

June 13, 2006

VIA E-FILING

Ms. Magalie R. Salas
Secretary
Federal Energy Regulatory Commission
888 First Street, N.E.
Washington, D.C. 20426

Re: *North American Electric Reliability Council and North American
Electric Reliability Corporation, Docket No. RR06-1-000*

Dear Ms. Salas:

Yesterday, the North American Electric Reliability Council and the North American Electric Reliability Corporation (jointly “NERC”) submitted, via e-filing, a Motion for Leave to File Reply Comments and Reply Comments (“Reply Comments”), in the above-captioned docket. Upon further review, the Reply Comments were discovered to contain a number of formatting and technical errors. While none of these errors is substantive in nature, NERC is hereby submitting a corrected version of the Reply Comments. Please replace the version filed yesterday with the version submitted concurrently with this transmittal letter.

Thank you for your assistance in this matter. Please contact the undersigned if you have any questions.



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Respectfully submitted,

/s/ Debra Ann Palmer

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Enclosure
cc (w/enc.): All parties on official service list

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UNITED STATES OF AMERICA
Before the
FEDERAL ENERGY REGULATORY COMMISSION

**NORTH AMERICAN ELECTRIC)
RELIABILITY COUNCIL and)
NORTH AMERICAN ELECTRIC)
RELIABILITY CORPORATION)**

Docket No. RR06-1

**MOTION FOR LEAVE TO FILE REPLY COMMENTS
AND REPLY COMMENTS OF NORTH AMERICAN
ELECTRIC RELIABILITY COUNCIL AND NORTH
AMERICAN ELECTRIC RELIABILITY CORPORATION**

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June 13, 2006

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Appendix A

Appendix B

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

NORTH AMERICAN ELECTRIC)	
RELIABILITY COUNCIL and)	Docket No. RR06-1-000
NORTH AMERICAN ELECTRIC)	
RELIABILITY CORPORATION)	

**MOTION FOR LEAVE TO FILE REPLY COMMENTS AND
REPLY COMMENTS OF
NORTH AMERICAN ELECTRIC RELIABILITY COUNCIL and
NORTH AMERICAN ELECTRIC RELIABILITY CORPORATION**

I. Request for Leave to File Reply Comments

The North American Electric Reliability Council (“NERC-Council”) and the North American Electric Reliability Corporation (“NERC-Corporation”) (jointly referred to herein as “NERC”), hereby move for leave to submit these reply comments to the more than 40 comments that were filed on NERC’s application for certification as the electric reliability organization (“ERO”) under Section 215 of the Federal Power Act (“FPA”).¹ While reply comments have not been specifically requested by the Commission, no party will be prejudiced by NERC’s submittal of these reply comments, and they will aid the Commission in the resolution of the issues before it in this proceeding. Further, in this filing NERC is proposing modifications to certain components of its application in response to comments received by the Commission. Therefore, NERC requests that the Commission include these reply comments in the record of this proceeding and consider these reply comments in reaching its decision herein.

II. Overview

NERC notes at the outset that virtually all of the commenters supported certification of NERC-Corporation as the ERO. In fact, NERC does not believe any commenters categorically

¹16 U.S.C. § 824o.

recommended denial of the application, although a few commenters stated that the Commission's certification of NERC as the ERO should be conditioned on implementation of specific requirements. However, a number of commenters, while supporting certification of NERC as the ERO, did propose changes or additions to NERC's proposed Bylaws, Rules of Procedure ("ROP") or pro forma Regional Delegation Agreement ("RDA"), or suggested the imposition of other conditions or requirements.

NERC believes that it would be worthwhile to outline for the Commission the process NERC followed in developing its certification application and its proposed Bylaws, ROP and pro forma RDA. The development of NERC's application included an extensive stakeholder participation process. When passage of the ERO legislation appeared likely, NERC appointed a Post-Legislation Steering Committee ("PLSC") consisting of representatives from the NERC-Council Stakeholders Committee, from each of the NERC-Council standing committees, and from key industry organizations,² along with two Trustees, reporting to the NERC Board of Trustees, to oversee the development of NERC's application for certification. The PLSC began its work even before the legislation was enacted, as it helped to shape the positions NERC took in the workshops on an international ERO sponsored by the Bilateral Electric Reliability Oversight Group held on December 8, 2004 and April 19 and June 22, 2005. Once the ERO legislation was enacted, the PLSC appointed task groups in four key areas: membership, funding, compliance penalties and sanctions, and regional delegation. These task groups were staffed by a broad cross-section of industry participants. The reports and recommendations of the task

²Industry organizations represented on the PLSC included the American Public Power Association, the Canadian Electric Association, the Edison Electric Institute, the Electric Consumers Resource Council, the Electric Power Supply Association, the National Association of Regulatory Utility Commissioners and the National Rural Electric Cooperative Association.

groups were delivered to the NERC-Council Stakeholders Committee and Board of Trustees in late 2005.

NERC posted three drafts of its certification application, Bylaws, and ROP on its website for public comment. These postings were made on December 16, 2005, January 27, 2006 and March 27, 2006. In the aggregate, approximately ninety sets of comments were received in response to these postings. NERC revised the documents after each posting period to take into account and reflect comments received on the drafts. The certification application that NERC filed on April 4, 2006 reflected this substantial stakeholder comment and represents the best judgment of NERC and its independent Board as to how to comply with the requirements of Section 215 of the FPA and the Commission's ERO rule.³

The comments the Commission received on NERC's application mirror NERC's experience as it posted drafts of its application for public comment. Often more than one reasonable approach was suggested to resolving an issue or complying with a statutory provision. There were few issues on which all commenters were in complete agreement on a single approach. NERC was not surprised by any of the comments on its application that were filed with the Commission – by and large, all of these comments were voiced during the public comment process on the application drafts.

NERC acknowledges that some of the issues raised in the comments submitted on the application may benefit from further consideration through the NERC stakeholder processes. The Bylaws, ROP and other documents NERC has submitted for approval as its "ERO Rules" are not being set in stone forever. To the contrary, there will be opportunities for further debate and discussion among NERC's membership and other stakeholders, to test particular

³18 C.F.R. Part 39.

alternatives, and to make changes in the ERO Rules reflecting experience gained in operating under and working with the initial set of ERO Rules. The Commission has also provided a formal mechanism to consider changes to the ERO's rules and programs, by requiring the ERO to submit a self-assessment of its performance three years after certification. The self-assessment is to include recommendations from stakeholders for improvements to the ERO's operations, activities, procedures and oversight. Thereafter, the Commission may issue an order directing the ERO to implement revisions as warranted.⁴

After considering all the comments it received on its posted drafts, NERC proposed the particular set of ERO structures, procedures, and programs reflected in its application as the most appropriate way to implement the requirements of the FPA and Part 39. NERC acknowledges that there can be legitimate differences of opinion as to some of the approaches chosen. However, NERC submits that the Commission should evaluate and rule on the certification application based on whether the application in its entirety satisfies the requirements of Section 215 and Part 39 for certification as the ERO, and should not be distracted by attempting to determine at this time what is the "best" way to satisfy each requirement.⁵ NERC submits that considered on that basis, its application for certification should be expeditiously granted.

⁴18 C.F.R. § 39.3(c).

⁵The courts have frequently held that in cases under Section 205 of the FPA and Section 4 of the Natural Gas Act, the filing entity need only demonstrate that its proposal is reasonable, not that its proposal is the best or prove that no other alternatives would be reasonable. *See, e.g., Duke Energy Trading and Marketing, L.L.C. v. FERC*, 315 F.3d 377, 382 (D.C. Cir. 2003) ("Nothing in Section 4 requires a pipeline to prove that its proposal is more just and reasonable than the existing system. The pipeline must only show that its proposal is just and reasonable in its own right."); *Exxon Corp. v. FERC*, 206 F.3d 47, 51 (D.C. Cir. 2000) ("Under Section 4 of the Natural Gas Act a pipeline proposing a rate change has the burden of showing that the proposed rate is just and reasonable. If it meets that burden, FERC approves the rate regardless of whether there may be other rates that would also be just and reasonable.").

Further, NERC requests that if the Commission determines that some components of NERC's filing, including components of its proposed ERO Rules, warrant modification or refinement, the Commission should identify those items in its Order, and provide the opportunity to submit a revised rule or provision in a compliance filing within a reasonable time period following issuance of the Order granting certification.

III. Discussion of Specific Comments

NERC will address the comments submitted to the Commission under several broad categories: Governance (including Board of Trustees, Member Representatives Committee and Bylaws provisions); Reliability Standards (including filing reliability standards for approval, Registered Ballot Body composition and regional differences); Compliance and Enforcement (including the compliance registry, confidentiality and disclosure, settlements, criteria for penalty amounts, and compliance orders and remedial orders); Budgets and Funding (including scope of the ERO budget, collection of the funding requirement, and accounting system); Delegation Agreements and Regional Entities; and Other Issues (including composition of committees, the Reliability Readiness Audit program, and Resource Adequacy assessments). Provided with these reply comments as Appendix A is a specific list of modifications to its proposed Bylaws and ROP that NERC intends to implement in response to comments that were submitted on the application.

A. Governance and Membership

The governance requirement for the entity certified as the ERO is set forth in Section 215(c) of the FPA, which requires that the ERO's rules:

assure its independence of the users and owners and operators of the bulk-power system, while assuring fair stakeholder representation in the selection of its directors and balanced decisionmaking in any ERO committee or subordinate organizational structure.

1. Board of Trustees

NERC's proposed Bylaws specify that its affairs are to be managed by a board of ten independent trustees and one management trustee. (Bylaws, Art. III, Sec. 1.) The management trustee will be the president of NERC who will be appointed by the independent trustees. (Bylaws, Art. III, Sec. 7.) The proposed Bylaws specify that an independent trustee cannot be an officer or employee of NERC, a member of NERC, or an officer, director or employee of a member of NERC or of any entity that would reasonably be perceived as having a direct financial interest in the outcome of Board decisions; or have any relationship that would interfere with the exercise of independent judgment in carrying out the responsibilities of a trustee. (Bylaws, Art. III, Sec. 3.)

