
July 21, 2017

Mr. Mario Bohorquez
Illinois Power Agency
Michael A. Bilandic Bldg.
Suite C-504
160 N. LaSalle Street
Chicago, IL 60601

BY E-MAIL: Mario.bohorquez@illinois.gov

RE: Illinois Industrial Energy Consumers Comments to the Illinois Power Agency's Draft Zero Emission Standard Procurement Plan – 2017

Dear Mr. Bohorquez:

Pursuant to Section 1-75(d-5)(1)(C), the Illinois Industrial Energy Consumers ("IIEC") respectfully submit these comments on the draft Zero Emission Standard Procurement Plan ("Plan") which the Illinois Power Agency ("IPA" or "Agency") released for public review and comment on July 11, 2017.

IIEC appreciates the considerable effort by the IPA to put forward a comprehensive Plan within what IIEC considers to be a very limited and unrealistic time period for the development of such Plan. Rather than using this comment process as a forum for contesting points of disagreement, IIEC has generally sought to limit its comments to areas where the IPA has either solicited comments, or to provisions which need to be modified to make the process more transparent and to consider the point of view of the Illinois utility customers required to pay for Zero Emission Credits ("ZEC").
IIEC reserves the right to make further edits, comments or proposals in subsequent filings, as well as to present additional or different positions and arguments in any docketed proceeding involving this Plan, based on the contents of the filed Plan and on other parties' positions. IIEC recommendations are also reflected in a redlined version of the elements of the Plan, which are attached to this letter as Appendix A.

**Section 3.5 ZEC Procurement Cost Cap**

The Plan observes that the Zero Emission Standard sets an annual rate impact cap on the amount a utility's end-use customers pay through surcharges for the purchase of ZECs. (Plan at 16). In its discussion of this issue, the Plan reports that the Illinois Power Agency Act contemplates an approach ". . . in which ZECs are delivered at the price arrived at through the Social Cost of Carbon minus the Price Adjustment (the ZEC price) *up until* the rate impact cap for that delivery

year is met; from that point forward, ZECs are to still be delivered under contracts to meet the delivery requirement set forth in Section 1-75(d-5)(1), and the requirement that the contracts be for 'all of the zero emission credits generated' by the winning facility, but are considered to be 'unpaid contractual volume' potentially eligible for a future year's payment." (Plan at 17).

The Plan goes on to report that if the ZECs produced by winning bidders exceed the ZEC volumes to be paid for at the ZEC price under the cost cap, the IPA believes those ZECs that are not eligible for payment in the subject delivery year, i.e. which are generated at a level that exceeds the target procurement quantities, would be delivered to the purchasing utility without charge for that delivery year and constitute "unpaid contractual volumes," eligible for payment in the future delivery year when the rate impact cap is not exceeded.

The Plan reports that the situation described above raises the issue of what should be the appropriate payment for the "unpaid contractual volumes" from previous delivery years. (*Id.*). The issue arises if there are changes in the ZEC payment price due to changes in wholesale energy and capacity prices, or to eventual increases in the Social Cost of Carbon. Such changes could be either positive or negative. Specifically, the IPA states that it "believes that the price paid per ZEC should be uniform across a given delivery year, the subsequent year's ZEC price should apply to any prior year's 'unpaid contractual volume' (doing otherwise would potentially result in a host of different ZEC prices applying to a given delivery year), … ." (Plan at 17, Fn. 60). The Plan invites further comments on this topic.

From a customer's point of view, IIEC agrees with the IPA that the ZEC price should be uniform across each delivery year and subsequent year prices should apply to a prior year's "unpaid contractual volume." IIEC agrees that customers should not be exposed to multiple ZEC prices during the relevant delivery service year. The effect of a "carry-over" ZEC obligation is to effectively increase the obligation in a subsequent year. Such increase in obligation should reflect the price in effect at the time it is eventually paid. For example, if the ZEC price is lower in a subsequent year, due to an increase in market revenues for capacity or energy then the zero emission facility has less need for subsidy. Likewise, if the ZEC price is higher in a subsequent year, due to decreases in market revenues for capacity and energy, then the zero emission facility has greater need for subsidy.

