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8 PANELISTS:

9 PANEL I

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- 14 DANIEL SKAAR
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1 PANELISTS:

2 PANEL I (Cont'd)

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4 Director, Regulatory Affairs and

5 NERC Reliability Standards

6 RRI Energy, Inc.

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8 PANEL II

9 GERRY W. CAULEY

10 President and Chief Executive Officer

11 NERC

12 STACY DOCHODA

13 General Manager

14 SPP Regional Entity

15 WILLIAM J. FEHRMAN

16 CEO and President

17 MidAmerican Energy Company

18 DAVID MOHRE

19 Executive Director

20 Energy and Power Division

21 National Rural Electric Cooperative

22 Association

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1 PANELISTS:

2 PANEL II (CONT'D)

3 JOHN DISTASIO

4 Chief Executive Officer

5 Sacramento Municipal Utility District

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1 P-R-O-C-E-E-D-I-N-G-S

2 (1:02 P.M.)

3 MR. BAY: Good afternoon. I am Norman Bay,
4 the director of the Office of Enforcement at the
5 Commission. I would like to welcome those of you who
6 are in the audience today and those of you who are
7 watching the webcast, the Commission's Technical
8 Conference under liability monitoring enforcement and
9 compliance issues and Docket No. AD11-1-00.

10 This technical conference follows up on the
11 Commissions' July 6th technical conference that
12 focused on the Electric Reliability Organizations'
13 standards development process in communication and
14 interactions between the Commission, NERC, and the
15 Regional Entities.

16 It is in that spirit of open communications
17 that the Commission will address today current issues
18 relating to the compliance with Reliability Standards
19 with two distinguished panels of experts from the
20 industry, NERC, and the Regional Entities. The
21 commissioners and the staff look forward to hearing
22 your views.

23 Before turning the meeting over to Chairman
24 Wellinghoff, let me cover a few housekeeping matters.
25 We have asked the panelists to limit their opening

1 remarks to five minutes, so the commissioners will
2 have sufficient time to follow up with questions.

3 Staff will time the presentations and inform
4 each panelist when he or she is approaching that
5 limit. The panelists will make the remarks in the
6 order they are listed in the agenda.

7 After each panel completes their remarks,
8 the floor will be opened to questions from the
9 commissioners. After the commissioners finish their
10 discussion with the first panel, we will take a short
11 break around 2:45 p.m. before beginning the second
12 panel.

13 After the discussion with the second panel
14 is complete, we will open the floor to questions from
15 the audience. We ask each person who wishes to pose a
16 question at that time to come to the microphones that
17 are set up at the edges of the seating area, identify
18 themselves and a company or organization they are
19 with. This is primarily to help the court reporter
20 and the people watching the proceedings via the
21 webcast.

22 Without further ado then, let me turn the
23 floor over to Chairman Wellinghoff.

24 CHAIRMAN WELLINGHOFF: Thank you very much,
25 Norman.

1 This is a Commission-chaired conference as
2 opposed to a staff-chaired conference, and normally
3 would chair the conference. However, when
4 Commissioner La Fleur first was confirmed and we sat
5 down and talked about her interests, she expressed to
6 me her deep interest in reliability.

7 I believe in allowing people to roll their
8 sleeves up and get right involved in things, so I have
9 asked
10 her to chair the conference, the technical conference,
11 this afternoon, and she has graciously accepted that
12 request.

13 My only remarks, I am very, very interested
14 in seeing and listening to what the panel has to say
15 with respect to reliability, monitoring, enforcement,
16 and compliance issues. I look forward to being able
17 to ask some questions and delve into this area. But I
18 think it is an extremely important area for the
19 Commission to keep on the top of our agenda, and we
20 continue to do that. I am very, very happy to have
21 Commissioner La Fleur having this very deep interest
22 in this particular area.

23 With that, I will turn it over to
24 Commissioner La Fleur to chair the conference.

25 COMMISSIONER LA FLEUR: Well, thank you very

1 much, Mr. Chairman. Thank you for this opportunity.
2 I had Chinese food for lunch in the brief time we were
3 out of this room, and it reminds me of the old fortune
4 cookie of life: "Beware of what you ask for. You may
5 get it."

6 (General laughter.)

7 COMMISSIONER LA FLEUR: I am, indeed, very
8 interested in reliability. Let me begin by joining
9 Norman and the Chairman in welcoming everyone to
10 today's conference. We are very fortunate to have two
11 panels that bring tremendous experience and expertise
12 to these topics, and I look forward to hearing their
13 perspectives.

14 Before I introduce the first panel, I have
15 some brief opening thoughts, and then I will turn it
16 over to my colleagues for their opening remarks.
17 Monitoring, compliance, and enforcement, the subject
18 of today's conference, are components of the overall
19 reliability structure for which FERC, Canadian
20 Authorities, NERC, the Regional Entities, and
21 Registered Entities all share responsibility.

22 Their purpose is at bottom to protect and
23 improve the reliability and security of the Bulk-Power
24 System by helping ensure compliance with Reliability
25 Standards. We have all been working on these matters

1 for nearly five years, and it is an appropriate time
2 to assess how these matters are going.

3 As we discuss these things today, there are
4 two questions in particular I hope we can reflect on.
5 First, are we all doing all that we can to learn from
6 experience and to make sure that lessons are learned
7 from mistakes and they are spread broadly so the same
8 things don't happen again? In my experience, this is
9 one of the most important elements of a compliance
10 program but usually the hardest to achieve.

11 Second, are we working on the right things?
12 Just as I think we should prioritize our efforts on
13 standards development, so should we ensure that the
14 resources collectively devoted to monitoring
15 compliance and enforcement are well spent and focused
16 to best achieve grid reliability and security.

17 Hopefully, in today's discussion it will
18 bring to light ways that we all of us involved in
19 these matters can step up our efforts to enhance the
20 reliability and security of the system for customers.

21 With that, I will turn it to my colleagues
22 beginning with Commissioner Moeller.

23 COMMISSIONER MOELLER: Thank you,
24 Commissioner La Fleur. Thanks to the members of the
25 two panels who are here today. Some of you have come

1 a great distance to be here.

2 I echo your thoughts that these are a couple
3 of excellent panels. We appreciate the effort of you
4 and those in the audience. This is part of our
5 ongoing effort to increase the transparency of this
6 general topic area.

7 Norman, thank you for your efforts on that.
8 In addition to the work that Commissioner Spitzer and
9 Chairman Wellinghoff have undertaken on this effort
10 over the last few years together, I really want to
11 commend Commissioner Norris and Commissioner La Fleur.
12 Whether you know it or not, they have dived in from
13 the moment they were here on reliability issues.

14 Again, sometimes, as we all know, these are
15 not necessarily the most glamorous, but really what is
16 more important than ensuring the reliability of the
17 Bulk-Power System. I look forward to the conference,
18 and thank you again for everyone's effort in putting
19 it on.

20 COMMISSIONER SPITZER: Thank you,
21 Commissioner. It is a great opportunity, one of the
22 best at FERC, to be entrusted with the mission of
23 reliability that of course was granted by Congress in
24 2005. It is important that our mission not be
25 misunderstood, and I think that there has been over

1 time occasionally some misunderstanding as to FERC's
2 belief in the work that the industry, the Regional
3 Entities, and NERC have done.

4 In fact, we have an admirable record of
5 reliability with the North American Grid that we can
6 put up beside any in the world, and we are very proud
7 of that. At the same time, it is aspirational to have
8 perfection even if perfection can never be achieved.
9 We are partners -- NERC, the Regional Entities, and
10 industry -- in our aspirational pursuit of perfection.
11 We have that in the two panels before us.

12 I am fond of reciting that government is
13 about balancing competing interests. We certainly
14 have that in the two panels before us. With respect
15 to Regional Entities, it is well known that there are
16 differences across this vast country: geography, fuel
17 use, and electrical engineering.

18 At the same time, there is the Congressional
19 mandate for uniform standards for reliability.
20 Balancing those competing interests is an interesting
21 task, and I am sure you will offer your observations
22 on how we balance standards across applicable across
23 the interconnections and at the same time account for
24 regional differences.

25 On the second panel, the competing interests

1 to be balanced I think are reflected in that old U.S.
2 Supreme Court decision "All deliberate speed" from
3 Brown v. the Board of Education.

4 Of course, "deliberate" and "speed" is an
5 internal contradiction, but in the penalty process we
6 want due process. We want the right to be heard, but
7 at the same time justice delayed could be justice
8 denied.

9 A number of entities have expressed concern
10 about the temporal length of the process. We want it
11 to be deliberate, and we want it to be swift. That is
12 obviously the subject of a lot of discussion in
13 balancing the competing interests on the second panel.

14 I mostly am here to listen. I look forward
15 to the discussion. I again want to reiterate the
16 pride that I have personally on behalf of my
17 colleagues as to the work that the industry, the
18 Regional Entities, and the ERO have done in performing
19 their mission for reliability for the electrical grid
20 of this country.

21 Thank you.

22 COMMISSIONER LA FLEUR: Commissioner Norris?

23 COMMISSIONER NORRIS: Thank you.

24 Welcome panelists and thanks for being here.

25 I am pleased that we are doing this in what is the

1 second of a series of technical conferences on
2 reliability issues that was launched with the
3 Technical Conference of July 6th. We will probably
4 get into that one more at a 30,000-foot level
5 conference, but at the same time we announced we were
6 going to have that one as well because this clearly
7 identified as an area of interest and concern for
8 making sure we have a reliable system.

9 I think one consistent theme on this issue
10 is that compliance and enforcement is about achieving
11 better liability, not an end in and of itself. I am
12 curious today to get a better understanding of how the
13 role of compliance and enforcement is helping us
14 achieve a more reliable system, which is the ultimate
15 goal here. Thanks for what you are going to add to
16 that discussion.

17 COMMISSIONER LA FLEUR: Thank you,
18 Commissioner Norris.

19 PANEL I: Reliability Standards COMPLIANCE AND
20 ITS MONITORING BY Regional Entities AND NERC

21 COMMISSIONER LA FLEUR: I will now introduce
22 the first panel. I feel like a little bit like Alex
23 Trebek. The topic will be "Reliability Standards
24 Compliance and its monitoring by Regional Entities and
25 NERC."

1 We have Tom Galloway, senior vice president
2 and chief reliability officer for NERC; Daniel Skaar,
3 the president of the Midwest Reliability Organization;
4 Steve Goodwill, general counsel of the Western
5 Electricity Coordinating Council; Doug Curry, general
6 counsel of Lincoln Electric System; and Chris Hajovsky
7 from RRI Energy, Inc., who is director regulatory
8 affairs and NERC Reliability Standards.

9 Mr. Galloway?

10 MR. GALLOWAY: Good afternoon, Chairman
11 Wellinghoff, commissioners, commission staff, and
12 other panelists. My name is Tom Wellinghoff and I am
13 the chief reliability officer for the North American
14 Electric Reliability Corporation.

15 Prior to joining NERC, I was the vice
16 president and director of compliance for the SERC
17 Regional Entity. Prior to joining SERC I held various
18 positions at the Institute of Nuclear Power
19 Operations. I appreciate the opportunity to provide
20 these comments today. Mine are sequenced for the
21 panel per one agenda topic.

22 First, the status of compliance, in my view
23 we are just now ending the ERO startup phase. The
24 terrain has been very challenging, but the
25 achievements are significant. NERC and the eight

1 regions are performing effectively in vastly different
2 roles from those under the premandatory and
3 enforceable period.

4 More than 1,900 entities have been
5 registered, representing a broad spectrum of entity
6 sizes, functions, and sectors. NERC and the regions
7 are working to further standardize and refine
8 processes and automate compliance information
9 management.

10 Regions are executing large numbers of
11 compliance audits per required schedules. In sum,
12 greater than 100 Reliability Standards containing over
13 1,000 separate mandatory and enforceable compliance
14 requirements are now being effectively monitored.

15 Of the compliance trends, the one I consider
16 most significant is the continued high levels of
17 industry self-reporting, something I consider to be a
18 significant, positive cultural indicator.

19 Next, compliance and consistency:
20 consistency is a key focus area with the primary goals
21 of equitable entity treatment and improved
22 predictability. Consistency improvements have been
23 made in processes, execution, and in compliance
24 decisions.

25 Some in-process improvement actions to keep

1 furthering performance in those areas include: cross-
2 regional working groups on topics like audits,
3 enforcement, registration that are used to identify
4 and correct inconsistencies, share best practices, and
5 coordinate related activities.

6 Designation of lead regions to coordinate
7 compliance activities for entities that operate in
8 multiple regions; process improvements, including
9 rules of procedural changes; compliance application
10 notices that are used to promote consistent field
11 decisions; compliance analysis reports that examine
12 the causes that frequently violated standards and
13 serve as a training tool for entity, NERC, and
14 regional staff.

15 NERC observation of regional audits and key
16 reliability spot checks are used to validate regional
17 approaches and findings and provide timely feedback.
18 Recently, a case notes process was created to
19 communicate preliminary sanitized information for
20 important in-process compliance determinations.

21 Some noted improvement opportunities exist
22 such as added consistency in a type and level of
23 evidence needed to demonstrate compliance and the
24 predictability and proportionality of compliance
25 actions following events.

1 While there is clearly room to improve, the
2 ERO has made significant progress and I believe
3 improvements are accelerating given the recent
4 emphasis towards acting as one ERO-wide enterprise.

5 Next, event analysis and compliance: the ERO
6 places very high value on the timely and comprehensive
7 sharing of lessons learned as a significant
8 reliability improvement driver.

9 The revised process now under Field TROC
10 categorizes events by significance, detailed the
11 associated level of cause analysis, and sets
12 responsibilities and timing for various actions,
13 including generational lessons learned. But events
14 analysis and compliance are not an either/or
15 proposition.

16 The process also sets expectations for
17 entity self-evaluation of the compliance implications
18 related to the event which are then subject to
19 validation by Regional Entities and NERC. As before,
20 Regional Entities and NERC can and will perform
21 compliance investigations for selected events based on
22 specific facts and circumstances.

23 Lastly, how can the Commission, NERC, and
24 regional staffs help to create a culture of
25 compliance? To promote a culture of compliance

1 culture, we must be clear on the desired behaviors and
2 aggressively reinforce them.

3 To me the most important reliability -- the
4 most important entity behaviors are CEO-level
5 engagement to demonstrate compliances, an essential
6 business element, performance by the entity of
7 systematic critical self-evaluations, timely and
8 candid self-reporting of findings, extent of condition
9 reviews that are used to ensure the full scope of any
10 violations are fully identified, and thorough
11 comprehensive corrective actions for identified gaps.

12 In terms of reinforcement, it takes two
13 basic forms. First, citing of positive examples, role
14 models, if you will, something that has not been done
15 very visibly and frequently to date.

16 Second, greater increasing differentiation
17 based on observed behavior, significant enforcement,
18 moderation when desired behaviors are observed,
19 significant escalation for undesired behaviors.

20 I will conclude by saying that a healthy
21 compliance culture is an essential element, but in my
22 view not the only element of a strong reliability
23 culture. That concludes my remarks. Are there any
24 questions?

25 COMMISSIONER LA FLEUR: Thank you very much.

1 Mr. Skaar?

2 MR. SKAAR: Good afternoon, Mr. Chairman and
3 commissioners. My name is Dan Skaar, and I am
4 president of the Midwest Reliability Organization.
5 Thank you for the opportunity to participate in
6 today's panel. I will direct my comments to the last
7 question for this panel, which is: How can the
8 Commission, NERC, and the Regional Entities help
9 create a culture of compliance?

10 As the Commission has long recognized
11 effective compliance programs marked by strong
12 procedures, engaged leadership, and internal oversight
13 provide a high level of assurance that Registered
14 Entities are doing what they can to proactively
15 address risk to reliability and prevent violations.

16 There are two areas where we can help
17 improve compliance by these entities. First, we can
18 devise ways to reward strong, effective compliance
19 programs. In this regard, the most obvious way, as
20 the Commission has pointed out, is to reduce or
21 eliminate fines for self-reported violations.

22 But not all self-reported violations are the
23 same. Self-reports resulting from a strong compliance
24 program that systematically detect, report, correct,
25 and prevent violations and risk to reliability should

1 receive extra credit.

2 Creating an environment that welcomes
3 self-reports as a means of identifying and correcting
4 problems to improve reliability is essential to our
5 success. Also, we should look at ways to
6 prospectively reward those with strong compliance
7 programs.

8 This in turn would require us to evaluate
9 the strength of Registered Entities' compliance
10 programs, and then we could tailor our oversight of
11 these entities which have invested in strong
12 compliance programs by using a more rifled approach.

13 Everything would be subject to audit, but
14 we may not choose to test everything every year. We
15 would examine those activities which pose a higher
16 risk to reliability and then randomly select other
17 items.

18 For example, in Year 1 we could audit
19 one-third of the standards and then selectively test
20 the other, and the same approach in the next two
21 years, something like that. Either way we could focus
22 on our primary goal of reliability while keeping our
23 Regional Entities sharp and accountable and balance
24 the work.

25 I believe this approach would send the right

1 message about the importance of compliance and help
2 those who may be trying to establish stronger
3 compliance programs in their own companies.

4 The second major area where we can encourage
5 a strong compliance culture involves improving our own
6 compliance procedures. To start with, we should find
7 ways to reduce the amount of paperwork because it
8 sends the wrong message that compliance is all about
9 paperwork. I mean, I think everybody in this room has
10 probably heard that several times.

11 Just because we can review and enforce
12 everything over a multiyear period during an audit
13 does not mean that we should in every case. For
14 example, a possible violation on an immaterial matter
15 from three years ago, which was corrected two years
16 ago, likely does not pose a risk today.

17 Currently, however, we would consider a
18 violation and process it for a potential remedy, more
19 added paperwork. Instead, we should simply score and
20 record the violation and move on.

21 Of course, we cannot ignore these matters
22 because we need a complete compliance record and
23 history. We need to maintain accountability to help
24 prevent the entity from reverting back to a deficient
25 program.

1 However, treating such matters in a formal
2 enforcement proceeding may discourage a registered
3 entity as such treatment may not provide adequate
4 credit. Therefore, from my perspective, it would be
5 more effective and efficient to treat an immaterial
6 matter through some other means.

7 Finally, to promote a culture of compliance
8 we should standardize the procedures around the three
9 elements of our compliance work. In everything we do,
10 we have to plan it, conduct it, and report it.

11 Unfortunately, today we measure consistency
12 based on outcomes rather than ensuring a uniform
13 approach to compliance monitoring on the front end. I
14 believe we have gained enough experience over the last
15 three years and the time is ripe for greater
16 standardization around these three elements.

17 In closing, I would like to invoke the 80/20
18 rule, focusing on the 20 percent that will get us 80
19 percent of the needed results and then sampling the
20 remaining 80 percent which will keep the industry
21 accountable and sharp on compliance.

22 In fact, I would be pleased to volunteer to
23 test such approach as a pilot program in the spirit
24 that one year of experience is worth a thousand
25 theories.

1 We appreciate the Commission's support and
2 look forward to working with your staff to achieve a
3 fair and balanced way to improve reliability of the
4 Bulk-Power System.

5 Thank you.

6 COMMISSIONER LA FLEUR: Thank you very much,
7 Mr. Skaar.

8 Mr. Goodwill?

9 MR. GOODWILL: Commissioner La Fleur,
10 Chairman Wellinghoff, commissioners, and staff, thank
11 you very much for this opportunity to provide comments
12 this afternoon on behalf of the Western Electricity
13 Coordinating Council.

14 Over the course of the past three years, all
15 of us -- FERC, NERC, the Regional Entities, and
16 industry -- have made progress have learned a great
17 deal about monitoring and enforcing the mandatory
18 Reliability Standards. It is crucial that we learn
19 from our experiences and apply those lessons going
20 forward.

