

A client briefing note from Stamp Jackson and Procter

Wind turbine land leases and options



Windturbines may be a new addition to the rural landscape but, although endorsed by Government policy and benefitting (at least for the developers) from Government subsidies, the lease of the land on which they are built is subject to the same legal requirements and commercial criteria as other land lease transactions.

Having been asked by farmer clients to look at a number of windturbine lease propositions we want clients to be aware that there are a number of potential pitfalls in proposed lease agreements.

We are not taking into account political, environmental, total national viability or energy requirement considerations – simply the degree of risk associated with any business proposition and the extent to which that risk can be minimised by the requisite provisions in option and lease agreements.

Our conclusion is that these are high risk ventures for any landowner. This note outlines the key issues clients should consider when contemplating such a lease.

Key points

- ✘ Rental income is the most uncertain element. As the German operators of the world's biggest "wind carpet" have observed "the wind blows as it will, where it will and when it will". The amount of electricity generated (to which rental levels are linked) is neither controllable or forecastable. Do not be too influenced by the developer's income offer – if it looks too good to be true it probably is.
- ✘ A wind turbine will almost certainly reduce the value of your property.
- ✘ Make sure the developer has substantial assets to back its obligations.
- ✘ Make sure the developer pays your professional costs, whether or not a deal is actually entered into.
- ✘ Make sure the option and lease cannot be transferred indirectly by a sale of shares
- ✘ Make sure the developer is under an obligation to do all it can to ensure that turbines are built on the landowner's land and generate electricity and therefore income.
- ✘ It is most important to ensure the site will be reinstated at the end of the lease and that performance of this obligation by the developer is secured.

The aim of this briefing is to acquaint you with the procedures and requirements of the land leasing process. We have tried to avoid too much legal terminology or complicated detail, concentrating on the main issues and the problems you need to consider. As is always strongly recommended in these situations, do take professional advice before reaching formal agreements with developers.

The process

Negotiating an option and lease on land for a specified business activity is a fairly standard process. The usual arrangement is for the landowner to grant to the developer a right for a specified time (an option) to call for the grant of a lease of the site, for an agreed period. The lease sets out the conditions for building and operating the windturbine and the payments to be made during the lease period.

Both are important agreements in which you need to understand short and long term implications and, in particular, what might lie behind what is generally referred to as “the small print.”

At this early stage of windturbine development in the UK the terms of options are particularly important. While an option period is a proper provision to enable full site assessments to be made, plans developed, planning permissions obtained etc. it can also be simply a strategic move – freezing out potential competition; setting up a series of smaller deals in order to establish a much larger final installation; or simply, as the name implies, setting up a number of options from which the most beneficial (for the developer) can be selected at a time that suits their purpose.

Matters to consider

Professional costs

You are likely to incur substantial professional costs with agents and legal advisers in negotiating the terms of the option and the lease. If those negotiations fail you could be faced with a large bill for professional fees and be out of pocket.

The fact that professional costs are mounting up can in itself weaken your negotiating position. Faced with the prospect of a large bill there is a temptation to settle for less than you might be entitled to rather than risk the deal falling through completely and being out of pocket on costs

Two ways to address this problem are:

- ◆ Insist from the start of negotiations that the developer pays your professional fees, and gives a solicitors’ undertaking to that. If given this will normally be limited to a maximum amount.
- ◆ Agree with your professionals that they work on the basis of no (or limited) charge unless the deal is agreed. If they are prepared to work on this basis they will want a substantial mark up on the normal fees to cover the risk of not being paid.

The cheaper option is to agree at the start that the developer pays your professional costs whether or not a deal is completed.

Option terms

Key points to consider here are:

- * Payment of your costs
- * Payment of a fee to you for the grant of the option
- * Period in which the developer can (but does not have to) exercise the option on the lease. Can it be



extended to allow for planning appeals? The developer often requires the right to extend the option period if there is a planning appeal. Such an extension can lead to the option being for much longer than originally anticipated. There should be a maximum period for the option.

* Obligations imposed on developer - such as an obligation to apply for and pursue a planning permission for your site and to construct turbines. This is important:

If there is no obligation on the developer to actually do their best to have turbines generating electricity on site then there is a risk they may use the arrangement with you to neutralise the site so they can develop a competing site

If they developed a competing site rather than yours, then yours will not be available for other power companies to develop and you will not receive any income.

* Your part in the planning procedure. Be sure you have the right to be informed and consulted. Check if it will be a joint application by you and the developer.

