

December 2, 2008

Howard Schneider, Esq.
Chairman, Board of Managers
PJM Interconnection, L.L.C.
955 Jefferson Avenue
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via facsimile and e-mail

Re: Integrating Energy Efficiency into Capacity Markets

Dear Mr. Schneider:

This letter is submitted on behalf of Consolidated Edison Solutions, Inc. (CES) and Consolidated Edison Energy, Inc. (CEE) to clarify the issues raised in the November 14, 2008 letter from six utility commission Chairs / Presidents and to request that PJM consider an equitable approach for integrating energy efficiency into the PJM capacity markets.

First and foremost, CES and CEE support efforts to integrate energy efficiency into the PJM capacity markets and have been active participants in the PJM stakeholder process to accomplish this goal. Collectively, CES and CEE serve several thousand MW of load within PJM without owning any generating assets. In addition, CES provides commercial and industrial customers with various “behind the meter” services including the design and installation of energy-efficiency equipment and control strategies. While our business interests are “load” oriented, we differ from some market participants in that we believe energy efficiency’s participation in the wholesale markets should be on an equal rather than a subsidized basis.

CES and CEE have significant concerns with the proposal advanced by PJM Staff to allow energy efficiency providers to qualify for four years of capacity payments because, after the initial year, the impact of the efficiency measures will be captured in the Peak Load Contribution (“PLC”) which is PJM’s mechanism for allocating capacity obligations to retail customers and their Load Serving Entity (“LSE”). The reduction in the PLC effectively doubles the value of the capacity payment to the energy efficiency provider in the second through fourth years and, because the zonal capacity obligations are predetermined for the full four year payment, would artificially increase the capacity obligation of other customers within that zone.

The potential for a multi-year payment to over-value energy was openly acknowledged by ISO-NE when it filed to incorporate energy efficiency into its capacity markets. However, ISO-NE decided that it would be too complicated to initially eliminate the double payment, and instead committed to evaluating a solution for possible implementation after three years:

“Without reconstitution of load, it is possible that the capacity value of [EE] Resources would be counted twice – once through a payment from the FCM and another through the reduced allocation of total capacity costs to the end-use consumers that installed the [EE] Resource... Because of the complexity of reconstituting load, the proposed rules do not include a provision implementing reconstitution. However, the rules state that ... beginning in February 2009, the ISO will evaluate, in consultation with its stakeholders, the need for a load reconstitution for Demand [and EE] Resources.”¹

¹ See p 167 of ISO-NE’s February 15, 2007 filing letter in docket ER07-546 et al.

During the stakeholder process, CES identified two options for energy efficiency participation in the PJM capacity markets that would not impose higher capacity obligations on other market participants:

- The first option, which received the most support (84 in favor, 40 opposed) at the October 10, 2008 Demand Response Steering Committee, would qualify energy efficiency for one year of capacity payments and, to capture the societal benefits until PJM's forecasting process recognized the load reduction, would decrement down the forecasted load and therefore the amount of capacity purchased in years two through four.
- The second option, which was never voted on², would allow the installation of energy efficiency measures to qualify for up to four years of capacity payments but would add back the impact of the energy efficiency measure for purposes of determining the retail customer's capacity obligation in years two through four. This "add back" approach, which mirrors PJM's existing rules for Demand Response providers, would allow a 10 MW customer installing 2 MW of energy efficiency to receive capacity payments for the 2 MW reduction provided their capacity obligation was calculated based on their original 10 MW peak load.

CES and CEE urge PJM to consider one of these two options in order to ensure that the integration of energy efficiency into the capacity markets does not artificially increase the capacity obligations and therefore impose additional costs on other customers. Since PJM's treatment of Demand Response has solved the "complexity of reconstituting load" that vexed ISO-NE, including an "add back" mechanism to the four year payment proposal would be appropriate.

Respectfully submitted,



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cc: Terry Boston, CEO & President, PJM
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Chairperson Agnes Alexander Yates, District of Columbia Public Service Commission
Chairman David Armstrong, Kentucky Public Service Commission
Chairman Douglas Nazarian, Maryland Public Service Commission
President Jeanne M. Fox, New Jersey Board of Public Utilities
Chairman Michael A. Albert, Public Service Commission of West Virginia

² CES did make a timely request to PJM Staff to have a sector weighted vote of the "add back" proposal at the November 19, 2008 Market and Reliability Committee ("MRC") but Staff did not include it as an agenda item. Nonetheless, CES made a brief presentation at the MRC outlining the issues and requested a formal vote but was not able to garner the 2/3 support necessary to hold such a vote.