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March 29, 2011

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

**VIA FEDERAL EXPRESS**

**RE: *Ex Parte* Communication on PJM Staff Whitepaper on Price Responsive Demand**

Dear Mr. Schneider:

As the PJM Board of Managers considers the PJM Staff Whitepaper on Price Responsive Demand ("PRD"), PJM Industrial Customer Coalition ("PJMICC")<sup>1</sup> offers the following comments in broad support of the PRD proposal set forth in the PJM Staff Whitepaper. As discussed herein, PJMICC endorses the PRD concept and generally supports the PRD proposal as it has been refined in the PJM Staff Whitepaper, which allows nominated PRD amounts to be appropriately reflected as an offset to the load forecast. PJMICC encourages the Board to consider, however, certain tweaks to the PRD proposal to ensure it is meaningfully available to all customer segments in a non-discriminatory manner and conforms to the Federal Energy Regulatory Commission's ("Commission") Final Rule on Demand Response Compensation.<sup>2</sup>

We commend PJM for recognizing, in its role of independent market administrator, a need for its market rules to evolve to address changing conditions at the retail level.<sup>3</sup> PRD reflects a solid and constructive effort to better integrate the impact of customers' responses to changing electric

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<sup>1</sup> PJMICC is an *ad hoc* coalition consisting exclusively of large commercial and industrial end-users of electricity. PJMICC members operate manufacturing and institutional facilities throughout the expanded PJM footprint, which encompasses all or parts of Delaware, Illinois, Indiana, Kentucky, Maryland, Michigan, New Jersey, Ohio, Pennsylvania, Tennessee, Virginia, West Virginia, and the District of Columbia. PJMICC member companies consume approximately 10 billion kilowatt-hours of electricity annually. Several PJMICC members are currently also voting participants of the PJM Members Committee and actively participate in the PJM committee process.

<sup>2</sup> See *Demand Response Compensation in Organized Wholesale Energy Markets*, 134 FERC ¶ 61,187 (2011)(codified at 18 CFR Part 35)("Order No. 745").

<sup>3</sup> See generally PJM Staff Whitepaper on Price Responsive Demand, at 6 (Mar. 3, 2011)("PJM Whitepaper").

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prices and the costs of new market overlays in its operations and planning activities. While we may have some concerns about certain details of the PRD proposal, we support PJM going forward with this proposal with all due deliberate speed, developing the needed details and securing the required regulatory approvals.

As the Board is well aware, the PJM wholesale market is inexorably linked with retail markets.<sup>4</sup> Developments at the retail level, in both regulated and restructured states, are changing the way customers purchase and consume electricity that PJM cannot ignore. While recognizing PJM's mission as set forth in the PJM's Operating Agreement,<sup>5</sup> it must not be forgotten that the wholesale electricity grid and markets PJM plans and operates ultimately exist to provide reliable electricity service to retail customers. If PJM planning and market operations do not reflect activity at the retail level, we are left with a transmission system and wholesale market that is, at best, inefficient, unreasonably increasing costs to customers, and, at worst, unreliable.

The challenges of managing the wholesale-retail interface can be attributed to jurisdictional issues, among other sensitive issues. However, in PJM's view, PJM's PRD proposal, as set forth in the PJM Whitepaper, appropriately anticipates and recognizes at the wholesale level changing consumption patterns at the retail level in both regulated and restructured jurisdictions. With rate caps expiring, smart meters becoming more prevalent and innovative and/or competitive rate design proliferating in the PJM footprint, fundamental principles of market efficiency and sound engineering dictate that PJM's market rules must reflect this "brave new world."<sup>6</sup>

As set forth in the Whitepaper, PRD was designed to be treated as a "subtraction" from the PJM load forecast, not as a supply resource in the market. This reflects the fact PRD is load for which PJM does not need to procure capacity in the Reliability Pricing Model ("RPM") forward-capacity construct because it is responsive to price and will not be on the system when the system is tight on capacity. By following this approach, the Whitepaper proposal accurately reflects the impact of the PRD resource on planning and market operations and thus provides demonstrable customer benefits. In this regard, the Whitepaper represents a positive change from the attempted compromise proposal in the PJM stakeholder process. Under that compromise proposal, the PRD resource would have been subtracted from the Short-Term Resource Target, which would have limited opportunities for resources with short lead times (like demand resources) in the RPM Base Residual Auction and failed to produce any meaningful customer benefit in terms of reduced RPM capacity commitments.

