STATE OF ILLINOIS
ILLINOIS POWER AGENCY

COMMENTS OF THE ENVIRONMENTAL LAW & POLICY CENTER, THE NATURAL RESOURCES DEFENSE COUNCIL, AND VOTE SOLAR ON THE REQUEST FOR STAKEHOLDER COMMENT ON THE INDEPENDENT REC PRICING REVIEW AND THE ILLINOIS ABP AND ILSFA REC PRICING POLICY DESIGN ISSUES, OPTIONS, AND IMPLICATIONS

March 28, 2023

The Environmental Law and Policy Center ("ELPC"), the Natural Resources Defense Council ("NRDC"), and Vote Solar commenting jointly as the Joint Non-Governmental Organizations ("Joint NGO"), appreciate the opportunity to provide comments to the Illinois Power Agency ("IPA" or "Agency") in response to the March 7, 2023, *Independent REC Pricing Review: Request for Written Comments from Stakeholders*.

The Request for Written Comments from Stakeholders from Sustainable Energy Advantage, LLC ("SEA") lists 13 questions on two different documents prepared by SEA on the current REC pricing policy of the Illinois Power Agency ("IPA") and key Inflation Reduction Act ("IRA") changes that will impact the Adjustable Block Program ("ABP") and the Illinois Solar for All ("ILSFA") program:

- *Illinois ABP and ILSFA REC Pricing Policy Design Issues, Options, and Implications* (hereafter the "Policy Design" document); and
- *Key Inflation Reduction Act (IRA) Changes Relevant to ABP and SFA Eligible Projects* (hereafter referred to as the "Key Changes" document).

The IPA's decision to engage an independent expert consultant to evaluate the REC Pricing Model prior to the release of the 2024 Long-Term Plan reflects the Agency's dedication to maintaining a relevant, accurate, and effective model that supports renewable energy development in Illinois. The Joint NGO expect that this effort will play a crucial role in shaping the development of REC prices for future years, governed by subsequent Plans.

The IPA's anticipation of utilizing the consultant's recommendations for adjusting REC prices in the 2024-2025 and 2025-2026 delivery years demonstrates the Agency's ongoing commitment to refining and enhancing the REC Pricing Model. This proactive approach ensures that the model remains current and adaptable to evolving market conditions and advancements within the renewable energy sector, ultimately contributing to the achievement of the state's goals.

The Joint NGO would like to express our gratitude to the IPA for providing the opportunity to comment on these important matters. We look forward to collaborating and offering our insights as we collectively work on the next Long-Term Renewable Resources Procurement Plan (LTRRPP) in the upcoming docket. Our continued partnership will help ensure the development and implementation of effective and sustainable renewable energy policies for the benefit of Illinois and its residents.

Section I: REC Pricing Policy Design Issues, Options, and Implications

Question 1. "Near Term Policy Options" described on slide 32.

a. SEA recommends continuing to use the cost-based modeling approach (and the CREST model) to set REC prices. Taking the full range of SEA recommendations into account, do you have a specific, quantifiable, alternative that balances market adoption and ratepayer cost?

b. SEA recommends a component-specific Net Metering (NM) Credit forecast. Should the IPA forecast PV NM credits rather than use a fixed percentage annual increase? Why or why not?

c. If the IPA pursues a component-specific NM Credit forecast, please comment on the indices you believe should apply to each NM Credit component.

d. Should the IPA pursue a year-to-year price adjustment of REC prices based on prior year block uptake, utilizing the method described in slide 29, or pursue a different approach? If different, please be specific enough that your recommendations are actionable.

e. Should IPA pursue the intra-year price adjustment as described in slide 31? If an alternate approach is preferred, please describe in enough detail that your recommendations are actionable.

f. Please comment on the REC price adjustment thresholds described and recommended on Slides 30 and 31 regarding year-to-year and intra-year adjustments, respectively.

Response to Question 1(a):

For several years, the Joint NGO have advocated for adopting an approach to REC prices that is more responsive to market signals sent by the most important signal of all, whether each category of statutorily required capacity is over- or under-subscribed relative to the amount of capacity.

In the docket on the last Long-Term Renewable Resources Procurement Plan, the Joint NGO made two recommendations to address the potential under-procurement of RECs in certain categories and to improve the IPA's ability to identify and respond to market signals. These recommendations can be beneficial for the overall efficiency and effectiveness of the Adjustable Block Program.

