

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

**RULES CONCERNING CERTIFICATION )  
OF THE ELECTRIC RELIABILITY )  
ORGANIZATION; AND PROCEDURES )  
FOR THE ESTABLISHMENT, APPROVAL, )  
AND ENFORCEMENT OF ELECTRIC )  
RELIABILITY STANDARDS )**

**Docket No. RM05-30-000**

**COMMENTS OF THE  
NORTH AMERICAN ELECTRIC RELIABILITY COUNCIL  
ON NOTICE OF PROPOSED RULEMAKING**

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## TABLE OF CONTENTS

|  |    |
|--|----|
| STATEMENT OF INTEREST.....   | 2  |
| COMMENTS.....  | 3  |
| I. THE NOPR PROVIDES A POSITIVE FRAMEWORK FOR THE ESTABLISHMENT<br>OF AN EFFECTIVE ERO.....  | 4  |
| II. CERTAIN LIMITED REVISIONS TO THE PROPOSED RULES<br>WILL FURTHER STRENGTHEN THE EFFECTIVENESS OF THE<br>ERO AND THE PROGRAM FOR ENSURING THE RELIABILITY<br>OF THE BULK POWER SYSTEM..... | 9  |
| III. RESPONSES TO SPECIFIC QUESTIONS RAISED IN THE NOPR.....   | 18 |
| IV. THE NOPR RAISES CERTAIN LEGAL ISSUES THAT SHOULD<br>BE CONSIDERED IN THE FINAL RULE.....   | 47 |
| CONCLUSION.....  | 53 |
| APPENDIX   |    |

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The North American Electric Reliability Council (“NERC”) hereby submits its comments in response to the Notice of Proposed Rulemaking issued in the above-referenced docket.<sup>1</sup> The Commission issued the NOPR in response to the enactment of subtitle A of the Electricity Modernization Act of 2005 (the “Act”),<sup>2</sup> which mandates the establishment of an Electric Reliability Organization (“ERO”) and electric reliability standards. The Act requires the Commission to develop rules to implement the provisions of subtitle A within 180 days of enactment.

These comments contain four parts. Part I reviews the Commission’s proposed rule. The Commission has done a commendable job of establishing the needed framework in the United States, and a guide for working cooperatively with Canada and Mexico, to develop an effective

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<sup>1</sup> *Rules Concerning Certification of the Electric Reliability Organization; and Procedures for the Establishment, Approval, and Enforcement of Electric Reliability Standards*, 70 Fed. Reg. 53177 (Sept. 7, 2005) (hereinafter cited as “NOPR”).

<sup>2</sup> The Electricity Modernization Act of 2005 is Title XII of the Energy Policy Act of 2005. The Energy Policy Act of 2005 was signed into law by President George W. Bush on August 8, 2005.

North American ERO. Part II describes certain modifications to the proposed rule that will further strengthen the effectiveness of the ERO. In Part III, NERC responds to each of the questions in the NOPR. Finally, Part IV addresses discrete legal issues raised by the NOPR.

### **STATEMENT OF INTEREST**

NERC was formed as a voluntary electric reliability organization shortly after the 1965 blackout in the northeastern United States and eastern Canada. Since its inception, NERC has adopted operating policies and planning standards to ensure the reliability of the bulk power system in North America. In response to the blackout of August 2003, NERC transformed its existing operating policies and planning standards into Version 0 reliability standards, which became effective on April 1, 2005. These standards are a comprehensive and measurable set of standards for the bulk power system.<sup>3</sup> NERC continues to improve and expand these standards through its open standards development process, which has been accredited by the American National Standards Institute (“ANSI”).

NERC has been engaged in the promotion and evaluation of bulk power system reliability and the development of reliability standards for almost 40 years. As a result, NERC is uniquely suited to become the North American ERO and plans to submit an application to that effect at the appropriate time. NERC, therefore, has a direct and substantial interest in the outcome of this rulemaking proceeding.

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<sup>3</sup> Certain of the Version 0 reliability standards relating to Transmission Line Loading Relief (“TLR”) orders have been filed with the Commission as part of NERC’s Electric Tariff, Original Volume No. 1. Moreover, the Commission has held that adherence to NERC’s Version 0 reliability standards constitutes “good utility practice.” *Policy Statement on Matters Related to Bulk Power System Reliability*, 110 FERC ¶ 61,096 at P 7 (2005).

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### **COMMENTS**

NERC commends the Commission's proposed rule. It embodies all the necessary themes and lays out the required principles, responsibilities, and authorities needed to create and oversee a strong and effective international ERO without being overly specific or restrictive. As such, it allows the ERO the flexibility it needs to develop its detailed rules of procedure, consistent with this larger foundation, and include them in its application. In short, NERC is confident that with only modest adjustments and strengthening, the proposed rule can be successfully implemented as written.

Self-regulation of the reliability of the bulk power system under the legislation is in fact *shared* regulation in which industry experts work in concert with regulators and self-regulators. Shared regulation promotes a culture of integrity that pervades the entire industry and one in which reliability will flourish. NERC looks forward to working in a close partnership with the

Commission, with appropriate regulatory authorities in Canada and Mexico, and with the regional entities to develop a strong and effective North American ERO.<sup>4</sup>

**I. THE NOPR PROVIDES A POSITIVE FRAMEWORK FOR THE ESTABLISHMENT OF AN EFFECTIVE ERO.**

The NOPR establishes a solid foundation on which to build a rigorous system of mandatory reliability rules. These rules will be developed and enforced by a strong and effective international ERO subject to Commission oversight within the United States. The criteria and requirements for the ERO provided for in the NOPR will meet the universally recognized need for a new system of clear, effective, and enforceable reliability standards.

The Commission has for many years been a steadfast supporter of and advocate for mandatory reliability standards and reliability legislation. The Commission's endorsement of the consensus legislative proposal for establishment of an ERO was an important contribution to the eventual enactment of the Act. In the NOPR, the Commission continues to recognize the importance of mandatory, enforceable reliability standards. To meet that goal, the NOPR (1) proposes appropriate criteria for the certification of the ERO, (2) contains a workable method for Commission approval of reliability standards, (3) recognizes the benefits inherent in delegating enforcement authority to regional entities, (4) proposes a reasonable funding mechanism, (5) recognizes that cross-border issues must be addressed, and (6) sets forth accountability standards.

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<sup>4</sup> Because a portion of Mexico is also interconnected with the United States and further interconnections are contemplated, Mexico also has an interest in these issues. NERC understands that legislation may be necessary in Mexico before that country would be in a position to provide recognition to the ERO. NERC will work with Mexican authorities as that becomes appropriate.

**A. The Final Rule should adopt the proposed certification criteria.**

The NOPR's proposed certification criteria faithfully reflect the requirements of the Act and will ensure the development of a strong ERO to carry out the statutory mandates. Congress identified a number of key characteristics required of the ERO, and the proposed rules reflect each of these characteristics. For example, the NOPR requires the ERO to be independent of users, owners, and operators involved in the bulk power industry. NOPR at P 40. Nonetheless, the ERO must also develop a process by which all stakeholders are fairly represented and through which the ERO will make balanced decisions reflecting stakeholder interests. *Id.* The proposed rule also requires that the ERO have an inclusive process for the development of reliability standards and a demonstrable commitment to gain recognition in Canada and Mexico. *Id.* at P 41.

The NOPR also proposes that any dues, fees, or charges imposed by or to fund the ERO be equitably allocated among end users. NOPR at P 40. The proposed rule also requires fair and impartial enforcement procedures, with effective penalties for non-compliance. The proposed rule will permit financial penalties as well as limitations on activities, functions, or operations to be imposed upon entities that violate the reliability standards. *Id.* at P 58. The certification criteria proposed in the NOPR will ensure that the Commission and the nation have confidence in the ability of the ERO to fully and fairly perform its reliability mission. The Final Rule should, therefore, adopt the proposed certification requirements set forth in the NOPR.

**B. The Final Rule should contain the proposed mechanism for approval of reliability standards.**

The NOPR clearly recognizes that the electric industry, working through the ERO (and duly constituted regional entities), will develop reliability standards based on industry expertise

and years of experience.<sup>5</sup> This recognition is crucial to gaining the support and confidence of the industry and in ensuring the highest degree of compliance. Of similar importance, the NOPR recognizes the Act's mandate that "due weight" be given to the technical content of a reliability standard developed by the ERO or by a regional entity organized on an interconnection basis. NOPR at P 45. In accordance with the Act, the Commission also correctly proposes to provide no deference when considering the effects a reliability standard may have on competition. *Id.* at P 48. These proposals properly reflect the fact that the ERO possesses expertise in the reliability arena, while the Commission is the expert with respect to competition in the energy industry.

To ensure that interested parties have the opportunity to express their views regarding proposed reliability standards, the Commission expects to provide notice and an opportunity for hearing on any such standards, or modifications to such standards, submitted by the ERO. NOPR at P 47. Moreover, the proposed requirement that the ERO submit, with a proposed reliability standard or modification to an existing standard, a concise statement of the basis and purpose of the proposed standard or modification and a summary of the process used to develop the standard or modification will facilitate an open and public process for the development of reliability standards. Proposed Regulation Section 38.4(a). Again, this open process will enhance confidence in the ERO, the reliability standards it establishes and enforces, and the reliability of the bulk power system. The NOPR also properly proposes to permit the Commission to remand to the ERO a reliability standard that it does not find to be just and reasonable. NOPR at P 50. The Commission, however, will not be authorized to rewrite the rejected standard. *Id.* at P 53 (noting that "the Commission's options are limited . . . to either

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<sup>5</sup> NERC expects the North American Energy Standards Board ("NAESB") to continue to provide expertise regarding complementary business practices.

accepting or remanding a proposed Reliability Standard”). This proposal permits the ERO to bring its technical expertise regarding reliability to bear at all phases of the drafting of reliability standards and to reflect and respect the international nature of the ERO.

In sum, the Final Rule should include the process for the development and approval of reliability standards proposed in the NOPR.

**C. The NOPR’s proposals properly recognize the potential benefits of regional entities.**

The Act permits the ERO to delegate enforcement authority regarding reliability standards to regional entities, and the NOPR recognizes the potential benefits of such delegation. NOPR at P 79. If a regional entity meets the statutory requirements for governance and the requirements established through the regional delegation agreements approved by the Commission, the delegation of enforcement authority to the regional entity will promote the effective and efficient administration of reliability. *Id.* Clearly, regional entities are in a better geographic position to enforce reliability standards across the continent.

**D. The NOPR proposes a workable mechanism to ensure reasonable costs are fairly allocated.**

The NOPR is correct in asserting that “certainty regarding the funding of the ERO is essential for the stability and ultimate success of the organization.” NOPR at P 99. Funding certainty is essential for the ERO in order to carry out its mission (particularly since the ERO will be organized as a not-for-profit entity) and to the industry in order to assure that costs associated with the ERO will remain reasonable. In addition, the proposed regulations appropriately require all entities subject to the Commission’s jurisdiction to pay the assessment developed by the ERO and approved by the Commission in order to provide the ERO with necessary funding to carry out its reliability mission. Proposed Regulation Section 38.13(d). In

particular, the NOPR expressly recognizes that the “net energy for load” methodology of allocating costs associated with the ERO and its reliability program meets the Act’s requirement that the funding mechanism provide for equitable allocation and assessment of ERO dues, fees, and charges. NOPR at P 102. The net energy for load methodology ensures that those that benefit from the bulk power system are assessed the costs of ensuring a reliable bulk power system and should be included as part of the Final Rule.

**E. The NOPR appropriately recognizes cross-border issues.**

The interconnected electric grid extends beyond the borders of the United States into Canada and Mexico. An ERO with participation from varied interests from affected countries, and with oversight from the Commission and appropriate regulatory authorities in Canada and Mexico (at the point Mexican authorities are prepared to undertake that role), is a practical and effective way to develop the common set of reliability standards needed for the international grid.

The NOPR appropriately recognizes the cross-border issues resulting from the continental nature of the electric grid. In particular, the Commission expressly recognizes that cross-border regional entities may emerge, and sets as a condition for certification a commitment that the ERO will undertake efforts to obtain recognition in Canada and Mexico. NOPR at P 41. The Final Rule should adopt this certification requirement.

**F. The Final Rule should include the proposed provisions ensuring that the ERO and regional entities are held accountable for maintaining and ensuring compliance with reliability standards.**

The goal of the Act is to enhance reliability in the bulk power system through the development of an ERO with the authority to (1) develop a mandatory set of reliability standards and (2) enforce those standards. To meet this goal, the NOPR properly includes various

provisions for assuring that the ERO and regional entities develop effective reliability standards and compliance programs.

The proposed regulations provide the Commission with various mechanisms to oversee the ERO and the regional entities. For example, under the proposed rules, the Commission has the authority to review the budgets of the ERO and regional entities on an annual basis, the authority to periodically audit the ERO and regional entities, the authority to require the ERO to submit or modify a reliability standard, the authority to review enforcement actions taken by the ERO or regional entities, the authority to require the submission of information regarding violations of reliability standards, the authority to require the submission of periodic reports, and the authority to order a change to ERO rules. The Commission also has general authority to take any action necessary or appropriate to ensure compliance with a reliability standard. In general, the Commission will have the oversight authority within the U.S. necessary to hold the ERO and regional entities accountable for their actions and ensure they are acting in the public interest. This oversight authority will increase confidence in the ability of the ERO and the regional entities to carry out the duties assigned to them by the Act and, therefore, should be included in the Final Rule.

