Cost of Clean Energy Focus Of October ELCON Workshop

ELCON's Fall Workshop, focusing on the cost of "clean" energy, will be held Oct. 17 in Washington, DC.

The program is formally titled "A Different Climate for Industrial Electricity Buyers" and will include speakers from the public and private sectors. ELCON's Workshops are open to ELCON members only, but representatives from other manufacturing companies with an interest in joining ELCON may request to attend. Contact ELCON at 202-682-1390 or at elcon@elcon.org.

Highlights of ELCON’s Spring Workshop

On Demand Response
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ELCON Responds to FERC Ex-Commissioners

Consumer Dissatisfaction with Markets Found Widespread

When nine former FERC Commissioners issued a letter recently praising the organized markets for their competitive qualities, ELCON, along with the American Public Power Association, rushed to respond.

While the letter from the former Commissioners did not criticize any organization by name, it was clear from the tone, as well as dialogue with press, that ELCON was a prime target because of its continued characterization of the organized markets as non-competitive.

ELCON's response reiterated a commitment to truly competitive markets and noted that today's markets are neither competitive nor consumer-oriented. The major points of the ELCON/APPA letter were:

- Competition and lower costs are in the eye of the beholder. While the Commissioners cited studies showing lower prices for consumers, other studies dispute those findings.
- Blaming the states' implementation of retail competition is not a useful exercise. What has been done by the states for the most part cannot be undone. But state and federal regulators can look ahead for ways to mitigate the acknowledged problems in retail access states and the wholesale power markets that underpin them.
- Higher fuel costs are not the whole story behind price increases. Electricity prices differ from region to region.

Energy Legislation Proceeding On Two Tracks

Energy legislation is proceeding on two separate tracks in the House and Senate, and it is not clear whether they will converge into an enacted public law.

In both houses, Democratic leaders pushed for legislation on conservation and energy efficiency early in the session rather than addressing the far-reaching, extraordinarily difficult, issue of greenhouse gas emissions and global climate change.

The Senate passed HR 6 with many new appliance standards and conservation measures, as well as stricter rules for automobile emissions (CAFÉ). It also includes a new non-binding federal standard requiring state commissions to consider, but not necessarily adopt, revenue decoupling when requested. (See related story.) ELCON opposed this measure.

During debate on the floor, the Senate voted against a proposal to institute a renewable portfolio standard (RPS).

In late July the House leadership took recommendations from 11 committees and packaged them into one bill, HR 3221, that was approved just before the August recess. The bill also focuses on energy efficiency and conversation and, like the Senate bill, includes non-binding language.

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A bout a year ago, the National Action Plan on Energy Efficiency put out a report on how our economy could reduce its energy consumption. As I looked at the roster of those who participated in this exercise (which was coordinated by the Department of Energy and the Environmental Protection Agency), I noticed almost immediately that there were very few consumers, large or small. There were plenty of utility executives, lots of regulators, and more than a few environmentalists. But there were not many representing those of us who actually use energy and pay the bills.

And, not surprisingly, the panel’s recommendations reflected this imbalanced approach.

Let me say at the outset that I am for energy efficiency, both personally and professionally. My company, like virtually every American manufacturer, has tried to make each of our facilities as energy efficient as possible. This is due in part to the global marketplace -- if we can manufacture our product more efficiently than our competitors, we stand to gain more market share and increase our profits. But our focus on energy efficiency is also due to our recognition that the earth’s resources are limited, and those resources will last longer if we use less of them today.

When I first looked at the energy efficiency efforts put forth by the National Action Plan, some of them just didn’t make sense from the consumer’s perspective. They may make sense to utility executives. I can see why they appeal to regulators. And I understand why they are supported by environmentalists. But, the fact is, that does not make them good for consumers.

The best example of this is the National Action Plan’s support for a concept called revenue decoupling. Simply put, this allows a utility’s earnings to stay constant if the utility implements energy conservation measures that reduce its sales. In this sense it “decouples” a utility’s earnings from its sales. A utility would, in fact, sell less energy but still make the same amount of money.

Again, if I were a utility executive, selling less and earning the same sounds like a good deal. If I were a state regulator who constantly fears a growing federal role in energy regulation, this proposal reinforces the role of my state commission. And, if I were an environmentalist, removing the utilities’ disincentive to implement energy conservation would be a major accomplishment.

But the missing component here is the consumer.

From the consumer’s perspective, I fail to see why states have an obligation to keep utilities’ profit levels constant. Many factors can cause reduced electricity sales, such as unpredicted weather, shifts in population, or a reduction in load from an industrial facility closing or reducing production. Utilities have no more right to “be kept whole” than any other company.

