MEMORANDUM

TO: Michael C. Wood & Oleg Nikolyszyn, Esq
FROM: Michael R. McElroy, Esq. & Leah J. Donaldson, Esq.
SUBJECT: Comments from Barry G. Craig regarding CRE Tax Agreement
DATE: October 22, 2016

Below please find an analysis of Barry G. Craig's comments submitted to the Town on October 10, 2016. Mr. Craig did not object to the payment amounts negotiated, nor did he object to the Town entering into the Tax Agreement, per se. Instead, he analyzed the terms and conditions of the agreement. In our opinion, his concerns are addressed under the current Tax Agreement.

Mr. Craig is a resident of the Town and an attorney, licensed in D.C. (not RI). His submission is written from his perspective as a transactional/business attorney. We respect Mr. Craig's experience in this area and appreciate his concern. However, most of the concerns raised by Mr. Craig are easily dispelled by Rhode Island municipal tax law – with which he is understandably unfamiliar, considering he has not practiced municipal tax law in Rhode Island. Indeed, most attorneys, not to mention most residents of the Town, are unfamiliar with the extraordinary protections that the Town enjoys regarding the collection of taxes.

Therefore, we will begin by setting forth a few relevant aspects of Rhode Island municipal tax law to set the backdrop for this analysis. Then we will address Mr. Craig's specific concerns, and our analysis regarding each.

Rhode Island Municipal Tax Law

Below you will find several relevant municipal tax statutes and cases that provide the Town with both a shield and a sword when assessing and collecting real estate taxes.[1] The Town retains these rights and protections under the proposed Tax Agreement. The Town is not a 'creditor' as Mr. Craig incorrectly alleges; it is a taxing municipality, with powerful collection laws available to it.

A. Tax liens on real estate are automatic and superior to any other lien

The Town's tax lien arises automatically and is superior to any other liens, mortgages, encumbrances or attachments (other than easements and restrictions). The Rhode Island Supreme Court has held that "[i]n general, "taxes that are assessed against a person's real or personal property are a lien against his [or her] real estate for a period for at least three years" and, other than an easement or

[1] As discussed below, the Tax Agreement proposed for the Invenergy/CREC property ("Tax Agreement") sets forth "tax payments" to be made "by the Company to the Town." (Tax Agreement, page 2, paragraph 2(b).) Additionally, the Town specifically reserves "all rights and remedies available to it the collection of taxes under State law…" (Tax Agreement, page 6, paragraph 8(a).)

Note that while the Tax Agreement has frequently been referred to as a PILOT Agreement, or "Payment in Lieu of Taxes Agreement," this is not accurate. Rhode Island law does not allow for the state aid of PILOT Agreement entered into after May 15, 2005. *See* R.I.G.L. § 45-13-14. For this reason, this is a Tax Agreement and not a PILOT Agreement.

restriction of record "is **superior to any other lien, encumbrance or interest in the property**."" *First Bank & Trust Co. v. Providence*, 827 A.2d 606 (R.I. 2003) (*emphasis added*) (*quoting Picerne v. Sylvestre*, 324 A.2d 617, 618 (R.I. 1974)).[2] Mr. Craig's assertion that the Town has "no surety" or "enforcement mechanism" for collecting the taxes has no basis.

B. Municipal taxes have priority when taxpayer becomes insolvent

Under R.I.G.L. § 44-7-10, if a taxpayer becomes insolvent, taxes due to the Town shall have preference over all other debts or demands, with the exception of debts or taxes due to the federal government or the State of Rhode Island.[3]

C. Tax collector may take, and sell, the land if taxes remain unpaid

Under R.I.G.L. § 44-9-8 *et seq*, if taxes remain unpaid, the Town's tax collector may take the land for the Town and "shall … sell [the property, or a portion of the property] by public auction for the amount of the taxes, assessments, rates, liens, interest, and necessary intervening charges…"

Concerns Raised by Mr. Craig

A. Clear River Energy LLC as contracting party to the Tax Agreement

Mr. Craig is concerned that the Town may be contracting with the wrong entity. Specifically, Mr. Craig argues that instead of contracting with Clear River Energy LLC ("CRE LLC"), the Town should contract with its parent company, Invenergy Thermal Global LLC ("ITG LLC"), or in the alternative, should contract with both entities. (Craig Memo, pg 2, 5, 7, 8, 9, 10, 11, 19.)

Under Rhode Island law, all property (including real, personal and tangible property) is subject to taxation. Since the taxes are assessed on the property itself, the entity responsible for the tax payments is the owner of said property. Therefore, the Town must assess the owner of each property in the Town.