**II. CERTAIN LIMITED REVISIONS TO THE PROPOSED RULES WILL FURTHER STRENGTHEN THE EFFECTIVENESS OF THE ERO AND THE PROGRAM FOR ENSURING THE RELIABILITY OF THE BULK POWER SYSTEM.**

As noted above, the Commission's proposed rules appropriately address nearly all significant issues involved in establishing an effective ERO pursuant to the Act. This part of NERC's comments will focus on those aspects of the proposed regulations that should be modified in order to more fully realize the goals of the Act. In addition, attached hereto as an

appendix is a red-lined version of the proposed regulations showing the modifications proposed in these comments.

**A. The regulations should require compliance by all owners, operators, and users of the bulk power system.**

The regulations should make clear that all owners, operators, and users of the bulk power system must comply with (1) the Commission's regulations implementing the Act, (2) approved reliability standards, (3) rules adopted by the ERO and regional entities, and (4) requests for data submitted by the ERO and regional entities issued in furtherance of the Act. The Commission should place all users of the bulk power system on notice of their obligations under the Act and the regulations. In addition, the ERO and regional entities may need to obtain information or data from users of the bulk power system in order to develop reliability standards and to ensure compliance with those standards. The Final Rule should require users of the bulk power system to respond to such requests for data.

The Commission should modify proposed Section 38.2 by renumbering the proposed provision as subpart (a) and by adding a subpart (b). Subpart (b) should read as follows:

Within the United States (other than Alaska and Hawaii), all owners, operators, and Users of the Bulk-Power System shall comply with the regulations of the Commission adopted under this Part, Reliability Standards made effective under this Part, and the rules adopted by the Electric Reliability Organization or a Regional Entity and made effective under this Part, and shall supply all data and information reasonably requested by the Electric Reliability Organization or a Regional Entity that is necessary or appropriate to carrying out its responsibilities under Section 215 of the Federal Power Act.<sup>6</sup>

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<sup>6</sup> As discussed in I.C. *infra*, NERC proposes addition of the defined term "Users of the Bulk-Power System" to the regulation.

**B. The regulations should require all owners, operators, and users of the bulk power system to register with the ERO and appropriate regional entity.**

The Act and the regulations proposed in the NOPR charge the ERO and the regional entities with monitoring and enforcing approved reliability standards. The ERO and regional entities must have a mechanism to learn the identity of the owners, operators, and users of the bulk power system in order to ensure that all such entities are complying with the reliability standards. Such a requirement will also enable those entities to gain a clear understanding of their responsibilities. The Final Rule should, therefore, include a provision requiring owners, operators, and users of the bulk power system to register with the ERO and the appropriate regional entity. Section 38.2 of the proposed rules should be changed to include the following subpart (c):

To facilitate compliance with, monitoring of, and enforcement of Reliability Standards, each owner, operator, and User of the Bulk-Power System shall register with the Electric Reliability Organization and the Regional Entity for each region within which it owns, operates, or uses bulk power facilities, in such manner as prescribed in the rules of the Electric Reliability Organization and each applicable Regional Entity.

**C. Certain definitions should be added to Section 38.1 of the proposed regulations.**

To ensure that the final regulations implementing the Act have sufficient clarity, the Final Rule should include the following definitions in Section 38.1:

*End User* means customers that receive service at retail.

*Net Energy for Load* means balancing authority area generation (less station use), plus energy received from other balancing authority areas, less energy delivered to balancing authority areas through interchange. It includes balancing authority area losses, but excludes energy required for storage at energy storage facilities.

*Physical Security Standards* means Reliability Standards adopted to safeguard personnel and prevent unauthorized access to critical equipment, systems, material, and information at critical facilities.

*User of the Bulk-Power System* means any entity that sells, purchases, or transmits electric power directly over the Bulk-Power system, or that maintains facilities or controls systems that are part of the Bulk-Power system, or that is a system operator. The term excludes customers that receive service at retail that do not otherwise sell, purchase, or transmit power over the Bulk-Power System or own, operate or maintain, control or operate facilities or systems that are part of the Bulk-Power System.

Each of these terms is used in the proposed rules. The suggested additional definitions were developed by NERC through its technical committees.

**D. The proposed funding mechanism should be modified to include costs of regional entities in the costs to be recovered.**

Section 38.13 of the proposed regulations governs funding of the ERO. Having certainty in the funding of regional entities is as essential to the success and stability of those programs as it is for the ERO itself. The Final Rule should include the following as subpart (b) to Section 38.13:<sup>7</sup>

The annual budget submission shall include amounts for those activities of Regional Entities that are delegated or assigned pursuant to Section 38.7 of this Part.

In addition, the Commission should modify the proposed funding mechanism to permit the ERO to seek additional funding during the course of a year in order to respond to unforeseen and extraordinary circumstances. This type of emergency funding mechanism will enhance reliability of the bulk power system by affording the ERO the ability to continue operations following extraordinary circumstances or to undertake important special or unplanned projects,

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<sup>7</sup> Proposed subparts (b) through (e) should be re-lettered as subparts (c) through (f).

funding of which cannot await the next budget and funding cycle. Section 38.13 should be amended to include the following subpart (g):

On a demonstration of unforeseen and extraordinary circumstances requiring additional funds prior to the next funding cycle, the Electric Reliability Organization may file with the Commission for authorization to collect a special assessment. Such filing shall include the supporting materials consistent with paragraph (a) of this subpart and a proposed recovery mechanism. After notice and an opportunity for comment, the Commission will approve or modify such request.

**E. The Final Rule should ensure that there is no “gap” between EROs following the recertification process.**

The NOPR states that the ERO must meet the applicable certification requirements on an ongoing basis and proposes to require the ERO to become recertified every five years. NOPR at PP 39, 42. NERC agrees with this interpretation of the Act and the proposed recertification requirement. In addition, the recertification requirement should be modified in two respects, to ensure that there is no time gap in which an ERO is not operating. First, the rule should provide that the ERO’s certification does not automatically expire at the end of the five- (or six, as NERC proposes) year period, but rather only expires if the Commission actually decertifies the ERO. Second, the rule should provide that if the Commission decertifies the ERO following its periodic review, the Commission should permit that entity to continue as the ERO until the certification of a replacement ERO. North America should not be left without an entity accountable for developing or enforcing reliability standards pending the certification of a successor ERO. In these comments, NERC suggests that one of the accountability mechanisms the Commission should use is an independent audit of the ERO’s compliance enforcement program every three years. A six-year recertification cycle would coincide with one of those independent audits, which could provide useful information to the Commission as it considers

recertification. In order to avoid a time gap between EROs, the following sentence should be added to Section 38.3(c) of the proposed rules:

The ERO remains certified until the Commission issues a final order decertifying the ERO. If the previously approved ERO is not recertified as the ERO, the previously approved ERO shall continue to serve as the ERO until the Commission is able to certify a replacement ERO.

**F. Enforcement proceedings should not be open to the public.**

The Commission proposes to provide the public with notice and opportunity to comment if an alleged violator appeals an enforcement decision taken by the ERO to the Commission. Proposed Regulation Section 38.3(d)(3). The Commission should reconsider this aspect of the NOPR. At the outset, it should be noted that the Commission does not currently provide the public the ability to participate in its enforcement actions. Enforcement actions are considered to be a matter for the Commission and the alleged violator. Enforcement actions related to reliability standards should be treated no differently, except that the ERO or applicable regional entity must be involved in any appeals. A reliability enforcement action will address only two issues: whether the alleged violator committed a violation of a reliability standard and, if so, what is the appropriate penalty. If the public is permitted to intervene, it is likely that extraneous issues will be introduced into the proceeding, which will simply delay final resolution or settlement of the enforcement matter. Following final resolution, the Commission should — as it does now with respect to other enforcement matters — issue a public report and order regarding the final determination.

In addition, the regulations proposed in the NOPR provide that enforcement actions involving Cybersecurity Incidents will be non-public. Proposed Regulation Section 38.5(d)(8). While the public should generally be informed, on an after-the-fact basis, of enforcement actions

taken by the Commission, most enforcement actions regarding reliability matters are likely to involve confidential or sensitive information. Enforcement actions regarding physical assets that make up the bulk power system may well involve such information. For example, actions to enforce reliability standards may include critical energy infrastructure information. Proposed Section 38.5(d)(8) should be modified, therefore, to permit non-public enforcement actions involving all confidential or sensitive information. The first sentence of that regulation in the Final Rule should read:

Unless the Commission determines otherwise, an enforcement action pursuant to section 38.5 involving confidential or sensitive information will be non-public.

NERC's current *Guidelines for Reporting and Disclosure* require public disclosure of all confirmed violations. That requirement should be carried forward in the ERO's rules of procedure. The fact that an enforcement proceeding involving confidential and sensitive information might have been conducted in a non-public way would not mean that a confirmed violation would not be made public. Such public disclosure would simply need to recognize that some details regarding the matter would need to remain protected.

**G. RTOs, ISOs, and other transmission organizations should participate in the development of reliability standards in order to avoid conflicts with existing tariff provisions.**

The NOPR correctly points out that reliability standards adopted by the ERO may conflict with tariffs or rules of various transmission organizations, such as regional transmission organizations ("RTOs") or independent system operators ("ISOs"). NOPR at PP 87-91. The proposed rules contain a mechanism to resolve such conflicts. Proposed Regulation Section 38.9.

The proposed conflict resolution mechanism is appropriate and should be included in the Final Rule. The Preamble to the Final Rule should also make clear that transmission organizations are encouraged to participate in the process by which reliability standards are developed. If the transmission organizations participate in the standard setting process, it is far less likely that conflicts with their tariffs will arise. The ERO and transmission organizations should take reasonable efforts to avoid such conflicts, rather than resort to use of the provisions of Section 38.9.

**H. The relationship between the Commission, the ERO, and regional entities should be linear in nature.**

The NOPR indicates that, in certain respects, regional entities will be held accountable directly to the Commission. For example, the Commission suggests that it may remand rejected reliability standards to regional entities. NOPR at P 52. The Final Rule should make clear that regional entities are accountable, through their delegation agreements, to the ERO for their delegated responsibilities. The ERO should, in turn, be accountable directly to the Commission for issues relating to reliability within the United States.<sup>8</sup>

If the Commission interacts directly with regional entities, the ERO's authority may be undermined and its effectiveness hampered. In addition, as some regional entities are likely to extend beyond the borders of the United States, direct Commission interaction may undermine the international nature of the ERO and the regional entities and also raise concerns with regulatory authorities in Canada or Mexico. The Commission, given its direct authority over the ERO, has ample ability to ensure that the ERO is holding regional entities accountable for their actions. The Commission will be requested in NERC's ERO application to approve a pro forma

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<sup>8</sup> In instances involving cross-border issues, the ERO may also be accountable to appropriate regulatory authorities in Canada or Mexico.

delegation agreement. Part of the ERO's accountability to the Commission will be to ensure that the regional entities are effectively implementing the delegation agreements. Should the ERO be unable or unwilling to ensure accountability by regional entities, the Commission may require the ERO to do so. In sum, the Preamble to the Final Rule should reflect a linear relationship between the Commission, the ERO, and regional entities.

**I. The Final Rule should permit the ERO to approve regional standards.**

The NOPR properly supports the idea of consistent reliability standards across North America. NOPR at P 44. Thus, the NOPR proposes that all standards, even regional standards, be approved by the ERO and filed with the Commission (and appropriate regulatory authorities in Canada). NOPR at PP 45-46, 79. NERC agrees with this proposal.

The NOPR states, however, that "regional variances would supplement ERO Reliability Standards, not substitute for them." NOPR at P 80. Regional variations may well be necessary to ensure reliable operation of the bulk power system. When issuing the Final Rule, the Commission should clarify that regional standards may go beyond ERO standards, but may not be less stringent than ERO standards and may not conflict with ERO standards.

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In sum, the Commission has proposed a solid framework for a strong and effective international ERO to assure compliance with mandatory reliability standards and thereby ensure the reliability of the bulk power system in North America. The recommendations made in Part II of these comments build on that foundation and further strengthen the ERO in its ability to meet its responsibilities under the Act.

### **III. RESPONSES TO SPECIFIC QUESTIONS RAISED IN THE NOPR**

NERC is providing these responses to the Commission's questions, so that the Commission has NERC's current position on all the issues presented in the NOPR. At the same time, NERC continues to work with representatives from stakeholder interests to achieve an industry consensus position on a variety of issues (such as budgets and funding, membership, penalties and sanctions, and delegations of authority to regional entities). With the few additions recommended in Part II of these comments, NERC believes that the regulatory text proposed by the Commission in the NOPR strikes the appropriate balance between deciding issues in the rulemaking and leaving them for resolution in connection with the Commission's certification of an applicant as the ERO. Deferring decision on the remaining issues until the application phase will provide the industry the opportunity to reach consensus on these remaining issues. NERC believes that achieving consensus on as many issues as possible will be the best way to ensure both the success of the ERO and the reliability of the bulk power system in North America.