Large consumers, like my company and other ELCON members, have already made significant progress in achieving energy efficiency and conservation. For virtually every industry, the amount of energy used to manufacture a ton of product (or whatever similar measure is used) is much less today than it was 20 or 30 years ago. As new technologies emerge, I expect manufacturers to become even more energy efficient. But as we reduce our energy intake, we expect our energy bills to be reduced as well -- and with revenue decoupling that is not likely to occur. In contrast, what is likely to occur is rate increases or additional add-on charges since the basic premise is that utility earnings should stay constant.

The situation is similar for residential consumers. Savvy shoppers know that one way they can reduce their energy bills is by purchasing today’s highly efficient appliances. Adventurous homeowners, as well

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ELCON hopedful on FERC's Advanced Rule for Organized Markets and ISO/RTO Governance.

ELCON complimented FERC for publishing an advanced notice of proposed rulemaking (ANOPR) on competition in regions with organized markets.

"We commend FERC for moving as fast as it has," ELCON President John Anderson said. "We hope the outcome will be as bold."

ELCON met with FERC’s "ANOPR A-Team" and filed comments focusing on four issues: demand response, long-term contracts, market monitoring principles, and ISO/RTO governance.

ELCON said it supports FERC's attempts to expand the role of incentive-based demand response in the organized markets and believes that each ISO or RTO has an obligation to purchase demand resources on a non-discriminatory basis in markets for ancillary services. ELCON also recommended standardizing the rules governing demand response so they are not based on the limitations of generators but rather on a neutral basis that reflects system reliability needs.

Demand response should be compensated on the same basis as generation for the same services, ELCON told FERC. If generators are given the option of the higher of LMP or opportunity costs, demand should be eligible for the same or a comparable pricing scheme.

"The most efficient megawatt is the one that is not built," Anderson said. "Demand response can be a vital and efficient means to meet the power needs of the future. FERC has recognized that and we now need to implement the appropriate rules to make it happen."

Buyers and sellers benefit from being able to choose a portfolio of short-term, intermediate-term, and long-term power supplies, but organized markets are currently structured as "suppliers' markets," ELCON noted. Changes will be necessary to establish the robust forward markets that will benefit consumers.

"Long-term contracts can benefit both buyers and sellers," Anderson explained. "But the way Day Two markets are constructed today, those benefits cannot be realized."

ELCON reiterated its long-held position about the importance of effective market monitoring. The best way to achieve that is through a two-tiered market monitoring unit structure, the top tier consisting of an external panel of part-time market experts reporting to the ISO/RTO board and the lower tier located internally.

"The market monitoring unit is necessary to ensure that the market is functioning properly," noted Anderson. "If the MMU is wholly responsible to the market leadership, there is an inherent conflict of interest. That is why we need some external input as well."

Finally, on governance, ELCON said it supported a "hybrid" board for ISOs and RTOs comprising independent members and a minority of members representing stakeholder interests. The "stakeholder" representatives should be evenly split between supplier and consumer interests.

"Governance of the organized markets is the key to their success," asserted Anderson. "We need board members who are knowledgeable, and we need board members who represent the spectrum of stakeholders involved in the market. ELCON members support the 'hybrid' approach."

ELCON Responds

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ELCON, PJM Start Constructive Dialogue

In July, ELCON met with several PJM executives at PJM’s request to discuss customer dissatisfaction with its service. Acknowledging the issue, PJM representatives said they hope to address the problems, pointing to scheduled workshops on demand response and long-term contracting -- two issues of importance to ELCON -- as examples of their willingness to listen to customers.

PJM’s customers’ attitudes reflect a problem ELCON addressed in two special reports. The first, "Problems in the Organized Markets," in 2005, saw in the anti-consumer structure, operation and governance of the organized markets reasons why they were not contributing to increased competition. A follow-up paper, "Today’s Organized Markets: A Step Toward Competition or an Exercise in Re-regulation," in December 2006 suggested the markets were so anti-consumer that even a return to cost-of-service regulation should be explored.

ELCON President John Anderson reacted positively to PJM’s outreach. "I am encouraged that PJM executives sought out ELCON to begin what we hope is a constructive and ongoing dialogue," he said.
Resource planning has three components, according to Faruqui: energy efficiency, renewable energy, and demand response. California set an annual goal of 5 percent reduction in electricity consumption per year through demand response, but it fell short last year when demand response yielded a reduction of only 2.2 percent.

