S&P Global
Ratings

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Summary:

Marin Clean Energy, California; Retail Electric

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Long Term Rating	A/Stable	Affirmed

Credit Highlights

- S&P Global Ratings affirmed its 'A' issuer credit rating (ICR) on Marin Clean Energy (MCE), Calif.
- The outlook is stable.

Security

The ICR represents our view of MCE's capacity and willingness to meet its financial commitments as they come due and does not apply to any specific financial obligation. MCE has no debt outstanding, nor does it plan to issue any debt in the near term.

Credit overview

The ICR reflects MCE's growing and predominantly residential customer base with well-above-average incomes across Contra Costa, Marin, Napa, and Solano counties. The rating also reflects the community choice aggregator's (CCA) robust liquidity balances and an overwhelmingly carbon-free energy portfolio. Tempering these strengths are the weakened fixed-charge coverage (FCC) in fiscal 2021 and 2022, the ease with which customers can transition back to the incumbent utility, and retail electric rates that are elevated relative to state averages. Additional risks are a power portfolio that is exposed to volatile market prices via short- and medium-term purchases and contracts, rising resource adequacy (RA) costs, and contracted power supply counterparties that include several companies that exhibit weak credit quality or that we do not rate.

MCE's enterprise risk profile further reflects the following:

- Service area income indicators are robust, and the customer base is diverse and primarily residential, which we believe provides the CCA with revenue stability.
- Retail electric rates are relatively high compared to the state average. However, MCE sets its rates based on its cost of service, which we believe provides it with greater ratemaking flexibility and ultimately allows it to cover costs more predictably and reliably in a wider array of market conditions.
- The fuel mix consists largely of renewable and non-carbon-emitting resources from 111 long-term, medium-term, and short-term power purchase agreements (PPAs) and 45 RA-only contracts.

MCE's financial risk profile further reflects the following factors:

- FCC weakened in fiscal 2021 and 2022 but rebounded to 1.18x in fiscal 2023 (excluding the transfer to the rate stabilization fund [RSF], 1.3x prior to the transfer) due to the lower power charge indifference adjustment (PCIA)

coupled with a significant generation rate increase in 2023.

- Liquidity is robust at over 168 days of operating expenses for fiscal 2023, including a $60 million line of credit and the RSF.
- The utility has no debt outstanding and no plans to issue debt in the near term.

Environmental, social, and governance

We believe that MCE faces limited environmental risks. Purchases of wind, solar, and hydroelectric generation resources that are free of greenhouse gas emissions covered about 90% of 2022's load when looking at its light green product (which the majority of its customers purchase). MCE has been supplying 90% greenhouse gas-free since 2017, years ahead of Senate Bill (SB) 100, and about 60% eligible renewable. Also, to comply SB 350, at least 65% of the procurement counts toward its renewable portfolio standards (RPS) shall be from contracts 10 years or more in duration. MCE has executed RPS contracts of 10 years or more in duration to meet the SB 350 requirement through 2027. We believe MCE's current and projected energy portfolio positions the utility favorably relative to California's stringent and continually evolving regulatory landscape. Yet, as a practical matter, the intermittency of renewable resources might frustrate the CCA from achieving those goals, especially given the rising costs of battery storage technology inputs.

Direct wildfire liability risk is limited because MCE outsources its transmission and distribution functions. However, public safety power shutoffs by the owners of the transmission and distribution systems serving MCE's customers could nevertheless adversely affect the reliability of customers' electric service. Additionally, they could lead Pacific Gas and Electric Co. (PG&E) to charge MCE's customers higher transmission and distribution costs. We understand if PG&E is held liable, it would first use its Wildfire Expense Memorandum account, which is funded on an ongoing basis through delivery fees. Management has indicated it is exploring the possibility of asset ownership in the future, which could create direct exposure to wildfires and related liability claims.

We believe MCE faces slightly elevated social risk. MCE's residential customers pay rates that are slightly lower than PG&E residential rates, and we note that PG&E's rates are elevated (124% of California's average retail system rate in 2021), which could weigh on financial flexibility. However, this is mitigated somewhat by well-above-average effective buying incomes across MCE's territory.