**NOPR P 8: On August 9, 2005, the Federal-Provincial-Territorial (FPT) Working Group in Canada and DOE jointly submitted to the Commission "Principles for an Electric Reliability Organization that Can Function on an International Basis" (bilateral principles) based on these stakeholder dialogues. We invite comment on those principles.**

The Bilateral Electric Reliability Oversight Group ("Oversight Group") principles are essential because they provide a foundation to guide the operation of the ERO as an international organization. The bilateral principles are a sound basis on which NERC expects that the appropriate regulatory authorities in Canada will extend recognition to the ERO.<sup>9</sup> Equally

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<sup>9</sup> At a number of places in these comments NERC refers to appropriate regulatory authorities in Canada. NERC understands that, at present, there is no regulatory authority in Mexico that is in a position to participate in oversight of the ERO. NERC believes that, at such time as a regulatory authority in Mexico is prepared to participate in that oversight, then the consultation and coordination discussed here with respect to Canada should also be extended to Mexico.

important for the process of assuring the effectiveness of the ERO as an international organization will be the Terms of Reference for the Bilateral Electric Reliability Oversight Group, executed by the Commission, the U.S. Department of Energy, and the Federal-Provincial-Territorial Electricity Working Group of the Council of Energy Ministers of Canada on June 30, 2005 (the “Terms of Reference”). The Terms of Reference establish the Oversight Group as an ongoing group whose role is to consult on the establishment of an international reliability framework and monitor its operation to help identify issues related to international aspects and options for resolution of those issues. NERC worked closely with the Oversight Group in a series of workshops to help fashion the bilateral principles. NERC supports the bilateral principles and will be guided by them in developing its rules of procedure and ERO application, in the following areas:

- Governance
- Membership
- Funding
- Remand of a standard
- Mechanisms to coordinate standards actions among regulators
- Enforcement<sup>10</sup>
- Audits
- Delegation of authority to regional entities
- Separation of reliability authorities and operating entities such as regional transmission organizations

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<sup>10</sup> The principle states that regulators in the U.S. and Canada should have the option of either enforcing standards directly or relying on the ERO or the regional entity. NERC urges that the appropriate regulatory authorities place primary responsibility for enforcement on the ERO and the regional entity, subject to regulatory review and oversight.

**NOPR P 42: We seek comments on what would constitute a reasonable length of time for such periodic certification [of the ERO] to be effective. For example, is a five-year certification period appropriate? How far in advance should an ERO be required to submit its application for recertification before its current certification period expires?**

Recertification every six years would be an appropriate exercise of the Commission's oversight responsibility. This is consistent with an independent audit of the ERO being completed every three years, as described in response to a later question. An independent audit will enhance the ability of international regulators to review the ERO's actions. The Commission will have extensive, ongoing oversight of the ERO through the annual budget and funding mechanism review and approval processes. The ERO's application for recertification should be submitted one year prior to the expiration of the six-year term. The certification should not automatically lapse at the end of six years. To prevent an unintended lapse in authority to set and enforce reliability standards, certification should remain in place until the Commission makes a recertification decision; or, if the Commission decides to decertify the ERO, the ERO should remain in place until a successor is certified. Consistent with the Terms of Reference, the Commission should consult with appropriate officials in Canada regarding any recertification decision.

**NOPR P 43: We seek comments on whether the term "end users" should be defined for purposes of the ERO's equitable allocation of reasonable dues, fees and charges among end users? Should "end users" be defined as customers using net energy for load? Should the term "end users" be defined in terms of those who directly or indirectly use the transmission system since "Bulk-Power System" is defined to exclude facilities used in local distribution of electric energy? Should "end users" be limited to entities transmitting electricity through the transmission facilities of others? Or, might "end users" include the transmission facility owners and operators whose businesses depend on the reliable operations of the interconnected Bulk-Power System?**

In Part II, NERC recommends defining "end users" and "users of the bulk power system," and provides suggested regulatory text. In brief, "end users" should be defined as ultimate customers who use electricity, that is, those who receive electric service at retail. In this

context, the “end users” serve as a basis of allocation of reasonable dues, fees, and charges on a net energy for load (“NEL”) basis. “Users of the Bulk-Power System” should include direct users who transact business on the bulk power system, but not customers who indirectly receive electricity from the bulk power system. These direct users would be subject to Commission jurisdiction under the legislation and required to comply with ERO reliability standards.

**NOPR P 48: Proposed Section 38.4(b)(3) provides that the Commission will not defer to the ERO or a Regional Entity with respect to the effect of a Reliability Standard or modification to a Reliability Standard on competition. How should the Commission define “competition” in this context? Commenters are asked to provide examples regarding the effect of a Reliability Standard on competition.**

Commerce and reliability are closely linked in the bulk power system. A reliable bulk power system is necessary for commerce in electricity to take place. Conversely, commercial solutions can provide for reliability. That is why NERC has a Memorandum of Understanding with NAESB, which is developing complementary business practice standards.

NERC has five market-reliability interface principles in its current standards process to guide its efforts:

1. The planning and operation of bulk electric systems shall recognize that reliability is an essential requirement of a robust North American economy.
2. A reliability standard shall not give any market participant an unfair competitive advantage.
3. A reliability standard shall neither mandate nor prohibit any specific market structure.
4. A reliability standard shall not preclude market solutions to achieving compliance with that standard.
5. A reliability standard shall not require the public disclosure of commercially sensitive information. All market participants shall have equal opportunity to access commercially non-sensitive information that is required for compliance with reliability standards.

**NOPR P 54: The Commission seeks comment on whether the Commission has authority to void a previously accepted Reliability Standard. If the Commission has such authority, is it beneficial to have such a provision in the Commission's regulations?**

The Act clearly provides the Commission with the authority to remand standards to the ERO or to direct the development of a standard at any time (that is, whether or not the Commission has previously approved the standard). The Act does not, however, expressly provide the Commission with authority to void a previously accepted Reliability Standard. Rather than voiding an existing standard, NERC would encourage the Commission to remand a standard to the ERO for revision or development of a replacement standard through the ERO process, which is accredited by the ANSI and has the attributes of due process, openness, and balance. Each standard provides a necessary component to the overall objective of a reliable bulk power system. Voiding an individual standard could leave a gap in the requirements while a replacement standard was being developed. Because the ERO is establishing international standards, the action of one jurisdiction to void a standard may create a conflict of standards or impact the reliability of the bulk power system in other jurisdictions. Therefore, a remanded standard should remain in effect during the time the ERO is responding to the remand. At a minimum, such action with respect to a standard should be coordinated with other regulators, as contemplated by the Terms of Reference. The ERO procedures should require the ERO to give significant attention to a remand, request, or directive for a standard from the Commission, but the response should be developed through the ERO's standards process.

**NOPR P 55: Section 215(d) of the FPA and proposed regulation section 38.4 provide that the Commission may approve a proposed Reliability Standard or modification to a proposed Reliability Standard if it determines that the standard is “just, reasonable, not unduly discriminatory or preferential, and in the public interest.” The Commission seeks comment on how this standard should be applied in the context of reviewing proposed Reliability Standards.**

The Commission should, as anticipated by the legislation and the NOPR, defer to the technical expertise of the industry (as expressed through the ERO’s standards development process) as to how to address the Commission’s concerns with the standards.<sup>11</sup> The industry should, through the standards process, strive to be responsive to the expectations of the Commission. The Commission will from time-to-time seek to address certain reliability issues by remanding proposed reliability standards to the ERO or by directing that a new standard be developed or an existing standard be modified. The ERO process for developing and approving reliability standards, which is accredited by ANSI, has important attributes valued by the Commission, including due process, openness, and balance. The current process will result in the most technically sound standards with inputs from a broad base of experts. The Commission should consider that the ERO is an international organization and that overly prescriptive directives on standards could jeopardize the ERO’s ability to assure consistent reliability standards across international borders. At a minimum, the Commission should engage in prior consultations with other appropriate regulatory authorities regarding such actions, as contemplated by the Terms of Reference.

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<sup>11</sup> The same considerations expressed here with regard to the ERO would apply to an Interconnection-wide regional entity for standards to be applicable on an Interconnection-wide basis.

**NOPR P 56: We seek comments on whether membership in the ERO or a Regional Entity should not be a condition for participation in the ERO's or a Regional Entity's standards development processes.**

NERC does not believe that membership in the ERO or a regional entity should be a condition for participation in the ERO's or a regional entity's standards development process. Those processes should be open to all interested persons. NERC understands that a membership requirement for participation in the standards development process would not be consistent with ANSI's accreditation of NERC's current standards development process.

**NOPR P 57: The Commission notes that the bilateral principles include a provision that if a regulatory authority remands a standard, the ERO should notify all relevant regulatory authorities and should work to ensure that all concerns of such regulatory authorities are addressed prior to resubmission of the standard to the Commission and authorities in Canada. (1) Should the proposed rule specify this process? (2) What are the implications of the remand by a Canadian authority of a Reliability Standard that has been approved by the Commission?**

The rule need not specify the process for coordinating standards actions, since the issue of international coordination affects each of the jurisdictions in the U.S. and Canada. The ERO should, in its rules of procedure submitted in the application for approval by the Commission, address how standards actions will be coordinated among the various jurisdictions. FERC and the appropriate regulatory authorities in Canada should consider the bilateral principles' requirement for notification of all relevant regulatory bodies as a mutually acceptable procedure for international coordination of standards approvals and remands, as well as compliance and other oversight actions. NERC's goal as the ERO would be to establish a common set of North American reliability standards and a consistent application of compliance procedures and penalties across all jurisdictions. Actions need to be coordinated among jurisdictions to avoid adverse impacts in other jurisdictions.

**NOPR P 57: Also, should the ERO certification criteria specify that the number of board members representing each participating country in the ERO, and the opportunities for each country to have an equitable number of members on all committees, must be in rough proportion to total load?**

Yes, the ERO certification criteria should include such a requirement. NERC is committed to the bilateral principles and intends to have equitable representation from each country on its board and major committees. Subordinate groups reporting to the committees need to ensure they have adequate technical expertise, but the ERO should maintain Canadian representation throughout its programs. As Mexican interests become more involved in the ERO's activities, the principle of equitable participation should be extended to Mexico as well. Such representation may be particularly appropriate even now for any cross-border regional entity that includes portions of Mexico within its footprint.

**NOPR P 63: The Commission seeks comment on this proposal [regarding non-public procedures for enforcement matters involving a cyber security incident] and, in addition, seeks comment on (1) whether the proposal provides sufficient due process and (2) the identification of other specific events that should be subject to non-public hearing procedures.**

Enforcement proceedings regarding cyber security incidents should be conducted through a non-public process, as proposed in the NOPR. As described in Part II, *supra*, all enforcement action proceedings at the Commission, not just those involving cyber security incidents, should be conducted through a non-public process, for two reasons:

- (1) Technical investigations into an alleged violation of a standard will almost always require disclosure of critical infrastructure information that should be shared openly with investigators, without concern that such confidential or sensitive information would in turn be made public.

- (2) There should not be a presumption that an entity violated a standard until the investigation and due process have been completed. (This point is addressed again later in this Part III.)

The Commission's proposal provides sufficient due process for the entity alleged to have violated a standard. Conducting the enforcement investigation in a non-public setting does not mean that confirmed violations should remain non-public. NERC now makes public confirmed violations, absent any confidential or sensitive information, once the investigation and any appeals process have been completed. That practice should continue once the ERO is certified.

**NOPR P 71: (1) What is the appropriate appeals process, if any, of an ERO or Regional Entity decision to impose a penalty? Would it be appropriate for the ERO or a Regional Entity with delegated enforcement authority to adopt enforcement, penalty and appeals processes similar to the SRO processes discussed above? Should appeals within the ERO be allowed before appeal to the Commission; should appeal of a penalty imposed by a Regional Entity be taken through the Regional Entity itself, with further appeal to the Commission; or should the appeal be through the ERO in the first instance, then to the Commission?**

The appropriate penalty appeals process of enforcement action taken by an ERO or regional entity must be fair, independent, and nondiscriminatory. The Self-Regulatory Organization ("SRO") appeals processes described in paragraph 70 of the NOPR meet that test. Those processes are also consistent with the processes that NERC and the regional councils have been developing for their compliance programs.

For matters regarding compliance with ERO reliability standards, the ERO will establish principles for the regional entities to use in developing their appeals processes. Each regional entity should have an appeals process that embodies these principles and mirrors the concepts contained in the ERO appeals process. For appeals of a penalty imposed by a regional entity, the regional appeals process should be completed first, with the ERO providing any necessary facilitation and oversight review. If a matter were still in dispute after the regional appeals

process, then the appeal would go through the ERO appeals process. If a matter were still in dispute at the ERO level, then the aggrieved party(s) would bring the appeal before the Commission and/or appropriate authorities in Canada or Mexico as a final step to resolve the dispute.

**NOPR P 71: (2) Should the Commission approve a penalty range or guidelines before the ERO can levy any penalty or sanction for violations, and, if so, should the penalty range or guidelines for a violation be submitted for Commission approval at the same time that the corresponding Reliability Standard is submitted to the Commission for approval?**

The Commission should review and approve an ERO developed enforcement policy that includes sanctioning guidelines and penalty ranges separate from the standards themselves. This would establish an enforceable sanctioning process adopted by the Commission for application by the ERO in the United States. The ERO would apply this policy to levy an appropriate penalty or sanction for a violation. At the time a reliability standard is filed with the Commission for approval, the ERO should indicate what part of the overall sanctioning guidelines and penalty ranges would apply to the particular standard. The standard setting process should not require that each standard have its own range or guidelines for penalties.