Interestingly, Faruqui said, 80 percent of the demand response came from 30 percent of the customers. Interviews showed 14 specific barriers to participation, some price-based, others technology-based.

Meanwhile, for a number of reasons, the whole issue of load management in California is "being revisited," Faruqui reported.

California’s 30-year flat load owes more to energy efficiency than to demand response.

As often happens, California is on the cutting edge of public policy once again with its use of demand response to reduce electricity consumption, according to Ahmad Faruqui of the Brattle Group energy consultants.

But it has not been the most effective tool the state has used to manage load, Faruqui told ELCON’s Workshop.

California has had a flat electricity load for 30 years, but it has been more a result of energy efficiency than demand response, Faruqui said. The state has had load management standards in place since the late 1970s.

New load management standards include automated demand response for all commercial and industrial customers.

In conjunction with the Spring Workshop in St. Louis, ELCON members and spouses took a special tour of ELCON member Anheuser-Busch’s brewery at its headquarters.

Speakers at ELCON’s Workshop, clockwise from immediately above: Bob Laurita, demand response supervisor for ISO-New England; Robert Borlick, energy consultant; Paul Centolella, Ohio Commissioner; Bernie Neenan, vice president of UtiliPoint International; and Ahmad Faruqui, Brattle Group consultants, addressing participants.
In order to understand how demand response fits into today's electricity markets, it is first necessary to acknowledge that electricity markets are changing, Bernie Neenan, vice president of UtiliPoint International, remarked at ELCON's Spring Workshop on Demand Response in St. Louis.

In the "old" world, the market was regulated and the emphasis was on volume and load factor, Neenan said. Long-term contracts were an integral part of that equation. In the "new" unregulated world the focus is on volume and load profiles. This leads market participants away from any long-term commitments, he said.

"The old perspective was to sell the product," but demand management and demand response are now "apple pie," he said.

Paul Centolella, a Commissioner with the Public Utilities Commission of Ohio, pointed out a local wrinkle arising in his state and others that have rate stabilization plans in effect to avoid high electric rate increases for consumers. Those plans will be ending sooner or later. The big question is how to end rate stabilization without "sticker shock," he reported.

Centolella cited a 2003 study by Rassenti, Smith and Wilson which concluded that "demand bidding can eliminate price spikes."

Thus, he concluded that "we can have efficient markets without demand response, but they would be one-sided."

Great Potential Seen for Demand Response

If 17 percent of a utility's electricity load could exercise demand response, new capacity costs could be reduced by $1.1 billion and investment in transmission and distribution assets could be significantly deferred, Paul Centolella, an Ohio PUC Commissioner, told ELCON's Spring Workshop. Centolella said the statistic came from a New York study on the potential of demand response.

Participants in electricity markets generally agree that demand response can make electricity markets more efficient. Yet, several Workshop speakers listed problems implementing an efficient demand response program.

Bernie Neenan, vice president of UtiliPoint, asked whether demand response "is a privilege or an obligation." He noted that the playing field is not level but heavily tilted toward utilities.

"Should ISOs even be in the demand response business?" asked Robert Borlick, an energy consultant. ISOs and RTOs administer wholesale markets whereas demand response deals with retail customers, he noted. Responding customers should be paid the difference between the locational marginal price and the retail energy rate, he said, but "in order to sell, you have to own what you're selling -- you need a property right."

Borlick characterized the programs implemented by several organized markets as "brilliant and audacious." But, he asked, "Are they legal?"

Bob Laurita, supervisor of demand response for ISO-New England, said recognition of the need for long-term capacity in the coming years led ISO-NE to adopt a plan to add capacity by auction. Supply and demand resources can compete "head to head" for future needs, he said. The demand side includes energy efficiency, load management, and demand response.

"All participants will be treated equally," he said. "A megawatt is a megawatt."

More than 400 entities have shown interest in participating in ISO-NE's demand response program, Laurita said, adding, "We need confidence that the reduction is real." He noted the ISO intends to "measure and verify."

Despite the general agreement over the power of demand response to make energy markets more efficient, potential participants still face barriers.

Malcolm Smith, CEO of Xtend Energy, listed three major barriers: the difficulty most people have understanding the programs, rules written in ISO-speak that are rarely synopsized, and poorly documented implementation guidelines.

The writers of the guidelines seem to "understand generation but not load," he said.

Smith foresaw great potential benefits for manufacturers who participate in demand response programs. Two keys to success are to "require a 'turnkey' contract for implantation and service and to talk to the ISOs personally," he said.
ELCON Activities Before The Federal Energy Regulatory Commission

California's two-tiered market monitoring program offers a workable model for the rest of the country, ELCON President John Anderson testified at FERC's recent conference, "Review of Market Monitoring Rules."