IIEC has not proposed any modification of the language of the plan in relation to this comment.

### 5.3.1 Risk-Based Multiplier and 5.3.2 Economic Stress Multiplier

In this section of the Plan it is reported, "[i]n order to reflect the lesser risks that zero emission facilities with rate-based cost recovery opportunities are exposed to as compared with zero emission facilities that are operated on a merchant basis, the Agency will incorporate a risk-based risk multiplier into the process for selecting successful bids." IIEC believes that in developing the risk-based multiplier (and the economic stress multiplier identified in Section 5.3.2), the Agency should be provided with all the relevant information needed to develop and apply such multipliers.

For example, a zero emission facility operating in a competitive electric market, such as Illinois, may be a party to one or more bilateral sales contracts, suggesting that their revenues may not be subject to the same commodity price fluctuations and supply/demand dynamics to which other

zero emission facilities in Illinois may be exposed or which are transparently reflected in the PJM and MISO real time energy markets or capacity procurement events. Thus, these particular facilities may be relatively less risky in comparison to zero emission facilities that rely on the regulatory process to adjust rates to ensure recovery of operating costs and a return on investment for their owners. In this example, zero emission facilities in Illinois with bilateral contracts, all else equal, would have less exposure to fluctuating market conditions and thus less risk of early retirement brought about by economic stress than the facilities without such contracts.

Therefore, in developing its risk-based multiplier, the Agency should require bidders to inform the Agency of the existence of any bilateral contracts and to provide such contracts to the Agency so that the Agency can determine the appropriate multiplier to apply to that bidder's bid.

IIEC also observes that the IPA has expressed interest in receiving comments on whether a comparison of operating costs for a zero emission bidder to a statutorily referenced baseline market price index is appropriate for establishing an economic stress multiplier, or if there is a sound, well supported, basis for the use of different information. (Plan at 43). IIEC respectfully suggests that receipt of information regarding bilateral contracts that the subject bidder has entered into would provide the IPA with information that would help in the establishment of an economic stress multiplier, since the existence of such contract and the pricing of same would, all else equal, reduce, or at least reveal, the economic stress associated with such facilities.

IIEC proposes that the Plan be modified to reflect this approach. Sections 5.3.1 – Risk-Based Multiplier and 5.3.2 – Economic Stress Multiplier, showing IIEC's recommended redline changes, are attached hereto as Appendix A.

### 6.4 ZEC Contracts

In this section of the Plan, the IPA reports that the Illinois Power Agency Act requires Illinois utilities to enter into binding contractual arrangements with winning zero emission facilities. The IPA observes that it will not be a party to the contract and that the term of each contract will be ten years. IIEC is concerned that given the lengthy nature of these contracts, there is a possibility that new markets for ZECs may be created in the PJM or MISO regions, or otherwise, and that ZECs could become a fungible trading instrument. In theory, utilities may be able to sell ZECs that they have acquired, but not yet paid for. If utilities are able to sell these ZECs at the end of the contract term, IIEC believes that the proceeds of any such sale should be refunded to utility customers. Under such circumstances, any contract form approved for the acquisition of ZECs from the winning zero emission facility, should include a provision requiring that revenue received by utilities from the sale of such ZECs should be refunded to utility customers.

IIEC recognizes that under Section 16-111.5(e)(2) of the Illinois Public Utilities Act, (220 ILCS 5/16-111.5(e)(2)) the procurement administrator is to develop and provide standard contract forms for the supplier contracts in conjunction with the utilities, the Commission, and other interested parties. Therefore, IIEC has not proposed any modification of the Plan to reflect this recommendation, but takes this opportunity to advise the IPA and other parties of its concern.

**Conclusion**

IIEC recognizes the considerable effort associated with the Plan development and appreciates the IPA's work in developing same. IIEC's comments are intended to help ensure the IPA considers all of the relevant information and submits a plan to the Commission that will allow the acquisition of zero emission credits with the least economic burden on consumers as is allowed by law.

