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PUBLIC SERVICE COMMISSION

November 14, 2008

Howard Schneider, Esq.  
Chairman, Board of Managers  
PJM Interconnection, L.L.C.  
955 Jefferson Avenue  
Norristown, PA 19403

Re: Energy Efficiency

Dear Mr. Schneider:

This letter is submitted on behalf of the Maryland Public Service Commission, the District of Columbia Public Service Commission, the Delaware Public Service Commission, the Kentucky Public Service Commission, the New Jersey Board of Public Utilities, and the West Virginia Public Service Commission.

We are writing to urge PJM to treat energy efficiency measures in the capacity market on an equal footing with other capacity resources, and not put this valuable component of the market at a disadvantage by compensating it for an unreasonably short period of time. The immediate reason for these comments is that on November 19 and 20 the Markets and Reliability Committee and Members Committee, respectively, will be presented with options in preparation for a December 15 filing at FERC. In the December 15 filing, PJM will propose RPM modifications for the May 2009 base residual auction for the 2012-2013 delivery year.

The above-named state commissions are responsible for implementing various aspects of energy policy and for ensuring just and reasonable rates for millions of customers. States are directly affected by all aspects of the wholesale market in general, and RPM in particular, because the retail prices which we regulate are virtually dictated by the energy and capacity prices resulting from PJM's market structure. Reliability is our highest priority and encouraging energy efficiency, which also reduces carbon and other emissions, is an important, cost-effective way to improve reliability.

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There is no debate that measured and verified energy efficiency provides essentially the same benefit as generation. With regard to compensating energy efficiency resources in the capacity market; therefore, when an appropriately measured and verified energy efficiency resource reduces peak demand, PJM should permit energy efficiency to be compensated in the capacity market in each year that the measure serves load and clears the auction, exactly as generators are compensated.

Critics sometimes characterize the practice of compensating energy efficiency for each year that the measure contributes to satisfying load as “double compensation.” This term is misleading; at worst, there may be incidental additional compensation depending on the specific cost allocation methodology selected.<sup>1</sup> However, there are those who would profit from undercompensating energy efficiency resources. For example, traditional generators have much to gain if PJM does not compensate energy efficiency on an equal playing field because this undercompensation limits the ability of energy efficiency resources to compete with traditional generation resources. The end result will be higher prices for customers due to additional capacity and higher energy prices, both of which could be reduced by energy efficiency.

As the Public Service Commissions of Maryland, the District of Columbia, and Delaware, and the New Jersey Board of Public Utilities explained in a more detailed letter to PJM on August 29, 2008 (<http://tinyurl.com/53ehbj>), the rules that PJM ultimately adopts should be designed to encourage and compensate energy efficiency. ISO New England Inc., as approved by the Federal Energy Regulatory Commission, has implemented procedures in which energy efficiency measures may participate in the forward capacity market as long as the measure contributes to meeting load, as is the case for generators and other capacity resources.

We urge PJM to adopt functionally similar rules, including strong measurement and verification protocols, with the goal of making energy efficiency a lasting and meaningful contribution to reliability while simultaneously benefiting the environment (by definition, energy efficiency results in a reduction in carbon and other emissions). PJM is already making headway in developing a measurement and verification protocol based on New England’s procedures, and we applaud this effort. Permitting energy efficiency to participate fairly and equally in the competitive capacity market alongside generation is an outcome that would be highly beneficial and in the spirit of the markets PJM is charged with operating. Adoption of the one-year proposal is highly objectionable and vigorously opposed by the undersigned.

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<sup>1</sup> The fallacy of this argument is illustrated by an example in which load providers, such as electric distribution companies, would turn down the opportunity to reduce their capacity bill from \$150/MW-day to \$143/MW-day because customers who installed energy efficiency measures may pay \$142/MW-day. This saving of \$1/MW-day to those who make energy efficiency improvements is a modest incentive for lowering the overall capacity bill from \$150/MW-day to \$143/MW-day. The \$7/MW-day benefit that would accrue to all customers through the competitive effect on RPM clearing prices associated with aggressive deployment of energy efficiency, along with reduced energy prices from lower demand, amply justifies this small, additional compensation, which would be subject to strict measurement and verification to ensure that the energy efficiency measure delivers the promised energy reductions.

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PJM needs to recognize the true value that energy efficiency brings to the capacity market by drafting a rule that enables energy efficiency to be compensated, subject to rigorous measurement and verification, in each year that the resource brings capacity to the market. Thank you for your attention to this important issue.

Sincerely,

/s/ Arnetta McRae

Chair Arnetta McRae

Delaware Public Service Commission

/s/ Agnes Alexander Yates

Chairperson Agnes Alexander Yates

District of Columbia Public Service Commission

/s/ David Armstrong

Chairman David Armstrong

Kentucky Public Service Commission

/s/ Douglas Nazarian

Chairman Douglas Nazarian

Maryland Public Service Commission

/s/ Jeanne M. Fox

President Jeanne M. Fox

New Jersey Board of Public Utilities

/s/ Michael A. Albert

Chairman Michael A. Albert

Public Service Commission of West Virginia

cc: PJM Board of Managers

Terry Boston, CEO & President, PJM

Andy Ott, Sr. VP – Markets, PJM

Bill Whitehead, VP, State Govt. Policy, PJM