SMALL DEAL OF THE YEAR (UP TO $200M): BLUE WOLF CAPITAL MANAGEMENT

Turning Landfill Gas Into Energy, Then Profits

Speed, knowledge and certainty of close were worth more than money in **Blue Wolf Capital Management**'s first-ever buyout.

The New York firm, despite being outbid by at least two other potential buyers, proved victorious in the auction process for landfill-gas collector **Montauk Energy Capital LLC**. While the sellers were targeting firms that could spend well over $100 million, Blue Wolf walked away with the company for just $101.8 million.

Landfills emit substantial amounts of natural gases, such as methane and carbon dioxide, due to microorganisms that feed on the buried waste. Montauk Energy sinks wells in those landfills, removes the gases produced by decomposition, separates out the methane, and sells the purified gas, or the electricity it produces, to utilities and other end-users. The Pittsburgh, Pa.-based company operates eight landfill gas-to-energy facilities across the United States, and holds passive investments in 13 others.

According to Blue Wolf, there are currently 423 developed landfill-gas-to-energy sites in the United States owned by more than 150 different entities. Meanwhile, there are about 600 other potential gas-producing sites waiting to be tapped. Aside from being a fragmented, fast-growing market, it's also one that's poised to receive increasing government incentives over time as alternative energies continue their way to the fore of public consciousness. But unlike some other alternative energies, landfill gas production is not dependent on government subsidies.

"Landfill gas makes money today, at today's energy prices," Blue Wolf Managing Director **Adam Blumenthal** told *Buyouts* Magazine earlier this year. "The raw material used to make the gas is a waste product, so it's very inexpensive. We know exactly what we're selling, [we] know what it's worth, we know it makes money, and therefore it's a good segment for a private equity investment."

In mid-September 2006, Duquesne Light Holdings, Montauk Energy's former owner, hired investment bank Ewing Bemiss & Co. to sell the company—basically an orphan—by year-end. Ewing Bemiss put together a short-list of parties that were familiar with the alternative energy sector and capable of financing a transaction over $100 million. Blue Wolf, founded in 2005, had spent the prior year studying the alternative energy market and had participated in previous Ewing Bemiss renewable energy auctions.

"Performing due diligence on a portfolio of eight active gas processing sites and 13 additional passive investments scattered across the United States is a difficult task in the best of conditions," noted **Henry Berling**, a managing director at Ewing Bemiss & Co.

But Blue Wolf—with the aid of advisors in the environmental, accounting, insurance, legal and financial structuring areas—accomplished the task in about four weeks.

"Many parties wavered" when it came to the tight timeline, but Blue Wolf displayed an air of confidence in its ability to close and fund the deal in 2006, Berling said.

Making matters more difficult was Montauk's orphan status within a much larger entity. The company had had no audits, sold a highly volatile commodity, had some money-losing operations, and was operated to generate tax credits for its parent rather than to maximize cash flow, according to a memo sent to *Buyouts* from GoldenTree Asset Management, which provided a $72 million senior secured credit facility for the deal.

To deal with the volatility of the natural gas market, Blue Wolf adjusted its purchase price by about $8 million (it originally agreed to pay about $110 million for the company) and used a system of put options to hedge against a downturn.

While Blue Wolf's knowledge allowed for an accelerated process, the professional history between Blue Wolf's Blumenthal, **Michael Ranson** (deal leader at GoldenTree) and **Charles Miller** (Blue Wolf's counsel at Patton Boggs) made cooperation between the firms very natural. Earlier in their careers, Blumenthal had hired Ranson as an associate at American Capital and both worked with Miller, as outside counsel, on several American Capital transactions. That camaraderie fostered an environment of trust and promoted efficiency in both diligence and documentation, according to GoldenTree.

Blue Wolf closed the Montauk deal on Dec. 29, 2006, about 10 weeks after signing its confidentiality agreement. —A.N.

SNAPSHOT:

Target: Montauk Energy Capital LLC
Sponsor: Blue Wolf Capital Management LLC
Sector: Alternative Energy
Purchase Price: $101.8 million
Seller: Duquesne Light Holdings
Financial Advisor: (Seller) Ewing Bemiss & Co.
Legal Counsel: (Sponsor) Patton Boggs LLP; (Seller) Eckert Seamans Cherin & Mellott LLC
Accountant: (Buyer) Grant Thornton

Why The Deal Won

- **Blue Wolf used speed, knowledge and certainty of close as tools to win the auction for Montauk.**
- **In a matter of about four weeks, conducted diligence that took it around the United States.**
- **Blue Wolf exploited its expertise in the area of alternative energy, having spent the previous year studying the sector.**
- **This represents Blue Wolf's first-ever LBO since the firm was founded in 2005.**