

124 FERC ¶ 61,260  
UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;  
Sudeen G. Kelly, Marc Spitzer,  
Philip D. Moeller, and Jon Wellinghoff.

PJM Interconnection, L.L.C.

Docket No. ER08-1144-000

ORDER ACCEPTING TARIFF REVISIONS AND REQUIRING COMPLIANCE  
FILING

(Issued September 18, 2008)

1. On June 20, 2008, under section 205 of the Federal Power Act (FPA),<sup>1</sup> PJM Interconnection, L.L.C. (PJM) submitted revisions to its Amended and Restated Operating Agreement. Specifically, PJM is adding a new Schedule 11 - Allocation of Costs Associated with North American Electric Reliability Corporation (NERC) Penalty Assessments (Schedule 11). PJM states that the purpose of the proposal is to create a method for allocation of penalties regarding violations of NERC Reliability Standards, in those instances where a specific entity other than the registered entity is at least partly culpable in the Reliability Standards violation. As discussed below, the Commission accepts the revisions, effective September 19, 2008, as requested, subject to the modifications discussed below.

**I. Background**

2. Section 1211 of the Energy Policy Act of 2005 (EPAct 2005)<sup>2</sup> added section 215 to the FPA, which provides for the development and enforcement of mandatory Reliability Standards by an electric reliability organization (ERO) to be certified by the

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<sup>1</sup> 16 U.S.C. § 824d (2006).

<sup>2</sup> Pub. L. No. 109-58, § 1211, 119 Stat. 594, 941-46 (2005) (codified at 16 U.S.C. § 824o (2006)).

Commission. Penalties for violations of Reliability Standards are to be imposed by the ERO, subject to Commission approval.<sup>3</sup> On July 20, 2006, the Commission certified NERC as the ERO.<sup>4</sup>

3. Order Nos. 672 and 672-A<sup>5</sup> implemented the requirements of EPCA 2005 regarding the selection, standard-setting procedures, and operational aspects of the ERO. In these orders, the Commission denied requests to: (i) exempt non-profit RTOs and ISOs from monetary penalties for violations of the Reliability Standards; and (ii) authorize RTOs and ISOs to recover such monetary penalties from their customers on a generic basis. Rather, the Commission stated it would consider on a case-by-case basis proposals under section 205 of the FPA by RTOs and ISOs to recover the costs of any monetary penalties that may be imposed on them for the violation of Reliability Standards.<sup>6</sup>

4. Each NERC-developed, Commission-approved Reliability Standard includes an “applicability” section that identifies the types of registered entities that must comply with the standard based on the NERC Functional Model, such as generator owners, transmission owners, transmission operators, or reliability coordinators. All RTOs and ISOs have registered as transmission service providers, as well as other functions as appropriate. Thus, an RTO or ISO that fails to comply with the requirements of the applicable Reliability Standards may be assessed a penalty by a Regional Entity, the ERO, or the Commission pursuant to section 215(e) of the FPA.

5. In Order No. 693, the Commission stated that it is important to have as much certainty and stability as possible regarding which users, owners, and operators of the Bulk-Power System must comply with which Reliability Standards. NERC, as the ERO, has developed its compliance registry process in order to accomplish this goal. The Commission has previously found NERC’s compliance registry process to be a reasonable means “to ensure that the proper entities are registered and that each knows

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<sup>3</sup> The Commission, on its own motion, may also investigate violations of the Reliability Standards and impose penalties. 16 U.S.C. § 824o(e)(3) (2006).

<sup>4</sup> *North American Electric Reliability Corp.*, 116 FERC ¶ 61,062, *order on reh’g*, 117 FERC ¶ 61,126 (2006).

<sup>5</sup> *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, at P 634-35, *order on reh’g*, Order No. 672-A, FERC Stats. & Regs. ¶ 31,212 (2006).

