

Wind Farm Construction Contracts

Before 2009, we saw tremendous growth in wind energy development in the United States. While growth has slowed during the current economic crisis, this upward trend is likely to continue in part as a result of the American Recovery and Reinvestment Act of 2009 (the Stimulus Act). Despite growth incentives, one of the primary roadblocks to developing a wind power project is being able to efficiently and effectively allocate risk between owners and their contractors. This article summarizes some of the key risk areas to be addressed in wind farm construction contracts.

Risk Allocation

Efficient and fair risk allocation can speed development of a wind power project. In this respect, wind farm development is no different than any complex project in other sectors, be it infrastructure, non-renewable power, oil and gas, transportation or telecom. Key design- and construction-related risks include the following:

- Schedule risk
- Price/budget risk
- Performance risk
- Risk of variance between design/construction assumptions and reality
- Liability/indemnity risk
- Safety risk
- Tax/permit risk
- Warranty/performance risk

Addressing these risks is necessary to negotiate any design/engineering contracts for a wind power project. Moreover, the ability to reach fair positions quickly can speed development and save costs.

Project Variations

Complicating this negotiation, however, is the wide variety of parties performing work at each project site, including (just to name a few) surveyors, engineers, construction contractors, electrical contractors, specialized subcontractors, turbine installers and turbine suppliers. Sometimes construction-related tasks are performed by only one or two contractors; sometimes they are each performed by a separate contractor. Moreover, there is wide variation in capability among owners. Some owners have the know-how to perform one or more major design and construction tasks in-house, while others rely almost exclusively on contracted expertise.

Due to this wide variation in parties and capabilities, it takes careful planning to efficiently and effectively allocate risk for a wind power project. Moreover, because projects vary widely, the hard-fought contractual arrangements for one project are unlikely to be a perfect fit for another project in which the constellation of parties and capabilities differ significantly.

As a result, careful attention must be paid in any negotiation to the parties who will be operating at the site and the unique nature of wind power projects. In particular, successful negotiations will focus on the following issues.

Schedule Risk

One of the most visible risk allocation issues relates to the schedule for development of the wind power project. From the owner's perspective, timing is a primary concern. As mentioned above, many parties can be performing work at the project site. In most

cases, the success and efficiency of the work to be performed by these parties is highly dependent upon timely completion of work performed by other parties or the owner. One objective is to create a schedule for the overall development of the project and identify critical milestones at the “interface points” between the schedules of each individual party.

Another concern for both owners and contractors is attaching certainty to each party’s schedule obligations. For the reasons mentioned above, owners want to be sure that schedules are met. Contractors also want certainty to ensure that their exposure is known and limited, and also to make sure that they are not held responsible for the delays of the owner or other contractors. As a result, reasonable liquidated damages are often negotiated for contractor milestones that are “critical path” to the completion of the wind power project. Contractors also may receive an equitable schedule adjustment for any delays directly caused by milestones missed by other parties. Due to the highly interactive nature of wind farm construction, however, immaterial delays and interactions among parties should be expected and tolerated without schedule adjustment.

Design and Construction Assumptions

Another key to successful wind farm development is ensuring that what looks good on paper is translated into reality at the project site. Inevitably, some assumptions are made at the planning level that turn out to differ from actual conditions at the site. This is particularly true for design and construction assumptions.

Most design and construction assumptions originate from development studies performed for the wind farm. A first step, therefore, is determining who will be responsible for performing these studies. Some are traditionally provided by owners (such as site plans and archaeological and environmental studies), while others are usually contractor-performed (such as surveying and labor/materials investigations). Finally, some studies can be performed by either party, such as geotechnical investigations and wind turbine transportation studies.

Once the necessary studies have been allocated, the next task is to determine who can rely on them. In general, owners are hiring contractors as design and

construction professionals. As a result, owners frequently rely on contractor-performed studies and contractors are held accountable for any inaccuracies. Moreover, owners also often look to contractors to review owner-provided studies and, where necessary, conduct further investigations reasonably necessary to confirm the assumptions included. There are many circumstances, however, in which contractors should be able to rely on owner-provided studies (performed by the owner or other contractors).