21 Based on WECC's experience, we believe the
22 greatest benefit going forward can be gained from a
23 thoughtful reprioritization of what we do and how we
24 do it. to most efficiently maintain and enhance
25 reliability of the Bulk-Electric System.

1 WECC suggests renewed emphasis on the
2 following areas. First, we must shift resources to
3 areas of greatest risk to the BES. We must focus on
4 the violations that actually pose the greatest threat
5 to reliability, and in doing so we must be willing to
6 acknowledge when it comes to reliability not all
7 standards are created equal.

8 Current monitoring efforts seem focused on
9 the most frequently violated standards, but we
10 propose a joint conversation with FERC, NERC, the
11 regions and industry to instead identify the most
12 critical standards.

13 To do this we must talk to the control
14 centers, reliability coordinators, regional auditors,
15 transmission operators, and trainers to find out what
16 they think of the standards that matter most to system
17 reliability.

18 We must also talk with the regional
19 compliance staffs. They analyze the violations and
20 prepare reliability impact assessments on a daily
21 basis. They have learned a lot about which violations
22 of which standards pose the most serious threat to
23 reliability. And of course we must talk with
24 industry. The front-line operators deal with
25 reliability issues every day and have a great insight

1 and experience regarding reliable operation for the
2 BES.

3 From these discussions, we can identify
4 high-priority standards and then focus more resources
5 on their monitoring and enforcement. This
6 reprioritization must include the critical
7 infrastructure protection, or "CIP," standards.

8 Regional Entities are seeing a steep
9 increase in CIP violations very similar to the large
10 number of violations identified when the Reliability
11 Standards approved in Order 693 became effective.

12 Current processes do not appear capable of
13 handling this quantity of violations in a reasonable
14 and timely manner. However, just as with the Order
15 693 standards, we must prioritize our actions based on
16 the recognition that not all CIP violations are of
17 equal importance to the reliability of the
18 Bulk-Electric System.

19 Rather than allowing this wave of CIP
20 violations to overwhelm us, we believe FERC, NERC, the
21 regions, and private industry can reach consensus on
22 which of the new CIP standards are absolutely critical
23 to cybersecurity and which while important do not
24 present the same risk if violated.

25 NERC and the regions are developing

1 significant initiatives to streamline processes. We
2 are working with NERC and the other regions to devise
3 and test new processes, and we encourage FERC to be
4 open to some real experimentation.

5 For example, WECC proposes testing truly
6 abbreviated processes which, for instance, would
7 involve very low-risk, low-impact violations. For
8 these violations, enforcement could take the form of
9 nothing more than regional tracking of mitigation
10 efforts and repeat violations.

11 NERC could monitor the regions for
12 consistency and file brief quarterly reports. FERC
13 could sample these violations, select a subset,
14 request the underling documentation from the region,
15 and ensure that regional efforts are in line with
16 expectations.

17 Finally, in line with these efforts to
18 reprioritize and identify efficiencies, WECC strongly
19 supports current efforts to make standards development
20 and provisions processes more efficient.

21 In order to ensure that these drafting
22 efforts produce clear, concise, and enforceable
23 standards, WECC encourages the inclusion of
24 professional facilitators and expert witnesses on
25 standards drafting teams.

1 We must also continue to incorporate lessons
2 learned from the auditors in the field into standards
3 revisions. WECC is encouraged by and proud of the
4 progress that has been made in the compliance
5 monitoring and enforcement process and looks forward
6 to working with FERC, NERC, the other regions, and
7 industry to further improve these processes.

8 We encourage FERC to work with us in
9 identifying and prioritizing those activities that
10 will produce the most reliability benefit for the BES
11 while recognizing the regions competence and primary
12 responsibility in compliance monitoring and
13 enforcement.

14 It is important that the regions have the
15 freedom to act and to analyze in the first instance on
16 the basis of their delegated authority and recognize
17 technical expertise. NERC and the regions have made
18 great strides in building an ERO enterprise that
19 recognizes and leverages the strengths that each of us
20 brings to this effort.

21 We look forward to building upon this
22 success by forging a more inclusive and collaborative
23 relationship with FERC and by focusing all of our
24 efforts and resources on those activities that matter
25 most to reliability. WECC believes our discussions

1 here today represent a significant step forward in
2 this effort.

3 COMMISSIONER LA FLEUR: Thank you very much,
4 Mr. Goodwill.

5 Mr. Curry?

6 MR. CURRY: Thank you.

7 I am general counsel for the Lincoln,
8 Nebraska, Electric System and also a member of
9 Mr. Skaar's MRO Board, but today I speak only for LES
10 and also for the Transmission Access Policy Study
11 Group, which is an informal association of
12 transmission-dependent utilities in more than 30
13 states.

14 LES is a municipal electric system serving
15 about 130,000 customers in and around Lincoln,
16 Nebraska, with a peak load of a little over 760
17 megawatts. We own transmission in and around Lincoln,
18 and we own transmission as part of the joint project
19 involving multiple utilities.

20 I served as an interim CEO for LES for over
21 a year ending in June of just this year. I can assure
22 you as a result of that experience that LES takes
23 compliance and is fully committed to reliability as we
24 operate our system, and we strive to maintain a
25 culture of compliance, and we strive even more to

1 achieve the culture of reliability excellence.

2 Our compliance committee meets monthly. We
3 include our chief operating officer, operating
4 division members of our executive staff, senior
5 managers that are involved in the affected areas. All
6 of us, all of those people, have direct access to our
7 CEO.

8 The meetings are an exchange of ideas and
9 lessons learned from our own experiences as well as
10 borrowing from what we can learn from other utilities
11 that are operating in our area.

12 MR. CURRY: (No microphone) However, we
13 have concerns about compliance audits. Small entities
14 with limited potential impact on reliability receive a
15 great deal of scrutiny for potentially even more since
16 there is less to look at. Much larger entities that
17 have far greater impact on LES.

18 MR. SKAAR: The LES 2008 onsite audit, for
19 example, took four days, which we understand to be
20 comparable to the time spent auditing the much larger
21 systems that have more facilities that have a greater
22 impact on BPS reliability. NERC Sanction Guidelines
23 rightly recognize that size matters.

24 A small entity with limited BPS facilities
25 poses less risk to the BPS than a large entity that

1 incurs the same violation. This risk-related
2 assessment of seriousness should be reflected in the
3 auditing priorities. Reliability would be enhanced by
4 a risk-informed approach to development of auditing
5 programs, which NERC CEO Cauley included in his
6 February 15th vision statement.

7 Undue emphasis on auditing of entities that
8 have little or no potential impact on reliability is
9 in part due to the all-or-nothing approach to
10 registration and the push in some regions to register
11 entities that have little or no impact on BPS
12 reliability.

13 For example, the City of Piggott, Arkansas,
14 serves its 12-megawatt load through a distribution
15 system connected at 69 kilovolt, with a 69 KV,
16 transmission system. Piggott is registered as a LSE
17 and DP only because it is part of the regional UFLS
18 Program.

19 Piggott has no objections to being part of
20 that regional program and complying with the NERC UFLS
21 standards. However, it does question the benefits to
22 the BPS reliability of burdening its very small
23 system, which has only 12 employees working in the
24 electric side with compliance with all DP and LSE
25 standards, including the new requirements with regard

1 to CIP when both FERC and NERC have decided correctly
2 already that entities like this one generally cannot
3 impact BPS reliability. There simply should be a way
4 to limit Piggott's compliance obligations to those
5 standards that are specifically related UFLS.

6 The auditing process should encourage not
7 penalize efforts to go beyond the minimum required for
8 compliance. LES had an experience that was just the
9 opposite. LES created a transmission vegetation
10 management program that complied with NERC's standards
11 The program required annual patrols which could be
12 either accomplished by foot or utility vehicle.

13 Annual inspections were determined to be
14 adequate based on our anticipated vegetation growth.
15 However, the plan went further stating that in
16 addition LES had a contract for aerial patrols at 345
17 KV lines 6 times a year.

18 The auditors concluded that our ground
19 control fully satisfied compliance requirements, but
20 at the same time LES was found in violation and
21 incurred and paid penalties because the aerial
22 contractor had flown the lines only one time during
23 the first five months of that year. The contract
24 required six times per year.

25 To avoid the unwarranted future fines that

1 come from having to comply with standards or practices
2 that exceed the standards, we removed that additional
3 pro-reliability action from our plan. There is just
4 simply something wrong with that picture.

5 Overemphasis on documentation and overly
6 prescriptive views of what it must look like tilts
7 expenditures toward documentation that could be better
8 spent on improving reliability.

9 One entity was almost found noncompliant
10 with the CIP-02 standard for providing its lists of
11 critical facilities in a written paragraph stating
12 that it had no critical assets rather than in the form
13 of an Excel

14 spreadsheet. The entity pushed back, and
15 the auditors eventually accepted the documentation,
16 but it never should have been an issue in the first
17 place.

18 The auditing process would be improved by
19 making standards clearer. For example, does "annual"
20 mean every 12 months or once each calendar year? Is
21 "directive" limited to instructions from an RC, or
22 does it include everyday switching orders and
23 generation dispatch instructions?

24 Unless the ambiguity is addressed through
25 the full interpretation process, an auditor should not

1 find a registered entity in violation when its actions

1 fall within the range of reasonable interpretation of
2 a given standard.

3 I agree with the importance of achieving a
4 culture of reliability excellence such as NERC is
5 seeking to promote. As our vegetation management
6 experience shows, the compliance and the auditing
7 process should be revamped to avoid undermining that
8 culture of excellence.

9 I thank you for the opportunity to address
10 you this afternoon and look forward to our discussion.

11 COMMISSIONER LA FLEUR: Thank you very much,
12 Mr. Curry.

13 Lastly, Mr. Hajovsky.

14 MR. HAJOVSKY: Thank you and thank you to
15 the Commission for the opportunity to get to speak in
16 front of this -- on this topic with this distinguished
17 panel.

18 My name is Chris Hajovsky, and I am with RRI
19 Energy. We currently own and operate generation in
20 four of the NERC Regions. We have operated generation
21 in the Fifth Region, and upon our completion of merger
22 with Mirant, hopefully forthcoming, we will get the
23 opportunity to be in the Sixth Region and participate.

24 Today, I would like to focus my prepared
25 remarks to three areas: consistency, documentation

1 monitoring of compliance, and a culture of
2 reliability. First, to discuss consistency,
3 consistency is an issue that presents great challenges
4 for NERC, Regional Entities, and Registered Entities.

5 Indeed, every page produced by a Regional
6 Entity and reviewed -- I'm sorry, produced by a
7 registered entity and reviewed by a Regional Entity
8 contains a potential consistency issue. As a result,
9 the practice as implemented by each of the eight
10 Regional Entities to expedite the audit process have
11 implications on consistency.

12 As an example, during a recent audit in this
13 year one Regional Entity demanded documents from early
14 2003, prior to when the legal duty to retain records
15 existed and before the 2003 blackout had occurred.

16 However in 2008 another Regional Entity
17 adopted a different approach to auditing the standard
18 using June 18th, 2007, as the documentation starting
19 point thereby avoiding a potential concern over any ex
20 post facto regulations or derivative issues that could
21 come up.

22 It is worth noting that the Regional Entity
23 that requested such records during the 2010 audit did
24 not make such a request in auditing an affiliate in
25 2009. That is not to make any negative comment about

1 a particular region.

2 It highlights the issue of consistency as
3 well as, kind of something we will talk about in a
4 little bit, of how regions are actively doing what
5 they think is right and how even in doing that they
6 could be differences of opinions that could lead to
7 inconsistency outcomes.

8 Another example is one Regional Entity might
9 recognize a self-reported violation that has a
10 generalized high violation of risk factors but really
11 an insignificant chance of even impacting the
12 Bulk-Electric System as a deserving relaxed penalty
13 assessment while another Regional Entity might ignore
14 such considerations of impacts and simply seek to
15 impose the maximum deterrents in the enforcement
16 process.

17 In a system that places such an extreme
18 emphasis on dotting the i's and crossing the t's,
19 consistency will always be an unreachable goal as long
20 as the focus is so granularly placed strict compliance
21 with every possible tangent for interpretation for
22 each word of the requirement.

23 Closely related to the topic of consistency
24 is the topic of documenting and monitoring compliance.
25 Compliance costs continue to escalate absent

1 objective, performance-based measures for reliability.
2 For example, as we have heard, the number of
3 Reliability Standard violations continues to grow, but
4 there is no available measure or metric that captures
5 that impact on the reliability of the Bulk-Electric
6 System.

7 At the inception of mandatory Reliability
8 Standards in June 2007, monitoring compliance became a
9 primary focus for NERC and the regions in documenting
10 compliance sufficiently enough to meet Regional Entity
11 reviews, and has become an even greater focus for
12 Registered Entities.

13 Despite a resource commitment by the
14 industry that has grown from the Commission's initial
15 assessment in the 2006 ERO NOPRA of an increase of
16 only 100 hours per company to the revised average
17 figure of just under 1,000 hours per company in
18 Order 693 to the significantly higher resource
19 commitment three and a half years later experienced by
20 both regional and Registered Entities. The number of
21 violations continues to grow as these entities become
22 more familiar with the standards and their potential
23 interpretations and applications.

24 Co-existent with the associated increase in
25 the documentation volume and demanded granularity,

1 which causes a diversion of resources toward the
2 immediate time-sensitive enforcement activities and
3 away from tasks more directly impacting overall
4 reliability such as training, improved maintenance and
5 testing, and clear and concise results-based standards
6 development.

7 Unfortunately, to date a comprehensive
8 solution to stabilize this continued upward sloping
9 trajectory of administrative violations has not
10 emerged, and what is perceived by many as an
11 overanalysis of each single word in a Reliability
12 Standard versus application of the general spirit and
13 intent of the Reliability Standard toward ensuring
14 reliability.

15 As an example, just it is the continued
16 expectation of most, if not all, entities that if one
17 single test record out of the records for 10,000 tests
18 is missing, the Regional Entity should self-report the
19 issue and endure the long, detailed,
20 resource-intensive enforcement process.

21 In one of our company's two self-reported
22 violations that have made it through to the point of
23 signing a settlement agreement, we spent close to
24 between three-quarters and a full year of a full-time
25 employee's worth of time collecting records for data

1 requests relating to this.

2 The message, and this is no reflection on
3 the region, but "FERC may ask us for this, so we need
4 to ask you the questions for this information."

5 "The Commission may ask us for this."

6 There is this sense of overpreparation for
7 something that may or may not come down the pike for
8 what ultimately resulted in a few thousands of
9 penalty. We spent a large amount of effort to prepare
10 every possible avenue, and that is contributing to the
11 situation we are experiencing today, the backlog.

12 Nevertheless, recognizing the criticality of
13 monitoring compliance, I am encouraged that the recent
14 consideration of the proposed parking ticket approach
15 to certain violations and believe this is an important
16 program to implement as quickly as possible.

17 After more than three years since mandatory
18 enforcement began, a strong case is emerging to find a
19 balance to the enforcement of major issues versus
20 minor issues. However, I also encourage the
21 Commission and NERC to look outside the box for even
22 more of this disposition opportunities that shorten
23 the process, reduce resource burden, and carry
24 reliability at their core rather than merely focusing
25 on strict compliance.

1 Toward this concept, I have heard many
2 references to the nuclear industry approach for
3 minimal infractions, which as I understand it involves
4 kind of a balanced approach to fix it and move on. I
5 am no where skilled in that, but I would encourage us
6 to look at folks who have gone before us in this area
7 and seek out the wisdom that they may have to impart
8 on us as we address difficult situations that we have
9 already heard several times today.

10 The third topic I would like to touch on
11 deals with developing a culture of reliability. One
12 of the most important ways to encourage a culture of
13 reliability across the industry is to have standards
14 that are clear and unambiguous regarding the
15 reliability goal and the expectations of how the
16 registered entity can demonstrate compliance.

17 To that end, first, it is critical to
18 recognize that standards submitted for approval in
19 2006 and approved in 2007 and thereafter are not
20 necessarily perfect. After nearly five years of
21 developing these standards, there are many instances
22 where the industry realizes the adequate level of
23 reliability identified and the reliability goal of a
24 particular Reliability Standard might involve a
25 solution that is different from the approach of the

1 current standard.

2 Different does not necessarily mean inferior
3 or imply de factor reduction to reliability. In many
4 instances, different means that the proposed revised
5 approach better conform with the understanding
6 attained through years of observation and experience.

7 Second, the industry should -- toward the
8 culture of reliability, the industry should be able to
9 request guidance from NERC on whether an action by a
10 Regional Entity may constitute a compliant activity in
11 advance of engaging in such an activity.

12 I understand that issuing guidance such as
13 this must be done carefully and thoughtfully. While
14 providing guidance that must be treated as absolute
15 may not be appropriate, there is nothing wrong with
16 providing guidance as a safe harbor until later
17 revised.

18 The Compliance Application Notice process
19 implemented by the NERC Compliance Group is a good
20 example of a step in the right direction. I encourage
21 in evaluating ways to both accelerate the issuance of
22 these notices as well as the level of detail contained
23 in such notices.

24 In conclusion, cultures of reliability and
25 compliance are best served by helping Registered

1 Entities avoid the the current demand to overdocument
2 compliance, anticipating every possible philosophical
3 and possibly overanalyzed avenue in which a particular
4 word in a standard might be interpreted by an auditor
5 during a compliance monitoring exercise.

6 Objective performance-based measures of
7 reliability applied across the regions consistently in
8 terms of compliance should provide a ready means to
9 that end. NERC and the Regional Entities are to be
10 applauded for so strictly following the Commission's
11 emphasis on monitoring compliance and aggressively
12 documenting enforcement considerations.

13 However, I encourage the Commission to now
14 consider alternative disposition opportunities. I
15 encourage the Commission to review the nuclear
16 industry and other forums that have gone before us. I
17 encourage the Commission to consider systems to permit
18 safe harbor guidance.

19 No one wants to reduce the reliability of
20 the Bulk-Electric System. That is something, a
21 message, that I hear consistently from staff members
22 who leave the Commission and get out into the
23 industry.

24 They realize, wow, people are wanting to do
25 the right thing. It is almost surprising that good

1 people want to see the reliability of the
2 Bulk-Electric System maintained; however, everyone
3 desires the focus to return to actual reliability.

4 Thank you for allowing me the opportunity.
5 I look forward to the discussion.

6 COMMISSIONER LA FLEUR: Thank you very much,
7 Mr. Hajovsky. You have all given us a lot to think
8 about, and I guess we will turn to questions,
9 beginning with Mr. Chairman Wellinghoff.

10 CHAIRMAN WELLINGHOFF: Thank you,
11 Commissioner La Fleur. Mr. Galloway, I was very
12 interested in your bio. You actually spent 10 years
13 with MPO before you came to NERC.

14 I am wondering if you can compare and
15 contrast the MPO compliance culture as you left it in
16 the nuclear industry under MPO with the compliance
17 culture as you find it today in the electric industry
18 under the NERC/FERC regulatory structure. I would ask
19 you to put that in the context of two of your three
20 requirements for compliance, one being the CEO
21 engagement and the other one being timely and candid
22 self-reporting?

23 MR. GALLOWAY: Thank you, Mr. Chairman. The
24 closest analog I would draw, and it matches several of
25 the points I had in the effective compliance culture

1 is in the nuclear industry one of the hallmarks is an
2 effective corrective action program that is instituted
3 at the unit level and is run typically under a site
4 vice president.

5 The basic construct of that is in the face
6 of any ambiguity as to whether or not there is an
7 improvement opportunity, whether it is a regulatory
8 failure, an industrial safety near miss, anything that
9 has to do with reliability and safety of the unit.

10 Employees are encouraged to come forward
11 with that improvement opportunity or potential
12 shortcoming into a formal system for evaluation.
13 Within that system, those issues go through a rigorous
14 set of steps in terms of the prioritization, the
15 assignment of risk, the assignment of cause analysis
16 that is on point with those risks, and then corrective
17 action. That is instituted, again, typically at the
18 unit level.

