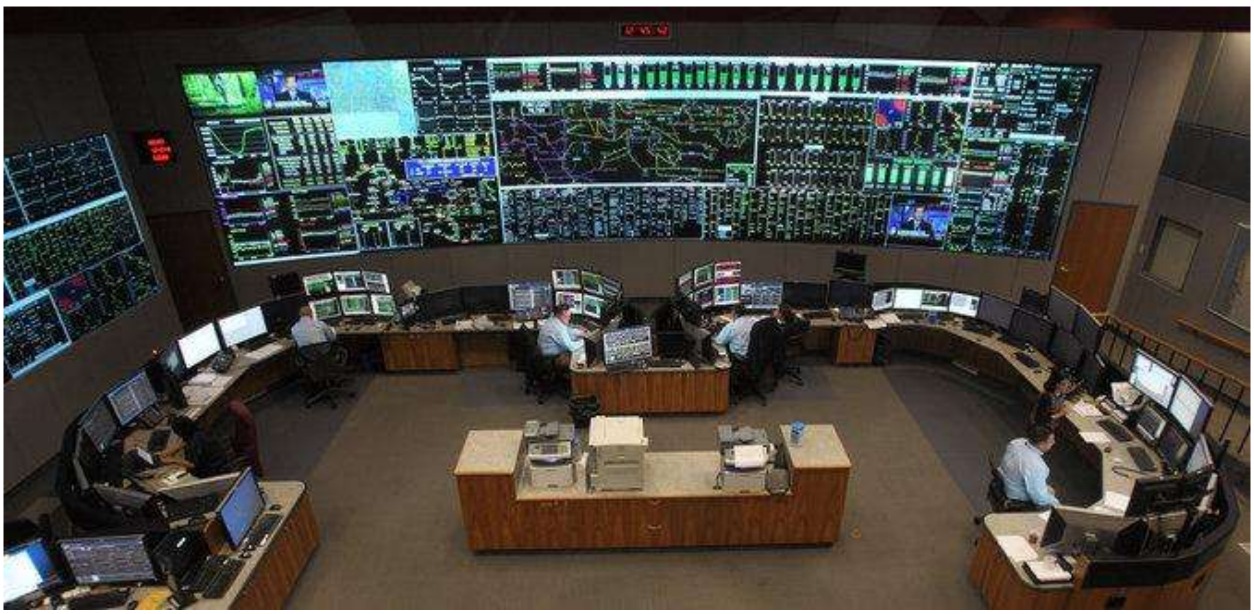
The New York Times

ENERGY & ENVIRONMENT

Legal Fight Pits Sellers of Energy Against Buyers

By DIANE CARDWELL and MATTHEW L. WALDNOV. 26, 2014



PJM Interconnection, a grid operator, says its program saved $650 million in a summer week.CreditPJM Interconnection, via Pr Newswire

Over the past few years, the federal government has nurtured the growth of an odd kind of player in the energy markets: companies that recruit consumers to unplug themselves when electricity use is high, in exchange for a price break.

The companies have been embraced by electric companies and system operators who say they have helped make service more reliable, and even helped avoid rolling blackouts during heat waves.

The approach has also lowered costs for all customers, experts and executives say, as utilities have needed to buy less of the most expensive power to meet peak needs.

“This market had been doing really well and functioning efficiently for quite some time,” said Craig C. Goodman, president of the National Energy Marketers Association, whose members sell electricity to consumers, speaking of the demand-response arrangement.

But that could soon change. Two important cases have challenged the approach, and one of them has won a significant ruling.

This year, in a case brought by companies that own power plants — which lose income when price spikes are avoided — a court ruled that the federal government overstepped its bounds in creating a market for turning down the dials.

In addition, FirstEnergy, a large Ohio-based electric utility, has filed a separate complaint that could further stymie the market.

The cases have put two important players in the energy market on a collision course: those companies that meet higher demand in peak hours by making more power, and those that find a way to reduce the demand.

