

## E-ALERT | Clean Energy and Climate

March 29, 2010

### FERC PROPOSES POLICY THAT COULD INCREASE PAYMENTS TO DEMAND RESPONSE PROVIDERS IN ORGANIZED MARKETS AND WAIVES SMALL QF FILING REQUIREMENTS

On March 18, 2010, the Federal Energy Regulatory Commission (FERC) issued a Notice of Proposed Rulemaking that would require organized electricity markets, such as RTOs and ISOs, to pay demand response resources the energy market price for reducing consumption, and revised QF certification requirements, including exempting QFs that are 1 MW or less from filing for certification.

#### DEMAND RESPONSE COMPENSATION

The proposal would require all organized wholesale electricity markets that allow demand response providers to participate as resources in day-ahead and real-time energy markets to pay those providers the Locational Marginal Price (LMP) for reducing consumption below expected levels. The proposal does not apply to demand resources that do not bid into these energy markets.

According to FERC, demand response resources can lower electricity prices and ensure reliability, and thereby can play a critical role in helping the Commission fulfill its Federal Power Act (FPA) mandate to ensure that rates are just and reasonable. Because FERC has allowed each RTO and ISO to develop its own compensation methodologies for demand response resources in energy markets, compensation levels vary significantly. The Commission is concerned that some existing, inadequate compensation structures have hindered the development and use of demand response and thus proposes that all organized markets pay demand resources the market clearing price, or LMP.

The organized markets rely on LMPs to encourage efficient behavior by market participants. The LMP represents the value of additional supply or reductions in consumption at each node within the RTO or ISO and thus reflects the marginal cost of the last unit necessary to efficiently balance supply and demand. FERC observed that in balancing supply and demand, a one megawatt reduction in demand is equivalent to a one megawatt increase. Demand resources, however, are not compensated at levels that reflect the marginal value of the resource being used by the RTO or ISO to balance supply and demand. This may cause under-investment in demand response resources, resulting, according to FERC, in higher, and unjust and unreasonable, prices. Paying LMP for demand reductions made in response to price signals will compensate demand resources in a manner that reflects their marginal value and is thus comparable to the treatment of generation resources.

FERC recognized that compensation for demand response resources has been the subject of debate. Some parties favor paying LMP minus components of the retail rate, on the theory that such an approach permits all consumers to react as if they were paying LMP. Others argue that paying LMP

is appropriate only during the most expensive hours, on the theory that demand response will have the greatest impact during those hours in which the aggregate supply curve is steep (*i.e.*, when supply is less elastic). FERC observed that while a perfect payment scheme may not exist, paying LMP to demand response resources in all hours “is the correct approach at this time.”

Comments on the proposal are due May 13, 2010. The proposal may be accessed at:

<http://www.ferc.gov/whats-new/comm-meet/2010/031810/E-1.pdf>

## SMALL QF FILING REQUIREMENTS

In a move to lessen regulatory burdens on certain renewable energy providers, FERC adopted Order No. 732, revising its regulations regarding the form (FERC Form No. 556) used in the certification of QF status for small power production or cogeneration facilities.

Most significantly, generating facilities with net power production capacities of 1 MW or less are now exempt from any filing for certification as a QF. FERC reasoned that many of the filings for QF status from such small facilities are for solar and wind powered facilities installed at residences or other relatively small electric consumers such as retail stores, hospitals, or schools and that there may not be a compelling need for such filings. Over the last five years, 48% of QF certification filings were from facilities 1 MW or smaller but represented only about one half of one percent of QF capacity certified. FERC also noted that from 2006 to date, 90% of such filings were made by solar-powered and wind-powered facilities.

While facilities 1 MW or less no longer need to file for QF certification, FERC noted that it expects those facilities to provide necessary technical information to the purchasing utility and that the purchasing utility may contest a facility’s QF status.

FERC also made a number of other revisions to the Form 556 regulations. The most noteworthy are:

- Form No. 556 must be filed electronically. FERC reasoned that electronic filings will reduce required staff resources and facilitate the compilation of QF data that could be made available to the public. With electronic filings, FERC will be able to automatically generate *Federal Register* notices directly from the electronic data. Accordingly, FERC eliminated the requirement that Form 556 applicants provide a draft notice suitable for publication in the *Federal Register*.
- FERC clarified the ownership information required on Form 556. Applicants need only provide information for direct owners that hold at least 10% equity interest in the facility, and must identify all upstream owners that both (1) hold at least a 10% equity interest in the facility and (2) are electric utilities or holding companies.

The final rule may be accessed at: <http://www.ferc.gov/whats-new/comm-meet/2010/031810/E-31.pdf>

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