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Challenges Facing Energy Businesses in the COVID-19 Outbreak

In addition to the multiple challenges facing all business entities, the COVID-19 outbreak is causing particular issues for companies in the energy sector. These include:

Regulated Utilities

One need look no further back than the twin long-term outages caused by Tropical Storm Irene and the Halloween snowstorm in New England in 2011 to appreciate the public relations and financial ramifications that electric utilities can face as a result of appearing unprepared for natural disasters. While the utilities had no ability to prevent those storms, the apparent lack of a recovery plan resulted in public embarrassment, the disallowance of costs deemed to be the result of the utilities' imprudence and, ultimately, the termination of several high-ranking executives. Without a different level of response, it is easy to envision the same result here, if utilities are unable to keep the lights on.

Maintaining reliability requires a trained workforce. The Edison Electric Institute, though, has estimated that some utilities may see as much as 40 percent of their workforce impacted by COVID-19. In light of this, the Federal Energy Regulatory Commission and the North American Electric Reliability Corp. have announced that the coronavirus will be considered an acceptable basis for noncompliance with certain of their standards, including the use of NERC-certified operator personnel. If personnel needed to operate the utility system are required to take time off for self-quarantines or for recovery from COVID-19, questions can quickly arise about the availability of adequately trained backups for those personnel, and about whether adequate steps have been taken to ensure 24/7 operation.

Similarly, regulated utilities may need to incur unexpected costs to continue operations that they may wish to recover in rates. Two examples are added costs arising from retaining contractors to replace personnel affected by COVID-19 and materially higher prices arising from replacing equipment because existing supply chains are disrupted as a result of the epidemic.

Anticipating and addressing these risks, regulated utilities will be well served to have documented plans for dealing with these issues. Equally important is the implementation of a communications plan to inform government officials and the public at large of the status of operations and restoration plans. While the pandemic itself may not have been modeled in the utilities' regular planning processes, it is not too late to develop plans that can be used later to demonstrate the prudence of their actions in addressing the issues now.

Another area of particular interest will be the moratoria on service disconnections for failure to pay that are being implemented in many states, either voluntarily or by order of the state regulator. COVID-19 is hitting precisely at the time when the bans on wintertime service shut-offs are ending, requiring the utilities to absorb additional costs that likely will not be recovered from those customers. In some cases, rate adjustments may be needed to account for that loss of revenue.

Finally, the potential for a recession resulting from this health crisis could translate into a serious drop in demand for utility services. The revenues of regulated utilities are affected to varying degrees by the volume of energy or gas consumed by their customers, and those revenues will decrease with a drop in demand. While they may ultimately be able to seek future rate adjustments to reflect lower demand, there will necessarily be a lag between the drop in revenue and any approved rate accommodation. Such projections may require notification to regulators, shareholders and the Securities and Exchange Commission.

Competitive Retail Suppliers

Third-party competitive retail electric or gas suppliers may be impacted by COVID-19 in a variety of ways, both immediately and in the coming months. In the near term, several states are moving to limit various types of marketing strategies. The types of marketing generally impacted are door-to-door marketing or sales at other venues where there are large gatherings of people, such as at public events or malls. While door-to-door sales typically refer to residential customers, public utility commissions may issue emergency orders to apply these channel restrictions to all customer classes. In addition, individual states typically have existing prohibitions on price gouging or excessive pricing during a state of emergency that is triggered by a declaration of the governor or the president. These prohibitions could impact pricing for both initial contract terms and renewal provisions. Many states establish a pre-set percentage threshold limiting automatic rate increases on renewals, generally ranging from 10 to 20 percent. Pricing in excess of the set threshold could be deemed evidence of excessive pricing; however, certain exceptions and carve-outs often apply.

Revenues of competitive retail suppliers, like regulated utilities, depend on the volume of sales to their customers. If consumption drops as a result of business interruptions and the recession, so too will the revenues of the suppliers.

Some best practices include reviewing those contracts that may require minimum or maximum usage to determine the obligations of both the competitive supplier and the customer. Part of this review should include an analysis of the force majeure provisions in the contract to determine if COVID-19 may trigger those provisions. Competitive suppliers should also be aware of various state moratoria on utility disconnections now in effect, as described above. Even if it is the utility, and not the competitive supplier, that controls the shutoffs, competitive suppliers could see long-term impacts from these policies in states where there is utility purchase of receivables from suppliers. Other considerations that may impact the day-to-day operation of a competitive supplier's business may include the continually decreasing number of people that can gather in one place. These restrictions may impact company meetings and daily operations such as the call center sales force and decrease consumption by that supplier's customers. Further, various state public utility commissions have already implemented certain temporary changes to filings, including acceptance of electronic submissions only and holding certain meetings by telephone or via virtual platforms.

Clean Energy Developers

Developers of wind, solar and other clean energy projects face two principal challenges as a result of COVID-19. First, development of the projects can be delayed, with numerous potential implications. There are already reports of supply chain disruptions, particularly for solar panels and other components produced in China, Germany and other nations hit hard by the virus, and these disruptions can push back construction schedules. If developers are able to acquire all the necessary materials for their projects when needed, there is also the risk that the project could be delayed if the skilled workforce needed to construct these projects is significantly impacted by COVID-19. Such delays can cause problems for developers both under their power purchase agreements and potentially in meeting "commencement of construction" deadlines for federal tax credits or running over the four-year continuity of construction requirement for those credits. Developers should be analyzing the *force majeure* provisions in their key contracts. While they may have sought to shift project delay risk to the engineering, procurement and construction contractors building those projects, those contractors may be able to avail themselves of *force majeure* provisions in their contracts with the developers. The power purchase agreements, may have narrower *force majeure* provisions (or shorter time periods until the other party can terminate after the start of a *force majeure*).

Second, the extreme volatility in the financial markets could result in a tightening of the available capital needed to build those clean energy projects. As was the case in the 2008 financial crisis, a recession will mean less income for the financial institutions that invest in those projects, making the tax credits that drive those investments less desirable. The combination of a tighter credit market and a depressed market for tax credits could have serious negative ramifications for some projects.

For more Day Pitney alerts and articles related to the impact of COVID-19, as well as information from other reliable sources, please visit our [COVID-19 Resource Center](#).

publication. We have not attempted to address the potential impacts of all local, state and federal orders that may have been issued in response to the COVID-19 pandemic.

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