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Japan Announces High Prices Under Feed-In Tariff for Renewable Energy Sales to Utilities

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On June 18, 2012, Japan's Ministry of Economy, Trade and Industry (METI) announced very attractive pricing for sales of renewable energy to Japan's regional utilities under a new feed-in tariff (FIT). Under the FIT, solar projects over 10kW in size can be paid ¥42 ($0.53) per kwH under a 20-year Power Purchase Agreement (PPA); wind projects over 20kW can be paid ¥23.1 ($0.29) per kwH under a 20-year PPA; and geothermal projects over 15MW can be paid ¥27.3 ($0.34) per kwH under a 15-year PPA.

These terms are in effect for the period from July 1, 2012 to March 31, 2013. Going forward they will be subject to annual review by a METI-appointed committee. The additional cost of the tariff over conventional power generation is directly passed on to consumers by means of a surcharge on all power consumers and the utility does not incur the additional cost.

Japan's Energy Shortfall

A major reason for the new FIT is to attract new renewable energy generation as a partial replacement for the nuclear reactors destroyed or taken offline as a result of Japan's March 2011 tsunami. Before the tsunami, Japan had 54 reactors with total installed generating capacity of 49 gigawatts, and nuclear energy provided 27% of all electric power in Japan in 2010. With most reactors still offline, Japan currently suffers a major shortfall in electricity generation capacity, and renewables are one element of Japan's strategy to bridge the gap. Bloomberg New Energy Finance forecasts that the new law may spur, for solar energy alone, at least $9.6 billion in new installations with 3.2 gigawatts of capacity.

METI and Utility Approval - Grid Interconnection Challenges

Developers seeking to take advantage of the FIT must obtain the approval of METI. Obtaining METI's approval requires, among other things, confirmation of the renewable energy supplier's technical ability to provide stable, measurable power by means of identified generation equipment. Once a supplier is approved by METI, it must enter into a PPA with a utility and negotiate the arrangement to interconnect the supplier's renewable energy project and the utility's grid. The PPA is typically signed before project construction begins.

Japan's electricity utilities consist of nine regional companies that hold a monopoly over the provision of power to consumers in their respective regions. Under the new FIT rules, these utilities are obligated to purchase power from generators of renewable electricity, but METI has granted the utilities a number of vague exemptions to their new obligation to purchase renewable energy, e.g., if the new supplier would add to grid instability. This is in addition to the normal utility bureaucracy and physical interconnection challenges involved in connecting a new electricity generator to the grid. Because the regional utilities have a number of practical and legal ways to opt out of their interconnection obligations, the corresponding risks to the renewable energy supplier must be analyzed carefully and managed to the extent possible through the appropriate allocation of such risks in the PPA.

Each regional power company in Japan may take a different approach to renewables based on their existing and future sources of power. The selection of a region in Japan to pursue new renewable opportunities will be a critical factor in a developer's success or failure.

Prospects for Non-Japanese Renewable Companies

A company without experience in Japan will probably find it impossible to manage a new renewable power project from start to finish by itself. We expect that there will be opportunities for international renewable energy developers to seek joint ventures with local partners in Japan in order to develop successful projects. A Japanese partner could take the lead in obtaining METI approval, negotiating the relationship with the regional utility, and managing local land and entitlement issues. The Japanese partner could be a Japanese trading company or technology company, or in some cases, a local government or even the regional utility itself.

An international renewable energy developer can bring a great deal to the table. Apart from expertise in interconnection agreements, PPAs and the development process, a non-Japanese developer who is not tied to a Japanese equipment supplier may bring a pricing advantage. With Japan's strong yen, the cost of manufactured products such as solar panels in Japan can be as much as double the costs in other developed markets. By using lower cost products of good quality, the international developer may be able to substantially improve the economics of a proposed renewable energy project.

If you have questions, please contact the Pillsbury attorney with whom you regularly work or a member of Pillsbury's renewable energy team:

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