**NOPR P 71: (3) Should a single monetary penalty be prescribed for a violation of a particular standard or should a schedule of monetary penalties be prescribed from which to select at the time of an infraction depending upon relevant circumstances such as the number of repeat offenses or length of time before adequate corrections are made to bring the violator into compliance?**

A schedule of monetary penalties, rather than a single monetary penalty, should be prescribed from which an appropriate penalty will be selected depending upon the circumstances surrounding a particular violation. The determination of the monetary penalty associated with a specific violation should be based upon the violation's possible impact on the reliability of the bulk electric system, the ERO enforcement policy, and the specifics of the situation surrounding the violation. The ERO enforcement policy should include a penalty structure that escalates

monetary penalties where appropriate, *e.g.*, based on the number of repeat offenses or length of time the violation persisted. The policy can also be structured to encourage compliance with the standards by reducing the monetary penalty where self-reporting and voluntary corrective actions are taken to resolve a violation.

**NOPR P 71: (4) The Commission interprets section 316A of the FPA, as amended by Congress in the Electricity Modernization Act of 2005, as establishing limits on monetary penalties for violation of Reliability Standards that may be imposed by the ERO, Regional Entities and the Commission. The Commission seeks comment on this interpretation.**

NERC agrees with the Commission's interpretation. In addition, limits on monetary penalties should be developed by the ERO and approved by the Commission and appropriate international regulatory authorities to assure that penalties will not negatively impact the ability of an entity to maintain the reliability of the bulk power system. On the other hand, penalties need to be sufficient to assure that those entities responsible for providing reliability do not make an economic choice to violate a reliability standard, thus degrading reliability, rather than meeting the standard and maintaining the reliability of the bulk power system.

**NOPR P 71: (5) Paragraph (d)(1) of proposed section 38.5 provides that the Commission will review a penalty on its own motion, or upon application of the entity that is the subject of the penalty. Should the Commission determine by rulemaking that certain categories of penalties should be automatically subject to Commission review? For example, should penalties above a certain dollar threshold automatically require Commission review?**

The Commission can rely on those on whom penalties are imposed to seek review of a penalty and need not establish a category of cases that require automatic review. The Commission will always have the option of reviewing a particular case. An automatic review provision may inadvertently involve the Commission in reviewing penalties associated with violations that took place in Canada or Mexico, where review should be conducted by the appropriate regulatory authorities in those countries. In addition, there is no need for review

where there is no contest, i.e., when the penalized entity accepts a finding of violation and penalty and wants to move forward with whatever remedial actions may be necessary.

**NOPR P 71: (6) What types of non-monetary penalties, if any, are appropriate?**

Non-monetary penalties, separate from or in conjunction with monetary penalties, are appropriate for encouraging compliance. Non-monetary penalties could include, among other things, a requirement to carry additional operating reserves for a certain period of time (for a violation of the disturbance control standard) or perhaps a period of probation. In addition, the ERO should be able to take a variety of actions to cause responsible entities to comply with reliability standards. Often these actions will be appropriate prior to or outside the setting of penalties for non-compliance. Examples include: directing the development of a remediation plan or specific corrective actions in response to a system disturbance investigation, increasing audits for marginal performance, or increasing training requirements to correct an operating problem. NERC currently uses letters to industry CEOs to draw executive attention to a reliability problem and would plan to continue using them as the ERO.

**NOPR P 71: (7) Who should receive, and what should be done with monies collected as monetary penalties? Should the monetary penalties collected by the ERO or Regional Entity be used to defray the cost of its enforcement program, or allocated to some other use? Would allowing the ERO or Regional Entity to use penalty money to fund an enforcement program create an appearance of impropriety?**

The ERO should receive all monies collected as monetary penalties for violations of ERO standards in the United States. For each compliance enforcement proceeding, the ERO should first apply monies received as monetary penalties to cover the incremental costs incurred by the ERO and the regional entities in overseeing the enforcement actions associated with the specific violations. This would include monitoring and verifying completion of corrective actions directed upon the entity that committed the violation. It would also include the incremental costs

of any ERO or regional entity studies, analysis, testing, or reporting necessary to verify that the violation was satisfactorily resolved.

The ERO should be authorized to disburse monies to any regional entity that incurs incremental costs associated with supervising corrective actions. When such monies are insufficient to cover the incremental costs of supervising the corrective actions of the violating entity, the ERO and applicable regional entities should allocate the monies proportionate to their incremental costs incurred. If there are no incremental costs to the ERO or regional entity associated with overseeing corrective actions, or there are monies left over, such monies should be returned to the general operating funds of the ERO for the current year and noted as additional surplus at the year-end true up with the ERO budget. If a standard is applicable only within a region, such as an interconnection-wide standard, the regional entity should collect monetary penalties directly and apply the same procedures as described above for a violation of an ERO standard.

NERC does not believe that using monies from penalties in this manner would present a conflict of interest. The Commission and other regulatory authorities would have an annual review of the use of such monies as part of the budget review process. In addition, the budgeting process should include a true up each year pursuant to which penalty revenues will be used to offset operating costs. The ERO cannot, under this proposal, benefit financially from the imposition of monetary penalties.

The Commission should leave these rules somewhat flexible in order to accommodate any different arrangements that may be necessary to address the needs of regulatory authorities in Canada or Mexico.

**NOPR P 71: (8) The Commission notes that the bilateral principles include a provision calling for rigorous audits by the ERO and Regional Entities to ensure the capability to comply with and actual compliance with the Reliability Standards. The bilateral principles also provide for the ERO to take steps to ensure that auditors are properly trained and that the same audit standards apply to all audits conducted by the ERO and Regional Entities. Should the proposed rule specify these audits requirements as part of the ERO certification requirements and the Regional Entity certification and delegation requirements?**

As noted above, NERC supports the bilateral principles on the subject of audits, and NERC would support inclusion of such requirements in the Commission's rule. NERC also supports including a requirement for the ERO to develop and approve audit requirements in the regional entity certification and delegation agreements. Certification and readiness audits ensure the capability to comply with reliability standards on an initial and ongoing basis, while the compliance audits monitor actual compliance with the reliability standards. NERC expects that both programs will include general audit criteria that will apply for audits of the ERO and regional entities and the certification of regional entities. Further, audit requirements for conducting audits by the regional entities should be part of the delegation agreement with regions.

**NOPR P 71: (9) The Commission notes that the bilateral principles provide that RTOs and ISOs should not become Regional Entities, and that the Regional Entities should be distinct from the operators of the system, such as RTOs and ISOs. Should the proposed rule mandate this? What are the enforcement implications of an RTO or ISO that is a Regional Entity? Are there ways for an RTO or ISO to adequately separate its enforcement function from its ownership, use or operation of the Bulk-Power System to fully ensure the independence of the enforcement unit? What process should such an enforcement unit follow to insulate itself from its RTO or ISO organization so that it may undertake any enforcement actions that become necessary against the RTO or ISO? How would this comport with the requirements of section 215 of the FPA?**

NERC supports the bilateral principles that preclude an RTO or ISO from also serving as the regional entity. As a major system operator performing a number of reliability functions, the RTO or ISO is one of the principal entities that must comply with the reliability standards. A

conflict of interest could arise if the RTO or ISO is the entity responsible for monitoring its own compliance with the reliability standards.

**NOPR P 71: (10) Paragraph (e) of proposed section 38.5 states that the Commission may order compliance with a Reliability Standard and may impose a penalty if the Commission finds that the user, owner or operator of the Bulk-Power System has engaged or is about to engage in any acts or practices that constitute or will constitute a violation of a Reliability Standard. Should the Commission clarify in the rule that, in a situation where an entity is about to engage in an act that will constitute a violation of a Reliability Standard, Commission action will be in the form of a compliance order with the goal of preventing the violation from occurring; and further clarify that an entity that has engaged in an actual violation may be subject to both penalties and a compliance order? Are there situations that may warrant penalties where an entity is about to engage in activity that would violate a Reliability Standard but the activity was ultimately averted?**

NERC would support the Commission clarifying in the rule that, in a situation where an entity is about to engage in an act that will constitute a violation of a reliability standard Commission action would take the form of a compliance order, and further clarifying that an entity that has engaged in an actual violation may be subject to both a penalty and a compliance order. NERC believes that most circumstances would not warrant imposition of penalties where an entity was about to engage in a violation of a reliability standard, but did not in fact do so. Imposition of a penalty in such a circumstance would raise serious due process questions that the Commission can easily avoid by not attempting to impose a penalty in that situation. This issue is addressed in more detail in Part IV of these comments.

**NOPR P 71: (11) Paragraph (g) of proposed section 38.5 requires that the ERO and all Regional Entities have in place procedures to notify the Commission of all violations and potential violations of Reliability Standards when the ERO or Regional Entity first notifies the user, owner or operator of the violation or potential violation. We seek comment on what confidentiality protections may be needed, particularly with regard to potential violations. For example, the Commission currently maintains confidential protection of other types of enforcement-related investigations pursuant to section 1b or our regulations, 18 C.F.R. § 1b (2005). Are similar protections needed here?**

For purposes of this question, it is important to distinguish between programs such as NERC's Readiness Audit Program (implemented by NERC) and programs such as NERC's

Compliance Enforcement Program (implemented by the regions). The Readiness Audit Program is specifically aimed at improvement in reliability capabilities and readiness. To encourage entities to willingly share information about the current state of their readiness, it is intentionally non-public, except for a final audit report. The Readiness Audit Program does not include penalties or other sanctions. If, during the course of a readiness audit, a NERC audit team encounters evidence of a possible violation, that matter is turned over to the Compliance Enforcement Program. The possible violation is not processed through the Readiness Audit Program. The ability to maintain this distinction is important to the continuing success of the Readiness Audit Program.

Under NERC's current Compliance Enforcement Program and the disclosure guidelines adopted by the NERC Board of Trustees, compliance investigations and any associated dispute resolution are handled on a non-public basis. Only the results of final, or confirmed, violations are made public, which is similar to how the Commission handles other enforcement actions. NERC currently does not publicly disclose potential violations under investigation. Only confirmed violations are publicly disclosed along with the identity of the violator. Disclosure of a potential violation with the violator's identity could have significant and possibly irreversible negative impacts for the entity even if it is ultimately determined to be compliant. More importantly, it would be extremely difficult for NERC or the regional entities to determine during the information-gathering phase the precise moment that a potential violation exists. Therefore, the ERO and regional entity processes should maintain as confidential the identities of entities being investigated for possible violations, and should provide for disclosure to the Commission the identities of only confirmed violators. Section 38.5(g) of the proposed regulations should, therefore, be amended to eliminate all references to potential violations.

Non-confirmed violations should be reported to the Commission only if the Commission ensures that the reports will remain non-public to protect the identity of the entity involved until the investigation and due process have been completed. Further, some violations may be designated as critical infrastructure information and must be held confidentially regardless of the potential or confirmed status of the violation.

However, if the Commission's Final Rule requires the reporting of potential violations, then the concept of a potential violation would need to be clearly defined. In that context, NERC would propose that "potential violation" should mean the point in the process where the ERO or regional entity has performed at least a preliminary investigation and is prepared to formally charge an entity with having committed the violation. That is the analogous point in governmental processes at which an allegation of a violation is made public. The ERO or regional entity would then go through a process to determine whether in fact the entity committed the violation. The ERO and the regional entities would need to develop an additional stage to their current compliance process, by establishing a formal "charging" step. The issue of potential violations is discussed in more detail in Part IV, *infra*. Again, NERC does not support reporting of potential violations.

**NOPR P 72: The Commission seeks comment on the feasibility and appropriateness of adopting a reliability assessment program similar to the NRC's nuclear power plant assessment program. Also, should the Commission establish a reliability watch list modeled on the NRC's Action Matrix? What features of the NRC program should the Commission adopt? What other features might be added?**

**NOPR P 73: The Commission asks commenters to discuss which aspects of the INPO's programs would serve as useful models for the ERO. What lessons can be drawn from INPO's complementary role with the NRC?**

The questions in paragraphs 72 and 73 will be answered together, by describing three NERC programs — Readiness Audit, Compliance Enforcement, and Reliability Performance.

NERC believes that it has and will continue to learn much from the programs of NRC, INPO, and other regulatory and self-regulatory organizations.

NERC's Readiness Audit Program is based in large measure on the evaluations program of the Institute of Nuclear Power Operations (INPO). The Readiness Audit Program identifies areas for improvement by electric operating entities following an on-site visit. These areas for improvement are not violations of NERC reliability standards, but rather are suggested improvements intended to help the entity become better prepared to meet NERC reliability standards. Readiness Audit reports are posted on NERC's public web site. NERC will continue to monitor INPO's programs for additional items that can be incorporated within the ERO program.<sup>12</sup>

Similar to the NRC's nuclear power plant assessment program, NERC's Compliance Enforcement Program utilizes both inspection findings and performance indicators. Inspection findings are on-site compliance reviews of reliability entities performed by regional compliance enforcement staff, while performance indicators represent self-reporting of noncompliance with reliability standards. The program tracks all violations of reliability standards and the responses of entities to mitigate those violations. NERC is in the process of developing categories of violations based on their severity, frequency, and relative risk to the reliability of the bulk power system. Under this program, the most severe or repeated violations will receive the most attention. This effort emulates, to a great degree, the NRC's Reactor Oversight Process "Action Matrix." As the Commission will be informed of violations of ERO reliability standards and

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<sup>12</sup> Indeed, given the ERO's new compliance enforcement roles with FERC under the Act, one concept that has already been discussed to a limited extent is the establishment of voluntary best practices' user group(s) within the ERO for the express purpose of facilitating candid exchanges of operational "lessons learned" and other best practices among similarly situated entities under arrangements similar to those used by INPO.