<sup>6</sup> Order No. 672 at P 634-35; Order No. 672-A at P 55-58.

which Commission-approved Reliability Standard(s) are applicable to it.”<sup>7</sup> For example, NERC registers only those distribution providers or LSEs that have a peak load of 25 MW or greater and are directly connected to the bulk electric system, or are designated as a responsible entity as part of a required underfrequency load shedding program or a required undervoltage load shedding program. For generators, NERC registers individual units of 20 MVA or greater that are directly connected to the bulk electric system, generating plants with an aggregate rating of 75 MVA or greater, any blackstart unit material to a restoration plan, or any generator regardless of size, that is material to the reliability of the Bulk-Power System.<sup>8</sup>

6. Order No. 693 states that the Commission will not assess penalties against an entity that has not previously been put on notice, through the NERC registration process, that it must comply with particular Reliability Standards. Under this process, if NERC later discovers that an unregistered entity should have been subject to the Reliability Standards, NERC has the ability to add the entity, and possibly other entities of a similar class, to the registration list and to direct corrective action by that entity on a going-forward basis.<sup>9</sup> The Commission believes that this should prevent an entity from being subject to a penalty for violating a Reliability Standard without prior notice that it must comply with that Reliability Standard.

7. In response in part to Order No. 672, Midwest ISO proposed to amend its Open Access Transmission and Energy Markets Tariff in order to ensure that Midwest ISO could pass through the costs of any and all ERO-imposed penalties, either to a targeted, culpable entity or else spread among Midwest ISO’s membership. The Commission rejected the proposal without prejudice and established a staff technical conference to address generically the issues raised by the proposal concerning Reliability Standard compliance and enforcement in regions with non-profit RTOs and ISOs.<sup>10</sup>

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<sup>7</sup> *Mandatory Reliability Standards for the Bulk Power System*, Order No. 693, FERC Stats. & Regs. ¶ 31,242 at P 92 (quoting *North American Electric Reliability Corp.*, 116 FERC ¶ 61,062, at P 689 (2006)), *order on reh’g*, Order No. 693-A, 120 FERC ¶ 61,053 (2007).

<sup>8</sup> Order No. 693 at P 93.

<sup>9</sup> See NERC Rules of Procedure, § 500.

<sup>10</sup> *Midwest Independent Transmission System Operator, Inc.*, 119 FERC ¶ 61,222 (2007).

8. In the Guidance Order<sup>11</sup> resulting from the technical conference, the Commission acknowledges the careful balance in which RTOs and ISOs found themselves. As the facilitators and managers of the nation's largest and most complex energy markets, RTOs and ISOs are essential to maintaining the reliability of the nation's electric system, but since these entities are typically member-supported non-profits, they do not have an independent source of funds with which to pay any Reliability Standards penalties that they might be assessed by the ERO. Granting blanket authority to automatically pass through monetary penalties to their customers, however, could dangerously diminish the incentives for RTOs and ISOs to maintain strict compliance with Reliability Standards. Accordingly, the Guidance Order prohibits RTOs and ISOs from adopting tariff mechanisms that provide automatic recovery of penalties incurred for Reliability Standard violations; instead, it requires that proposals to recover any such penalties be filed case-by-case.<sup>12</sup>

## II. PJM Proposal

9. PJM is the first RTO or ISO to make a filing on this subject since the Guidance Order was issued. PJM is registered with the applicable Regional Entities (ReliabilityFirst Corporation (RFC) and SERC Reliability Corporation (SERC)) for the following functions: Transmission Operator, Balancing Authority, Planning Coordinator, Reliability Coordinator, Resource Planner, Transmission Planner, and Transmission Service Provider. PJM states that PJM Members have also registered themselves with RFC and SERC in accordance with the registration process, based on each company's own responsibilities and consistent with the PJM's Governing Agreements. Currently, PJM states, the entity that registers for a given function will be the entity subject to penalty where such standards are violated.

10. PJM states that in March 2007, PJM and its Members began a stakeholder process to modify the Operating Agreement to allow for the direct assignment of Reliability Standards penalty costs. PJM states that the consensus of its membership is that if an entity other than the registered entity, by its act or omission, causes the registered entity to violate a Reliability Standard, then the culpable entity should compensate the registered entity for any reliability penalty levied by NERC or its Regional Entities. PJM therefore proposes in the present filing to add a new Schedule 11 to its Operating Agreement.<sup>13</sup>

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<sup>11</sup> *Reliability Standard Compliance and Enforcement in Regions with Regional Transmission Organizations or Independent System Operators*, 122 FERC ¶ 61,247 (March 20, 2008) (Guidance Order).