Under the proposed Bylaws, the independent trustees will be elected by a broadly representative group of stakeholders, the Member Representatives Committee ("MRC"). To assure broad support, each trustee nominee must receive not just a majority, but rather a two-thirds affirmative vote of the MRC to be elected. (Bylaws, Art. III, Sec. 6.) Trustee candidates will be nominated by a nominating committee that will include those trustees whose terms are not expiring in the upcoming year and at least three representatives of the MRC; the proposed Bylaws give the Board the authority to appoint additional members to the nominating committee as appropriate. (Bylaws, Art. III, Sec. 5.) The proposed Bylaws also require that members of NERC be given the opportunity to suggest candidates to the nominating committee. (*Id.*)

This proposed structure satisfies the requirements of Section 215(c) of the FPA. The trustees will be independent of the owners, operators, and users of the bulk power system, and

they will be elected by a fair cross-section of stakeholders.⁶ NERC carried this structure over from the current Bylaws of NERC-Council, where it has been used since NERC-Council moved to an independent Board in 2001.⁷ These procedures have produced an extraordinary Board of highly qualified trustees with diverse expertise and experience, as detailed in the application. Moreover, contrary to certain comments, the proposed Bylaws do not provide for a “self-perpetuating” board.⁸ A “self-perpetuating” board is one where the board members themselves choose or elect their own successors. Here, stakeholders will participate in the selection of Board nominees, and a representative committee of stakeholders will elect the independent trustees to the NERC Board.

2. Member Representatives Committee

Under the proposed Bylaws, the MRC will elect the independent trustees, act jointly with the Board to amend the Bylaws, and provide advice to the Board on the development of the annual budget and funding mechanism and on matters of policy. (Bylaws, Art. VIII, Sec. 1.) The MRC will include representatives of the NERC membership from each of the following

⁶NERC notes that the MRC will be selected by the members of NERC (Bylaws, Art. VIII, Sec. 3) and that membership in NERC will be open to any person or entity that has an interest in the reliable operation of the bulk-power system (Bylaws, Art. II, Sec. 1); however, membership in NERC will not be mandatory for any person or entity. Despite the non-mandatory nature of membership (which was a consistent theme from commenters during NERC’s application development process) and the potential decision by some stakeholders not to become members of NERC, the proposed Bylaw provisions will still result in the election of independent trustees by a fair cross-section of stakeholders.

⁷The proposed structure for NERC-Corporation actually provides even greater assurance of “fair stakeholder representation” in the selection of the trustees, in that under the proposed Bylaws the MRC (who will elect the independent trustees) will be formally selected by the membership of NERC from the respective membership sectors. (Bylaws, Art. VIII, Sec. 2 and 3.)

⁸Motion to Intervene and Comments of the Electricity Consumers Resource Council, the American Forest & Paper Association, the Council of Industrial Boiler Owners, and the American Iron and Steel Institute (“ELCON”) at p. 17; Motion to Intervene and Limited Protest of Transmission Access Policy Study Group (“TAPS”) at p. 8.

sectors: (i) investor-owned utilities; (ii) state/municipal utilities; (iii) cooperative utilities; (iv) federal or provincial utilities/power marketing administrations; (v) transmission-dependent utilities; (vi) merchant electricity generators; (vii) electricity marketers; (viii) large end-use electricity customers; (ix) small end-use electricity customers; (x) independent system operators/regional transmission organizations; (xi) regional reliability organizations; and (xii) government representatives. (Bylaws, Art. VIII, Sec. 2.)

NERC expects to have more than two hundred members. Some membership sectors could have dozens of members, while other sectors may have less than ten members. To provide balance among the various membership sectors, the proposed Bylaws provide for two representatives from each of the first ten sectors listed above. (*Id.*) To ensure that all regions of the U.S. were represented on the MRC (an objective that a number of commenters emphasized with respect to various aspects of NERC's activities), the proposed Bylaws provide for the members of each regional reliability organization to elect one representative to the MRC, through "a fair and transparent voting process that has been approved by a vote of at least two-thirds of the members of the regional reliability organization." (Bylaws, Art. VIII, Sec. 2 & 3b.) That representative does not represent the regional reliability organization, but rather is elected to the MRC by the *members* of the regional reliability organization, in order to assure diverse geographic representation on the MRC. Additionally, the proposed Bylaws provide for representation on the MRC from various governmental entities, some voting and some non-voting. (Bylaws, Art. VIII, Sec. 2.) Finally, the proposed Bylaws include a mechanism to assure an appropriate number of representatives from Canada on the MRC. (Bylaws, Art. III, Sec. 4.)

The composition of the MRC was among the most widely discussed and debated topics NERC dealt with as it developed the proposed ERO organizational structure. The composition

provided for in the proposed Bylaws was arrived at only after considering substantial stakeholder input. While some commenters may wish to see greater representation on the MRC for some sectors of the industry and lesser representation for other sectors,⁹ the proposed composition of the MRC assures fair stakeholder representation in the selection of NERC's trustees and balanced decision-making in the MRC's decisions, as required by Section 215(c) of the FPA.

3. Other Bylaws Issues Concerning Governance and Membership

a. Proposals to Modify Reliability Standards or the NERC Rules of Procedure

Some commenters expressed concern that they might not be able to seek modifications in reliability standards or the ERO's Rules of Procedure.¹⁰ Neither concern is well-founded. Under NERC's ANSI-approved Reliability Standards Development Process, any person (not just members of NERC) can propose a new or modified reliability standard, and the proposal will be evaluated in accordance with the procedures specified in the Reliability Standards Development Process. (*See* ROP, § 308.1.) With respect to the ROP, amendment or repeal of existing rules or adoption of new rules may be proposed by the MRC, by any 50 members of NERC including members of at least three membership sectors, by a committee of NERC to whose purpose and functions the affected ROP pertains, or by an officer of NERC.¹¹ (Bylaws, Art. XI, Sec. 2.) While this provision will not allow individual members of NERC to propose changes to the ROP

⁹Comments of the ISO/RTO Council at p. 13 ("ISO/RTO Council"), ELCON at p. 15, Motion to Intervene and Comments of National Grid USA at p. 32 ("National Grid").

¹⁰Motion for Leave to Intervene and Comments of Northern Indiana Public Service Company at p. 3 ("NIPSCO").

¹¹As pointed out by the Bonneville Power Administration ("Bonneville") at p. 9, Section 1401 of the proposed ROP states that any ten members of NERC can propose a revision to the ROP. NERC will modify Section 1401 to be consistent with Article XI, Section 2 of the proposed Bylaws on this point.

for consideration, any member or group of members will be free to work through the MRC, relevant committees or the membership at large to obtain the necessary consensus (e.g. at least 50 members) to propose a change to the ROP. Further, the “minimum” levels of support necessary to propose a change to the ROP are not onerous, but do necessitate that a proposal have a reasonable level of support within NERC before it will be formally considered. Stated differently, any proposal that could not garner the modest aggregations of support called for by Article XI, Section 2 of the proposed Bylaws would be highly unlikely ultimately to be adopted.

b. “Hold Harmless” Provision of the Proposed Bylaws

Several commentators expressed concern with respect to the following provision of Article II, Section 3b of the proposed Bylaws:¹²

As an additional condition of membership in the Corporation, each person or entity registering as a member shall be required to execute an agreement with the Corporation, in a form to be specified by the board, that such person or entity will hold all trustees, officers, employees, and agents of the Corporation, as well as volunteers participating in good faith in the activities of the Corporation, harmless for any injury or damage caused by any act or omission of any trustee, officer, employee, agent, or volunteer in the course of performance of his or her duties on behalf of the Corporation, other than for acts of fraud.

Commenters suggested that this provision should be eliminated, or that it should exclude acts of gross negligence and/or intentional misconduct.

NERC believes, however, that this “hold harmless” provision is essential to its continued ability both to attract high-quality candidates to stand for election as independent trustees, and to attract volunteers from industry, government and academia with appropriate technical expertise to serve on its committees, task forces, audit teams and in other capacities critical to accomplishment of the ERO’s purpose. With respect to trustee candidates, the potential

¹²Motion to Intervene and Comments of Entergy Services, Inc. at pp. 6-7 (“Entergy”), Motion to Intervene and Comments Pacific Gas & Electric Company at pp. 19-20 (“PG&E”), TAPS at pp. 5-7.

exposure to litigation and liability for actions taken while on the Board of NERC can only serve to discourage qualified candidates (who, by the definition of “independent” in NERC’s Bylaws, can stand to gain no direct or indirect economic benefit from NERC’s activities and decisions) from being willing to stand for election, and serve, as independent trustees. With respect to potential industry volunteers, they of course are individuals who can be expected to have no interest in engaging in activities that pose a risk of exposure to litigation and personal liability. Further, virtually all potential volunteers will be employees of organizations that are unlikely to consent to their employees serving as volunteer members of ERO committees, task forces or audit teams if these activities carry any potential risk of exposing the employer to litigation and liability.

Modifying the “hold harmless” provision to exclude alleged acts of “gross negligence” and “intentional misconduct” would be similarly problematic – it is easy for a complainant to file an administrative complaint or a lawsuit characterizing the actions complained of as “gross negligence” or “intentional misconduct.” While these limitations may make it more difficult for a complainant to *establish liability* against a NERC trustee or volunteer, they do not make it materially more difficult to *initiate litigation* against a trustee or volunteer – and the possibility of exposure to the expense, distraction and risk of litigation as a result of serving as a trustee or NERC volunteer will be sufficient to discourage many qualified individuals from assuming these roles.¹³

More generally, NERC believes that commenters expressing concern over the “hold-harmless” provision lack sufficient focus on the big picture. NERC is structured to act, as the

¹³Indeed, the act of a trustee or a committee member in, for example, voting for adoption of a reliability standard or other proposal to which a disgruntled complainant objects, will almost certainly be an “intentional” act.

ERO, as an industry self-regulatory organization. NERC's intention is to operate to develop, adopt and enforce compliance with reliability standards, and to carry out other activities with the objective of assuring reliable operation of the bulk-power system, as a cooperative industry effort. Reliable operation of the bulk-power system is in the interest of all users, owners and operators; the promotion, achievement and maintenance of that result should be a cooperative effort among all industry participants – not an “us versus them” proposition between NERC, its trustees, staff and volunteers on the one hand and individual users, owners and operators of the bulk-power system on the other. Moreover, any entity wishing to challenge actions taken by the ERO is not deprived of a forum by the “hold harmless” provision, because there will be a right of appeal to the Commission (and from an adverse Commission decision, to the courts) from any ERO action adopting or revising a reliability standard, Bylaws provision or ROP or imposing a penalty or sanction for violating a reliability standard.

