North American Solar Deal of the Year 2012: Topaz Solar

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Large utilities are taking the lead in developing new capital markets financing structures for solar power assets. They have the financial and technical resources to meet non-bank lenders concerns about construction and operational risk, and the ability to make large equity commitments.

Even allowing for the advantages that MidAmerican Energys utility operations and Berkshire Hathaway parentage confer, the bond financing for its Topaz solar project marks several firsts. It is comfortably the largest renewables bond financing ever, the first large-scale solar financing that does not feature a government guarantee, and the first rated investment grade from all three agencies.

With these steps, MidAmerican has expanded the group of possible buyers of solar project bonds immensely. It also used its financial resources to mitigate one of the most common complaints with greenfield project bond financings negative carry.

Topaz is a 550MW solar photovoltaic project located in San Luis Obispo county, California. The projects original developer was Optisolar, which was unable to raise the financing for the project itself, but managed to sign, and win California Public Utility Commission approval for, a 25-year power purchase agreement with Pacific Gas & Electric. Optisolar sold its development portfolio with the Topaz project as its crown jewel to First Solar in 2009.

First Solar is supplying the project with its own Series 3 cadmium telluride thin-film solar photovoltaic modules, and will be building and operating the plant. First Solars original plan was to use a guarantee from the US Department of Energy to help fund construction, and received an offer for a $1.93 billion guarantee under the departments financial institutions partnerships programme, with RBS as lender-applicant. It was, however, unable to close on that deal by 30 September 2011, when the departments authority to offer the guarantee expired.

In early December 2011 First Solar agreed to sell the project to MidAmerican. MidAmerican, a subsidiary of Berkshire Hathaway, owns utility operations in Iowa, Illinois, South Dakota, and Nebraska, and a substantial wind portfolio, but had not made any solar investments before Topaz. But MidAmerican was one of the few entities able to meet the equity commitment on a $2 billion solar plant, not to mention cope with the carry issues associated with a large bond financing.

MidAmericans way of dealing with the negative carry on a bond issue was to defer a large chunk of the bonds until later on in construction, and provide an equity backstop to that issue. The project would still have been economical if MidAmerican had had to borrow the full amount upfront, but according to Calvin Haack, MidAmerican Energy Holdings Companys treasurer, negative carry was one of the many economic impacts we considered as well as depth of the investor market for these types of projects. It planned a $700 million initial issue, followed by a subsequent $565 million tranche. In the end, investor demand was strong enough that the sponsor felt that an increase to $850 million on the initial tranche was justified.

The 144A issue priced for an all-in interest rate of 5.75% and will mature in 2039. Barclays (left lead), Citi and Royal Bank of Scotland ran the sale, along with co-managers Bank of Tokyo Mitsubishi UFJ, Lloyds, Mizuho and Royal Bank of

Canada. The bookrunners are also providing the project $345 million in five-year letters of credit.

MidAmerican, to meet its target $1.265 billion total debt amount, now just needs to issue another $415 million in bonds. The bond deal closed on 16 February 2012, though construction on the project started in December 2011, with completion scheduled for all 550MW in February 2015.

The success of the lead banks in increasing the issue size, closing the deal so quickly, and winning investment grade ratings from Moodys and S&P (BBB- and Baa3, respectively) should not obscure how new the asset class was. Ratings agencies had issued few public ratings, and none for uncovered issues. First Solar, as supplier, builder and operator, was assumed to be under many of the same stresses as solar panel manufacturers everywhere.

The rest of the projects $2.44 billion total costs will be met with sponsor equity, though that total includes the 30% investment tax credit for which solar projects are eligible, and which MidAmerican is well-placed to exploit.

MidAmerican now appears comfortable with the risks attached top solar projects. On 2 January this year it said it would buy the 579MW Antelope Valley solar project from SunPower. Antelope Valley has 20-year power purchase agreements with Southern California, and a $2.5 billion price tag.

Topaz provides an obvious financing template for well capitalised utility sponsors that do not need to include any tax structuring or absorb all of the negative carry on solar deals. Haack sees no reason why a strong sponsor could not replicate the structure. For the largest utility-scale projects, it will serve as a benchmark. Smaller deals for smaller sponsors will have to use more complicated and more expensive debt products.

Topaz Solar Farms LLC
Status
Closed 16 February 2012
Size
$2.443 billion
Description
Project bond financing for a 550MW solar photovoltaic power project
Sponsor
MidAmerican Energy
Debt
$1,280 billion
Bookrunners
Barclays, Citi, RBS
Managers
Lloyds, Mitsubishi UFJ, Mizuho and RBC
Sponsor financial adviser
Barclays
Sponsor legal counsel
Gibson, Dunn & Crutcher
Underwriter legal counsel
Latham & Watkins
Underwriter insurance adviser
Aon
Trustee
Bank of New York Mellon
Independent engineer and solar resource consultant
Black & Veatch
Developer, supplier, EPC and O&M contractor
First Solar

Developer legal counsel
Skadden, Arps, Slate,
Meagher & Flom