To the extent you have questions or would like to discuss any of the comments, please feel free to contact Eric Robertson, Lueders, Robertson & Konzen, 1939 Delmar Avenue, P. O. Box 735, Granite City, Illinois, 62040 (618-876-8500) erobertson@lrklaw.com or Robert Stephens, Brubaker & Associates, 16690 Swingley Ridge, Suite 140, Chesterfield, Missouri, 63017 (636-898-6725) bstephens@consultbai.com.

Very truly yours,

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Illinois Industrial Energy Consumers

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### 5.3.1 Risk-Based Multiplier

Zero emission facilities operating in competitive electricity markets, such as in Illinois, compete on a merchant basis where the facility's revenues are subject to commodity price fluctuations and supply/demand dynamics. Alternatively, facilities that are able to recover their costs through State regulated rates are less exposed to the risks associated with competitive market conditions. Rate- based facilities do not rely on market prices to cover the costs of operation and provide a regulated return on investment to their owners. These facilities can rely on regulatory processes to adjust rates to ensure that return on investment. With greater exposure to fluctuating market conditions, merchant facilities have a greater risk of early retirement brought about by economic stress than facilities with rate-based cost recovery.[120]

Nuclear generating unit closures or planned retirements prior to the expiration of the unit's NRC operating license are driven primarily by one or a combination of the following factors: adverse market conditions, state policy decisions such as agreements with political or regulatory authorities, or structural and mechanical problems such as steam generator failures. For example, the Crystal River 3 unit in Florida, and the San Onofre 2 and 3 units in California are examples of plants where structural and mechanical problems led to their closure because of the prohibitive cost that would have been required for repairs. The planned retirements of Indian Point 2 and 3 in New York as well as Diablo Canyon 1 and 2 in California reflect a combination of adverse market conditions and State policy decisions.

Since 2013, six nuclear generating units have been retired, three of these units were closed due to structural and mechanical reasons as described above, and three units were closed due to adverse market conditions. Of the units that retired due to adverse market conditions, Kewaunee in Wisconsin and Vermont Yankee in Vermont were operating in competitive markets, while the small single-unit Fort Calhoun in Nebraska was operated by a public power agency.[121] As of the second quarter of 2017, the owners/operators of 19 units have announced plans to close or have indicated that their units are in danger of retiring prematurely because they are losing money.[122] All of these units with the exception of Diablo Canyon 1 and 2 are merchant facilities operating in competitive markets.

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[120] See: Congressional Research Service, "Financial Challenges of Operating Nuclear Power Plants in the United States," R44715, December 14, 2016. Haratyk, Geoffrey, "Early Nuclear Retirements in Deregulated U.S. Markets: Causes, Implications and policy Options," MIT Center for Energy and Environmental Policy Research, Working Paper Series, CEEPR WP 2017-009, March 2017.

[121] Nuclear Energy Institute, "Nuclear Costs in Context," April 2017.

[122] These units are: Fitzpatrick, Clinton, Quad Cities 1 and 2, Pilgrim, Oyster Creek, Diablo Canyon 1 and 2, Three Mile Island 1, Indian Point 2 and 3, Nine Mile Point 1 and 2, Ginna, Palisades, Perry, Davis Besse, and Beaver Valley 1 and 2.

Also, the zero emission facilities with bilateral contracts for all or part of their capacity or energy output are less risky and have less economic stress than such facilities without bilateral contracts. In developing and applying the risk based multiplier and the economic stress multiplier, it is important to know if the zero emission facility bidding into the procurement process has any such contract and what the terms are. Therefore, zero emission facilities wishing to bid into the auction will be required to inform the Agency of the existence of any bilateral contracts involving the zero emission facility's capacity and/or energy output and to furnish copies of such contracts to the Agency for proper determination and application of the risk-based and economic stress multipliers.