ERO actions against those found out of compliance, it should not be necessary for the Commission to establish its own reliability assessment program or reliability “watch list.”

The details of the ERO reliability compliance enforcement program will be included in its rules of procedure, which will accompany the ERO application.

Finally, NERC conducts reviews and investigations of significant system disturbances and unusual operating events for lessons learned through its Reliability Performance Program. These reviews are not designed to identify noncompliance with NERC standards, but rather to understand what impacts different types of events can have on the overall reliability of the bulk power system, how the system responded to actual events, and what the industry can learn by systematically examining them that will help improve system reliability.

If certified as the ERO, NERC will draw on these programs and experiences to continue to refine and improve its rules of procedure.

**NOPR P 76: What mechanism of review and methods of oversight should be used to assure the Commission that the ERO or a Regional Entity is meeting its responsibilities for monitoring compliance with the Reliability Standards?**

The Commission should rely on independent audits of the ERO once every three years to assure compliance with the criteria established by the Commission and the ERO. The independent audit should also serve the needs of other regulatory authorities. Since the ERO is responsible for the operation of the regional entities through the delegation agreements, the ERO should perform an audit of each regional entity at least once every three years and report the results of its audits to the Commission. The process that the ERO uses to audit the regional entities, and the results of these audits, should be included in the independent audit of the ERO.

**NOPR P 77: With respect to any monetary penalties levied directly by the Commission against the ERO or a Regional Entity for violation of the FPA, should the ERO or a Regional Entity be able to recover such penalties through dues, fees, or other charges?**

The Commission has a number of tools to assure the accountability of the ERO and the regional entities, including the authority to review the budgets on an annual basis; the authority to periodically audit the ERO and regional entities; the authority to require an ERO to submit a reliability standard or a modification to a standard; the authority to review enforcement actions taken by the ERO or a regional entity; the authority to require the submission of information on violations or potential violations; and the authority to require a change in ERO or regional entity rules. The Commission also has the periodic recertification and the decertification options discussed in the NOPR. It should be unnecessary for the Commission to resort to monetary penalties to bring about compliance by the ERO. In response to the specific question, the ERO and the regional entities will be organized as non-profit organizations, so they would have no source of funds other than the dues, fees, and charges that they collect from the owners, operators, and users of the bulk power system.

**NOPR P 78: Section 215(e)(5) of the FPA provides that, “[t]he 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 Regional Entity.” Since the ERO and Regional Entity provisions of the Electricity Modernization Act of 2005 are modeled on the SRO provisions of the securities law, and under those provisions, the Securities and Exchange Commission can impose monetary and non-monetary penalties on SRO board members, should the Commission adopt the same approach with respect to the board members of the ERO and Regional Entities?**

As noted in response to the prior question, the Commission has ample tools at its disposal to ensure the accountability of the ERO and the regional entities. Sound policy reasons exist for the Commission to eschew this particular remedy. Foremost, the specter of individual liability for penalties would have a chilling effect on the ability of the ERO to retain and recruit board members of the highest quality. The Commission should pursue a policy that will enable the

ERO to attract the best candidates it can to take on the responsibilities of governing the ERO in performing its critical mission. Directors of the ERO cannot profit monetarily when carrying out their duties, due to the requirement that the directors be independent, i.e., that they have no financial or other interest in any owner, operator, or user of the bulk power system or in any other entity that has a financial interest in the operation of the bulk power system. The Commission has not previously suggested that it has authority to impose personal liability on directors of entities subject to its jurisdiction, and the Commission should not take that step in the Final Rule.

**NOPR P 80: A Regional Entity may also propose Reliability Standards to the ERO that, if ultimately approved by the Commission, would become regional variances in a specific region. Any such regional variances would be ERO variances, not Regional Entity Reliability Standards, since it would be the ERO, not the Regional Entity, which submits the proposed Reliability Standard to the Commission for its review. The Commission anticipates that any such regional variances would supplement ERO Reliability Standards, not substitute for them. The Commission seeks comment on this interpretation.**

NERC agrees with the approach described by the Commission that a regional entity may propose reliability standards that, if approved by the ERO and the Commission, would become part of the reliability standards. To more fully understand this issue, NERC notes that there can be several types of variances that are appropriate. In some cases a proposed ERO standard would conflict with a regional practice, such as a protocol approved by the Commission in a regional transmission organization tariff. In these instances, the regional variance replaces the North American standard with an alternative practice that achieves the same reliability objective and is consistent with the FERC-approved tariff. There are currently seven such regional variances in NERC's approved standards.

A second type of regional variance occurs when the ERO standards require the regional entity to define regional criteria and procedures necessary to implement and achieve the

objectives of the ERO standard. These region-specific criteria and procedures are necessary to accommodate the physical characteristics and limitations of the electric system in each region. Such region-specific implementations that are mandated by the ERO standard should become part of the ERO standards.

A third type of regional variance occurs when a region proposes a regional standard that places additional or more stringent requirements within the region and wishes to enforce the regional variance as mandatory within the region. There can be valid reasons that these additional requirements are necessary to meet the needs of the electric system or loads within a particular area. Such regional variances that will be enforceable under the statute must be approved by the ERO and the Commission.

Beyond these regional requirements that become a part of the reliability standards, the regions will develop system operating and planning protocols, criteria, and procedures that describe how entities within the region have agreed to implement the ERO standards. These additional protocols, criteria, and procedures are not standards and would not be enforceable under the legislation. Accordingly, it would be inappropriate to incorporate them as ERO standards or variances. These regional protocols, criteria, and procedures define an important “middle layer” between the enforceable reliability standards and the operating and planning protocols of each individual entity by providing for accepted practice in implementing the standards.

In summary, NERC believes that all regional variances that are to be mandatory and enforceable under the statute and rule must be approved by the ERO and filed with the Commission (and appropriate regulatory authorities in Canada) for approval, including the three types of ERO variances described above.

NERC is developing rules of procedure for the approval of regional variances and plans to submit those rules with its ERO application for approval by the Commission and regulatory authorities in Canada and Mexico. These rules will also distinguish between approval of regional variances intended to apply on an Interconnection-wide basis and approval of those that are not. The existing NERC reliability standards process addresses the criteria for regional variances and is consistent with the Act and the proposed rule. What remains to be worked out are the specific administrative procedures for approving regional standards developed on an Interconnection-wide basis and those that apply within an Interconnection.

**NOPR P 84: (1) The Commission seeks comment on the following related issues: (1) Should the Commission prescribe a size, scope, or configuration requirement for the Regional Entities? And, if so, what should it be?**

NERC supports the bilateral principles on these matters, which state the following:

- When considering the delegation of authority to a proposed regional entity, the ERO, FERC, and international regulatory authorities should take into consideration whether the size or scope of the proposed regional entity would result in difficulty in conducting cross-border trade.
- A regional entity that has cross-border scope should ensure that each country represented in the region has the opportunity to have members from the country on the board in numbers that reflect the country's approximate percentage of its net energy for load in that region.
- Where possible, the boundaries of regional entities should encompass boundaries of other transmission organizations, such as regional transmission organizations (RTOs) and independent system operators (ISOs).

Any further requirements should be specified in the criteria the ERO develops for delegating authority to a regional entity and in the delegation agreements themselves.

**NOPR P 84: (2) What is the role of the Regional Entities in relationship to the ERO?**

Under the Act the ERO is able, subject to FERC's approval, to delegate the ERO's authority to a regional entity for two undertakings — (a) to propose reliability standards to the ERO, and (b) to enforce reliability standards. The regional entity is expected to be the first-line

enforcer for many of the standards. There is no requirement that a regional entity actually propose standards to the ERO, but the ability to propose standards is a statutory minimum requirement in order to be considered for regional entity status.

**NOPR P 84: (3) Beyond enforcement and the proposal of Reliability Standards to the ERO, what, if any, additional authority should the Regional Entities be given?**

Like the ERO, the regional entities should be able to perform functions in support of the responsibilities that are specifically legislated, i.e., proposing standards, compliance enforcement, and reliability assessment, and should be allowed to propose such functions in their annual budgets for approval. The ERO will include the regional entities' annual budgets in its annual budget request filed with the Commission or international regulatory authorities. However, any such supporting functions undertaken by the regional entities do not require additional delegations of authority beyond enforcement and proposal of standards. These supporting functions include readiness audits, organization certification, reliability assessment, and reliability coordination. Regional entities, as requested by their members, can also be expected to carry out a number of other functions beyond those necessary to implement the functions listed in the Act, but those functions would not be dependent upon authority delegated by the ERO or ERO funding.

**NOPR P 84: (4) Should the ERO be required to submit a pro forma form of delegation agreement concurrently with the ERO application that would delineate a uniform relationship between the ERO and all Regional Entities or should delegation agreements be tailored to the individual needs and circumstances of each region and the ERO and submitted for approval as they are executed by the parties?**

NERC believes the ERO applicant should submit a pro forma delegation agreement, developed with stakeholder input, as part of its application. This agreement should establish the general terms for delegation of authority and minimum requirements to qualify as a regional entity. If certified as the ERO, NERC plans to negotiate and execute a delegation agreement,

based upon the pro forma agreement, with each regional entity. Each individual agreement would identify specifically how each region meets the qualification criteria and would include the rules of procedure used within the region for delegated functions. Consistency among regions should be strongly encouraged. However, there may be valid reasons for some variations in individual agreements, each of which would be identified as such and submitted for approval by the Commission. If certified as the ERO, NERC intends to provide strong oversight of the regional entities in the delegated functions, which NERC believes to be the Commission's expectation.

**NOPR P 84: (5) To what extent should the ERO, when delegating responsibility to Regional Entities, require uniform processes in matters including, but not limited to, governance, collection of dues and fees, compliance monitoring, and enforcement action procedures?**

The pro forma regional delegation agreement should specify the necessary uniform processes within the regional entities. The requirements in the regional delegation agreement should address all factors necessary to ensure a strong and effective compliance enforcement program. The pro forma agreement and the specific regional agreements will be subject to Commission approval. In discussions with various regulatory authorities, NERC has learned that a number of jurisdictions would prefer that the details of how dues and fees are to be collected within their jurisdiction not be specified in the delegation agreements or the Commission's rule. This would require leaving some flexibility on this point.

**NOPR P 84: (6) What role, if any, should the ERO play in the approval or appeal of an enforcement action undertaken by a Regional Entity?**

The critical issues are that the regional entity has a properly structured compliance enforcement program, that it is approved as being in conformance with the statutory requirements, that it functions effectively as it was designed, and that the regional entity provides

information to the ERO so that the ERO can carry out its necessary oversight of the regional program. The role of the ERO in reviewing a specific enforcement action is a separate question. NERC recommends that to ensure consistency of application of sanctions among the various regional entities and jurisdictions, as well as to maximize the due process rights of those entities subject to sanctions, appeals from enforcement actions taken by regional entities should come to the ERO before going on to the appropriate regulatory authority for review.

**NOPR P 84: (7) What, if any, responsibility or involvement should the ERO have with regard to the funding of the Regional Entities?**

Consistent with the ERO's ongoing responsibility to ensure effective enforcement of reliability standards that provide for an adequate level of reliability for the North American bulk power system, the ERO must be assured that regional entities operating under agreements that delegate enforcement authority to them have the resources they need to meet the responsibilities they have been assigned. While there may be other alternatives, NERC believes that the best way to accomplish that assurance is for the regional entities to submit their budgets to the ERO for review and approval. The regional budgets would then be included in the ERO's annual funding submission to the Commission and other appropriate regulatory authorities.

**NOPR P 84: (8) Should the certification and delegation criteria for a Cross-Border Regional Entity specify that each country represented in the region should have the opportunity to have members from the country on the board of the Regional Entity in numbers that reflect the country's approximate percentage of net energy for load in that region, similar to that provided in the bilateral principles?**

NERC supports the bilateral principles, including the principle for cross-border regional entities to have board membership in approximate percentage to net energy for load in that region.

**NOPR P 84: (9) Should the Commission set the standard by which Regional Entity applications to the ERO will be reviewed or should the ERO be allowed to determine this standard? Given that section 215(e)(4) of the FPA requires that the ERO and the Commission shall rebuttably presume that a proposal for a Regional Entity organized on an Interconnection-wide basis promotes effective and efficient administration of bulk-power reliability, should a higher standard apply to Regional Entities that are not organized on an Interconnection-wide basis? What should the higher standard specify? Should a Regional Entity not organized on an Interconnection-wide basis have the burden to demonstrate that it has appropriate regional scope and configuration to promote effective and efficient administration of Bulk-Power System reliability?**

Section 215(e)(4) sets the criteria that a regional entity must meet to be eligible for a delegation of enforcement authority. All regional entities must meet the statutory criteria. Additional specific criteria will be defined in the pro forma regional delegation agreement. The pro forma agreement will be subject to Commission approval, as will the individual agreements with each region. Under the Act, regional entities organized on an Interconnection-wide basis are rebuttably presumed to promote effective and efficient administration of bulk power reliability. A regional entity not organized on an Interconnection-wide basis must demonstrate to the ERO that it promotes effective and efficient administration of bulk power reliability.

