

150 FERC ¶ 61,108
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Cheryl A. LaFleur, Chairman;
Philip D. Moeller, Tony Clark,
Norman C. Bay, and Colette D. Honorable.

North American Electric Reliability Corporation

Docket No. RR15-2-000

ORDER ON ELECTRIC RELIABILITY ORGANIZATION
RELIABILITY ASSURANCE INITIATIVE AND REQUIRING
COMPLIANCE FILING

(Issued February 19, 2015)

1. On November 3, 2014, the North American Electric Reliability Corporation (NERC), the Commission-certified Electric Reliability Organization (ERO), submitted a filing describing the Reliability Assurance Initiative (RAI), in which NERC plans to transition to a risk-based approach for compliance monitoring and enforcement.

2. As discussed below, the Commission approves NERC's implementation of RAI, finding that NERC's overall goal of focusing ERO and industry compliance resources on higher-risk issues that matter more to reliability is reasonable. However, to ensure that NERC implements RAI in a reasonable and transparent manner, and that the Commission will maintain its oversight role in a meaningful manner, the Commission directs, pursuant to section 215(f) of the Federal Power Act (FPA), that NERC submit a compliance filing proposing revisions to the NERC Rules of Procedure that articulate the RAI concepts and programs.¹ Further, as discussed below, the Commission identifies certain conditions as to NERC's implementation and continued development of the risk-based approach for compliance monitoring and enforcement reflected in RAI. In addition, we require NERC to submit an annual report on RAI, to be submitted within one year from the date of the issuance of this order.

¹ 16 U.S.C. § 824o(f) (2012).

I. Background

A. Section 215 and NERC Compliance Monitoring and Enforcement

3. Section 215(c) of the FPA requires the Commission to certify an ERO to develop mandatory and enforceable Reliability Standards, as well as rules to provide fair and impartial procedures for enforcement of such Standards, subject to Commission review and approval.² This statutory requirement is reflected in section 39.3 of the Commission's regulations.³ In addition, section 215(f) of the FPA requires the ERO to file with the Commission for approval any proposed rule or proposed rule change.⁴

B. NERC Compliance Monitoring and Enforcement

4. On February 3, 2006, the Commission issued Order No. 672 to implement the requirements of section 215 of the FPA governing electric reliability.⁵ On July 20, 2006, the Commission certified NERC as the ERO, including the approval of the NERC Rules of Procedure (NERC Rules) addressing, among other things, the NERC Compliance Monitoring and Enforcement Program (CMEP).⁶ The intent of the ERO compliance program, as noted by the Commission, is to facilitate the "ongoing monitoring of user, owner and operator compliance with Reliability Standards."⁷ The Commission specified that the three required components of an ERO compliance program are: (1) a compliance program that includes proactive compliance audits; (2) an investigation program for

² 16 U.S.C. § 824o(c)(2)(C).

³ 18 C.F.R. § 39.3 (2014).

⁴ 16 U.S.C. § 824o(f).

⁵ *Rules Concerning Certification of the Electric Reliability Organization; and Procedures for the Establishment, Approval, and Enforcement of Electric Reliability Standards*, Order No. 672, FERC Stats. & Regs. ¶ 31,204, *order on reh'g*, Order No. 672-A, FERC Stats. & Regs. ¶ 31,212 (2006).

⁶ *North American Electric Reliability Corp.*, 116 FERC ¶ 61,062, at P 299, *order on reh'g and compliance*, 117 FERC ¶ 61,126 (2006), *order on compliance*, 118 FERC ¶ 61,030, *order on compliance*, 118 FERC ¶ 61,190, *order on clarification and reh'g*, 119 FERC ¶ 61,046 (2007), *rev. denied sub nom. Alcoa Inc. v. FERC*, 564 F.3d 1342 (D.C. Cir. 2009). The CMEP is Appendix 4C to the NERC Rules.

⁷ *North American Electric Reliability Corp.*, 116 FERC ¶ 61,062 at P 293.

alleged violations of Reliability Standards that includes prompt Commission notification of incidents and their dispositions; and (3) a penalty program.⁸

5. On December 20, 2012, the Commission issued an order pursuant to FPA section 215(f) conditionally approving revisions to the NERC Rules of Procedure.⁹ Among the revisions approved in the December 20 Order was a proposal to revise section 5.0 and Sanction Guidelines section 2.2 to grant NERC the flexibility to deviate from the standard CMEP procedures so that other approaches to enforcement could be considered and applied where the circumstances warrant such flexibility. In approving NERC's proposed revision, the Commission explained that the new flexibility should be used in "limited circumstances" as a reasonable exercise of NERC's enforcement discretion.¹⁰

6. On March 15, 2012, the Commission issued an order accepting, with conditions, NERC's petition requesting approval of the Find, Fix, Track and Report (FFT) program to allow NERC to address lesser-risk, remediated possible violations of Reliability Standards through FFT spreadsheet informational filings as opposed to the formal Notice of Penalty process.¹¹ On June 20, 2013, the Commission issued an order accepting NERC's first annual FFT report and approving five enhancements to the FFT program.¹² Most recently, on September 18, 2014, the Commission issued an order accepting NERC's second FFT annual report, as well as approving the expansion of the FFT program to moderate risk possible violations that meet certain Commission-approved criteria.¹³ In approving the expansion of the FFT program, the Commission recognized

⁸ *North American Electric Reliability Corp.*, 116 FERC ¶ 61,062, at P 293 (citing Order No. 672, FERC Stats. & Regs. ¶ 31,204).

⁹ *North American Electric Reliability Corp.*, 141 FERC ¶ 61,241 (2012) (December 20 Order).

¹⁰ *Id.* P 95.