The issue has gained the attention of lawmakers. Last week, Senator Martin Heinrich, a New Mexico Democrat, introduced legislation that would effectively reverse the May court decision. The law on which the court ruled was written for a different era, he said in a statement.

“Modernizing our electrical grid is central to becoming a nation that’s more energy-efficient and provides cost savings for everyone,” he said.

At the center of the conflict is an agency called the Federal Energy Regulatory Commission, which has authority over wholesale interstate transactions. Wanting to encourage efficient use of power plants, and avoid construction of those that are needed only a few hours a year, the commission laid out rules for how to line up the volunteers to be unplugged. The rules are somewhat similar to the way airlines deal with an overbooked flight: Ask for passengers to give up their seats in exchange for a payment.

Under the current system, which is called demand response, a company that rounds up those volunteers will bundle together a group of customers — some big office buildings, a shopping center or a few industrial plants — that can shut down a bank of elevators, reset their thermostats, and maybe even close a production line for a few hours.

Bulk power grid operators have become eager customers for these services, which can slice wholesale prices that utilities pay at peak hours from $1,000 a megawatt-hour down to $200, Mr. Goodman said.

But the arrangement has rankled power producers, by reducing peak prices on their busiest, most profitable days. In the end, the producers say, they need that income to survive.
In 2011, their patience ran out.

That year, the Electric Power Supply Association sued the federal commission, saying that demand response should be regulated by the states, not the federal government because the transactions are retail, not wholesale.

In May, the United States Circuit Court of Appeals in Washington sided with the association.

Now, FirstEnergy, in a complaint filed with the commission this spring, asserts that the demand-response arrangement — by only focusing on the demand side — does not recognize just how much it costs to build and operate a power plant. The company has a certain experience with power outages, having played a central role in the cascading blackouts that crippled a huge swath of the country from the Midwest up through Ontario and New York in August 2003.

“There’s a real difference between demand response and more valuable capacity that’s provided by fuel-diverse power plants that our communities rely upon, really around the clock,” said Donald A. Moul, vice president for commodity operations at FirstEnergy.

The complaint — which power industry experts say is unlikely to progress until federal officials decide whether to appeal the May ruling to the Supreme Court — involves a company called PJM Interconnection, a grid operator that smooths out the flow of electricity among 13 states in the Midwest. PJM said that its demand-response program saved more than $650 million in payments for energy in a single week in August 2013.

But the loss of that kind of income was painful to generators like FirstEnergy, which became like sidewalk ice-cream vendors whose customers were told to stay home on hot days.

If demand response continues to reduce prices, Mr. Moul said, it will lead to the closure of more conventional plants. That, in turn, would lead to a less reliable power supply.

“Instead of a generator sitting there ready to provide megawatts to the grid, you’ll have to rely on a retail, large commercial-industrial customer to shut off their load during some of these peak times,” he said.

But Jon B. Wellinghoff, the former chairman of the commission who championed using the approach in the wholesale markets, disagreed.

“These capacity auctions need to be not so rich that you have aging, polluting generating plants that should be retired still getting payments and not getting the right economic signals to get out of the market,” said Mr. Wellinghoff, now a partner at Stoel Rives law firm.

As the cases make their way toward resolution, demand-response providers are making plans in the event the rulings go against them.

“There are certainly alternatives being proposed,” said Gregg Dixon, senior vice president of marketing and sales at EnerNOC, which provides demand response for utilities and commercial electricity customers.

“The problem is that none of those alternatives are practical,” and they would still leave the market in a state of uncertainty while regulators devise new rules, he added.

J. Scott Perry, the chief executive of Vantage Commodities, a company that finances electricity retailers, said that the market for electricity had worked in an unusual way for a long time, until demand response came along.

“In every other market we’re in, if we buy gasoline or milk, if the price is too high, you buy something else or you buy less,” he said. “Why shouldn’t we have the same right in electricity?