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Corporate Energy Sourcing: A New Engine for Renewable Energy

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Over the past several months, a number of major corporations have announced renewable energy transactions or have made public commitments to procure 100 percent of their electric energy requirements from renewable sources. However, none of these corporations are traditional energy companies — instead, these deals are part of a trend in which companies and other entities are taking a greater role in controlling the characteristics and cost of their energy supply.[1]

According to the Business Renewables Center, roughly 10 percent of all utility-scale solar power purchase agreements (PPAs) in 2014 were signed by corporate off-takers, and approximately 25 percent of such PPAs have been signed by corporate buyers so far in 2015. To achieve what are often ambitious renewable energy procurement targets, these and other companies will need to continue to purchase significant amounts of renewable energy. As a result of these trends, some sources predict that corporations will drive more renewables development than state renewable portfolio standard (RPS) programs in the next five years. This article summarizes the tools available to corporations that want to procure renewable energy and to developers who want to sell to corporate end users.

In the past, corporations often purchased unbundled renewable energy credits (RECs) to achieve procurement goals, but unbundled REC purchases are less favored in today's market. Some companies take the view that an effective renewable procurement strategy must produce "additionality," which means directly causing a new renewable project to be built or indirectly increasing market demand so as to incentivize investment in renewable energy. These companies also want to remove obstacles to the growth of renewables by entering into long-term contracts that enable project financing. Purchase agreements for unbundled RECs may not achieve these objectives.[2]

Corporate off-takers also install or purchase energy from on-site renewable energy projects, and these projects have been a significant source of renewable energy for corporate end users over the past several years. However, an on-site, intermittent renewable energy generator may not work well for a large, 24/7 load such as a data center, and in any case there may not be enough space at the company's site to build a renewable energy project big enough to serve the load. The load may also be located in an area that is not optimal for the renewable resource involved, in which case it may make more sense to purchase the renewable energy from a better situated off-site facility.[3]

Another option is to purchase energy under green tariffs offered by regulated utilities. Historically, these tariffs have involved the use of unbundled RECs purchased from existing projects. The utility providing the service will often charge a premium over its

standard tariff rates, as adjusted from time to time, so the arrangement will not result in a fixed price for renewable energy. Some utilities, such as NV Energy, are now beginning to offer green tariff arrangements in which the utility supplies energy and RECs from its own project or a project contracted from an independent power producer in a back-to-back transaction. The tariff may lock in a fixed price for electricity and RECs and may result in the construction of a new renewable energy project. However, green tariffs are at this point available only from certain utilities in the United States and may not be available to an end user seeking to buy renewable energy.

Recognizing the limitation of REC purchase agreements, on-site project agreements and green tariffs, corporate buyers may decide to enter into a power purchase agreement with the owner of an off-site renewable energy project. Off-site renewable energy PPAs are structured as either “physical” or “virtual” transactions. A corporate buyer may choose a physical PPA when: (1) the buyer has a discrete load, such as a data center, that it wants to serve with renewable energy; and (2) it can use retail direct access to deliver the energy to the load.

In this case, the corporate buyer or a designated market participant will take title to the energy that the project generates. The energy would then be transmitted to a delivery point on the system of buyer’s local utility and delivered to buyer’s load by the utility. The delivered price of the renewable energy would be a function of the contract price, the cost of transmission across the grid and the cost of moving the electricity over the local utility’s distribution system. If the buyer wishes to participate in the wholesale market, it will need to obtain power marketing authority from the Federal Energy Regulatory Commission; otherwise, it may engage a third-party contractor to serve as the market participant.

Physical PPAs are physical, forward contracts that are usually not subject to the Dodd-Frank Act's reporting requirements. However, if the PPA contains features such as price optionality, a buyer right to require the project to curtail output, or an option to settle financially, it may be deemed a swap subject to Dodd-Frank regulation unless the option satisfies a seven-factor embedded volumetric optionality test.

Although a number of corporations continue to use physical PPAs, virtual PPAs (VPPAs), which are also known as synthetic PPAs, are being deployed more frequently. A corporate purchaser may use a VPPA when: (1) it has a distributed load, such as scattered retail outlets; (2) open access is not available to the retail load(s), which means that the load(s) can receive energy only from an incumbent utility; or (3) when projects that could be contracted with a physical PPA are not cost-effective sources of renewable energy compared to those reachable by a VPPA. Even with a virtual PPA, however, some buyers may require that the project be located in the same market as the load so that the virtual energy is generated and used in the same region.

A VPPA is a “contract for differences,” the terms of which may be embedded in the VPPA, set out in a separate long-form swap agreement, or documented as a transaction under an ISDA Master Agreement. The VPPA is a swap transaction that is

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