Finally, NERC notes that if a government organization were performing the functions that NERC will perform – such as standards setting, auditing and compliance enforcement -- the government officials and staff would generally be immune from suit and liability in their personal capacities for any actions or inactions in the scope of their official activities and employment. These activities are similar to the activities that NERC and its trustees, staff and industry volunteers will be performing.

c. Board Meetings without Notice

Some commenters expressed concern about provisions of the proposed Bylaws that allow the Board of Trustees to establish meetings to be held “without notice.” (*See* Bylaws, Art. V, Sec. 1.)¹⁴ The purpose of this provision, which is quite common in corporate bylaws, is to allow

¹⁴Bonneville at pp. 7-8.

the Board to establish a schedule of meetings that can thereafter take place without the provision of notice of each specific meeting *to the Trustees*. NERC agrees with the thrust of the comments that its Board should not meet without notice being given to the membership and the public, via a posting on the NERC website and electronic notification to the members, and that any materials provided to the Board in connection with a meeting should be posted on the website (subject to redaction of information concerning personnel matters, compliance and enforcement matters, litigation, or commercially sensitive or critical infrastructure information of any entity). However, such notice to the membership and the public, and the posting of materials, is already provided for in the proposed Bylaws with respect to *all* meetings of the Board as well as with respect to proposed actions by consent without a meeting. (*See* Bylaws, Art. V, Sec. 4 & 6.)

d. Comments Regarding Specific Terms Used in the Bylaws and Rules of Practice

One commenter pointed out a difference between the definition of “system operator” in the proposed Bylaws and the definition of that term in the ROP.¹⁵ Because this term is not otherwise used in the Bylaws, the ROP, or the currently proposed reliability standards, NERC will delete the definition from both the proposed Bylaws and the ROP.

Some commenters requested clarification (from either NERC or the Commission) of the term “bulk power system.”¹⁶ (This comment arose, at least in part, in the context of comments addressing the scope of provisions applying to “owners, operators and users of the bulk-power system.”) Section 215 of the FPA defines “bulk-power system” as follows:

The term ‘bulk-power system’ means—

¹⁵Bonneville at p. 9.

¹⁶Comments of the National Association of Regulatory Utility Commissioners at pp. 5-6 (“NARUC”), Notice of Intervention and Comments of New York Public Service Commission at p. 7 (“New York PSC”).

- (A) facilities and control systems necessary for operating an interconnected electric energy transmission network (or any portion thereof); and
- (B) electric energy from generation facilities needed to maintain transmission system reliability.

The term does not include facilities used in the local distribution of electric energy.

As a preliminary matter, NERC's proposed Bylaws and ROP use the statutory definition, which (as noted by some commenters) is similar to, but not the same as, the definition of "bulk electric system" contained in the NERC Glossary of Terms Used in Reliability Standards. The Commission Staff raised this point in their May 11, 2006 preliminary assessment of NERC's proposed reliability standards. The NERC Planning Committee and Operating Committee are currently reviewing these definitions. NERC expects to provide suggestions regarding the use of the terms "bulk-power system" and "bulk electric system," as related to the setting and enforcement of mandatory reliability standards, in its response to Staff's preliminary assessment of the reliability standards.

With respect to the various requests for clarification of the term "bulk-power system," the Commission has experience in the sometimes difficult line-drawing that occurs with respect to other provisions of the FPA, where the reach of the Commission's jurisdiction turns on the line between "transmission" and "local distribution" facilities. The exercise to determine the scope of the term "bulk-power system" will be similar. For example, facilities of a certain voltage level may in one part of the country serve a distribution function, while in another part of the country facilities at that same voltage level form the backbone of the bulk-power system. NERC does not believe providing further clarification to the term "bulk-power system" in its application

and proposed ERO Rules will be helpful because the applicability of the term cannot be further clarified in the abstract.

Finally, contrary to some comments, NERC does not believe it is appropriate as a general matter for regional reliability organizations to define what elements are in or not in the “bulk-power system,” except under very limited circumstances.

Some commenters urged elimination of the term “regional reliability organization” from the proposed Bylaws and the ROP, stating it is redundant to the term “regional entity.”¹⁷ NERC has intentionally maintained both terms, and each term serves a purpose. The term “regional reliability organization” refers to the existing regional reliability councils. These organizations have specific responsibilities under NERC’s reliability standards. The term “regional entity” refers to an entity that has received delegated regional compliance enforcement authority, either by entering into a RDA with NERC (that is then approved by the Commission) or through direct assignment by the Commission. While it is generally assumed that each of the eight existing regional reliability councils will seek delegated regional compliance enforcement authority, and thereby become a “regional entity”, this may not be the case in all instances. For example, at least one regional reliability council is considering formation of a separate legal entity to seek the delegated authority and function as a “regional entity.”

B. Reliability Standards

Section 215(c)(2)(D) of the FPA requires that the rules of the ERO:

provide for reasonable notice and opportunity for public comment, due process, openness, and balance of interests in developing reliability standards[.]

NERC’s reliability standards development process is accredited by the American National Standards Institute as meeting ANSI’s requirements for due process, openness, balance, lack of

¹⁷TAPS at p. 24.

dominance by particular groups or sectors, reasonable notice, and opportunity to participate. Those are essentially the same requirements imposed by Section 215(c)(2)(D).

1. Filing Reliability Standards with the Commission for Approval

Some commenters expressed concern that NERC may not file all reliability standards with the Commission.¹⁸ To be clear, NERC understands that as the ERO it must file all reliability standards with, and obtain approval from, the Commission if the standards are to become mandatory and enforceable. This is the case whether a reliability standard is developed through the NERC standards development process or through an approved regional entity standards development process, and whether a standard covers the entire bulk-power system or only a particular region. There are no exceptions.

2. Composition of the Registered Ballot Body

NERC's Registered Ballot Body ("RBB"), which forms the basis for the ballot pools that will vote on proposed reliability standards, includes nine segments¹⁹:

- Segment 1 – Transmission owners
- Segment 2 – ISOs, RTOs, and regional reliability organizations
- Segment 3 – Load-serving entities
- Segment 4 – Transmission-dependent utilities
- Segment 5 – Electric generators
- Segment 6 – Brokers, aggregators, and marketers
- Segment 7 – Large electricity end-users
- Segment 8 – Small electricity end-users
- Segment 9 – Regulators and other government entities

NERC uses weighted-segment voting for approving reliability standards, which gives each segment one-ninth of the vote, regardless of the number of entities in that segment for a

¹⁸Comments of Southern California Edison Company at pp. 7-8 ("SoCalEdison").

¹⁹The provisions described in this section are applicable to NERC-Council's current reliability standards development process as well as to NERC-Corporation's proposed reliability standards development process.

particular ballot pool.²⁰ The use of weighted-segment voting assures that segments with relatively fewer members can still have a meaningful impact in determining whether a proposed standard or amendment is adopted. It also prevents any single segment or pair of segments from determining the outcome of a vote on a proposed standard (which could otherwise potentially occur if the weighting of votes were based on the number of participants in each segment). Additionally, a Standards Committee with two representatives (each with one vote) from each segment of the RBB is responsible for overseeing the standards development process.

A number of commenters raised questions about the composition of the RBB. Some commenters suggested that voting is disproportionately weighted toward segments whose members will not be required to or involved in implementing the standards.²¹ Some commenters proposed that the number of segments should be increased, so that each type of responsible entity under the reliability standards would have its own segment.²² Others commenters proposed that segment 2 should be divided so that ISOs and RTOs would each have their own segment.²³ Some commenters proposed revisions to the segment definitions.²⁴ Finally, one commenter

²⁰NERC currently has posted for pre-ballot review a modification to the standards process that would reduce the one-ninth proportionality if fewer than 10 voters from one segment vote on a particular standard.

²¹NIPSCO at p. 3, Limited Protest of and Comments on ERO Application of the Florida Reliability Coordinating Council at p. 15 (“FRCC”).

²²Motion to Intervene and Comments of Georgia System Operations Corp. at pp. 5-8 (“Georgia System Operations Corp.”).

²³ISO/RTO Council at pp. 10-13; Motion to Intervene and Comments of California ISO at pp. 4-10 (“California ISO”).

²⁴NARUC at p. 8.

questioned whether entities whose businesses and activities qualify for membership in multiple segments should be allowed to participate in more than one segment.²⁵

All of these issues, and more, were raised by various stakeholders in their comments as NERC was revising its standards development process in anticipation of passage of the reliability legislation. There undoubtedly exists a number of different but reasonable ways of subdividing the large and diverse set of entities and individuals who are interested in reliability standards into segments for purposes of balloting proposed standards. The composition of the RBB in NERC's standards development process and ROP assures that all entities with an interest in reliability standards will have a fair opportunity to participate in the development and voting processes and that no single entity or single interest can dominate the process. The composition of the RBB satisfies the statutory requirement that the ERO's rules provide for a "balance of interests in developing reliability standards." Additionally, despite the comments submitted to the Commission on this topic, the current structure and composition of the RBB and the balloting process has the support of a very large majority of NERC's stakeholders. NERC's standards development process was approved using the same weighted-segment voting NERC uses to approve reliability standards. The standards process, with the current nine-segment RBB, was approved by an affirmative 96% weighted vote on November 29, 2004, and an affirmative weighted vote of 95% on July 29, 2005.

To date, the nine-segment, weighted-voting RBB model has worked well to produce a sound body of reliability standards. However, the NERC Board has the ability, subject to obtaining (once NERC is certified as the ERO) this Commission's approval, to adjust the segments if experience proves that necessary. Moreover, stakeholders have the ability to

²⁵National Grid at pp. 29-30.

propose changes to the composition of the RBB through the standards developments process. (ROP, § 316.) If experience indicates that a change in the composition of the RBB is necessary or appropriate in the future to assure that the standards development process continues to meet the statutory requirements (and the ANSI criteria), the mechanisms are in place to make such revisions.