¹¹ *North American Electric Reliability Corp.*, 138 FERC ¶ 61,193 (2012) (March 15 Order); *order on reh'g*, 139 FERC ¶ 61,168 (2012).

¹² *North American Electric Reliability Corp.*, 143 FERC ¶ 61,253 (2013) (June 20 Order).

¹³ *North American Electric Reliability Corp.*, 148 FERC ¶ 61,214 (2014) (September 18 Order) (the expansion of the FFT program to certain moderate risk possible violations followed a pilot program approved by the Commission in the June 20 Order).

the efficiencies that had resulted from the FFT program, but also highlighted situations where NERC and the Regional Entities could improve the risk assessments underlying FFT treatment and provide greater clarity in the information provided to support FFT treatment.¹⁴

II. Description of NERC's Reliability Assurance Initiative

7. In the November 3 Filing, NERC provides an overview of the specific components of RAI. NERC explains that RAI was developed to transition the ERO Enterprise¹⁵ to a risk-based approach for compliance monitoring and enforcement. NERC states that RAI will provide a reasonable assurance of reliability through compliance monitoring, appropriate deterrence through enforcement, and a feedback loop to improve Standards.¹⁶ NERC explains further that this approach benefits reliability, and thereby the public interest, by allowing the ERO Enterprise to focus time and effort on higher-risk issues while still identifying, correcting, and tracking lesser-risk issues.¹⁷

8. NERC explains that RAI is based upon two separate programs - risk-based compliance monitoring and risk-based enforcement, which are outlined below.

A. Risk-Based Compliance Monitoring

9. NERC outlines four components of risk-based compliance monitoring: (1) Risk Elements Identification; (2) Inherent Risk Assessment (IRA); (3) Internal Controls Evaluation (ICE); and (4) CMEP Tools. NERC explains that, pursuant to the first component - Risk Elements Identification - NERC will regularly identify and prioritize ERO-wide risks to reliability based on "significance, likelihood, vulnerability and potential impact to the reliability of the [Bulk-Power System]," as outlined in NERC's *Risk Elements Guide*.¹⁸ NERC states further that the risk elements will be mapped to related Standards and will be used in developing the ERO's annual CMEP

¹⁴ September 18 Order, 148 FERC ¶ 61,214 at PP 28 & 30.

¹⁵ "ERO Enterprise" refers to NERC and the eight Regional Entities.

¹⁶ NERC Filing at 1.

¹⁷ *Id.* at 1-2.

¹⁸ *Id.* at 24; *see*

Implementation Plan, as well as Regional Entity Implementation Plans, and may be updated on a dynamic basis. NERC explains that this process replaces the Actively Monitored List used in prior years.¹⁹

10. NERC explains that the second component of risk-based compliance monitoring - IRA - is a review by a Regional Entity of potential risks posed by an individual entity to the reliability of the Bulk-Power System. NERC notes that an IRA considers factors such as assets, system, geography, interconnectivity, prior compliance history and factors unique to the entity. NERC explains that the results of an entity-specific risk assessment may result in the scope of compliance monitoring for a particular entity to include more, fewer, or different Standards than those contained in the ERO and Regional Entity annual CMEP Implementation Plans.²⁰

11. The third component of risk-based compliance monitoring outlined by NERC - ICE - is a voluntary evaluation by a Regional Entity of an entity's internal controls that detect, correct, and mitigate the entity-specific risks identified in the IRA. NERC states that the ICE may further refine the scope of an audit, including the depth and breadth of a particular area of review, or determine whether an audit is necessary. NERC states that the result of an ICE may decrease the depth and breadth of a particular area of review if the registered entity demonstrates effective internal controls; however, if a registered entity does not demonstrate effective internal controls for a particular area, the scope will not change from that established in the IRA.²¹

12. NERC explains that when the Regional Entity has reasonable assurance that internal controls are functioning to protect reliability in accordance with the Standards, the Regional Entity may rely on those internal controls and, therefore, extensive testing may not be necessary under the CMEP.²² NERC notes that there may be instances where, after an IRA has been completed, an entity posing a small inherent risk is only subject to a limited number of applicable Reliability Standards as part of its compliance monitoring scope. In such instances, an ICE may not significantly further tailor the CMEP monitoring activities applied by the Regional Entity, but could provide an opportunity for improvement in controls that could increase reliability and mitigate risks.

¹⁹ *Id.* at 25.

²⁰ *Id.* at 26.

²¹ *Id.* at 31.

²² *Id.* at 33.

NERC also notes that the complexity of internal controls is scalable depending on the size of an entity.²³

13. NERC explains that under the final component of risk-based compliance monitoring - NERC CMEP Tools - a Regional Entity will determine the type and frequency of application of the compliance monitoring tools (e.g., off-site or on-site audits, spot checks or self-certifications) appropriate for a particular registered entity based on its specific reliability risks as evaluated through IRA and, if used, ICE.²⁴ NERC explains that, while the Regional Entity CMEP implementation plans may indicate the compliance monitoring tools to be used during that implementation year, the Regional Entities will continue to identify appropriate tools to use based on the results of the individual IRAs and ICEs.²⁵

B. Risk-Based Enforcement

14. NERC provides a discussion of two primary components of risk-based enforcement: (1) compliance exceptions, and (2) the self-logging process. First, NERC explains that the compliance exception process currently is intended to identify minimal risk instances of noncompliance that do not warrant a penalty, which will be recorded and mitigated without triggering a formal enforcement action under the CMEP. NERC explains further that a “compliance exception is an alternative disposition method and is not a dismissal, FFT, or Notice of Penalty” and, rather, “is essentially the exercise of enforcement discretion...”²⁶ According to NERC, the compliance exception process builds on the FFT program, but is a distinct enforcement track.