**NOPR P 84: (10) Paragraph (f) of section 38.7 requires a Regional Entity approved by the Commission to periodically submit to the Commission an application to be re-approved as a Regional Entity. We seek comments on what would constitute a reasonable length of time for such periodic re-approval to be effective. For example, is a five-year approval period appropriate? How far in advance should a Regional Entity be required to submit its application for re-approval before its current approval period expires? What role, if any, should the ERO have in the re-approval process? Would the ERO have to resubmit a delegation agreement?**

NERC agrees that a periodic review and approval of regional entities would be appropriate. Because the form of the Commission's initial approval will be to review and approve the delegation agreements between the ERO and the regional entities, any subsequent review and approval should take the same form. The same basic principles NERC recommended for recertification of the ERO should apply to re-approval of the delegation agreements. The

Commission's approval should not automatically expire, but should continue until the Commission completes its periodic review of the regional delegation agreements. The regional delegation agreements should be subject to review every six years, consistent with the ERO certification review period NERC recommends. As with recertification of the ERO, periodic re-approval of a delegation agreement should be coordinated with appropriate regulatory authorities in Canada, as contemplated by the Terms of Reference. Because the delegation agreement is between the regional entity and the ERO, the ERO (or the ERO and the regional entity, jointly) should submit the delegation agreement for re-approval. Appendix A contains a suggested revision to proposed section 38.7 to implement this recommendation.

**NOPR P 84: (11) Section 215(e)(4) of the FPA and proposed regulation section 38.7(c)(3) require that the ERO, when filing a delegation agreement, include a statement demonstrating that the agreement promotes effective and efficient administration of Bulk-Power System reliability. What standards, guidelines, measures or criteria should the Commission apply in determining whether a delegation agreement promotes effective and efficient administration of Bulk-Power System reliability? If the primary function of a Regional Entity is enforcement of Reliability Standards, in what ways will Regional Entities bring effective and efficient administration in the enforcement function?**

This is a statutory test. NERC suggests that these terms be defined as follows:

“Effective” means the ability to reach all owners, operators, and users of the bulk power system in the region and establish sanctions that will deter the prohibited conduct by these entities.

“Efficient” means the ability to address regional needs more appropriately, through better-informed standards development and better implementation systems that are more attuned to the particular grid operation of the region.

**NOPR P 91: The Commission seeks examples of situations or areas of concern in which commenters believe that conflicts between reliability standards and Transmission Organization tariffs exist or may arise.**

The open process for standards development incorporates inputs from regional transmission organizations, and efforts are made to avoid conflicts with tariffs. No instances of conflicts between reliability standards and transmission organization tariffs have been brought to

NERC's attention, other than the seven specific variances that NERC has included within its current reliability standards. (See the response to the questions in NOPR P 80, *supra*.)

**NOPR P 94: In addition to comment on the proposed regulation discussed above, the Commission seeks comment on the scope of the term "region" as used in section 38.10. In particular, should the region represented by a Regional Advisory Body correspond to that of an existing or proposed Regional Entity?**

In order to avoid overlapping or conflicting advice, the ERO will be best served by a regional advisory body corresponding to the area covered by a regional entity.

**NOPR P 103: In addition to comments on the proposed ERO funding regulations, the Commission asks for comments on the following questions: (1) Should the proposed funding requirements be extended to the Regional Entities?**

The funding requirements of the regional entities should mirror those of the ERO to the extent practicable and should be specifically defined within the regional delegation agreement. Funding for regional entities should be included within Section 38.13 of the Commission's regulations, as described in Part II.

**NOPR P 103: (2) The Commission notes the bilateral principles include several funding principles: (a) a principle specifying that net energy for load should be the primary basis upon which the costs of the ERO are assigned and that costs for one region or entity should be directly assigned to that region or entity; (b) a principle specifying that funding mechanisms, budget direction and budget levels should reflect consultations with appropriate stakeholders and authorities in each country; and (c) a principle specifying that the appropriate authorities in each country should be responsible for approving and ensuring cost recovery by the ERO and Regional Entities within their respective jurisdictions in a timely manner. Should the proposed rule address these types of funding-related details or should the ERO and Cross-Border Regional Entities have the discretion to address these matters at a later time?**

NERC supports the bilateral principles on these issues and will reflect those principles in its application. These matters will be developed further by the ERO and the regional entities as they develop their budgets and procedures, in consultation with appropriate regulatory authorities. NERC understands that regulatory authorities have different views on how costs should be recovered within their jurisdictions. The Commission's rule should not include a

provision specifying what other jurisdictions should do. The governments of the United States and Canada have already agreed on that principle.

#### **IV. THE NOPR RAISES CERTAIN LEGAL ISSUES THAT SHOULD BE CONSIDERED IN THE FINAL RULE.**

This Part of NERC's comments addresses, in more detail, a number of legal issues raised in the NOPR. The Commission should consider these legal issues in arriving at the Final Rule. Resolution of these issues in an appropriate manner will enhance the ERO's credibility and effectiveness.

##### **A. The Commission need not hold trial-type hearings regarding proposed reliability standards.**

The NOPR proposes to afford interested parties notice and an opportunity for hearing prior to considering a proposed reliability standard or a modification to an existing reliability standard. NOPR at P 47. While the Commission must provide interested parties with the ability to be heard, the Commission need not hold trial-type hearings regarding reliability standards.

The Final Rule should modify this proposal and provide interested parties with notice and an opportunity to *comment* upon proposed reliability standards or proposed modifications to reliability standards. Interested parties may submit comments for the Commission's consideration, or in more complicated cases, the Commission could use "paper hearing" procedures.<sup>13</sup> The institution of trial-type hearing procedures will inevitably delay the development of enforceable reliability standards in this country. In addition, as reliability standards are technical in nature, the use of comments or the paper hearing process will permit

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<sup>13</sup> The courts have repeatedly approved the use of paper hearing procedures by the Commission. See, e.g., *Moreau v. FERC*, 982 F.2d 556, 568 (D.C. Cir. 1993); *Cities and Carlisle and Neola, Iowa v. FERC*, 741 F.2d 429, 431 (D.C. Cir. 1984).

parties an adequate opportunity to explain their support of, or concerns with, a proposed reliability standard. Live cross-examination at a trial-type hearing is simply unnecessary.

**B. All remands of proposed reliability standards should be to the ERO.**

The Commission suggests that, if a proposed reliability standard is found not to be just and reasonable, the Commission “may remand it to the ERO or the relevant Regional Entity.” NOPR at P 52. As noted above, the Commission’s proposal to remand reliability standards after concluding that they have not been shown to be just and reasonable is appropriate. The Final Rule, however, should provide that all such remands should be to the ERO.<sup>14</sup>

The ERO is the only entity that will be submitting proposed reliability standards to the Commission. While regional entities may propose such standards to the ERO, the ERO — not the regional entities — will submit the standards to the Commission for approval. Any necessary remands, therefore, should be to the ERO, as the filer of the proposed reliability standard. In addition, Section 215(d)(4) of the FPA states that the “Commission shall remand to the Electric Reliability Organization for further consideration a proposed reliability standard or modification to a reliability standard that the Commission disapproves in whole or in part.” The Act does not provide for remands to regional entities.

**C. The Final Rule should further define the concept of “potential violations” and should not impose monetary penalties unless a violation has actually occurred.**

The Commission proposes to require the ERO and regional entities to report “information regarding all potential violations of Reliability Standards.” NOPR at P 67. The NOPR does not, however, define the concept of “potential violations.” As noted in Part III, above, public

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<sup>14</sup> How the ERO would then deal with that remand would depend on where the proposed standard originated, whether from the ERO’s own program or from an Interconnection-wide regional entity.

reporting of potential violations may have a chilling effect on the ability of the ERO and the regional entities to ensure compliance with reliability standards, because entities under investigation may be harmed by disclosure and may be unwilling to cooperate with the ERO and regional entities. In the Final Rule, therefore, the Commission should delete any requirement that the ERO report potential violations from Section 38.5(g).

If the Final Rule does require the reporting of potential violations, however, then the Final Rule must also define “potential violations” in order to provide the ERO and regional entities with notice of the types of activities that must be reported to the Commission. The Final Rule should define “potential violation” as a situation in which the ERO or regional entity has performed a preliminary investigation and is prepared to formally allege that an entity has violated a reliability standard. This definition will ensure that only imminent potential violations are reported to the Commission.<sup>15</sup>

In addition, the ERO and regional entities should not impose monetary penalties on an entity that is engaged in a potential violation of a reliability standard. If the alleged violation has not been proven to have occurred, standards of fundamental fairness militate against the imposition of monetary penalties. In appropriate circumstances, however, the ERO or the regional entity should be authorized to issue orders or notices requiring the alleged potential violator to take action to ensure that an actual violation is not committed. These types of compliance orders will enhance the reliability of the bulk power system.

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<sup>15</sup> If the Final Rule continues to require reporting of potential violations, the Commission should add a new Section 38.5(g)(5) stating as follows: “For purposes of this Section 38.5(g), a potential violation occurs when the ERO or Regional Entity has performed a preliminary investigation and is prepared to formally charge an entity with a violation of a Reliability Standard.”

**D. Section 316A of the FPA limits the level of monetary penalties that may be imposed by the ERO and regional entities.**

As noted in Part III, NERC concurs with the Commission's interpretation of Section 316A of the FPA as establishing limits on the level of monetary penalties that may be imposed by the ERO and the regional entities for violations of reliability standards. NOPR at P 71. That section places a \$1 million per day cap on the amount of a civil penalty that may be levied against a person for violating the FPA. This cap is applicable to all FPA violations, whether the monetary penalty is levied by the Commission in the first instance or initially by the ERO or a regional entity, with possible appeal to the Commission.

**E. Regional entities may submit regional variations to the ERO, which may become reliability standards if the ERO submits them to the Commission for approval.**

The NOPR proposes that regional entities may propose reliability standards to the ERO "that, if ultimately approved by the Commission, would become regional variances in a specific region." NOPR at P 80. The NOPR goes on to state that "[a]ny such regional variances would be ERO variances, not Regional Entity Reliability Standards, since it would be the ERO, not the Regional Entity, that submits the proposed Reliability Standard to the Commission for review." *Id.* This interpretation is consistent with the Act and should be maintained in the Final Rule. Section 215(d)(1) of the FPA provides: "The Electric Reliability Organization shall file each reliability standard or modification to a reliability standard that it proposes to be made effective under this section with the Commission." In addition, Section 215(d)(3) requires the ERO to apply a rebuttable presumption to a reliability standard or modification proposed by a regional entity organized on an Interconnection-wide basis. As noted above, Section 215(d)(4) states that the Commission shall remand proposed standards that it does not approve to the ERO. Taken together, these statutory provisions demonstrate that the ERO is charged with filing reliability

standards or modifications thereto with the Commission. The regional entities may propose standards or modifications to the ERO, which may, in turn, submit them to the Commission for approval. The Final Rule should reflect this linear structure.

**F. Proposed section 38.12 should be modified to reflect the Act's provisions regarding the State of New York.**

Section 215(i)(3) of the FPA provides that the "State of New York may establish rules that result in greater reliability within the State, as long as such action does not result in lesser reliability outside the State than that provided by the reliability standards." Section 38.12 of the proposed rule, which addresses review of state action, does not contain this statutory language.

The Final Rule should modify Section 38.12 to so reflect by adding the following subpart (d):

The State of New York may establish rules that result in greater reliability within the State, as long as such action does not result in lesser reliability outside the State than that provided by the Reliability Standards.

**G. Section 38.5(d)(4) should be clarified.**

In order to make its meaning clear, the first sentence of Section 38.5(d)(4) of the proposed rules should be modified to read:

An applicant *for review of a penalty* shall file an original and fourteen (14) copies of an application for review and shall comply with the requirements set forth in the Commission's Rules of Practice and Procedure, unless otherwise directed by the Commission.

**H. The Final Rule should specify the criteria for recertification of the ERO and reapproval of delegation agreements.**

Section 38.3(c) of the proposed rules requires the ERO to "periodically submit an application to be recertified as the ERO, in accordance with any requirements the Commission issues in this regard." Section 38.7(f) of the proposed rules contains a similar requirement for reapproval of delegation agreement. The Final Rule should specify the criteria for any such

applicable recertification or reapproval. Further, the criteria for recertification of the ERO and reapproval of delegation agreements should be no different than those for initial certification or approval. The requirements for certification and for filing a request for certification are found in proposed sections 38.3(a) and (b). The requirements applicable to the initial filing and approval of delegation agreements are contained in proposed sections 38.7(c).

In the Final Rule, Section 38.3(c) should read as follows:

The approved ERO is required to submit an application to be recertified as the ERO every six (6) years. In order to be recertified as the ERO, the ERO must demonstrate continued compliance with the requirements set forth in subpart (b) of this Section 38.3. The ERO remains certified until the Commission issues a final order certifying the ERO. If the previously approved ERO is not recertified as the ERO, the previously approved ERO shall continue to serve as the ERO until the Commission is able to certify a replacement ERO.

Section 38.7(f) should be revised to read:

The ERO shall be required to submit each delegation agreement it has with a Regional Entity for re-approval every six (6) years. In order for the delegation agreement to be re-approved, the Regional Entity must demonstrate continued compliance with the provisions of Section 38.7(c).

- I. The Final Rule should permit the simultaneous filings of an application to serve as the ERO and reliability standards and should permit the Commission to consider jointly filed reliability standards on an individual basis.**

The NOPR states that a one-step process, pursuant to which an applicant submits its application to serve as the ERO along with proposed reliability standards, may “allow for quicker implementation of Reliability Standards.” NOPR at P 104. The Commission also proposes to permit the ERO to submit several proposed reliability standards simultaneously, although the Commission may consider each proposed standard individually. *Id.*

The NOPR is consistent with the Act in these respects. An applicant to serve as the ERO should not be required to submit reliability standards along with its application, but it should not be precluded from doing so. The Commission correctly notes that this one-step process may speed the development of enforceable reliability standards in the United States. In addition, the submission of multiple proposed reliability standards at the same time would enhance efficiency. The Commission should not, however, be required to consider such multiple filings as a package, but may, if appropriate, approve some of the standards, while remanding others to the ERO. Of course, when considering reliability standards — whether filed individually or with multiple standards — the Commission must give due weight to the ERO's expertise, as required in the Act.