3. Regional Differences

Some commenters requested clarification of the processes and criteria for approval of regional differences in reliability standards.²⁶ The Commission's Order No. 672 recognizes two types of regional differences: (1) a regional difference that is more stringent than the continent-wide Reliability Standard, including a regional difference that addresses matters that the continent-wide Reliability Standard does not; and (2) a regional reliability standard that is necessitated by a physical difference in the bulk-power system.²⁷

NERC implemented the Commission's provisions for regional differences in proposed ROP Sections 311-314. ROP Section 311 sets forth the requirements for an approved regional standards development process. ROP Section 312 describes the procedures for approval of variances to NERC's continent-wide reliability standards. A variance would, for example, be required if a regulator-approved electricity market protocol or transmission tariff precluded meeting a reliability objective in the manner specified in a continent-wide reliability standard. A variance may also be needed because of a physical difference in the electric system. For example, ERCOT has a variance for the control performance standard because it is a single balancing area within an Interconnection. An entity variance is a subset of this category, where

²⁶National Grid at pp. 25-26.

²⁷Order No. 672 at P 291.

needed for an entity smaller than a region. PJM and MISO currently have such variances incorporated into NERC's reliability standards. ROP Section 313 describes the procedures for approval of regional standards that do not require a variance from a NERC standard. Such regional standards could exist in two circumstances: (1) the regional standard could be more stringent than the continent-wide standard, or (2) the regional standard could cover a matter not covered by an existing reliability standard. Both variances (Section 312) and regional standards (Section 313) must be approved by both the ERO and the Commission before becoming enforceable.

Finally, ROP Section 314 describes the status of regional criteria (under whatever name) that do not become reliability standards under Section 215 of the FPA. Such criteria may be protocols for implementing reliability standards, or cover matters that are outside the scope of reliability standards under Section 215. These criteria are not enforceable under Section 215 and would not need to be approved by the ERO or the Commission. However, NERC will work with the regional entities to develop a catalog of such items.

C. Compliance and Enforcement

Sections 215(c)(2) and 215(e) of the FPA set the requirements for the compliance and enforcement activities of the ERO and regional entities. The statute requires that the rules of these entities must provide for:

- Fair and impartial procedures for the enforcement of reliability standards (Section 215(c)(2)(C)).
- Notice and an opportunity for a hearing (Section 215(e)(1)).
- A written finding of violation (Section 215(e)(2)(A)).
- Filing notice of a violation and the record of the proceeding with the Commission (Section 215(e)(2)(B)).

- The right to appeal the decision to the Commission and the opportunity for the Commission to review the decision on its own (Section 215(e)(3)).

Order 672 adds a requirement that there be the opportunity for a single appeal within the ERO/regional entity structure. Finally, the Commission's decisions are subject to judicial review in the same manner as are other orders of the Commission under the FPA.

NERC's plan as the ERO is to delegate enforcement authority to regional entities pursuant to Commission-approved RDAs and have the regional entities carry out the primary compliance and enforcement responsibilities with respect to the activities of owners, operators, and users of the bulk-power system. The compliance and enforcement activities of the regional entities will be overseen by NERC, with all compliance and enforcement activities also subject to government oversight in the U.S. and Canada. To that end (and as called for by Order No. 672²⁸), NERC included with its application a pro forma RDA that sets out the requirements for each regional entity's compliance and enforcement program. NERC's ROP meet, and the rules of the regional entities to be included in Exhibit D to each RDA will meet (or NERC will not enter into the RDA) the statutory and Commission requirements for a compliance and enforcement program under Section 215 of the FPA and Part 39.

Many of the questions raised by commenters concerning the specifics of the compliance and enforcement programs will be addressed in the detailed provisions of the RDAs; therefore, these questions should be addressed and resolved in the context of the Commission proceedings to approve the RDAs. NERC expects to make a filing or filings with the Commission for approval of the RDAs later this year, after it has been certified as the ERO and completed negotiation of RDAs with the prospective regional entities. However, in the subsections below,

²⁸Order No. 672 at P 712.

NERC addresses certain of the more general comments submitted to the Commission regarding the compliance and enforcement program.

1. Compliance Registry

NERC is in the process of developing, in conjunction with the regional reliability councils, a registry identifying those entities that are subject to reliability standards. (*See* ROP, § 500.) Entities whose activities could have a material adverse effect on the reliability of the bulk power system will be included on the compliance registry. NERC will provide notice to those entities proposed to be included on the registry, and they will be given an opportunity to challenge their inclusion. (ROP, § 501.1.3.) NERC will post the registry on its web site, and will update the registry as necessary. Third parties will have the opportunity to suggest that an entity not on the registry be added to it.

NERC has developed detailed guidelines to ensure consistent development of and inclusion of entities in the compliance registry across the bulk-power system of North America. Appendix B is a copy of these guidelines. The guidelines, while focused on those entities whose activities could have a material adverse effect on reliability, are structured so as not to categorically exclude any entity that fits in the definition of “owner, operator, and user” if reaching that entity is necessary to assure the continued reliability of the bulk-power system. Further, as standards are revised over time, NERC expects that additional granularity will be added to the “applicability” or “responsible entities” provisions of individual standards as appropriate, to define with greater particularity those entities that are subject to the standards.

One commenter suggested that entities such as joint action agencies should be allowed to register on behalf of their members (e.g., transmission dependent utilities) if the joint action

agency takes responsibility for assuring compliance with the reliability standards by its members.²⁹ This approach is provided for in Section 501.1.2.7 of NERC’s proposed ROP.

2. Confidentiality and Disclosure

NERC agrees with the commenters who stated that compliance investigations and proceedings should be non-public until such time as NERC reports a confirmed violation to the Commission.³⁰ NERC’s proposed ROP for compliance proceedings specifies that NERC shall disclose confirmed violations and shall maintain as confidential alleged violations. (ROP, § 402.5.) The ROP also specify that confirmed violations, penalties and sanctions shall be posted on NERC’s website when the affected bulk-power system owner, operator or user agrees with the violation, the time for submitting an appeal has passed, or all appeals procedures are completed. (ROP, § 408.6.) NERC also agrees that NERC and the regional entities must develop and maintain the record for each compliance proceeding, and that these records would be filed with the Commission at the time NERC files a notice that it has confirmed a violation and imposed a penalty.³¹

3. Settlement of Compliance Matters

Commenters raised questions regarding the possibility of settlements of compliance matters.³² NERC understands the possibility of settlement to be an important element of its

²⁹Georgia System Operations Corp. at p. 10.

³⁰National Grid at p. 11, Motion to Intervene and Comments of Ameren Services Co. at p. 8 (“Ameren”).

³¹Ameren at p. 7.

³²Motion to Intervene of the Edison Electric Institute and Comments in Support of Application at p. 22 (“EEI”), Motion to Intervene and Comments Midwest Reliability Organization at pp. 4-5 (“Midwest Reliability Organization”).

compliance program, just as settlements are used by the Commission in its enforcement program. NERC also understands the need for consistency across the regional entity compliance programs in this regard. To assure that consistency, NERC has reserved the right to participate in regional entity settlement processes, and will review all settlements prior to filing a notice of penalty with the Commission. As urged by some commenters and consistent with Order No. 672, NERC will also make settlements of compliance proceedings public once the matter is concluded.³³

4. Determination of Penalty Amounts

Section 215(e)(6) requires that penalties imposed for violations of ERO reliability standards must:

bear a reasonable relation to the seriousness of the violation and shall take into consideration the efforts of such user, owner, or operator to remedy the violation in a timely manner.

The goal of NERC's compliance enforcement program as the ERO will be to promote and achieve compliance with the reliability standards so as to assure the reliability of the bulk-power system -- not to collect penalties. But the prospect of the imposition of penalties is a necessary element of an effective compliance and enforcement program. NERC agrees with the commenters who stated that penalties for noncompliance must be applied consistently across all regional entity programs.³⁴ To aid in that consistency, NERC developed sanctions guidelines for use by the regional entities, which were provided in NERC's application as Appendix 4, ERO Sanction Guidelines, to the ROP. NERC patterned those sanctions guidelines after the enforcement guidelines recently published by the Commission. (*See* Application, pp. 64-65.)

³³Order No. 672 at P 598.

³⁴EI at p. 20.

NERC will also provide oversight to the regional programs in this area, including through the use of audits, as a further aid to achieving consistency of application of penalties.

Several commenters raised questions concerning whether and to what extent an entity's size should be taken into account in determining the amount of a penalty. Some commenters stated that size should not be a factor; some commenters stated that an entity's ability to pay should be considered;³⁵ some commenters stated it would be discriminatory to impose the same size penalty on a small entity as on a larger entity;³⁶ some commenters stated it would be discriminatory not to apply the same penalty for the same violation committed by two different entities, regardless of their sizes;³⁷ some commenters stated that in assessing penalties, NERC must take account of the increased reliability burden carried by larger entities;³⁸ and some commenters stated that size should be considered only when size actually affects the seriousness of the violation.³⁹ NERC is in the process of developing "size factors" to be taken into account in determining the amount of a penalty to be assessed. The size factors will be based on a number of considerations including the entity's generator size, plant size, and kV-miles of transmission line. The size factors will generally recognize the contribution of the organization's size to the seriousness of the risk of its violation to reliability.

³⁵Motion to Intervene and Comments in Support of the National Rural Electric Cooperative Association at pp. 8-9 ("NRECA").

³⁶*Id.*

³⁷National Grid at p. 28.

³⁸Entergy at p. 8.

³⁹National Grid at pp. 27-29.

Some commenters recommended that penalties should be defined through a fixed look-up table from which deviations would not be permitted.⁴⁰ NERC's proposed penalty criteria *start* with a look-up table. However, NERC believes that a more flexible approach than suggested by some commenters is necessary for the proper administration of a penalty program in order to deal with the wide variety of circumstances that undoubtedly will be presented. NERC's sanctions guidelines should provide sufficient notice of the likely scope of penalties to provide incentives for entities to meet their responsibilities for complying with reliability standards. The sanctions guidelines that NERC has developed will guide the exercise of discretion by both NERC and the regional entities when setting penalties. As noted above, NERC's sanctions guidelines follow the approach outlined by the Commission in its own enforcement policy statement.

A number of commenters raised questions that will need to be addressed in the compliance programs of the regional entities with whom NERC enters into RDAs.⁴¹ These questions should be dealt with in the context of reviewing the regional entity compliance programs as part of the overall review of the proposed RDAs. As noted earlier, NERC expects to file the proposed RDAs, and the details of each regional entity's compliance program, with the Commission later this year after being certified as the ERO and completing negotiation of the RDAs with the regional entities.

5. Compliance Orders/Remedial Orders

NERC agrees with the commenters that recommended that remedial orders or compliance directives generally should be limited to instances in which NERC or the regional entity has

⁴⁰Comments of the Western Electricity Coordinating Council at pp. 6-7 ("WECC").