<sup>12</sup> Guidance Order at P 16.

<sup>13</sup> See PJM June 20, 2008 Filing.

11. Section 1.1 of Schedule 11 states that the Schedule's purpose is to allow either PJM to seek to pass through NERC penalties to a Member who contributed to PJM's being fined, or vice versa: a Member may seek to pass through NERC penalties to PJM if PJM contributed to the Member's being fined. Section 1.2 defines various terms in the agreement, such as the Compliance Monitoring and Enforcement Program, a phrase that encompasses any investigations, hearings, and levying of penalties by NERC and its Regional Entities.<sup>14</sup>

12. Section 1.3(a) of Schedule 11 would authorize PJM to "directly allocate [] penalty costs or a portion thereof to the Member or Members whose conduct contributed to the Reliability Standards violation(s)." According to section 1.3(a), PJM would only have this authority if all three of the following preconditions are met:

- The target "Members receive[] notice and an opportunity to fully participate in the Compliance Monitoring and Enforcement Program" conducted by NERC or NERC's Regional Entities.
- The NERC Compliance Monitoring and Enforcement Program holds a proceeding that finds that the target Members at least in part "contributed ... to the NERC Reliability Standards violation(s)", and files this finding with the Commission.
- NERC also files a root cause filing with the Commission, "identifying the Member's or Members' conduct as causing or contributing to the Reliability Standards violation charged against PJM."

13. Section 1.3(b) clarifies that PJM bears responsibility for notifying the target Members not only during the investigation phase, but again after the target Members are "found to have contributed to a violation," at which point PJM must specify in writing its intent to assign penalty costs. Section 1.3(d) similarly requires PJM to notify the target Members after the investigation is complete that it believes the criteria for seeking pass-through have been satisfied. Section 1.3(c), by contrast, clarifies that target Members may not escape penalization by simply failing to avail themselves of their right to participate in the NERC proceedings.

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<sup>14</sup> Proposed section 1.2 defines Compliance Monitoring and Enforcement Program as: "The program to be used by the NERC and the Regional Entities to monitor, assess, and enforce compliance with the NERC Reliability Standards. As part of a Compliance Monitoring and Enforcement Program, NERC and the Regional Entities may, among other things, conduct investigations, determine fault, and assess monetary penalties."

14. PJM claims that, based on NERC's written statements in the technical conference leading up to the Guidance Order, "it is [] clear that NERC will not determine the proportion of parties' culpability.... Therefore, the final apportionment of financial responsibility among PJM and its Members is left for them and ultimately the Commission to decide."<sup>15</sup> To that end, sections 1.3(e), (f), and (g) lay out a process for determining proportions. First, PJM establishes "an initial apportionment for purposes of the cost allocation on a basis reasonably proportional to the parties' relative fault consistent with such NERC's root cause analysis."<sup>16</sup> If a target Member disagrees with PJM's apportionment, it may choose either non-binding dispute resolution with PJM<sup>17</sup> or else a section 205 filing with the Commission. Finally, if the target Members and PJM are in agreement, the proposed Schedule also calls for a section 205 filing with the Commission. In other words, Schedule 11 requires all direct assignments of Reliability Standards penalties to receive Commission approval under Federal Power Act section 205 before taking effect.<sup>18</sup>

15. Section 1.3(h) requires the target Members either to "pay their share of the Reliability Standard violation costs within 30 days of the notice required in [section] 1.3(b)", or else pay later with interest. Target Members are only obligated to pay the penalty and interest, however, if the Commission "supports the NERC's root cause findings" and also affirms "PJM's initial determinations in paragraph 1.3(f)" on the dollar apportionment of financial responsibility.

