CP Energy

US Wind Tax Equity Update

September 2008

Table of Contents

Overview of CP Energy

- Established in 2004 between affiliates of Commonwealth Capital Advisors, LLC ("CCA"), a Boston-based financial advisory and investment firm, and Paragon Energy Holdings LLC ("Paragon"), a Houston-based energy asset management and advisory firm.
- CP Energy's renewable technology experience includes wind, solar, geothermal, biomass and biofuels.
- CP Energy provides renewable energy project advisory and asset management services to institutional investors and project sponsors.
- The principals of CP Energy have significant renewable energy experience in finance, development and operations and have worked with numerous developers, equity investors and debt providers that are currently active in the market.

Select Recent Wind Energy Experience

- Since the first quarter of 2006, CP Energy has advised either the tax equity or project sponsor in connection with the financing of 31 wind farms in 10 states with an aggregate nameplate capacity in excess of 3600 MW.
- Advised Orion Energy in connection with the sale of its 4 GW wind development portfolio and development platform to BP Alternative Energy North America.
- Advised a developer on a 2GW wind development portfolio transaction focused on the Southwest renewable energy market.
- Advised Noble Environmental Power, LLC in connection with the term financing of an approximately 282 MW project portfolio in New York. Deal recognized as "2007 North American Renewables Deal of the Year" by Project Finance Magazine.
- Arranged a $420 MM turbine loan with a 100% advance rate for a large wind developer.
- Representative clients include BNB Renewable Energy, BP Alternative Energy North America, Eurus Energy America Corporation, Foresight Wind Energy, Metropolitan Life Insurance Company, MSD Capital, Noble Environmental Power, Orion Energy, Textron Financial Corporation, Third Planet Wind and Wachovia Securities.

Other Energy Industry Experience

- CP Energy advised an institutional investor in connection with its investment in an approximately 750 MW CCGT project located in Texas.
- A CP Energy affiliate advised an institutional investor in connection with its investment in an approximately 240 MW geothermal project located in California.
- CP Energy affiliates currently serve as asset manager for a gas fired cogeneration facility in Henderson, Nevada and a waste coal power generation facility in Colstrip, Montana.
- CP Energy affiliates also manage a compression services company with 4 electric compression stations in New Mexico and Florida.
- CP Energy affiliates have a significant ownership interest in and serve as the co-manager of a 357 mile natural gas pipeline in Colombia.
- CP Energy has hands-on experience in structuring, negotiating and implementing agreements and transactions to hedge both physical and financial commodity delivery and price risk.

Other Energy Industry Experience (cont'd)

- For further information regarding CP Energy and its personnel, please visit our website at www.cpenergygroup.com.

General Market Update

- Various factors have contributed to robust domestic growth in the US wind market over the past several years.
- Consecutive renewals of the production tax credit (2004, 2005 and 2006) at the federal level, renewal portfolio standards in 26 states, a steady flow of comparatively low cost capital (in part due to introduction of large balance sheet foreign players), a favorable political climate and relatively broad public support have all in part contributed to a 4 year boom in installed capacity.
- Over 5,200 MW of new wind capacity was installed in 2007 representing a 45% increase from 2006. Total installed capacity as of the end of 2007 was over 16,900 MW. AWEA recently reported installed generations had passed 20,000 MW. Estimates for 2008 installations are as high as 8,000 MW.
- Pending expiration of PTC has already impacted the market, including:
  - Race to complete in 2008 (bonus depreciation)
  - Reduced advance rates on turbine warehouse facilities
  - Refusal of tax investors to take PTC risk
  - Several examples of capital constrained sponsors seeking mezzanine and equity bridge financing
  - Possibility of turbines available in secondary market

General Market Update (cont'd)

- PTC gaps have historically led to dramatic downturns in US market (75- 90% reduction from prior year's capacity in each of 1999, 2001 and 2003).
- Presence of large balance sheet players should reduce such effect in 2009 as such players will in all likelihood plow ahead in anticipation of retroactive PTC legislation.
- Market conditions in ERCOT West have created substantial financing challenges in the tax equity market. CREZ is coming but in the relative near term the measure of a developer's success may be determined by its ability to execute outside of Texas.
  - Recent IRS guidance on related party sales provides a means for large balance sheet players to remove "Texas Risk" in order to attract tax equity.

Tax Equity Market

- Modern tax equity market started to take shape in the early part of this decade with the widespread acceptance of disproportionate partnership structures that maximize tax efficiency and provide institutional tax investors a preferred rate of return.
- To CP Energy's knowledge, less than 20 institutions have made tax equity investments in wind transactions since 2003. Even at the height of the market the tax equity pool was not deep and due to the factors mentioned below is shallower still. There are a variety of reasons for the lack of depth in the tax equity market (negative pre-tax GAAP earnings, project finance nature of investments, lack of yield premium as compared to low income housing, etc.).
- The rapid expansion of the overall market, the entrance of foreign and private equity owned sponsors without US tax appetite have combined to create the need for an ever increasing amount of tax equity dollars. Each MW of installed capacity equates to approximately $1 million in tax equity investment.
- 2007 was the peak of the market from the sponsors' perspective. After-tax yields for portfolio financings dropped below 6% and in certain instances single project financings approached 6%. In addition, sponsors were successful in using leverage to garner substantial operational flexibility, especially in the context of portfolio transactions.
- 2008 has seen a sea change in the market.
- The effects of the credit crisis started to impact the market in the first quarter. Institutional tax investors were almost uniformly being held to a higher standard given risk adjusted returns to reflect their own increased cost of funds and escalating yields for alternative tax based investments. Most importantly, the market has seen several substantial investors exit the market or significantly scale back their appetites as institutions are forced to conserve capital.

Tax Equity Market (cont'd)

- In addition, market conditions in ERCOT West have compounded an existing predisposition on the part of tax investors towards any project <u>not</u> located in Texas. Certain investors will not consider a Texas project and those that will consider Texas now require yield premiums and often handicap the sponsor's financing assumptions.
- After-tax yield requirements have dramatically escalated. Single project yields range from 6.75 (outside of TX) to as high as 10% (structural considerations). Portfolio yields range from a low of 6.40 (pricing agreed to early in 2008) to in excess of 7.5%.
- In some instances, despite the availability of yield premiums, there are several examples of deals that have not attracted tax equity or lack full coverage (including portfolio transactions).
- Absent the entry of new tax investors, the limiting factor on growth in 2009 may be the availability of tax equity and not the timing of the PTC extension.
- Utility ownership and project level leverage may both become increasingly common as sponsors seek sources of capital to finance build-out.

Looking Forward

- Despite the current challenges in the tax equity market, the overall market should continue to grow for a variety of reasons.
  - General consensus that the passage of a PTC extension is not a matter of "if" but "when."
  - Continued support at the state government level.
  - Increasing public support for renewable energy which results in support from both Democrats and Republicans.
  - Possibility of national RPS or carbon market.
  - CREZ build-out over time should restore investor confidence in Texas and serve as a model or transmission initiatives elsewhere.
- Low level of tax risk coupled with the increasing yield environment should result in new market entrants.
- IRS guidance should permit utilities to play a larger role.