19 One of the things from a regulatory
20 oversight that is done is that the regulator really
21 looks at the health of that self-managed corrective
22 action programs show some defect where they have
23 repetitive issues, they have an issue that was of
24 particular import that they didn't attend to
25 appropriately, then that begets more regulatory

1 action.

2 Now, there are exceptions to that. There
3 are some things which are directly reported to the NRC
4 in a formal process outside of the unit-level
5 corrective action program, but a large number of the
6 day-to-day issues that happened in the nuclear unit
7 are handled through that internal process.

8 CHAIRMAN WELLINGHOFF: Would you
9 characterize that process as what you would see to be
10 a superior process to the one that we do with the
11 NERC, FERC, or --

12 MR. GALLOWAY: Well, I think it is. To give
13 you a short answer, I would say yes.

14 CHAIRMAN WELLINGHOFF: If it is a better
15 structure, do you see any way we can start moving to
16 that type of structure?

17 MR. GALLOWAY: Well, I think one of my
18 opening comments was I think a positive cultural sign
19 right now is that of all the violations we have in the
20 system the largest fraction comes from self-reporting,
21 which I think is a positive. I would not want to see
22 us move in a direction where we discourage that.

23 What we really need to do is kind of
24 incentivize the entities to keep coming forward with
25 those things, and then really on a more macrobasis

1 look at how the entities are identifying them and
2 dealing with those from a process and organizational
3 standpoint rather than each individual issue.

4 Kind of managing and helping to grow the
5 health of their internal compliance program that would
6 kind of identify those issues. We are trying to do
7 that, incentivize that on a case basis, but as some of
8 the other panels have mentioned sometimes it is a
9 pretty arduous path.

10 We have examples on either end of the
11 spectrum in my experience where we have had entities
12 that come forward and done a very good job in terms of
13 an extended condition, and we have given them
14 significant credit in settlement space.

15 Whereas, in other cases we have really had
16 to engage at the regional level to kind of drive out
17 the full extent of condition, which turned out to be a
18 lot broader and maybe the entry put on that was what
19 would seem to be a documentation in the first instance
20 turned out to be an actual operational issue when we
21 dug into it.

22 To close in response, I think we need to
23 shift that much more focus on the entities' internal
24 compliance programs and continue seeing the continued
25 evolution of those rather than each individual

1 instance.

2 CHAIRMAN WELLINGHOFF: How about in the area
3 of CEO engagement, do you see more or less of that
4 with respect to NERC regulatory compliance of the
5 Bulk-Electric System than you saw with respect to
6 nuclear safety in the MPO model?

7 MR. GALLOWAY: Well, I would have to say I
8 see a fair amount of CEO engagement. I mean,
9 certainly any CEO in this industry right now is well
10 aware of compliance and the implications. It is
11 really kind of getting to a common vision of what good
12 looks like, I think, and there is a spectrum on that
13 right now. A lot of it around unintended
14 consequences. Folks at a high level in the
15 organization say, "Hey, we will have no violations,
16 right, at our facilities." That can be construed as
17 "Well, we shouldn't be self-reporting any potential
18 violation, which is exactly the opposite of the
19 behavior I think we want to incentivize.

20 CHAIRMAN WELLINGHOFF: Yes. That could have
21 the opposite -- drive the opposite effect.

22 Let me turn to some of the other panelists
23 for my last series here. Mr. Skaar and Mr. Goodwill I
24 think related to some of your testimony, Mr. Skaar
25 under the 80/20 rule and Mr. Goodwill talking about

1 identifying the most critical standards to focus on.
2 How do we best get there, I guess? How do we best get
3 to either focusing on the things that are most
4 important and trying to minimize the time and effort
5 that we are applying to things that are not as
6 critical to the whole system? What are your
7 recommendations about how we get there?

8 Mr. Hajovsky, I think you touched on this as
9 well. You might want to begin.

10 MR. SKAAR: Well, I can go ahead, I guess.
11 Thank you.

12 You know, I think if you got half of the
13 folks from the industry in a room, we could probably
14 figure out what the 20 percent is, I think. I mean,
15 it is relay misoperations, for example. It is tree
16 contacts. It is training. I mean, we might argue
17 over the bottom two or three, but we could get
18 consensus, I think, quickly.

19 I think we know based upon not only the past
20 disturbances, but also I think what we see forward as
21 well as far as resources and things like that, I mean,
22 I think we could come up with the 80/20. I think when
23 we look, at least this is how I think about risk in my
24 work, there is the inherent risk of the registered
25 entity, which is more touch points on the BES, more

1 inherent risk.

2 Then, there is control risk or compliance
3 risk, which would mean their compliance program
4 potentially won't detect a problem. Weak compliance,
5 more risk. And then there is audit risk, which is the
6 risk that I may not find something that I potentially
7 should have found.

8 To the extent that I think our work is
9 focused on the administrative nature type things, I
10 think our risk may go up. One of the things I have
11 kind of looked at and studied is the SoCs learning
12 curve recognized this, and then in 2007 they
13 established -- this is probably too technical folks --
14 AS5, which effective allowed for more risk and
15 materiality-based approaches because they were facing,
16 I think, the same problem when that came out and then
17 four years later they looked at different ways of
18 looking at that. I am not saying that SoCs is a
19 one-for-one, but I think we can compare notes.

20 Thank you.

21 CHAIRMAN WELLINGHOFF: Anybody else?

22 MR. GOODWILL: Mr. Chairman, I would just
23 add to that WECC began this effort, an effort to
24 identify the Reliability Standards posing the greatest
25 risk this past summer by looking back at data from

1 July of '09 to June of 2010.

2 We identified the most violated standards
3 within the Western Interconnection, but then we had
4 the conversation that I discussed in my remarks with
5 our own staff, our experts, and our Reliability
6 Coordinator Centers, as well as our subject matter
7 experts in our compliance department and found that
8 there was very little overlap between what they felt
9 were the most critical standards for the maintenance
10 of reliability and the standards that were violated
11 most often.

12 Now, as Mr. Skaar indicated, we would need
13 to expand that conversation outside of WECC staff to
14 other regions, industry, NERC, and FERC, but I
15 believe we would fairly quickly get to some consensus
16 on what those most critical standards are.

17 The problem I believe comes in
18 operationalizing that information. While we are now
19 aware at least within WECC for the Western
20 interconnection, what we believe are most critical to
21 the BES, we do have annual implementation plans that
22 guide us in what we must audit, what standards must be
23 self-certified to, and so forth.

24 It is difficult to take that information and
25 to translate it into a more meaningful compliance

1 monitoring and enforcement program at this time.

2 CHAIRMAN WELLINGHOFF: Anybody else?

3 (No verbal response.)

4 CHAIRMAN WELLINGHOFF: Thank you.

5 Commissioner La Fleur?

6 COMMISSIONER LA FLEUR: Thank you very much
7 Mr. Chairman.

8 Commissioner Moeller?

9 COMMISSIONER MOELLER: Thank you.

10 A comment and two questions: The first was
11 I am just going to make sure to emphasize to people
12 that today panelists and anyone from the audience, I
13 presume we are taking comments, people shouldn't hold
14 back. They should let us know, and I think based on
15 our first panel that is exactly what is going to
16 happen. We want the unvarnished perspective of
17 people.

18 Mr. Galloway, you mentioned the "case notes"
19 process. Maybe you can elaborate a little bit more on
20 that. I am so glad you put that together, because
21 when we were in the height of the backlog I heard a
22 lot of frustration from people saying it was a black
23 hole.

24 We didn't know what the leading violations
25 were, and you can't learn from anybody else. It

1 sounds like this is the effort to address that. I
2 would like you to explain it a little bit more and
3 then get any of the other panelists' reactions as to
4 if it is going well and if it can be improved.

5 MR. GALLOWAY: Well, thank you for the
6 question. The case notes approach is brand new. The
7 intent there is to kind of recognize the fact that we
8 are not currently at a throughput level that we want
9 in terms of the individual violations.

10 We do feel that to be a learning
11 organization, if you look broadly ERO-wide, having
12 more timely feedback to the industry in terms of
13 issues and violations, potential violations that
14 others have incurred, and what they have done to
15 address those is a great source of information to put
16 back out into the industry so it is actionable and
17 folks can kind of in a more proactive fashion learn
18 from others.

19 The balance point there was we were looking
20 to protect the identity of the individual entity so as
21 to not compromise their due process rights. We will
22 sanitize that information and put it in a form where
23 it can't be tied to any particular entity but put it
24 out in enough granularity so that others in the
25 industry that might be subject to the same issue can

1 learn from that.

2 COMMISSIONER MOELLER: For the panelists,
3 have you found that helpful so far in your various
4 roles or not?

5 MR. SKAAR: Well, I was actually pleasantly
6 surprised that Registered Entities actually found it
7 more helpful than I thought it was going to be to
8 them. We are in the process of doing it. We think it
9 will be a good thing.

10 MR. CURRY: I agree. I mean, if you don't
11 share what you have learned from others' experiences
12 and get it out as soon as you possibly can, you
13 increase tremendously the risk of that event occurring
14 again; so, it can only help.

15 COMMISSIONER MOELLER: Conceptually, I would
16 completely agree with you. But have you used them?
17 Do you recall having seen one, or is it too new to
18 have seen some cases notes saying, "Okay, that could
19 apply to us, and we will make a corrective action with
20 that situation"?

21 MR. CURRY: It is exactly the
22 kind of information that our compliance committee
23 reviews on a monthly basis.

24 COMMISSIONER MOELLER: Great. All right.
25 Progress. Thanks for doing that. I think that will
help a lot.

1 The last question, specifically for Mr.
2 Curry, is you mentioned your involvement with I guess
3 the four-day audit from the North American
4 Transmission Forum. I think that is the former TOOF,
5 the "Transmission Owners and Operators Forum," it is
6 the closest thing we have to kind of an MPO model. If
7 you care to elaborate on how that went, we might find
8 that interesting.

9 But I am also kind of interested, if you are
10 free to talk about it, since you have an excellent
11 culture of compliance, what did they find that you can
12 continue to improve? Can you elaborate on that at
13 all?

14 MR. CURRY: Certainly. It was intensive
15 actual review. I think we had 24 people, industry
16 experts, from around the country in Lincoln, Nebraska,
17 looking at a relatively small system.

18 They went through everything from our
19 control room practices to our training to our
20 vegetation management, and concluded afterwards with
21 an exit interview, which in this particular instance
22 had not only senior management present, but we also
23 had board representation in the room at the exit
24 interview.

25 The remarks that we got were really very

1 high. There were a number of people who said, "We are
2 taking back lessons from Lincoln, Nebraska. They do
3 some things that we can incorporate."

4 On the other hand, they encouraged us to
5 formalize and spend some money in our training effort,
6 which we are going to do and are in the process of
7 upgrading. They talked to us about vegetation
8 management. Again, there was a difference of
9 interpretation that our staff had with regard to what
10 was required.

11 We were told from the peer review we were
12 less tolerant -- or we were more tolerant, I guess, of
13 that kind of growth that doesn't have any risk of
14 getting high up into the transmission lines. We have
15 changed our practices. to a certain degree with
16 regard to that.

17 All in all it was a really positive
18 experience. Our staff was sufficiently encouraged that
19 we have now got volunteers from Lincoln who have
20 already scheduled their peer reviews that they are
21 going to be doing over the course of the next year.

22 COMMISSIONER MOELLER: Well, very good.
23 Thank you. I think we have heard great things so far
24 about the progress of the forum, and we would at least
25 personally do everything that we can to encourage its

1 success.

2 Thank you.

3 COMMISSIONER LA FLEUR: Thank you.

4 Commissioner Spitzer?

5 COMMISSIONER SPITZER: Thank you.

6 This issue of the consistency of the audits
7 is interesting to me, and Mr. Hajovsky gave two
8 discrete examples. I alluded in my opening remarks to
9 this tension certainly in vegetation management. The
10 topography of the West is going to be different and
11 management techniques would reasonably be expected to
12 be different. The one particular example
13 with the temporal document retention appeared to have
14 no -- it was an inconsistency without a corresponding
15 symmetrical benefit. That is the kind of
16 inconsistency that we might want to eliminate.

17 I didn't hear specific examples from the
18 rest of you, and I was wondering if I could elicit
19 maybe one example from each of you of an inconsistency
20 that you have seen that might have the symmetrical
21 benefit such as the vegetation management among the
22 regions, and then one such as the documentation
23 retention '03 versus '08, was it, or '07 where it
24 would seem to be an inconsistency in the audit that
25 ought to be resolved?

1 By way of background, I was a tax lawyer in
2 my prior life. I had a professor of law at the
3 University of Michigan who wrote the "IRS Audit
4 Manual," and that is the bible. I handled thousands
5 of these types of audits from the taxpayers' point of
6 view.

7 In a candid discussion once over cocktails,
8 he admitted that the manual was designed to create an
9 appearance of consistency across the United States
10 from the thousands of Registered Entities.

11 Recognizing that the actually of such could
12 consistency was impossible given the subjective nature
13 of the Code, now of course are dealing with a whole
14 different realm and I would like to think there is a
15 bit more science to the Reliability Standards and the
16 electrical engineering inherent therein and the Code,
17 but at the same time there will be occasional
18 differences in interpretation.

19 Mr. Curry alluded to one that maybe you
20 could make good arguments on both sides. I do want to
21 drill down on the issue of consistency and maybe
22 solicit some more similar anecdotes that Mr. Hajovsky
23 portrayed.

24 MR. GALLOWAY: If I may, there are actually
25 two different examples referenced, and both of them

1 are familiar to me. One was what does the term
2 "annual" mean? Just processwise what we tried to do
3 is across each of the regions we would have a working
4 group composed of audit managers that would meet on a
5 periodic basis, normally every two weeks.

6 They would accumulate items like that, like,
7 what is the definition of "annual," if there is any
8 ambiguity around that. That group would discuss the
9 range of possible applications that would be
10 reasonable and would work towards what would seem to
11 be a consensus decision in parallel with submitting a
12 SAR to help refine the standards that were involved.

13 COMMISSIONER SPITZER: Do you end up with
14 calendar year or 12 months?

15 MR. GALLOWAY: There is actually a range of
16 possible --

17 (General laughter.)

18 COMMISSIONER SPITZER: Kind of making a
19 point, I guess.

20 MR. GALLOWAY: The flip side of that is we
21 also experience examples that that collective set of
22 folks wouldn't feel was a valid definition of annual
23 and it would drive towards these would be credible and
24 these would not.

25 The other example that was given when we

1 talk about reaching back into the pre-June 18th of '07
2 date, that was around how do you validate the
3 maintenance interval for selected devices.

4 The point in time that you are doing the
5 audit, if you are supposed to be executing maybe on a
6 five-year interval, you need to look back "X" number
7 of years to validate that. There were differences in
8 approach on that region to region, so that would be
9 another such item that would get put on the list and
10 that group would try to drive to a consensus approach
11 on it

12 COMMISSIONER SPITZER: Is that resolved?
13 One would think that that would be a documentation
14 issue that would be without debate in order to
15 establish -- you have to look back to establish --

16 MR. GALLOWAY: I believe that is the final
17 position that was landed on is that if the item of
18 interest was the interval, and that is called out
19 within the standard that you have to look at Point A
20 to Point B in terms of time to establish that.

21 Those are the type of things that each and
22 every audit that is executed, it is like the level of
23 detail question that the folks in the field are trying
24 to work through, and processwise are trying to capture
25 those and get consensus going, get something into the

1 system to improve the standard on that front but have
2 something that you could work operationally in the
3 meantime.

4 COMMISSIONER SPITZER: Mr. Skaar, any
5 inconsistencies that might be explainable and
6 debatable among your colleagues?

7 MR. SKAAR: Sure. Well, I was going to
8 answer the question, which may not be popular with the
9 Registered Entities, but I just wanted to make it
10 clear that not all Registered Entities comply with the
11 requirements the same way, so we have to keep that in
12 mind. There is some judgment and discretion in that.
13 It depends on size, how they are organized, things
14 like that. The regions need to have a little bit of
15 flexibility for judgment and discretion on that
16 matter.

17 But the consistency issue I think is real.
18 I mean, I agree with the Registered Entities. I have
19 talked to many of the trade associations inside my
20 region as well as outside region; I agree with them.

21 Where I think we need to go is standardize
22 on approach. In my opening remarks, I commented that
23 everything we do we have to plan it, conduct it, and
24 report it. What I would like to see is standardized
25 practices around that.

1 I understand the "IRS Audit Manual," but
2 there are baseline standardize practices in planning,
3 for example, making sure that you have a sufficient
4 understanding of the registered entity, making sure
5 that you have a sufficient understanding of what the
6 risks are, what the role is, things like that.

7 I think we could come up with a checklist
8 which would really ease the anxiety and create, I
9 think, more predictability for the industry so that
10 they understand how we are going to approach it
11 because I think predictability is a good think. It is
12 good to be boring in our business, I think.

13 Then, I think in the conduct of the work, I
14 mean, we could standardize on an evidentiary review
15 standard, and make sure that we drill down and
16 everybody is really trained on that.

17 Then, in the reports, I think we could make
18 the reporting more meaningful for the registered
19 entity. I think we need to look at that and MRO is --
20 and I am working with Mike Moon to see how we can make
21 the reports more meaningful for the Registered
22 Entities, and for the readers of the report.

23 I look at it as you can standardize on
24 approach. Our scope may not be identical each time,
25 and that is because you can't remove judgment and

1 discretion out of the field.

2 MR. CURRY: Just another comment related, a
3 little expansion that I mentioned in my comments
4 earlier. That has to do with whether we all have a
5 common understanding of what a "directive" is. We had
6 that arise in our first audit. It was an
7 communication issue that I think resulted because we
8 were so small in that our crews meet every day and
9 then they go and they report back and the
10 communication occurs.

11 The common definition of "directive" does
12 not exist. It doesn't include a switching order, for
13 example. It doesn't include a dispatching order. We
14 have made that inquiry so that we could attempt to get
15 an answer to what a "directive" is so that everybody
16 would have the same common understanding, auditors and
17 utilities alike. I understand it is still pending.
18 That question is some place how it works but not in
19 here.

20 COMMISSIONER SPITZER: How difficult is the
21 fix?

22 MR. CURRY: I'm sorry?

23 COMMISSIONER SPITZER: How difficult is the
24 fix for that?

25 MR. CURRY: I think it just takes an order,

1 somebody to determine what it means so that we all
2 understand the same definition of the word.

3 MR. HAJOVSKY: If I may, to the extent that
4 some regions feel as strongly or feel strongly in a
5 different way, that can slow the progress down. So,
6 the importance of having some central decision-making
7 authority say "This is what we are going to do," the
8 safe harbor concept that I mentioned where "For now,
9 this is it, let's move forward," is something we
10 should consider.

11 Without even talking about the directive, it
12 just seems like at some point there needs to be -- to
13 your point, it seems like something that needs to be a
14 cutoff and "This is the way we are going to do it
15 going forward."

16 MR. CURRY: We would just tag on to that, it
17 is not only beneficial for those of us who have to
18 comply, it would also help if all auditors understood
19 that the standard was the same and they were applying
20 the same yardstick.

21 The directive issue came to our attention
22 because we were criticized for it and then
23 subsequently were told "I think that would have been a
24 directive, that switching order would have been a
25 directive." The auditors were having in their

1 approaches to the auditees different definitions of
2 the same word.

3 COMMISSIONER SPITZER: Anything from WECC,
4 Steve?

5 MR. GOODWILL: Commissioner, I --

6 COMMISSIONER SPITZER: Obviously, we know
7 the West is different.

8 MR. GOODWILL: I think my focus as an
9 attorney advising the WECC Compliance Department has
10 been more on the standards themselves. I can
11 certainly sympathize with those in industry and our
12 partners at NERC and the other regions. In trying
13 sometimes to determine what those standards mean. It
14 goes back to the question about: What does "annual"
15 mean? What does "directive" mean?

