

## Developers Beware: Agricultural Subsidies Create Unique Legal Risks

In the 2011 fiscal year, the United States Department of Agriculture (USDA) is planning to spend roughly \$1.9 billion on conservation programs designed to encourage landowners to improve their natural resource stewardship, and meet environmental challenges on their land. Roughly 275 million acres are enrolled in these programs this year, with an estimated 300 million acres anticipated in 2011.

These programs exist in many forms, but the two most commonly found are the Environmental Quality Incentives Program and the Conservation Reserve Program.

### Environmental Quality Incentives Program (EQIP)

With roughly 190 million acres enrolled in 2010, EQIP is the largest of the USDA's conservation programs. EQIP encourages landowners to implement certain conservation management practices by refunding up to 75 percent of the incurred costs and income foregone, with total payments within six years not to exceed \$300,000.

However, if the landowner permits an activity that defeats the purpose of the program or transfers an interest in the land to a party who is unwilling or unable to perform, the landowner could lose the right to all future payments, be required to refund past payments plus interest and be subject to liquidated damages. Depending on the wording of any agreements between the landowner and the developer, it is possible that the developer might be required to pay the landowner's damages to the USDA.

### Conservation Reserve Program (CRP)

With roughly 31 million acres enrolled, CRP is the second largest USDA conservation program. CRP helps agricultural producers safeguard land by incentivizing, through rental payments and cost sharing, the planting of long term covers to improve the quality of water, control soil erosion, and enhance wildlife habitat.

If the USDA determines that the landowner has breached a CRP contract, the landowner may lose the right to all future payments, be required to refund past payments received plus interest and be subject to liquidated damages. A developer may be liable to the landowner under contractual provisions of leases or easements which may require the developer to indemnify the landowner for such costs.

Because it is often difficult to discover whether a parcel of land is enrolled in a program, it is vital for developers to obtain experienced energy legal representation. ■

THE POLSINELLI SHUGHART WIND AND RENEWABLE ENERGY DEVELOPMENT group is experienced in the areas of corporate/transactional law, energy, real estate, construction, environmental, land use/zoning, finance, governmental affairs and litigation. With more than 495 attorneys in 14 cities stretching from Washington, D.C., to Phoenix, Polsinelli Shughart is where energy development is occurring. For more information and contacts within the Energy group, see page 6.

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## Severance of Wind Rights

The question of severance of wind rights is a matter that will likely be decided by the state legislatures, but in the absence of any state statute, the court systems are forced to interpret the law utilizing analogous mineral, oil, gas and water examples.

### State Legislatures

Only a few state legislatures have directly weighed in on wind severance, but those that have are so far unanimously opposed. The state legislatures of Nebraska, North Dakota and South Dakota have all enacted statutes prohibiting severance.

### Courts

- In 1997, the California Court of Appeals held that wind rights are distinct and severable from the fee simple estate in *Contra Costa Water Dist. v. Vaquero Farms, Inc.* The court disagreed, holding that wind developers could hold the wind rights without owning any interest in the underlying land.

- Last year, the United States District Court for the District of New Mexico also issued an opinion on wind severance in *Romero v. Bernell*. The court in *Romero* held that wind rights could be severed, so long as the property's principal value is derived from wind farm development. However, the court further stated that the wind rights do not vest until they are reduced to possession, and therefore wind rights cannot be severed until after wind power has actually been generated.
- Currently a case being considered by the Kansas Supreme Court which might determine the permissibility of severance of wind rights in that state. The case, *Zimmerman v. Board of County Commissioners of Waubensee County*, deals with a county's outright ban on wind farm developments, which one wind developer claims constituted an unconstitutional taking of wind rights which had been severed. ■

## Cash Grant Program Stimulus — Update

Section 1603 of the American Recovery and Reinvestment Act of 2009 (ARRA) gives qualifying taxpayers the option of receiving a cash grant (a Section 1603 Grant) in lieu of the investment tax credit (ITC) under Internal Revenue Code (IRC) Section 48 or the production tax credit (PTC) under IRC Section 45. The Section 1603 grant was primarily created to alleviate concerns with tax equity financing availability created by the recent financial system crisis.

### Eligible Projects

Applicants may receive Section 1603 Grants for investments in the following types of renewable energy property: solar electric, thermal, or lighting property; wind energy property; closed-loop and open-loop biomass property; hydropower property; marine and hydrokinetic renewable energy property; geothermal property; fuel cell property; microturbine property; combined heat and power system property; and landfill gas and trash combustion property.