Mr. Craig is concerned that CRE LLC will not be the owner of the project, because it is not the applicant before the EFSB. (Craig Memo, pg 9.) Rhode Island law anticipates that the owner/operator of an energy facility project may not be the same entity that undertakes the application process. Under R.I.G.L. § 42-98-8, any application to the EFSB must include the "identification of the proposed owner(s) of the facility…" The EFSB application in this docket, filed

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[2] "R.I.G.L. § 44-9-1. Tax liens on real estate.
(a) Taxes assessed against any person in any city or town for either personal property or real estate shall constitute a lien on the real estate. The lien shall arise and attach as of the date of assessment of the taxes, as defined in § 44-5-1.
(b) The lien shall terminate at the expiration of three (3) years thereafter if the estate has in the meantime been alienated and the instrument alienating the estate has been recorded; otherwise, it shall continue until a recorded alienation of the estate. **The lien shall be superior to any other lien, encumbrance, or interest in the real estate whether by way of mortgage, attachment, or otherwise, except easements and restrictions**." (*Emphasis added.*)

[3] "R.I.G.L. § 44-7-10. Priority of city or town taxes in insolvency.
Whenever any person shall become insolvent, or die insolvent, city or town taxes due from him or her or his or her estate shall have preference, after debts or taxes due the United States and this state, over all other debts and demands, save those due for necessary funeral charges, and for attendance and medicine during his or her final sickness."

by Invenergy Thermal Development LLC ("ITD LLC") names CRE LLC as the "project company for the CREC project." In its Preliminary Decision and Order, the EFSB specifically recognized that CRE LLC would be "the project company for the Clear River Energy Center."

The EFSB permits, therefore, will be premised on the application's assurance that CRE LLC will be the project owner/operator for the Clear River Energy Center ("CREC"). As the project owner/operator of the CREC Project, Clear River Energy LLC is the proper entity for the Tax Agreement.[4]

B. Financial strength and stability of Clear River Energy LLC

Mr. Craig is also concerned about whether CRE LLC will have the "financial strength" to meet its projected obligations. (Craig Memo, pg 6, 9, 10, 11, 15.)[5] The CREC project will cost an estimated $500-$800 million to build, and will be worth hundreds of millions of dollars once in operation. In addition, the project will receive millions of dollars in ISO-NE capacity payments, together with additional millions related to actual energy sales.

As noted above, by law the property tax assessment is against the property. Should taxes remain unpaid (under the Tax Agreement or otherwise), the Town has the security of the property itself. R.I.G.L. § 44-9-8 states that if taxes remain unpaid the tax collector shall sell the property, or a portion thereof, by public auction for the amount of taxes, assessments, rates, liens, interest, and necessary intervening charges. The annual tax payments (a minimum of $4.6 million on average) will be easily covered by the tax sale of a facility worth hundreds of millions.[6]

Similarly, Mr. Craig questions whether CRE LLC's parent company, affiliates, or creditors will be permitted to hold a lien superior to that of the Town. (Craig Memo, pg 12, 17.) As noted above, under Rhode Island municipal tax law, the Town's tax lien is automatically superior to any other lien, mortgage or attachment. There is no need to include this in the Tax Agreement.

C. Assignment

Additionally, Mr. Craig asserts that "no assignment should be permitted while Clear River LLC is in default of its obligation to make payments to the Town, until those liabilities, including interest associated therewith, are paid, either by Clear River LLC or the party benefiting from the assignment." This protection already exists within the Tax Agreement. Before CRE LLC may

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[4] It is also in Invenergy's best interest to ensure the Tax Agreement is entered into by the actual owner of the property. It would be Invenergy (and its subsidiaries) that would suffer if an entity other than CRE LLC becomes owner/operator, not the Town. The Town remains fully protected under municipal tax law. The owner, whoever that may be, remains responsible to the Town for its taxes and CRE LLC remains liable under the Tax Agreement. For example, if for any reason, CRE LLC does not take ownership of the CREC project but instead ITD LLC retains ownership, the Town would put the property on the tax rolls and tax the legal owner (in this case: ITD LLC). In addition, the Town could enforce the Tax Agreement against CRE LLC.

[5] Mr. Craig is also concerned about CRE LLC's ability to fund the Decommissioning Agreement. The terms of the Decommissioning Agreement require secured funding for the Town's benefit prior to construction, and increasing annually until 125% of the projected cost of decommissioning is secured prior to the project beginning operations.

