132 FERC ¶ 61,024
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;
Marc Spitzer, Philip D. Moeller,
and John R. Norris.

North American Electric Reliability Corporation Docket No. RR10-7-000

ORDER CONDITIONALLY ACCEPTING COMPLIANCE MONITORING AND ENFORCEMENT PROGRAM AGREEMENTS AND REVISED DELEGATION AGREEMENTS, AND ORDERING COMPLIANCE FILING

(Issued July 12, 2010)

1. On March 10, 2010, the North American Electric Reliability Corporation (NERC) filed a petition requesting approval of two Compliance Monitoring and Enforcement Program Agreements (CMEP Agreements). These agreements, formed between SERC Reliability Corporation (SERC) and Southwest Power Pool (SPP) (SERC-SPP Agreement), and between SERC and Florida Reliability Coordinating Council (FRCC) (SERC-FRCC Agreement), provide that SERC will act as the Compliance Enforcement Authority for compliance matters involving all registered entity functions for FRCC and SPP within their respective regions. NERC also requests approval of amendments to the Regional Entity Delegation Agreements of FRCC, SERC, and SPP, which were modified to reflect the proposed CMEP Agreements. The Commission conditionally accepts the aforementioned agreements, subject to NERC making a compliance filing, as discussed below.

I. Background

2. On February 3, 2006, the Commission issued Order No. 672 to implement the requirements of section 215 of the Federal Power Act (FPA) governing electric reliability.[1] Among other things, Order No. 672 authorizes the Electric Reliability

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

Organization (ERO) to delegate its authority to a Regional Entity applicant by filing a delegation agreement with the Commission.[2] In its final rule, the Commission considered the appropriateness of a combined system operator serving as a Regional Entity.[3] Recognizing that such an organization may have "an inherent conflict of interest," the Commission determined that a combined system operator or regional reliability council may seek Regional Entity status, but to qualify as a Regional Entity, the entity must demonstrate "a very strong separation between the oversight and operations functions."[4]

3. On April 4, 2006, NERC submitted an application seeking authorization to serve as the ERO. In its application, NERC submitted its proposed organizational documents and operating agreements, including a proposed *pro forma* delegation agreement. In July 2006, the Commission issued an order certifying NERC as the ERO but directing NERC to incorporate specific changes to its proposed *pro forma* delegation agreement.[5] NERC subsequently amended its *pro forma* delegation agreement and requested authority, pursuant to FPA section 215(e)(4) and section 39.8 of the Commission's regulations, to delegate certain of its functions to eight Regional Entities, including SERC, SPP, and FRCC. On April 19, 2007, the Commission conditionally approved the delegation agreements of the eight Regional Entities.[6] However, in its order approving the Regional Entity delegation agreements, the Commission expressed concern over potential conflicts of interest in several of the Regional Entities affiliated with a registered entity and directed NERC to remedy these independence concerns in a compliance filing.[7] In response, NERC submitted a compliance filing detailing temporary measures intended to remedy the Commission's independence concerns.

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[2] *Id*. P 670-673.

[3] *Id*. P 687.

[4] *Id*. P 697-700.

[5] *North American Electric Reliability Corp.*, 116 FERC ¶ 61,062 (2006), *order on reh'g and compliance*, 117 FERC ¶ 61,126 (2006), *aff'd sub nom. Alcoa v. FERC*, 564 F.3d 1342 (D.C. Cir. 2009).

[6] *Order Accepting ERO Compliance Filing, Accepting ERO/Regional Entity Delegation Agreements, and Accepting Regional Entity 2007 Business Plans*, 119 FERC ¶ 61,060 (2007) (*Order Accepting ERO Compliance Filing*), *order on reh'g*, 120 FERC ¶ 61,260 (2007).

[7] *See Order Accepting ERO Compliance Filing*, 119 FERC ¶ 61,060 at P 397, 456, 551.