15. NERC states that sections 3.8 and 5.0 of the CMEP provide that an alternative enforcement process such as “compliance exceptions” may be considered and used to

²³ *Id.* at 30-34.

²⁴ *Id.* at 34-35.

²⁵ *Id.* at 34. For example, NERC states, “prior to 2015, Regional Entities conducted audits for all entities on a three- and six-year audit cycle. Using a risk-informed approach, Regional Entities will continue to conduct three-year audits per the [NERC Rules]. However, a registered entity’s IRA, and ICE if used, will determine the frequency and Compliance Audit scope rather than a standardized approach[.]” *Id.*

²⁶ *Id.* at 44. According to NERC, the FFT process will remain an available option for processing matters that do not qualify for compliance exception treatment. *Id.* at 47.

achieve the overall objectives of the compliance program.²⁷ NERC avers that the proposed compliance exception process under RAI provides such an alternative enforcement process for the resolution of minimal risk noncompliance that is fully consistent with the overall objectives of the CMEP. NERC goes on to explain that a common understanding of the levels of risk is fundamental to the continued evolution of a risk-based enforcement program, outlining the three levels of risk it uses as: “serious and substantial,” “moderate,” and “minimal.” NERC explains that a minimal risk determination will be “based on the combination of the subject Reliability Standard requirement and the attendant facts and circumstances.”²⁸ NERC states that, if nothing serious could have occurred and there were complete or significant protections in place to reduce the risk, the risk assessment would likely be minimal. NERC further states that, if something serious could have occurred and there were only some protections in place to reduce risk, the risk assessment would likely be moderate. NERC adds that “lack of harm is not sufficient justification, by itself, for a minimal or moderate risk assessment.”²⁹ Finally, NERC states that, if an instance of noncompliance is related to a serious event, the risk assessment would likely be serious and substantial.³⁰

²⁷ As relevant, section 3.8 of the CMEP states that, “If the Preliminary Screen results in an affirmative determination with respect to the above criteria, a Possible Violation exists and the Compliance Enforcement Authority shall proceed in accordance with Section 5.0, unless an alternative enforcement process is used.” As relevant, section 5.0 of the CMEP states that, “The following enforcement process is undertaken by the Compliance Enforcement Authority following identification of a Possible Violation of a Reliability Standard Requirement by a Registered Entity. However, under the circumstances presented by some Possible Violations, Alleged Violations or Confirmed Violations, absolute adherence to the following enforcement process, to the exclusion of other approaches, may not be the most appropriate, efficient or desirable means by which to achieve the overall objectives of the Compliance Program for NERC, the Compliance Enforcement Authority and the Registered Entity. In such circumstances, other approaches may be considered and employed. The Registered Entity shall be entitled to object to the use of any such other approach.”

²⁸ NERC Filing at 42-43. According to NERC, the risk analysis is based on prior Commission orders and discussed in the ERO Self-Report User Guide. *Id.* at 42, citing March 15 Order, 138 FERC ¶ 61,193 at PP 44-45.

²⁹ *Id.* at 43.

³⁰ *Id.* See also *id.* at 42, identifying examples of “serious and substantial” issues set forth in the March 15 Order, 138 FERC ¶ 61,193 at P 49.

16. NERC states that it will not publicly post compliance exceptions. Rather, Regional Entities will retain records for each compliance exception and provide NERC a summary of the record. NERC states that although it will not publicly file or post compliance exceptions, the Commission will receive a monthly, non-public spreadsheet with a summary of the record on each compliance exception.³¹ NERC explains that it will communicate information regarding the “overall rationale for decisions not to pursue certain matters” through a Compliance Exceptions Overview document that NERC now posts on its website.³² NERC also commits to submit an annual informational filing to the Commission that would review the progress of the program, discuss appropriate enhancements, provide examples of matters processed as compliance exceptions, and discuss observed trends.³³ Beginning in 2015, similar to its oversight of FFTs, NERC regularly will review a sample of compliance exceptions and provide guidance or adjustments on a prospective basis.³⁴ NERC states that its annual review of the compliance exception program will consider the inclusion of moderate risk noncompliance in the future.³⁵

17. NERC asserts that it is appropriate to treat compliance exceptions as non-public, contending that regulatory agencies, including the Commission, maintain as non-public the existence of ongoing investigations, as well as the decision to close a matter based on the application of enforcement discretion. NERC states that publicly posting compliance exceptions may adversely impact an entity’s reputation without making a formal decision regarding a violation. Further, NERC states that posting individual accounts of trivial instances of noncompliance does not provide a benefit, diverts resources that should be allocated elsewhere, and “dilutes the message” provided by the public disposition of higher-risk matters (i.e., the attention drawn to entities involved in high-risk compliance matters is diluted if entities involved in trivial matters are also made public).³⁶

³¹ *Id.* at 44.

³² *See id.* at 50 (referencing NERC’s Compliance Exceptions Overview Document, available at: <http://www.nerc.com/pa/comp/Pages/Reliability-Assurance-Initiative.aspx>).

³³ *Id.* at 51.

³⁴ *Id.* at 55.

³⁵ *Id.* at 46.

³⁶ *Id.* at 51-53.

18. Regarding the second component of risk-based enforcement, NERC states that the self-logging process will allow registered entities with demonstrated effective management practices to self-identify, assess, and mitigate minimal risk instances of noncompliance and then record the issue on a log in lieu of individually self-reporting each instance of possible noncompliance. NERC states that a log will contain a detailed description of the issue, the risk assessment, and the mitigating activities completed or to be completed. NERC explains that the Regional Entity will periodically review and approve the log and, once approved, the logged issues typically will be resolved as compliance exceptions.