1. Adjusting the REC pricing model: If full block capacity is not expected to be procured at proposed prices or if REC prices have not led to full procurement in the most recent blocks, the Joint NGO recommended that the IPA adjust the REC pricing model for those specific categories. This adjustment would help to ensure that REC prices remain competitive and in line with market conditions, ultimately supporting the growth of the renewable energy market in Illinois.

2. Investigating and developing analytical tools: The Joint NGO suggests that the IPA should investigate and develop analytical tools for identifying and quantifying market signals. This would allow the IPA to better diagnose the causes of under-procurement and predict price responses needed to address the issue. By refining its analytical capabilities, the IPA can more effectively respond to market fluctuations and ensure the Adjustable Block Program meets its intended goals.

In developing its recommendations, SEA began with two important observations:

- Effective and durable program design starts with a clear articulation of the intended outcome, and
- Overall, the policy objective is to meet RPS targets with eligible resources.[1]

SEA reviews the characteristics of effective RE incentive programs and correctly observes that both the ABP and ILSFA program have a fairly prescriptive design in the statute that prioritize "one or more specific market segments, or with multi-faceted objectives related to technology, project type, and project size categories, tend to establish more prescriptive designs such as standard offer incentives intended to provide the predictability necessary to attract market participants and grow targeted market segments."[2]

SEA's analysis focuses on the difference between cost-based and value-based approaches to incentive modeling. SEA discusses two approaches to cost-based incentive modeling approaches: discounted cash flow (DCF) and recovery factor analyses. The cost based approach relies on the concept of a 'representative project' -- the hypothetical project for which the all-in cost of energy represents a value within a specified percentile range for a specified category installed during a specified period of time.

As a result of its analysis, SEA recommends continuation of the cost-based approach, specifically discounted cash flow analysis using the CREST model for "Initial REC Price-Setting."[3] They also recommend continuing to reset the cost-based benchmark annually.

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[1] Policy Design Document, slide 13
[2] Policy Design Document, slide 14
[3] Policy Design Document, slide 25

In light of the year-to-year adjustments proposed by SEA and discussed below, the Joint NGO do not object to the continued use of the cost-based approach for initial price setting and for annual benchmarking. However, it should be clear that in the event of a conflict between the conclusions that would be drawn from year-to-year adjustments and the cost-based modeling, the year-to-year adjustments should prevail.

Response to Questions 1(b) and (c):

SEA recommends that as part of the annual cost based approach, the IPA should use a component-based forecast for the Net Metering Credit (for each utility and applicable rate class) and their current values and then calculate the NM Credit starting point as an average of prior NM credit rates. Further, they recommend forecasting the NM credit with component-specific indices.[4] The cost components for C&I customers are:

- Energy Charge ($/kWh)
- Transmission Charge ($/kWh)
- Capacity Charge ($/kWh)
- Energy Transition Assistance Charge ($/kWh)
- Energy Efficiency Adjustment ($/kWh)
- Zero Emission Adjustment ($/kWh)
- Renewable Energy Adjustment ($/kWh)
- Environmental Cost Recovery Adjustment ($/kWh)

The cost components for residential customers are different because residential customers receive a distribution facilities credit:

- Energy Charge ($/kWh)
- Transmission Charge ($/kWh)
- Distribution Facility Charge ($/kWh)
- Energy Transition Assistance Charge ($/kWh)
- Energy Efficiency Adjustment ($/kWh)
- Zero Emission Adjustment ($/kWh)
- Renewable Energy Adjustment ($/kWh)
- Environmental Cost Recovery Adjustment ($/kWh)

Currently, the Net Metering Credit is escalated by a set inflation rate for all components (for example in the 2023-2024 Delivery year model, the Inflation Rate is set at 1.00% in the Net Metering Credit tab).

[4] Policy Design Document, slide 32

Presumably, SEA's recommendation is to set a different inflation index for each component based on the characteristics of that component. For example, the Energy Charge has been remarkably stable for the decade prior to 2021, even declining in certain years, while the Distribution Facilities Charges have increased at a steady rate.

In response to SEA's recommendation for a component-specific Net Metering (NM) Credit forecast, we believe that the current REC pricing model is sufficiently robust to provide a good estimate of the approximate value of a hypothetical project. The model already incorporates a number of assumptions and uncertainties, and adding another layer of complexity, such as forecasting component-specific NM credits, might create a false precision.

