

RENTS, ROYALTIES, EASEMENTS AND LAND VALUES

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INTRODUCTION

Developers and landowners have invested in long term leases for wind farms potential sites in the American Midwest in states such as Iowa, Indiana, Wisconsin and Illinois. Wind farming started in north-central and northwest Iowa and spread to the vast expanses of the USA Midwest states.

A major advantage of wind power production in the USA is a short time for executing a project of about two years for acquiring the leases and the engineering design followed by about eight months for construction and production. Authorization is obtained from sympathetic local authorities and state governments. This is compared with about 10 years for the planning of execution of fossil or nuclear power production projects requiring adversarial federal government scrutiny, hearings and authorizations and a deeper level of bureaucracy. The smaller scale of the wind projects in the hundreds of megawatts of installed capacity compared with thousands of megawatts for the fossil and nuclear project also simplifies the capital financing process.

The installation of wind power systems does affect property values. Where they can generate royalties, land values can be enhanced, and in fact some property owners do welcome the installation of wind turbines on their property for the extra income that they produce. County boards, tax collection bodies and school systems boards do encourage their installation because of the extra tax revenue they generate. On the other hand, because of the landscape and other environmental and industrial effects, they are perceived to reduce neighboring property values; a situation leading to conflict between those who benefit from the income and those who complain about the siting effects, some of them expecting compensation.

RENTS AND ROYALTIES PAYMENTS

Rents and royalties paid to landowners and farmers for the installation on wind turbines on their property typically varies over the range of \$3,000-\$5,000 per turbine per year. The range depends on the site's wind resources and access to a neighboring power line for access to the electrical power grid. Such an access is not only important to export the generated power, but for importing about 3-5 kW of power needs per turbine on a standby basis. Such power import is continually needed for the turbine controls and measurement systems, to keep the equipment from freezing in harsh winters, and to activate its yaw mechanism to face the wind as it starts blowing, its pitch mechanism to keep the rotors at the right pitch angle; at which time the turbine becomes a net power exporter to the grid.

Each turbine occupies about a ½ acre of land. However, accounting for the access roads and the buried electrical cabling raises the land use per turbine to 2-3 acres per turbine.

SITING CRITERIA

Developers' first consideration is the identification geographical locations with good wind resources since power extraction from the wind is proportional to the cube of the wind speed. A second consideration is the presence of transmission lines and coupling to the grid system for dispatching the produced electrical power from the rural areas to the consuming industrial sites, urban areas and cities.

Construction of a wind farm takes typically two years of preparation, acquiring the leases and engineering design, but once the actual construction is started, the wind farm is completed within an 8 months period. This is a measurable advantage for wind farms compared with the 10 years period for fossil fuel and nuclear power plants.

INVESTMENT CRITERIA

Buyers of farmland with utility wind production and royalty and easement potential look for 10 percent internal rate of return on the scheduled payments over a five decades period. They expect a 4 percent annual operating income for the land.

The expectation here is that the installed wind turbines would be replaced at least twice with a design lifetime of 20 years.

Royalty payments on wind turbines depend of the installed power capacity of the turbine, the proximity to end users, the wind resources and the carrying capacity of the power grid.

The easement payments generate additional value above the land value, increasing the annual revenue and the market for a farm above just the raw land.

LEASE DURATION, SUNSET CLAUSE, DECOMMISSIONING

Typical farm land leases are over 50 years and the energy company may have the right to renew the lease for two additional 20 years additional time frames.

A sunset clause is necessary in wind power contracts. What it amounts to is basically that if a contract is signed today, a wind turbine should be erected and operational within a specified time frame such as 4 years. If this does not happen, the agreement becomes null and void. The developer could not tie up the land for 50 years, nor sell the easement to some other developer, and the owner could seek an agreement with another developer himself.

Reduction in the land productivity and crop damage costs during a two years construction period and even beyond it due to maintenance and repair activities, due to compaction by heavy equipment is compensated in most contracts.

An escrow account must also be established for the decommissioning and restoration costs of removing the steel, cabling, and concrete at the end of the project, even if the developer or utility company is not in existence anymore.

TAX CREDITS

Wind power investments are encouraged by tax credits that are available in the form of the Production Tax Credit (PTC) for the electrical production over the first ten years of the 20 years design lifetime of a utility wind turbine.

On October 3, 2008 a small wind turbines tax credit was signed into law in the USA. It involves a 30 percent tax credit of up to \$4,000 per property, off the installed cost of a small wind turbine system.