[6] Also, in a practical sense, should CRE LLC ever default on its tax payments, its financiers would likely immediately provide the tax payment(s) to prevent the property from being sold at auction and wiping out their mortgages.

"assign, convey, pledge, transfer or otherwise encumber" the Agreement, it must have "cured all monetary defaults of the Company." Default can be cured by CRE LLC or by the lender or successor entity. (Tax Agreement, pg 4, paragraph 6.)

D. Insolvency

Mr. Craig also expresses concern that CRE LLC will become insolvent or threaten to do so to force a reduction in its tax payments. (Craig Memo, pg 10.) As discussed above, if a Rhode Island taxpayer becomes insolvent, taxes due to the Town have preference over all other debts, except debts to the federal or state government. Therefore, tax payments to the Town would have priority over all other mortgages or private liens.

E. Insurance

Additionally, Mr. Craig addresses the issue of CRE LLC maintaining adequate insurance, and naming the Town as an additional insured. (Craig Memo, pg 14.) CRE LLC's investors will require CRE LLC to maintain insurance to cover hundreds of millions of dollars. Also, the Town has its own insurance coverage through the Rhode Island Interlocal Risk Management Trust.

F. Cross-default between agreements and form of agreements

Mr. Craig argues that the Tax Agreement should be cross-defaulted with the Decommissioning Agreement and the Property Value Guarantee Agreement ("PVGA"), as well as with agreements from CRE LLC's major creditors "so that an uncured material event of default in one of those documents gives the Town the flexibility to declare an event of default to protect its interests." (Craig Memo, pg 6, 18.) While such cross-default language may be expected and even necessary in a lending context, it is unnecessary and possibly harmful here.

As stated above, the Town retains the sword and shield of RI municipal tax laws if CRE LLC defaults on its obligations under the Tax Agreement. However, it would be improper for the Town to tie obligations not related to property assessment to CRE LLC's obligations to pay its taxes to the Town. For example, if the agreements were cross-defaulted, and CRE LLC failed to meet its obligations under a non-tax related agreement, cross-default would permit the Town to invalidate the Tax Agreement and place CRE LLC on the tax roll (or threaten to do so). It is possible that taking such action against CRE LLC would provide CRE LLC with a legal basis to appeal such an assessment.

Mr. Craig also suggests that the agreements should have been structured as a "master agreement" between the parties, with the three agreements as subsidiary agreements to the master agreement. (Craig Memo, pg 3.) The agreements could have been drafted as a master with subsidiary agreements, however, since the agreements are purposefully independent from each other (as discussed above), a master agreement would add no additional value for the Town and create an ambiguity that could threaten the Town's tax collection rights.

Mr. Craig proposes that no assignment of the Tax Agreement should be permitted unless the assignee assumes the obligations under all three agreements. While the agreements are purposefully independent, the Tax Agreement requires any assignee to assume such obligations. The Decommissioning Agreement cannot be assigned without the Town's consent and CRE LLC will not

be relived of its responsibilities. The PVGA promises that if it is assigned, CRE LLC's assignee will be fully bound.

Mr. Craig proposes that all three agreements should automatically terminate if the EFSB application is dismissed. (Craig Memo, pg 19.) To do so would only harm the Town and benefit Invenergy and its subsidiaries. For example, even if the EFSB application is dismissed, the Company remains responsible for the minimum of $2,925,000 in up front payments under Exhibit A of the Tax Agreement ($1,175,000 due by January 10, 2017), unless and until it exercises its right (with written notification to the Town) to terminate the Agreement if it discontinues development of the project. (Tax Agreement, pg 2, paragraph 2.)

G. Additional taxation

Mr. Craig also asserts that the Town should consider whether the cost to build pipelines or other off-site improvements should be expressly excluded from the Tax Agreement. This is unnecessary, because the Town reserves the right under municipal tax law to tax all property related to the project that are not on the project site (including pipelines).

H. Applicability of the Tax Agreement

Finally, Mr. Craig has concern about paragraph 11, subpart (e) of the Tax Agreement, which states, in part "This Agreement … constitutes the entire understanding and agreement of the parties with respect to its subject matter…" Mr. Craig argues that this invalidates the Decommissioning Agreement, because it is an agreement apart from the Tax Agreement. However, by its own terms, paragraph 11(e) applies only the subject matter of this tax agreement, and not to any other subject matter (i.e. decommissioning).

I. EFSB approval of agreements

Mr. Craig postulates that the law "might" require the EFSB to approve the Tax Agreement, Decommissioning Agreement, and Property Value Agreement. (Craig Memo, pg 1.) However, no approval by the EFSB is required for these agreements.