While forecasting PV NM credits could potentially add nuance to the model, it is important to weigh the benefits against the increased complexity and potential inaccuracies that may arise from additional forecasting variables. The existing model already provides a solid foundation for estimating project values, and maintaining its simplicity can help stakeholders better understand the underlying factors driving REC prices.

Thus, the Joint NGO recommend maintaining the current approach of using a fixed percentage annual increase, as it strikes a balance between accuracy and simplicity, ensuring the REC pricing model remains accessible and functional for its intended purpose.

Response to Questions 1(d), (e), and (f):

On Slides 29 and 30, SEA presents options for post-calculation of year-to-year pricing adjustments. The first option is an adjustment of prices on a year-to-year basis. Under Option 1, subsequent program year revenue requirements for affected categories would be administratively adjusted based on block uptake in prior program year. Under Option 2, the post-processing update would be calculated as a % of the REC price and not as a percentage of the total revenue requirement. Put differently, both options would adjust the REC price, but Option 1 would do so indirectly, while under Option 2, the IPA would simply make a percentage adjustment to the REC price directly based on the over- or under-subscription.

The Joint NGO strongly support post-modeling adjustments on a year-to-year basis based on prior year block uptake, as described in slide 29. This suggestion aligns with our concerns about responding to market signals and ensuring that the REC pricing model remains adaptive to changing conditions in the renewable energy market.

By considering prior year block uptake in the pricing adjustment process, the IPA would be able to tailor REC prices to actual market conditions better and promote balanced and sustainable growth of renewable energy projects in Illinois. This approach helps address potential issues of

under-procurement or oversupply and supports the state's renewable energy goals more effectively.

The Joint NGO believe that Option 2 would be a simpler and more predictable approach for post-calculation of year-to-year pricing adjustments. By directly adjusting the Renewable Energy Credit (REC) price as a percentage based on over- or under-subscription, Option 2 offers a clear, straightforward method for making adjustments. This transparency allows stakeholders, developers, and customers to anticipate pricing changes better and adjust their plans accordingly. In contrast, Option 1 involves an administrative adjustment to subsequent program year revenue requirements based on block uptake, which could be more complex and challenging to predict.

Question 2. "Long Term Policy Options" described on slide 33. (Note: If legislative amendments or additions are required to implement a particular option, such options will not be included in the next long-term plan.)

a. *Based on your experience with project financing and operation, please comment on the advantages and disadvantages of a "strike price"-based approach in the context of the ABP and ILSFA programs.*

Response to Question 2:

The Joint NGO acknowledges the intent behind the proposal to implement an indexed REC approach for the Adjustable Block Program; however, we find this approach to be extremely complicated for customers. The complexity associated with calculating and adjusting the REC prices based on market factors, such as the net metering credit and LCOE, might create confusion and uncertainty for customers seeking to participate in the program.

Additionally, the Joint NGO would be concerned about the risks to the renewable energy budget and the program from implementing indexed RECS. We have been extremely concerned about the budget impacts of the utility-scale indexed REC procurements. This could undermine the primary objective of procuring renewable energy at the least cost to ratepayers and negatively impact the overall success of the renewable energy programs in Illinois. The Joint NGO suggests that a simpler, more transparent, and predictable approach would better align with the interests of customers, developers, and ratepayers.

Question 3. The ILSFA recommendations described on slide 34.

a. Please comment on the recommendations presented in Slide 34.

b. In addition, what other ILSFA program changes do stakeholders recommend for consideration for the 2024-25 plan period?

Response to Question 3:

In general, the Joint NGO support the recommendations vis-a-vis the Illinois Solar for All. SEA's recommendations provide a solid foundation for maintaining consistent REC pricing strategies and addressing under-participation in the program, particularly among low- and moderate-income (LMI) customers. However, our concerns about over-reliance on the cost-based model approach relative to the ABP also pertain to ILSFA.

The Joint NGO recommend that the IPA should also adopt the year-to-year adjustments as proposed for the ABP. Integrating this approach would help to align both the ILSFA and ABP programs further, providing a more cohesive strategy for REC pricing and incentivizing renewable energy adoption in Illinois. Annual adjustments would also allow for more flexibility in responding to changes in the market and addressing any potential barriers to the adoption of renewable energy.

In addition to the recommendations from SEA, adopting year-to-year adjustments for REC prices in the ILSFA program would enable the IPA to make data-driven decisions based on market trends and the effectiveness of incentives. This approach would provide a more dynamic method for addressing the unique challenges faced by LMI customers and ensuring that the program remains accessible and beneficial for all Illinois residents.

Question 4. Data Collection

a. SEA recommends IPA begin to collect actual cost and performance data from all operating ABP and ILSFA projects. It may be appropriate to broaden this recommendation to include a detailed dialogue (among stakeholders, IPA, and its consultants) regarding the inputs to the annual CREST modeling. Such a dialogue would enable stakeholder participation in topics including (but not limited to):

i. Project installed cost (and associated target cost percentile)
ii. Risk-adjusted equity return target (by category), and
iii. Operating expenses.

Please comment on the advantages and disadvantages of expanding the stakeholder process to include discussion of these topics on an annual basis.

b. Are there any other important program elements not discussed herein that you believe should be considered? If yes, please describe in detail.

Response to Question 4:

The supplemental data collection requirements proposed by SEA offer several benefits that will enhance the renewable energy market in Illinois. Firstly, these requirements will provide additional transparency that improves decision-making by market participants. By having access to accurate and comprehensive project cost and performance data, market participants can make more informed decisions when developing or investing in renewable energy projects. This

transparency enables stakeholders to better understand the financial implications of their choices, leading to more efficient allocation of resources and ultimately contributing to a healthier and more robust renewable energy market.

Secondly, the data collected from these requirements will improve the accuracy of future cost-based modeling. As the IPA continues to refine its incentive programs, having access to reliable and detailed project data becomes crucial for developing accurate models that reflect the unique characteristics of the Illinois market. Improved cost-based modeling will enable the IPA to create better-targeted incentives, which will maximize the effectiveness of their programs and ensure that state renewable energy goals are met as efficiently as possible.

Lastly, the supplemental data collection requirements will provide policy makers with important information for monitoring the progress and effectiveness of current and proposed programs. By collecting project-specific data, policy makers can gain valuable insights into the performance of existing renewable energy programs, identify areas of success or underperformance, and adjust policies as needed to achieve desired outcomes. This iterative approach to policy development allows for the continuous improvement of renewable energy programs, fostering a more adaptable and responsive regulatory environment that supports the growth and long-term success of the renewable energy market in Illinois.

Section II: Inflation Reduction Act (IRA) Changes Relevant to ABP and SFA-Eligible Projects

Question 5. Should the IPA adopt the "IRA Modeling Implications for ABP Program Categories" described on slides 11-19 of the IRA presentation?

Question 6. Should the IPA adopt the "IRA Modeling Implications for Solar For All Program Categories" described on slides 20-28 of the IRA presentation?

Response to Questions 5 and 6:

On slide 11-19, SEA identifies how different provisions of the IRA might impact different categories of the ABP. Slides 20-28 identify how different provisions of the IRA might impact different categories of ILSFA. The Joint NGO respond that that the Inflation Reduction Act (IRA) has introduced a number of new variables that must be considered when evaluating the financial returns of renewable energy projects. This added complexity can make it more challenging to develop a financial model for a representative project and may reduce the effectiveness of the cost-based approach currently used in setting REC prices.

Additionally, it is crucial to note that stakeholders (e.g., customers, developers, and policy-makers) are still awaiting guidance from the Internal Revenue Service (IRS) on various aspects

of the eligibility for certain tax incentives included in the IRA. This includes clarification on the eligibility criteria for participation in the domestic content and energy communities bonus tax credits. The lack of clear guidance on these tax incentives further exacerbates the uncertainty inherent in cost-based modeling and highlights the importance of the Joint NGO's recommendation to adjust REC prices based on actual market response.

Question 7. Should the IPA establish REC adders for IRA bonus credit-eligible projects that may or may not align with certain public policy priorities, if claiming such bonus credits results in projects with higher REC prices than those that do not claim the credit? For examples of potential projects that could fit this description, please see slide 30 of the IRA presentation.

Question 8. Conversely, should the IPA adjust REC prices <u>downward</u> for ABP and SFA projects eligible for IRA bonus credits if claiming such bonus credits costs less than a project that is not eligible for such credits? For examples of potential projects that could fit this description, please see slide 31 of the IRA presentation.

Response to Questions 7 and 8:

The policy underlying the creation of the Illinois Solar for All program in 2016 and the new categories of projects in the Adjustable Block Program in 2022 is to spur the development of certain policy priorities within the broader context of increasing adoption of all types of distributed generation. Likewise, the introduction of bonus tax credits for projects in energy communities, for meeting domestic content requirements, and for projects meeting certain low-income benefit eligibility requirements in the Inflation Reduction Act is intended to advance identified policy priorities.

The federal policy goals embedded in the bonus credits are well aligned with the goals of CEJA and the state of Illinois. As such, the Joint NGO do not support the IPA adjusting REC prices either upward (as posed in Question 7) or downward (as posed in Question 8) in response to the introduction of the bonus tax credits. By adjusting REC prices to offset the benefit of the bonus credits to equalize the expected return for qualifying projects with the expected return for non-qualifying projects, the IPA would effectively countervail the benefit of the bonus credits, thus undermining the policy intent of introducing the credits.

Question 9. Does the cost of claiming elective payment in cash of federal investment credits (a practice known more informally as "direct pay") increase prices by more than 25% (the statutory threshold for a Treasury waiver) If so, how should the IPA and its planning consultant approach the task of quantitatively benchmarking the differential for differing project blocks?

Response to Question 9:

In response to the question regarding the potential impact of claiming elective payment in cash of federal investment credits (also known as "direct pay") on project prices, it is important to acknowledge that this is a tax-related question. The JNGO do not possess the expertise to provide specific insight into how developers and customers will handle tax questions, including the potential increase in prices due to the direct pay option and its relation to the 25% statutory threshold for a Treasury waiver.

Given the specialized nature of tax-related matters, the Joint NGO hope that this Request for Stakeholder Feedback will generate responses from qualified tax experts who possess the necessary knowledge and experience to provide guidance on these issues. This approach will ensure that any decisions or recommendations made regarding the potential impact of direct pay on project prices are well-informed and accurately account for the complexities and nuances of tax-related matters.

Additionally, we continue to suggest that the IPA and its planning consultant make appropriate simplifications in their approach that would be applicable to the broadest set of potential participants in each category. By doing so, the IPA can develop a more comprehensive understanding of the implications of direct pay on project prices and determine the most appropriate course of action for addressing this issue in the context of the Adjustable Block Program and the Illinois Solar for All program. This inclusive approach will help ensure that the various interests and needs of the different stakeholders are taken into account when making policy decisions related to the REC pricing model and other aspects of these programs.

Question 10. Is it reasonable to assume that direct pay recipients could also claim the cost of interconnection property in the basis for receiving ITC or the Clean Energy Investment Credit (CEIC)?

Response to Question 10:

See response to Question 9.

Question 11. Should there be a separate REC price (or REC adder) for direct pay eligible ABP Community-Driven Community Solar projects?

Question 12. Should there be a separate REC price for SFA Non-Profit projects owned by host customers vs. Public Facilities projects owned by host customers (since public entities can get municipal bond financing, and nonprofits cannot)?

Response to Questions 11 and 12:

The Joint NGO acknowledge the potential differences in project types within the Illinois Solar for All (ILSFA) program. However, we do not believe it is in the best interests of the program to further fragment the project categories by creating separate REC prices or adders for specific project variations. Doing so could introduce additional complexity and administrative burden to the program, which may not necessarily result in improved outcomes.

That being said, we are open to the possibility of implementing separate REC prices or adders for specific project types if feedback from prospective program participants indicates that they would be disadvantaged by not having REC prices modeled to accommodate their specific projects. In such cases, the IPA should take into consideration the unique challenges and financial requirements of these projects when determining REC pricing.

It is essential that the IPA maintains a balance between addressing the specific needs of different project types and ensuring the overall efficiency and effectiveness of the ILSFA program. By carefully considering the feedback from stakeholders and conducting a thorough assessment of the potential benefits and drawbacks of creating separate REC prices or adders for specific project types, the IPA can make informed decisions that best serve the interests of both the program and its participants.

Question 13. Are there other REC prices that you believe should change to account for the expected approval of rules allowing direct pay?

Response to Question 13

The Joint NGO have no response to this question at this time.