19. NERC states that participation in the self-logging program is voluntary, and a Regional Entity will determine whether an entity is eligible to self-log. NERC identifies six eligibility criteria for self-logging: (1) the entity's history of initiative and recognition of compliance obligations, (2) reliable and accurate self-reporting of non-compliance, (3) history of timely and thorough mitigation, (4) quality of internal compliance program, (5) cooperation with the Regional Entity during compliance monitoring, enforcement, and Regional Entity outreach activities, and (6) performance during compliance audits. NERC states further that, while an ICE will inform a Regional Entity's decision regarding an entity's participation in the self-logging program, an ICE is not a prerequisite for participation. NERC also explains that a registered entity may be eligible to self-log noncompliance with certain Standards but not others, and that the registered entities may lose eligibility to self-log for various reasons.³⁷

20. NERC explains that there are two processes by which a registered entity can qualify for compliance exception treatment. First, NERC states that a Regional Entity can make a case-by-case determination that an instance of noncompliance qualifies as a compliance exception based on the underlying facts and circumstances, including: "what happened, why, where and when;" potential and actual level of risk to reliability; the quality of a registered entity's internal compliance program; and the presence and applicability of aggravating factors, such as repeat or repetitive noncompliance. Second, NERC states that a self-logged compliance matter, described below, is "presumed to be appropriate" for disposition as a compliance exception.³⁸

21. NERC states that a compliance exception must be mitigated within twelve months of a Regional Entity notifying an entity that the underlying issue of noncompliance will be resolved as a compliance exception without an enforcement action. NERC adds that,

³⁷ *Id.* at 55-64.

³⁸ *Id.* at 43-54.

similar to FFTs, when a Regional Entity disposes of a matter that has yet to be mitigated as a compliance exception, the record must include the expected completion date for mitigation, the justification for the time required to mitigate an issue, and a description of the compensating measures in place during the period of noncompliance.³⁹ NERC states further that the failure to mitigate an issue within the established timeframe, or any material misrepresentation, “will result in rescission of the eligibility for compliance exception treatment.”⁴⁰

22. NERC explains that a compliance exception is part of an entity’s compliance history “only to the extent that it serves to inform the Regional Entity and NERC of the minimal risk issues that are detected and corrected by the entity, and may inform the Regional Entity’s decision on how to treat future noncompliance with the same or similar facts.”⁴¹ NERC explains that repeat compliance exceptions may not always be indicative of poor performance and may, in fact, be evidence of robust controls in place to detect and correct instances of noncompliance as they occur.⁴²

III. Notice of Filing, Interventions, and Comments

23. Notice of NERC’s November 3, 2014, filing was published in the *Federal Register*, 79 Fed. Reg. 68,230 (2014), with comments due on or before December 3, 2014.⁴³ Exelon Corporation filed a timely motion to intervene. American Public Power Association, Electricity Consumers Resource Council, Large Public Power Council, National Rural Electric Cooperative Association, and Transmission Access Policy Group, filing collectively as Joint Commenters; Edison Electric Institute and Electric Power Supply Association, filing collectively as the Associations; and Midcontinent Independent System Operator, Inc. (MISO), filed timely motions to intervene and comments.

³⁹ *Id.* at 48.

⁴⁰ *Id.* at 49.

⁴¹ *Id.* at 44.

⁴² *Id.* at 44.

⁴³ While NERC styled the submission as an informational filing, the Commission publicly noticed the filing for comment. *Cf.*, *PSEG Energy Resources & Trade LLC*, 134 FERC ¶ 61,080 (2011); *ISO New England, Inc.*, 128 FERC ¶ 61,135 (2009) (Commission acting on pleading titled as informational filing).

24. All commenters support RAI as described in NERC's filing as a means of helping to focus the ERO Enterprise's limited compliance and enforcement resources based on risk to the reliability of the Bulk-Power System. As discussed below, the commenters do not agree, however, on the appropriate level of transparency that should accompany the implementation of RAI. Joint Commenters argue that transparency is necessary, at least for the first two years as RAI is implemented, while the Associations generally argue that greater transparency, in the form of reporting and public posting of self-logging and compliance exceptions, is unnecessary. MISO encourages the Commission to keep compliance exceptions and logs non-public to avoid the risk that registered entities would be more hesitant to report certain issues on their logs.

IV. Discussion

25. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2014), the timely motions to intervene filed by Exelon, Joint Commenters, the Associations, and MISO serve to make them parties to this proceeding.

26. We approve NERC's implementation of RAI, as described in the November 3 filing, agreeing that NERC's overall goal of focusing ERO and industry compliance resources on higher-risk issues that matter more to reliability is reasonable. However, pursuant to section 215(f) of the FPA, we direct NERC to submit a compliance filing that includes proposed revisions to the NERC Rules of Procedure to articulate the RAI concepts and programs.⁴⁴ In addition, we set forth certain conditions pertaining to the implementation and continued development of RAI. These conditions are intended to ensure that NERC implements RAI in a reasonable and transparent manner, and that the Commission will maintain a meaningful oversight role, as discussed below. We also require NERC to file an annual report on RAI, the first to be submitted within one year from the date of the issuance of this order, as discussed below.

27. In approving the FFT program, the Commission stated that while "the FFT initiative represents a significant change in the paradigm for monitoring and enforcing compliance with Reliability Standards," experience with NERC's compliance program supported granting "the flexibility to more efficiently process and track lesser-risk violations in order to focus their resources on issues that pose the greatest risk to reliability."⁴⁵ NERC's continued experience with compliance monitoring and

⁴⁴ 16 U.S.C. § 824o(f).