⁴¹California ISO at pp. 12-15, Ameren at pp 9-11.

identified a violation of a reliability standard that must be corrected promptly to reduce the threat that the identified violation poses to the reliability of the bulk power system. In light of the exigencies of such circumstances, it should not be necessary that such orders or directives be on file with the Commission for 30 days before they could take effect. As the Commission stated in Order No. 672, an entity may be violating a reliability standard of such significance or in such a manner that NERC or the regional entity is compelled to issue a directive that the entity immediately stop the violation and come into compliance.⁴²

Additionally, NERC and the regional entities must have the ability to take informal actions, where warranted, for the purpose of ensuring reliability, such as notifying an entity's CEO or its regulator, or directing an entity to develop a remediation plan. Any imposition of sanctions in such situations would, of course, be subject to exercise of an entity's full due process rights under Section 215, Part 39 and NERC's ROP.

D. Budgets and Funding

Section 215(c)(2) of the FPA requires that the rules of the ERO:

allocate equitably reasonable dues, fees, and other charges among end users for all activities under this section[.]

In general, NERC proposes to allocate its costs for recovery between the U.S. and Canada, and among the regions, based on net energy for load ("NEL"). (ROP, § 1102.1.) The reasonableness of the amounts to be expended by NERC during the upcoming fiscal year will first be examined through a stakeholder process as the budget is developed. (Bylaws, Art. XIII, Sec. 2 & 4.) Following approval by NERC's independent board, the budget will be submitted to the Commission for approval, as required by Part 39.

⁴²Order No. 672 at P 475.

Commenters raised issues concerning the scope of the ERO's budget, how the ERO's funding requirement will be collected, and the system of accounts the ERO will use. As a general matter, NERC believes that issues regarding its budget and funding should be addressed in connection with the Commission's review of the first annual budget filing NERC expects to make in mid-August 2006 after being certified as the ERO. That filing will contain detailed descriptions of the programs NERC expects to carry out during its initial fiscal year (2007) as the ERO and the associated costs of those programs. That filing will provide the appropriate forum to address the issues raised by commenters concerning the budget and funding. However, the following paragraphs briefly address certain points raised in the comments.

1. Scope of Activities Included in the ERO Budget

NERC believes that all the functions it proposes to perform as the ERO are either explicitly required by Section 215 of the FPA, or are necessary and appropriate corollaries to carrying out the ERO's express statutory responsibilities.⁴³ As stated in the certification application, NERC's vision for accomplishing the ERO's ultimate mission of assuring reliable operation of the bulk-power system is based on a continuous cycle of activities to achieve reliability improvements: (1) measuring reliability performance – past, present, and future; (2) analyzing and benchmarking the results of those measurements; (3) identifying problems and assessing needs for improvement; (4) developing solutions to address those problems and needs, including new or revised reliability standards; and (5) implementing solutions, including

⁴³Certain of NERC's activities and programs, such as the System Operator Certification Program, training workshops and the maintenance of the Generation Availability Data System, generate revenues through user fees. Generally, NERC has attempted to develop fees for these services to recover the costs of the programs. Nevertheless, in the preparation of the ERO's annual budget, these revenues will be used to offset the total funding requirement that must be recovered through the ERO's proposed NEL-based funding mechanism.

expanded compliance monitoring and enforcement. (*See Application, pp. 8-10.*) This ongoing cycle of activities promotes continuous, measurable improvements in reliability.

To effectively and efficiently implement this approach, NERC will build upon a set of programs whose goals and objectives include reliability standards, compliance and certification, reliability readiness, training and personnel certification, reliability assessments and performance analysis, and situation awareness and infrastructure security. NERC will provide detailed descriptions of each of these activities in its budget submission to the Commission. For present purposes, there is obviously no disagreement that the development of reliability standards, the enforcement of compliance with those standards through, among other activities, a program of audits, the oversight of regional programs, and assessments of the reliability and adequacy of the bulk-power system, are all within the ERO's express statutory responsibilities. The following paragraphs briefly describe how other programs NERC intends to continue as the ERO are necessary and appropriate corollaries to fulfilling the express statutory responsibilities.

Reliability Readiness Audit and Improvement Program. The Reliability Readiness Audit and Improvement Program will be an important component of NERC's accomplishment of its statutory functions as the ERO. The activities and functions of the operators of the bulk-power systems of North America that will be the subjects of the readiness audits are critical to achieving excellence in the reliable operation of the bulk-power systems. Readiness audits will be specifically focused on addressing the capabilities of entities to identify and respond to emergency conditions that could impact the reliable operation of the bulk-power system. By implementing a continuous program of auditing the tools, training, system and procedures of entities, as well as sharing among them best practices and examples of excellence in the industry, NERC will be striving to promote an ongoing high standard of performance by entities in the execution of their reliability-related functions, and thereby further to ensure the reliable operation of the bulk-power systems.

Situation Awareness and Infrastructure Security. On an ongoing basis, NERC will monitor conditions on the bulk-power system and provide leadership coordination, technical expertise and assistance to the industry in responding to abnormal events on the bulk-power systems. NERC will maintain real-time situation awareness of conditions on the bulk-power system; notify the industry of significant bulk-power system events that have occurred in one area, and which have the potential to impact reliability in other areas; maintain and strengthen high-level communication, coordination, and cooperation

with governments and government agencies regarding real-time conditions on the bulk-power system; and enable the reliable operation of interconnected bulk-power systems by facilitating information exchange and coordination among reliability service organizations. NERC will also provide tools and other support services for the use and benefit of bulk-power system operators including reliability coordinators, such as the Area Control Error and Frequency Monitoring System, the NERC Hotline, Real-time Flows, the System Data Exchange, the Reliability Coordinator Information System, the Transmission Services Information Network, the Interchange Distribution Calculator, the Interregional Security Network and the Central Repository for Security Events. NERC will facilitate real-time voice and data exchange among bulk-power system reliability coordinators. Additionally, NERC will take a leadership role in critical infrastructure protection of the electricity sector so as to reduce the vulnerability and improve the mitigation and protection of the critical infrastructure of the electricity sector. NERC will act as the electricity sector's Sector Coordinator and operate its Information Sharing and Analysis Center to gather information and communicate information about security-related threats within the sector, with U.S. and Canadian government agencies and with other critical infrastructure sectors. These situation awareness and infrastructure security activities will be important components of fulfilling the ERO's statutory responsibilities. Maintaining real-time awareness of conditions on the bulk-power systems, communicating information concerning system conditions and abnormal events to, and facilitating real-time communications among, system operators responsible for the reliable operation of the bulk-power systems, is critical to maintaining reliable operation of the bulk-power systems, as is promoting and planning for protection of the electricity sector's critical infrastructure. These activities will also assist NERC in identifying areas where new or revised reliability standards may be required.

System Operator Certification Program and Other Training and Education Programs. Developing and maintaining training, education and certification programs for bulk-power system operating personnel and the other targeted audiences of these programs will also be an important component of NERC's activities to fulfill its statutory responsibilities as the ERO. Providing for a system of certification of the qualifications and competencies of operating personnel of users, owners and operators of the bulk-power system, and providing training and education programs for operating personnel of users, owners and operators of the bulk-power systems relating to their compliance with reliability standards and other reliability-related job functions, will help to achieve high levels of knowledge and competence among these operating personnel in the performance of their reliability-related functions, as well as helping to promote a culture of compliance within the industry, and thereby will help to further ensure the reliable operation of the bulk-power system.

Maintenance of Other Bulk-Power System Operating Tools and Resources and Collection and Dissemination of Electric Industry Information. In addition to maintaining and making available to the industry the tools and support services listed above, NERC will continue to maintain and offer other tools and support services useful to users, owners and operators of the bulk-power systems in the performance of their reliability-related functions, and will operate programs for the collection of industry data that will be useful in analyzing the reliability performance of the interconnected bulk-

power systems. For example, NERC will maintain the Generating Availability Data System to collect operating information about the performance of electric generating equipment; this data can be used by industry participants seeking to analyze past and prospective equipment reliability. NERC will also maintain the Electric Supply and Demand Database containing aggregated regional ten-year projections of electricity demand, electric generating capacity, electricity production, fossil fuel requirements, transmission lines and generating unit additions and retirements; this data will be used by NERC and can be used by industry participants in conducting reliability and planning assessments. Maintenance of these operating tools and databases will aid NERC in fulfilling its statutory responsibilities as the ERO by collecting and making available to users, owners and operators of the bulk-power system and other electricity sector participants data and resources that can be useful to them in performing their reliability-related functions and helping to ensure the reliability of the bulk-power system.

2. Collection of the ERO's Funding Requirement

NERC proposes to collect its Commission-approved annual funding requirement from load-serving entities (or their designees). This is the best way to assure that costs are distributed equitably across all end-users (as required by Section 215(c)(2)) and to not have any entities “pay twice,” as could occur, for example, if the funding requirement were collected through transmission rates. NERC will work with each regional entity to determine the entity or identities within that regional entity’s geographic boundaries that are capable of collecting the ERO funding assessment in the most efficient manner. NERC is currently working with each regional entity to develop a list of entities that will be assessed to recover the ERO’s Commission-approved funding requirement.

Some commenters expressed concern about the proposed waiver of assessments to load-serving entities for which the annual assessment is less than \$100.⁴⁴ This waiver is proposed to lessen the administrative burden and costs of the ERO, the regional entities and the load-serving entities subject to assessments of less than \$100, for the billing and collection of assessments below this minimum threshold.

⁴⁴SoCalEdison at p. 4.

NERC agrees with those commenters that emphasized that any potential for cost subsidization among regions must be minimized.⁴⁵ NERC has included a provision in the proposed ROP (Section 1102.4) requiring that costs incurred for one interconnection, regional entity, or group of entities must be directly assigned to that interconnection, regional entity, or group of entities.

3. The ERO's System of Accounts

Some commenters stated that NERC and the regional entities should follow the accounting method the Commission recently adopted for RTOs.⁴⁶ The Commission's ERO Rule requires that NERC develop a system of accounts sufficient to enable comparisons of budgets to actual results. While the Commission did not require the ERO to adopt the Uniform System of Accounts ("USOA"), it expressed a preference that the ERO's accounting system be comparable to the USOA.⁴⁷ NERC has developed a system of accounts for its use and the use of the regional entities that will enable the ERO and the regional entities to report budget requirements and actual results on a consistent basis and that has a level of detail and record-keeping that is comparable to the USOA. NERC's budget filing is the proper place to address any additional or more specific issues concerning its system of accounts.

