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## **I. INTRODUCTION**

The North American Electric Reliability Corporation (“NERC”) submits this response to the *Motion to Intervene, Motion to Consolidate, and Comments* filed by the Edison Electric Institute (“EEI”) on February 22, 2013 in Docket Nos. FA11-21-000 and RR12-13-000. EEI’s filing was in response to NERC’s *Compliance Filing in Response to Paragraph 30 of November 2, 2012 Commission Order*, filed February 1, 2012, in Docket No. FA11-21-000, in which NERC submitted the “NERC Written Criteria for Determining Whether an Activity is Eligible to Be Funded Under Section 215 of the Federal Power Act” (“NERC Written Criteria”).<sup>1</sup> As directed by P 30 of the 2013 Budget Order, the NERC Written Criteria were developed and submitted in response to Recommendation 37 of the Final Audit Report in this docket.<sup>2</sup>

## **II. RESPONSE TO MOTION TO INTERVENE**

Assuming that the Commission allows interventions in Docket No. FA11-21-000, NERC has no objection to EEI’s request to intervene in that docket.

## **III. RESPONSE TO MOTION TO CONSOLIDATE**

NERC disagrees with EEI’s request that Docket No. FA11-21-000 be consolidated with Docket No. RR12-13-000, which was the proceeding for review and approval of NERC’s 2013 Business Plan and Budget. The 2013 Budget Order approved the 2013 Business Plans and Budgets of NERC and the Regional Entities and the proposed assessments to fund the approved budgets, and NERC and the Regional Entities are now operating under their Commission-approved 2013 Business Plans and Budgets. No requests for rehearing of the 2013 Budget Order were filed. Although the Commission added Docket No. FA11-21-000 to the caption of the 2013 Budget Order, the Commission expressly stated “Not Consolidated” in the caption.

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<sup>1</sup> The November 2, 2012 Commission Order is *North American Electric Reliability Corporation, Order Accepting 2013 Business Plan and Budget of the North American Electric Reliability Corporation and Ordering Compliance Filing*, 141 FERC ¶ 61,086 (2012) (“2013 Budget Order”).

<sup>2</sup> The Final Audit Report was issued by the Office of Enforcement, Division of Audits on May 4, 2012 in Docket No. FA11-21-000. *Performance Audit of the North American Electric Reliability Corporation for Budget Formulation, Administration, and Execution* (“Final Audit Report”).

Further, in the portion of the 2013 Budget Order addressing Recommendation 37 of the Final Audit Report, the Commission clearly stated:

As discussed above, EEI and APPA submitted comments relating to Audit Report recommendations 37 and 38, concerning the statutory nature of NERC's activities funded under FPA section 215. These concerns touch on the identification and funding of NERC's statutory functions as the ERO. Given that NERC and Office of Enforcement staff appear to generally agree on a process for resolving these issues, we address those two recommendations here **in order to ensure that these issues are promptly resolved for reflection in the 2014 budget.**<sup>3</sup>

The Commission also clearly stated:

We are not consolidating the two proceedings in this order and, therefore, **the compliance filing directed herein should be submitted to the Commission in the Performance Audit proceeding in Docket No. FA11-21-000.**<sup>4</sup>

As directed by the Commission, NERC filed its compliance filing to P 30 of the 2013 Budget Order only in Docket No. FA11-21-000.<sup>5</sup>

EEI is also incorrect in stating that NERC's compliance filing and the NERC Written Criteria "grew out of the concerns presented in" EEI's comments filed in Docket No. RR12-13-000.<sup>6</sup> This is mere bootstrapping. EEI elected to gratuitously file comments in Docket No. RR12-13-000 relating to Recommendations 37 and 38 from the Final Audit Report in Docket No. FA11-21-000; however, NERC developed the NERC Written Criteria specifically in response to Recommendation 37 of the Final Audit Report. NERC had committed to develop

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<sup>3</sup> 2013 Budget Order at P 29 (emphasis added).

<sup>4</sup> *Id.* at P 32 (emphasis added).

<sup>5</sup> EEI states that NERC filed its Compliance Filing in both Docket No. FA11-21-000 and Docket No. RR12-13-000. EEI filing at 2-3. EEI's statement is incorrect. NERC filed the Compliance Filing only in Docket No. FA11-21-000. EEI is apparently referring to the first paragraph on page 1 of NERC's Compliance Filing; however, the reference there to both docket numbers is to the fact that the 2013 Budget Order was issued in both dockets. It was not a statement that the Compliance Filing was being submitted in both dockets.

