

June 18, 2009

PJM Interconnection LLC  
Board of Managers  
955 Jefferson Ave  
Norristown, PA 19403

Re: PJM Economic Demand Response Program is Unjust and Unreasonable

Dear Board Members:

Demand Response Providers and Participating End Use Customers request that the Board acknowledge that the existing PJM Economic Demand Program is unjust and unreasonable and requests that the Board require PJM to redesign the mechanisms for Economic Demand Response to provide appropriate and non-discriminatory compensation for this critical resource, including full LMP compensation without an arbitrary sunset, and submit those revisions for approval by the Federal Energy Regulatory Commission.

The current basis for Demand Response DR compensation [LMP – (G+T)], is unjust and unreasonable as the PJM staff has explained in their straw DR compensation proposal.<sup>1</sup> Compensation for DR at less than LMP is also discriminatory in as much as Demand Resources in other PJM markets are paid the market clearing price for capacity and ancillary services whereas PJM currently pays less than the market clearing price to Demand Resources in the energy markets.

Furthermore, to ensure comparable, just and reasonable treatment of DR, compensation at full LMP is essential to overcome market barriers. The first major barrier is the PJM governance structure, which controls market rules and is dominated by traditional utilities and their affiliates who often vote generator interests in whatever sector they happen to vote in as part of PJM's flawed governance model. This leads to discriminatory rules for DR such as the compensation sunset that led to the serious diminution of demand side activity in PJM 2008. As noted elsewhere herein, there has been a dramatic fall off in DR participation in the energy markets. Unless those rules are fixed, the growth seen in the capacity markets will not be duplicated in the energy markets.

To the best of our knowledge no supply side compensation mechanism, such as RPM, has ever been expressly sunsetted in a comparable manner. Including sunset in PJM market rules creates a *per se* barrier to DR; it creates uncertainty about the sustainability of any business focused on demand side resources, which in turn can and does inhibit access to capital for demand side resource investment.

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<sup>1</sup> PJM Straw Proposal for Compensation Paid to Demand Resources Providing Demand Reductions in the Economic Load Response Program <http://www.pjm.com/committees-and-groups/committees/~media/committees-groups/committees/mc/20090604/20090604-item-04d-pjm-straw-proposal-pkg-1.ashx>

Customer response to peak period prices is seriously lacking today, and as the PJM Market Monitoring Unit has repeatedly noted, DR participation in PJM's energy markets is seriously underdeveloped. This results in an inefficient PJM energy market that is unjust and unreasonable. The load volumes that can respond to price, and are willing to do so under today's inadequate compensation mechanism, are simply too small to discipline the PJM energy market toward efficient pricing. The PJM Board can and must remedy unjust and unreasonable market rules that are leading to inefficient market outcomes. Customers should have adequate incentives to reduce consumption and demand when applicable generation rates are higher than customers want to pay for the service and, in its role of operating efficient wholesale markets, PJM should promote such customer action.

We believe that zonal LMP is the correct economic level of compensation for all customers regardless of whether they are fixed price or LMP rate based. . It reflects the value of an incremental MWH or a decremental MWH. The value of a MWH on the wholesale market is the same whether the MWH is generated by a nuclear unit, a coal unit, or by a reduction in load. Moreover, as PJM's experience has demonstrated, DR can reduce clearing prices to the benefit of customers, can result in avoiding the dispatch of less efficient generating units, can mitigate the concentration of generation ownership in the markets, enhances reliability and produces environmental benefits. Simply put, DR improves the competitiveness and efficiency of the markets. We note in this regard Mr. Ott's article in T&D World describing the beneficial impact of DR on PJM operations in August 2006.

While we appreciate PJM staff's laudable efforts to work toward a compromise on this matter, unfortunately its proposal is unfair to DR and will not address today's market design shortcomings. Unfortunately, today the entrenched interests that want to preserve barriers to demand response have enough influence to prevent progress through the stakeholder process.

PJM's staff's proposal was a good faith attempt to get a compromise in a stakeholder process that is stacked against demand side interests. We appreciate the effort, but must object to a number of its elements, especially the three year sunset on customer participation.

We urge the PJM Board to act to remedy the discriminatory and unjust treatment of DR in PJM's market. The stakeholder process has failed the market – it is now time for the PJM Board to act favorably toward removing barriers to demand response in PJM's energy market where the stakeholder process is unable and unwilling to do so. We respectfully urge the PJM Board to direct PJM staff to file an economic load response market rule change that includes full LMP compensation, recognition of LMP customer's contributions, and no unfair sunset provision.

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cc

Chairman Jon Wellinghoff, FERC

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