16. Section 1.4 of the proposed Schedule 11 mirrors the text of section 1.3, but applies to the converse circumstance in which the Member seeks to recover from PJM for contributing to a violation and penalty that NERC assessed against the Member. In other words, under this proposal, a PJM Member that is liable for a NERC penalty based on its status as the Registered Entity may seek to pass that penalty on to a culpable PJM, following the same preconditions, notice requirements, and settlement principles articulated in section 1.3.

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<sup>15</sup> PJM June 20, 2008 Filing at 15.

<sup>16</sup> Proposed Schedule 11, section 1.3(e).

<sup>17</sup> Proposed Schedule 11, section 1.3(f), calls for a simplified resolution process rather than the previously approved Dispute Resolution Procedures in section 5 of PJM's Operating Agreement.

<sup>18</sup> PJM June 20, 2008 Filing at 16-17.

### **III. Notice of Filing and Responsive Pleadings**

17. The Commission gave notice of PJM's filing on June 25, which was published in the *Federal Register*, 73 Fed. Reg. 37,948, on July 2, 2008. Interventions and protests were due on or before July 11, 2008.

18. The Allegheny Energy Companies, American Municipal Power - Ohio, Inc. (AMP-Ohio), Baltimore Gas and Electric Company, Constellation Energy Commodities Group, Inc. and Constellation NewEnergy, Inc., Dominion Resources Services, Inc., Duke Energy Corporation (Duke), Exelon Corporation (Exelon), the FPL Energy Generators, the J.P. Morgan Entities (J.P. Morgan), the NRG Companies, the PHI Companies, PPL Electric Utilities Corporation, the PSEG Companies (PSEG), and Rockland Electric Company (Rockland) filed timely motions to intervene.<sup>19</sup> American Electric Power Service Corporation (AEP) filed a motion to intervene out of time.<sup>20</sup>

#### **A. Comments in Support**

19. Exelon filed comments in support of the proposal. Exelon states that the proposed schedule is the result of substantial give and take among stakeholders and will foster

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<sup>19</sup> The Allegheny Energy Companies consist of Allegheny Energy Supply Company, LLC, Monongahela Power Company, The Potomac Edison Company, and West Penn Power Company (d/b/a Allegheny Power). Dominion Resources Services, Inc., intervenes on behalf of Virginia Electric and Power Company (d/b/a Dominion Virginia Power). The FPL Energy Generators consist of FPL Energy Marcus Hook, L.P., North Jersey Energy Associates, L.P., Doswell Limited Partnership, Backbone Mountain Windpower LLC, Mill Run Windpower LLC, Somerset Windpower LLC, Meyersdale Windpower LLC, Waymart Wind Farm, LP, and Pennsylvania Windfarms, Inc. The J.P. Morgan Entities consist of J.P. Morgan Ventures Energy Corporation, Bear Energy LP, BE Allegheny LLC, and BE Red Oak LLC. The NRG Companies consist of NRG Power Marketing LLC, Conemaugh Power LLC, Indian River Power LLC, Keystone Power LLC, NRG Energy Center Dover LLC, NRG Energy Center Paxton LLC, NRG Rockford LLC, NRG Rockford II LLC, and Vienna Power LLC. The PHI Companies consist of Pepco Holdings, Inc., Potomac Edison Power Company, Delmarva Power & Light Company, and Atlantic City Electric Company. The PSEG Companies consist of Public Service Electric and Gas Company, PSEG Power LLC, and PSEG Energy Resources & Trade LLC.

<sup>20</sup> American Electric Power Service Corporation intervenes on behalf of Appalachian Power Company, Columbus Southern Power Company, Indiana Michigan Power Company, Kentucky Power Company, Kingsport Power Company, Ohio Power Company, and Wheeling Power Company.

accountability, and states that it expects that any disputes that arise under the proposed schedule will be resolved informally.

20. PSEG filed comments in support of the proposal. PSEG states that the proposed schedule is the by-product of lengthy stakeholder discussions, in which the interests of both PJM and its Members were vetted and thoroughly considered. PSEG also claims that the proposal comports with the Guidance Order. While PSEG urges the Commission to approve the proposal in this docket, PSEG states for the record that NERC should improve its investigatory process, in order to ensure that the root cause findings are as detailed and accurate as possible.

