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www.BlankRome.com March 2011

# FERC Issues Order Requiring The Standardization Of Demand Response Resource Compensation

On March 15, 2011, the Federal Energy Regulatory Commission (the "Commission" or "FERC") issued an order (the "Order") modifying its regulations to require each Regional Transmission Organization ("RTO") and Independent System Operator ("ISO") to standardize the method for compensating demand response resources participating in their respective wholesale energy markets. Demand response entails the reduction in the consumption of electricity by customers in response to price signals. Specifically, the Order requires RTOs/ISOs to pay a demand response resource that is dispatched the market price for energy (i.e., locational marginal price ("LMP")) if: (1) the demand response resource has the capability to balance supply and demand; and (2) it will be cost-effective to dispatch and pay the LMP to the demand response resources.

To ensure that it will be cost-effective to dispatch and pay the LMP to a demand response resource, FERC directed RTOs and ISOs to utilize a "net benefits" test to demonstrate that the benefit of the reduced LMP that results from dispatching the demand response resource exceeds the costs of paying the LMP to the demand response resource. In order to implement the "net benefits" test, ISOs and RTOs must develop a mechanism that approximates the price level at which the dispatch of a demand response resource will be cost-effective. Finally, pursuant to the modified regulations, each RTO and ISO must allocate the cost of compensating its respective demand response resources proportionally among all the entities that purchase energy from the respective energy market in the area or areas where the demand response reduces the market price at the time when the demand response resource is committed or dispatched.

The modified regulations should increase the compensation for demand response resources. Moreover, the standardization and increased compensation for demand response providers should encourage new entrants and innovation from entities seeking to enter the demand response market.

The Order requires each RTO and ISO to submit a compliance filing to FERC by July 22, 2011, that contains the respective RTO's or ISO's tariff changes necessary to implement the new compensation structure required by the rule, a net benefits test, and the cost allocation methodology. Additionally, the Order requires that by September 21, 2012, RTOs and ISOs conduct and submit to FERC a study examining the requirements for and effects of implementing a dynamic approach to determining when demand response resources are cost-effective as part of the software systems used by RTOs and ISOs to dispatch supply and demand in the electric systems they operate.

If you have questions concerning the material described in this client alert, please contact any of the following members of Blank Rome's Energy Industry Group:

Nicholas A. Giannasca
212.885.5018 ▪ Giannasca@BlankRome.com

Carlos E. Gutierrez
212.885.5095 ▪ CGutierrez@BlankRome.com

James M. Burlew
215.569.5587 ▪ Burlew@BlankRome.com