



## NEWS ANALYSIS: CORPORATES CONTINUE TO CREATE MARKET FOR RENEWABLE DEALS

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**Corporate PPA volume for renewable generation is set to reach a record high in the US this year, with a broad range of companies signing deals with developers. Now, the industry must begin to look past the Microsofts and Amazons of the world and find a way to reach agreements with smaller firms while limiting their own risk.**

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### USA & Canada

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In the past five years, power purchase agreements (PPA) between clean energy developers and corporations have risen from a drop in the ocean of renewable development, growing nearly nine-fold in the US.

But even corporate PPAs have become competitive, leading some developers to search for counterparties beyond the Fortune 500. Contracts also feature complex terms that require negotiation of how much risk each party must bear.

“The biggest players with the biggest appetites are starting to get filled up,” Giji John, a partner in Orrick’s Energy and Infrastructure group, told *Inframation*. “So how do you service these guys who only want 10MW, 15MW, for less than a full 12-year term?”

In 2013, just five corporate PPAs were signed comprising a mere 320MW, according to the Business Renewables Center at the Rocky Mountain Institute, a Colorado-based think tank that tracks these deals. By 2017, that figure had multiplied to 2.78GW and this year is expected to be the most active yet – by the end of April, more than 2GW of corporate PPAs had been signed.

The early movers were technology firms, such as Google and Amazon, which comprised 70% of the corporate offtakers in 2015. This year, such firms only

comprised about a third of the megawatts signed, an indication of a broadening market.

NextEra Energy Resources inked two of the biggest agreements, selling 520MW from its wind farms in Oklahoma and Texas to AT&T. **Invenergy** reached deals with pharmaceutical firm Merck, the Grupo Bimbo bakery chain, and MGM Resorts totaling 260MW.

Several factors are creating what one advisor called a “perfect storm” for these PPAs, also called corporate and industrial (C&I) deals.

For corporations, these deals help meet renewable standards while offering a hedge against fluctuating power prices. Developers, meanwhile, gain access to counterparties, many of which are creditworthy or guaranteed by credit-worthy parent companies, in an increasingly competitive marketplace. And this trend is expected to continue at least through 2020, when production tax credits used for wind projects end and investment tax credits used primarily in solar begin to wind down.

### **Motivations**

Developers saw corporate PPAs as a new opportunity after utility PPAs became more scarce and competitive, but even corporate agreements are not an easy win these days.

Leeward Renewables, a Dallas-based wind farm developer, inked its first corporate deal in December with data center operator Digital Realty for roughly 85MW. But the firm had lost bids on several previous projects.

Greg Wolf, the firm’s CEO, said utility PPAs were traditionally coveted because they tend to feature long-term contracts, credit-worthy counterparties, and also deal with locational and delivery issues in a way that is fair. Many of these qualities are also present in a C&I deals, he noted.

While a corporation may be highly rated (Microsoft, for example, has a Aaa rating from Moody’s), it is more difficult to project how these ratings will hold up looking two decades ahead. Corporate PPAs tend to be shorter, usually running between 10 and 15 years, while a PPA with a utility generally lasts 20 to 25 years, according to Wolf. Because developers are more comfortable with long tenor that makes financing easier, utility PPAs remain the gold standard. On the other hand, utility PPAs tend to have a longer and more intensive solicitation process.

Skip Rankin, who chairs the North American renewable energy practice at Baker McKenzie, noted that counterparty risk between utilities and corporates are actually quite similar. “Many of these corporate offtakers actually have higher credit ratings than utilities,” he noted. “There is a bit of a misconception sometimes. Utilities can go bankrupt.”

For the corporate offtaker, the push for a renewables PPA is typically born out of the corporation’s sustainability team. Companies may have a renewable energy target or face pressure from employees, customers or shareholders.

“What gets these buyers in the door is this overarching global momentum for corporations to move forward on renewable energy, emissions reductions and those kinds of goals,” said Misti Groves, director of Cleantech Client Management for Schneider Electric Energy and Sustainability Services. “But ultimately, transacting on a deal also means that the corporation and the stakeholders within need to be convinced that it is a good financial deal for them.”

Schneider Electric, which purchased Renewable Choice Energy last year, works with corporations looking to contract for renewable power. It advised Digital Realty on its agreement with Leeward and this year helped firms including Fifth Third Bank and Brown-Forman (the maker of Jack Daniels and other spirits and wine) reach renewables agreements.

