is uncertainty. The Italian government has indicated that it will avoid the precipitous drop in photovoltaic feed-in tariffs that have blighted further investment in countries like Spain (Spanish PV tariffs were slashed by 30% in 2008), by gradually lowering tariffs.

Stefano Saglia, Undersecretary of Economic Development with special responsibility for energy, recently announced a gradual reduction in incentives was likely, but in line with the falling cost of photovoltaic panels to avoid the trauma caused in Spain. So far, there have been no official figures or proposed solution, but government and industry negotiations will take place in the next few weeks.

The next large solar deals to come to the market are both located in Puglia and should be financed by the end of the year. AES has a 43MW plant with a funding requirement of around Eu205 million – there is a seven-strong bank club in place led by SG and Unicredit, and including Rabobank, WestLB, Calyon, BNP Paribas and Dexia. Global Solar Fund is also in the market for a 48MW plant with backing from CDP, Unicredit, Intesa, WestLB and Santander.

As a template, Montalto di Castro will have most relevance for upcoming developers backed by private equity houses. SunRay has demonstrated that financing for new developers is achievable, even in the recovering financial climate, if relationships with local stakeholders are built and maintained (SunRay has a dedicated team of over 35 people in Italy),

there are enough people on the ground to manage construction, proven technology is used and equity is committed before financing. New developers must also convince banks they are in it for the long haul to offset angst over equipment unreliability and poor project management.

As well as holding assets for the long term, SunRay differentiates itself from pure private equity houses by actively managing projects through construction and operations, and has significant experience in both engineering and financing: Both Murphy (from Nomura) and Corfield (from Deutsche and Bank of America) have extensive banking experience.

Corfield is convinced that solar deals will soon be introduced to the capital markets. "Solar should be an investment grade asset. The asset class, like most infrastructure, is well suited to the capital markets – it is supported by feed-in tariffs so it is a long-term regulated asset. Also, banks have a finite amount of capital. We are exploring all options such as leasing and the involvement of the EIB. When it comes to those options, maturity is our priority."

SunRay has a strategic partnership with Denham Capital to develop over 300MW of solar projects by 2012 and is focusing on large utility-scale projects. By using its community-based development model with environmental integration it hopes to develop large PV plants beyond Italy in parts of France, Greece and Israel.

The next financing for SunRay is for a 9MW plant at the same site as Montalto di Castro, located in the middle of the 24MW plant. Financial close is due this year. SunRay also has permitting and plans to finance a 12MW plant and a 60MW plant, either as a single deal or separately, at adjacent sites in Lazio. The fully developed 100MW PV plant will be the largest in the world, surpassing the current leader – the 60MW Olmedilla plant in Spain.

#### **Cassiopea PV S.r.l.**

Status: Signed 17 September, financial close 24 September, drawdown 30 September

Description: Eu120 million financing of a ground-tracking PV solar plant in Montalto di Castro Lazio, Italy

Sponsor: SunRay

Mandated lead arrangers: Banca Infrastrutture Innovazione e Sviluppo (facility agent and insurance); Societe Generale jointly with SACE (coordination and documentation); WestLB AG (technical and modelling)

Sponsor legal counsel: Allen & Overy

Lender legal counsel: Gianni, Origoni, Grippo & Partners

Technical adviser: Fichtner

Insurance: Marsh

Energy market adviser: Poyry

*Thank you for printing this article from IJGlobal.*

*As the leading online publication serving the infrastructure investment market, IJGlobal is read daily by decision-makers within investment banks, international law firms, advisory firms, institutional investors and governments.*

*If you have been given this article by a subscriber, you can contact us through [www.ijglobal.com/sign-in](http://www.ijglobal.com/sign-in), or call our London office on +44 (0)20 7779 8870 to discuss our subscription options.*