E. Regional Entities and Regional Delegation Agreements

NERC plans to use regional entities as the primary focus of its compliance and enforcement program. NERC intends to delegate authority to those regional entities by means of

⁴⁵Protest of Consolidated Edison of New York, Inc., Long Island Power Authority, and Orange & Rockland Utilities, Inc. at p. 7 ("ConEd"); Motion to Intervene and Initial Comments of the South Carolina Public Service Authority at p. 4 ("Santee Cooper").

⁴⁶PG&E at p. 28.

⁴⁷Order No. 672 at P 246.

a Commission-approved RDA with each regional entity. NERC agrees with those commenters who stated that the RDAs should be as uniform as possible.⁴⁸ NERC intends to file its negotiated RDAs for Commission approval later this year, after receiving certification as the ERO and completing negotiations with the prospective regional entities. NERC's objective is to file all of the RDAs simultaneously, if possible, so the Commission and stakeholders will be able to evaluate how consistent the RDAs and the regional entity compliance and enforcement programs are. However, the RDAs are likely to differ in some respects. For example, Section 215(e)(4)(A) authorizes different forms of governance among regional entities so long as a regional entity meets the statutory tests of being governed by an independent board, a balanced stakeholder board or a combination independent and balanced stakeholder board and having rules that provide for fair stakeholder representation in the selection of directors and balanced decision making in committees and subordinate organizational structures.

The RDAs that NERC files with the Commission for approval will have a standard set of exhibits that contain the details of each regional entity's compliance enforcement program⁴⁹:

- Exhibit A will define the geographic area in which the regional entity will exercise delegated authority.
- Exhibit B will include the governance documents for the regional entity.
- Exhibit C will contain the details of the standards development procedure that the regional entity intends to use.
- Exhibit D will provide the detailed procedures for the regional entity's compliance program.
- Exhibit E will describe how the regional entity will collect the funding assessments and will also identify the scope of the activities to be included in the regional entity's budget submissions to NERC.

⁴⁸See, e.g., Ameren at pp. 4-6; EEI at p. 14; ELCON at pp. 6-7.

⁴⁹See the pro forma RDA included as Exhibit D to NERC's certification application.

- Exhibit F will provide a transition plan that describes the timetable and actions necessary for the regional entity to be fully prepared to carry out its activities under the RDA.

Because a number of the commenters raised questions about details of the regional entity programs, and those details will be included in the exhibits to the RDAs, many of the issues raised by commenters concerning regional entity programs will need to await the filing of the RDAs for approval by the Commission. Certain commenters, however, raised questions concerning the pro forma delegation agreement that NERC included with its application; those questions can be addressed at this time.

First and foremost, it is important to understand the nature of the RDA itself. The RDA will be a contract between NERC and the regional entity delegating to the regional entity certain portions of NERC's authority as the ERO to carry out specified functions regarding developing reliability standards and enforcing compliance with reliability standards. The RDA is a voluntary agreement that sets forth the terms and conditions under which those delegated functions will be carried out. Section 215 prescribes what some of the terms and conditions of an RDA must be, and the agreements will be subject to approval by FERC. But, until there is an agreement between the parties, there is nothing to submit to the Commission for approval.⁵⁰

A number of commenters raised questions about Section 16 of the pro forma RDA.⁵¹ Section 16 states that NERC will not seek to amend provisions of its ROP that affect matters covered by the RDA without first obtaining the consent of the regional entity. Section 16 further

⁵⁰NERC recognizes that Section 215 authorizes the direct assignment of delegated authority by the Commission to a regional entity in the event the ERO and the regional entity are unable to come to agreement.

⁵¹EEI at p. 5, Motion to Intervene and Comments of Exelon Corporation at pp. 3-6 ("Exelon"), Midwest Reliability Organization at pp. 3-4.

says that if NERC is unable to gain that consent, it will enter into dispute resolution with the regional entity. Section 16 then provides that if NERC is still unable to gain the consent of the regional entity, it may file the requested ROP amendment with the Commission and ask the Commission to use its statutory authority to impose the change.⁵² If the Commission approves the change, then the regional entity must either accept the change or terminate its responsibilities under the RDA.

Section 16 is a critical part of the RDA because it enables the regional entity to preserve the agreements and commitments it made when it entered into the RDA. The RDA will require the regional entity to agree to comply with the ERO's ROP. The content of the ROP will be known at the time the parties enter into the RDA, and the regional entity will be able to know its obligations and responsibilities under the RDA before signing it. The regional entity's ability to know and rely on the obligations it assumed when it signed the RDA could be defeated, however, if thereafter the ERO were free to modify the regional entity's obligations under the RDA -- not by negotiating an amendment to the RDA itself -- but instead by revising its ROP. Thus, Section 16 provides a fair mechanism for assuring that the ERO can make changes needed to adjust its ROP over time, while at the same time preventing the ERO from unilaterally imposing (through ROP amendments) changes in the functions that regional entities, by contract, have undertaken to perform.

One commenter questioned the legal authority for compliance enforcement with regard to the regional entities and the ERO itself, because neither the regional entities nor the ERO is an

⁵²As NERC's ROP will be ERO Rules, any amendments to them will have to be filed with and approved by the Commission in any event, as required by Section 215(f).

owner, operator, or user of the bulk-power system.⁵³ The Commission's authority over NERC, as the ERO, and the regional entities is stated in Section 215(b)(1) of the FPA, which expressly gives the Commission jurisdiction over the ERO and regional entities. That authority is further amplified in section 215(e)(5), which states:

The Commission may take such action as is necessary or appropriate against the ERO or a regional entity to ensure compliance with a reliability standard or any Commission order affecting the ERO or a regional entity.

With respect to NERC's authority over the regional entities, it will be founded upon the RDAs, which in turn will incorporate NERC's ROP.

A separate question was raised by commenters with respect to the regional reliability organizations, which also are not owners, operators, or users of the bulk-power system. A number of NERC's current standards apply to the regional reliability organizations. Further, those organizations are expected to become members of NERC once NERC becomes certified as the ERO. As NERC members, they will be bound contractually by the NERC membership agreement, as required by the proposed Bylaws:

Each member shall agree, in writing, to accept the responsibility to promote, support, and comply with the purposes and policies of the Corporation as set forth in its Certificate of Incorporation, Bylaws, Rules of Procedure, and Reliability Standards as from time to time adopted, approved, or amended. (Bylaws, Art. II, Sec. 3.)

Some commenters expressed concern over how the RDAs might apply to regional entities that cover areas outside the United States.⁵⁴ In NERC's view, the RDAs, in which the ERO by contract delegates statutorily-created responsibilities to the regional entities, are creatures of the U.S. legislation and (at least at the present time) apply only within the United States. Stated

⁵³EEI at pp. 10-12.

⁵⁴WECC at pp. 9-10.

differently, at this time NERC (or the U.S. ERO) has no authority outside the U.S. to be delegated. However, nothing in the RDAs or in U.S. law will preclude cross-border regional entities from developing agreements with governmental entities outside the United States. Indeed, NERC expects that it and the cross-border regional entities will have agreements or memoranda of understanding with non-U.S. government authorities covering similar matters to those covered in the RDAs.

Some commenters raised questions concerning the scope of the ERO's authority over amendments to the procedural rules of the regional entities.⁵⁵ Regional entity rules covering governance, standards development, and compliance will be included as exhibits to the RDAs that are submitted to the Commission for approval, and may play a critical role in establishing that the RDA satisfies the criteria for Commission approval (e.g., that the regional entity's governance satisfies the statutory requirements). To the extent any of the regional entity rules on which NERC relied in entering into an RDA are subsequently changed, those rules would be subject to NERC review and approval. However, changes to regional entity rules covering matters not included in the RDA exhibits would not be subject to review and approval by NERC.

F. Other Issues

1. Composition of NERC Committees

One commenter suggested that NERC's application does not meet the "balanced decision making" requirement of Section 215, because that criterion does not apply to all committees.⁵⁶ However, NERC believes that its proposed Bylaws categorically address and comply with this statutory requirement. Specifically, NERC's proposed Bylaws state:

⁵⁵WECC at p. 4.

⁵⁶Bonneville at p. 18.

The board shall appoint standing committees and other committees of the Corporation that are representative of members, other interested parties and the public, that provide for balanced decision making, and that include persons with outstanding technical knowledge and experience.⁵⁷

Other commenters presented various suggestions for changes in how NERC's committees are structured, such as by combining the standing committees into a single technical advisory committee.⁵⁸ Those are issues for further consideration by NERC (with, of course, stakeholder input), not the Commission, and in any event certainly are not relevant to whether NERC should be certified as the ERO.

The goals, responsibilities and accountabilities, membership, and organization and procedures of the NERC committees are currently under active review. At a special Board meeting held on March 28, 2006 to approve the filing of NERC's ERO certification application, many stakeholders as well as Trustees stated that the NERC Operating Committee and Planning Committee were critical to NERC's success. Many stakeholders asked that NERC not rush to change the committee structures or membership. Some suggested waiting for at least two years after NERC is certified as the ERO, while others thought 12 months would be more appropriate. NERC expects the Board to take action on new committee charters in 2007. The committee charters and structures will need to evolve as NERC establishes itself as the ERO and identifies its needs for the committees. The issues raised by commenters regarding committee structures can be addressed in the context of those revised committee charters.

⁵⁷Bylaws, Art. VII, Sec. 1.

⁵⁸ELCON at pp. 16-17.

NERC agrees with the commenters who stated that NERC committees must be open.⁵⁹ NERC has included such a requirement in its proposed ROP (Section 1304). As noted in that provision, however, there are circumstances in which a committee a meeting would be properly held in closed session.

2. Readiness Audit and Improvement Program

Some commenters questioned whether NERC should be responsible both for overseeing and enforcing compliance with reliability standards and for conducting its Reliability Readiness Audit and Improvement Program, and suggested potential conflicts in these two roles.⁶⁰ NERC disagrees with commenters who suggested that as the ERO, NERC should drop the Reliability Readiness Audit and Improvement Program. There is no conflict between the ERO's role in conducting compliance enforcement and its role in conducting the Readiness Audit and Improvement Program.

