

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Supplemental Notice of Proposed
Rulemaking on Demand Response
Compensation in Organized Wholesale
Energy Markets

RM10-17-000

Comments of the
Electricity Consumers Resource Council
(ELCON)

The Electricity Consumers Resource Council (ELCON) appreciates the opportunity to comment on the Commission's August 2, 2010 *Supplemental Notice of Proposed Rulemaking (NOPR)* on issues related to the initial March 18, 2010 NOPR. In the March NOPR, the Commission proposed an approach for compensating demand response resources in order to improve the competitiveness of organized wholesale energy markets and thus ensure just and reasonable wholesale rates. The *Supplemental NOPR* seeks comment on whether the Commission should also adopt requirements related to two issues addressed in stakeholder comments: (1) if the Commission were to adopt a net benefits test for determining when to compensate demand response providers, what, if any, requirements should apply to the methods for determining net benefits; and (2) what, if any, requirements should apply to the allocation of the costs of demand response.

Summary

In ELCON's comments on the original NOPR, we unequivocally supported the proposed rule and regarded it as a significant and long overdue contribution to enhancing the competitiveness of organized wholesale energy markets. We also supported the proposal that demand response providers be allowed to participate in the energy markets on a 24-by-7, year-round basis. LMP would be equal to the marginal value of both demand response and generation in any hour, any season or any time of day. There is nothing in the *Supplemental NOPR* that changes our position or support for the original proposed rule. There is no need for a "net benefits test" to limit eligibility of demand response bids in any hour. Regarding the allocation of the costs of demand response, we recommend that the total combined costs of demand response and generation be divided by the total billing units to produce a per energy unit charge that is allocated to all customers consuming energy in any hour in which demand response resource is dispatched. The allocation should be on a zonal basis. This refinement to the settlements process should resolve the so-called "missing money" problem, which is the concern of LSEs that they might under-recover the revenue requirement.

Issue # 1: Net Benefits Test

The *Supplemental NOPR* seeks comments on the need for a "net benefits test" for determining when (*i.e.*, in which hours) to compensate demand response. Commenters to the March NOPR seeking a net benefits test offered one primary point -- that some

customers may not experience net benefits in off-peak hours (i.e., low-load, low-price hours) if providers of demand response resources are allowed to bid in all hours. The intent of the net benefits test is to limit the number of hours in which demand response resources may participate to the steepest part of the supply curve, which is typically the hours of highest demand and cost. *Supplemental NOPR* at ¶ 6. It is simply an oblique effort, without a sound basis, to stifle demand response.

ELCON does not support the need for a net benefits test because this would contradict and undermine the purpose of the bid-based pricing mechanism in organized wholesale electric markets. The merit-order bid stack used to determine the clearing price is itself a market-oriented “benefits” test that applies equally and fairly to both generation and demand response bids. The motive for proposing another test that second guesses the pricing mechanism seems intent on obstructing the implementation of a viable demand response resource capability and thus preserving the generators’ monopoly control of the energy market by limiting price elasticity in the market.

ELCON believes that the concern that demand response may not be beneficial to all customers in all hours may be misplaced. Cost optimization of a bid-based security constrained dispatch is achieved over time and increases with longer multi-hour, multi-day time periods. One reason for this is the need by system operators to declare at certain times that some generating units be run in “out of merit” dispatch. Nonetheless, the nodal pricing mechanism is designed to be self-regulating regarding when and at what price a resource efficiently clears the market in each bid cycle. It is somewhat ironic that an additional, non-market test would be proposed to restrict the deployment

of dispatchable demand response resources because energy markets are only efficient when price-responsive demand-side resources are fully integrated in the markets and allowed to bid. End users do not have to be a demand response participant to benefit from demand response. A huge benefit of the NOPR's 24-by-7 proposal is adding the risk, in every hour, that any bid from the generator sector might be undercut by a demand response provider and induce more efficient (i.e., lowest possible) bids from generators. Demand response does not have to be exercised in any hour for this benefit to be realized by all end users. It is the mere threat of entry that creates more competition in the bid stack.

Issue # 2: Cost Allocation

The main concern regarding the allocation of costs associated with demand response compensation is the so-called "missing money" problem – the reduction in demand inevitably results in having a smaller amount of load over which to spread the costs. The fear is that the remaining load on the system may pay higher LMPs than had demand response not been dispatched, or that LSEs may not fully recover their revenue requirements. ELCON believes that the first issue is exaggerated and the second is easily addressed.

Dispatchable load curtailment has been a feature of the electric industry for decades with cost-effective results for all customers. We are not convinced that integrating dispatchable DR with the nodal market design will be so successful as to be self-defeating.

The costs of demand response resources should be allocated the same way generator costs are allocated, i.e., to the beneficiaries. Specifically, we recommend that the total combined costs of demand response and generation be divided by the total billing units to produce a per energy unit charge that is allocated to all customers consuming energy in any hour in which demand response resource is dispatched. The allocation should be on a zonal basis. This refinement to the pricing and settlements process should resolve the “missing money” problem that concerns some LSEs. In addition, this zonal method for cost allocation is the most practical “granular” allocation method (to beneficiaries) given the nature of the nodal market. For example, PJM’s witness at the Commission’s September 13, 2010 Technical Conference stated that two reasons prevent more accurate assignment to beneficiaries:

First, it is not practical to rerun market results with and without demand resources with sufficient granularity to accurately identify specific beneficiaries for specific hours. The second reason is that wholesale customers may not directly benefit from reduced prices because they may already be hedged through forward contracts or other mechanisms such that they do not actually realize benefit from the reduced prices in the Energy Market that result from demand response. As a practical matter there is no way to observe what type of contract or hedging instrument each energy consumer has acquired. A requirement to obtain such information from all consumers would be burdensome on market participants and RTOs and would be cost prohibitive to implement.

Statement of Andrew L. Ott.

ELCON Response to Commission Questions on Cost Allocation

1. FERC seeks comment on whether standardizing demand response compensation among ISOs and RTOs requires simultaneous standardization of a method for allocating the costs associated with such compensation. In addition, whether standardizing demand response compensation among ISOs and RTOs requires

consideration of corresponding settlements and other impacts associated with the compensation mechanism.

ELCON Response: ELCON supports some degree of standardization – consistency might be a better term – of the method used by FERC-jurisdictional ISOs and RTOs to allocate the costs of demand response compensation. This would avoid protracted deliberation by ISO/RTO stakeholder processes and minimize the potential for unintended “seams” problems.

2. If the Commission standardizes an approach for allocating the costs associated with requiring payment for demand response, what type of approach is appropriate.

ELCON Response: ELCON supports a broad-based allocation of demand response costs to reflect the fact that integrating dispatchable price response in the market design of organized wholesale electric markets is a fundamental enhancement of overall market operation. Dispatchable demand response increases market transparency and system load factors, reduces the market power of traditional suppliers, and adds an important tool for enhancing reliability. These factors support a broad-based approach. We recommend that the total combined costs of demand response and generation be divided by the total billing units to produce a per energy unit charge that is allocated to all customers consuming energy in any hour in which demand response resource is dispatched. The allocation should be on a zonal basis.

3. How the use of a net benefits test would affect the need for and methodologies for determining cost allocation.

ELCON Response: The point is irrelevant because some method for cost allocation is necessary and the need for a separate benefits test is not.

Notices and Communications

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Dated: October 13, 2010

Certificate of Service

I hereby certify that I have this day served the foregoing document upon each person designated on the official service list compiled by the Secretary of this proceeding.

Dated at Washington, D.C.: October 13, 2010

/s/ MARK W. WALKER
Mark W. Walker