However, the Commission subsequently found it proper to direct NERC to assume the expanded compliance oversight itself, or to find alternative parties capable of enforcing compliance, in order to ensure that a Regional Entity that also has registered entity functions, would not monitor compliance of its own registered entity functions.[8]

II. Summary of NERC Petition

4. NERC requests approval of two CMEP Agreements—the SERC-SPP Agreement and the SERC-FRCC Agreement.[9]

5. Section 1 of each CMEP Agreement provides that SERC will: (1) administer all compliance processes in section 3.0 of the NERC Uniform CMEP with respect to the FRCC or SPP registered functions, respectively; (2) lead all compliance audits and compliance violation investigations of the FRCC or SPP registered functions; (3) determine if notices of alleged violations and proposed penalties or sanctions should be issued with respect to the FRCC or SPP registered functions, and calculate or determine any proposed penalties or sanctions in accordance with the NERC Sanction Guidelines; (4) administer notifications and other processes as specified in section 5.0 of the NERC Uniform CMEP with respect to any notices of alleged violations and proposed penalties or sanctions issued with respect to the FRCC or SPP registered functions; (5) review and approve proposed mitigation plans submitted by a FRCC or SPP registered function; (6) determine if Remedial Action Directives should be issued to FRCC or SPP with respect to their registered functions, and issue such Remedial Action Directives if determined to be necessary; (7) conduct settlement negotiations for any violations of reliability standards discovered by SERC; and (8) provide due process

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[8] *Order Addressing Revised Delegation Agreements*, 122 FERC ¶ 61,245, at P 226 (2008). Specifically, in the context of discussing the delegation agreement between NERC and the Western Electricity Coordinating Council (WECC), we stated:

> We accept WECC's proposal regarding the separation of its compliance and reliability coordinator functions as an interim measure, i.e., until additional measures can be put in place that will ensure that WECC does not monitor compliance of its own operations. If NERC continues to be unable to assume an expanded role regarding these matters, NERC and WECC will be required to assign this role to: (i) another Regional Entity; or (ii) a third party who reports directly to NERC and who is approved by NERC and the Commission.

[9] The CMEP Agreements include sections 6 through 17, which are not discussed in the body of this order. *See* NERC Petition, Attachments 1 & 2.

hearings for the FRCC and SPP registered functions in accordance with Attachment 2 of the NERC Uniform CMEP.[10]

6. Sections 2(a), 2(b), and 2(c), of each CMEP Agreement, specify that FRCC and SPP agree to: (1) establish and designate to SERC a primary compliance contact for each registered function in accordance with section 2.0 of the NERC Uniform CMEP; (2) timely respond to and comply with all notices, requests for information and schedules issued by SERC as the Compliance Enforcement Authority pursuant to the NERC Uniform CMEP; and (3) provide subject matter experts as requested by SERC to provide technical advice and assistance to SERC in SERC's carrying out of the CMEP with respect to the FRCC and SPP registered functions.[11] In section 2(e), FRCC and SPP agree to continue to perform all CMEP responsibilities within the FRCC and SPP regions that are not covered by the agreements with SERC, in accordance with the NERC-FRCC and NERC-SPP delegation agreements.[12]

7. Sections 2(d) and 5 of the CMEP Agreements address the method of compensation for SERC acting as the Compliance Enforcement Authority. Section 2(d) obligates FRCC and SPP to reimburse SERC for the actual, reasonable costs of SERC's performance of the CMEP with respect to the FRCC and SPP registered functions, and requires that such reimbursement include an appropriate allocation of SERC's general and administrative costs. Section 5 of the SERC-FRCC Agreement states that, for 2010, FRCC agrees to compensate SERC $5,000 per quarter, to be pro-rated for any partial quarter. Section 5 of the SERC-SPP Agreement provides that SPP agrees to pay SERC a fixed compensation amount of $40,000 for the remainder of 2010. Section 5 further provides that, in its annual business plan and budget for 2011 and each subsequent year, SERC shall identify that portion of its CMEP budget that is attributable to the performance of the CMEP with respect to FRCC and SPP registered functions. The amount of the FRCC/SPP registered functions CMEP budget for each year shall be excluded from the calculation of SERC's assessments to load serving entities in the

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[10] NERC Petition at 8-9, 14-16, Attachments 1 & 2.

[11] We note that each of the CMEP Agreements provide that subject matter experts that may be provided to SERC, by FRCC or SPP, are limited to consulting or advising on technical matters alone and "shall have no decision-making responsibilities with respect to any compliance processes or compliance enforcement matters, and shall not be a member of any compliance audit team, CVI team, or review team for self-certifications, spot check responses, periodic data submittals, self-reports, exception reports or complaints submitted by or relating to a [FRCC or SPP] Registered Function." *Id*. at 11, 17, Attachments 1 & 2.

[12] *Id*. at Attachments 1 & 2.

SERC region and shall be included in FRCC and SPP assessments. As a function of SERC submitting its annual business plans and budgets to NERC and the Commission for review and approval, the SPP and FRCC portion of SERC's CMEP budget will also be subject to review.