<sup>6</sup> EEI Filing at 4.

such criteria in response to Recommendation 37 well before Docket No. RR12-13-000 was even opened.<sup>7</sup>

The only other reason EEI offers for consolidation is that “the Commission should therefore consolidate these proceedings so that these intertwined issues can proceed upon a single procedural path.”<sup>8</sup> However, there are no “intertwined issues” in Docket Nos. FA11-21-000 and RR12-13-000. Docket No. RR12-13-000 is concluded, and the NERC and Regional Entity 2013 Business Plans and Budgets and assessments have been approved. Docket No. FA11-21-000 is the proper proceeding for addressing – and provides a “single procedural path” for addressing – NERC’s compliance with Recommendation 37. As noted above, the Commission directed NERC to develop the NERC Written Criteria in response to Recommendation 37 and to file them in Docket No. FA11-21-000 by February 1, 2013 in order to ensure that these issues are promptly resolved “**for reflection in the 2014 budget.**”<sup>9</sup>

In the comments it filed with the Commission in Docket No. RR12-13-000 on NERC’s proposed 2013 Business Plan and Budget, EEI was fully on board with this plan.<sup>10</sup> EEI stated in at least five different places in that filing that it fully supported approval of NERC’s proposed 2013 Business Plan and Budget, and that it “does not at this time contest whether or not any of the activities listed in the NERC budget are statutory.”<sup>11</sup> NERC was deeply appreciative of EEI’s undiluted support for approval of the 2013 Business Plan and Budget. Further, in that filing, EEI quoted approvingly, from NERC’s initial brief on the disputed audit issues in Docket No. FA11-21-000, NERC’s proposal to develop criteria through a stakeholder process in 2012

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<sup>7</sup> See *Initial Brief of the North American Electric Reliability Corporation* in Docket No. FA11-21-000, filed July 19, 2013, at 99 (in response to Recommendation 37 of the Final Audit Report, NERC proposed to “Establish written criteria for determining whether an activity is a statutory activity and should be funded under section 215 through an open and transparent process initiated by NERC”).

<sup>8</sup> EEI Filing at 4.

<sup>9</sup> 2013 Budget Order at P 29 (emphasis added).

<sup>10</sup> *Motion to Intervene and Comments of the Edison Electric Institute*, filed September 28, 2012 in Docket No. RR12-13-000.

<sup>11</sup> *Id.* at 1, 3, 4, 10 and 11.

and 2013 to be completed in sufficient time to use the criteria in preparing NERC's 2014 business plan and budget filing, stated its intention to participate in this initiative, and stated that it "envision[ed] that NERC will apply these criteria and any accompanying prioritization processes when developing its 2014 business plan and budget, subject to any Commission order on the criteria filing after notice and opportunity for public comment."<sup>12</sup>

#### **IV. RESPONSE TO COMMENTS**

##### **A. Request for Leave to Respond to EEI Comments**

NERC's Compliance Filing in this docket was a compliance filing in response to a Commission directive and was not an "application, complaint, petition, order to show cause, notice of tariff or rate examination, or tariff or rate filing."<sup>13</sup> Nonetheless, for purpose of this response, NERC treats EEI's comments as a "protest" pursuant to §385.211(a) and, therefore, to the extent necessary, requests leave to file the following brief response to EEI's comments. The Commission's rules do not permit the filing of answers to protests, unless otherwise ordered;<sup>14</sup> however, the Commission has granted leave to file such answers if they will clarify the issues in dispute, ensure a complete and accurate record, or otherwise provide information that will assist the Commission in its decision-making process.<sup>15</sup> To ensure that the Commission has complete and accurate information upon which to make a decision, NERC requests leave to submit a response to EEI's comments.

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<sup>12</sup> *Id.* at 9-10.

<sup>13</sup> 18 C.F.R. §385.211(a)(1).

<sup>14</sup> *See* 18 C.F.R. §385.213(a)(2).

