

June 30, 2015

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Dear Mr. Walker:

Re: NERC 2016 Business Plan and Budget, Draft #1

The Independent Electricity System Operator (IESO) welcomes the opportunity to comment and provide recommendations on Draft #1 of the North American Electric Reliability Corporation's (NERC) 2016 Business Plan and Budget (BPB). The Draft 2016 BPB reflects a proposed budget increase of 3.2% from 2015, a preliminary 3.1% increase in 2017 and 0.7% decrease in 2018.¹ The IESO also provided written comments on the Draft 2016 Business Plan and Budget of the Northeast Power Coordinating Council, Inc. (NPCC). Since the NERC and Regional Entity BPBs are consolidated to reflect an Electric Reliability Organization (ERO)-wide view, and NERC and the Regional Entities share responsibilities to achieve the ERO Strategic Plan, some of what follows also includes recommendations for adoption across the ERO.

The IESO recognizes that NERC and the ERO are reaching a milestone of organizational maturity with the integration of risk management principles to set reliability priorities and closure of the majority of directives and projects leading to achieving standards "steady state" in 2015.² Indeed, it is about 10 years since the *Energy Policy Act of 2005* and the certification of NERC as the ERO. This milestone did not come without substantial burden on industry to support the industry-led consensus process necessary to achieve the robust reliability framework in place today. This state of maturity is widely recognized and supported as shown in the range of policy inputs to the NERC Board of Trustees in May 2015 and this was a common theme heard during the June 4, 2015 Federal Energy Regulatory Commission Reliability Technical Conference.

The IESO shares the view that the nature of the international, interconnected bulk power system is changing with new and emerging risks that are changing the nature of reliability. The IESO is committed to meeting these challenges; the elimination of coal-fired generation is just one area where these risks have already manifested in Ontario. At the same time, the IESO also operates

¹ As of June 20, 2015, NERC has not determined how stabilization reserves will be applied, compliance credits to Canadian entities have not been determined and applicable ERO-wide Net Energy for Load (NEL) has not been disclosed; IESO is not able to comment on projected assessments at this time.

² NERC 2016 Business Plan and Budget, Draft 1, Page 97

in an environment of significant cost constraint and is keenly aware of stakeholder and regulator expectations for increased operating efficiency while maintaining and enhancing reliability through focus on key reliability risks and priorities; having to absorb additional ERO costs (NERC and NPCC) directly leads to cuts to IESO programs and changing priorities.

1. NERC Program Spending Observations

The IESO is encouraged to see the standards “steady state” achievement and movement towards risk-based methods beginning to appear in the proposed Reliability Standards (both reduced budgeted expenses and full time equivalents or FTE) and the Compliance Enforcement (as shown by reduced FTE) Programs budgets. However, the IESO continues to have concerns that the enduring efficiency gains anticipated as part of the move towards “steady state”, the expected completion in 2015 and 2016 of major initiatives such as facilitating transition to CIPv5 and CIP-014, and adoption of risk-based methods, are not evident in the Draft 2016 BPB. The lack of enduring efficiency gains is clear given NERCs total budgeted FTE is forecast to remain flat from 2015 to 2016 (going from 192.3. to 192.48) and is forecast to remain flat through 2018.

Some observations related to proposed Program headcounts (measured as FTE) and Program spending:

- Although reduced workload in some Programs allowed for reduced FTEs in these Programs, the positions were reallocated to other Programs or Administrative Services areas, sometimes without a clearly defined need. For example, staff were reallocated to the Reliability Risk Management Event Analysis Program, which is budgeting for an increased budget in 2016 of about \$1.2M (27.9%) and an increase of 1.7 FTE (17.9%), without describing an incremental need from 2015 to 2016.
- The Electricity Sector Information Sharing and Analysis Center (ES-ISAC, excluding CRISP) is projecting an under budget variance in 2015 primarily from reduced Personnel costs (approximately \$200K and 1.5FTE). It is difficult to determine given available information if this is due to unfilled vacancies. If ES-ISAC continues to meet its obligations under the current staff complement, NERC should reduce the budget to reflect this capability. It is understood that there could be budget impacts depending on the actions taken to address recommendations in the ESCC strategic review,³ but it is not appropriate at this time to hold these open positions until such time as the need is defined and approved.
- Net reallocations of 4.67 FTEs from Programs results in a proposed offsetting increase of 4.85 FTE in 2016 for Administrative Services. This maintains the trend for increased Administrative Services budgeted FTEs from 52.8 in 2013 to 72.4 in 2016, while at the same time that budgeted Programs FTEs decreased from 133.5 to 120.1. The rationale given for Program staff reallocations in 2016 is reduced workload, but the corresponding incremental need in the Administrative Services area is not clearly identified.