Reliability standards set the *minimum thresholds* that responsible entities must achieve, not targets for excellent performance. The Compliance Enforcement Program will determine *if* the responsible entities have met the minimum requirements contained in the reliability standards. In contrast, the objective of the Reliability Readiness Audit and Improvement Program (which is described in Section IV.E of NERC's Application and in Section 700 of the proposed ROP) is *not* to advise entities as to how to achieve the minimum performance levels necessary to comply with reliability standards and avoid penalties and sanctions for non-compliance. Rather, the Reliability Readiness Audit and Improvement program is designed to partner with reliability coordinators, transmission operators and balancing authorities to strive for

⁵⁹Bonneville at pp. 6-8.

⁶⁰FRCC at pp. 4-5.

excellence in operations, recognizing that reliability standards cannot prescribe every aspect of reliable operations. Further, there are many different approaches to operations that may enable a responsible entity to meet the requirements of a particular reliability standard, yet some of these approaches may enable the entity to achieve excellence in operations while others may not. The reliability readiness audits assess the quality of these approaches to determine an entity's readiness to support its responsibilities to maintain a reliable system. To use an analogy, meeting the minimum requirements to obtain a driver's license does not necessarily guarantee that a person will be a safe driver (and in fact, some people with driver's licenses are involved in accidents). The Reliability Readiness Audit program is designed to determine if entities are "safe drivers" of the bulk power system.

Moreover, the Reliability Readiness Audit and Improvement Program is not a duplication of the Compliance Enforcement Program as suggested by some comments.⁶¹ The ERO's Compliance Enforcement Program, through the regional entity compliance programs, will perform audits of entities responsible for adherence to reliability standards. These audits will be historical in nature and will be strictly based on the requirements and measurement criteria in the reliability standards. Under Section 215, the ERO is responsible for assessing compliance, issuing notices of non-compliance, and levying sanctions and penalties. Accordingly, the Compliance Enforcement Program includes a punitive element. Further, as compliance with reliability standards is mandatory, entities are required to mitigate any identified violations. In contrast, the reliability readiness audits have a forward-looking perspective. The basic objective of the reliability readiness audit is to assess an entity's readiness to avoid and to recognize, and respond effectively when faced with, emergency conditions. The audit team assesses the quality

⁶¹Progress Energy at p. 3.

of the tools, training, processes, and procedures that the entity uses to perform its reliability functions and execute its responsibilities. The reliability readiness audit teams consist of industry volunteers who offer recommendations for improvement to help the entities achieve excellence in reliability performance. The Reliability Readiness Audit and Improvement Program partners with the entity in a constructive and consultative manner to identify gaps in the entity's systems and procedures that could prove problematic in the face of emergency conditions impacting the bulk-power system, and to share examples of excellence with the industry.

Unlike the Compliance Enforcement Program, the Reliability Readiness Audit Program is not designed nor administered to uncover violations of reliability standards. If a readiness audit team should uncover a potential violation during a readiness audit, the potential violation is referred to the regional compliance program.

Removing this key element in the continuous cycle of activities to achieve reliability improvements would severely hamper NERC's ability to foster and achieve improvements in the reliability performance of owners, operators and users of the bulk-power system. The Reliability Readiness Audit and Improvement Program identifies problems and makes recommendations for improvement. The Program serves a crucial role in improving the performance of registered entities tasked with executing reliability functions.

3. Resource Adequacy Assessments

Some commenters questioned how NERC, will prepare its assessments of resource adequacy, which are a statutorily-required ERO function.⁶² As required in paragraph 805 of Order No. 672, NERC will ensure that each reliability assessment that it prepares is

⁶²Section 215(g) of the FPA.

comprehensive and sufficient for the ERO, regional entities, and the Commission to fulfill their respective responsibilities. Section 800 of NERC's proposed ROP describes how NERC will carry out that function. NERC will rely not only on data and information requested of regional reliability organizations, but also on regional reliability organization self-assessments, which are to be conducted in compliance with NERC standards and the respective regional planning criteria. NERC's teams of technical experts will also conduct interviews with the regional reliability organizations. Through this process, NERC will take into account regional or sub-regional metrics and targets as well as all reasonably credible operating conditions.

IV. Conclusion

NERC has submitted these reply comments in order to assist the Commission in addressing and resolving questions raised by commenters on NERC's application for certification as the ERO. NERC emphasizes that virtually all commenters supported certification of NERC as the ERO, and that the issues raised by commenters that have been addressed in these reply comments do not cast any doubt on NERC's overall qualifications to be certified as the ERO. Further, as noted in these comments, many of the points raised by commenters will be more appropriately addressed in future proceedings, such as the proceedings for approval of NERC's RDAs with the regional entities. NERC urges the Commission to act expeditiously on its application for certification as the ERO and to approve the proposed ERO Rules filed with the application. Additionally, NERC requests that if the Commission identifies changes or additions to NERC's proposed ERO Rules or other provisions which the Commission concludes should be implemented as a condition to certification, the Commission's order should authorize and direct NERC to make those revisions in a compliance filing within a reasonable time period following issuance of the certification order.

Dated: June 13, 2006

Respectfully submitted,

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**List of Revisions and Corrections
To NERC Documents**

A number of commenters pointed out inconsistencies or corrections that need to be made in various documents that NERC filed as part of its application. The more substantive comments are discussed in the text of NERC's reply comments, and the specific change is shown here. Other commenters pointed out obvious corrections that need to be made; those items are simply shown here without further discussion. (~~Strikethrough~~ indicates language to be deleted; underscoring indicates language to be added.)

Bylaws

1. The definition of "system operator" will be deleted in Article I, Section 1.

Rules of Procedure

1. Section 202.7: The definition of "bulk power system" is slightly different than the definition of "bulk power system" in Article I, Section I of the Bylaws and will be revised as follows to achieve consistency:

"Bulk power system" means facilities and control systems necessary for operating an interconnected electric energy ~~supply and~~ transmission network (or any portion thereof), and electric energy from generating facilities needed to maintain transmission system reliability, but does not include facilities used in the local distribution of electricity.

2. The definition of "system operator" will be deleted in Section 202.16.
3. Section 305.5.1.4 will be revised as follows:

This segment excludes regional transmission organizations and independent system operators (they are eligible to join Segment 2).

4. Section 305.5.5.2 will be revised as follows:

A company that sets up separate corporate, limited liability company or partnership entities for each one or two generating plants in which it is involved may only have one vote in this segment regardless of how many single-plant or ~~two-plant~~ multiple-plant entities the parent company has established or is involved in.

5. Section 305.5.9 will be revised as follows:

Segment 9 includes federal, state, and provincial regulators and other government entities, including public utility commissions. This segment does not include federal power ~~management~~ marketing agencies or the Tennessee Valley Authority.

6. Section 402.7 will be revised as follows:

Due Process —NERC shall establish and maintain a fair, independent, and nondiscriminatory appeals process. The appeals process is set forth in Sections 409–411. The process shall allow bulk power system owners, operators, and users to appeal the regional entity’s findings of noncompliance and to appeal penalties, sanctions, and remedial actions that are levied by the regional entity. Appeals beyond the NERC process will be heard by the applicable governmental authority.

The appeals process will also allow for appeals to NERC of any findings of noncompliance issued by NERC to a regional reliability organization for standards and requirements where the regional reliability organization is monitored for compliance to a reliability standard. No monetary penalties will be levied in these matters; however sanctions, remedial actions, and directives to comply may be applied by NERC.

7. Section 403.13 will be revised as follows:

Investigations — Investigations are necessary to evaluate compliance with reliability standards when certain system events occur, or when other owners, operators, or users of the bulk power system file complaints. NERC is ultimately responsible for how a regional entity conducts investigations. Investigations are initiated at the discretion of the regional entity compliance enforcement program staff, the senior executive officer of the regional entity, NERC compliance staff, or the NERC president. The regional entity shall respond to any complaints filed by one entity against another ~~that~~ if that entity alleges a violation of reliability standards by a bulk power system owner, operator, or user. The regional entity may ask NERC to assist with the investigation. Situations that can trigger an investigation include but are not limited to (i) significant problems arising on the system, (ii) chronic noncompliance violations, (iii) bulk power system owners, operators, and users not submitting data in a timely or accurate manner, (iv) probable violations identified during readiness audits, (v) spot-checks to verify submitted data, (vi) filing of a valid compliance complaint with the regional entity or NERC, or (vii) Nuclear Regulatory Commission-defined incidents occurring on the transmission system.

All investigations are to be non-public unless NERC or regional entity determines a need to conduct a public investigation. ~~For all public investigations, enforcement audit, or permit interventions when determining whether to impose a penalty, advance authorization from the applicable governmental authority is required.~~ NERC or a regional entity must obtain advance authorization from the appropriate governmental authority prior to conducting a public investigation or enforcement audit, or to permitting interventions in a proceeding to impose a penalty.

8. Section 403.17 will be revised as follows:

Mitigation of Violations — Each regional entity compliance enforcement program will require that any bulk power system owner, operator, or user found in noncompliance to a reliability standard requirement shall submit a mitigation plan with a timeline addressing how the noncompliance will be corrected. The mitigation plan shall be reviewed and approved by the regional compliance staff and the ~~regions~~ region's compliance panel or board as appropriate.

9. Section 502.1.3 will be revised as follows:

Regional entities participating in the program shall perform their roles and responsibilities to meet NERC's requirements, as specified in the rules of procedure or NERC approved materials, including requirements for quality, thoroughness, timeliness, accuracy, efficiency, cost-effectiveness, and ~~participants~~ participation.

10. Section 502.1.7 will be revised as follows:

NERC, or ~~by~~ the regional entity as authorized by NERC, shall make all assessments and decisions with respect to all aspects of the organization registration and certification program, including the completeness and accuracy of entities' applications.

11. Section 1401 will be revised as follows to be consistent with Article XI, Section 2 of the Bylaws:

Proposals for Amendment or Repeal of Rules of Procedure

In accordance with the bylaws of NERC, ~~requests~~ proposals to adopt new rules of procedure or to amend or repeal the existing rules of procedure may be submitted by (1) any ~~ten~~ fifty members of NERC, which number shall include members from at least three membership ~~segments~~ sectors, (2) the Member Representatives Committee, (3) a ~~standing~~ committee of NERC to whose functions and purpose the rule pertains, or (4) an officer of ~~the ERO~~ NERC.