### **B. Comments in Opposition and Protests**

21. J.P. Morgan files comments in opposition, while AMP-Ohio, Duke, and Rockland file protests. In addition to several miscellaneous concerns, the opponents' primary concerns were on four issues: (1) a lack of sufficient due process in NERC's Compliance Monitoring and Enforcement Program, which would accrue to the advantage of the party seeking to pass through the penalty; (2) a perceived circumvention of the NERC registration process; (3) concerns about PJM's impartiality in proposing the apportionment of penalty costs for Commission review; and (4) concerns about an imbalanced provision on interest payments.

22. In arguing for greater due process, J.P. Morgan notes that, in the Guidance Order, the Commission stated that it will not entertain a filing by an RTO or ISO to assign costs of the penalty directly to another entity unless the targeted entity has been notified during the course of the investigation that it may be held responsible by the RTO or ISO for the violation. J.P. Morgan acknowledges PJM's statement that it will give notice to an entity that may be directly assigned penalty costs and provide an "opportunity to fully participate in the underlying Compliance Monitoring and Enforcement Program (CMEP) proceeding." J.P. Morgan counters, however, that PJM admits that neither NERC nor the Regional Entities have committed to provide a procedural mechanism to allow a targeted entity to intervene and participate in the CMEP proceeding. Since PJM lacks authority to compel NERC to implement sufficient due process, J.P. Morgan argues, Schedule 11 provides no assurance of due process to a targeted entity. J.P. Morgan proposes that PJM instead use the Federal Power Act's section 206 complaint proceedings when seeking to pass through penalties.

23. Additionally, AMP-Ohio and Rockland object that Schedule 11 offers insufficient notice and due process. Rockland specifically asks the Commission to require any party seeking pass-through to specify the factual predicate for their claim and cite their authority under the PJM tariff.

24. AMP-Ohio protests that PJM should not be authorized to pass proposed penalties through to parties that the Commission did not require to register with the NERC. AMP-

Ohio states that PJM's proposal is overbroad, because it contradicts the principle that certain (usually smaller) entities that do not have a material impact on the reliability of the bulk electric system should not be forced to comply with complex and onerous Reliability Standards given their relative insignificance to grid reliability. AMP-Ohio states that PJM's proposal would create an unnecessary regional anomaly: an entity that NERC did not require to register, which in all other regions of the country would be exempt from the Reliability Standards, would be subject to potential fines for violation of such Standards within PJM.

25. Rockland similarly objects to the proposal as undermining the NERC registration system. According to Rockland, PJM's proposal would accomplish indirectly that which NERC is barred from doing: directly assessing penalties to entities not listed on its Compliance Registry. Rockland proposes that the registered entity must specifically identify what PJM tariff or contractual obligation the targeted entity has violated as a prerequisite for seeking to pass through a NERC penalty.

26. Insofar as sections 1.3(e) and 1.4(e) allows PJM or its Members to engage in discretionary apportionments of penalties, Rockland and Duke object that PJM could not act as a disinterested independent party because its ability to assess penalties for reliability infractions relieve PJM of a financial burden it would otherwise have to suffer, thus compromising the independence expected of an RTO. Duke notes that the Guidance Order states that the Commission "does not believe the RTO or ISO should be permitted to pursue a second, de novo hearing on the issue of determining responsibility for Reliability Standard [violations]."<sup>21</sup> According to Duke, the ERO is responsible for determining which entities are at fault for causing a Reliability Standards violation by examining the "root cause" of a violation; therefore, the ERO is the entity allocating both fault (to both registered entities and non-registered entities) and penalties (to registered entities). In the event that the ERO declines to allocate fault in a manner that allows PJM to collect the penalty without using some discretion and further apportioning fault, Duke argues that the filing party should simply inform the Commission that the relevant root cause findings are not clear as to allocation, and request that the Commission resolve the apportionment issue.