Pending legislation in the USA Senate as the Renewable Energy Alternative Production Act (S. 1094) would provide a PTC for nonelectric renewable energy production for the same first 10 years period of operation as a current PTC for wind and other renewable electrical generation systems.

CASE STUDY

A case of land value appreciation is reported by Loyd Brown, the president of the Hertz Farm Management company in Story County, Iowa.

The case concerns an 80 acres land tract on which 3 wind turbines were installed on a 50 years lease.

The property is considered to have increased the land value from \$5,600 per acre to \$7,600 per acre for an extra \$2,000 per acre generating an extra income of $80 \times 2,000 = \$160,000$ of value for the seller.

The new owner would receive the future easement for roads and buried cables and royalties from the 3 installed turbines. Each turbine royalty payment is \$4,000 per year for an extra income of $3 \times \$4,000 = \$12,000$ per year. There is also a \$2,500 per year payment for the road that crosses the property raising the total income to $12,000 + 2,500 = \$14,500$ per year.

This corresponds to a return of $14,500 / 160,000 = 0.0906$ or a 9 percent on the extra investment for the buyer.

The contract also includes an escalation clause where the annual payments are adjusted for inflation according to the Consumer Price Index, CPI.

DISCUSSION

About 75 percent of landowners who are approached by the wind energy developers accept their offers to install wind turbines on their property. Most of them eye the substantial extra income that their land can generate. The presence of the extra income increases the land value at the time of selling, since the land is being sold as well as the rights to a future extra income. Some even consider at the contribution to energy in general, and to renewable energy sources in particular.

Yet, the other 25 percent take into consideration the need for access roads on their prime land, the buried high voltage electrical cabling and the difficulty of farming around the turbines. The large cranes used in construction could crush underground drainage tiles and compact the ground, even though a well written land contract would require the contractors to repair any damaged tiling. A main concern is the long term surface and subsurface drainage and compaction which would definitely affect the land's productivity and crop yields.

Any royalty and easement agreement should be carefully reviewed by an attorney since it will have major consequences for the current and future generations land owners.

APPENDIX

The following standard wind farm lease agreement does not include an escalation provision accounting for inflation. It also does not cover legal hazards from nuisance from noise, environmental concerns, and tax problems. The rental income may not be considered as farm

income, possibly causing loss of tax benefits under local property tax and federal income and estate tax rules.

STANDARD WIND FARM LAND LEASE AGREEMENT

This Wind Farm Land Lease Agreement is between:

- A. (Landowner name and address), and,
- B. (Wind Farm Development Company, name and address)

Section 1

TERMS AND CONDITIONS

1. The Landowner agrees that the Lessee shall be granted the exclusive rights to construct access roads, install and operate wind turbine electricity generating equipment, route the necessary grid connection cables, install switching and measuring gear, transformer stations, maintenance workshops and carry all the required construction works necessary for installing and operating the wind farm on the land designated in the attached plan. The land leased will consist only of the access routes, building sites and the wind turbine base areas. The wind turbines and all of the ancillary equipment and buildings, remains the property of the Lessee.
2. The location of the wind turbines, the routing of the cables and the positioning of the substations and workshops will be detailed on a site plan, which on completion will form part of this agreement.
3. Under the terms of this agreement, the Landowner has a duty to declare all burdens on, attached to, and third party interests in the leased land forming part of this agreement.
4. The wind farm assets, including the wind turbines and all the ancillary equipment required to operate the wind farm may be used by the Wind Farm Operating Company as collateral and assigned to banks and finance institutions as security.
5. The Landowner and the Lessee agree, that in the event of the Wind Farm Operating Company party to this original Lease Agreement, for unforeseen legal reasons arising, being required to hand over the control of the Operating Company to a third party that that third party will assume all the rights, assets and duties contained in this Lease Agreement.

Section 2

DURATION

1. The Land Lease Contract will take effect from the date of completion of this agreement, (signed and witnessed by both parties). The land and access as designed in Section one will be immediately opened to the Wind Development Company. In the event of the start of the wind farm development, (Planning Application) etc. being delayed by more than one year from completion of the Lease, both parties have the right of a no penalty withdrawal from this agreement.

2. The term of the Land Lease will be for Twenty Years or the useful production life of the installed wind turbines, whichever is the greatest. The Lessee reserves the option to lengthen or shorten the term of the Land Lease to coincide with the useful technical life of the installed wind turbines.