Section 1603 Grants generally range in amounts from 10 percent to 30 percent (depending on the type of property) of the tax basis of qualifying renewable energy property placed in service by the grant applicant. For wind and solar developments, the amount is 30 percent.

### In-Service Requirements

To qualify, property must generally be placed in service during 2010. However, even if property is placed in service after 2010, it may still qualify if construction began during 2009 or 2010, provided that the property is placed in service before 2013 (in the case of large wind property), 2017 (in the case of IRC Section 48 property) or 2014 (in the case of other qualifying property). In addition, the property must be eligible for depreciation or amortization.

### Subsequent Guidance

On July 9, 2009, the Treasury Department issued the following guidance:

- The Treasury Department's Program Guidance on Section 1603 Grants: <http://www.ustreas.gov/recovery/docs/guidance.pdf>
- A "sample" Application Form for Section 1603 Grants: <http://www.ustreas.gov/recovery/docs/Application.pdf>
- The Terms and Conditions applicable to Section 1603 Grants: <http://www.ustreas.gov/recovery/docs/energy-terms-and-conditions.pdf>

Supplemental guidance was issued in January 2010. And in March 2010 the Treasury issued Revised Guidance which largely restates the July 2009/January 2010 guidance, but substantially revises the section of the previous guidance relating to the “beginning of construction” requirement for projects placed in service after 2010.

Based on the success of the 1603 Grant Program, there are also legislative efforts to extend the bill. As of the date of this newsletter, the Feinstein-Merkley Bill, S. 2899 has been proposed to extend the cash grant program through 2012. Additionally, H.R. 4599 would enable taxpayers to elect to receive the payment either as a cash grant or a tax credit through 2013 (Rep. Blumenauer’s proposal). Finally, S. 3069 would suspend the program indefinitely until it is legislatively to prevent funds from being spent overseas. ■

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## NEPA Update — Proposed CEQ Guidance Indicates Renewed Focus on Mitigation

The Council on Environmental Quality (CEQ) has proposed new draft guidance on the implementation and monitoring of mitigation efforts to reduce the environmental impacts of projects subject to the National Environmental Policy Act (NEPA). This guidance, which is open to public review and comment until May 24, 2010, provides valuable insight into the new administration’s focus upon improvement of mitigation measures.

New CEQ Guidance – Methods to Improve Mitigation. CEQ recognizes that successful mitigation involves consideration of future impacts and conditions, which is especially true for the evolving alternative energy industry. To help promote robust mitigation practices, CEQ proposes three goals to improve agency mitigation and monitoring.

The first goal strives to ensure that mitigation requirements are enforceable. To this end, CEQ proposes several new requirements concerning mitigation implementation and documentation. First, CEQ proposes that agencies require that all mitigation measures undertaken be thoroughly documented in NEPA documents, and

suggests methods for ensuring this implementation is enforced, such as conditioning funding, permits or approvals on the fulfillment of measurable performance standards. Second, CEQ proposes the adoption of more adaptive management policies to ensure that, if a mitigation strategy is not working efficiently, the agency can respond quickly to correct the problem.

CEQ’s second proposed goal is to improve agency monitoring of mitigation program implementation and effectiveness. To encourage better mitigation monitoring, CEQ proposes that monitoring be implemented each time a mitigation commitment is made, with the party responsible for oversight of the mitigation clearly identified in the transaction documents.

CEQ’s third goal is to encourage more thorough public involvement for mitigation monitoring. To this end, CEQ proposes that agencies make the results of all mitigation monitoring reports publicly available through online and print media rather than requiring that requests be made directly to the agency, as is currently the case. ■

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## Renewable Portfolio Standards — New Developments

Although renewable portfolio standards have gained an increasing amount of momentum in recent years, some states long ago took the lead in encouraging the development of alternative energy sources through the adoption of programs known as Renewable Portfolio Standards (RPSs). First enacted in Iowa in 1983, RPS programs are state legislative initiatives that require threshold amounts of a utility company’s total energy portfolio be generated from renewable sources (such as wind, solar, biomass,

geothermal or other sources). Typically, these laws provide that the percentage of renewable energy that must be generated by a utility company increases incrementally over time, until the full renewable energy target is met.

Currently, 35 states and the District of Columbia have enacted some form of RPS program. Because these RPS programs were implemented individually, they vary significantly from state-to-

state, as you will see in the enclosed chart. Furthermore, the penalties for not meeting the standard range significantly from mandatory fines (the most common result) to no fines at all (as in North Dakota).