J. EFSB enforcement of Tax Agreement

Mr. Craig suggests that the obligations within the Tax Agreement be made a condition of the EFSB permit issuance. (Craig Memo, pg 3, 13.) While he correctly points out that the parties to the Decommissioning Agreement and the PVGA have agreed that compliance with them shall be conditions of an EFSB permit, it is unnecessary and possibly harmful to the Town, to create a similar EFSB enforcement option in the Tax Agreement.

As discussed above, the Town is fully protected by Rhode Island municipal tax law. If the Tax Agreement looks to the EFSB for enforcement of its terms, this could conflict with the accelerated process available to the Town under RI law.

K. EFSB enforcement of non-tax related issues

Mr. Craig includes several concerns related to safety, noise limits, air quality, environmental issues, and agreements with other local districts. (Craig Memo, pg 4, 6, 14, 15)

The Town shares many, if not all, of these concerns and has properly raised them with the EFSB via EFSB conditions requested in the advisory opinions submitted to the EFSB by various Town entities. In short, these issues are not part of the Tax Agreement because they do not relate to the assessment of property taxes within the Town. As discussed above, the Town is best protected if the Tax Agreement remains strictly related to tax matters.

Mr. Craig incorrectly asserts that the "EFSB statute does not appear to give the EFSB authority to enforce the conditions under which a permit is issued after construction of the Project." However, not only does the EFSB fully possess such authority, but the Town and its entities also retain their own rights to ensure compliance at the project site for the life of the project. The project will also be monitored by DEM, EPA, CRMC, and the Army Corps of Engineers.

Under the Energy Facility Siting Act, the EFSB retains authority to monitor compliance with the licenses it grants and to punish non-compliance. Specifically, the EFSB may perform routine inspections itself, or may designate officials or staff from any state agency as its agents to investigate complaints, perform routine maintenance, and issue cease and desist orders. R.I.G.L.[7] § 42-98-16. If the licensee fails to comply with any provision, condition or limitation in an EFSB license, the EFSB has the power to fine the licensee up to $20,000 per day while the entity remains non-compliant, and/or to suspend or revoke the license. CRE LLC would lose millions of dollars in capacity and energy revenue if suspended for any length of time.

L. Recording

Mr. Craig suggests that the Tax Agreement should be recorded by the Town with the Registry of Deeds. If the Town wishes to do so, it may record the Tax Agreement without any revision to the text of the agreement itself. However, because of Rhode Island law, the tax lien is automatic, so no such recording is necessary.

M. Delayed operation

Mr. Craig also inquires whether CRE LLC will continue to pay $750,000 each year if the Commercial Operation Date extends beyond 2021. (Craig Memo, pg 16.) If the project is delayed beyond 2021, it would no longer fall within the safe-haven of the payments currently set forth in Exhibit A to the Tax Agreement. Further, if it was not yet operational, it would not fall under the payment schedule included in Exhibit B to the Tax Agreement. If this occurs, the Town would place the property on the tax rolls for the interim period.[8]

N. Inflation

Mr. Craig also inquires whether the Town should use an inflation standard other than 2.5% per year. (Craig Memo, pg 16.) The parties negotiated an annually compounding 2.5% inflation standard (as opposed to use of an index) to provide certainty to both parties for both budgetary and planning purposes. The rate of 2.5% per year (compounded) is reasonable, considering the average U.S.

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[7] For example, in its advisory opinion to the EFSB, the Town Planning Board requested that the EFSB delegate such authority to the Planning Board during the construction, start up and reporting period.

[8] In the alternative, the Town could negotiate an addendum to the Tax Agreement for the interim period.

annual inflation rate for 2000-2009 was 2.54% and the average U.S. annual inflation rate for 2010-2015 was only 1.86%.

O. Dispute resolution

Additionally, Mr. Craig proposes that the Tax Agreement require the parties to resolve disputes through binding arbitration. Binding arbitration is insufficient in this situation. For example, with binding arbitration any decision is usually made by a single arbitrator and is final. The Town usually cannot seek discovery. The Town cannot request a jury trial, and cannot appeal a negative result to the RI Supreme Court. Additionally, arbitration is usually private and lacks the transparency of public litigation in Superior Court. For disputes arising under the agreement, the Tax Agreement currently requires negotiation between the parties, followed by mediation. If the dispute remains unresolved, the parties may then seek judicial enforcement from the Rhode Island Superior Court and an appeal to the Rhode Island Supreme Court.