⁴⁵ March 15 Order, 138 FERC ¶ 61,193 at P 1.

enforcement, reflected in noted improvements in NERC's performance,⁴⁶ supports the significant shift to the risk-based approach for compliance monitoring and enforcement reflected in RAI. We support an approach to compliance monitoring and enforcement that focuses time and effort on higher-risk issues while still identifying, correcting, and tracking lesser-risk issues.⁴⁷

28. Below, we discuss the following matters: (A) revisions to the NERC Rules of Procedure to articulate the RAI concepts and programs; (B) transparency of the compliance exception process; (C) qualifications for the self-logging program; (D) the treatment of compliance exceptions in an entity's compliance history; (E) finality of compliance exceptions; and (F) annual reporting requirement.

A. Inclusion of RAI Concepts in NERC Rules of Procedure

29. As an initial matter, while we support the objective of the development of the risk-based approach for compliance monitoring and enforcement, we believe that NERC must include fundamental RAI concepts and elements in the NERC Rules of Procedure. We are not persuaded by NERC's filing that the general language regarding "alternative enforcement processes" set forth in sections 3.8 and 5.0 of the CMEP provides an adequate basis for implementing the major shift in approach represented by the RAI framework.⁴⁸ NERC's filing indicates that a significant percentage of compliance matters will be processed pursuant to the new compliance exception and logging

⁴⁶ See *North American Electric Reliability Corp.*, 149 FERC ¶ 61,141 (2014) (noting improvements in NERC's compliance monitoring and enforcement program).

⁴⁷ The adoption of the streamlined RAI programs to process lower risk compliance matters suggest that there may be provisions of Reliability Standards that provide little protection to the reliable operation of the Bulk-Power System, and we support NERC's efforts to identify such provision for proposed retirement. See *Electric Reliability Organization Proposal to Retire Requirements in Reliability Standards*, Order No. 788, 145 FERC ¶ 61,147 (2013) (approving retirement of requirements that provide little protection for Bulk-Power System reliability or are redundant with other aspects of Reliability Standards).

⁴⁸ As explained by NERC, under RAI "the transformation to focus on identifying and prioritizing risks replaces a static, one-size-fits-all list of Reliability Standards and prioritizes functions and Reliability Standards based on risk to determine the appropriate oversight method." NERC Filing at 21.

programs.⁴⁹ Yet, unlike other NERC compliance processes, there would be no mention of the RAI processes in the NERC Rules of Procedure. Indeed, in approving proposed revisions to section 5.0 to grant NERC the flexibility to deviate from the standard CMEP procedures where warranted, the Commission stated that it understood that the flexibility granted to NERC through the revised language “would be used under limited circumstances” and “should be limited to a reasonable exercise of NERC’s enforcement discretion.”⁵⁰ The significant changes to compliance monitoring and enforcement reflected in RAI go beyond the scope of what we then understood and intended.

30. We do not believe that the availability of RAI guidance documents and the information provided in NERC’s RAI filing, all subject to change without prior Commission notification and approval, provide for adequate Commission oversight and transparency and certainty for others. To be clear, we do not expect NERC to include in the Rules of Procedure detailed procedures that would unduly hamstring the intended flexibility and streamlined processes that are the hallmark of RAI. We do, however, conclude that it is appropriate, both for purposes of maintaining meaningful Commission oversight and ensuring that the ERO has rules that “provide fair and impartial procedures for enforcement...,”⁵¹ that the NERC Rules of Procedure, at a minimum, recognize the existence of the RAI processes, articulate basic RAI concepts and define fundamental RAI elements, and require Commission approval for significant changes in RAI as NERC further develops and implements its risk-based approach.⁵²

31. As noted above, FPA section 215(f) requires the ERO to file any proposed rule or proposed rule change with the Commission for review and approval.⁵³ Therefore, we

⁴⁹ *E.g.*, NERC Filing at p. 39, n. 30 (approximately 70 percent of instances of noncompliance posed a minimal risk to the system reliability during 2013 and 2014). NERC indicates that many minimal risk matters are eligible for processing as compliance exceptions and subject to self-logging.

⁵⁰ December 20 Order, 141 FERC ¶ 61,241 at P 95.

⁵¹ 16 U.S.C. § 824o(c)(2)(C).

⁵² For example, similar to the process that NERC used for the initial FFT program and its subsequent expansions, NERC should provide to the Commission advance notice for Commission consideration any expansion of the compliance exception approach to possible violations that are deemed to present a moderate risk to Bulk-Power System reliability. *See* NERC Filing at 46.

⁵³ 16 U.S.C. § 824o(f). The Commission will provide public notice of the proposed revisions and opportunity for comment.

direct NERC to submit a compliance filing within 90 days of the date of this order proposing revisions to the NERC Rules of Procedure to articulate the RAI concepts and programs in the CMEP.

32. In addition, NERC states that it is currently developing measures of success to evaluate the risk-based approach to compliance monitoring and enforcement.⁵⁴ NERC also asserts that it uses a combination of review processes to ensure that the Regional Entities are implementing the CMEP effectively. We find that NERC's commitment to conduct Regional Entity reviews during the first quarter of 2015 is appropriate in order to ensure the program is implemented properly at its outset.⁵⁵ However, we find NERC's plan for oversight beyond these reviews to be lacking in specifics. In its 90-day compliance filing, NERC should provide details on: a) its oversight processes for the RAI program and b) how it intends to measure the success of the risk-based approach to compliance monitoring and enforcement, to include the types of data-driven metrics it will track as the RAI program develops.