State	Amount	Year
Arizona	15%	2025
California	33%	2020
Colorado	20%	2020
Connecticut	23%	2020
District of Columbia	20%	2020
Delaware	20%	2019
Hawaii	40%	2030
Iowa*	105MW/1,000MW	2010
Illinois	25%	2025
Kansas	20%	2020
Massachusetts	22.1% **	2020
Maryland	20%	2022
Maine	40%	2017
Michigan	10% + 1,100 MW	2015
Minnesota	25%	2025
Missouri	15%	2021
Montana	15%	2015
New Hampshire	23.8%	2025

State	Amount	Year
New Jersey	22.5%	2021
New Mexico	20%	2020
Nevada	25%	2025
New York	29%	2015
North Carolina	12.5%	2021
North Dakota*	10%	2015
Ohio	25%	2025
Oregon	25%	2025
Pennsylvania	18%	2021
Rhode Island	16%	2019
South Dakota*	10%	2015
Texas	5,880 MW	2015
Utah*	20%	2025
Vermont*	20%	2017
Virginia*	15%	2025
Washington	15%	2020
West Virginia*	25%	2025
Wisconsin	10%	2015

\* The following states have set voluntary goals instead of mandatory portfolio standards: Iowa, North Dakota, South Dakota, Utah, Virginia, Vermont and West Virginia.

\*\* Plus 1% each year, thereafter. ■

## Colorado State Law Update

In March 2010, Colorado Governor Bill Ritter signed into law House Bill 1001, which expands the scope of the state’s existing Renewable Portfolio Standard (RPS). Although Colorado has had an RPS since November 2004, when it became the first state to enact an RPS by ballot initiative, this new legislation establishes it as a leader among the states in establishing strong mandates on renewable energy.

### The New Standards

Prior to this new legislation, Colorado’s existing RPS required investor-owned utility companies in the state to generate or purchase enough renewable energy to supply 20 percent of their

retail electric sales by 2020. House Bill 1001 increases this mandate to 20 percent renewables by 2015, and 30 percent by 2020.

The new law also states that three percent of investor-owned utilities’ total retail electric sales must come from small-scale distributed generation systems (such as residential solar systems) by 2020. The Governor’s Energy Office predicts that this standard could help promote the use of residential solar panels and small wind turbines, and thereby provide energy consumers another tool to lower their electricity bills.

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### Rationale for the Change

The lawmakers behind the new legislation have cited several reasons for increasing the RPS.

First, Colorado's largest public utility company, Xcel Energy, publicly supported increasing the RPS, which marks a shift in its stance on the mandatory standards. Xcel opposed the 2004 legislation that implemented the first Colorado RPS, but since has been able to more fully evaluate and optimize its plans for generating and managing the new renewable resources.

The second rationale for increasing the RPS relates to Colorado's significant population growth.

Current projections indicate that Colorado's population in 2009 was 5,083,000, a nearly 18 percent increase. With this influx of new residents comes an increased demand for additional electricity. Because Colorado currently only generates about six percent of its power from renewable sources, this increased demand for electricity will require a significant amount of new renewable generation in order to keep pace with the RPS. ■

## Illinois State Law Update

### Proposed Legislation to Extend the "Illinois Preference"

During the current legislative session, Illinois legislators have been considering several bills that which would extend a key policy instrument favoring Illinois-based renewable energy projects over other states (S.B. 2550, S.B. 3686, and H.B. 4797). Under current law, the so-called "Illinois preference" expires June 1, 2011. These proposed bills would extend that date until 2016. However, recent efforts by one of the state's largest utilities may thwart this effort.

The Illinois preference is a component of the state's Renewable Portfolio Standard, which passed in 2007. Under Illinois' current RPS, the Illinois Power Agency, which procures power for Illinois' major electric utilities, must purchase power from Illinois projects before purchasing from other states. The preference clause has benefited Illinois renewable projects, which last year fulfilled the entire RPS requirement in the state.

However, recently, Exelon Corporation has vigorously lobbied against the bills, demonstrating that cost of Illinois wind energy is higher than in other states like Texas, North Dakota and Iowa, where property taxes are lower and turbines have more capacity. As the time of this publication, these bills remain pending.

### City of Evanston Approves Offshore Wind Proposal

In April, 2010, the Evanston, Illinois City Council voted unanimously to pursue an approximately 200MW offshore wind farm in Lake Michigan. The next step in the project will be to determine the feasibility and estimate costs, and the city plans to issue a Request for Information (RFI) from wind developers in the near future.