<sup>15</sup> *See, e.g., San Diego Gas & Electric v. Sellers of Energy and Ancillary Services*, 108 FERC ¶ 61,219, at P14, n. 7 (2004) (answer was accepted as it "provided information that assisted [the Commission in its] decision-making process"); *Michigan Electric Transmission Co.*, 106 FERC ¶ 61,064, at P 3 (2004) (the permitted answer "provides information that clarifies the issues"); *North American Electric Reliability Corporation*, 116 FERC ¶ 61,062, at P 24 (2006) (reply comments of NERC and others accepted "because they have provided information that assisted us in our decisionmaking process"); *North American Electric Reliability Corporation*, 117 FERC ¶ 61,091, at P 18 (2006) (same); *North American Electric Reliability Corporation*, 119 FERC ¶ 61,248, at P 6 (2007) (same); *North American Electric Reliability Corporation*, 127 FERC ¶ 61,209 (2009), at P 5 (same).

## **B. NERC Response to EEI Comments**

Without descending into the minutiae of EEI's comments, NERC offers three overarching points in response.

**First**, EEI has misapprehended the task assigned to NERC in Recommendation 37, and the purpose of the NERC Written Criteria. NERC was not assigned to define the scope of FPA §215. Recommendation 37 was based on statements in the Final Audit Report that “NERC did not have written criteria to determine whether activities should be funded under the section 215;” that “NERC has not developed any policies, procedures, processes or practices (i.e., criteria) to guide its staff in the types of activities permissible in section 215” and had not established “written criteria to determine whether its activities are statutory;” that “NERC had not developed project specifications that laid out the statutory goals to be accomplished by [new projects] with sufficient clarity” and “had no clear written criteria;” and that “NERC needs to establish and operate under formal criteria that ensure all of its program activities that are funded pursuant to FPA section 215 are statutory.”<sup>16</sup> These observations by Audit Staff were the basis for Recommendation 37 in the Final Audit Report that NERC should “establish written criteria for determining whether a reliability activity should be funded under section 215 through coordination and discussion with Commission staff and stakeholders.” With this origin of Recommendation 37 in mind, and also keeping in mind that this proceeding is a financial and budget performance audit, the NERC Written Criteria have two specific purposes, as stated in NERC's Compliance Filing:

- The NERC Written Criteria will be used by NERC for internal purposes to determine whether proposed reliability activities fall within FPA §215 and therefore should be eligible to be funded through the FPA §215 funding mechanism. If new reliability activities are proposed internally during development of NERC's annual budget, the written criteria should be applied by management to determine if the proposed activities can be included in the budget as statutory activities; if new activities are proposed internally or need to be undertaken during the budget year, the written criteria should be

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<sup>16</sup> Final Audit Report at 70, 75, 77 and 78.

used by management to determine if the activities can be undertaken using FPA §215 funding.

- The NERC Written Criteria will be used in NERC's annual business plan and budget filings as a basis for demonstrating that NERC's proposed activities are statutory and should be funded through the FPA §215 funding mechanism.<sup>17</sup>

In short, the written criteria are NERC's criteria to be used in evaluating, for internal approval and business planning and budgeting purposes, whether proposed reliability activities are FPA §215 activities.

Further, it is not the purpose of NERC's Compliance Filing or this proceeding to determine if specific current or proposed activities should be funded through the FPA §215 funding mechanism. Neither Recommendation 37 nor the 2013 Budget Order directs NERC to make this determination. To the contrary, the Commission expressly stated in the 2013 Budget Order: "we are not requiring NERC to apply its proposed criteria to all of its activities as part of its February 1, 2013 compliance filing."<sup>18</sup> Rather, those determinations will be made in the annual business plan and budget development process and, if necessary, in business plan and budget proceedings, as provided in the revised Recommendation 38 that the Commission adopted in the 2013 Budget Order:

In its annual business plan and budget filings, [NERC should] provide an explanation as to why the proposed activities to be undertaken by each program area for the budget year are statutory, including, at a minimum: a description and the purpose of the major activities to be undertaken by each program area and an explanation for why the activity is a statutory activity.<sup>19</sup>

EEI seeks in its comments to argue whether specific individual activities should be funded through the FPA §215 funding mechanism, but this is not the proceeding in which to make those determinations.

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<sup>17</sup> See NERC Compliance Filing at 5-7.

<sup>18</sup> 2013 Budget Order at P 31.

<sup>19</sup> See 2013 Budget Order at P 31 and NERC Compliance Filing at 5.