27. J.P. Morgan argues that proposed section 1.3(h) on interest payments discourages target Members from defending against an attempt to shift NERC penalties. Just as the registered member is entitled to earn interest on amounts owed beyond 30 days if its section 205 claim succeeds, J.P. Morgan argues, a targeted entity that pays but is later exonerated of any liability should receive a refund of any amounts paid plus interest.

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<sup>21</sup> Guidance Order at 22, *quoted in* Duke June 11, 2008 Protest at 4.

28. In addition to these main arguments parties raised several miscellaneous concerns. For example, J.P. Morgan submits that any recovery of costs from an entity other than PJM or a PJM Member is a matter outside the scope of the PJM Operating Agreement. J.P. Morgan requests clarification that proposed Schedule 11 respects PJM's limited scope. To do so, J.P. Morgan recommends that the Commission require PJM to add the following sentence at the end of proposed section 1.1: "This schedule only applies to the allocation of costs from PJM to another Member or Members or, conversely, the allocation of costs from a Member to PJM." Rockland also proposes that the Commission require the registered entity to pay a certain percentage of any NERC penalty, rather than passing on the entire cost.

### **C. PJM's Answer**

29. On July 28, 2008, PJM submitted an answer to the comments of J.P. Morgan and the protests of AMP-Ohio, Duke, and Rockland, in which it addressed each party in turn.

30. In response to J.P. Morgan's due process concern, PJM clarifies that if the targeted entity does not "have an opportunity to participate in the NERC" investigation, then "a direct assignment of the penalty will not be permitted under Schedule 11."<sup>22</sup> PJM further states that a section 205 filing is sufficient to effect Schedule 11, and that use of section 206 complaint procedures would be inconsistent with the Guidance Order. In response to J.P. Morgan's concern about non-PJM Members, PJM clarified that the proposed schedule would not apply to entities that are not PJM members.

31. PJM states that AMP-Ohio is "incorrect" in asserting that Schedule 11 would "impose excessive burdens on small non-registered entities."<sup>23</sup> PJM states that its proposal preserves the obligations of NERC-registered entities, and that Schedule 11 is designed to be a "response to violation of [PJM's] Governing Agreements."<sup>24</sup> Further, PJM argues, Schedule 11 may work to the net benefit of small non-registered entities, since they are likely to be found responsible for comparatively few NERC penalty costs, but will be spared paying the trickle-down effect if PJM were forced to absorb the costs of penalties caused by larger PJM members, which would increase the cost of doing business for everyone in the PJM region. In response to AMP-Ohio's due process point, PJM argues that AMP-Ohio misinterprets the Guidance Order. PJM states that, under the

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<sup>22</sup> PJM July 28, 2008 Answer at 6.

<sup>23</sup> *Id.* at 4.

<sup>24</sup> *Id.* at 4.

Guidance Order, the NERC registration process need not be the only means of providing sufficient notice, and may instead be provided, for example, through “provisions ... in their contracts with their members and customers and/or in their tariffs.”<sup>25</sup>

32. In response to Duke’s protest regarding discretionary apportionments of penalties, PJM argues that Duke has misunderstood the proposal. While “under Schedule 11 ... PJM and its Members can agree on apportionment ... the ultimate determination of the proportion of parties’ culpability ... will be decided by the Commission.”<sup>26</sup>

33. In response to Rockland’s argument regarding the due process, PJM “agrees in principle.”<sup>27</sup> PJM repeats that PJM and its Members delegate tasks to one another through the Governing Agreements. PJM offers, if necessary, to “amend Schedule 11 sections 1.3(b) and 1.4(b) to require that the subject notifications must include the underlying factual basis supporting a penalty cost assignment including the conduct contributing to the violation and the violations of PJM Governing Agreement assigned tasks.”<sup>28</sup> PJM rejects, however, Rockland’s proposal to require the registered entity to bear a minimum percentage of any reliability penalty. PJM states that any minimum percentage chosen would be arbitrary, and states that Rockland’s proposal was already considered and rejected by PJM and its Members.