B. Transparency of Compliance Exceptions

33. As noted above, NERC states that it will not publicly file or post compliance exceptions but, rather, rely on non-public monthly submissions to the Commission and an annual informational filing that includes, among other things, observed trends and examples of matters treated as compliance exceptions. NERC asserts that it is appropriate to treat compliance exceptions as non-public based on the treatment of investigations and use of enforcement discretion by regulatory agencies, including the Commission, and that publicly posting compliance exceptions may adversely impact an entity's reputation without making a formal decision regarding a violation, especially when associated with trivial instances of noncompliance.

34. The commenters do not agree on the appropriate level of transparency that should accompany the implementation of RAI. Joint Commenters argue that transparency is essential, at least for the first two years as RAI is implemented, "to educating industry to avoid and mitigate noncompliance with reliability standards, and to maintain the credibility of NERC's compliance and enforcement regime."⁵⁶ In addition, Joint

⁵⁴ See NERC Filing at 15.

⁵⁵ See NERC Petition at 16 ("NERC will conduct Regional Entity reviews during the first quarter of 2015 with the intent of supporting conceptual consistency in the application of the ERO Enterprise's risk-based approach").

⁵⁶ Joint Commenters Comments at 9.

Commenters assert that public disclosure of compliance exceptions would neither be an undue burden on NERC, nor an undue intrusion into NERC's enforcement discretion.⁵⁷

35. The Associations, for their part, argue that greater transparency in the form of “more extensive reporting and public posting of self-logging and compliance exceptions” is unnecessary.⁵⁸ The Associations assert that the annual report proposed by NERC will provide sufficient information to evaluate the effectiveness of RAI and NERC's exercise of enforcement discretion. The Associations proffer that requiring greater transparency “will discourage use of these important tools and is contrary to the overall RAI principle that compliance and enforcement, and the associated reporting and burden, should be aligned to risk.”⁵⁹ Likewise, MISO encourages the Commission to keep compliance exceptions and logs non-public to avoid the risk that registered entities would be more hesitant to report on their logs “issues that are ambiguous or issues about which the disposition of the violation is likely to be uncertain.”⁶⁰

36. We will require NERC to publicly post compliance exceptions in a manner similar to how FFTs are currently posted.⁶¹ We find arguments that publicly posting compliance exceptions is unnecessary or will discourage entities from taking advantage of the efficiencies of RAI unpersuasive. Public disclosure of compliance exceptions would appear to require only minimal additional resources since information will be compiled monthly in a spreadsheet and provided to the Commission. Moreover, the Commission's requirement for NERC to publicly post FFTs does not appear to have been a burden on registered entities, as NERC states that since 2011, FFTs were used to process over 2,000 instances of non-compliance. Rather, we agree with Joint Commenters that transparency in compliance and enforcement matters is beneficial to educate industry and provide additional oversight of the ERO Enterprise. It also serves to allow interested registered entities and other parties to measure consistency across entities, classes of entities, or Regional Entities, as well as demonstrating the quality of registered entities'

⁵⁷ *Id.* at 10-11.

⁵⁸ Associations Comments at 7.

⁵⁹ *Id.* at 7.

⁶⁰ MISO Comments at 5.

⁶¹ NERC's rationale to not make compliance exceptions public because there is no formal decision regarding a violation under the compliance exception process is similar to the argument the Commission rejected with regard to FFTs. *See* March 15 Order, 138 FERC ¶ 61,193 at P 68.

internal controls programs, particularly an entity's ability to swiftly and effectively identify, assess, and correct possible instances of noncompliance.

37. The Commission has recently addressed the appropriate flexibility and associated transparency for compliance and enforcement actions such as FFTs. Among the enhancements to the FFT program approved in the June 20 Order noted above was a proposal to publicly post FFTs on a common website on a monthly basis, as opposed to NERC submitting a monthly informational filing to the Commission.⁶² In approving the public posting of FFTs instead of monthly informational filings, the Commission noted that the proposal "will allow NERC and the Regional Entities to more efficiently report on FFTs."⁶³ We find that the current flexibility provided to the FFT program reflects the risk associated with the underlying instances of noncompliance, and that treating compliance exceptions in a manner similar to FFTs will provide a reasonable level of transparency with minimum effort.

38. The Commission has also maintained a consistent view with regard to transparency in compliance monitoring and enforcement matters. Specifically, in an order directing NERC to make public the disposition of compliance matters through FFT, the Commission stated:

Because there may be similarly situated registered entities, public disclosure of the identity of the entity in an FFT informational filing will provide industry with valuable information on compliance issues. Further, public disclosure will make the full information regarding an FFT matter available to state regulators and the public, thus, providing additional accountability and deterrence.⁶⁴

More recently, in an order addressing NERC's five-year performance assessment, the Commission stated that it "expect[s] NERC to continue making information publicly available concerning possible non-compliance (other than those involving physical security or cybersecurity concerns) resolved through any and all processing methods."⁶⁵ Thus, requiring public disclosure of compliance exceptions is consistent with

⁶² June 20 Order, 143 FERC ¶ 61,253 at P 38.

⁶³ *Id.*

⁶⁴ *North American Electric Reliability Corp.*, 138 FERC ¶ 61,193, at P 68 (2012).

⁶⁵ *North American Electric Reliability Corp.*, 149 FERC ¶ 61,141, at P 72 (2014).