Nor is it the purpose of the development of the NERC Written Criteria, or of this proceeding, to prioritize NERC's programs and activities and to eliminate specific activities that may be regarded as less effective and cost-beneficial in maintaining and enhancing the reliability of the Bulk Power System. As NERC made clear in its Compliance Filing:

[I]n neither of the above-described uses of the written criteria will application of the criteria be the final determinant of whether NERC should undertake proposed activities. The written criteria will only be used to evaluate whether activities are statutory activities and can be funded through the FPA §215 funding mechanism. Assuming activities are determined to be statutory activities, management must also determine that the activities are or will be an efficient and productive use of resources in carrying out the ERO's statutory responsibilities and achieving its objectives.<sup>20</sup>

To the extent that (1) the statutory nature, and (2) the benefits and cost-effectiveness of specific proposed activities, are not thoroughly vetted through NERC's annual internal strategic planning and business plan and development processes and through the stakeholder input phase of NERC's annual strategic plan and business plan and budget development, the business plan and budget dockets at the Commission provide the forum for evaluating whether the NERC Written Criteria have been appropriately applied and for contesting and determining whether particular activities are a worthwhile expenditure of resources and should be undertaken. The purpose of the NERC Written Criteria, as directed by Recommendations 37 and 38 and the 2013 Budget Order, is to provide a specific, written framework for determining, both in NERC's internal business planning and budgeting activities and, if necessary, in the formal business plan and budget dockets, whether specific proposed activities can be funded through the FPA §215 funding mechanism.<sup>21</sup>

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<sup>20</sup> NERC Compliance Filing at 8.

<sup>21</sup> One of EEI's specific concerns is NERC's activity as the ES-ISAC, particularly the interplay between the information-gathering and dissemination activities of the ES-ISAC and the operation of the Reliability Standards Development and Compliance Monitoring and Enforcement Programs. EEI Comments at 27-29. NERC notes that the operation and functions of the ES-ISAC are the subject of a separate agreed recommendation, Recommendation 39, in the Settlement Agreement for this proceeding that was approved by the Commission in *North American Electric Reliability Corporation, Order Approving Settlement Agreement*, 142 FERC ¶ 61,042 (2013).

**Second**, as one outcome of this performance audit proceeding, NERC already has controls in place with respect to expenditures on new activities arising between business plan and budget cycles, including procedures to ensure that significant unbudgeted expenditures on major activities receive Commission approval. NERC developed and adopted a Working Capital and Operating Reserve Policy (“Reserves Policy”) which was included in its 2013 Business Plan and Budget. The Reserves Policy requires that working capital and operating reserves be budgeted and maintained in, and expended from, specific categories for specific purposes. The Reserves Policy also creates a hierarchy of management and Board controls and approval requirements, depending on the amount of the expenditure, on proposed expenditures from reserves. Further, the Reserves Policy establishes specific procedures and management approval requirements for the reallocation of funds between or among budget areas during the course of the year. Finally, with respect to expenditures of \$500,000 or more from Operating Reserves, the Settlement Agreement that the Commission has approved expressly requires:

NERC will file for Commission review and approval Board-of-Trustees-approved proposals to expend \$500,000 or more from operating reserves designated for “unforeseen contingencies” (as that term is defined in NERC’s Working Capital and Operating Reserve Policy (Reserve Policy)). Each such filing will include supporting materials in sufficient detail to justify the proposed expenditure. The filing will be deemed approved if the Commission does not act on it or issue a tolling order extending the time for Commission action within thirty days of the filing date.

The Parties agree that this requirement for Commission review and approval is triggered if any amount allocated from the unforeseen contingencies account of operating reserves plus any amount re-directed from previously budgeted funds is, in the aggregate, \$500,000 or more for any one specific project or major activity in a program area.<sup>22</sup>

**Third**, contrary to EEI’s characterizations, all of the eleven NERC Written Criteria are

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<sup>22</sup> Settlement Agreement at 3. The Settlement Agreement also requires that NERC will file for Commission review and approval any proposed revisions to the Reserves Policy that would alter any of its definitions of the terms “working capital reserves,” “operating reserves,” “known contingencies” or “unforeseen contingencies,” or that would change the Reserve Policy’s requirement that all excess funds be added to the unforeseen contingency operating reserves and expended in accordance with the Reserve Policy’s unforeseen contingency guidelines. *Id.* at 4.

rooted in §215 of the FPA. NERC acknowledges that it could have truncated the eleven major criteria into a smaller number of major criteria, but it chose to separate the criteria into a larger number of major categories so that the activities falling under each major criterion can be more readily identifiable to a major criterion.