³ NERC 2016 Business Plan and Budget, Draft 1, Page 11

- NERC expects the successful implementation of Risk-Based Compliance Monitoring and Enforcement Program (CMEP, formerly RAI) and substantial completion of CIPv5 transition in 2016. NERC has identified these significant initiatives as drivers of incremental costs in the Compliance Assurance (CA) Program and across multiple Programs in prior BPBs, and so the IESO anticipated the CA Program would experience reduced proposed spending in 2016 and thereafter. It is possible to infer that the proposed CA Program budget increase (\$1.9M, 33.4%) is the result of 3.5FTE staff reallocated from ES-ISAC⁴, but given the information available and winding down of significant initiatives, it's not clear how NERC will realize any of the anticipated enduring reduced Program spending.
- The 2016 Budget reflects that Compliance Enforcement (CE) Program staff were reallocated to other departments during 2015 due to reduced workload (1.6 FTE), but there is no corresponding decrease in CE Program Personnel costs, as would be expected. Again, with Risk-Based CMEP implementation expected complete in 2016, the IESO anticipates NERC would experience additional Program efficiencies starting in 2016.

2. Review and Benchmarking ERO Programs and Priorities

With NERC and the ERO reaching the organizational maturity milestone, it is an appropriate time for NERC management to lead an ERO-wide review and benchmarking of spending on Programs and priorities. The objective of a review would be to ensure NERC and Regional Entity spending for all Programs and priorities is consistent with regulatory and delegated responsibilities, and is proportional relative to strategic priorities and emerging reliability risks. Examples of areas where further study would be informative include:

- Regional Entity Division budgeted spending on Reliability Standards Programs ranges from 0% to 9.8% across each of the Regional Entities.
- Regional Entity Division budgeted spending on Situation Awareness and Infrastructure Security (SAIS) Programs ranges from 0% to 10.2% across each of the Regional Entities.
- NERC's Reliability Standards Program budget is starting to reflect the "steady state" achievement with a projected decrease of about 19% in 2016 but that trend is not consistently reflected at the Regional Entity level.⁵

These are examples of areas where further study could identify opportunities for greater efficiency across the ERO. Such a review should include capital and non-capital spending and all major cost categories.⁶ This ERO-wide review would provide Regional Entity Management, their Boards of Directors, and stakeholders with valuable benchmarking on cost drivers, trends, and enhanced annual ERO performance assessment capability.

⁴ This includes Personnel Expenses and increased allocation of Indirect Expenses.

⁵ Based on Draft 2016 Regional Entity Business Plans and Budgets, Reliability Standards Program budgets are projecting decreases of 23% to increases of 76% and a combined 3% increase in budgets.

⁶ This includes all Expense categories and subcategories broadly described as Personnel, Meetings, and Operating Expenses in NERC and Regional Entity Business Plans and Budgets

3. Delay planned IT infrastructure investments

IESO recognizes that the ERO is in the midst of a significant IT infrastructure investment program with shared tools across NERC and the Regional Entities (known as the ERO Enterprise IT Application Strategy). However, there is still insufficient visibility to member entities of the implementation costs/investment measured against achievement of projected benefits and expected outcomes (efficiencies and realized savings relative to costs, risks managed, etc.)

Starting in 2015, NERC and the Regional Entities propose to proceed with implementing a new Document Management System⁷ and will continue updating and refreshing other tools through 2016. The IESO recommends NERC examine and report back to stakeholders the business risks, costs and benefits to extend the life of existing tools and processes and to delay further effort to implement proposed all new, replacement or refreshed tools, including the new Document Management System (entirely, or certain lower priority modules) and other tools investment planned through 2018.

4. Budget implications of ESCC Strategic Review of ES-ISAC

The IESO understands the Electricity Subsector Coordinating Council's (ESCC) Report on the Strategic Review of ES-ISAC is nearing completion and that there may be NERC budget impacts depending on the actions taken to address recommendations.⁸ The IESO offers the following related to possible actions that may be taken to respond to ESCC recommendations:

- The IESO recommends that NERC commit to fund any potential capital or operating budget needs related to actions taken through the existing overall NERC budget envelope (capital and operating budgets, excluding reserves). NERC should carefully weigh the relative reliability risks of all NERC priorities against the relative risks of any ESCC recommendations to identify trade-offs and alternative funding opportunities before committing to additional budgeted funding in 2016 or future years. This includes eliminating or scaling back current ES-ISAC activities that are no longer meeting the ES-ISAC renewed strategic needs. Further, related to the IESO's recommendation below, NERC should consider piloting an enhanced stakeholder capital planning process along with any new capital investments related to Strategic Review.
- The ES-ISAC is widely recognized and supported in its role as the ISAC for the Electricity Subsector. The IESO continues to support NERC's ongoing role in governance of the ES-ISAC and recognizes NERC's efforts to enhance segregation of the function from other NERC Programs. ES-ISAC registrants include NERC member entities and non-NERC entities, and the IESO encourages the ES-ISAC effort to add non-NERC

⁷ Due to unbudgeted expenses related to the Document Management System implementation, NERC applied to FERC in May 2015 to use operating reserves greater than \$500K for "unforeseen contingencies" to proceed with implementation in 2015.