### **CONCLUSION**

The Commission should modify the proposed rules as described above when issuing a Final Rule.

Respectfully submitted,

NORTH AMERICAN ELECTRIC  
RELIABILITY COUNCIL

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# **APPENDIX**

**Part 38 -- RULES CONCERNING  
CERTIFICATION OF THE ELECTRIC RELIABILITY ORGANIZATION;  
AND PROCEDURES FOR THE  
ESTABLISHMENT, APPROVAL, AND  
ENFORCEMENT OF ELECTRIC RELIABILITY STANDARDS**

Sec.

- 38.1 – Definitions.
- 38.2 – Jurisdiction and applicability.
- 38.3 – Electric Reliability Organization certification.
- 38.4 – Approval of Reliability Standards.
- 38.5 – Enforcement by the Electric Reliability Organization or a Regional Entity.
- 38.6 – Enforcement against the Electric Reliability Organization.
- 38.7 – Delegation of certain Electric Reliability Organization authority to Regional Entities.
- 38.8 – Changes in Electric Reliability Organization Rules and Regional Entity Rules.
- 38.9 – Process for resolution of conflicts with a Reliability Standard.
- 38.10 – Procedures for establishment and recognition of Regional Advisory Bodies.
- 38.11 – Reliability reports.
- 38.12 – Review of state action.
- 38.13 – Funding of the Electric Reliability Organization.

Authority: Section 215 of the Federal Power Act, 16 U.S.C. § \_\_\_\_

§ 38.1 Definitions.

As used in this part:

Bulk-Power System means facilities and control systems necessary for operating an interconnected electric energy transmission network (or any portion thereof), and electric energy from generating facilities needed to maintain transmission system reliability. The term does not include facilities used in the local distribution of electric energy.

Cross-Border Regional Entity means a Regional Entity for which the size and scope includes a portion of Canada or Mexico.

Cybersecurity Incident means a malicious act or suspicious event that disrupts, or was an attempt to disrupt, the operation of those programmable electronic devices and communications networks including hardware, software and data that are essential to the Reliable Operation of the Bulk-Power System.

Electric Reliability Organization or “ERO” means the organization certified by the Commission under section 38.3 the purpose of which is to establish and enforce Reliability Standards for the Bulk-Power System, subject to Commission review.

End User means a customer that receives service at retail.

ERO Rules means, for purposes of this section, the bylaws, rules of procedure and other organizational rules and protocols of the Electric Reliability Organization.

Interconnection means a geographic area in which the operation of Bulk-Power System components is synchronized such that the failure of one or more of such components may adversely affect the ability of the operators of other components within the system to maintain Reliable Operation of the facilities within their control.

Net Energy for Load means balancing authority area generation (less station use), plus energy received from other balancing authority areas, less energy delivered to balancing authority areas through interchange. It includes balancing authority area losses, but excludes energy required for storage at energy storage facilities.

Physical Security Standards means Reliability Standards adopted to safeguard personnel and prevent unauthorized access to critical equipment, systems, material, and information at critical facilities.

Regional Advisory Body means an entity established upon petition to the Commission pursuant to section 215(j) of the FPA that is organized to advise the Electric Reliability Organization, a Regional Entity, or the Commission regarding certain matters in accordance with section 38.10.

Regional Entity means an entity having enforcement authority pursuant to section 38.7.

Regional Entity Rules means, for purposes of this Part, the bylaws, rules of procedure and other organizational rules and protocols of a Regional Entity.

Reliability Standard means a requirement approved by the Commission under this section, to provide for Reliable Operation of the Bulk-Power System. The term includes requirements for the operation of existing Bulk-Power System facilities, including cybersecurity protection, and the design of planned additions or modifications to such facilities to the extent necessary to provide for Reliable Operation of the Bulk-Power System, but the term does not include any requirement to enlarge such facilities or to construct new transmission capacity or generation capacity.

Reliable Operation means operating the elements of the Bulk-Power System within equipment and electric system thermal, voltage, and stability limits so that instability, uncontrolled separation, or cascading failures of such system will not occur as a result of a sudden disturbance, including a Cybersecurity Incident, or unanticipated failure of system elements.

Transmission Organization means a regional transmission organization, independent system operator, independent transmission provider, or other transmission

organization finally approved by the Commission for the operation of transmission facilities.

User of the Bulk-Power System means any entity that sells, purchases, or transmits electric power directly over the Bulk-Power system, or that maintains facilities or controls systems that are part of the Bulk-Power system, or that is a system operator. The term excludes customers that receive service at retail that do not otherwise sell, purchase, or transmit power over the Bulk-Power System or own, operate or maintain, control or operate facilities or systems that are part of the Bulk-Power System.

§ 38.2 Jurisdiction and applicability.

(a) Within the United States (other than Alaska and Hawaii), the Electric Reliability Organization, any Regional Entities, and all users, owners and operators of the Bulk-Power System, including but not limited to entities described in section 201(f) of the Federal Power Act, shall be subject to the jurisdiction of the Commission for the purposes of approving Reliability Standards established under this section and enforcing compliance with this section.

(b) Within the United States (other than Alaska and Hawaii), all owners, operators, and Users of the Bulk-Power System shall comply with the regulations of the Commission adopted under this Part, Reliability Standards made effective under this Part, and the ERO Rules and Regional Entity Rules made effective under this Part, and shall supply all data and information reasonably requested by the Electric Reliability Organization or a Regional Entity that is necessary or appropriate to carrying out its responsibilities under Section 215 of the Federal Power Act.

(c) To facilitate compliance with, monitoring of, and enforcement of Reliability Standards, each owner, operator, and User of the Bulk-Power System shall register with the Electric Reliability Organization and the Regional Entity for each region within which it owns, operates, or uses bulk power facilities, in such manner as prescribed in the rules of the Electric Reliability Organization and each applicable Regional Entity.

§ 38.3 Electric Reliability Organization certification.

(a) Any person may submit an application to the Commission for certification as an Electric Reliability Organization no later than sixty (60) days following Commission issuance of the final rule. Such application shall include a form of notice and an original and fourteen (14) copies of the application.

(b) The Commission may certify one such applicant as an Electric Reliability Organization, if the Commission determines such applicant:

(1) Has the ability to develop and enforce, subject to section 38.5, Reliability Standards that provide for an adequate level of reliability of the Bulk-Power System, and

(2) Has established rules that:

(i) Assure its independence of users, owners and operators of the Bulk-Power System while assuring fair stakeholder representation in the selection of its directors and balanced decisionmaking in any Electric Reliability Organization committee or subordinate organizational structure;

(ii) Allocate equitably reasonable dues, fees and charges among end users for all activities under this section;

(iii) Provide fair and impartial procedures for enforcement of Reliability Standards through the imposition of penalties in accordance with section 38.5, including limitations on activities, functions, operations, or other appropriate sanctions or penalties;

(iv) Provide reasonable notice and opportunity for public comment, due process, openness, and balance of interests in developing Reliability Standards, and otherwise exercising its duties; and

(v) Provide appropriate steps, after certification by the Commission as the Electric Reliability Organization, to gain recognition in Canada and Mexico.

(c) The approved ERO is required to ~~periodically~~ submit an application to be recertified as the ERO, ~~in accordance with any requirements the Commission issues in this regard every six (6) years. In order to be recertified as the ERO, the ERO must demonstrate continued compliance with the requirements set forth in subpart (b) of this Section 38.3. The ERO remains certified until the Commission issues a final order decertifying the ERO. If the previously approved ERO is not recertified as the ERO, the previously approved ERO shall continue to serve as the ERO until the Commission is able to certify a replacement ERO.~~

#### § 38.4 Approval of Reliability Standards.

(a) The Electric Reliability Organization must consider and develop Reliability Standards or modifications to Reliability Standards to be applicable to the entire Bulk-Power System or a particular region or Interconnection. The Electric Reliability Organization shall file each Reliability Standard or modification to a Reliability Standard that it proposes to be made effective under this section with the Commission. The filing shall include an original and fourteen (14) copies, a form of notice, a concise statement of the basis and purpose of the standard and a summary of the standard development proceedings conducted by the Electric Reliability Organization.

(b) The Commission may approve by rule or order a proposed Reliability Standard or a modification to a Reliability Standard if it determines, after notice and opportunity for public hearing, that the standard is just, reasonable, not unduly discriminatory or preferential, and in the public interest.

(1) The Commission shall give due weight to the technical expertise of the Electric Reliability Organization with respect to the content of a proposed Reliability Standard or modification to a Reliability Standard,

(2) The Commission shall give due weight to the technical expertise of a Regional Entity organized on an Interconnection-wide basis with respect to a Reliability Standard to be applicable within that Interconnection, and

(3) The Commission shall not defer to the Electric Reliability Organization or a Regional Entity with respect to the effect of a Reliability Standard or modification to a Reliability Standard on competition.

(c) An approved Reliability Standard or a modification to a Reliability Standard shall take effect as approved by the Commission.

(d) The Electric Reliability Organization shall rebuttably presume that a proposal for a Reliability Standard or a modification to a Reliability Standard to be applicable on an Interconnection-wide basis is just, reasonable, not unduly discriminatory or preferential, and in the public interest, if such proposal is from a Regional Entity organized on an Interconnection-wide basis.

(e) The Commission shall remand to the Electric Reliability Organization for further consideration a proposed Reliability Standard or modification to a Reliability Standard that the Commission disapproves in whole or part.

(f) The Commission may, upon its own motion or a complaint, order the Electric Reliability Organization to submit a proposed Reliability Standard or modification to a Reliability Standard that addresses a specific matter if the Commission considers such a new or modified Reliability Standard appropriate to carry out this section.

(g) The Commission may, upon its own motion or a complaint, review a previously-approved Reliability Standard. If, after notice and opportunity for hearing, the Commission determines that the Reliability Standard, or any provision thereof, is unjust or unreasonable, unduly discriminatory or preferential, or not in the public interest, the Commission may remand the Reliability Standard to the Electric Reliability Organization.

(h) The Commission, when remanding a Reliability Standard, may state a deadline by which the Electric Reliability Organization must submit a proposed revised Reliability Standard.

§ 38.5 Enforcement of Reliability Standards.

(a) The Electric Reliability Organization, or a Regional Entity, may impose, subject to paragraph (d) of this section, a penalty on a user, owner or operator of the Bulk-Power System for a violation of a Reliability Standard approved by the Commission under section 38.4 if the Electric Reliability Organization or the Regional Entity, after public notice and opportunity for hearing:

(1) Finds that the user, owner or operator has violated a Reliability Standard approved by the Commission under section 38.4; and

(2) Files notice and the record of the Electric Reliability Organization's or Regional Entity's proceeding with the Commission. Simultaneously with the filing of a notice with the Commission, the Electric Reliability Organization or Regional Entity shall serve a copy of the notice on the entity that is the subject of the enforcement action.

(b) A Regional Entity shall file notice with the Electric Reliability Organization of any enforcement action it takes.

(c) Any notice of an enforcement action, whether by the Electric Reliability Organization or a Regional Entity, shall consist of:

(1) The name of the entity against whom the enforcement action was taken;

(2) A statement describing the enforcement action taken;

(3) A statement setting forth findings of fact with respect to the act or practice that resulted in the enforcement action;

(4) A statement describing any sanction imposed;

(5) The record of the proceeding;

(6) A form of notice suitable for publication; and

(7) Other matters the Electric Reliability Organization or the Regional Entity, as appropriate, may find relevant.

(d) A penalty imposed under paragraph (a) of this section may take effect not earlier than the thirty-first (31st) day after the Electric Reliability Organization or Regional Entity files with the Commission notice of the penalty and the record of the proceedings.

(1) Such penalty shall be subject to review by the Commission, on its own motion or upon application by the user, owner or operator of the Bulk-Power System that is the subject of the penalty filed within thirty (30) days after the date such notice is filed with Commission. In the absence of the filing of an application for review or motion or other action by the Commission, the enforcement action shall be affirmed by operation of law upon the expiration of the 30-day period for filing of an application for review.

(2) Application to the Commission for review, or the initiation of review by the Commission on its own motion, shall not operate as a stay of such penalty unless the Commission otherwise orders upon its own motion or upon application by the user, owner or operator that is the subject of such penalty.

(3) In any proceeding to review a penalty imposed under paragraph (a) of this section, the Commission, after public notice and opportunity for hearing (which hearing may consist solely of the record before the Electric Reliability Organization or Regional Entity and the opportunity for the presentation of supporting reasons to affirm, modify, or set aside the penalty), shall by order affirm, set aside or modify the penalty and, if appropriate, remand to the Electric Reliability Organization or Regional Entity for further proceedings.

(4) An applicant [for review of a penalty](#) shall file an original and fourteen (14) copies of an application for review and shall comply with the requirements set forth in the Commission's Rules of Practice and Procedure, unless otherwise directed by the Commission. An application shall contain a complete and detailed explanation of the reasons why the applicant believes that the Electric Reliability Organization or Regional Entity erred when assessing the penalty, the amount of the penalty or the form of the penalty, and such application must provide any additional support for this contention that is not included in the record submitted by the Electric Reliability Organization or Regional Entity pursuant to this section.