Commission precedent regarding transparency in ERO compliance and enforcement matters.⁶⁶

39. Accordingly, we condition our approval of NERC's RAI implementation on NERC making information regarding non-CIP and CIP compliance exceptions available to the public on an ongoing basis as currently provided for FFTs.⁶⁷

C. Qualification for Self-Logging

40. As noted above, NERC states that participation in the self-logging program is voluntary, and a Regional Entity will determine whether an entity is eligible to self-log based upon six eligibility criteria. Specifically, NERC states that the criteria for self-logging are: (1) the entity's history of initiative and recognition of compliance obligations, (2) reliable and accurate self-reporting of non-compliance, (3) history of timely and thorough mitigation, (4) quality of internal compliance program, (5) cooperation with the Regional Entity during compliance monitoring, enforcement and Regional Entity outreach activities, and (6) performance during compliance audits. NERC states further that, while an ICE will inform a Regional Entity's decision regarding an entity's participation in the self-logging program, an ICE is not a prerequisite for participation.

41. We find it unreasonable to grant the flexibility inherent in self-logging without some level of formal review of an entity's internal controls. The concept of self-logging instances of noncompliance represents a significant change in NERC's oversight of registered entities. Registered entities will, in effect, self-regulate compliance with the Reliability Standards with minimal oversight, including the possibility that some

⁶⁶ See *North American Electric Reliability Corp.*, 116 FERC ¶ 61,062, at P 404 (2006); *North American Electric Reliability Corp.*, 138 FERC ¶ 61,193, at P 68 (2012) (finding it reasonable to view the closure of a possible violation in an FFT as a negotiated disposition so as to require its public disclosure as provided in 18 C.F.R. § 39.7(b)(4)).

⁶⁷ In addition to the name of the registered entity (for non-CIP compliance exceptions), compliance exceptions should, at a minimum, identify how the matter was identified, mitigated, and resolved (i.e., case-by-case compliance exception or self-logged compliance exception). We presume that all self-logged items should be treated as compliance exceptions unless additional risk factors are involved and, therefore, expect that all self-logged items will be included in the posting. We direct NERC to work with Commission staff to ensure they can review each posting of compliance exceptions in an effective and efficient manner, as the Commission previously provided for FFT postings. See June 20 Order, 143 FERC ¶ 61,253 at P 39.

registered entities would not experience a compliance audit for more than six years. While it may be reasonable to scale an entity's ICE based on risk, we do not find it reasonable to grant the level of flexibility inherent in self-logging where a Regional Entity has not confirmed the existence - or quality - of an entity's internal controls.

42. Therefore, we condition our approval of NERC's RAI implementation on NERC requiring some level of formal review of an entity's internal controls before granting the flexibility to self-log instances of noncompliance. NERC should address in its 90-day compliance filing, a methodology for assessing an entity's internal controls and the circumstances under which an alternate methodology will be used in place of an ICE.

43. In addition, it is not clear what basis Regional Entities will use to validate an entity's log of self-identified possible violations, or how such a review would compare to the review of self-reported potential violations. Considering the significant change in compliance and enforcement that could occur with self-logging, we believe that it is worthwhile to have some level of standardization of the content and review of an entity's compliance logs that would allow for consistency and ease of compilation and comparison - without taking away flexibility or failing to account for differences among entities in their size and approaches to internal controls. Accordingly, we direct NERC to address in its compliance filing the establishment of an appropriate level of standardization for the content and review of an entity's compliance logs.

D. Treatment of Compliance Exceptions in Compliance History

44. We accept NERC's proposal that compliance exceptions not be included in a registered entity's compliance history for penalty purposes. However, we believe that there is one specific scenario in which an entity's history of compliance exceptions would be directly relevant. In particular, earlier compliance exceptions may be relevant to an entity's compliance history where a later violation classified as "serious" and/or "substantial" follows or occurs because of the entity's unsuccessful or partial remediation of the compliance exception(s), or remediation of the compliance exception(s) reasonably could have enabled the entity to prevent the later serious or substantial violation, but did not.⁶⁸ In such situations, a matter treated as a compliance exception relates to a later serious or substantial violation, indicating that the registered entity failed to remediate the

⁶⁸ The latter situation could occur, for example, with respect to a transmission owner's compliance exception for FAC-008-3 by rating a transmission line inconsistently with its facility ratings methodology if another of the entity's transmission lines later sagged into a tree, causing a serious violation of FAC-003-2, because the entity failed to rate the other line consistent with its facility ratings methodology.

compliance exception or prevent similar violations, or that its response otherwise was insufficient or too limited in scope.⁶⁹ The facts relating to the entity's prior compliance exceptions may be relevant to the later violation and, as such, may inform any enforcement action associated with the later "serious" and/or "substantial" violation.⁷⁰

45. Based on the same rationale, we condition our approval on the relevant Regional Entity assessing any subsequent noncompliance of the same or closely-related Standards and Requirements to determine whether the registered entity should continue to qualify for compliance exception treatment regarding the subject of the repeat noncompliance.⁷¹ While we recognize that subsequent noncompliance of the same or closely-related Standards and Requirements in and of itself should not disqualify an entity from RAI, repeat noncompliance could be indicative of shortcomings in an entity's internal controls or other serious concerns. This understanding appears to be consistent with NERC's, as NERC recognizes that an entity's history of compliance exceptions "... may inform the Regional Entity's decision on how to treat future noncompliance with the same or similar facts."⁷²

46. Accordingly, we condition our approval of RAI on having NERC and the Regional Entities: (1) consider a history of compliance exceptions where the failure to fully remediate the underlying compliance matter contributes to a subsequent serious and/or substantial noncompliance matter; and (2) assess subsequent noncompliance to

⁶⁹ Cf. March 15 Order, 138 FERC ¶ 61,193 at P 64 (In discussing how an FFT would be factored into a registered entity's compliance history, the Commission observed, "[A]nalysis of a poor compliance history may reveal, for example, shortcomings in the registered entity's training program [.]")