16 I have found it in that role, advising
17 compliance, very frustrating that we could not -- that
18 we were left to our own as a region to figure that
19 out. I think we are starting to get better and better
20 and faster guidance from NERC.

21 Also, as time has gone on as Mr. Skaar
22 mentioned the regional auditing managers get together
23 and talk, and the regional enforcement managers get
24 together and talk and try to come up with some
25 consensus as a way to proceed. I think that has been

1 very, very helpful.

2 I would encourage to the extent that we can
3 some process to get those interpretations out to the
4 field, to all of us who need them much more quickly so
5 that we all can apply a common definition to what are
6 oftentimes difficult standards to interpret.

7 COMMISSIONER SPITZER: One final point. I
8 have heard quite a bit over the last couple of years
9 that there is a feeling in the regulated community
10 that "You've got too much obsession with
11 documentation" and that we are chasing squirrels and
12 looking at documents and not focusing on the real
13 reliability metrics.

14 This is probably more geared towards Chris
15 and Mr. Curry. My experience in the tax law was that
16 where I had clients that had good documentation,
17 oftentimes you would end up with a clean return. And
18 those that had documentation problems, guess what,
19 they had issues.

20 There was this nexus, not a perfect
21 correlation but nevertheless the documentation, a
22 failure of documentation reflected in some cases a
23 lack of internal controls and discipline that led to
24 more serious matters. What would be your response to
25 that?

1 MR. HAJOVSKY: I absolutely agree with your
2 analogy. But to my prepared remarks, I used the term
3 "strict compliance." "Strict compliance" deals with
4 anything down to one word. Your example deals with
5 documentation problems and systematic issues that are
6 embedded in an organization and would agree with
7 exactly what you are describing. However, one of my
8 examples was one test out of 10,000 would still count
9 as a violation here. That is not a systemic problem.
10 That is somebody thought they clicked "save" on an SAP
11 submittal through their program, and it didn't get
12 embedded well and so the auditor comes and sees "Oh,
13 you've got a really good program. Everything is well
14 done behind the scenes. I completely understand how
15 this type of thing"; so, there is a difference in the
16 analogy, and that is the way I would respond to that
17 part.

18 COMMISSIONER SPITZER: All right.

19 MR. CURRY: I would just add that
20 documentation may or may not be a reliability problem.
21 I assert that it has to go hand in hand with
22 performance, that you can't divorce reliability
23 performance from documentation.

24 If you look at documentation in a given
25 situation and you find three or four times during the

1 course of the year that something was not documented,
2 but it is obvious from the performance that the act
3 occurred, that is not a reliability problem. That may
4 have been a bad day. It ought not to be a
5 sanctionable event.

6 But on the other hand, if you look at the
7 same number of documentation omissions and can couple
8 them to something that was happening, an incident that
9 was occurring, clearly it is telling you something.

10 COMMISSIONER LA FLEUR: Thank you.

11 Commissioner Norris?

12 COMMISSIONER NORRIS: Thank you.

13 Let me throw one question out, pose it to
14 all of you, and I guess have a few individual followup
15 questions here. The first one is one of you mentioned
16 the issue, which maybe it is not an issue, or if it
17 is, I am curious to your thoughts on the tension
18 between event analysis and the lessons gained from
19 that and the NERC RE need to investigate on compliance
20 and enforcement. Is there a tension, and how do we
21 deal with that?

22 MR. GALLOWAY: Well, I think there is. The
23 way I would characterize it is I don't think it is an
24 either/or proposition. I think if an event occurs on
25 the system, and we can have a debate about what

1 constitutes an event, but we have moved to putting
2 some framework around the threshold that you would
3 consider something an event and then categorization
4 within that as to how severe it was.

5 From a reliability context, what you want is
6 you want the entity to learn from that and fix that so
7 that they don't have a repetition of that issue, but
8 also want everybody else on the system who might be
9 susceptible to it to learn from that as well.

10 You also want the entity when they are
11 looking at the facts and circumstances around the
12 event to understand was a cause or contributor related
13 to that a failure to comply with existing standards or
14 perhaps a gap in the existing set of standards that
15 exist that could be closed.

16 I think there are kind of parallel
17 activities, but we do get into some tension around the
18 sequencing of those activities and, for lack of a
19 better term, how "expansive" a compliance review needs
20 to be undertaken for different significance events.

21 If you have something that is on a low
22 order, a relatively low-significance event, there is
23 an item to be gained from that. There is a compliance
24 that might be appropriate from that, but it is not
25 necessarily the best use of the entity, NERC time, to

1 do a completely expansive review of every potential
2 compliance consideration that might be involved there.

3 Probably a superior way to do that is to
4 look at those low-level events in a trending way to
5 see is there repetition either with that entity or
6 across that topic or across multiple entities that
7 should be looked at in a more intrusive way
8 downstream.

9 I think to me it is not an either/or
10 proposition. It is really appropriately balancing
11 both ends of that and really to what extent and what
12 scope really from a compliance perspective makes sense
13 for a given event, specially those low-level events.

14 COMMISSIONER NORRIS: Anybody else?

15 MR. SKAAR: Sure. Thank you. I think you
16 raised a good point. There has been tension. We
17 certainly have lived through it. I think one of the
18 things we concluded was when there is an event, we
19 should set the expectation that there is going to be a
20 compliance review at the end. That is number one.

21 But I don't think that compliance review,
22 because there is always time for determining
23 culpability, should not interfere with having the
24 technical people from the industry which we rely on
25 for this to figure out what happened, what did we

1 learn, how we can prevent it.

2 What I have seen is if you pull the trigger
3 on an investigation simultaneously, it can chill the
4 technical analysis, which is unfortunate. We want to
5 avoid that. I think setting the expectation that
6 there will be, one, but we are not going to let that
7 interfere with our work, and we need to be smart about
8 it.

9 For example, we need to protect ourselves
10 related to data. Maybe on event analysis or when an
11 event occurs set the expectation and pull all your
12 data so that it can be preserved.

13 Thank you.

14 COMMISSIONER NORRIS: Mr. Curry?

15 MR. CURRY: I would just like to jump in and
16 say amen to what Mr. Skaar just said. The
17 enforcement, the holding the entity accountable for a
18 violation can wait, but the more important has got to
19 be to share the lesson and get it to everybody else so
20 that we can learn.

21 COMMISSIONER NORRIS: Mr. Curry -- oh, no,
22 Mr. Goodwill first. You mentioned that the right
23 people in the room could come up with some standards
24 that are really critical. I think that is a summary
25 of one of our comments, to come up with some standards

1 that are critical to reliability. There is a number
2 of them that are most critical. How does that happen?
3 You are empowered today to pull the right people in
4 the room. Give me a little sense of how we pull that
5 off.

6 MR. GOODWILL: Mr. Norris, I think as I
7 mentioned, it really would start out as a discussion
8 from FERC, through NERC, the regions, and the industry
9 with our CIP experts as to what they believe. I mean,
10 as an attorney on a daily basis working with our
11 compliance department, I would discuss with our CIP
12 SMEs, our CIP auditors, the reliability impact of a
13 given violation. They know when they look at a
14 particular standard and a particular violation and the
15 facts on the ground that an entity -- they very
16 quickly have a good sense of how serious they think
17 that impact, the risk, is from that violation. I
18 think you can do the same thing in a larger
19 conversation to get at the heart of what is important
20 in CIP.

21 For instance, we end up treating all
22 violations the same. There might be different
23 penalties proposed at the end of the day, but an
24 entity failing to produce evidence that a senior
25 manager actually approved their security plan may well

1 be different than a violation going to the six-wall
2 requirement for physical security for a CIP facility,
3 yet they all go through the notice of alleged
4 violation process. They all go through the same,
5 hopefully, settlement process and up through NERC and
6 on to FERC through the same NOP process.

7 I think we could target our resources better
8 to finding and fixing the things that matter most if
9 we were able to deal with those differing types of
10 violations in different ways at the very beginning of
11 the enforcement process.

12 Back to your question. I might be naive,
13 but I think, again, with the 693 standards I don't
14 think it would be that difficult to find a relatively
15 good consensus fairly quickly on what our experts
16 think matters most to reliability.

17 MR. HAJOVSKY: If I may just add a quick
18 other set of examples. I agree that I think it would
19 be fairly easy to do. I think somebody had made the
20 comment a certain amount we might have some discussion
21 over. Some more examples are CIP-04 requires training
22 on an annual basis for those who have access to
23 critical cyber assets.

24 Well, if you missed that by a day in your
25 annual training, that is the type of thing that gets

1 reported, going back to the granularity, and those
2 could be handled in a different way by missing
3 something by a quarter or even six months, by a
4 tracking glitch.

5 Another might be if you didn't update your
6 password in a period of time from another standard.
7 There are these type of routine elements in the CIP
8 standards that are a different category in my opinion
9 than as you used the 6-wall example, analogy. I think
10 there are a lot of examples we could easily parse out.

11 COMMISSIONER NORRIS: This may be an example
12 of a topic for our next tech conference on setting
13 priorities, so I just wanted to flesh that out a
14 little bit. Mr. Curry, hear a lot, and I think Mr.
15 Spitzer asked you some questions relative to this,
16 about concerns for smaller entities. Sometime the
17 notion of critical assets and cybersecurity can be
18 overwhelming because it seems larger and it may be an
19 issue that I will not have dealt with as much.

20 Put me inside a half a dozen of your
21 counterparts, what is the conversation? What is the
22 problem? What do we need to do about it? I think it
23 is the burden of compliance if it is an organization
24 that is of some size.

25 If it is Piggott, Arkansas, it is "Why in

1 the world if the only thing I am responsible for is
2 that UFLS responsibility to maintain that program and
3 perform well, and if my 12-megawatt system blows up
4 and goes off the face of the earth, is it any threat
5 at all to the BPS?

6 I mean, that is just requiring them to do
7 something that won't contribute anything to the
8 reliability of the BPS.

9 COMMISSIONER NORRIS: Is there a recognition
10 though that their system could be an access point for
11 cyber?

12 MR. CURRY: Insofar as it would touch the
13 UFLS obligation, certainly. But is there a
14 requirement that they have to maintain the same degree
15 of awareness and reliability with regard to the
16 operation of their system that would have to be the
17 case with regard to a much larger system or a system
18 that if it failed would impact the system?

19 COMMISSIONER NORRIS: Is it a question of
20 the same degree, or is it a question of they really
21 don't know what that degree is, and the uncertainty of
22 that is intimidating?

23 MR. CURRY: I don't have any evidence to
24 suggest they don't know what it is, but it wouldn't
25 surprise me to find that that is the case. If you've

1 got a couple of dozen people working for your entire
2 utility, you are not going to have the same level of
3 specification awareness knowledge of what the
4 requirements are that you will be able to maintain in
5 a much larger system.

6 In LES' case, we really take seriously the
7 matter of compliance. We have the compliance
8 committee that is headed by a young engineer who is
9 enthused and forceful and doing a great job for us.
10 He knows he can talk to anybody at LES, if he has to,
11 in order to identify problems and get the support that
12 he needs.

13 They meet monthly. They are candid. They
14 are honest. They hold no punches. They come after
15 each other. That is the kind of culture of compliance
16 we want but it is driven because reliability is really
17 our concern, and that I think is going to be a culture
18 that may vary from utility to utility, but the larger
19 you get perhaps to a certain point the easier it is to
20 maintain that culture. I suspect you get to the point
21 where you are so large that it becomes a handicap. On
22 either extreme, maybe you've got the problem of
23 maintaining consistency, maintaining common
24 understandings. But the vast majority in the middle
25 should be able to make that accommodation and comply.

1 COMMISSIONER NORRIS: I do think -- I'm sure
2 we will have more conversations about this going
3 forward -- but there has to be some way to assist the
4 smaller entities with technical expertise and ability
5 to handle this because there is a scale problem here.
6 I think we need to keep that in mind going forward.

7 MR. CURRY: We've got more people on our
8 committee than Piggott, Arkansas, has for the entire
9 operation of the system.

10 COMMISSIONER NORRIS: We won't give the same
11 deference when they join the big 10, but we will for
12 smaller ones.

13 (General laughter.)

14 MR. CURRY: That is understood.

15 COMMISSIONER NORRIS: Okay. Finally,
16 Mr. Skaar, you talked about the culture of compliance
17 and the self-reports and how you want to prepare and
18 eventually reward strong programs because that yields
19 a self-report. How do we treat the self-report that is
20 the result of an audit notice? Does that help the
21 culture of compliance to credit a show of compliance,
22 or does that hinder to get a credit for a self-report
23 subsequent to an audit notice?

24 MR. SKAAR: Is this a self-report prior to
25 an audit or after?

1 COMMISSIONER NORRIS: It is a self-report
2 subsequent to a notice of a pending audit. Does that
3 help the culture of compliance or hurt the culture of
4 compliance.

5 MR. SKAAR: Do you mean after an audit is --
6 let me make sure I've got the example. After an audit
7 is complete?

8 COMMISSIONER NORRIS: No, no, after
9 receiving notice of a pending audit.

10 MR. SKAAR: No. Once you receive, I think
11 we use 90 days now, because I think the trade
12 associations wanted to use 90 days rather than 60 days
13 on the notice, our view is once we give you that audit
14 notice, I mean we really need to peel back that
15 self-report.

16 As I said, all self-reports are not the
17 same. If this was a self-report by accident that or
18 through preparation for an audit, that is different
19 than a self-report as a result of a strong compliance
20 program, not part of that audit period.

21 I think that we have to be very discerning
22 about self-reports, but it works the other way as
23 well. Repeat violations, for example, as a result of
24 a strong compliance program, I mean, I don't
25 automatically think repeat violations should be

1 considered aggravating.

2 I mean, it depends on the situation. It
3 really depends on the strength of the compliance
4 program. I say "program" rather than "culture"
5 because I think you have to talk the talk but walk the
6 walk. Walking the walk is in the compliance programs
7 and in the controls. Did that answer your question?

8 COMMISSIONER NORRIS: Yeah, yeah. Thanks.

9 COMMISSIONER LA FLEUR: All right. Thank
10 you, Commissioner Norris. I will try to keep us on
11 schedule, but I have a couple of questions. Really
12 everyone alluded in some way to making sure we are
13 working on the right things.

14 We are putting our resources in the right
15 places, priorities, some pretty compelling examples of
16 maybe putting monitoring and compliance resources,
17 things of less importance like something being in a
18 Word

19 document rather than an Excel spreadsheet or one
20 in 10,000 fields not being filled out.

21 Assuming we could now figure out how to stop
22 all that and now we have freed up the resources, what
23 should we be doing more of? Whether it is NERC, FERC,
24 or the Regional Entities, what are we not doing enough
25 of, the things on the other end of the spectrum that

1 need more resources or more audits or more something

1 than they are getting now to help the system?

2 MR. CURRY: I don't know whether or not the
3 forum is something that is applicable or possible for
4 everyone, but certainly that is an exercise that is
5 beneficial. It has been for LES, and we look forward
6 to doing it with others. We have learned a lot from
7 it. We also received some reinforcement of what we
8 were doing, which is helpful. It is not always good
9 just to be told where you failed. It is good
10 sometimes to hear that that you are doing things well.
11 I would encourage that.

12 COMMISSIONER LA FLEUR: I think Mr. Galloway
13 made that point, rewarding the excellence as well.
14 That is something that the forum is well situated to
15 do.

16 MR. HAJOVSKY: If I may, a few things come
17 to mind. First, guidance is always welcome whether it
18 be with respect to process, with respect to
19 interpretation. I interpreted your question to "we"
20 being the Commission, so I will try to frame it in
21 those terms.

22 COMMISSIONER LA FLEUR: It could be "we,"
23 the whole body of this working on this.

24 MR. HAJOVSKY: Yes, I understand. I
25 understand. I will respectfully just offer two

1 thoughts for your consideration. Guidance is always
2 welcome. I think participation in standards
3 development is something I have heard at other
4 settings, and then I guess sort of even tie it back to
5 the guidance.

6 As we go through this next iteration of
7 developing standards, we want to write them in a way
8 that guides people not just for how reliability will
9 be taking place, but how are we going to monitor the
10 compliance.

11 This results-based standard concept is
12 important because it gets to that point. It gives
13 folks a clear definition for "How do I show what is
14 going on," because the standards are written better.

15 But to the extent that the Commission --
16 well, not even with the results-based process -- feels
17 that any deviation from an existing standard, unless
18 it is in addition to, we would benefit from your
19 participation because some standards may involve
20 taking a fresh look at how we do things.

21 It is again kind of going back to some of my
22 introductory remarks. Those are the two that come
23 immediately to mind.

24 Thank you.

25 MR. GALLOWAY: I will speak kind of from

1 the ERO, the registered entity side. There are a
2 couple of different things that kind of come to
3 mind, assuming that we could prioritize the work a
4 little differently.

5 One, I would see that much more effort
6 being placed in looking at the health of the
7 entity's compliance program, all right. Does it
8 have, to Dan Skaar's point, all the right program
9 elements? Is it well attended to by senior
10 management? Is it yielding the right actions from
11 staff? It is kind of a forward-looking item in
12 terms of entity health and moving in the right
13 direction.

14 This may seem to go a little bit in
15 contrast to the consistency discussion, but I do
16 think entity performance isn't equal, call right. I
17 think that with a little more resource available,
18 more up-front preparation in terms of getting ready
19 to execute the audit in terms of really deeply
20 understanding the entity's performance history,
21 their culture, and so forth, and combine that with
22 the higher-value standards to look at, I think we
23 could do a little bit more of an informed look on
24 the audits than we are doing right now where you are
25 trying to cover a broad set of topics, and therefore

1 you are covering at maybe one level of depth that
2 isn't appropriate.

3 Then, the other thing that we haven't
4 talked about much at all is just really kind of
5 working through training to make sure that all the
6 folks in the ERO side understand process, understand
7 application of standards, understand interpersonal
8 action, and so forth.

9 What we do have -- my goal is for training
10 of auditors, lead auditors, and so forth, but that
11 could be taking the next level of detail down.
12 Certainly there is training opportunity for other
13 folks in the overall process as well. Those are
14 some of the things that come to mind.

15 COMMISSIONER LA FLEUR: Thank you.

16 Mr. Skaar?

17 MR. SKAAR: I think one of the things is
18 if we can take the mystery out of compliance I think
19 that would be good, but by providing more details
20 and what we call these "QRSAWs" in setting clear
21 expectations.

22 I think that would go a long way to help
23 in the industry and to be more constructive, because
24 I do think compliance is more like kind of an open
25 book test. You either did it or you didn't, and we

1 will figure out whether you did or didn't. I think
2 that it is fair. I think that a registered entity
3 should be encouraged to ask: "What are your
4 expectations? What are the elements to demonstrate
5 compliance?"

6 I think that is a fair question. I think
7 it is an unfair question for Registered Entities to
8 ask us: "If I do this, will I be compliant?" My
9 response to that is: "Are you making a self-report?"

10 (General laughter.)

11 COMMISSIONER LA FLEUR: Mr. Goodwill?

12 MR. GOODWILL: Commissioner La Fleur, I
13 would offer, and I'm not sure that it is something
14 that I think we need to do more, but one of the
15 things that WECC has done now for the past couple of
16 years is develop and expand its outreach to industry
17 in the West.

18 I think that has been very, very
19 successful through our compliance user group
20 meetings, periodic open mike sessions where industry
21 can call in and talk to WECC experts on the phone.

22 We have used those forums to talk about
23 lessons learned from our own compliance process,
24 what our auditors are seeing at audit, the audit
25 approach that they take, the types of evidence that

1 they look for, that they suggest that an entity
2 might want to think about having.

3 That necessarily gives the entities an
4 understanding of where really WECC is coming from in
5 interpreting the standards. As I discussed earlier,
6 I think the difficult we all have is in arriving at
7 a common interpretation.

