Wild West of Renewables

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The Wild West of Renewables: What New Entrants to the Market Should Know

The renewable energy industry is increasingly resembling the "Wild Wild West." Current market forces, prioritization of environmental, social and governance (ESG) frameworks and differing renewable energy policies across states have driven more opportunity seekers into this new frontier.

Renewable energy has been the fastest growing energy source in the U.S. since the turn of the century. According to the International Renewable Energy Association, "The United States of America installed 29 GW of renewables last year, nearly 80 per cent more than in 2019, including 15 GW of solar and around 14 GW of wind." And the Biden Administration has made renewable energy a priority, including $73 billion in the infrastructure bill, passed by the Senate in August, to expand the nation's power transmission grid and better equip it to carry renewable energy. Additionally, the recently released "Build Back Better Act" includes numerous proposals intended to further incent renewable energy development, including incentives for carbon sequestration and wind and solar power generation, storage and transmission.

As a result, many players entering the industry – whether traditional power suppliers looking to diversify asset portfolios with renewable investments, vertically integrated utilities looking to demonstrate their commitment to decarbonization and cleaner energy to their customers and regulators, companies looking to offset their carbon footprint, and/or private equity investors gravitating toward sustainable finance — hold renewable energy in their portfolio. To succeed, these pioneers need a clear understanding of how regulation, tax reform and investor scrutiny impact the sector.

For those unfamiliar with the territory, key areas to consider are ESG strategy and reporting, and tax policy.

ESG is adding horsepower to renewables, and companies must have a tight grip on the evolving landscape

Increasing demand for renewable sources of energy is creating a market for new entrants, driven by the increased prevalence and visibility of extreme weather events like wildfires, rising sea levels and other warming events. The investor landscape forming around ESG is opening new frontiers of opportunity for companies to drive profitable growth and increase value for investors.

Companies entering this market should be prepared to define their sustainability strategies and enhance their reporting using both qualitative statements and quantitative metrics to prove how these efforts generate value to the company. One of the most prominent frameworks to articulate the risks and rewards of climate-related efforts is the Taskforce on Climate-related Financial Disclosures (TCFD) which details how companies can articulate these emerging risks which threaten profitability and new opportunities that unlock value.

In its 2020 status report, The Financial Stability Board (FSB), which established the TCFD, [notes](https://www.fsb.org/2020/10/2020-status-report-task-force-on-climate-related-financial-disclosures/), "Energy companies and materials and buildings companies are leading on disclosure, with an average level of TCFD-aligned disclosures of 40% for energy companies and 30% for materials and buildings companies in fiscal year 2019." [1] Through this reporting, companies are expected to disclose their strategies for companies to reduce emissions. Additionally, KPMG outlines some ways companies are looking to operationalize sustainable behavior: "While carbon offsets and Renewable Energy Credits (RECs) remain prominent, there is particular emphasis on making the transition to renewables via Purchase Power Agreements (PPAs) as well as investment in onsite or offsite generation." [2] Meanwhile, investors and activists are also demanding action and strategies for companies to reduce emissions.

With efforts to develop global reporting standards progressing, new entrants should prove their impact and establish credibility by engaging an assurance provider to assess the completeness and accuracy of their reporting and the rigor of their processes to produce this information. Preparing now can help ensure that they meet all stakeholders demands with sophistication to gain trust over the long-term.

Tax policies accelerate growth

As ESG gains steam, a thoughtful tax strategy that takes the evolving legislative and regulatory environment into account will become more important.

The use of incentives, largely through the tax code, has traditionally been the way energy policy has been implemented in the U.S. Most recently, the Consolidated Appropriations Act, signed into law in December 2020, enacted provisions favorable to the renewable energy industry. It included a two-year extension of the phasedown of the investment tax credit for solar energy and a one-year extension of the production tax credit for wind energy facilities.[3]

While the legislation is not yet finalized, it is clear the Biden Administration, through the "Build Back Better Act," intends to induce electric utilities and power producers to further shift to emission-free power sources. The proposed legislation provides tax incentives to build high-voltage capacity power lines and electric vehicle charging stations and includes additional incentives for carbon capture and sequestration efforts. It also includes a direct pay feature which could result in some of the incentives essentially refunded to the project owner – a potential game changer for financing these projects which currently rely on the tax equity financing market.

Additional opportunities could come from areas of public investment interest, including solar panel technology and storage capabilities. Up to this point, this has been an area dominated by China and remains a barrier to U.S. energy independence. The recent proposals include an additional incentive for facilities that are composed of primarily products manufactured in the U.S. as well as an incentive for investment in U.S. facilities that manufacture clean energy equipment.

With effective policy, the renewable energy supply chain has the capacity to expand rapidly and push the U.S. toward the proposed goal of 80 percent clean-energy sources within the next decade.

A wide-open landscape for new entrants, with caveats

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[1] "2020 Status Report: Task Force on Climate-Related Financial Disclosures," Financial Stability Board, October 29, 2020, https://www.fsb.org/2020/10/2020-status-report-task-force-on-climate-related-financial-disclosures/.
[2] "Demystifying Decarbonization: The Journey to Net Zero," KPMG U.S., accessed October 7, 2021, https://info.kpmg.us/news-perspectives/industry-insights-research/demystifying-decarbonization-the-journey-to-net-zero.html.
[3] "Favorable Tax Provisions for Renewable Energy Industry Enacted," KPMG U.S., December 30, 2020, https://home.kpmg/us/en/home/insights/2020/12/tnf-favorable-tax-provisions-renewable-energy-industry-enacted.html.

ESG strategies and reporting and tax policy will continue to be critical areas of focus as pressure increases from consumers and regulators, and utilities and other companies move to reduce their carbon footprint and come closer to reaching net zero goals.

Understanding the nexus between ESG accounting and reporting and tax policies specific to the industry, will ensure you are pioneering. Boards and leadership teams can help drive this by ensuring close coordination between the tax and finance departments and those responsible for ESG reporting, as lack of coordination may compound audit and tax risks, especially for those new to the reporting process.

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