⁷⁰ Violations that are serious or substantial are more concerning on a risk basis than other violations. Also, consistent with what we have explained previously, the categorization as serious or substantial should depend on risk and compensating measures at the time of the violation, not on after-the-fact determinations of actual harm. September 18 Order, 148 FERC ¶ 61,214 at P 26.

⁷¹ See *North American Electric Reliability Corp.*, 132 FERC ¶ 61,182, at PP 5-8 (2010) (providing guidance to NERC and Regional Entities on assessing compliance history for an entity's prior violations of the same or closely-related Reliability Standards and requirements).

⁷² NERC Filing at 44. We also agree with NERC's statement that repeat violations could be due in some instances to a registered entity's use of robust internal controls to detect and correct violations as they occur. See *supra* P 22.

determine whether an entity should continue to qualify for compliance exception treatment, as described above.

E. Finality of Compliance Exceptions

47. We recognize that the transition to a risk-based approach for compliance monitoring and enforcement reflects an expansion of NERC's enforcement discretion. The Commission retains its independent enforcement authority pursuant to FPA section 215(e)(3), and this includes further review of a compliance exception after it has been reported to the Commission.⁷³ In recognition of the need to bring finality to matters addressed through the RAI process, we adopt a time limit for Commission review of compliance exceptions similar to the treatment of FFT informational filings.⁷⁴ Specifically, the Commission will consider a compliance exception to be closed sixty days after the compliance exception is reported to the Commission, subject to the limitations outlined below.

48. First, we will not reopen a compliance exception for review unless the Commission provides notice during the sixty-day period that it will review a specific matter. As is the case with the Commission review of FFTs, the sixty-day period is necessary given the possibility that a large number of compliance exceptions could be filed each month. However, the Commission expects to exercise its authority to review compliance exceptions infrequently and only in limited and rare circumstances, such as in situations where the described remedial action does not appear to mitigate the underlying noncompliance, where an event that appears to have posed more than a minimal risk to the reliability of the Bulk-Power System was processed as a compliance exception, or where the Commission determines that there was a pattern of non-compliance and NERC has not adequately explained why the matter is appropriate for compliance exception treatment. Where the Commission initiates a review of a compliance exception, the Commission will review it in a timely manner, but is not committing to complete each review within the sixty-day period. In addition, the Commission retains the discretion to review a compliance exception reported to the Commission even after the sixty-day period if it finds that compliance exception treatment was obtained based on a material misrepresentation of the facts underlying the compliance exception.⁷⁵

⁷³ 16 U.S.C. § 824o(e)(3).

⁷⁴ See March 15 Order, 138 FERC ¶ 61,193 at PP 71-72.

⁷⁵ *Id.* P 72.

F. Annual Filing

49. NERC states that it will make an annual informational filing with the Commission “reviewing the progress of the [RAI] program and considering any enhancements or expansions that may be necessary.”⁷⁶ NERC states further that the informational filing would include observed trends by standard, region or other categories, as well as examples of matters treated as compliance exceptions. We find the annual report content suggested by NERC reasonable and direct NERC to submit an informational filing on RAI, including the information outlined in NERC’s November 3 filing, with the Commission annually, along with the following items.

50. The annual report should also address the interplay between the RAI program and other NERC program areas. One important example would be the feedback loop that NERC describes from RAI to the Reliability Standards development process.⁷⁷ NERC should explain the feedback process and give examples of how compliance or enforcement matters influenced the process. Another such area of interest is the analysis of Bulk-Power System events. NERC has previously stated that “[t]he anatomy of major disturbances, such as the August 2003 Blackout, reveals it is often a combination of relatively lesser mistakes and problems occurring simultaneously that precipitate a major disturbance.”⁷⁸ NERC should address how RAI enables NERC to focus attention on such events as indicators of this type of reliability risk and identify resulting actions taken to identify and mitigate the types of minor mistakes or problems known to be causal of major events.

51. The annual report should also address whether a baseline audit is needed to properly evaluate a registered entity’s internal controls. NERC provides two examples from the Midwest Reliability Organization⁷⁹ that do not clearly explain whether the review of internal controls under ICE is based only on a review of program documents, or whether the review also examines the effectiveness of the program, i.e., a baseline evaluation of actual compliance performance under the entity’s internal controls. A process that reviews both program documentation and the actual effectiveness of a

⁷⁶ NERC Filing at 51.

⁷⁷ *Id.* at 19.

⁷⁸ *Petition Requesting Approval of New Enforcement Mechanisms*, Docket No. RC11-6-000, at 12 (September 30, 2011).

⁷⁹ NERC Filing at 32-33.

program may be appropriate to ensure adequate compliance with the risk-based oversight under RAI.

52. The annual report should address and provide an update on NERC's oversight of the RAI program (e.g. whether RAI has been implemented in a consistent manner across the Regional Entities). In addition, the annual report should address and provide an update on the metrics that NERC has or will employ to measure the effectiveness of the RAI program.⁸⁰ Finally, the annual report should also address and provide examples of how a Regional Entity assesses and factors into a registered entity's risk assessment and audit scope that entity's use of NERC Alerts, Lessons Learned, Reliability Guidelines, and other NERC learning tools.

The Commission orders:

(A) The Commission hereby accepts NERC's implementation of RAI, subject to conditions, as set forth in the body of this order.

(B) NERC is hereby directed to make a compliance filing within 90 days of the date of issuance of this order, as discussed in the body of this order.

(C) NERC is hereby directed to file an annual report on RAI, the first to be submitted within one year from the date of the issuance of this order, as discussed in the body of this order.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.

⁸⁰ *Id.* at 15 (NERC "...is currently developing measures of success to evaluate the risk-based approach to compliance monitoring and enforcement").