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<sup>4</sup> See *id.* at 5-6.

<sup>5</sup> See Amended and Restated Operating Agreement of PJM Interconnection, L.L.C., Section 7.7(i).

<sup>6</sup> As demonstrated by PJM's interest in refinements to the PJM load forecasting process, PJM continues to encourage PJM to improve its knowledge and understanding of actual consumer impacts of its markets and the reaction of customers to its markets. PRD represents a valued attempt by PJM to do so.

Of particular importance, the PJM Whitepaper correctly recognizes that PRD is an additional and comprehensive option for demand response participation in PJM's wholesale markets.<sup>7</sup> However, PRD in no way does nor should replace existing PJM opportunities and programs for demand response, most recently endorsed in the energy market with the Commission's Final Rule on Demand Response Compensation. Contrary to some stakeholder representations, no broad-based agreement exists that the development of PRD should coincide with a wind-down of the existing DR programs.<sup>8</sup>

In fact, if that were the case, the narrowly defined and interpreted PRD eligibility requirements proposed in the PJM proposal could restrict the ability of industrial customers to utilize this option, leaving a large end-user segment on the sideline in terms of offering demand response capability to the PJM markets. Certainly that was not the intent of PJM's proposal; otherwise, the PJM system would lose the overwhelming majority of its demand response capability that undeniably improves the reliability and efficiency of PJM's markets.

That being said, PJMICC encourages PJM to expand its PRD proposal efforts to include other segments of the end-user community, not just residential and smaller commercial customers. The PRD concept can be easily translated to be available on a non-discriminatory basis to those industrial customers that are exposed to dynamic retail rates, have significant control over their operations and possess real-time metering. An aspect of PRD most intriguing to PJMICC members is the ability of a PRD participant to designate the "firm" amount of capacity that it wants procured on its behalf, subject to an appropriate penalty structure. Expanding this ability to the industrial sector provides a much desired option to limit exposure in RPM to only that amount of capacity that is actually required by the individual end-user and therefore the system as a whole. For customers that have the requisite supervisory control, PRD may result in a much cleaner hedge to capacity costs than the existing DR program can provide (and even an improvement over the terminated Interruptible Load for Reliability ("ILR") program).

In addition to PJMICC's interest in industrial segment PRD participation, PJMICC respectfully requests that the PJM Board reconsider the Whitepaper's proposed lifting of the \$1,000/MWh offer cap for two reasons. First and foremost, PRD loads should, at least initially, be those loads that will respond prior to LMP exceeding PJM's existing supply offer cap. Raising the PRD price threshold should only be considered after PJM has seen a saturation of the available PRD that will respond at or below that existing supply offer cap.

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<sup>7</sup> See PJM Whitepaper, at 7.

<sup>8</sup> In fact, given the recent Final Rule on Demand Response Compensation, support for PRD as a substitute for PJM's existing PJM opportunities and programs, subject to compliance filings to implement the Final Rule, represents an inappropriate collateral attack on the Commission's DR Compensation Rule. Prior to any FERC filing, PJM should closely consider the ramifications of the Commission's DR Compensation Rule on PRD resources' eligibility to receive energy market payments.

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Our other concerns in this regard are similar to those PJMICC previously raised with the Commission on PJM's pending shortage pricing proposal with respect to the impacts on customers. FERC should first be given an opportunity to address PJM's pending shortage pricing proposal before the substance of that proposal finds its way into a PRD framework.

PJMICC's concerns about the proposed elimination of the offer cap become even more acute with respect to PRD due to concern with interaction between traditional supply resources and affiliated load-serving entity ("LSE")/electric distribution company ("EDC")/PRD provider programs. Particularly when retail customers may not have control over the LSE/EDC/PRD providers' bidding strategies in PRD and their affiliates' energy market bidding strategies, PJMICC perceives serious potential for market power, particularly at the higher end of the supply curve, where market ownership concentration is greatest. Adequate safeguards are necessary to ensure that such complex market strategies are not allowed to occur.

We appreciate the PJM Board's consideration of PJMICC's support for and recommendations regarding the PRD Whitepaper. PJMICC encourages the Board to endorse the PRD proposal with the enhancements described herein. Thank you.

Very truly yours,

McNEES WALLACE & NURICK LLC

By 

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