A key bid scoring consideration in the Act involves maintaining the environmental attributes of existing zero emission facilities through the procurement of ZECs: "In particular, the selection of winning bids shall take into account the incremental environmental benefits resulting from the procurement, such as any existing environmental benefits that are preserved by the procurements held under this amendatory Act of the 99th General Assembly and would cease to exist if the procurements were not held, including the preservation of zero emission facilities."[123]

In order to reflect the lesser risks that zero emission facilities with rate-based cost recovery opportunities are exposed to as compared with zero emission facilities that are operated on a merchant basis, the Agency will incorporate a rate-based risk multiplier into the process for selecting successful bids. To ensure that this reflection of risk is significant without being entirely determinative (as the Zero Emission Standard does not prohibit facilities with costs recovered through rates from participating, as the Renewable Portfolio Standard does in Section 1-75(c)(1)(J)), a multiplier of 0.5 will be applied to the bid scores of facilities with rate-based cost recovery, while a multiplier of 1.0 (i.e., no discount to the environmental benefits at all) will be applied to the bid scores of merchant zero emission facilities.[124] For this draft Plan, the IPA would be interested in receiving comment on whether this multiplier level is appropriate in discounting the risk of closure faced by rate-based facilities, or if there is a sound, well-supported basis for the use of a different multiplier level.

### 5.3.2 Economic Stress Multiplier

In addition to whether a facility's costs are recovered through rates, the degree to which a zero emission facility may be at risk of closure due to economic and market conditions can be measured through the facility's operating costs measured against an average baseline. If a facility has a particularly high cost structure, it should have a higher level of economic stress. If a facility is able to produce electricity at a lower cost, then it is presumably facing reduced economic stress and at less risk of closure.

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[123] 20 ILCS 3855/1-75(d-5)(1)(C).

[124] As part of the submission of eligibility information, bidders will be required to certify the status of each zero emission facility as either a) a merchant facility or b) a facility that recovers its costs through regulated rates. In the case of a facility owned by more than one entity, to maintain consistency with the statutory directive that "if the zero emission facility is owned by more than one entity, then the quantity of zero emission credits to be procured under the contracts shall be the amount of zero emission credits that are generated from the portion of the zero emission facility that is owned by the winning supplier," this certification shall be based on that individual bidder's "portion of the zero emission facility" owned by it. (20 ILCS 3855/1-75(d-5)(1)).

To capture this dynamic, the IPA's proposes the use of an economic stress multiplier ("ESM"), which works to determine whether a given facility faces economic stress greater or lesser than a baseline market rate. The ESM reflects the general condition that zero emission facilities with higher operating costs, as defined above, are more likely to face economic stress and potential closure than facilities with lower operating costs.[125]

The ESM is calculated as follows: to maintain consistency with other information found in the statute, the ESM is calculated through the ratio of the zero emission facility's operating costs divided by the Base Market Price Index of $31.40/MWh. The zero emission facility operating costs utilized to determine the ESM would be the sum of the fuel expenses, operating & maintenance expenses and the capital expenses necessary to maintain operation of the facility as reported through the final facility eligibility information form, which is provided in draft format as Appendix F.[126] For purposes of making this determination, operating cost data will be taken from the eligibility information that each zero emission facility interested in submitting a bid is required to submit to the IPA (thus maintaining additional consistency with information expressly required to be submitted in the statute).[127] As this information will be certified by the bidder for accuracy and will be subject to additional review and verification by the Agency and the Procurement Administrator, the IPA is confident that this information will be sufficiently accurate for determining a bid score multiplier. For this draft Plan, the IPA would be interested receiving comments on whether a comparison of operating costs to a statutorily referenced baseline market price index is appropriate for establishing an economic stress multiplier, or if there is a sound, well-supported basis for the use of different information, such as a local or regional cost baseline for a given facility—and if so, what information should be used?

[125] Congressional Research Service, "Financial Challenges of Operating Nuclear Power Plants in the United States," December 14, 2016.

[126] The zero emission facility costs as used in the ESM are defined by the Nuclear Energy Institute as shown in the whitepaper "Nuclear Costs in Context" updated April 2017. The ESM is determined based on the fuel costs, O&M costs and sustaining capital costs selected from the eligibility information supplied by the potential bidders to be consistent with industry cost analysis approach presented in the NEI whitepaper.

[127] See 20 ILCS 3855/1-75(d-5)(1)(A)(iii).