Pro forma Regional Delegation Agreement

1. Section 11(c) will be revised as follows:

If any provision of this Agreement, or the application thereof to any person, entity or circumstance, is held by a court or regulatory authority of competent jurisdiction to be invalid, void, or unenforceable, or if a modification or condition to this Agreement is imposed by a regulatory authority exercising jurisdiction over this Agreement, the Parties shall endeavor in good faith to negotiate such amendment or amendments to this Agreement as will restore the relative benefits and obligations of the signatories under this Agreement immediately prior to such holding, modification or condition. If either Party finds such holding, modification or condition unacceptable and the Parties are unable to renegotiate a

mutually acceptable resolution, either Party may unilaterally terminate this Agreement upon thirty (30) days' notice to the other Party. Such termination shall be effective ninety (90) ~~(180)~~ days following written notice by [REGIONAL ENTITY] to NERC and the Commission, or at such other time as may be mutually agreed by [REGIONAL ENTITY] and NERC.



NORTH AMERICAN ELECTRIC RELIABILITY COUNCIL

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Statement of Compliance Registry Criteria

Summary

In preparation for becoming the Electric Reliability Organization (ERO), NERC has recently initiated a program to identify additional potential candidate organizations for its compliance registry. The program, conducted by NERC and the current NERC regional councils, will also confirm the functions and information now on file for currently-registered organizations.

This document describes how NERC will identify organizations — particularly smaller or relatively (electrically) isolated entities — that may be candidates for registration as load-serving entities, distribution providers, generation owners, generation operators, or transmission owners.

NERC and the regions must also identify the entities responsible for funding the implementation of the ERO; however, that will be done separately and is not addressed in this document.

Background

In 2005, NERC and the regional councils conducted a voluntary organization registration program limited to balancing authorities, planning authorities, regional reliability organizations, reliability coordinators, transmission operators, and transmission planners. The list of the entities that were registered constitutes what NERC currently considers its compliance registry.

NERC has recently initiated a broader program to identify additional organizations potentially eligible to be included in the registry and to confirm the information of organizations currently on file. NERC believes this is a prudent activity at this time because:

- NERC was the only applicant to file with FERC for certification as the ERO created for the U.S. by the Energy Policy Act of 2005 (EPAAct) and FERC Order 672. NERC has also filed with Canadian authorities for similar recognition in their respective jurisdictions.
- FERC's Order 672 directs that owners, operators and users of the bulk power system shall be registered with the ERO and its designees (i.e., regional entities with delegated authority – regional entities).
- Anticipating that it will be certified as the ERO, NERC has also filed its current reliability standards with FERC and with Canadian authorities. Should these be substantially accepted and approved by FERC and appropriate Canadian authorities, they will no longer be voluntary, and organizations that do not fully comply with them may face penalties or other sanctions determined and levied by NERC or the regional entities.

- NERC’s reliability standards include compliance requirements for additional reliability function types beyond the six types registered by earlier registration programs.
- NERC’s ERO application proposes extension and expansion of NERC’s current registration program¹ as the means by which NERC and the regional entities will plan, manage and execute reliability standard compliance oversight of owners, operators, and users of the bulk power system.
- Organizations listed in the compliance registry are subject to NERC’s and the regional entities’ compliance and enforcement programs.

Statement of Issue

As the ERO, NERC intends to comprehensively and thoroughly protect the reliability of the grid. To support this NERC will include in its compliance registry each entity that it concludes is needed to accomplish that goal. However, the potential costs and effort of ensuring that every organization potentially within the scope of “owner, operator, and user of the bulk power system” becomes registered while ignoring their impact upon reliability, might be disproportionate to the improvement in reliability that would reasonably be anticipated from doing so.

In preparation for becoming the ERO, NERC wishes to identify additional organizations that may need to be listed in its compliance registry. Identifying these organizations is necessary and prudent at this time for the purpose of determining resource needs, both at the NERC and regional entity level, and to begin the process of communication with these entities regarding their potential responsibilities and obligations. NERC and the regional entities believe that primary candidate entities can be identified at this time, while other entities can be identified later, as and when needed. Selection principles and criteria for the identification of these initial entities are required.

Resolution

NERC and the regional entities have identified two principles which they believe are key to the entity selection process. These are:

1. There needs to be consistency between regions (i.e., regional entity system footprints) and across the continent with respect to which entities are registered, and;
2. Any entity reasonably deemed material to the reliability of the bulk power system should be registered, irrespective of other considerations.

To address the second principle the regional reliability councils, working with NERC, will (presently) identify and (eventually²) register any entity that they deem material to the reliability of the bulk power system.

In order to promote consistency, NERC, the regional reliability councils and, once they are established, the regional entities and cross-border regional entities (CBREs), intend to use the following criteria as the basis for determining whether particular entities should be identified as

¹See: NERC ERO Application; Exhibit C; Section 500 – Organization Registration and Certification.

² NERC will be unable to require that entities be registered until it has been certified as the ERO.

candidates for registration. All organizations meeting or exceeding the criteria will be identified as candidates.

Load-serving Entity:

- 1) Load-serving entity peak load is > 25 MW and is directly connected to the bulk power system, or;
- 2) Load-serving entity is designated as the responsible entity for facilities that are part of a required regional under-frequency load shedding (UFLS) program designed, installed, and operated for the protection of the bulk power system, or;
- 3) Load-serving entity is designated as the responsible entity for facilities that are part of a required regional under-voltage load shedding (UVLS) program designed, installed, and operated for the protection of the bulk power system.

Distribution Provider:

- 1) Distribution provider system serving >25 MW of peak load that is directly connected to the bulk power system.
 - Exclusion: A distribution provider will not be registered based on this criterion if responsibility for data sharing and reporting to NERC and regional entities have been transferred by acceptable contract to another entity, such as an load-serving entity, balancing authority, transmission operator, G&T cooperative, or municipal joint action agency.
- Or;
- 2) Distribution provider is the responsible entity that owns, controls or operates facilities that are part of any of the following protection systems or programs designed, installed, and operated for the protection of the bulk power system:
 - a. a required regional UFLS program.
 - b. a required regional UVLS program.
 - c. a required regional special protection system.
 - d. a transmission protection system.
 - Exclusion: A distribution provider will not be registered based on these criteria if effective control and responsibility for maintenance and operation have been transferred by acceptable contract to another entity, such as an load-serving entity, balancing authority, transmission operator, G&T cooperative, or municipal joint action agency.

Generator Owner / Operator:

- 1) Individual generating unit > 20 MVA (gross nameplate rating) and is directly connected to the bulk power system, or;
- 2) Generating plant/facility > 75 MVA (gross aggregate nameplate rating) or when the entity has responsibility for any facility consisting of one or more units that are connected to the bulk power system at a common bus with total generation above 75 MVA gross nameplate rating, or;
- 3) Any generator, regardless of size, that is a black start unit material to and designated as part of a transmission operator entity's restoration plan, or;

- 4) Any generator, regardless of size, that is determined by the regional entity or CBRE to be material to the reliability of the bulk power system.
 - Exclusion: A generator owner/operator will not be registered based on these criteria if effective control and responsibility for maintenance and operation of the generator/generation have been transferred by acceptable contract to another entity, such as an load-serving entity, G&T cooperative or municipal joint action agency.

Transmission Owner:

- 1) An entity that owns an integrated transmission element associated with the bulk power system 100 kV and above, or lower voltage as defined by the regional entity/CBRE; or
- 2) An entity that owns a transmission element below 100 kV associated with a facility that is included on a critical facilities list that is defined by the regional entity/CBRE, or;
- 3) Ownership of radial transmission facilities serving only load with one transmission source are generally not included in this definition.

Notes to the above Criteria

1. The above are general criteria only. The regional entity or CBRE considering registration of an organization not meeting (e.g., smaller in size than) the criteria may propose registration of that organization if the regional entity or CBRE believes and can *reasonably demonstrate*³ that the organization is a bulk power system owner, or operates, or uses bulk power system assets, and is material to the reliability of the bulk power system. Similarly, the regional entity or CBRE considering not registering an organization that meets the criteria may propose that the organization not be registered if the regional entity or CBRE believes and can reasonably demonstrate that the bulk power system owner, operator, or user does not have a material impact on the reliability of the bulk power system.
2. Organizations may challenge their registration within the compliance registry. Organizations not identified using the criteria may be nominated for registration. Organizations not identified using the criteria, but wishing to be registered, may request that they be registered. For further information refer to: NERC ERO Application; Exhibit C; Section 500 – Organization Registration and Certification; Part 1.3.
3. Distribution providers and load-serving entities meeting the criteria above may be exempt from registration if another entity (such as (i) a generation or transmission cooperative, or similar joint-action agency, or (ii) another balancing authority or transmission operator) is registered in lieu of each such load-serving entity or distribution provider registering individually, provided the entity registered accepts the reliability responsibilities through agreement or other mechanisms.
4. A given entity may be part of a class of entities that individually are unlikely to have a material impact on the reliability of the bulk power system, but that in aggregate could

³ The reasonableness of any such demonstration will be subject to review and remand by NERC itself, or by any agency having regulatory or statutory oversight of NERC as the ERO (e.g., FERC or appropriate Canadian authorities).

have such an impact. This is adequate grounds for registration of the entity and other entities in the class, irrespective of other considerations.

5. Organizations will be responsible to register and to comply with approved reliability standards to the extent that they are owners, operators, and users of the bulk power system. NERC's ERO application includes implicit proposal of the following principles regarding registration:
 - Organizations listed in the compliance registry are responsible and will be monitored, etc, for complying with approved mandatory reliability standards; NERC and REs will not monitor nor hold those not in the registry responsible for compliance with the standards.
 - Required compliance by a given organization to the standards will begin the later of (i) certification of NERC as the ERO; (ii) inclusion of that organization in the compliance registry, and (iii) approval by the appropriate governmental authority of mandatory reliability standards.

If NERC or a regional entity encounters an organization that is not listed in the compliance registry, but which should be subject to the reliability standards, NERC or the regional entity is obligated and will add that organization to the registry, subject to that organization's right to challenge.

CERTIFICATE OF SERVICE

I hereby certify that I have served a copy of the foregoing document upon each person listed on the official service list compiled by the Secretary in this proceeding.

Dated at Washington, DC, this 13th day of June, 2006.

_____/s/ Debra Ann Palmer
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