8. Section 3 of the CMEP Agreements addresses the disposition of any penalty monies collected from FRCC and SPP as a function of SERC's CMEP activities. Specifically, the agreements provide that any penalties paid by FRCC or SPP for reliability standards violations by a FRCC or SPP registered function, shall reduce that portion of the FRCC ERO or SPP RE ERO assessment paid by load-serving entities and designees in the FRCC or SPP region for the subsequent fiscal year.

9. Section 4 of the CMEP Agreements provides for the transfer to SERC of responsibility for CMEP activities with respect to the FRCC and SPP registered entity functions in progress on the effective date of the agreements.

10. Section 6 of the CMEP Agreements indicates that the initial term of each agreement will last from the effective date to December 31, 2012. Absent notice of intent to terminate, from one of the parties, each agreement will automatically renew for additional three-year terms, indefinitely.

11. NERC also requests approval of amendments to the Regional Entity Delegation Agreements of SERC, SPP, and FRCC, as well as provisions of the SERC Bylaws, to ensure their conformity with the CMEP Agreements. Specifically, modifications were made to the Regional Entity Delegation Agreements to ensure that delegation of the pertinent CMEP authority is transferred from FRCC and SPP to SERC.[13]

12. Finally, NERC requests approval of an unrelated amendment to the FRCC Regional Entity Delegation Agreement which removes section 1.2 of Exhibit D, titled "Deviations from the NERC Compliance Monitoring and Enforcement Program." NERC indicates that enactment of the SERC/FRCC agreement will no longer require FRCC to have deviations from the NERC CMEP.

13. NERC does not request a specific effective date for the agreements. Rather, NERC notes that the effective date of each agreement is left blank but will be a date subsequent to Commission approval, or an effective date specified by the Commission.

III. Notice of Filing and Responsive Pleadings

14. Notice of the NERC Petition was published in the *Federal Register*, 75 Fed. Reg. 13,112 (2010), with interventions and protests due on or before March 31, 2010. FRCC,

[13] *Id*. at 20-24, Attachments 3-8.

SERC, and Midwest Reliability Organization (MRO) filed timely motions to intervene; FRCC and SERC filed comments, while MRO filed a protest. SPP Registered Entity (SPP-RE) filed a late motion to intervene. SPP-RE, FRCC, and NERC filed responses to MRO's protest.

IV. Discussion

A. Procedural Matters

15. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2010), the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

16. We find the late intervention of SPP-RE demonstrates that it has an interest in this proceeding that cannot be adequately represented by any other party. Given this fact and the lack of undue prejudice or delay, we will grant the late-filed motion to intervene. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2010), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We will not accept the answers filed by SPP-RE, FRCC, and NERC, because they do not provide information that would further assist us in our decision-making process.

B. CMEP Agreements

17. We conditionally accept both the SERC-SPP Agreement and the SERC-FRCC Agreement, subject to NERC submitting a compliance filing to address our concerns, as discussed below.

1. Independence and Qualifications of SERC

a. NERC Petition and Supporting Comments

18. In support of SERC undertaking CMEP responsibilities with respect to the FRCC and SPP registered entity functions, NERC explains that SERC has developed organizational expertise, staffing, resources and experience in Regional Entity CMEP functions which it could utilize effectively to perform the CMEP responsibilities at issue. More specifically, NERC asserts that SERC, as the Compliance Enforcement Authority for the SERC Region that has developed staffing, resources and processes to carry out day-to-day CMEP activities as a Regional Entity, is better suited than NERC to similarly carry-out such CMEP activities with respect to FRCC and SPP.

19. In its comments, FRCC supports NERC's petition, agreeing that SERC is qualified to undertake effective and efficient compliance monitoring and enforcement of FRCC and SPP's registered functions. FRCC states that because of SERC's experience,

resources, geographic proximity, and other factors cited in the NERC Petition, SERC will provide a high standard of compliance monitoring and enforcement.