(5) Unless otherwise ordered by the Commission, answers, interventions, and comments to an application for review of a penalty imposed under paragraph (a) of this section must be filed within twenty (20) days after the application is filed.

(6) One of the following procedures may be used to resolve application for review of a penalty imposed under paragraph (a) of this section:

(i) The Commission may issue an order on the merits to affirm, set aside, reinstate or modify the penalty and, if appropriate, remand to the Electric Reliability Organization or Regional Entity based upon the pleadings; or

(ii) The Commission may establish a hearing before an administrative law judge or initiate such further procedures as may be appropriate.

(7) Expedited review. Unless determined otherwise by the Commission on a case by case basis, the Commission shall take action on an application for review of a penalty within sixty (60) days of the date the application is filed. Expedited procedures shall be established for any hearing before an administrative law judge on a case by case basis.

(8) Unless the Commission determines otherwise, an enforcement action pursuant to section 38.5 ~~that involves a Cybersecurity Incident~~ involving confidential or sensitive information will be non-public. The user, owner or operator of the Bulk-Power System that is the subject of the enforcement action will be given timely notice and an opportunity for hearing. The public will not be notified and the public will not be allowed to participate in an enforcement action before the Electric Reliability Organization, a Regional Entity or the Commission.

(e) On its own motion or upon complaint, the Commission may order compliance with a Reliability Standard and may impose a penalty against a user, owner or operator of the Bulk-Power System, if the Commission finds, after public notice and opportunity for hearing, that the user, owner or operator of the Bulk-Power System has engaged or is about to engage in any acts or practices that constitute or will constitute a violation of a Reliability Standard.

(f) Any penalty imposed for the violation of a Reliability Standard shall bear a reasonable relation to the seriousness of the violation and shall take into consideration efforts of such user, owner or operator of the Bulk-Power System to remedy the violation in a timely manner. The imposition of penalties is not limited to monetary penalties and may include, but is not limited to, limitations on activities, functions, operations, or other appropriate sanctions, including the establishment of a reliability watch list composed of major violators. Monetary penalties shall be paid in a timely manner.

(g) Reporting of Violations ~~and Potential Violations~~: The Electric Reliability Organization and all Regional Entities shall have in place procedures to immediately notify the Commission of all violations ~~and potential violations~~ of Reliability Standards when the Electric Reliability Organization or Regional Entity first notifies the user, owner or operator of the violation ~~or potential violation~~.<sup>1</sup>

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<sup>1</sup> If the Final Rule continues to require reporting of potential violations, the Commission should add a new Section 38.5(g)(5) stating as follows: “For purposes of this Section 38.5(g), a potential violation occurs when the ERO or Regional Entity has performed a preliminary investigation and is prepared to formally charge an entity with a violation of a Reliability Standard.”

(1) Any person that submits an application to the Commission for certification as an Electric Reliability Organization shall include in such application a proposal for the notification and reporting to the Commission of all violations ~~and potential violations~~ of Reliability Standards.

(2) Any agreement for the delegation of authority to a Regional Entity shall include a proposal for the notification and reporting to the Commission of all violations ~~and potential violations~~ of Reliability Standards.

(3) All reports of violations and ~~potential violations~~ shall include the entity's name, when the violation ~~or potential~~ occurred, what standard was violated ~~or potentially violated~~ and the name of a person knowledgeable about the violation or ~~potential violation~~ to serve as a point of contact to provide the Commission with further details on the matter, as they develop, on an ongoing basis.

(4) All reports of ~~violations and potential~~ violations shall be filed electronically with the Commission.

#### § 38.6 Enforcement of Commission Rules and Orders.

(a) The Commission may take such action as is necessary and appropriate against the Electric Reliability Organization or a Regional Entity to ensure compliance with a Reliability Standard or any Commission order affecting the Electric Reliability Organization or a Regional Entity, including, but not limited to:

(1) Upon notice and opportunity for hearing, suspension or rescission of the Commission's grant of certification to the Electric Reliability Organization, if the Electric Reliability Organization no longer meets the statutory standards for certification.

(2) Upon notice and opportunity for hearing, suspension or rescission of the Commission's approval of an agreement to delegate certain Electric Reliability Organization authority to a Regional Entity.

(3) Imposition of civil penalties under the Federal Power Act.

(b) The Commission will periodically audit and review the Electric Reliability Organization's and Regional Entities' compliance with the statutory and regulatory criteria for certification and delegation of functions.

§ 38.7 Delegation of certain Electric Reliability Organization authority to Regional Entities.

(a) The Electric Reliability Organization may enter into an agreement to delegate authority to a Regional Entity for the purpose of proposing Reliability Standards to the Electric Reliability Organization and enforcing Reliability Standards under section 38.5(a).

(b) A delegation agreement shall not be effective until it is approved by the Commission.

(c) The Electric Reliability Organization shall file an original and fourteen (14) copies of a delegation agreement. In addition, such filing shall include a detailed statement demonstrating that:

(1) The Regional Entity is governed by an independent board, a balanced stakeholder board, or a combination independent and balanced stakeholder board,

(2) The Regional Entity otherwise satisfies the provisions of section 38.3, and

(3) The agreement promotes effective and efficient administration of Bulk-Power System reliability.

(d) The Commission may modify such delegation; however, the Electric Reliability Organization and Commission shall rebuttably presume that a proposal for delegation to a Regional Entity organized on an Interconnection-wide basis promotes effective and efficient administration of Bulk-Power System reliability and should be approved.

(e) If an entity seeking to enter into a delegation agreement is unable to reach an agreement with the Electric Reliability Organization within 180 days after proposing a delegation agreement to the Electric Reliability Organization, and it can demonstrate that continued negotiations with the Electric Reliability Organization would not likely result in a delegation agreement within a reasonable period of time, such entity may request that the Commission assign the Electric Reliability Organization's authority to enforce Reliability Standards within a region to such entity.

(f) The ERO shall be required to submit each delegation agreement it has with a Regional Entity for re-approval ~~An approved Regional Entity shall be required to periodically submit an application to be re-approved as a Regional Entity, in accordance with any requirements the Commission issues in this regard.~~ every six (6) years. In order for the delegation agreement to be re-approved, the Regional Entity must demonstrate continued compliance with the provisions of Section 38.7(c).

§ 38.8 Changes in Electric Reliability Organization Rules and Regional Entity Rules.

(a) The Electric Reliability Organization shall file with the Commission for approval any proposed Electric Reliability Organization Rule or rule change. A Regional Entity shall submit a Regional Entity Rule or rule change with the Electric Reliability Organization and, upon approval by the Electric Reliability Organization, the Electric Reliability Organization shall file with the Commission for approval of any proposed Regional Entity Rule or rule change. Such filing by the Electric Reliability Organization shall be accompanied by an explanation of the basis and purpose for the rule or rule change, together with a description of the proceedings conducted by the Electric Reliability Organization or Regional Entity to develop the proposal.

(b) The Commission upon its own motion or complaint may propose changes to the Electric Reliability Organization rules or Regional Entity rules.

(c) A proposed Electric Reliability Organization rule or rule change or Regional Entity rule or rule change shall take effect upon a finding by Commission, after notice and opportunity for public comment, that the change is just, reasonable, not unduly discriminatory or preferential, is in the public interest, and satisfies the requirements of section 38.3.

§ 38.9 Process for resolution of conflicts with a Reliability Standard.

(a) If a Transmission Organization determines that a Reliability Standard may conflict with a function, rule, order, tariff, rate schedule, or agreement accepted, approved, or ordered by the Commission with respect to such Transmission Organization, the Transmission Organization shall expeditiously notify the Commission, the Electric Reliability Organization and the relevant Regional Entity of the conflict.

(b) Unless the Commission orders otherwise, after notice and opportunity for hearing, within sixty (60) days of the date that a notice was filed under paragraph (a) of this section, the Commission shall issue an order determining whether a conflict exists and, if so, resolve the conflict by directing (i) the Transmission Organization to file a modification of the conflicting function, rule, order, tariff, rate schedule, or agreement pursuant to section 206 of the Federal Power Act or (ii) the Electric Reliability Organization to propose a modification to the conflicting Reliability Standard pursuant to section 38.4 of the Commission's regulations.

(c) The Transmission Organization shall continue to follow the function, rule, order, tariff, rate schedule, or agreement accepted, approved, or ordered by the Commission until the Commission finds that a conflict exists, the Commission orders a change to such provision pursuant to section 206 of the Federal Power Act, and the ordered change becomes effective.

§ 38.10 Procedures for establishment and recognition of Regional Advisory Bodies.

(a) The Commission shall consider a petition to establish a Regional Advisory Body that is submitted by at least two-thirds of the states within a region that have more than one-half of their electric load served within the region.

(b) A petition to establish a Regional Advisory Body shall include all organizational documents and a statement that the Regional Advisory Body is composed of one member from each participating state in the region, appointed by the governor of each state, and may include representatives of agencies, states and provinces outside the United States.

(c) A Regional Advisory Body established by the Commission may provide advice to the Commission, Electric Reliability Organization or a Regional Entity with respect to:

(1) The governance of an existing or proposed Regional Entity within the same region;

(2) Whether a Reliability Standard proposed to apply within the region is just, reasonable, not unduly discriminatory or preferential, and in the public interest;

(3) Whether fees for all activities under this section proposed to be assessed within the region are just, reasonable, not unduly discriminatory or preferential, and in the public interest; and

(4) Any other responsibilities requested by the Commission.

(d) The Commission may give deference to the advice of a Regional Advisory Body established by the Commission if it is organized on an Interconnection-wide basis.

§ 38.11 Reliability reports.

(a) The Electric Reliability Organization shall conduct periodic assessments of the reliability and adequacy of the Bulk-Power System in North America and report its findings

to the Commission, the Secretary of Energy, Regional Entities, and Regional Advisory Bodies annually or more frequently if so ordered by the Commission.

(b) The Electric Reliability Organization and Regional Entities shall report on their enforcement actions and associated penalties to the Commission, the Secretary of Energy, relevant Regional Entities, and relevant Regional Advisory Bodies annually or quarterly, in a manner to be prescribed by the Commission.

§ 38.12 Review of state action.

(a) Nothing in this regulation shall be construed to preempt any authority of any state to take action to ensure the safety, adequacy, and reliability of electric service within that state, as long as such action is not inconsistent with any reliability standard.

(b) Where a state takes action to ensure safety, adequacy, and reliability of electric service, the Electric Reliability Organization, Regional Entity or other affected party may apply to the Commission for a determination of consistency with a Commission-approved Reliability Standard.

(1) The application shall:

(i) Identify the state action complained of;

(ii) Identify the Reliability Standard(s) with which the state action is claimed to be inconsistent;

(iii) State the basis for the claim that the state action is inconsistent with a Reliability Standard; and

(iv) Include a form of notice.

(2) Within ninety (90) days of the application of the Electric Reliability Organization or other affected party, and after notice and opportunity for public comment, the Commission shall issue a final order determining whether the state action is inconsistent with a Reliability Standard, taking into consideration any recommendation of the Electric Reliability Organization.

(c) The Commission, after consultation with the Electric Reliability Organization and the state taking action, may stay the effectiveness of the state action, pending the Commission's issuance of a final order.

(d) The State of New York may establish rules that result in greater reliability within the State, as long as such action does not result in lesser reliability outside the State than that provided by the Reliability Standards.

§ 38.13 Funding of the Electric Reliability Organization.

(a) The Electric Reliability Organization shall file with the Commission its proposed annual budget for activities within the United States and supporting materials in sufficient detail to justify the requested funding requirement 130 days in advance of the beginning of each fiscal year.

(b) The annual budget submission shall include amounts for those activities of Regional Entities that are delegated or assigned pursuant to Section 38.7 of this Part.

(c) The Commission, after public notice and opportunity for comment, shall issue an order either accepting, rejecting or remanding or modifying the proposed Electric Reliability Organization budget and business plan no later than sixty (60) days in advance of the beginning of the Electric Reliability Organization's fiscal year.

(~~e~~d) Any person who submits an application for certification as the Electric Reliability Organization pursuant to the rules set forth in this section shall include in such application a plan, formula and/or methodology for the allocation and assessment of Electric Reliability Organization dues, fees and charges. The certified Electric Reliability Organization may subsequently file with the Commission a request to modify the plan, formula and/or methodology from time-to-time in the Electric Reliability Organization's discretion.

(~~e~~) All entities within the Commission's jurisdiction as set forth in section 215(b) of the Federal Power Act are required to pay the Electric Reliability Organization's assessment of dues, fees and charges in a timely manner reasonably designated by the Electric Reliability Organization .

(~~e~~f) Any person who submits an application for certification as the Electric Reliability Organization pursuant to the rules set forth in this section may include in such application a plan for a transitional funding mechanism that would allow such person, if certified as the

Electric Reliability Organization, to continue existing operations without interruption as it transitions from one method of funding to another. The maximum duration of any proposed transitional funding mechanism is not to exceed eighteen (18) months from the date of certification.

(g) On a demonstration of unforeseen and extraordinary circumstances requiring additional funds prior to the next funding cycle, the Electric Reliability Organization may file with the Commission for authorization to collect a special assessment. Such filing shall include the supporting materials consistent with paragraph (a) of this Section 38.13 and a proposed recovery mechanism. After notice and an opportunity for comment, the Commission will approve or modify such request.