FIT 2.0 contract finalized

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Following the draft feed-in-tariff (FIT) contract released on April 5, 2012 (our commentary on the draft is available here), the Ontario Power Authority released the final form of the new FIT contract on August 10, 2012. With this contract and the new rules released on the same day, Ontario has reformatted its FIT Program – FIT 2.0 – to give greater incentives to developments by or including aboriginal groups, community groups and education and health providers.

Applications for "small" FIT contracts, being projects which, subject to the voltage of their connection line, are under 500 kW, will be accepted between October 1, 2012 and November 30, 2012. During that period, FIT applications made under the existing FIT Program framework may transition to the new FIT 2.0 regime. For further discussion on the new FIT rules, see our blog post here.

Below is a summary of material points in the new contract:

Changes to Project Specifications
As was proposed in the draft contract, the OPA will be able to arbitrarily refuse any change to the specifications of a project listed in the contract or the application. Based on FIT 1.0 experience, this could include minor changes to the connection point, GPS location, feeder and so on. Under FIT 1.0 the OPA could not unreasonably reject those changes. Developers should be cautious to carefully review and double-check their site specifics before submitting an application.

Pre-NTP Termination
The final version of the contract affirms the OPA's right to assume any security paid by the developer as damages if the developer opts to terminate the contract before it obtains "notice to proceed". This is consistent with the OPA's current practice. The OPA is also entitled to terminate the contract before the notice to proceed is issued provided any security payments are returned to the developer and documented pre-construction costs, up to a maximum limit.

The final version of the contract clarifies that the "Stop Work Direction", by which the OPA can force a developer to stop all construction and development, can only be issued if the OPA exercises its pre-NTP termination right, which was not clear in the draft contract.

Post-NTP Termination
Developers hoping to finance their projects will likely breathe a sigh of relief as the right the OPA had in the draft contract to terminate the contract at its convenience after notice to proceed was issued has been removed from the final version of the contract. Many lenders had suggested to us that they would not be prepared to lend to FIT 2.0 projects if the termination-for-convenience right remained in the contract.

Deadline Changes

While small FIT projects used to be able to submit their NTP requests at any time before the milestone date for commercial operation, an NTP request under FIT 2.0 contracts must be submitted at least 3 months before the milestone date. Large FIT projects will still need to submit the request at least 6 months before the milestone date as failure to do so is an event of default that entitles the OPA to terminate the contract. Under the final version of the contract, large FIT projects that miss that deadline must provide whatever information the OPA requires, which will include at least status information regarding the project and a "credible and detailed project plan" demonstrating how the project will achieve commercial operation.

The milestone date for rooftop solar projects has been reduced to 18 months following the contract date whereas, under FIT 1.0, such projects had the same timeframe as those for projects using other types of fuel (i.e. 3 years). However, rooftop solar projects can maintain the 3 year milestone date if they are part of a portfolio of two or more projects and the developer's application for a designation as a portfolio is accepted by the OPA. Developers should be cautious applying for portfolio status – once a project is part of a portfolio, the OPA will consider it to always be part of the portfolio and the developer may not be able to sell each portfolio in parts.

Term and MCOD Penalties

While under the FIT 1.0 contract, a developer could miss the milestone date and buy-back the portion of the 20-year term lost by the delay by paying liquidated damages, the term of FIT 2.0 contracts will now start to run on the milestone date and a term "buy-back" is not available. Accordingly, each day after the milestone date before the project achieves commercial operation is one day of lost FIT revenue. We expect this change will cause lenders to exert significant pressure to ensure projects achieve commercial operation on or before their milestone dates.

The additional $0.25/kW payable per day as liquidated damages for failing to reach commercial operation by the milestone date, as contemplated in the draft contract, has been deleted.

Contract Capacity

The OPA has reverted to substantially the same obligation as previously existed under the former FIT regime regarding meeting contract capacity, meaning a developer can satisfy its obligations by building a project which is able to produce at least 90% of its contract capacity at the commercial operation date. As in the FIT 1.0 contract, if the project is above 90% but below 100% at commercial operation, the developer can still bring the project's contract capacity up to 100% within 1 year after commercial operation.

Rooftop solar facilities, however, cannot be overbuilt by more than 120%. In particular, the DC nameplate rating of the installed modules cannot be more than 120% of the AC nameplate rating of the installed inverters.

Domestic Content – Operation and Maintenance

The OPA has revised the domestic content obligations of wind and solar projects. In addition to being developed and constructed in order to meet the minimum required domestic content level (e.g. 50% for wind and 60% for solar, based on the satisfaction of specific designated activities), each of those projects are also required to operate and maintain the project in accordance with the minimum required domestic content level.

Although the contract entitles the OPA to audit at any time, the developer is only required to retain records for a limited period of time and the developer only reports on its domestic content activities within 90 days after achieving commercial operation. These audit and reporting obligations were not changed in the final version of the contract. Thus, while the developer has an obligation to maintain the facility in accordance with its domestic content obligations, it's unclear how it would demonstrate those obligations after it submits its domestic content report and its record retention obligation expires.

Regardless, developers should be cautious of this obligation when considering which designated activities it will rely upon to meet its domestic content obligation and whether the warranties offered by the equipment suppliers for those designated activities will satisfy the designated activities. Developers should also take this obligation into consideration when looking at its insurance coverage.

Domestic Content Report

The domestic content report regime has improved from the draft 2.0 contract. The OPA is now required to review and respond to the report within 90 days of its receipt of the report rather than having a "reasonable" time. Both parties are required to cooperate after the OPA requests any additional information in order to finalize the report within a reasonable period. Under the FIT 1.0, the OPA had 60 days to review, then the developer had 30 days to respond and the OPA then had 30 more days to review the response.

REA Representation

As was the case in the draft, developers represent that they have made due inquiry into the requirements to obtain a renewable energy approval (where applicable). The effect of this representation is that the developer will not be able to claim force majeure for any issue related its REA which ought reasonably to have been known to the developer at the time it made its application. Developers requiring an REA should perform due diligence investigations prior to applying for a 2.0 FIT contract to ensure it can reasonably obtain an REA.

Participation Points

Developers who are relying on community, aboriginal or education or health equity participation should carefully review provisions relating to participation projects and the applicable definitions. If, for instance, a developer has a community co-op as an equity participant and that co-op fails to maintain the minimum required number of members (who must, in addition to being a co-op member, also own land in the community in which the project is built over a rolling 2 year window), the OPA will be entitled to terminate the FIT contract. Although there are certain rights to cure that kind of a default, it may be difficult for the developer to recruit new members to a co-op or to convince co-op members to remain landowners in the area.

Those relying on points for hosting the project on an education or health facility should seek comfort that the facility will remain an education or health facility for at least 5 years after commercial operation. Subject to the ability of the supplier to cure by either becoming a participation project or replacing the education or health host with a new education or health host (both of which may be difficult to do after the project is operational), if the facility changes use before such time (which could occur through no fault of the developer), the developer will be in breach of the FIT contract. While still risky, the 5 year milestone will be more palatable to developers than the 10 year milestone contemplated by the draft contract.