20. In its comments, SERC also expresses support for NERC's petition. SERC states that, due to its institutional expertise, its proximity to both regions, and the fact that affiliates of SPP are already registered in the SERC region, SERC is qualified to conduct the compliance monitoring and enforcement of the FRCC and SPP registered functions.[14]

b. MRO Protest

21. MRO protests that the proposed CMEP Agreements would compromise the independent functioning of Regional Entities and that issues related to accommodating Regional Entities that also perform reliability activities (e.g., registered entities) hinder improvements to reliability, and are contrary to a strong, independent self-regulatory organization. MRO contends that NERC is in a better position to ensure proper accounting of extra-regional Compliance Enforcement Authority responsibilities and to ensure that costs are not unfairly allocated to either party. Further, MRO expresses concern that, because the Regional Entities work closely with one another in a cooperative fashion, any Regional Entity that is Compliance Enforcement Authority over another "would be inclined to overcompensate" its authority in an attempt to appear "extra objective."[15]

22. MRO requests that the Commission direct NERC to enter into the agreements with SPP RE and FRCC as the Compliance Enforcement Authority, or minimally, that the Commission approve the agreements on the condition that, after an established transition period, NERC would draft new agreements to replace SERC as the Compliance Enforcement Authority, with ultimate responsibility for fulfilling CMEP activities.

c. Commission Determination

23. The Commission finds that the record adequately supports that SERC is both qualified and sufficiently independent to act as the Compliance Enforcement Authority

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[14] SERC also contends that it provides advantages over NERC. Specifically, SERC claims that NERC acting as the Compliance Enforcement Authority would diminish due process rights since the right to appeal would bring a registered entity before the same authority that assessed the penalties. While we approve SERC as the Compliance Enforcement Authority, we reject this rationale offered by SERC because NERC's compliance staff is separate and distinct from the component of NERC responsible for handling the appeal process.

[15] MRO March 31, 2010 Protest at 7 (MRO Protest).

for the registered functions performed by FRCC and SPP.[16] Further, we are not persuaded by MRO's claims that the proposed CMEP Agreements jeopardize the independent functioning of Regional Entities. The Commission has previously stated that a Regional Entity may perform compliance monitoring and enforcement duties for another Regional Entity.[17] Thus, contrary to MRO's assertions, the Commission finds that designating SERC as the Compliance Enforcement Authority does not make NERC any less responsible for ensuring ultimate compliance. Regardless of which entity is the Compliance Enforcement Authority or physically participates in the CMEP activities, NERC retains responsibility over all reliability standard compliance by a registered entity that is a Regional Entity or affiliated with a Regional Entity.[18] Accordingly, the Commission approves the CMEP Agreements authorizing SERC to serve as the Compliance Enforcement Authority for SPP and FRCC.[19] However, we wish to address MRO's concern that the proposed arrangements could disturb the equal footing of the Regional Entities and make them less inclined to cooperate effectively. As discussed below, we approve NERC's petition for a limited time period to assess the effectiveness of the CEMP Agreements and to determine whether, in practice, any drawbacks have developed.

2. Disposition of Penalties Paid (Section 3)

a. NERC Petition

24. In its petition, NERC asserts that because "the LSEs in the FRCC [and SPP] Region will be paying, through the annual assessments, SERC's costs to perform the CMEP responsibilities with respect to the FRCC [and SPP] registered entity functions," it is appropriate that any penalty monies resulting from violations against FRCC or SPP should offset the funding requirement for those respective regions.

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[16] SPP, Inc. is registered in the NERC compliance registry as a transmission service provider and other functions for its regional transmission organization (RTO) operations. The SERC-SPP agreement pertains to compliance and enforcement monitoring of SPP RTO registered functions.

[17] *Order Addressing Revised Delegation* Agreements, 122 FERC ¶ 61,245 at P 226.

[18] Order No. 672, 114 FERC ¶ 61,104 at P 654.

[19] We note, however, that the proposed CMEP Agreements merely represent one approach to addressing the Commission's previously articulated independence concerns.

b. Commission Determination

25. The Commission is not persuaded by NERC's arguments to allow penalty monies collected from SPP or FRCC to offset the funding requirements of the respective regions. The Commission has made it clear that monies from any penalties levied against a registered entity that is also a Regional Entity may not be used to offset the funding of that region, and that the investigating entity should receive any penalty monies resulting from its properly conducted compliance investigations.[20] Specifically, we have explained:

> In a situation where a monetary penalty is assessed against the operational side of one of these organizations, it is inappropriate for the Regional Entity to receive the penalty money as an offset against its next-year budget. We are concerned that allowing the Regional Entity to retain the penalty money would merely result in an accounting transfer from one division of the umbrella organization to another. Reducing a monetary penalty to an accounting notation would diminish the effectiveness of the statutory penalties and would not serve as sufficient deterrent to ensure that the operational side of the organization is in compliance with all applicable reliability standards. This reasoning applies regardless of whether the investigation and hearing leading up to the penalty assessment are conducted by the Regional Entity or the ERO….[W]e conclude that a monetary penalty assessed against the operational side of the organization should be received by the ERO and should be treated as a general offset of the next year's ERO budget for statutory activities. This will remove the disincentives created by having the same organization pay and receive a monetary penalty.[21]