8 We have tried as much as we can, and we
9 are continuing to improve our efforts, to pass on to
10 the entities what we believe the standards mean
11 without getting toward the official interpretations
12 that we know need to flow through a separate
13 process.

14 We have found a fairly steady decrease in
15 violations in the West over the past couple of
16 years. I am sure there are many reasons for it but
17 we attribute one of the major reasons for it to be
18 our outreach efforts. We are trying to take the
19 mystery out of what this thing called "compliance"
20 is and how we can work together to build the
21 Registered Entities' compliance, and therefore have
22 a positive effect on reliability.

23 COMMISSIONER LA FLEUR: Well, thank you.
24 I could ask followup questions on every single one,
25 but I see it is 2:45, and I want to keep us on

1 schedule because we have another excellent panel
2 coming up at 3 o'clock.

3 I want to thank the panel. I know this is
4 a dialogue that is definitely going to continue into
5 the next technical session and in between. Thank
6 you all and see you all back here at 3 o'clock.

7 (A recess was taken from 2:45 p.m. to
8 3:06 p.m.)

9 PANEL 2: VIOLATION PROCESSING AND PENALTIES

10 COMMISSIONER LA FLEUR: This afternoon we
11 are going to turn our attention to one of the more
12 difficult to talk about parts of compliance but
13 another important topic, "Violation Processing and
14 Penalties." We have an all-star lineup sitting
15 before us to talk about that.

16 I haven't prepared any little opening
17 remarks for this part, but I just want to read a
18 paragraph that our star lawyer, Jonathan First,
19 actually handed me that I had not previously focused
20 on in this way that is actually from back in
21 February 2006. The first order, 693, setting up
22 this whole schema, had just a one-paragraph on what
23 penalties are all about.

24 The Commission concurs that the
25 fundamental goal of mandatory enforceable

1 Reliability Standards and related enforcement
2 programs is to promote behavior that supports and
3 improves Bulk-Power System reliability.

4 "A monetary penalty must be assessed and
5 structured in such a way that a user, owner, or
6 operator does not consider its imposition simply as
7 an economic choice or a cost of doing business.
8 Further, a non-monetary penalty should be structured
9 to encourage or require compliance and improve
10 reliability. In its oversight role, the Commission
11 plans to monitor the effectiveness of penalties,
12 both monetary and non-monetary."

13 Here we are. Good work whoever was on the
14 Commission. Commissioner Moeller and perhaps others
15 were there, but that is exactly where we are as
16 monitoring how that penalty schema is going.

17 We have, known to all, Gerry Cauley, the
18 president and CEO of NERC; Stacy Dochoda, who runs
19 one of the Regional Entities at the Southwest Power
20 Pool; Bill Fehrman from MidAmerican Energy, the CEO
21 and president there, thank you for coming out;
22 David Mohre, the executive director of the Energy
23 and Power Division of NRECA, the "National Rural
24 Electric Co-Op Association"; John DeStasio, CEO of
25 SMUD, the "Sacramento Municipal Utility District";

1 and Steve Naumann, vice president of Exelon.
2 I guess we will follow the same rules and start with
3 Mr. Cauley.

4 MR. CAULEY: Thank you, Commissioner
5 La Fleur. Good afternoon, Chairman Wellinghoff,
6 commissioners, staff, and fellow panelists. I was
7 very intrigued by the questions and the discussion
8 in the first panel. I was kind of wishing I had
9 been up here.

10 I did think that most of the discussion
11 centered around things that we have identified as
12 areas we are working on and very consistent with our
13 risk-based approach and some of the directions that
14 we have recently taken. We will be submitting some
15 comments, written comments, to that effect.

16 In the past three and a half years, NERC
17 has made substantial progress in standing up a
18 comprehensive program for monitoring, enforcing
19 compliance with mandatory standards, working with
20 Regional Entities.

21 We have developed standardized procedures,
22 forms, and electronic tools and provided training to
23 enhance the qualifications of our compliance
24 personnel.

25 To date, 5,487 possible violations have

1 been identified, an average of 30 new violations
2 every year since inception. Of these, 1,219 have
3 been closed through filings of notices of penalty,
4 1,265 have been dismissed, and 3,003 remain open in
5 the current caseload.

6 We have worked closely with the
7 Commission's staff on what constitutes an adequate
8 record for a violation. The Commission's of
9 July 3d, 2008, approving the first group of NOPS
10 established a baseline of expectations regarding
11 sufficiency of the record.

12 The Commission's Guidance Order issued on
13 August 27th of this year further clarified the
14 treatment of repeat violations. We understand what
15 is expected by the Commission, and we continue
16 learning and improving with regard to the record of
17 violations. I believe our results to date have had
18 a positive impact on reliability. The industry has
19 invested substantial resources in achieving
20 compliance with the NERC standards which were
21 previously voluntary and subject to
22 self-interpretation. The 1,200-plus violations that
23 have been closed and made public offer more
24 transparency to the industry with respect to what
25 constitutes compliance. NERC and the regions, as we

1 heard in the previous panel, have been publishing
2 compliance application notices to further clarify
3 expectations.

4 Most importantly, of the 4,222 possible
5 violations that have been closed and made public are
6 for more transparency to the industry with respect
7 to what constitutes compliance. NERC and the
8 regions, as we heard in the previous panel, have
9 been publishing application notices to further
10 clarify expectations.

11 Most importantly, of the 4,222 possible
12 violations not dismissed over 2,700 or two-thirds of
13 these have already been mitigated. Building such a
14 substantial record of learning and correcting is
15 clearly in the public interest and is consistent
16 with the intentions of Congress in establishing
17 Section 215 of the Federal Power Act.

18 Despite this progress, I am concerned with
19 the present caseload of over 3,000 violations and
20 the current pace of 200 new violations reported each
21 month. I am concerned with the time it takes to
22 process violations and the administrative burden on
23 the industry, NERC, the regions, and the Commission.

24 Compliance results should improve
25 reliability -- compliance results will improve

1 reliability of non-compliance processing. In some
2 respects, I can argue that the current caseload is
3 transitional.

4 There was an initial wave of violations
5 stemming from the operating and planning standards
6 approved in Order 693, and there are strong
7 indications in recent months that this wave has
8 crested and is beginning to subside.

9 We are currently experiencing a second
10 wave of violations based on the cybersecurity
11 standards. In fact, more than half of all incoming
12 violations are related to cybersecurity.

13 I worry that this wave is still building
14 and that even though cybersecurity is essential to
15 reliability it may draw attention for more prevalent
16 risks related to operating and planning.

17 In spite of the transitional nature of the
18 caseload, I believe there are also underlying
19 programmatic issues that need to be addressed. Most
20 important is the tendency to treat every violation
21 as being of equal importance to reliability.

22 The effectiveness of the compliance
23 program depends on achieving proportionality between
24 compliance efforts and benefits to reliability.
25 NERC and the regions working with the Commission

1 have made progress on this front.

2 Earlier this year, we started using an
3 abbreviated NOP format, and half of the violations
4 in 2010 have been processed with a simplified
5 format.

6 NERC and the regions have worked together
7 to align expectations regarding the quality and
8 level of detail in filings. The amount of rework
9 between NERC and the regions has been substantially
10 reduced.

11 We have a new initiative underway to treat
12 the lowest priority of violations as administrative
13 citations. These violations are typically related
14 to paperwork, present the lowest risk to
15 reliability, and are quickly remedied.

16 We have been working with the Commission
17 staff on a proposal and look forward to feedback on
18 the initial filings of these administrative
19 citations early in 2011.

20 I would ask the Commission to consider
21 over time whether there is sufficient trust in the
22 program to allow NERC and the regions to exercise
23 further discretion to verify that minor infractions
24 have been corrected and to maintain a record of
25 these minor infractions but not file an NOP in each

1 case.

2 This is consistent with Order 693, at
3 paragraph 225, which recognizes the enforcement
4 discretion of NERC and the Regional Entities and the
5 Order of April 19th, 2007, at paragraph 133 on
6 delegation agreements.

7 Finally, I will note that the penalty
8 sanction and guidelines, the NERC Penalty and
9 Sanction Guidelines, which were modeled after the
10 Commission's policies on enforcement, are entirely
11 sufficient and appropriate in their current form to
12 serve our reliability mission.

13 The guidelines allow a wide range of
14 penalty outcomes to reinforce positive compliance
15 behaviors while allowing substantial penalties to
16 discourage egregious behavior.

17 If I do have a concern with our
18 enforcement actions to date, it is that we may be
19 overemphasizing the need for consistent penalties on
20 a superficial level, that a violation of a
21 particular requirement should result in similar
22 dollar penalties.

23 This may provide a sense of equity and
24 fairness to the Registered Entities; however, it is
25 much more important to our reliability risk strategy

1 that we understand consistency of sanctions to mean
2 consistent with the compliance behaviors to be
3 encouraged or discouraged. I am more interested in
4 penalties that send the right messages than the ones
5 that send the same messages all the time.

6 In conclusion, I am proud of the progress
7 that we have made in the developing the compliance
8 program over the past several years. We have
9 several great opportunities ahead to improve
10 expediency, consistency, and reliability benefit. I
11 thank you, and look forward to your questions.

12 COMMISSIONER LA FLEUR: Thank you,
13 Mr. Cauley.

14 Ms. Dachoda?

15 MS. DOCHODA: Yes. I have slides, if we
16 could cue up the computer, please. Thank you.

17 My name is Stacy Dochoda, and I am the
18 general manager of the Southwest Power Pool
19 Regional Entity. I would like to discuss a few of
20 the accomplishments that I think we have had in the
21 enforcement area.

22 I think we have achieved a better
23 scalability of the penalties associated with the
24 seriousness of the violation, and also I think we
25 have achieved better guidance and have been able to

1 implement zero penalties where appropriate.

2 I think in the last year in particular we
3 have reduced the rework that we have between the
4 Regional Entities and NERC, and also we have
5 increased resources substantially.

6 (PowerPoint
7 presentation in progress.)

8 This graph shows the resources in terms of
9 dollar budgets and also FTE's at the Regional Entity
10 level and both of those have doubled since the 2008
11 time period.

12 In terms of our current environment, as
13 Mr. Cauley mentioned, we are definitely seeing an
14 increase in violations both in terms of the
15 violations that come in, and unfortunately, because
16 we are not processing them as fast as they come in,
17 we are experiencing a significant increase in our
18 backlog of violations.

19 This chart shows that while in 2008 we had
20 a significant number of active violations, around
21 1,500 violations; today, we sit at 3,000. There are
22 many reasons, I think, that lead to that.

23 I think that we have more experienced
24 auditors. We have more resources that we are
25 applying. We have also had more information sharing

1 in terms of best practices. Our processes have

1 improved. We have preaudit and more sampling that
2 we do. Also, the number of standards has increased
3 by 35 percent since we implemented the program, and
4 that does include the CIP standards.

5 In addition, another item that I think may
6 be a little more subtle is we have done a
7 significant amount of outreach. Among the regions
8 we have done 580 hours of face-to-face outreach to
9 Registered Entities in 2010.

10 I think obviously that is an admirable
11 thing and results in good outcomes, but it also does
12 result in increased self-reports as entities
13 understand what is required for compliance.

14 This chart is the one that keeps me up at
15 night. As the Regional Entity general manager, one
16 of my main responsibilities is to ensure that we
17 have the appropriate resources to carry out the
18 functions that we are delegated to do, and it is
19 important to me that we are spending our resources
20 where they matter.

21 What this chart shows is it shows the
22 amount of our backlog that we would forecast under
23 different scenarios at the SPP Regional Entity. The
24 bottom lines of this chart are assuming varying
25 processing speeds. A year ago at the SPP Regional

1 Entity, for each FTE that I had in enforcement we
2 were able to process approximately six violations in
3 one month -- excuse me, six violations in one year.
4 We have doubled that production rate to where one
5 person is now able to process about 12 violations in
6 one year.

7 At the rate that violations are coming in
8 to the SPP Regional Entity, which this year it was
9 over 250 violations, if I don't change something
10 significantly about the way that I process
11 violations, by the end of 2013 I will have a backlog
12 of 600 violations.

13 Now, you might ask me, "Well, you just
14 need to increase your resources," but there are two
15 reasons that I think that is not the right way to
16 go. First of all, I currently have eight FTEs that
17 I devote to auditing, and I have eight FTEs that I
18 devote to enforcement.

19 In order to keep up with the rate of
20 violations that come in, I would need to increase my
21 enforcement by FTEs to 20. I think if I have an
22 organization where I have 20 people in enforcement
23 and 8 in the auditing team that there is something
24 fundamentally wrong with what I am doing.

25 The next slide will expand on that a

1 little bit. This is a chart by violation risk
2 factor, and the violations that I have processed or
3 are in process. Eighty-one percent of the
4 violations I have do not have a high risk factor.

5 Again, I think we have to make sure that
6 we are spending our resources where they matter
7 most. I think that will involve both streamlining
8 processing, but I also think that we have to think
9 about whether we should have more discretion in the
10 field as to whether items are violations to begin
11 with.

12 Finally, I am going to make a specific
13 request. There have been several orders that have
14 come from the Commission where we have received
15 guidance on what the Commission would like to see in
16 future notices of penalties.

17 I welcome that guidance, and we certainly
18 plan to put that in place, but one of the logistic
19 factors that we have to face is that at any given
20 time we have about 500 violations that are in
21 essentially final draft stage.

22 What I would like to request of the
23 Commission is consideration such that when we have
24 guidance about what should be in future NOPs that we
25 are able to do that in a way that we don't have to

1 rework those violations that are already almost
2 ready to come to you.

3 That concludes my remarks.

4 COMMISSIONER LA FLEUR: Thank you very
5 much, and thanks for the specificity of that
6 recommendation.

7 Mr. Fehrman?

8 MR. FEHRMAN: Thank you. Good afternoon,
9 commissioners, I am Bill Ferhman president and COO
10 of MidAmerican Energy Company. I will be speaking
11 on behalf of both my company and my fellow CEOs of
12 EEI member companies this afternoon and want to
13 reinforce that we are committed to maintaining
14 reliability, promoting a culture of compliance, and
15 striving for operational excellence.

16 I am here this afternoon to offer EEI's
17 perspective on how the Commission's, NERC's, and the
18 industry's collective compliance and enforcement
19 resources should be appropriately prioritized and
20 allocated so we achieve our common goal of improving
21 reliability in a more cost-effective fashion.

22 As the industry works on improving the
23 electric reliability two essential elements are our
24 strong compliance culture and a firm but fair
25 enforcement.

1 The Commission, NERC, and the industry
2 must strike the right balance between managing
3 reliability risk and managing compliance risk. EEI
4 is concerned that our priorities are out of balance,
5 causing industry to collectively develop more
6 resources to managing compliance risk than we do to
7 identifying the priorities, the resources, and the
8 incentives needed to manage reliability risks.

9 I would like to briefly describe what EEI
10 believes are some of the symptoms of this problem
11 and suggest some ways that the Commission, NERC, and
12 industry must work together to strike the proper
13 balance.

14 NERC has a significant and growing backlog
15 of unprocessed violations as you have heard, many of
16 which are highly unlikely to adversely impact
17 reliability.

18 NERC also manages a compliance enforcement
19 program on the premise that all violations must be
20 equally addressed regardless of reliability risks
21 and the facts and the surrounding circumstances.

22 The regions have no discretion in making
23 threshold determinations on how to enforce a
24 violation. The regions and NERC developed highly
25 detailed records that that significant time and

1 resources to produce. Such time and resources could
2 be better devoted to areas of greatest risk. After
3 all no utility has unlimited resources, and all
4 utilities should be cognizant of managing costs that
5 will ultimately be borne by our customers.

6 To help address these issues, I offer two
7 policy recommendations this afternoon for your
8 consideration. First, the Commission and NERC need
9 to agree on a clear set of common priorities for
10 compliance enforcement and then allocate their
11 enforcement resources and in turn our company
12 resources where they matter most to the reliability
13 of the Bulk-Electric System.

14 Toward that end, the Commission should
15 allow NERC and the regions greater enforcement
16 discretion. In addition, NERC should immediately
17 develop a no action letter and speeding ticket
18 proposal for minor administrative violations
19 reasonably considered not to pose a significant
20 threat to Bulk-Electric System reliability.

21 The Commission has clearly invited such
22 proposals. Many violations driving the backlog are
23 due to zero defect violations severity levels for
24 violations that are unlikely to pose a significant
25 threat to the Bulk-Electric System.

1 The process clearly needs changing when
2 the resource requirements for addressing an
3 inadequate system protection testing and monitoring
4 program, which is critical, are the same as for
5 missing a test by a few days as is the case today.

6 Second, EEI remains concerned that the
7 Commission is inadvertently supplanting the NERC
8 standards process by independently interpreting
9 standards through orders in some instances
10 significantly altering the requirements that
11 industry must meet.

12 The Commission should not misinterpret
13 this position as an unreasonable effort on
14 industry's part to avoid accountability. When
15 reasonable subject matter experts can disagree about
16 a standard definition, there should be no finding of
17 a violation.

18 Instead interpretation of standards should
19 in the first instance be made by NERC, and the NERC
20 Reliability Standards development process should be
21 leveraged to render interpretations promptly and
22 efficiently.

23 EEI members are committed to identifying,
24 prioritizing, and addressing any ambiguous standards
25 in need of further refinement as a part of the

1 broader NERC Reliability Standards development
2 process.

3 Before I close, I would like to also
4 update you on the status of our efforts to expand
5 and strengthen the North American Transmission
6 Forum, a topic that was also discussed at the
7 July 6th technical conference.

8 As you know, the forum is a member-driven
9 entity separate and apart from NERC. It's mission
10 is to promote excellence in the reliable operation
11 of the electric transmission system by cultivating
12 and ensuring the expertise of its members who
13 recognize that rules and standards alone do not
14 ensure reliability.

15 Utilities can and should learn from each
16 other's successes not just their failures, and the
17 forum serves this precise purpose and is developing
18 relevant metrics for a performance evaluation,
19 developing best practices, and engaging in peer
20 reviews.

21 Entities are increasingly recognizing the
22 forum's value and it has now grown to 55 members,
23 including our company. I would also like to note
24 that since that conference there have been two EEI
25 CEO meetings at which the forum was discussed in

1 detail. All of the EEI CEOs were briefed. I
2 personally have attended the forum's board meeting
3 this fall and will be attending the next forum board
4 meeting.

5 Again, I appreciate the opportunity to be
6 here today, and I look forward to participating in
7 the discussion.

8 COMMISSIONER LA FLEUR: Thank you,
9 Mr. Fehrman.

10 Mr. Mohre?

11 MR. MOHRE: Yes, thank you. Commissioner
12 Wellinghoff -- Chairman Wellinghoff, excuse me, and
13 members of the Commission, I want to introduce
14 myself. I am David Mohre. I am executive director
15 of the Energy and Power Division of NRECA.

16 As you are probably aware, NRECA's members
17 supply retail power in all or parts of 83 percent of
18 the counties in the United States. I will come back
19 to that in a moment.

20 I would like to thank you very much for
21 the invitation to come here and express our views on
22 violation processing and penalties, but I would also
23 even more like to thank you for continuing your
24 outreach effort that you started in July. This is a
25 very important issue to all of us, and I think this

1 outreach effort is very commendable.

2 At the outset, I would like to reinforce
3 that the co-op strongly supported mandatory
4 Reliability Standards before they were law, and
5 continue to support that.

6 I would like to stress as I did in July
7 that we think things are going pretty well,
8 particularly when you look at the enormity and
9 complexity of the issue, the evolution that we are
10 undertaking, over the past few years.

11 We think we have a great view of what is
12 going on across the country from the 47 states that
13 our members serve. Importantly, we analyze how
14 things are going from the following perspective that
15 we continue to come back to over and over again.

16 Is the process producing focus on material
17 issues? Is it a proper risk-based prioritization of
18 effort? Is the effort timely? And, is the effort
19 consistent?