Finally, we view the utility's governance factors as generally credit supportive, as they include proactive risk management, robust joint powers agency (JPA) member agreements that limit both the ability and incentive for member departure, and strong policies and planning. However, the potential for retail customer opt-out is beyond management's control and tempers our view of the CCA's governance factors somewhat.

Outlook

The stable outlook reflects our anticipation that exceptionally strong incomes across the service territory will continue to mitigate high rates, the robust and increasing liquidity balance coupled with counterparty collateral posting requirements will reduce (but not eliminate) counterparty and customer migration risks, customer retention rates will remain stable, and the resource portfolio will continue to limit the utility's exposure to increasingly stringent emissions

regulations and competitive and potentially volatile wholesale markets

Downside scenario

We could lower the rating if the cost of future power and/or energy storage negatively affects competitiveness, especially against the backdrop of a growing customer base, or if MCE faces significant power supply counterparty nonperformance that erodes the CCA's competitive position and/or financial performance while simultaneously increasing dependence on wholesale market prices. We could also lower the rating if MCE experiences customer opt-outs that leave it with meaningful surplus energy purchase commitments whose cost must be recovered through either liquidation into competitive wholesale markets or rate increases.

Upside scenario

We do not expect to raise the rating during the two-year outlook time frame given the recent lower FCC, recent increased costs associated with RA, and potential recontracting costs related to short-term contracts. However, we could do so if MCE procures reliable and competitive power under longer-term contracts to support load growth while FCC materially improves on a sustained basis without material erosion of customer retention, rate competitiveness, or liquidity. We would reassess financial metrics and wildfire exposure if MCE were to issue debt.

Credit Opinion

Enterprise profile

MCE is a JPA originally formed in 2008 (with retail service beginning in 2010) to procure retail electric power on behalf of about 580,000 accounts serving more than a million people across 37 member communities in four San Francisco Bay Area counties. The customer base increased by about 20% from 2020 to 2023. MCE derives the majority of its retail revenues from residential customers (about 51% in fiscal 2022), which we believe provides the CCA with revenue stability. Management indicated no new communities being added in 2023 or 2024, but potentially in 2025 in Contra Costa County. We believe MCE's large size provides the utility with economies of scale. However, the continued growth results in an ongoing need for MCE to expand its power portfolio--a potential exposure.

PG&E, on behalf of MCE, performs monthly retail electric meter readings, bills MCE's customers, collects customer payments, and conveys over its transmission and distribution systems the electricity MCE procures. PG&E segregates and remits to MCE the revenues it collects for MCE; we understand these revenues are insulated from an investor-owned utility (IOU) bankruptcy.

Retail electricity customers who migrated to MCE at the introduction of service in their area may return to their respective incumbent IOU upon 60 days' notice. MCE does not impose fees on departing customers. We consider the relative ease with which customers can return to their previous electric utility a potential risk to MCE's revenue stream. While MCE's opt-out rate is elevated relative to that of other rated CCAs at about 13%, we note that a significant portion of these departures occurred closer to MCE's inception as the first CCA in California. The participation rate has increased since 2020.

Representatives of MCE's member jurisdictions comprise the CCA's board. The board sets the retail rates for the power it procures. In addition to MCE's energy charges, the major components of the customer bills that PG&E

prepares also include charges for energy delivery, administrative expenses, and the PCIA. The PCIA is a legislatively created vehicle. It provides for the IOUs' recovery of those portions of pre-existing generation investments and energy procurement costs that market sales of energy surpluses created by customer migrations to CCAs do not financially support. The PCIA shields IOUs' non-CCA customers from the cost shifting that might otherwise occur due to the migration of retail customers to CCAs. The PCIA varies by customer class, but decreased by about 90% since 2021 to 2023, which somewhat enhanced MCE's ratemaking flexibility. MCE raised rates in January 2023, the average retail generation rate increased by approximately 20% which was somewhat offset by the reduction in the PCIA. Moreover, no further rate increases are planned at this time.

Rather than following PG&E's rates up and down as many CCAs' rates do, which could result in uneven financial performance, MCE sets its rates based on its cost of service. We believe this rate-setting practice provides the utility with greater ratemaking flexibility and ultimately allows MCE to cover costs more predictably and reliably in a wider array of market conditions. This model has resulted in MCE net rates (inclusive of the PCIA charge) exceeding those of PG&E for certain periods in the past. Importantly, customer opt-outs have not increased markedly during these periods, suggesting an additional layer of ratemaking flexibility.