### Proposed Legislation to Extend Illinois' Property Tax Valuation for Wind Turbines

The Illinois Legislature passed Public Act 095-0644, which provided, among other things, that beginning in the 2007 assessment year through 2011, wind energy devices larger than 500 kilowatts (kW) and producing power for commercial sale would be valued at \$360,000/Megawatt (MW) of capacity, adjusted annually based on the CPI. Because Illinois assesses property for property tax purposes at 1/3 of its fair cash value, the assessed value of commercial wind energy property has been \$116,998/MW (adjusted for inflation).

While this five-year "test period" is currently set to expire in 2011, the Illinois Legislature has been considering extending the applicability of the law another five years, or until 2016. As of the time of this publication, this bill remains pending. ■

## Prominent Environmental and Regulatory Groups Join Polsinelli Shughart

### Polsinelli Shughart Expands Environmental Practice

The Phoenix office of Polsinelli Shughart now houses one of the largest environmental and natural resources law groups in the southwestern United States. The nine lawyers bring decades of nationwide experience in all aspects of environmental counseling, permitting, liability transfers, litigation and enforcement defense with special emphasis on energy and mining industries. Shareholder Lucas J. Narducci leads the group. In addition to his general business and transaction practice, he has specialties in mining, environmental, natural resources, safety and health law.

Margaret B. LaBianca is also a shareholder in the group with more than 10 years of experience counseling clients on a broad range of regulatory compliance and strategic considerations with respect to development, operations and transactions. She has extensive experience working with clients involved in solar power development.

### Polsinelli Shughart Adds Jefferson City Presence

With the addition of Jefferson City-based Hendren Andrae LLC in April 2010, Polsinelli Shughart expanded its public policy, government relations, regulatory law and business litigation

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services in the state capital of Missouri. The firm now has public policy presence in four state capitals and in Washington, D.C.

The acquisition of Hendren Andrae complements the firm's nationally recognized Regulatory Law group, Business Litigation practices, and Public Policy group. Former Missouri Congressman Kenny Hulshof, who divides his time between Kansas City, St. Louis and Washington, D.C., will also maintain an office in Jefferson City. The firm also recently announced the addition of Pete Levi, former president of the Greater Kansas City Chamber of Commerce, who leads the Kansas City regional public policy practice group and will be closely aligned with the Jefferson City team.

#### **Polsinelli Shughart Adds Nationally Known Energy Attorneys**

Mark A. Gershon and Ronald G. Rossi have joined Polsinelli Shughart's Wind and Renewable Energy Development group as equity

shareholders. Mr. Gershon practices in the firm's Chicago office and Mr. Rossi is based in the Polsinelli Shughart Denver location.

Mr. Gershon has been involved in many of the largest energy projects in the Chicago region. His clients include owners and developers of energy facilities, including wind farms, peak and base load energy plants and other renewable energy projects, in addition to industrial, office and retail centers, and redevelopment of challenged sites ranging from former oil refinery, brownfield and deteriorated sites to economically challenged properties.

Mr. Rossi assists clients in the energy and biotechnology fields with complex financial transactions. He serves the Denver region's leading and emerging clean technology and alternative energy industries. He brings more than 30 years of experience related to mergers and acquisitions, corporate governance and finance and project development in industries such as oil and gas, alternative energy, biosciences, health care and technology. ■

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## About Polsinelli Shughart's Wind and Renewable Energy Development Group

Polsinelli Shughart attorneys have extensive knowledge of renewable energy development, energy industries and public utility services. Our team includes the former General Counsel for the Kansas Corporation Commission, a former Congressman who represented the Dallas-Fort Worth area for 26 years in the U.S. House of Representatives, and attorneys with significant experience in areas such as wind and renewable energy, oil and gas, regulatory and governmental affairs.

Our attorneys acted as lead counsel in the development and construction of one of the largest wind farms in Kansas. The total project size is approximately 250 MW. In assisting with

the development, Polsinelli Shughart negotiated leasehold arrangements with more than 100 landowners that encompass nearly 30,000 acres.

With more than 495 attorneys and offices throughout the country, Polsinelli Shughart attorneys offer service in key renewable energy regions. We are assisting wind developer clients with current and ongoing development of more than 30 wind projects in 12 states: Texas, Oklahoma, Kansas, Colorado, Iowa, Nebraska, Arkansas, Indiana, Ohio, Illinois, Michigan and Missouri. Once completed, these projects will generate nearly 10,000 MW of renewable energy.

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Polsinelli Shughart is very proud of the results we obtain for our clients, but you should know that past results do not guarantee future results; that every case is different and must be judged on its own merits; and that the choice of a lawyer is an important decision and should not be based solely upon advertisements.