Section 3 RENTAL

1. The Lessee agrees to pay the Landowner no less than Three Percent of the Gross Annual earnings (before tax) of the Wind Farm in the form of rent for the use of the land by the Wind Farm Operator.
2. Payments will be calculated from the date of commissioning the first stage of energy production plant (wind turbines) installed.
3. The Landowner will receive an additional rental payment for each individual wind turbine in operation on the wind farm in the amount of \$2,000 per turbine per year.
4. Payments will be made in arrears during the calendar year following the end of the previous financial year.
5. The Landowner will have the option to take equity in the Wind Farm Operating Company as rental payment.
6. The Landowner will be paid reasonable financial compensation for the disruption of agricultural production during Wind Farm construction works and ongoing repair and maintenance work when the Wind Farm is operational.

Section 4 LANDOWNER OBLIGATION

1. The Landowner agrees, that it is a statutory requirement of the local and national authorities, to countersign planning applications, declaration of intent, questionnaires and documentation necessary for developing and operating the wind farm, they will do so.
2. The Landowner guarantees rights of access to the Lessee and the Lessee's nominate subcontractors for the purpose of carrying out necessary work on the wind turbines and any ancillary equipment during the term of this lease.
3. The Landowner agrees not to erect, plant or allow third parties to create structures within the boundaries of the wind farm agreed in Section one of this agreement that may adversely interfere with the energy production capacity of the wind farm.

4. The Landowner, in the event of the land on which the wind farm is developed being offered for sale, agrees to include the terms and conditions of this lease as a legally binding non-negotiable burden or lien on the property.

Section 5

LESSEE OBLIGATION

1. The Lessee guarantees to install and maintain the wind turbines and ancillary equipment to the highest current technical standards.
2. The Lessee will be required to give the Landowner at least two weeks notice of works to be carried out during the development and operation of the wind farm.
3. The Lessee will replace top soil where necessary and practicable as soon as possible after completion of all building or excavation work.
4. The service supply lines, etc. installed on the land leased, may be rerouted if necessary after due consultation with the Landowner and at the expense of the Lessee who will then be responsible for keeping the modified equipment in good repair.
5. Where possible, the wind turbines and all of the ancillary wind farm equipment will be located where it will cause minimal disturbance to agricultural work.
6. The Lessee will provide adequate third party and public liability insurance cover concerning the wind farm development and operation that will include the Landowner risk of third party damage claims resulting from wind farm activities.

Section 6

TERMINATION

1. When the lease expires, the Lessee will reinstate the land, as far as it is possible and practicable, to its original state, with the option of allowing the power lines and services to remain in place.
2. During the last ten years of the lease, the Lessee guarantees to set aside a percentage of the gross annual income from each wind turbine as security for reinstating the land.
3. The Lessee guarantees to decommission the wind farm at the end of the lease agreement.

Section 7

HERITABLE RIGHTS

1. All of the legal rights and obligations agreed to in this contract between the Landowner and the Lessee shall be passed to their rightful heirs and successors, whosoever they may be.

Section 8

JURISDICTION

1. All legal matters and arguments appertaining to the content and conditions contained in this contract will be settled subject to the rules of the USA Legal System in force at the time.

Section 9

CONTRACTUAL CONDITIONS

1. The obligations of the Landowner and the Lessee will take effect from the date on which the following conditions have been fulfilled.

- a. The Land Lease is registered at the County Recorder of Deeds at the location of the wind farm.
- b. All of the required consents and agreements necessary for the development and operation of the wind farm have been granted by the relevant county, state, and federal bodies.

2. Changes and amendments to this agreement must be in written form, agreed and witnessed by both parties.

Section 10

EQUITY

1. The Landowner has the right to buy and own equity in the wind farm development and operating company.

Section 11

COSTS

1. The Lessee(the wind farm development and operating company) will be responsible for meeting all of the costs incurred during setting up and running the wind farm, e. g. planning applications, consultations, operating consents and connections.

Section 12

ARBITRATION

1. Should any item or items contained in this agreement be mutually judged by the signatory parties to be unworkable, the rest of the agreement will remain in force unaltered. The signatories guarantee to strive together for solutions that will enable their common goals, (the development and operation of the wind farm), to be achieved.

2. Both parties agree to replace unworkable items or loopholes that may arise in this agreement with amendments or corrections that come closest to achieving the context and meaning that the parties originally wished to express and expedite under the terms of this contract.

Signed: _____ Landowner, _____ Witness
Date.

Signed: _____ Lessee, _____ Witness

Date: