To: Analysis Group Inc. ("AGI")
Burns & McDonnell ("BMCD")
New York Independent System Operator, Inc. ("NYISO")

From: Ron Paryl, Director, Markets and Risk Management

Date: July 1, 2020

Re: Comments on Analysis Group Financing Assumptions of Reference unit for Installed Capacity Demand Curve Parameters.

Cricket Valley Energy Center, LLC (CVEC) is one of the most recently financed gas fired generators in the NYISO and has had in-depth experience in financing multiple gas fired assets in NYISO and PJM. Based on our experience in financing gas fired projects in NYISO and recent discussions with multiple equity advisors and lenders with whom Advanced Power, as the Cricket Valley asset manager, has relationships, we do not believe that the financing assumptions that Analysis Group is using for the Gross CONE are credible or reflect the risk premiums that are being demanded by both equity and debt to invest in generation facilities in the NYISO market.

1. **The Analysis Group ROE assumption of 13% is too low**

Over the last 4 years, the risks to equity investors in gas fired generation in NYISO have increased substantially, which should increase the ROE from the last DCR. Issues that investors in gas fired generation are concerned with include (i) subsidized generation competing with unsubsizided gas fired generation and suppressing capacity and energy prices, (ii) CLCPA inducing further state subsidized resources as well as prematurely terminating the useful life of gas fired assets, (iii) uncertainty over NY CO2 pricing policy, (iv) recent bankruptcies in the NYISO market of gas fired generation (Empire / Athens) and (v) construction of ratepayer funded transmission facilities that will suppress capacity and energy prices in NYISO markets.

Feedback that we received from equity advisors is that investors considering investing in NYISO gas fired generating assets without hedges are seeking an ROE in the 15-17% range to compensate for the significant risks associated with investing in a gas fired generating asset in NYISO. A well hedged asset in NYISO may acquire equity in the 13-15% range.

2. **Debt/Equity ratio and cost of debt is too aggressive**

To achieve the debt / equity ratio of 55/45 that Analysis Group is proposing is aggressive without including the costs of significant hedges that a new gas fired unit would require for construction financing. Construction financing is commonly financed with a construction + 5 year term loan

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that utilizes a hedge instrument to provide contracted cash flows to ensure debt service coverage for the first 5 years of operations. These hedges are usually in the form of a revenue put or heat rate call option (HRCO). In the case of a revenue put, a significant upfront premium payment at financial close is required to secure the hedge. For a HRCO, an upfront payment is not required, but significant financial security in the form of Letters of Credit (L/C) is required as a carrying cost on the unit being financed as well as and reduction in Net E&AS due to long term hedge discount to market. As the reference unit is a peaking unit, it may also seek to secure a capacity hedge, but this would also require significant credit support in the form of L/Cs to secure this hedge.

Feedback that we received from the infrastructure lenders was that a 55/45 debt to equity ratio would not be achievable without significant hedging to provide debt service coverage. If the unit was unhedged, we were advised that an LHV or ROS unit would be likely only be allowed 40% leverage and would have debt priced around 8%. An unhedged Zone J asset would only be recommended to leverage to 50% debt.

The lenders that we spoke with also noted that they will continue to pressure leverage ratios down on gas fired assets in the future as the amortization period shrinks due to the CLCPA's premature closure of these assets in 2040. The reduction in duration for full loan repayment is forcing lenders to be much more cautious with leverage going forward for gas fired assets.

CVEC recommends, that if Analysis Group does not account for the significant costs associated with hedges to secure cash flow for the lenders, that a more conservative 50/50 debt to equity ratio be utilized for Zone J and a 40/60 debt to equity ratio be used for LHV and ROS with a higher interest rate of 8%. For Analysis Group to account for a hedge on the reference unit, we would recommend adding upfront costs of approximately $70/kW to account for the cost of a revenue put or similar hedge to provide downside margin protection to secure the financing.

3. **Not utilizing an SCR in the LHV reference unit is viewed negatively by equity investors and lenders**

Discussions on the topic of financing a peaker in LHV without an SCR was viewed negatively by equity advisors and lenders. The assumption that permitting might be achieved without an SCR by limiting run hours would need to be balanced with increased risks to returns and would need to have those risks reflected in a higher ROE and lower debt leverage compared to a unit with an SCR. We don't believe that given the current difficult permitting environment in New York that a gas fired peaker in LHV would ever be permitted by NY DEC.

Respectfully submitted