Finally, once these issues have been negotiated, the parties need to determine what happens if site conditions end up differing from the base assumptions. The parties could agree, for example, to provide contractors with an equitable schedule and/or cost adjustment unless the difference should have been reasonably foreseen. Otherwise, contractors will need to correct any work at their own cost and schedule risk.

Indemnifications and Liability Caps

A key goal of each party to a wind farm construction contract is to limit its risk exposure. Two ways of doing so are indemnifications and liability caps. An appropriate list of indemnifications is dependent upon the nature of work to be performed and the various roles of parties working at the site. Indemnifications for wind farm projects usually cover a wide variety of topics, such as third party bodily injury and property damage, intellectual property, hazardous materials and lien/title indemnities. These indemnifications allocate risk to the party in the best position to minimize such risk, thereby reducing the overall risk profile of the project and heightening the chances of success.

In addition, risk exposure is often limited by liability caps. These caps can, for example, operate as sub-limits on certain liquidated damages or provide an overall limit on all liability under the contract. While the negotiation of the actual limit is primarily a business decision, the legal issue is the amount and scope of any carveouts to such limits. In other words, while liability caps enhance certainty by limiting exposure, there are still some risks for which a party should nevertheless remain fully responsible. Negotiating which risks can be limited and which should remain unlimited can be a difficult task, but one that is necessary to successfully allocate and mitigate risk.

Taxes

Another important contracting element in wind farm construction is allocating the responsibility for taxes. Although tax responsibility is an issue in many types of contracts, it is of particular importance in the wind sector due to the many relevant taxes, exemptions and credits. The first issue is to identify and allocate responsibility for anticipated taxes and remedies associated with an inability to achieve expected tax benefits and treatments. Failure to openly discuss and allocate taxes can result in a contract price that, for better or worse, does not reflect the cost of performing the work. In some instances, this can be a significant and costly oversight.

A second issue is to identify any relevant tax exemptions. Taxing authorities frequently encourage renewable energy development with sales tax exemptions, use tax exemptions and/or enterprise zone programs, just to name a few. The procedures required to secure such exemptions can often be detailed and, in some cases, difficult to identify with full certainty. This is particularly true if the exemption is provided to the owner of the project but the contractor is procuring relevant exempt materials. Many of these exemptions cannot be procured after the fact, so it is important that the parties discuss exemptions and related procedures before any work begins.

Tax credits or other incentives also are used to encourage wind farm development. Though beyond the scope of this overview, it is important to recognize the conditions surrounding such tax credits and incentives and how each parties' obligations are tied to such conditions (*see* our separate overview on renewable energy tax credits/incentives). In particular, careful attention should be paid to scheduling to ensure wind turbines are placed in service before expiration of any relevant federal production tax credit expiration date, and that reasonable remedies are negotiated for missed deadlines or any failure by a party to follow procedures necessary to achieve beneficial tax treatments.

Safety

Allocating responsibility for site safety is a key issue for ensuring the successful completion of a wind project. Multiple entities are often engaged in construction or development activities at the site. At any given time, for example, there could be construction activity at the site by the owner and its subcontractors, the turbine supplier, the turbine erector, the transportation company, the utility and the balance of plant contractors. Primary safety responsibility can rest with one party or can be divided among multiple parties. Either way, there should be clear contractual terms that ensure allocation of safety responsibility and compliance with safety regulations.

Conclusion

Wind energy development continues to grow in the United States, and the Stimulus Plan will provide new and substantial opportunities for further development. This article provides a sample of the construction-related issues to be resolved in each project to ensure an efficient and successful development. As is always the case, each project will present new challenges to overcome. Fair negotiations in good faith can speed the resolution of these and other issues, speeding development of wind projects and benefiting owners and contractors alike.

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