Based on this rational, we conclude that it is inappropriate that, when SERC assesses a penalty against SPP or FRCC pursuant to the compliance agreements, the penalty money be treated as an offset against the funding requirements of either the SPP or FRCC Regional Entity, respectively. While the above-quoted statement suggests that the ERO should receive the penalty monies, we believe that it is reasonable in the context of the immediate proceeding for SERC to receive any penalty money as a general offset

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[20] Order No. 672, 114 FERC ¶ 61,104 at P 626. Under the current NERC-WECC arrangement, NERC is compensated for its services and, in addition, any penalty monies resulting from violations against the registered entity functions of WECC will offset the funding requirement of NERC, rather than WECC. *See* WECC Delegation Agreement, Section 8(h) and Exhibit E, Section 4 (Docket No. RR07-1-004).

[21] *Order Accepting ERO Compliance Filing*, 119 FERC ¶ 61,060 at P 228-229.

to its next-year statutory budget, as SERC will be the Compliance Enforcement Authority conducting the audits, investigations or other enforcement activities that result in the assessment of a penalty. Therefore, we direct that the CMEP Agreements be modified such that SERC will receive any monies from penalties against SPP and FRCC, and that there will be no offset to SPP's or FRCC's assessments from the ERO for such penalty monies.

3. Term and Termination (Section 6)

a. MRO Protest

26. MRO asserts that the inclusion of an automatic renewal provision in the CMEP Agreements would "[extend] indefinitely a co-dependent rather than [] independent relationship" between Regional Entities.[22] MRO suggests that, if the Commission is inclined to approve the agreements, the Commission should revise the CMEP Agreements to remove the automatic renewal provision.

b. Commission Determination

27. The Commission generally agrees with MRO on this issue. Because the effectiveness of such CMEP arrangements has not yet been tested, the Commission finds it is necessary to modify the CMEP Agreements by removing the automatic renewal provisions, subject to our re-evaluation and re-approval following the initial term, scheduled to end on December 31, 2012. This opportunity for re-evaluation and re-approval will provide the Commission, NERC, and the parties to the CMEP Agreements with an essential opportunity to consider issues that may arise from these CMEP arrangements, after assessing their effectiveness for an initial period of time, prior to renewal.

C. FRCC, SERC, and SPP Regional Entity Delegation Agreements and SERC Bylaws

28. The Commission finds that the proposed modifications to the SERC Regional Entity Delegation Agreement and Bylaws are consistent with the above discussed modifications to the CMEP Agreements and allow SERC to act as the Compliance Enforcement Authority with respect to those reliability functions for which FRCC and SPP are the registered entity within their respective regions. However, as discussed above, to the extent we cannot accept that portion of the CMEP Agreements that provides for distribution of penalty monies to the non-compliant entity rather than to SERC, we must similarly direct SERC, FRCC, and SPP to alter the corresponding provisions of the

[22] MRO Protest at 10.

Regional Entity Delegation Agreements. Notwithstanding the aforementioned concerns, we will accept the modified Regional Entity Delegation Agreements but direct SERC, SPP and FRCC to revise these agreements such that SERC will receive any monies from penalties against SPP and FRCC. The Commission also approves the modification to the FRCC Regional Entity Delegation Agreement, which revises section 1.2 of Exhibit D relating to FRCC's deviations from the NERC Uniform CMEP and eliminates certain obsolete attachments.

The Commission orders:

(A) The SERC-SPP Agreement is hereby conditionally accepted, to become effective on the date of the issuance of this order.

(B) The SERC-FRCC Agreement is hereby conditionally accepted, to become effective on the date of the issuance of this order.

(C) With the exception of the proposed modification to Exhibit D of FRCC's Regional Entity Delegation Agreement and associated modifications, which are unconditionally accepted, the modified Regional Entity Delegation Agreements are hereby conditionally accepted, to become effective on the date of the issuance of this order.

(D) NERC is hereby directed to submit a compliance filing within 90 days of this order, with amended CMEP Agreements and Regional Entity Delegation Agreements, as discussed in the body of this order.

By the Commission.

(S E A L)

Kimberly D. Bose,
Secretary.