However, the fact that NERC has more rather than fewer criteria does not mean that any of the criteria are not rooted in §215. Each of Criteria I through VII is expressly based on one or more of the text of §215; the text of the Commission's Part 39 regulations which have been issued specifically under the authority of, and to implement, §215; the text of a Commission order, issued under authority of §215, directing NERC to take specific actions or implement specified activities as the Electric Reliability Organization; or NERC's Rules of Procedure that are required by §215 to be approved, and have been approved, by the Commission pursuant to the criteria specified in §215 and the Commission's Part 39 regulations issued pursuant to §215.

Criteria VIII, IX and X are not expressly based on one or more of the aforementioned §215 sources, but Criterion VIII encompasses audits conducted by the Commission of the performance by NERC and the Regional Entities of their §215 responsibilities; Criterion IX encompasses work by committees, subcommittees and working groups on activities encompassed by one or more of the other criteria; and Criterion X encompasses analysis and evaluation of activities encompassed by one or more of the other criteria for the purpose of identifying means of performing the activities more efficiently and effectively. (That EEI objects to Criterion X as a statutory criterion is particularly odd given EEI's insistence that NERC needs to focus on prioritizing its activities and performing them with greater efficiency.)

Finally, Criterion XI encompasses NERC's overhead or administrative functions that are necessary to operating the organization. These activities and costs by definition are not directly assignable or attributable to specific individual statutory activities; if they were, they would not be classified as overhead/administrative costs, but rather would be budgeted and recorded

directly under the applicable statutory activity. Further, as the Commission is well aware and NERC is certain EEI is well aware, NERC allocates its overhead/administrative costs to its direct statutory programs, through an allocation procedure the Commission has consistently accepted, just like “a centralized service company in a public utility holding company system must allocate the costs of the various overhead and administrative services it provides to the various companies in the holding company system that benefit from those services using an appropriate cost allocation methodology.”<sup>23</sup> Additionally, Criterion XI expressly states that “Should NERC perform any non-FPA §215 activities, the costs of governance and administrative/overhead functions must be appropriately allocated,” so EEI’s suggestion that NERC needs to do that is superfluous.<sup>24</sup>

Moreover, contrary to EEI’s assertions, none of the NERC Written Criteria are based on the fact that the Commission approved a particular activity in one or more previous budget orders.<sup>25</sup> As NERC stated in its Compliance Filing, “NERC has not attempted to develop and justify the written criteria based solely on the Commission’s approval of the activities that fall within the criteria as statutory activities in NERC’s previous annual business plans and budgets.”<sup>26</sup> At the same time, however, for purposes of developing the written criteria, NERC is not in a position to ignore Commission final orders, issued under the authority of §215, that have directed or approved activities as statutory activities.

Notwithstanding the foregoing responses to the EEI comments, NERC emphasizes that it is fully in agreement with EEI that it is critically important for NERC to continue to focus on prioritizing its activities and resources towards those areas that are the most important for maintaining and improving the reliability of the Bulk Power System, eliminating lower-value

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<sup>23</sup> EEI Filing at 18-19.

<sup>24</sup> *Id.* at 19.

<sup>25</sup> EEI Filing at 8-11.

<sup>26</sup> NERC Compliance Filing at 13.

activities, and performing all of its activities in a more efficient, efficacious and cost-effective manner. NERC looks forward to continuing to work with EEI and other stakeholders on these efforts through the NERC strategic planning process, the business plan and budget development process, and other initiatives.

**V. CONCLUSION**

NERC respectfully requests that the Commission accept this response to the EEI Filing and take it into consideration in its determinations in this proceeding.

Respectfully submitted,

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**CERTIFICATE OF SERVICE**

I hereby certify that I have served a copy of the foregoing document upon all parties listed on the official service lists compiled by the Secretary of the Commission for Docket No. RR12-13-000 and Docket No. FA11-21-000.

Dated at Chicago, Illinois, this 6th day of March, 2013.

/s/ Owen E. MacBride

Owen E. MacBride

Attorney for North American  
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