* Make sure you have the right to end the option if the developer does not honour its obligations

* Is the option transferable by the developer? If so, are there any controls on that? Be careful that the developer cannot get round transfer controls by transferring the option to a subsidiary with no assets or indirectly selling on the benefit of the option by selling the shares in the developer rather than the option owned by the developer. A change of control provision can protect against this.

Financial standing of the developer

It is always important to ensure that the developer is of sufficient financial standing. You would find it difficult to enforce a developer's obligations or get compensation for loss suffered as a result of the developer's default, if the developer has no money or assets.

It follows that if the developer has no assets, in practice it can agree to all manner of obligations, knowing it does not have to honour them if it does not wish to.

Because of the above it is important to check exactly who the developer actually is. Organisations with material assets can form shell subsidiaries with no assets and have the shell with no assets enter into a contract.

Where a company with material assets has formed a shell to act as the developer then the company with the assets should join in to guarantee the shell developer's obligations.

In addition to guarantees, some obligations are so important that you should consider insisting on a bank giving a bond to ensure developer obligations are met - for example the obligation to reinstate the site.

Terms of lease

With the uncertainties currently faced by the farming industry the rental income will be the crucial element for most of our farming and landowning clients. There will be a balancing of possible short term cash gains against longer term revenue flows (and risks) which are decisions only you can make, together with the core calculation as to whether or not a windturbine lease would be a more productive use of your land asset than current or future farming use. Prime considerations on rent are:

* Rent is usually based on the income received for the electricity generated and is therefore uncertain.

It is obviously important to ensure that the income you get gives an adequate return. You should consider agreeing a minimum annual payment (basic rate) and then a share of the income over and above a certain level.

* When considering the viability of the developer's proposal do not be too influenced by the potential income shown in the draft lease attached to the option. The option commits you - but not the developer. So you will not get more income than is stated, but may get less.

* The option could commit you to proceed with the lease at the income level stated in the option. But be aware it could be possible for the developer to seek to renegotiate that income downwards and to threaten not to proceed with the lease if you do not agree.

* Provison should be made for regular review of basic rent and percentage of income receivable.



- * A thought that should occur early on but often arises embarrassingly later – are you alone in this? Are consents required, say, from tenants, lending banks or those with use covenants?
- * For this type of investment a long term lease (i.e. 20 years or more) is in the developer's interest and yours too if you are convinced of an acceptable and sustainable rental income. However be careful of break clauses, you don't want to be left holding the baby if it's a massive wind turbine that nobody wants!
- * There should be an obligation to construct the turbines and generate power within a certain period, failing which the lease should end.
- * The developer's repair and maintenance obligations should be clearly defined in the lease.
- * Insurance – the developer must protect you from all liability arising from the existence and use of the wind turbines and related structures. The developer should be responsible for complying with all relevant laws and regulations relating to the turbine and should fully protect you from all costs/claims etc. relating to it.
- * Be very careful to ensure the developer cannot transfer the lease without your being aware of and happy with the proposed new developer/tenant. Be equally careful with any provisions for alteration and change of use of the site.
- * The extent of the land to be let should be limited so that loss of agricultural property relief is minimised. For example, if a large area is let for a number of wind turbines with possibly the right to graze the area then APR may well be lost. Single turbines may just lose APR only on the site of the actual turbine. Make sure the turbine arrangements do not lead to loss of Single Farm Payment. You must retain the right to farm the land around the turbines.
- * Make sure you are fully conversant with and understand any rights to be granted with the lease e.g. access roads for construction and maintenance, rights to lay and maintain cables from turbine to grid, land for electricity substations. Pay particular attention to areas of joint usage e.g. a farm track which becomes a joint access could become an unforeseen expense if there is shared cost of repair and maintenance increased by heavier use. Also any restrictions on the use of your adjoining land, such as the removal or non-planting of trees to protect wind flow to the turbines. Plus the usual headaches over fencing - they put them up, but you're responsible if you or your staff damage them.

Finally, possibly the most important requirement of all – reinstatement of the property at the end of the lease. Turbine structures and foundations are substantial. You could be responsible, at great expense, for reinstating land that has been used for turbines either at the end of their life or if for some reason they have been built or part built and then abandoned. This responsibility should be left entirely with the developer and bonded to ensure performance.

These observations and the points covered are by no means exhaustive. Renewable energy is a high profile subject. Don't let the "hype" or controversy divert you from making a diligently analysed and considered business decision. Our own summation can only be these two words:

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