20 Viewed through this lens we think many
21 things are going very well except for something that
22 has been talked about both in the last panel and
23 this panel, and that is, it has become obvious to us
24 and hopefully to everybody that we are making
25 perhaps a continuing mistake if we continue to treat

1 all violations the same.

2 Whether it is a major or minor operation
3 or maintenance violation or whether it is a
4 documentation violation, treating them the same is a
5 mistake. We are very happy with the efforts that
6 NERC has undertaken to start down this path and the
7 acceptance the Commission has shown in its writings,
8 and we think that needs to continue with pace.

9 The reason we think that is important and
10 the reason we think we must streamline the violation
11 process and do it quickly -- and we don't care
12 whether you call it a parking ticket, a traffic
13 ticket, we don't care what you call it -- is the
14 following.

15 First, if we continue to do what we are
16 doing, as you have heard from this panel and other
17 panels, you will continue to spend less time and
18 focus on things that truly matter. You have heard
19 it over and over again; we agree.

20 Second, we think we will continue to
21 overload both NERC and RE staff and the RE and NERC
22 processes in continuing to build backlogs that have
23 a rather difficult kind of outcome.

24 Third, and this is fairly important and it
25 is a little tough to talk about, we are afraid that

1 if we don't change some of this we will continue at
2 an effort that will raise questions in people's
3 minds of the ultimate usefulness of and the
4 motivation behind a lot of the process itself. I
5 discussed that a little bit in my written testimony.

6 It is interesting that 693 was mentioned
7 and particularly the part about encouraging positive
8 behavior. We fully agree, but I call to your
9 attention through analogy when is the last time you
10 put a quarter in a parking meter, you did the right
11 thing, walked away, and got a ticket?

12 The question is: Are you going to spend
13 the time and money to appeal that \$25 ticket, okay,
14 and what happens when you get this over and over
15 again?

16 That is what has been happening to many of
17 our members. They have spent the time and effort,
18 they are told they do a good job, and then they get
19 dinged for some almost irrelevant thing that
20 couldn't affect the reliability of the Bulk-Power
21 System in any event. We think that is an important
22 issue.

23 I would particularly like to mention the
24 effect this kind of thing has with regard to the
25 smaller entities. The smaller entities were

1 mentioned earlier today. Again, it is the idea that
2 the fine is almost in many cases insignificant,
3 let's say it is \$2,000 or \$3,000, but in the view of
4 the entity that has been fined this was a mistake.
5 It was wrong.

6 It is very expensive if you have to go
7 through a process, whether it is negotiation for a
8 settlement -- that takes legal time, it takes
9 technical staff time -- or go through due process at
10 FERC, NERC, and, God forbid, the courts.

11 It is just an issue we wanted to bring up.
12 We think this has a lot to do with the idea of
13 speeding up and streamlining this process, and we
14 hope that you will consider what we say here.

15 Finally, we would like to say another
16 thing. Kudos, if you will, to our friends at NERC
17 for their efforts, recent efforts, with regard to
18 lessons learned analyses and getting that
19 information out. That is critically important to
20 improve reliability, and we think that is the most
21 important thing we do.

22 With that, thank you very much.

23 COMMISSIONER LA FLEUR: Thank you,
24 Mr. Mohre.

25 Mr. DiStasio?

1 MR. DISTASIO: Thank you. Good afternoon,
2 Chairman Wellinghoff and commissioners. Thank you
3 for the opportunity to speak to you today. I am
4 John DiStasio. I am the manager and the CEO of the
5 Sacramento Municipal Utility District, "SMUD."

6 I am speaking today on behalf of SMUD but
7 also on behalf of the Large Public Power Council,
8 "LPPC." LPPC represents 24 of the largest municipal
9 and state-owned utilities in the nation. The
10 members are part of the public power community but
11 represent the larger asset-owning members of the
12 community.

13 Together LPPC members own approximately 90
14 percent of the transmission investment owned by
15 non-federal public power entities in the
16 United States.

17 The provision of reliable, reasonably
18 priced, electric service is the core business of the
19 LPPC. It is what we do. It is what our customers
20 expect.

21 To better ensure that we can continue to
22 meet this fundamental mission, LPPC supported the
23 provisions of Section 215 of the Federal Power Act
24 to make Reliability Standards mandatory nationwide.

25 Though we will always be looking for ways

1 to improve reliability, it bears no small emphasis
2 that we currently operate an extremely reliable
3 Bulk-Power System. This backdrop should not be
4 overlooked when we consider issues related to
5 enforcement and application of penalties.

6 I also believe that in determining
7 penalties we must not lose sight of the fact that
8 the Reliability Standards serve to prevent
9 catastrophic or cascading impacts to the
10 Bulk-Electric System, and enforcement should be
11 tailored to focus on these types of events.

12 We will all be better served from a
13 regulatory and enforcement regime that is
14 specifically right sized to the risk. My remarks
15 touch on the need to develop streamlined enforcement
16 processes so that appropriate emphasis can be placed
17 on those violations that pose the greatest risk to
18 reliability.

19 I also want to discuss some changes that
20 may be made in the application of the sanction
21 guidelines to better ensure that potential penalties
22 bear a reasonable relationship to the severity of
23 the violations.

24 Finally, I would like to outline the
25 importance of establishing an informal feedback loop

1 to clarify ambiguous standards and establish best
2 practices for compliance in a manner that does not
3 unreasonably penalize Registered Entities with a
4 demonstrated intent to comply.

5 In the three years since the establishment
6 of the mandatory Reliability Standards, the industry
7 has devoted unprecedented time and resources on
8 standards development and compliance.

9 In response to the Commission's policy
10 statements, many companies like SMUD have developed
11 robust internal compliance programs in order to
12 monitor the increasing number of Reliability
13 Standards and requirements. This heightened focus
14 on reliability benefits us all.

15 While we have accomplished much in the
16 past few years, we also face formidable challenges.
17 In particular, LPPC has grown increasingly concerned
18 with an enforcement and compliance process that
19 though well-intentioned is more cumbersome and
20 costly than it needs to be.

21 The sheer breadth and magnitude of the
22 Reliability Standards makes perfect compliance
23 impossible. Although great strides have been made
24 in reducing the amount of outstanding violations
25 waiting to be processed, the Regional Entities and

1 NERC continue to have compliance violation backlogs.

2 Part of the backlog may be attributed to
3 the number of self-reports being filed, especially
4 with the recent implementation of the CIP standards.
5 Significantly a large number of the violations are
6 documentation related and pose minimal risk to the
7 reliability of the Bulk-Power system.

8 However, the current compliance regime
9 gives too little recognition to the difference
10 between violations that do not threaten system
11 performance and those that do.

12 This causes significant time and scarce
13 resources to be squandered on inconsequential
14 violations and diverts attention from addressing
15 those violations that pose the real and significant
16 reliability risks.

17 To resolve this problem, NERC and the
18 Regional Entities must have the discretion to fast
19 track those violations that pose a minimal risk to
20 the reliability of the Bulk-Power System.

21 LPPC supports the concept of a traffic
22 ticket approach, as was mentioned before, under
23 which these types of violations would be handled in
24 an expedited fashion. This concept was discussed
25 favorably in the Commission's order on NERC's

1 three-year assessment.

2 Other documentation-related violations
3 that pose minimal risks to the Bulk-Power System
4 should be handled through the application of
5 baseline penalties in the order of a few thousand
6 dollars. These baseline penalties could increase
7 for repeat violations within a specified time
8 period.

9 I also believe the Regional Entities
10 should have the discretion to assess zero dollar
11 penalties for self-reported violations that pose no
12 or little or no risk to the Bul-Power System.

13 The Commission expressed some concern in the
14 three-year assessment that permitting a warning
15 ticket mechanism would not require that sufficient
16 attention be paid to a Regional Entity's compliance
17 history.

18 An entity's compliance history is
19 important, but NERC's current sanction guidelines by
20 permitting penalties without fines only for first
21 time violations and never afterward amounts to a
22 zero-tolerance policy that in the long run is
23 counterproductive.

24 I am confident that the industry
25 participants can work successfully with NERC to

1 develop a means of tracking and punishing cumulative
2 poor behavior without resorting to the unnecessarily
3 inflexible approach of the current guidelines.

4 To ensure consistency within the regions,
5 all baseline penalties should be developed jointly
6 between the Regional Entities and NERC. NERC should
7 also make a quarterly filing describing the types of
8 violations that it handled through the expedited
9 process instead of filing individual notices of
10 penalty similar to what it does for omnibus filings.
11 LPPC supports the expansion of a short-term
12 settlement established by NERC and by the Regional
13 Entities.

14 I would like to next address a few
15 comments on the matter of proportionality of the
16 potential penalties listed in the notice of alleged
17 violations and the penalties that are ultimately
18 assessed generally through settlement.

19 It has been LPPC's members' experience
20 that there is often a huge chasm between potential
21 penalties detailed in a NOAV and a settlement with a
22 Regional Entity. That gap seems often to us to
23 signify that the NOAV is out of proportion with what
24 the Regional Entity reasonably believes the
25 violation is worth.

1 The effect of the penalty stated in the
2 NOAV can be quite damaging. This is especially true
3 for a municipal utility seeking financing which must
4 report the potential liability even if the ultimate
5 result is not likely to be damaging.

6 The potential penalty may leave the
7 utility with little choice but to enter into a
8 settlement even if it generally believes it has
9 acted appropriately.

10 Our experience has been that for one
11 reason this lack of proportionality relates to the
12 manner in which the duration of a violation is taken
13 into account.

14 I should mention that I understand that
15 NERC has an understanding that this matter of
16 proportionality is something that reasonably should
17 be addressed and that discussions are underway
18 internally to come up with solutions.

19 I am not going to probably go a lot
20 further because I think I am getting short on time.
21 I just would like to add one additional point, and
22 that is, in the past several months NERC has
23 published lessons learned on its Web site.

24 I think we would reinforce the importance
25 of transparency and communication. We want to work

1 to ensure that timely information regarding system
2 events are circulated through the industry in a way
3 that they can become preventative in nature so that
4 others can learn from these experiences.

5 I would like to also press for an open
6 line of communication between NERC, the Regional
7 Entities, and the industry with respect to the
8 interpretation of standards more like what occurs
9 between Commission staff and industry partners.

10 We find oftentimes that while those
11 discussions are non-binding, they are valuable as
12 guidance for how to best comply with the orders of
13 the Commission.

14 Finally, I want to close in commenting
15 that I believe under Jerry Cauley's leadership NERC
16 is looking for ways to address many of the concerns
17 we are discussing today.

18 We believe that NERC is transitioning to
19 an organization that understands not only the
20 importance of vigorous enforcement where
21 appropriate, but also a sense of proportionality
22 between enforcement activity and penalties.

23 The key role of cooperation and
24 communication between NERC, the Regional Entities,
25 the industry, and FERC is improving reliability.

1 Thank you again for the opportunity to
2 speak today, and I will look forward to your
3 questions.

4 COMMISSIONER LA FLEUR: Thank you,
5 Mr. DiStasio.

6 Finally, Mr. Naumann.

7 MR. NAUMANN: Good afternoon and thank you
8 for inviting me to speak at this conference. I will
9 discuss two topics, processing of violations and
10 accounting for violations of affiliates.

11 In engineering school, I learned a
12 formula: input minus output equals accumulation.
13 That concept applies to filling a bathtub, to the
14 concentration of carbon dioxide in the atmosphere,
15 and to the processing of NERC violations.

16 Whether we call the difference between
17 input and output caseload or backlog, there is an
18 accumulation issue with NERC violations.

19 (PowerPoint presentation in progress.)

20 MR. NAUMANN: This chart shows the
21 cumulative difference between the violations that
22 come into the NERC process and those that are fully
23 processed, and by that I mean those that are
24 dismissed or filed with the Commission.

25 As you can see, there has been an

1 accumulation of over 1,100 violations since the
2 October 2009 omnibus filing, and the trend is
3 upward.

4 As you will recall, the purpose of the
5 omnibus filing was to clear the backlog. The theory
6 at that time was that the large number of violations
7 that had accumulated as the compliance and
8 enforcement program got its sea legs needed to be
9 addressed so that the program could achieve a steady
10 state.

11 But these data show that the program was
12 not simply that the program was young. It was that
13 the program needs to deal with the large number of
14 self-reports that Regional Entities themselves
15 detect in their review of compliance with new and
16 sometimes ambiguous standards aided by what they
17 learned from the filed notices of violations and
18 from NERC's compliance analysis reports.

19 There needs to be a process change. The
20 Commission recognized this and indicated that it
21 would be appropriate to develop a parking ticket or
22 speeding ticket approach for minor violations as
23 well as appropriate procedures for resolving purely
24 documentation-related violations. These processes
25 need to be developed now.

1 At the recent NERC Board of Trustees
2 Compliance Committee meeting, there was extensive
3 discussion as to how to implement a proposed
4 administrative citation process.

5 Questions on whether repeated violations
6 could be included, whether this was restricted to
7 new violations, and what "minimal risk to the
8 Bulk-Electric System" means were discussed.

9 While it appears that NERC is making
10 progress, these issues have not yet been resolved.
11 It seems that in the debate to ensure that this
12 process is strictly limited to only those violations
13 that will have a minimal risk to the Bulk-Electric
14 System, implementation is being delayed.

15 In my opinion, NERC can do this, and the
16 Commission should allow NERC to make it happen with
17 the goal of implementing this administrative
18 citation process by January 1st, 2011.

19 If there are imperfections, the process
20 can be adjusted along the way. There is no need for
21 micromanaging the process up front to ensure
22 perfection. Every month's delay means an
23 accumulation of several hundred more violations.

24 Another source of the accumulation is the
25 input, and you heard a little bit about that in the

1 first panel. Certainly, it is incumbent on the
2 industry to comply with the standards, but as the
3 Commission knows there are ambiguities in the
4 standards. Beyond that, there are interpretations
5 of what proof is needed for compliance.

6 Hypertechnical interpretation of
7 subjective words can unnecessarily add to the input
8 stream of violations. For example, Requirement 1.2
9 of CIP 003 requires the cybersecurity policy to be
10 "readily available."

11 If this is interpreted in an unreasonable
12 and subjective manner, individual audit teams' ideas
13 of what "readily available" means can increase the
14 violation streak. Does this really improve
15 reliability?

16 Finally, on the subject of repeated
17 violations as applied to affiliates, I would ask the
18 Commission to understand that what may appear to be
19 different and thus repeated violations by affiliates
20 are often actually the same violation that was
21 uncovered as part of a corporatewide extent of
22 condition analysis based on discovery of a violation
23 in one of the affiliated entities.

24 If these violations are uncovered as part
25 of a corporate-wide analysis, they should not be

1 considered multiple violations or an aggregating
2 factor that increases penalties rather NERC, the
3 Regional Entities, and the Commission should support
4 such actions as a step toward increasing reliability
5 in an efficient manner.

6 The fact that some organizations have many
7 affiliated entities should not result in worse
8 treatment than if they were organized into a single
9 integrated entity registered with NERC as one
10 registered entity.

11 Thank you and I welcome any questions.

12 COMMISSIONER LA FLEUR: Well, thank you
13 very much, Mr. Naumann.

14 Pretty clear messages coming from all of
15 you, and I guess it is our turn to respond, starting
16 with the Chairman.

17 CHAIRMAN WELLINGHOFF: Do we have a theme
18 here?

19 (General laughter.)

20 CHAIRMAN WELLINGHOFF: I guess, Gerry, you
21 are on the hot seat. The question of the hour is:
22 How fast can we put the traffic ticket system in
23 place? What have we got to do to get there? How
24 can we as a Commission or our staff help you do
25 that? What can we do to move there?

1 Because everybody wants to move there. I
2 think my fellow commissioners do, and I certainly
3 do. We all recognize that that is one thing we need
4 to do, as was so aptly stated by a number of
5 panelists here, that we need to set up a system
6 where we don't treat all violations the same, that
7 we have got some kind of a more functionally and
8 administratively easy process that can be used for
9 these lower-level violations so we can stop all of
10 the resources going each one of these things even
11 though they shouldn't all be treated equally.

12 What do we need to do to get there by, as
13 I think was suggested by Mr. Naumann, January 1st,
14 2011?

15 MR. CAULEY: Thank you, Mr. Chairman. We
16 are shooting for January but not the first.

17 CHAIRMAN WELLINGHOFF: Of 2011, though?

18 (General laughter.)

19 MR. CAULEY: Of 2011.

20 CHAIRMAN WELLINGHOFF: Because we know
21 also we have to define our terms here. We have been
22 told that.

23 MR. CAULEY: There has been a long history
24 on trying to get the record and the workload for
25 violations skinnyed down to being appropriate. It

1 was probably a year and a half ago we first launched
2 a program to come up with a short-form settlement.

3 By the time we finished all of the
4 negotiations about what the criteria and when would
5 it work and how would it fit and how would it be
6 used, the short form wasn't really very short.

7 We had another effort which I think was
8 more successful this year, which was the abbreviated
9 NOP, which basically puts the filing of the record
10 in a standardized format. It is sort of fill out
11 the box. It is easier to get to, and it is a little
12 quicker.

13 I have always through that whole process
14 thought that for some of the simplest violations,
15 the record should fit on one piece of paper, one
16 sheet. I have not given up on that goal.

17 We have had some discussions with the
18 enforcement staff and the reliability staff here,
19 and I think we have an agreement on what this
20 administrative citation looks like.

21 We are looking to bring a number of those,
22 probably on the order of close to a hundred but I
23 don't want to quote that number exactly, a good
24 number of them to our Board's Compliance Committee
25 meeting in January and file them shortly after that.

1 We are ramping this up. I think it is
2 very promising if this takes, and we do certainly
3 need the Commission's help on this in terms of did
4 we get it right.

5 My judgment, without also not holding me
6 to numbers but my intuitive instinct, is that we
7 should be able to treat half of our violations with
8 this one-page citation.

9 CHAIRMAN WELLINGHOFF: I will certainly
10 commit to you our support in any way possible and
11 turnaround as quickly as possible either from the
12 Commission and/or our staff to get this process in
13 place because I think we are all anxiously,
14 obviously, awaiting this.

15 The only other area I have is just a
16 comment on, Mr. Fehrman, some of the things you
17 talked about on the North American Transmission
18 Forum. I am glad for the update and the information
19 you provided.

20 I am very supportive, as Commissioner
21 Moeller mentioned with the last panel, of this new
22 process. Anything we can do as a Commission to
23 support you and our staff with respect to that
24 effort on the North American Transmission Forum,
25 please let us know.

1 MR. FEHRMAN: Yes, thank you,
2 Mr. Chairman. The forum held a held a very
3 comprehensive strategic planning session just a
4 couple of weeks ago on how to move the forum further
5 along in the good things that they already do.

6 With the Commission's help and support, I
7 think that the forum will really pay off dividends
8 as time goes on. We are excited that, including
9 ourself, more of the industry has become involved in
10 the forum. In fact, just over the past couple of
11 months, the membership has grown significantly.

12 CHAIRMAN WELLINGHOFF: I notice you have
13 some interesting sort of anomalies in your
14 membership. You don't have a lot of people in the
15 West for some reason. Is there some reason for
16 that?

17 MR. FEHRMAN: I am not sure. PacifiCorp
18 just joined as a part of us.

19 CHAIRMAN WELLINGHOFF: Oh, they did?
20 Okay, so that is going to take care of it, okay.

21 MR. FEHRMAN: Absolutely. That
22 fundamentally takes care of the West.

23 (General laughter.)

24 CHAIRMAN WELLINGHOFF: There are a few
25 other folks, Arizona and New Mexico.

1 MR. FEHRMAN: The part of the West that I
2 care about.

3 COMMISSIONER LA FLEUR: PacifiCorp has a
4 big chunk of that upper Northwest section.

5 MR. FEHRMAN: Yes.

6 CHAIRMAN WELLINGHOFF: That is very true.
7 Well, thank you for that information.

8 Thank you, Commissioner La Fleur. I don't
9 have anything further.

10 COMMISSIONER LA FLEUR: Thank you.

11 Commissioner Moeller?

12 COMMISSIONER MOELLER: Thank you,
13 Commissioner.

14 I have spent time with all of you,
15 sometimes significant time, over the last few years
16 dealing with these issues. Again, a great panel.
17 Thank you for being here.