"We have looked at markets across the country, and we find that the two-tiered market monitoring structure, similar to that in operation in California, provides a practical means to perform this important function," Anderson said.

The model structure that Anderson described would include an independent market monitoring unit (MMU) operating within the ISO/RTO that would have unimpeded access to all ISO/RTO data and personnel and perform real-time screening and analysis to identify circumstances that require further investigation. A separate, independent market monitor operating outside the ISO/RTO would prepare analyses of the potential harm of market flaws to consumers, determine when market activities should be temporarily suspended, address and investigate concerns or complaints of stakeholders, and coordinate with the internal MMU.

"History has shown that internal market monitoring units that report to the ISO and RTO management may not have the independence to adequately protect consumers," Anderson suggested. "The need for MMUs would be minimized if the structure and the operation of the ISOs and RTOs were improved and made more competitive. In addition, if the organized markets were largely unconstrained and local market power concerns were mitigated, the potential for competition would be enhanced and the need for an MMU reduced. However, in today's world, the need for MMUs is critical."

ELCON also weighed in on the issue of market monitoring in PJM. "When we look at markets like PJM, we don't find competition," Anderson stated. "What we find instead is re-regulation resulting in failed markets. If these markets are to have any credibility with consumers, the market monitoring function is crucial. And for the market monitoring function to be effective, it must be truly independent of the market operators."

When PJM announced that it was going to adopt a one-tiered external market monitor, Anderson said it showed PJM recognized it needed an effective market monitoring structure and that the previous structure was "not adequate." But he still voiced ELCON's preference for a two-tiered, internal/external approach.

**Compliance Registry Working Well**

The Energy Policy Act of 2005 (EPAct) authorized FERC to approve an electric reliability organization (ERO) to develop standards to assure the reliability of the North American grid.

Last year FERC approved the North American Reliability Corporation (NERC). One of its tasks was to develop a compliance registry, a listing of owners, operators and users of the bulk power system subject to reliability standards. Two crucial questions were whether all generators -- utility and non-utility -- would be listed regardless of size or potential impact, and whether large manufacturing facilities would be included as "users" of the system.

ELCON was instrumental in working with NERC, FERC, and others to develop "material impact" criteria so that only generators and other entities with a material impact on grid reliability would be included in the registry. Other entities would not be listed and would not be subject to the NERC standards.

"At first it was unclear whether there would be 1,000 or 10,000 entities on the registry," said ELCON President John Anderson. "There was a difference of opinion within NERC's staff, with several people recommending as large a number as possible. We argued that, first, having a large number in the registry would be burdensome to a number of industrial installations, and, second, with a large number NERC examiners would be stretched too thin to concentrate on those facilities that can really cause damage to grid reliability."

NERC delegated the development of the registry to various regional reliability entities. They nominated facilities to be in the registry. A nominated facility can appeal to NERC if it does not believe it can have a material impact on grid reliability. Several industrial facilities have appealed successfully.

NERC reported in August that the compliance registry now contains 1,721 entities. Most are utilities, but there are some industrial facilities with on-site generation as well.

"The process and the resulting Registry are generally good," Anderson said. "Those who originally suggested a larger registry would have included many industrial facilities as well as some small utilities that really could not impact grid reliability. Eventually common sense prevailed. From the perspective of the industrial user and cogenerators, I am generally satisfied that only facilities with a potentially material impact on grid reliability have been included." E
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as large and small businesses, are investing in alternative light bulbs that use just a fraction of the electricity when compared to the standard incandescent bulbs. A host of other energy-conserving products and services are also available, and new technologies are emerging almost every day.

But why are they doing this? Simple -- they want to save money. And, if revenue decoupling is adopted, the incentive for consumers to make energy conservation investments is removed because the consumer will not see a lower electric bill.

That is why the National Association of State Utility Consumer Advocates (NASUCA), with representatives in each state, recently adopted a resolution strongly opposing revenue decoupling. They recognize that giving those charged with selling electricity the additional task of implementing energy conservation programs presents an inherent conflict of interest, and that revenue decoupling eliminates any incentive for the utility to seek greater efficiency on its own.

But consumer opposition to date has not been sufficient. Legislation has progressed in both the House and Senate that endorses the concept of decoupling. Several states have had decoupling programs on the books. At least one state, Maryland, adopted it just recently, and several more are considering it.