Each corporation has its own financial criteria, Groves said. Some firms may pay a premium for clean energy, while others will demand the economics stand on their own. All companies, however, will have some fiscal metric the deal must pass. As Rankin explains, “They are not going to want to take a bath on this.”

### **Types of PPAs**

When MGM Resorts, which owns 13 hotels and casinos on the Las Vegas Strip, decided to go solar, the company never gave serious thought to going the virtual PPA route.

“It is just not part of our personality to do projects that are out of sight, out of mind,” Cindy Ortega, MGM Resorts’ Chief Sustainability Officer, told *Inframation*. “If I did a virtual PPA in Iowa and bought wind [energy], tore the renewable energy certificates (RECs) off of that and then counted it towards Las Vegas’s greenness, we really feel like that is leaving some of the primary value of this transaction on the table.”

In 2016, MGM announced it would leave NV Energy, its public utility, to purchase electricity on the wholesale market. The company paid a USD 86.9m exit fee and left the grid with the primary goal of lowering its energy bill. In April, MGM announced an agreement to buy power from a 100MW solar project with Invenergy to be built 25 miles north of Las Vegas. Once the plant is running, power generated will go directly to the 13 hotels, providing 90% of their daytime energy.

This kind of direct transaction – in which corporates directly buy physical power from a selected wind or solar facility without going through the grid – is increasingly rare.

Even in physical (also called standard) PPAs, power almost always flows from the developer to the purchaser through the utility. The corporate offtaker works with a third party, often a scheduler or the utility itself, to deliver the power from the generator to the buyer. Along with the power, the buyer receives associated RECs.

A standard PPA requires the corporate buyer and the energy asset to be located on the same electric grid. Furthermore, they must be built in a state that permits this kind of direct access between energy developer and buyer.

Virtual PPAs – commonly called a contract for difference – require neither of these conditions. In these arrangements, the developer and the buyer agree upon a strike price which the corporate will pay for a given unit of energy. The corporate and the developer then respectively buy and sell energy at whatever price the market dictates, with the difference between the strike price and the market price then settled between the two parties.

In virtual PPAs, basis risk stems from differences between pricing at the point of interconnection, or the busbar, and the point at which electricity is priced, also called the hub. This potential difference can be large enough to quickly eliminate a project's expected returns, according to Rohit Sachdev, a partner in Orrick's Energy and Infrastructure Group.

“Oftentimes developers will find themselves in a situation where they cannot economically take the full amount of basis risk because they realize the PPA will be unfinanceable if they do,” Sachdev told Inframation. “I have not seen a PPA that does not have some kind of financial or operational cap on basis risk.”

A similar basis risk exists in physical PPAs when there are pricing differences between the busbar and the point of delivery. Corporates and developers must

negotiate the appropriate way to split this risk; as Wolf of Leeward Renewables acknowledges, there is no cookie-cutter solution.

Though less intuitive than a physical PPA, the virtual PPA is a fairly simple transaction, according to Groves. Unlike the physical PPA, it has few moving parts and requires no third party. Another advantage is that the wind or solar project does not need to be built near the corporate buyer. A single asset can power multiple sites in different parts of the country, while under a physical PPA separate transactions would be necessary.

“Virtual PPAs have opened up the off-site solar market and created opportunities for companies to make bigger investments in solar,” research director Shawn Rumery of the Solar Energy Industries Association, an advocacy group, told *Inframation* in an e-mail.

### **What comes next?**

The first quarter and change of 2018 has seen agreements reached at an unprecedented pace, and many in the industry expect this to continue.

The Renewable Energy Buyers Alliance, which promotes corporate renewable deals, targets an additional 60GW of these transactions by 2025. While the types of corporates pursuing these deals has broadened beyond tech firms, large corporations still dominate the space. For the current rate of growth to continue, it will be important for smaller firms with less sizable power needs to participate.

Utilities may end up playing a role as an intermediary, according to Orrick’s John.

“We are seeing deals which are technically utility deals, but on the backside they are contracting with retail C&Is to lay off particular green power,” John said. “I think you are going to see a rise of intermediaries that are looking to solve some of the problems that small C&I offtakers have.”

These questions notwithstanding, the industry remains optimistic that the rise of corporate renewables deals is sustainable.

“We haven’t reached the peak of the US market yet,” said Groves. “There are strong tailwinds for corporations to continue this trend of being vanguards of renewable energy adoption, and I don’t see that slowing down. If anything, it’s accelerating.”

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