



Demand Response: The Debate Lives On The Perspective of US Manufacturers

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- ELCON was established in 1976 in anticipation of the enactment of Title I of PURPA – specifically to address the proposed federal ratemaking standards. PURPA was enacted in 1978.
- Founding principles for economic regulation are based on cost causation (i.e., cost of service).
- Members are variously energy intensive or energy extensive.
- Some members are Demand Response Providers and typically their own LSE. One large member is not state jurisdictional. Other members are not DR capable but enjoy the benefits of lower LMPs.
- ELCON was a strong supporter of FERC rulemakings that resulted in Order No. 719 and Order No. 745.



Experience with DR



- ELCON members have curtailed load for the benefit of utilities and/or their ratepayers for decades
- There were different names for it:
 1. Load Management
 2. Interruptible Rates
 3. Curtailment Rates
 4. Cogeneration Deferral Rates
 5. Load or Job Retention Rates

Compensation

Compensation usually took one of two forms:

1. The customer was given a discounted rate in return for the obligation to be interrupted when the utility requests that customer to do so under pre-specified circumstances. The rate was generally negotiated and varied anywhere from recovering only variable costs to the full firm service tariff rate. This rate was often a means by which the customer received a truly cost-based rate, i.e., cross-class subsidies were removed.
2. The customer choose to be interrupted when the utility requests the customer to do so under pre-specified circumstances. The customer receives the rate discount only when the customer actually interrupts its load. This form was less common.



EPSA v. FERC

- Decision was issued May 23, 2014.
- Judges Janice Rogers Brown and Laurence Silberman were the majority. Judge Harry Edwards dissented.
- Brown wrote the 16-page Opinion of the Court; Edwards wrote the 28-page dissenting opinion.
- The majority concluded that Order 745 exceeded FERC's authority under the Federal Power Act. Further, because the FPA unambiguously restricts FERC from regulating the retail market, the court held that the FPA foreclosed FERC's claimed regulatory authority over demand response. Compensation based on full LMPs was found “arbitrary and capricious.”



Judge Janice Rogers Brown

- In a speech in 2000, Brown lamented the triumph of "the collectivist impulse", in which capitalism receives "contemptuous tolerance but only for its capacity to feed the insatiable maw of socialism."
- She argued that "where government moves in, community retreats, civil society disintegrates, and our ability to control our own destiny atrophies..."
- She suggests that the ultimate result for the United States has been a "debased, debauched culture which finds moral depravity entertaining and virtue contemptible".



How are Rates/Prices Set in Different Markets?

Rate/Price Structure	Examples	The Right Rate/Price?
Economic Regulation: Average Embedded Costs	Bundled rates offered by traditional utilities in so-called bilateral markets	Just and Reasonable
Economic Regulation: Marginal Costs Using Auctions	Unbundled generation component of rates in organized markets	Just and Reasonable
Competitive Markets	Global markets set competitive prices for oil, corn, chemical commodities, paper products, automobiles	Whatever the Market Decides



Appropriate Compensation for DR

- This is not an exercise in normative price theory. It is economic regulation. “Prices” are established by an administrative construct.
- A “just and reasonable” price is a rate. But rates are for sales not forgone consumption. How should an incentive intended to discourage consumption be compensated?
- Compensation for DR should be based on traditional ratemaking principles and precedent. Call it sausage-making if you like. Its purpose is to balance the interests of ratepayers and the utility’s shareholders.
- One principle and precedent that comes to mind: AVOIDED COSTS.
- If done right, avoided costs meet the standards of cost of service.
- Avoided costs in an organized market are LMPs.



“Chevron” Will Prevail at the Supreme Court

- The FPA is ambiguous regarding whether forgone consumption constitutes a “sale.” Nor does the statute dictate that DR be treated solely as a matter of retail regulation.
- Act is also ambiguous as to whether a rule requiring administrators of wholesale markets to pay a specified level of compensation for such forgone consumption constitutes “direct regulation” of retail sales.
- Two-Step Chevron Precedent:
 - (1) Does the FPA unambiguously “speak to the precise question?” The answer is clearly no.
 - (2) If not, whether the Commission’s interpretation is a permissible construction of the statute? We believe the answer is yes.



FERC Authority

- The Commission has authority to “determine the just and reasonable . . . practice” by setting a level of compensation for demand response resources that, in its expert judgment, will ensure that the rates charged in wholesale electricity markets are “just and reasonable.”
- There is an opt-out from the compensation requirement for ISOs and RTOs in States where local regulatory law stands in the way. Thus, Order 745 preserves State regulation of retail markets. As Judge Edwards stated: “This is hardly the stuff of grand agency overreach.”
- Under the FPA, DR is neither a retail sale nor a wholesale sale.



Judge Edward's Dissent

“All Order 745 says is that *if* a State's laws permit demand response to be bid into electricity markets, and *if* a demand response resource affirmatively decides to participate in an ISO's or RTO's wholesale electricity market, and *if* that demand response resource would in a particular circumstance allow the ISO or RTO to balance wholesale supply and demand, and *if* paying that demand resource would be a net benefit to the system, then the ISO or RTO must pay that resource the LMP. That is it.” *At page 17 emphasis added.*



DR Debate is a Ruse for Bigger Concerns Regarding the Organized Markets

- The organized markets are not now capable of supporting long-term investments in generation – especially merchant generation – which was the expressed intent of industry restructuring 15 to 20 years ago. The only innovation has been DR.
- A purpose of industry restructuring that began almost two decades ago was to shift business risk to suppliers and away from ratepayers.
- It is not clear if the merchant generators have the wrong business model or the organized market is the wrong market design.
- Since the formation of ISOs and RTOs there has been an endless cycle of market redesigns and fixes—a most egregious form of regulatory uncertainty. This cycle must end. DR is an essential part of the solution. DR gives these markets a soul.