MCE's power portfolio is diverse, in our view, with more than 150 power purchase contracts and RA contracts in place. Similarly, the CCA's fuel mix is diversified among a number of clean and renewable resources including large hydro, solar, biomass, geothermal, small wind, and wind. With large hydro and solar making up the bulk at about 60%. Tempering these strengths are the rising cost of RA, volatile energy costs, and short-term recontracting risk, which could result in MCE raising rates, weakening competitiveness or financial metrics. Additionally, although there is significant diversity among counterparties, there is still risk associated with the low-rated or unrated counterparties.

To mitigate impacts of price spikes and market volatility, MCE continues to add long-term contracts. The long-term contracts include geothermal, wind, stand-alone storage, and solar and storage. MCE was in full compliance with RA requirements in 2023 and is adding storage capacity and long-term purchased power agreements to continue to meet these requirements.

Financial profile

MCE does not have any debt; however, S&P Global Ratings calculates FCC to reflect our view that MCE is funding its contracted power suppliers' recovery of investments in generation capacity. When calculating FCC, our proxy for suppliers' recovery of capital investment from their purchasers reduces operating expenses and imputes debt service by a matching amount. Applying that adjustment, we calculated FCC fell to 1.07x in 2021 and 1.14x in 2022 due to higher PCIA rates and elevated energy costs. However, it rebounded to 1.26x in fiscal 2023 (prior to the transfer to the RSF), given the sizable generation rate increase in 2023 and lower PCIA. When removing the transfer to the RSF, FCC was 1.18x. Based on our calculations of management-provided projections, we expect FCC will remain strong at between 1.2x and 1.5x, and averaging 1.2x over the next five years. Management expects power supply costs to increase by about 14% from fiscal 2023 to 2024, primarily due to the increase costs of RA. Management's projections do not assume any rate increases, but we understand management would consider further rate increases if needed.

At fiscal year-end March 31, 2023, MCE had $277 million of unrestricted cash and investments (including a $60 million revolving credit agreement and the RSF), equivalent to 168 days of operating expenses. In our view, this provides a

robust cushion for tempering exposures to potential customer departures or supplier disruptions. Moreover, liquidity is projected to rise continually through the forecast period, providing additional cushion in the event of above-budget power costs or other expenses. In 2020, MCE created an operating reserve to defer revenue when financial results are strong and to use in future years when financials are stressed. For fiscal 2023, this fund will total $30 million. We believe the continued maintenance of robust liquidity underpins the current rating, given the previously discussed operational risks MCE faces.

MCE indicated it is exploring the possibility of direct asset ownership through debt issuances, if the additional debt and associated assets were economical and would fit within its risk management tolerances. No such projects or assets have been identified at present. We would revisit our assessment of MCE's debt and liabilities if the CCA added concrete plans to issue debt.

Marin Clean Energy, California--key credit metrics

	--Fiscal year ended March 31--		
	2023	**2022**	**2021**
Operational metrics			
Electric customer accounts	586,000	575,000	540,000
% of electric retail sales from residential customers	51	51	51
Top 10 electric customers' sales as % of total electric retail sales	7	7	7
Service area median household effective buying income as % of U.S.	149	149	149
Financial metrics			
Gross revenues ($000s)	655,594	487,703	454,740
Total operating expenses less depreciation and amortization ($000s)	602,625	473,384	426,745
Debt service ($000s)	N.A.	N.A.	N.A.
Debt service coverage (x)	N.A.	N.A.	N.A.
Fixed-charge coverage (x)	1.2	1.1	1.1
Total available liquidity ($000s)*	277,727	209,627	223,177
Days' liquidity	168	162	191
Total on-balance-sheet debt ($000s)	N.A.	N.A.	N.A.
Debt-to-capitalization (%)	N.A.	N.A.	N.A.

*Total available liquidity includes available committed credit line balances, where applicable. Debt service coverage--Revenues minus expenses divided by debt service. Fixed-charge coverage--Sum of revenues minus expenses minus total net transfers out plus capacity payments (or their proxy), divided by the sum of debt service plus capacity payments (or their proxy). N.A.--Not available.

Related Research

Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022

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