

Energy Risk Flying Under the Radar: Yieldcos and Net Metering

By Jared Anderson*

Energy businesses are fraught with risk, from political uncertainty to commodity price fluctuation to various financial obstacles. And while renewable energy industries like solar are not directly impacted by commodity price movements, new asset classes like yieldcos are currently under pressure from numerous angles, including uncertainty with regard to future net metering policy.

Yieldco is short for “Yield Company,” in which “yield” refers to income. “YieldCos are similar in concept to an MLP (master limited partnership) in the oil and gas sector or a REIT (real estate investment trust) in the real estate sector. All three investments are designed to provide a dependable stream of cash flow to investors,” according to Louis Berger.¹

Yieldcos use income from completed projects – often solar installations – with long-term power purchase agreements (PPAs) to distribute returns to investors in the form of dividends. All yieldcos are structured differently, meaning they consist of assets that vary from utility-scale, commercial/industrial and residential rooftop projects.

The prospect of higher interest rates, changes to renewable energy policy and stock market turbulence are all risks to the yieldco business model which have recently been highlighted. But the role of net metering has received less attention.

Net metering “allows utility customers who generate electricity on-site, usually from a solar PV rooftop system, to run their meter backward by sending the excess electricity generated back to the grid, or utility company. In turn, the utility company must pay the retail rate for the electricity sent back to the grid. This was done because it is the easiest way for the utilities to accommodate solar with their old meters and antiquated billing systems,” according to clean energy entrepreneur Jigar Shah.²

Forty-four states, Washington, D.C. and Puerto Rico have net metering policies in place.

The net metering concept has come under attack from utilities who fear their traditional revenue sources are drying up as more people sell power back to the grid from on-site renewable energy operations, while energy efficiency measures simultaneously chip away at bottom lines based on volume of power sold. It appears net metering, as traditionally applied, is unsustainable and lots of work is currently underway to find new models that more adequately reflect current power market trends.

But where does that leave investments like yieldcos that are supported by PAs designed – particularly in the rooftop residential sector - around net metering policies? It appears existing systems would not be greatly impacted, but new projects constructed under different net metering terms could change the yieldco investment calculus going forward, according to Jamie Mandel and Jeff Waller, experts at the Rocky Mountain Institute.

For example, a yieldco with a large percentage of long-term PPAs based on a bundle of rooftop solar installations calculated at a given cost per kilowatt hour could look much different if net metering policies are changed. Currently many net metering arrangements pay retail rates for the power generated by a residential rooftop system. But if this changes, what happens to yieldcos built around the old net metering system? These investment vehicles need to add new assets in order to continue growing and paying out returns and potential net metering changes cloud that future growth picture.

Indeed, President and CEO of NRG Home, Steve McBee, said his only concern with regard to the company’s yieldco structure is the “uncertainty” around net energy metering. “I would trade certainty for some potential modification to the net metering rules,” he said in an interview with Utility Dive.³

8point3 Energy Partners LP is a limited partnership between First Solar and Sun Power that did an initial public offering this past June, which raised \$420 million from investors. Class A shares were valued at \$21. By mid-October those shares were trading at about \$12.50.

In its registration statement filed with the US Securities and Exchange Commission, 8point3 clearly identifies uncertainty around future net metering policy as an investment risk:

“Our Residential Portfolio may be adversely impacted by the failure to expand existing limits on the amount of net metering in states that have implemented it, the failure to adopt a net metering policy where it currently is not in place, the imposition of new charges that only or disproportionately impact customers that utilize net metering, or reductions in the amount or value of credit that customers receive through net metering [...] Limits on net metering, interconnection of solar energy systems and other operational policies in key markets could limit the number of solar

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energy systems installed in those markets. For example, California utilities limit net metering credit to 5% of the utilities' aggregate customer peak demand. California has adopted legislation to establish a process and timeline for developing a new net metering program with no cap on participation. If the caps on net metering in California and other jurisdictions are reached or if the amount or value of credit that customers receive for net metering is significantly reduced, future customers will be unable to recognize the current cost savings associated with net metering. Net metering is used to establish competitive pricing for prospective customers and the absence of net metering for new customers would greatly limit demand for residential solar energy systems." - 8point3 Energy Partners LP⁴

Inasmuch as net metering policies are still very much a topic of debate in the US, there are more pressing risks facing yieldcos over the short term. The potential risk associated with net metering changes may currently be overshadowed by stronger headwinds, over the longer term however, yieldcos with large residential solar portfolios in states where net metering is likely to be changed could be impacted. Investors looking at yieldcos should consider the size of the company's residential portfolio and the states in which those systems are located in order to more accurately evaluate potential risk associated with this relatively new asset class.

Footnotes

¹ "What You Need to Know About How Clean Energy YieldCos Work," Greentech Media, July 10, 2014. <http://www.greentechmedia.com/articles/read/what-you-need-to-know-about-how-yieldcos-for-clean-energy-work>

² "Solar To Eat Costs of Net Metering if Utilities Cough Up Data," LinkedIn Pulse, May 29, 2015. <https://www.linkedin.com/pulse/solar-eat-costs-net-metering-utilities-cough-up-data-jigar-shah?redirectFromSplash=true>

³ "What happened when NRG Energy disrupted its own business model?"

Its biggest new subsidiary, NRG Home, is building a business around empowering customers," Utility Dive, July 1, 2015. <http://www.utilitydive.com/news/what-happened-when-nrg-energy-disrupted-its-own-business-model/401472/>

⁴ "8point3 Energy Partners LP REGISTRATION STATEMENT UNDER THE SECURITIES ACT OF 1933," US SEC, June 10, 2015. http://secfilings.nasdaq.com/edgar_conv_html%2f2015%2f06%2f10%2f0001193125-15-218889.html#D876955DS1A_HTM_ROM876955_12



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