#### **IV. Discussion**

##### **A. Procedural Matters**

34. Pursuant to Rule 214 of the Commission’s Rules of Practice and Procedure,<sup>29</sup> the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

35. In view of the early stage of this proceeding, its interest, and the absence of undue prejudice or delay, we will grant AEP’s motion to intervene out of time.

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<sup>25</sup> *Id.* at 4 (quoting Guidance Order at P 24).

<sup>26</sup> *Id.* at 7.

<sup>27</sup> *Id.* at 2.

<sup>28</sup> *Id.* at 3.

<sup>29</sup> 18 C.F.R. § 385.214 (2008).

36. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure<sup>30</sup> prohibits an answer to a protest or another answer unless otherwise ordered by the decisional authority. We will accept PJM's answer because it provided information that assisted us in our decision-making process.

**B. Substantive Matters**

37. The Commission accepts PJM's proposed revisions to its Operating Agreement, subject to conditions, to become effective September 19, 2008. PJM's Schedule 11 provides a reasonable mechanism for the assignment of penalties issued for violation of Reliability Standards. Further, Schedule 11 is consistent with our earlier Guidance Order. In the Guidance Order, the Commission held,

[W]e will not allow RTOs and ISOs to adopt tariff mechanisms that provide automatic recovery of penalties incurred for Reliability Standard violations and will instead require that proposals to recover any such penalties be filed case-by-case. In evaluating such proposals, the Commission will consider, among other things, the nature of the Reliability Standard violation and the factors that contributed to the violation, including the integrity of the RTO or ISO's compliance program to prevent such violations.<sup>31</sup>

In approving PJM's proposed tariff revision, the Commission does not deviate from that guidance. Schedule 11 does not provide for universal pass-through; rather, PJM or its Members may only pass through penalties when NERC or one of its Regional Entities concludes from its fact-finding that the targeted entity substantially contributed to the Reliability Standards violation. Schedule 11 also requires the Commission's approval, through a section 205 filing, of each specific pass-through. Should any of the concerns raised by the various protestors manifest themselves in a particular case, the Commission can and will ensure at that time that these concerns are addressed in a fair and reasonable manner.

38. Several parties raise concerns regarding due process at NERC. PJM has clarified, if the targeted entity does not "have an opportunity to participate in the NERC" investigation, then "a direct assignment of the penalty will not be permitted under Schedule 11."<sup>32</sup> The Commission finds that PJM's clarification matches section 1.3(a)(1)

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<sup>30</sup> 18 C.F.R. § 385.213(a)(2) (2008).

<sup>31</sup> Guidance Order at P 16.

<sup>32</sup> PJM July 28, 2008 Answer at 6.

and section 1.4(a)(1) of the tariff, which state that no party may invoke the allocation procedures of Schedule 11 unless the target Member has “an opportunity to fully participate in the Compliance Monitoring and Enforcement Program.” The Commission finds, therefore, that PJM’s clarification adequately resolves these concerns.

39. Several parties express concerns regarding the detail of any notice that a targeted entity may receive. In its answer, PJM volunteers to “amend Schedule 11 sections 1.3(b) and 1.4(b) to require that the subject notifications must include the underlying factual basis supporting a penalty cost assignment including the conduct contributing to the violation and the violations of PJM Governing Agreement assigned tasks.”<sup>33</sup> We will therefore accept this filing conditioned on PJM filing within 60 days to make such a tariff change.

40. AMP-Ohio argues that entities that have not been registered at all by NERC, and therefore are not directly liable for any Reliability Standards, should not be allowed to become indirectly liable under Schedule 11. The Commission disagrees. Unregistered entities in the PJM footprint will not be registered for any mandatory Reliability Standards and neither NERC nor a Regional Entity may assess a penalty against an unregistered entity. This is wholly consistent with the Commission’s Guidance Order, in which we stated “neither NERC nor the Commission may assess a penalty for the violation of a Reliability Standard against an entity which is not registered as the responsible party for complying with that Standard.”<sup>34</sup>