But, common sense prevailed in another state. The New Mexico Public Regulation Commission recently turned down a utility request for revenue decoupling -- supported, not surprisingly, by a major environmental group. The rejection was emphatic and "with prejudice," meaning the utility cannot put forth that proposal or any similar decoupling proposal in the future.

I hope common sense prevails more often. It just doesn't seem right that a consumer could use less of a product but pay more for it. To me, that is the bottom line of revenue decoupling. It is not good for consumers, and that's why I oppose it.

Lloyd Webb is energy manager for Eastman Chemical.

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Defense Council. The New Mexico Commission expressed concern over negative impact on consumers and rejected the application "with prejudice," thus precluding PNM from offering the request again.

Other state legislatures are considering decoupling, and it is almost certain to be brought before state commissions. ELCON President John Anderson observed, "Revenue decoupling is one of those rare issues that is supported, for different reasons, by both utilities and environmental groups. But it is consumers, large and small, who suffer because they no longer benefit from their own energy efficiency and conservation efforts. This issue has been considered for years -- and rejected more often than adopted. Consumers hope that pattern will continue." E

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on revenue decoupling. It also contains a proposal to reward manufacturers for the capture of waste heat, which, according to one congressional staff person, could produce as much as 90 gigawatts from what is not being harnessed at present.

By a floor amendment, the House approved a renewable portfolio standard requiring investor-owned utilities to acquire 15 percent of their power from renewable energy by 2020 (four percent of which may come from utility-implemented energy efficiency). The House also passed a $16 billion tax bill that provides credits for renewable and non-conventional energy sources. Funds for this will be raised primarily from the oil and gas industries.

A conference committee will convene in the fall, presumably with members of the Senate Energy Committee and House representatives from all 11 committees that contributed to the House bill. That format may prove cumbersome, and some hot button issues will be difficult to reconcile. As examples, the House bill but not the Senate one contains renewable portfolio requirements, and the Senate bill but not the House version includes CAFÉ standards. Most observers do not foresee a speedy conference.

Also in the fall, committees in both houses expect to take up greenhouse gas legislation. In the House that task will fall to the Energy and Commerce Committee, whose staff reportedly is trying to choose between a cap-and-trade system, which is the common approach, and a carbon tax as suggested by Committee Chairman John Dingell (D-MI). Most believe the carbon tax is the most equitable approach since it treats all segments of the economy the same, but it is also generally believed to be politically untenable since it affects consumers most directly and is extremely difficult to implement.

In the Senate, debate on greenhouse gas legislation will occur in the Committee on Environment and Public Works. At least three major proposals (Boxer-Sanders, Lieberman-Warner, and Bingaman-Specter) have already been offered, each with a different approach to capping emissions. Many members in both houses were persuaded to withhold offering amendments to the energy efficiency bill and to propose them as part of the greenhouse gas effort. If that greenhouse gas effort fails to gain traction, it is uncertain how that will affect the outcome of both the greenhouse gas debate and the conference committee on the energy efficiency bill.

According to ELCON President John Anderson, "One issue receiving less attention than it deserves is the cost of greenhouse gas legislation on the economy." He noted that early studies attempting to assess electricity price increases and fuel costs vary tremendously. "If legislation is enacted, it will have a profound impact on the ability of America’s manufacturers to compete in world markets," he said. "That should not stop progress on this issue, but we should thoroughly investigate the total impact as we go through the legislative process." E
WHAT IS ELCON?

- **DATE ORGANIZED:** January 15, 1976

- **WHO WE ARE:** The Electricity Consumers Resource Council (ELCON) is the national association representing large industrial consumers of electricity. ELCON was organized to promote the development of coordinated and rational federal and state polices that will assure an adequate, reliable and efficient supply of electricity for all users at competitive prices. ELCON's member companies come from virtually every segment of the manufacturing community.

- **MEMBER COMPANIES:** Air Liquide • Alcoa • Anheuser-Busch Companies, Inc. • BOC Gases • BP • Chevron • Corning, Inc. • DaimlerChrysler • Dow Chemical Co. • E.I. du Pont de Nemours & Co. • Eastman Chemical Company • ExxonMobil Power and Gas Services, Inc. • Ford Motor Company • General Motors Corporation • Gerdau Ameristeel • Honda • Honeywell • Intel Corporation • Johns Manville • Lafarge • Monsanto Co. • Occidental Chemical • Praxair • Procter & Gamble • Rio Tinto • Shell Oil Products • Smurfit Stone Container Corp. • Solutia, Inc. • Tate & Lyle • Valero Energy Corp.

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Don’t miss ELCON’s Fall Workshop on the cost of “clean” energy, Oct. 17 in Wash., DC