18 I won't beat the horse too much more.
19 Stacy, first of all, than you for hosting me and
20 Rob Ivanauskas of my staff in Little Rock in
21 September. I think you are getting Commissioner
22 La Fleur there, too, for one of your quarterly
23 Regional Entities stakeholder meetings.

24 Although I was asked some difficult
25 questions, I appreciated the chance to be there. I

1 don't know if all the RE's do that, but it certainly
2 seemed like a good forum to air concerns of the
3 entities within the RE.

4 Did I hear you right that of your staff
5 allocation essentially it takes a person on average
6 -- they go through 12 a year of violations?

7 MS. DOCHODA: Currently, that is correct.

8 COMMISSIONER MOELLER: Essentially, that
9 is on average a month's time per violation?

10 MS. DOCHODA: That is correct.

11 COMMISSIONER MOELLER: That is some
12 significant cost even just for you, not just the
13 entity. Even if it is a zero-dollar violation,
14 there is still a lot of cost involved there.

15 MS. DOCHODA: Right. I guess I would add
16 to that that at least in the early days I think
17 sometimes it took more to process a zero-dollar
18 penalty than a non-zero dollar penalty because we
19 had to justify it in more detail.

20 Even though we have made significant
21 strides, as Mr. Cauley referred to, this past year
22 the processes have improved quite a bit. bit it is
23 just at the rate that it is coming in, it is as if
24 we have a fire outside and we have brought out a cup
25 of water to it. We are going to have to approach it

1 in a more expeditious way.

2 I think the administrative citation
3 suggestion is one that I am very excited about. I
4 think that it could be that step change that we
5 need, but I will make one comment.

6 As it is currently devised, the suggestion
7 is that it would require that the registered entity
8 admit to the violation.

9 There is a processing issue that I
10 struggle with there, and that is, if the entity
11 admits to the violation at the Regional Entity level
12 but that is not yet a final determination as to
13 whether the penalty is going to be accepted, and
14 then it goes to NERC or FERC and is changed, I think
15 it could be really difficult for us to process the
16 number of violations we would like process, if we do
17 require an admission at that NS process. I think I
18 would like to see us consider a neither admit nor
19 deny or a no contest type of approach.

20 COMMISSIONER MOELLER: Okay. Thank you.

21 Well, again, I appreciate all of your
22 testimony, the detailed nature of it, and the fact
23 that you are here today.

24 COMMISSIONER LA FLEUR: Thank you.

25 Commissioner Spitzer?

1 COMMISSIONER SPITZER: Thank you.

2 Certainly I am not one to break the
3 consensus on this concept of bifurcation with
4 respect to severity so the resources go where there
5 is a potential for harm and not where the effect on
6 our liability is trivial.

7 Let me share with you maybe a conceptual
8 framework because the devil is in the details is at
9 going to be drawing that line.

10 You have got the subsidiary issue, which I
11 think is very significant you raised, Stacy, with
12 respect to the admission of a violation which not
13 just with public entities, but, as Mr. DiStasio
14 pointed out with municipal, may carry some economic,
15 political, or other consequences attached to an
16 admission of any type may be problematic.

17 In some discussions I had with my own
18 legal advisors, and I shared the discussion I
19 believe with Mr. Bay of enforcement and with my
20 colleagues, which is a conceptual distinction
21 between an "amnesty" and "forbearance." They are
22 very different considerations.

23 An "amnesty" is a recognition of wrongful
24 conduct, but for reasons either of government
25 efficiency or cost savings or simply we don't want

1 to be bothered, there is a declaration that
2 notwithstanding the wrongful conduct we are going to
3 absolve culpability.

4 The second is "forbearance," which is a
5 different concept, which is there may have been a
6 violation but for reasons not of simply convenience,
7 and this is what I think you are getting to when
8 you, David, said "We don't want to impose penalties
9 where the issue was, I think you used the word,
10 "trivial."

11 A triviality is subject and appropriate
12 for forbearance. That is a very different concept
13 than an amnesty. Maybe this is helpful, maybe not,
14 but I would like the reactions.

15 At some point if we are going to implement
16 the proposal, Mr. Cauley, with the support of the
17 stakeholders and with the support of the Commission,
18 it is going to have to, I think, end up on the side
19 of which of these notices of penalty -- let's start
20 with the self-reports, just for the sake of
21 argument, self-reporting, as opposed to an audit
22 finding.

23 Which self-reports are those where the
24 government and the ERO ought to forebear from
25 further action as opposed to an amnesty? I don't

1 think that is what you intend. How would you maybe
2 respond to this demarcation line?

3 MR. CAULEY: That is a very good question,
4 Commissioner Spitzer. A principle we are trying to
5 get to is how do we reinforce the right behaviors.
6 I think on the first panel there was a suggestion
7 about the proper effective controls because we are
8 all about trying to fix things and improve
9 reliability.

10 I look at the case where the entity has
11 the reverse program and is self-assessing and
12 self-reports. In some cases, the volume of those
13 self-reports is repeated, but it is because of a
14 good program.

15 In MISCE I want to reward good strong
16 controls and a good ethic in terms of
17 self-reporting, and that seems to be lining up with
18 your definition of forbearance.

19 I want to send positive signals, and I
20 want to send them widely so other people get the
21 same message and start acting with those same
22 behaviors.

23 COMMISSIONER SPITZER: An amnesty of
24 course is the absence of a sanction or the
25 exculpation of wrongful conduct not connected with

1 internal controls, but because government is too
2 busy?

3 MR. CAULEY: I think my opinion is we
4 don't really need amnesty, per se, but we need what
5 I just described as a concept of forbearance in
6 terms of rewarding positive behaviors.

7 The other thing we need to do is just
8 prioritize our work and our activities. If we have
9 3,000 things we are going after, it seems like we
10 should be prosecuting the ones that are most
11 important.

12 Maybe three years from now, when all of
13 the big things are taken care of, we will be looking
14 at a different level of things, which not to me is
15 amnesty, but it is which ones are we going to pursue
16 now in front of us to help prioritize some of the
17 work. It doesn't mean you are off the hook forever,
18 but it means I have bigger fish to fry right now in
19 terms of improving reliability.

20 COMMISSIONER SPITZER: Any other reactions
21 to this? Dave?

22 MR. MOHRE: I don't usually negotiate with
23 myself.

24 (General laughter.)

25 MR. MOHRE: I think I agree with Gerry on

1 the forbearance for actually another reason.
2 Although the issue of repeated trivial violations is
3 a tough one sometimes, you can have people of bad
4 attitude that keep doing the same trivial things
5 over and over again, and forbearance makes sense
6 there and that can accumulate to something
7 significant, if you catch my drift. If you have
8 amnesty, of course you wouldn't have that.

9 COMMISSIONER SPITZER: Yes.

10 MR. MOHRE: I would just like to add to
11 the point of self-reporting I think the way we have
12 approached that is that is that is a way for us to
13 demonstrate a culture of compliance by providing a
14 certain evidence of rigor for our own self-audits.
15 In fact, I think it is important that that
16 continues.

17 Now, obviously if an entity were to
18 continue to self-report the same type of thing over
19 and over, it might end up having a diminishing
20 benefit.

21 But I do think that having rigorous
22 self-reporting by the Registered Entities I think is
23 important and should be encouraged because it is a
24 key part of our learning to have that information
25 out there.

1 MS. DOCHODA: I would just like to add
2 that I think the importance of mitigation is also
3 something we have to incorporate into whether it is
4 forbearance or amnesty. I always want to close
5 whatever gap there is, so I really want to
6 concentrate my effort on the mitigation and bring
7 that into play.

8 To me for an example of a category that
9 could fit into either of these, I think we have a
10 number of standards where just from what I can see
11 in the field there is a lack of understanding about
12 what is required. What is the difference between an
13 "incident plan" and a "recovery plan"?

14 When you see common things that company
15 after company have struggled with to be able to get
16 exactly right, I think that the most important thing
17 is that they take their plans and get them right.
18 But to assess violations on them when they are so
19 common, I think is not particularly productive.

20 MR. MOHRE: Okay. I guess one more issue
21 to raise is this question of in one of the topics:
22 "Do the current -- processes provide approaches and
23 improve reliability by reducing future Reliability
24 Standard violations and system disturbances."

25 To me that is original entities have cases

1 that come before them, and so an awful lot of time
2 is spent putting out fires. The utilities, you have
3 matters that come before you, and it is putting out
4 fires.

5 What collectively can we do to engage in
6 the long-term thinking and planning necessary to be
7 proactive in light of the pressure that we are all
8 under with regard to putting out fires on a daily
9 basis? It is a challenge to us all really.

10 I will try that first, if I may. I think
11 that David mentioned something that really resonates
12 with me early in his comments, and that is, that to
13 the degree that we are spending a lot of time or
14 working with the entities on very trivial matters, I
15 do think it hurts our credibility in terms of what
16 we are really trying to accomplish.

17 I think to the degree that we are really
18 working with Regional Entities and we are focusing
19 on the things that really impact their liability, I
20 think that that will also enhance our ability to
21 work with those entities to improve reliability
22 going forward whether it is an event analysis or
23 other assessments that we do with the entities.

24 COMMISSIONER SPITZER: Steve?

25 MR. NAUMANN: I think there are two

1 things. First, to take a step back and prioritize
2 which things are really, really important to the
3 reliability of the Bulk-Electric System.

4 As I think we heard this morning, if you
5 had a list of eight, very quickly we could probably
6 agree on the first five or six without much argument
7 and maybe a little disagreement on the bottom two.
8 Because that is where the emphasis should be.

9 The second is education. Under Gerry's
10 leadership, that has started to turn around. But
11 from my view in the industry, it is not happening
12 fast enough. That may well be because the input
13 stream is coming in pretty fast.

14 There are, I don't know, about seven or
15 eight of these compliance analysis reports to date,
16 and there are a lot more standards out there than
17 seven or eight.

18 They kind of need to get ahead of the
19 curve. That is difficult because you have a plan
20 and then now all of a sudden the CIP standards are
21 coming and you have got to kind of turn on a dime
22 and say, "Well, I've got to analyze those."

23 I think more information, more analysis,
24 and a deeper dive into what the real problem is, and
25 the real problem is not necessarily the fever, for

1 example, it is what is causing the fever. That is a
2 change in emphasis. I know Gerry has only been on
3 the job 11 months, and it takes a little time to get
4 there, but I think you need to do that. The same
5 thing with the event analysis reports.

6 Again, that is now going through a change
7 in process, but we in the industry have clearly not
8 been seeing that in any kind of timely manner.
9 There are reasons we have been told that they are
10 confidential, there is confidential information in
11 them, we can't see them, they are protected, they
12 contain critical energy infrastructure information.
13 Well, we deal with critical infrastructure
14 information all the time, so I find it hard to
15 understand why our people who have some of the most
16 confidential data to understand on their own what
17 has happened. There are some of these events that
18 are three years old that we still do not have the
19 reports. Again, I think that is changing with the
20 new processes, but the more info we get about what
21 the problems are, we can take action on that. That
22 is the real improvement in reliability.

23 COMMISSIONER SPITZER: I would agree that
24 Mr. Cauley is moving away from the putting out of
25 fires to long-range planning that is what is needed.

1 I thank you for that.

2 Thank you.

3 COMMISSIONER LA FLEUR: Thank you.

4 Commissioner Norris?

5 COMMISSIONER NORRIS: A followup to what
6 Commissioner Spitzer was talking about and several
7 of the commissioners with regard to the no action
8 letter or the traffic ticket.

9 I probably shouldn't ask this I know. In
10 those submissions of self-reports or even someone
11 who has been called for a violation, do they ever
12 request to submit their own recommendations for a
13 penalty?

14 MR. CAULEY: Well, I think in most cases
15 the entity does submit their own recommendation, but
16 usually there is some negotiation and haggling,
17 because it is pretty much a settlement process.

18 The vast majority of our violations are
19 treated through settlements. Typically, the region
20 will come in with a proposal and the entity will
21 have a proposal, then there will be some
22 negotiation.

23 COMMISSIONER NORRIS: The entities will
24 generally propose it first?

25 MR. CAULEY: Yes. I think in the

1 administrative citation I wouldn't rule out that
2 that is there, but what we want to avoid is an
3 extended months' long negotiation over that, because
4 it sort of defeats the purpose.

5 As long as it was an expedited discussion,
6 I think that would be -- my sense is I worked in a
7 region for a while, and we are always willing to
8 listen and hear proposals and issues and things like
9 that, so I think that would still continue.

10 MR. NAUMANN: Just in our experience and
11 maybe in different regions, the region proposes a
12 penalty first and then the entity responds to that.

13 COMMISSIONER NORRIS: Okay. I am just
14 curious. Sometimes asking someone to propose the
15 penalty gives you some sense of their recognition,
16 or lack thereof of, of the severity of the
17 violation. If that is a shortcut to getting the
18 resolution, perhaps it is one to think about.

19 Mr. DiStasio, you mentioned that you had
20 some concerns about the NERC Sanctioning Guidelines.
21 I am just curious about if you have, you or any of
22 the other panelists have, other thoughts or ideas on
23 additional changes or how to make them work better?

24 MR. DISTASIO: I think one of the things
25 that we have experienced I think in discussions with

1 my colleagues that have had similar circumstances
2 where the sanction guidelines apply to penalties on
3 a day-to-day basis until there is a mitigation
4 completed.

5 We could have a circumstance where we may
6 have missed a reporting requirement by five minutes.
7 We have a daily load report, and we have to report
8 that every day. If we miss it one time for five
9 minutes and we are compliant every day thereafter,
10 but the clock continues to run, the sanction
11 guidelines end up getting applied in the totality of
12 that whole time until the mitigation is completed,
13 which could be a significant number.

14 It might be material enough in some cases,
15 as I mentioned, that we would have to disclose that
16 if we were in the midst of a financing or something
17 even though at the end of the process it may
18 ultimately be a very small amount we ultimately end
19 up getting assessed.

20 The application of the sanction
21 guidelines, I think we just need to take a look at
22 how those get complied initially, because sometimes
23 in our case we have found they don't bear a
24 significant resemblance to what we ultimately end up
25 paying on that issue even if it doesn't go through

1 settlement.

2 MR. NAUMANN: I think a tangible example
3 would be you have a system protection device that is
4 supposed to be tested on a five-year interval, and
5 we are now over a thousand days past June 18th,
6 2007.

7 If it were to come up now and with a
8 minimum fine of \$3,000 a day, you are facing for one
9 device a possible fine of \$3 million because it has
10 been unmitigated for a thousand days. One can argue
11 whether the system has been really in danger
12 \$3 million worth, but I think that is the kind of
13 thing that is a concern.

14 MR. CAULEY: Thank you, Commissioner. The
15 per-day accumulation is something that was clearly
16 directed by the Commission and it is sort of part of
17 the thinking in the background, but I think in every
18 instance that I am aware of there is a lot of
19 pragmatism and realism applied to that. It is not
20 that we just take \$3,000 and multiply it by
21 550 days.

22 If there are instances where somebody is
23 providing the maximum credible numbers as the number
24 put on the table, I would like to hear those case
25 because I don't think that would be consistent with

1 our approach. The approach that we have would be
2 that the regions and anyone in negotiation should
3 put down their realistic number in terms of what the
4 value of that penalty should be as an initial
5 proposal but not maximum theoretical for the very
6 reasons that we heard today.

7 If we were being impractical about this,
8 we would have had a lot more \$5 million,
9 \$10 million, \$30 million penalties by now. The
10 larger numbers are very rare, and I think that is an
11 indication of the realistic and pragmatic approaches
12 being taken in the regions. We will look into it,
13 but if there are cases, we would like to know about
14 that.

15 COMMISSIONER NORRIS: Thank you.

16 COMMISSIONER LA FLEUR: Thank you very
17 much.

18 Well, I have a couple of questions that
19 are somewhat broad. A lot of the theme of what
20 everyone has said has really kind of revolved around
21 work on the big things, less on the little things
22 with which it is impossible to disagree. In fact, I
23 have made no secret I think we need to focus on our
24 priorities in this process.

25 Just to kind of push at that for a minute,

1 there is a well-known phenomenon. I am sure a lot
2 of you are aware of the "safety pyramid" where there
3 is, say, like an occupational safety. For every so
4 many times you do a little thing wrong, a big thing
5 is going to happen.

6 For every time you don't wear your
7 seatbelt, one in every so many times there will be a
8 fatality or whatever. This is the same phenomenon
9 Commissioner Spitzer was talking about, the people
10 who have terrible documentation and maybe other
11 things are wrong, too.

12 Obviously to make the system work, we are
13 going to have to batch the process and streamline.
14 It is obvious from the figures, but is there some
15 way that we can get lessons from those little things
16 or from leading indicators that might not be the top
17 five things that Steve Naumann talked about?

18 Is there some way we can get the lessons
19 of whether there is a -- I don't know whether it is
20 a system audit where you look at the overall how a
21 compliance system is going or whether you do
22 trending, so we don't just in our focusing on the
23 big things lose stuff that might prevent a big thing
24 in the future? It is a pretty general question, but
25 I would appreciate any thoughts.

1 MR. FEHRMAN: I appreciate the question,
2 Commissioner. I think that I spent a considerable
3 amount of my career in the nuclear power industry,
4 and the issue you just raised is exactly why the
5 nuclear power industry continues to get safer and
6 safer every year.

7 The problem identification and resolution
8 process, which is the underlying foundation of
9 everything you just talked about, is really what
10 gets focused on when auditors come in from either
11 MPO or from NRC.

12 We spend a considerable amount of time in
13 this forum and other forums talking about the
14 sanctions and the other amount of money, and I don't
15 think spend a fair amount of time talking about the
16 underlying process that needs to be put into place
17 at utilities such that it forms a very robust
18 mechanism for identifying what the problems are and
19 then correcting them.

20 To your point exactly, particularly in the
21 nuclear power field, as you look at trends through
22 the problem identification and resolution process,
23 you will find those things that will continue to pop
24 up and drive you to make risk-based decisions.

25 I think the same applies to this business

1 of reliability. When we look at opportunities for
2 developing processes and procedures, it would be my
3 hope that we spend a lot more time when people come
4 see us challenging the veracity of my problem
5 identification and resolution.

6 That is where when I find issues I report
7 them and identify them, and you look at those to
8 decide whether or not they really should have been
9 reported.

10 NRC has a very comprehensive way of
11 putting the severity on an issue. I just think
12 there is a lot to learn from that that has reaped
13 benefits over time that can be applied in this area
14 and do exactly what it is you are hoping and asking
15 us to do.

16 COMMISSIONER LA FLEUR: Thank you.

17 MR. CAULEY: Yes, Commissioner, I also
18 came out of the nuclear industry, and I think
19 perhaps that is sort of what drives the vision of
20 where we are trying to get in terms of risk-based
21 and fixing and correcting things because I ascribe
22 to that same thinking.

23 But I think your point, we have heard a
24 lot today about important standards and unimportant
25 violations and important violations, the approach we

1 need to take is really a defense in depth and
2 preventive barriers to bad things happening.

3 I don't write off entirely that some
4 little violations, they can be symptoms of things.
5 They can be symptoms of larger things. They can be
6 symptoms of breakdowns in checks and balances of
7 controls. We need to get the response
8 proportionate. We need to be able to read the signs
9 of what is this telling us and then take corrective
10 action.

11 I go back to the point earlier as if we
12 could establish good measures of: What is a good
13 system of controls, checks and controls, to make
14 sure that things are being identified and corrected
15 and made non-repeatable to the extent we can?