41. The Guidance Order, however, continues, “[s]imilarly, we will not allow the direct assignment of penalty costs to another entity under section 205 unless that entity had previously been put on notice of its potential liability for penalty costs in the event that it contributed to the RTO or ISO’s violation of a Reliability Standard and incurrence of the penalty. It is therefore important for the RTOs and ISOs to include provisions regarding the appropriate reasonability for reliability-related monetary penalties in their contracts with their member and customers and/or in their tariffs . . .”<sup>35</sup> PJM proposes to do just that. As PJM stated in its Answer, an action under Schedule 11 is designed to be a “response to violation of [PJM’s] Governing Agreements,”<sup>36</sup> in the sense that causing another entity to violate a NERC Reliability Standard is also a violation of PJM’s own

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<sup>33</sup> PJM July 28, 2008 Answer at 2-3.

<sup>34</sup> Guidance Order at P 24.

<sup>35</sup> *Id.*

<sup>36</sup> PJM July 28, 2008 Answer at 4.

rules about member relations and Good Utility Practice.<sup>37</sup> By agreeing to PJM's Operating Agreement, therefore, small unregistered parties have already conceded that they will make some effort to help maintain reliability within PJM. As we stated earlier, however, all Schedule 11 claims must come before the Commission as section 205 filings, and in accordance with our Guidance Order, we must review those filings on a case-by-case basis. Such unregistered entities will have the opportunity, if they so choose, to raise similar challenges before NERC during the Compliance Monitoring and Enforcement Program phase.

42. As noted above, Rockland and Duke object to sections 1.3(e) and 1.4(e), which let the registered entity make the initial proposed apportionment of the penalty costs, in a manner reasonably proportional to the parties' relative fault. Protestors argue that PJM could not perform this task in a disinterested manner. The Commission finds it reasonable, however, that the party who files the section 205 filing also propose in its filing the amount that it seeks to allocate. As with any section 205 filing, the allocating entity's proposal is not binding on the Commission and will be rejected if it is unreasonable.

43. The Commission also notes that sections 1.3(h) and 1.4(h) provide that if the allocating entity notifies the targeted entity that it seeks to allocate costs associated with a NERC penalty, and the targeted entity fails to pay the noticed amount within 30 days of receiving such notice and the Commission later confirms the noticed amount, the targeted entity owes the payment plus interest calculated at the FERC authorized rate from the date of payment of the penalty by the Registered Entity to NERC. As J.P. Morgan notes in its comments, these sections fail to provide for the reciprocal contingency in which the targeted entity pays the penalty allocation amount under protest by it or another party to the allocation, and later the Commission determines that the targeted entity should have paid none or some lesser portion of that allocation. As a condition of accepting this filing, therefore, PJM must file revised sections 1.3(h) and 1.4(h) within 60 days providing a means by which an entity paying the penalty amount can earn interest on such payment in the event it prevails.

44. Other possible amendments are raised by protestors, namely, a limit on the initial apportionment of penalties, and a further clause affirming the self-evident principle that Schedule 11 can only apply to PJM and its Members. The Commission finds it just and reasonable that PJM's proposal does not to impose an arbitrary limit on the total amount recoverable from a culpable entity. PJM should be permitted to recover any amount for which another party is responsible. The issue of penalty apportionment need not be delineated in the tariff, because such an issue may be dependant on particular facts and

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<sup>37</sup> See, e.g., PJM Operating Agreement, Schedule 1, section 1.7.4 (a)(i) ("each Market Participant shall at all times (i) follow Good Utility Practice.")

circumstances and can be resolved when such an issue is raised in a particular case. Finally, we accept PJM's clarification, in its answer, that the proposed schedule would not apply to entities that are not PJM members.

45. The Commission finds that the proposed tariff revisions are just and reasonable, and supported by the majority of PJM members. The revisions are, therefore, accepted to become effective September 19, 2008, as requested.

The Commission orders:

The tariff revisions filed June 20, 2008 are accepted to become effective September 19, 2008, subject to the condition that PJM file, within 60 days of the date of this order, to amend Schedule 11 sections 1.3(b), 1.3(h), 1.4 (b), and 1.4(h), as discussed in the body of this order.

By the Commission.

( S E A L )

Kimberly D. Bose,  
Secretary.