⁸ NERC 2016 Business Plan and Budget, Draft 1, Page 11. The Report is expected to be publicly available by Q3 2015.

registrants to continue enhancing the value of ES-ISAC member services. Coinciding with the ESCC Strategic Review, the IESO recommends that it is an appropriate time to examine the ES-ISAC funding model to ensure it is aligned with membership and corresponding services and benefits.⁹

5. Process Improvements

The IESO continues to appreciate and support NERCs on-going efforts to refine the BPB document and all Regional Entities adopting a similar template. Consistency across the ERO is essential to ensure the BPB is an effective communication tool. Draft #1 of the 2016 BPB continues to reflect that and the IESO looks forward to additional information in Draft #2. The IESO offers these additional recommendations for ongoing improvements to the BPB document and stakeholder review process:

- NERC is budgeting increased Direct Expenses and relatively flat staffing levels in the Reliability Assessments and Performance Analysis (RAPA) Program for 2016 (with a proposed \$10.4M budget, RAPA will be the highest funded NERC Program, excluding ES-ISAC CRISP). At the same time, NERC acknowledges, as in prior years, that actual business needs are undecided as the “RISC and ERO continue to refine the efforts to establish a multi-year perspective addressing the key reliability initiatives, the specific projects and goals for 2016 (and potentially into 2017 and 2018) will be more clearly defined.”¹⁰ This uncertainty significantly reduces the value of the budget as a communication tool and makes substantive review or comment difficult. The IESO recommends NERC look at enhancing RISC and ERO project and Program prioritization timelines to align with the BPB schedule.
- The annual audited financial statements report NERC spending by financial statement category. Stakeholders typically review the NERC and Regional Entity BPBs on a Program basis. Currently, NERC and Regional Entity BPBs show the current year approved Budget by Program, the current year projection (which, based on Q1 results, may not be reliable), and the subsequent year proposed Budget. It would be very informative for stakeholders if the draft BPB also included prior year actual Program spending based on the prior year audited results. Having this information, stakeholders would be better able to assess the proposed Budget while also assessing budget development performance (e.g. trends on significant over or under variances), validity of year-to-year assumptions, and conduct trending analysis using actual results.
- Starting with the 2016 BPB, the IESO recommends NERC use enhanced capital project implementation reporting to provide member entities on an ongoing basis, analysis of ERO investments measured against achievement of benefits as defined at the outset of

⁹ This includes all ES-ISAC budgeted costs, including CRISP costs shared with non-CRISP participants, but does not include the portion of CRISP funded by direct CRISP participants. As CRISP is a voluntary program, the IESO continues to support the principle adopted by NERC in 2015 that CRISP is primarily funded by voluntary participants.

¹⁰ NERC 2016 Business Plan and Budget, Draft 1, Page 46. A similar caveat is expressed on Page 50 and on the corresponding pages 29 and 32 of the Final 2015 Business Plan and Budget.

the projects (including all capital projects whether part of the ERO Enterprise IT Application Strategy or other approved capital spending, and include all capital and related non-capital implementation and ongoing costs such as Personnel, Consultants and Contracts, and Meetings). This would also include supplementing the capital budget disclosures in the BPB to include the expected qualitative and quantitative benefits associated with the related business cases, and year-to-year tracking of changes to scope and deliverables.

- The IESO recommends NERC and the ERO enhance capital planning and budgeting processes to secure greater stakeholder understanding and buy-in of the business case and merits of all new capital programs. This could include leveraging industry experts through the pre-budget period to define, document and communicate business needs and requirements (this could have dual benefits of ensuring the tools are optimized to suit NERC and industry needs, while also creating opportunities for reduced up front consulting costs).
- For the 2015 BPB, along with copies of stakeholder comments received by NERC and in support of 2014-2016 ERO Strategic Plan Goal 5,¹¹ NERC published on its website an Accountability Matrix that included all NERC responses to stakeholder comments. This is a very welcome initiative and the IESO is pleased that NERC has kept a similar goal and “key deliverable” for the 2015-2017 ERO Strategic Plan approved by the Board of Trustees in November 2014. Starting with the 2016 BPB year and in support of the ERO Strategic Plan, the IESO recommends that NERC require all Regional Entities to prepare a similar Accountability Matrix and that these Matrices be published on the NERC website along with copies of all stakeholder comments received on Regional Entity BPBs.

Once again, the IESO appreciates the opportunity to comment and to provide these recommendations to NERC on the Draft 2016 BPB and for ongoing improvements to the ERO BPB documents and stakeholder review processes.

Sincerely,



Signed

Michael Lyle

Vice-President

Planning, Law and Aboriginal Relations

IESO

cc: Bruce Campbell, President and CEO, IESO
Any Josephson, Budget Analyst, NERC

¹¹ Goal 5: Improve transparency, consistency, quality, and timeliness of results; operate as a collaborative enterprise; and improve efficiencies and cost-effectiveness.