16 At some companies, you have a standard and
17 you maintain your relay and document it in a certain
18 way. But if you have 25,000 of those, statistically
19 it is impossible to not to have an error.

20 But if you have a very robust program for
21 measuring and capturing those things, and you have a
22 way to capture even the most minor discretion in
23 terms of whether their signature was a day late or
24 not and be able to correct that and sort of loop
25 back and fix that, those are really strong programs

1 that we need to build off of.

2 The other area that a couple of people
3 mentioned, a couple of panelists mentioned, is the
4 Event Analysis Program. It is new. If I could have
5 written it myself, it would have been out back in
6 March, but it has taken a lot of work and
7 consensus-building and getting buy in from the
8 industry.

9 I think it is going to be a cornerstone of
10 getting us focused on the important things, because
11 we are going to look at events, why they are
12 happening, do the root cause, and bubble that back
13 into what can we do to fix the standard, what things
14 will be focused on in compliance.

15 Are the barriers we think we have in place
16 from catastrophes happening, are they really
17 working, or are they not working? How do we really
18 fix that? We are depending on the industry to not
19 be a victim in this, but to be a participant and
20 part of the process to help us get there.

21 I think it is a very similar model that
22 has worked well in the safety record in the nuclear
23 arena for the last 15 years, and we are going to
24 emulate that.

25 COMMISSIONER LA FLEUR: Thank you for

1 those very thoughtful answers. I mean, again, I am
2 not saying that every little documentation has to
3 treated like a big vegetation management problem
4 that leads to an enormous outage, but somehow we
5 can't lose in whatever process we design, lose those
6 lessons that you can get from the trending just as
7 you both spoke of.

8 I am kind of debating with myself whether
9 to ask my last question, but I can't resist because
10 of the expertise I see sitting out there. You kind
11 of teased it up with your last reference to "event
12 analysis" because it has kind of been in the back of
13 my mind.

14 There is kind of an old saying that "What
15 is good about something and what is bad about
16 something is always the same."

17 What is so great about our reliability
18 process is how broad-based it is, and how much
19 buying you have, and how everything goes to so many
20 sectors and gets debated, gets vetted, then gets
21 voted and revoted, and comes to the Commission where
22 we consider it carefully and do it so enormously
23 comprehensively and all.

24 But that is is one of the challenges of
25 the program is just how long it takes to get

1 standards out or get the new traffic ticket design,
2 system designer, get the event analysis out the
3 door.

4 Without losing the input, I mean, is there
5 anything -- you guys have been at this a long time
6 -- that we can do to make this faster? I mean, is
7 the forum the answer? Go behind closed doors and
8 get it done? Or, is there an answer that we can
9 start helping with? Just an easy question at
10 4 o'clock in the afternoon.

11 (General laughter.)

12 MR. CAULEY: Yes, it is an easy question I
13 will take. Well, first off, I have been doing
14 consensus or consensus type things at EPRI and NERC
15 and the region. I have been doing that kind of
16 thing for 25 years.

17 I actually feel there is a tremendous
18 value in getting consensus through a broad-based
19 process. It is tougher, and it is more challenging,
20 but at the same time, almost every hard thing I
21 wanted to do in my career I think got done.
22 Sometimes it is harder, and it just takes longer.

23 My particular frustration now is in the
24 standards, in getting those moved along. I am ready
25 at this point to say maybe we need to relook at how

1 we do the process, that maybe we do take standards
2 crafting offline in some process where it is open
3 and experts can get involved, but we don't encumber
4 the whole development process through our comments,
5 balloting, iterations, and so on, and save that for
6 the end where all the stakeholders get their vote.

7 They all have to be able to comment. They
8 all have to be able to. I think we need to look at
9 different ways to break through out of the box just
10 different ways to think about how we do things.

11 Also, I want to try to loop back to a
12 prior comment, but in the regions, the resourcing
13 and getting the work done, we started out thinking
14 every violation had to be a negotiation and
15 settlement of a contract.

16 If one little signature was missing, a
17 zero-dollar or a \$1,000 penalty we devote months of
18 lawyers and technical staff to produce a \$1,000
19 contract.

20 We have to break out of that mentality and
21 that cycle and start thinking about not just the
22 administrative citation, but how do we just rethink
23 our work, and how do we get things done.

24 My answer is yes and no. Yes, I do
25 relish the input and the due process, but in certain

1 areas we have got to break down some of these
2 barriers and get moving.

3 COMMISSIONER LA FLEUR: Mr. Naumann has
4 the answer.

5 (General laughter.)

6 MR. NAUMANN: No, I don't. Well, I don't.
7 Obviously, it's pretty hard to have the answer.
8 Coming back to this panel on compliance and
9 enforcement, I think NERC needs a little bit of room
10 to make mistakes.

11 We all make mistakes. We are not perfect.
12 NERC may send up out of 400 violations 2 that
13 somebody in retrospect says shouldn't have used the
14 short form.

15 The response shouldn't be the hammer that
16 "You did it wrong" because I think as Stacy said you
17 get a directive and now the 400 others that are
18 almost at the end of the process have to all be
19 looked at one by one. That, to use the bathtub
20 analogy, puts the stopper in the bathtub and you now
21 have the accumulation.

22 NERC should have the feeling that they can
23 be almost perfect. But if there is something that
24 there is a reasonable disagreement with, that it can
25 be handled in a different way.

1 Because I think the standard still is when
2 it comes up in reliability, it is still just and
3 reasonable. Reasonable, I don't think there is one
4 definition -- in law school, the judge gives the
5 charge to the jury of a "reasonable person," and the
6 jurors ask, "What does that mean?" A reasonable
7 person is a reasonable person.

8 I think to give them a little leeway, I
9 think they will come to right answer. As we all
10 acknowledge, the jury has got a new team in place.
11 They have made progress in a number of areas, and I
12 think that is how they could be supported in the
13 compliance and enforcemtn program.

14 MR. FEHRMAN: I would like to touch on the
15 forum very briefly. First of all, I think the forum
16 prior to it becoming very relevant was doing
17 outstanding work, albeit they were doing it amongst
18 the utilities that were in there, and the programs
19 and processes that they had were very robust.

20 Since a few months ago, the relevance of
21 the forum has grown tremendously, and people see the
22 value of the forum. I give Gerry credit. He has
23 shown tremendous leadership with regards to trying
24 to bring the forum and NERC together.

25 In fact, I was at a meeting where Gerry

1 basically stood up in front of the board of the
2 forum and said, "Tell me all of your issues, and
3 let's work on them." That is a very positive, a
4 very powerful message for Gerry to do and come to
5 the forum.

6 Specifically to your specific question, I
7 think that as the forum grows in its relevance the
8 fact that the membership of the forum now is getting
9 to be such a broad base that using it as a way to
10 vet a number of these things I think will become
11 more and more possible and will occur over a period
12 of time as it matures.

13 I think that having that will save a lot
14 of time and effort because arguments can be done
15 there, and then hopefully from there it can
16 transcend into the NERC process.

17 Whether it stays the same or if Gerry
18 modifies it in some way, I think that having that
19 ability will be very powerful for the industry to
20 use.

21 MR. DISTASIO: I was just going to just
22 add on to that. I know several of the LPPC members
23 are part of the forum, including Los Angeles in the
24 West as well.

25 I know for me I think education and the

1 more that we can have the ability to talk about
2 things that increase a common understanding of what
3 is necessary to be compliant and to improve our
4 compliance over time, I think that is going to be
5 helpful.

6 I mean, I think the compliance action
7 notices are helpful and the event analyses are
8 helpful, but sometimes those are corrective after
9 the fact.

10 We need to have places where we can
11 communicate in advance. Without undermining the
12 compliance efforts, we need to have places where we
13 can talk about what should best practice look like.

14 Then, the only other thing I would say is
15 we are taking responsibility from the industry.
16 LPPC has just finalized an action plan to get
17 greater CEO engagement in the balloting process, so
18 that in standards development we take some
19 responsibility to move those along with our staffs,
20 because believe it or not we have sometimes a fair
21 amount of disagreement amongst technical people even
22 within our own organization. We need to do a better
23 job pulling that together. We have made a
24 commitment on LPPC's behalf to do that.

25 COMMISSIONER LA FLEUR: Thank you.

1 Mr. Mohre?

2 MR. MOHRE: I feel compelled at this point
3 to just mention a couple of things. One is and
4 certainly -- how do I say this? The consensus
5 process as Gerry described is sometimes slow, slower
6 than we would like it to be, but it is also very,
7 very useful and productive in that sense that it
8 allows time for industry buy in of both the process
9 and the product.

10 Also, I don't want to get into -- I have
11 to say it straight out. It also is sort of
12 consistent. If you read the legislative history of
13 215, you will see it right there, okay, the industry
14 (chuckling), the expertise of the industry balanced
15 with the FERC approval process and ultimate
16 authority there and balanced with the ERO.

17 It is important that we keep in the back
18 of our minds that that buy in takes some time, but
19 is very important and is consistent with at least
20 the legislative history and I think the plain
21 meaning.

22 But it is also true when we need to do
23 something quick, we have a FERC-approved process
24 called the "urgent action process" that will allow
25 standards to be developed very, very quickly. There

1 is also an immediate process.

2 Gerry, I have forgotten the name of it.

3 God help me. I will be punished.

4 There are processes to do it. Can we find
5 ways to facilitate this? Sure, we can find ways to
6 do that, but I also think we have to remember some
7 of these foundational issues, too.

8 Thank you.

9 COMMISSIONER LA FLEUR: Well, thank you
10 for all those comments. I certainly take your point
11 on the legislative history. We are just trying to,
12 I think, all of us find ways to uphold the purpose
13 of the legislation, which at bottom was reliability
14 in the best way that we can.

15 With that, I think I have asked enough
16 questions. We will go to closing statements.

17 Mr. Wellinghoff?

18 CHAIRMAN WELLINGHOFF: I want to just
19 thank all of the panelists on this panel and the
20 earlier panel as well. The willingness of
21 everybody --

22 MR. BAY: Excuse me, Mr. Chairman. I think
23 this is actually time for questions from the
24 audience.

25 CHAIRMAN WELLINGHOFF: Okay. We can do

1 that.

2 COMMISSIONER LA FLEUR: Sorry, Norman, I
3 screwed up my thing. Okay. I guess now we are
4 going to do the questions from the audience. I'm
5 sorry.

6 THOMAS POPICK: Hello. My name is Thomas
7 Popick (phonetic). I come here today as a member of
8 the public. I represent only myself. I don't work
9 for the electric power industry.

10 I have already been cautioned that my
11 question today might be inappropriate, but I would
12 just like to say if this really is open to the
13 public, I think we need to be able to ask questions.

14 My question is what the electric power
15 industry is doing to protect against catastrophic
16 events like solar flares. I want to say at the
17 outset I would like to express my appreciation for
18 what the commissioners recently did in releasing a
19 report about so-called high-impact, low-frequency
20 events.

21 My understanding is that events of this
22 kind could collapse the North American power Grids
23 and could result in the end of the United States as
24 a nation.

25 I want to say this isn't just my opinion.

1 I recently attended a conference at the Army War
2 College where many of the attendees took this
3 position.

4 I would like to say something else, too.
5 This is really disturbing to me. In my everyday
6 life I run across people who are storing large
7 quantities of food and water to protect against the
8 power grid failing.

9 I understand that there is actually a
10 technical solution for this. As a matter of fact, I
11 have talked to one of the world's foremost experts,
12 who is here in the room today, who says that this
13 can be protected against at moderate cost.

14 My question, and I am just going to put it
15 to the commissioners and it is very simple. I
16 understand a lot of things about how complicated the
17 legal process is and how complicated the regulation
18 in this industry is. I appreciate that many people
19 have good intentions that are trying very hard, but
20 I think we are running out of time here.

21 My question very simply put is: If NERC
22 does not fix this problem of high-impact/low-
23 frequency events, especially solar flares, within
24 the next three years, will the commissioners vote to
25 decertify NERC? That is my question.

1 COMMISSIONER LA FLEUR: Well, thank you
2 for the question and for bringing up the importance
3 of the issue. I guess as the question presages the
4 first thing is to ask what NERC is doing on this,
5 which I know is something that is on all of our
6 minds. Maybe we will start there.

7 MR. CAULEY: Thank you, Commissioner.

8 First of all, I appreciate that there is a
9 concerned customer in the room. I was thinking
10 earlier it would be interesting to have had customer
11 perspectives on the panel.

12 The issue raised and a few others are the
13 things that we take very seriously. The industry
14 has a tremendous record of dealing with major crises
15 in terms of hurricanes, earthquakes, and storms and
16 being able to restore the system quickly. There are
17 some things that we have not faced. The question
18 is: Are we ready for them? And, what are we doing
19 to get ready?

20 The high-impact, low-frequency report I
21 don't know if the Commission also did one, but I
22 know we did one where we had a workshop and we
23 gathered the industry experts in North America and
24 produced a report.

25 From that report, the NERC Board just

1 recently approved an action plan that really focuses
2 on three. One is a concurrent attack on multiple
3 facilities and substations, a physical attack; a
4 concurrent cyber attack; and the third priority is
5 the GMD or the solar flare issue that was raised.
6 We have assigned groups to work on that.

7 I agree with the gentleman that some of
8 the solutions may be low-hanging fruit that we can
9 implement and some will be much more difficult, much
10 more expensive. We are going after those.

11 Those are my worries as well for the
12 catastrophic failure type events where there are
13 prolonged outages, more than the customary hours and
14 days following a storm, but something that could
15 seriously disable the system for a longer period of
16 time, we must be ready for those. I know I have got
17 the commitment of the industry CEOs to resolve those
18 particular three problems.

19 COMMISSIONER LA FLEUR: Is that anyone
20 else who would like to add anything?

21 (No verbal response.)

22 COMMISSIONER LA FLEUR: I mean, I guess I
23 would just say that when the next certification of
24 NERC comes, we will look at NERC's performance
25 overall, just as we did this time, but it sounds

1 like we can expect action considerably sooner than
2 three years from everything that is going on.

3 MR. JAMES: Thank you. Good afternoon,
4 commissioners. My name is Dan James. I am vice
5 president of public affairs and marketing at P&GC
6 Power located in Portland, Oregon.

7 I am here today representing 12 small,
8 rural electric distribution cooperatives located in
9 the Pacific Northwest that are required to be
10 registered with WECC and NERC.

11 We worked very closely with our colleagues
12 at WECC and NERC, but we are advised by counsel that
13 WECC is applying Reliability Standards the
14 facilities used in local distribution in a manner
15 that violates specific limitations expressed in
16 Section 215 of the Federal Power Act.

17 As you know, this section states that
18 Reliability Standards are to apply only to the
19 Bulk-Power System and expressly are not to apply to
20 facilities used in local distribution.

21 For example, WECC is interpreting
22 Reliability Standard PRC 5 to require registered
23 facilities in their maintenance and testing
24 programs, not just Bulk-Power System facilities.
25 This is not allowed under Section 215 of the Act.

1 We have already had initial conversations
2 with WECC and we are planning to sit down with WECC
3 and NERC to discuss this issue face to face in more
4 detail.

5 We are hopeful that such discussions will
6 result in specific guidance to ensure the
7 Reliability Standards stop being interpreted to
8 apply to facilities used in local distribution as
9 Congress intended.

10 Here is my question. How does the
11 Commission intend to ensure that Regional Entities
12 do not extend their reach over facilities not
13 covered by Section 215?

14 Thank you for this opportunity to ask this
15 question.

16 MR. CAULEY: I can help with that one.

17 COMMISSIONER LA FLEUR: Well, I was going
18 to say that earlier this morning, it seems like a
19 week ago now, but I believe it was this morning we
20 were in this room and actually issued an order on
21 that very topic, not this specific topic of those
22 LPCs, but the topic of the definition of the
23 Bulk-Electric System. NERC will be looking at that.
24 It is a bit unfair to ask Mr. Cauley to comment on
25 the order that just was put out a couple of hours

1 ago.

2 MR. CAULEY: I won't try to, Commissioner.
3 To answer the gentleman's question, some of the
4 standards do apply to users of the Bulk-Power
5 System. The legislation was carefully crafted to be
6 owners, operators, and users of the Bulk System.
7 There are some standards that do apply to
8 distribution operators and load-serving entities.

9 I agree with the gentleman that we should
10 not be directing maintenance of distribution
11 facilities. There are exceptions where, for
12 example, the interfrequency load shedding relays
13 that are in the distribution system are actually
14 used for a Bulk-Power purpose.

15 Not knowing any more about the facts and
16 circumstances, I would welcome a letter or an email
17 or something in terms the specific circumstances
18 because we would not have a standard on maintenance
19 of distribution.

20 I do agree conceptually the order, which I
21 haven't read yet, would give us the ability to look
22 at the issues in terms of what really is necessary
23 for Bulk-Power reliability. Whether that be a relay
24 that is in the distribution system under frequency
25 load-shedding purposes or whatever that purpose is.

1 I look forward to reading that order. I also look
2 forward to any written submittal, if you have
3 something in particular.

4 COMMISSIONER LA FLEUR: Thank you,
5 Mr. Cauley.

6 Other questions from the audience? Yes?

7 MR. MANTA: Hello. My name is
8 Chuck Manta. I am coming as an individual.
9 Although, for background purposes, I am strategic
10 advisor to a national association of local
11 governments called Public Technology Institute, an
12 InfraGard member.

13 In my consulting duties, I help emergency
14 management planners and IT officials with their
15 business continuity plans and their cybersecurity
16 plans.

17 The question I have that came to mind as I
18 was at the hearing today listening to everyone was
19 trends that I see that may increase your workload
20 orders of magnitude, and I would like to relay what
21 that question is in my question this way by posing
22 an example.

23 If you are a federal CIO, for example,
24 and you outsource half of your work to, say,
25 Northrop Grumman, you are not only responsible by

1 law to prove that you are securing government
2 information assets, you are also required to prove
3 that any of your subcontractors follow those same
4 guidelines, including those that might provide any
5 of the environment necessary for that information to
6 be secure.

7 Now, with the convergence of power and
8 telecommunications, that means a company like that
9 also has to prove that their telecommunications
10 providers are meeting those same requirements they
11 are legally upheld to provide.

12 With convergence with power, for example,
13 with Smart Grid, and also global threats such as
14 hackers, or the Hundred Year Solar Storm, suddenly I
15 could imagine all of those folks in the public
16 sector initially and eventually in the private
17 sector wanting to go to their utility and ask a very
18 simple question.

19 "Prove to me that you are reliable or show
20 me your contingency plan as to what you are going to
21 do, if you are not because by law I have to create a
22 contingency plan that takes all of that into
23 consideration."

24 I am wondering in light of that, is there
25 with these emerging trends and the growth of these

1 cyber threats that are as pervasive as they are, is
2 that going to require all of us to figure out a way
3 to work more closely together in a facilitative way
4 where the end-user customers are working through
5 their entire supply chain or reliability of power
6 this way? That is a question for either an answer
7 from a process point of view.

8 Thank you.

9 MR. NAUMANN: I would just say in general
10 utilities work very closely with their end-use
11 customers. The type of contact obviously depends on
12 the type of customer and their specific needs. We
13 have done that for a long time.

14 I know a number of fellow EI companies
15 that serve sensitive federal facilities have very
16 specific contacts with those facilities and continue
17 to. I would expect that would continue going
18 forward looking at their needs for reliable supply
19 and for restoration, if something bad happens.

20 COMMISSIONER LA FLEUR: Thank you,
21 Mr. Naumann.

22 Obviously the topics the gentleman spoke
23 about, the convergence of telecom and the importance
24 of the security of the grid, are pretty central to a
25 lot of what we will be working on.

1 COMMISSIONER SPITZER: Commissioner, the
2 gentleman may not have been aware that Sunday
3 morning the five of us were in Atlanta at a
4 technical conference noticed to the public jointly
5 with the National Association of Utility
6 Commissioners, covering a panel with very detailed
7 discussions of precisely that issue, the convergence
8 of telecomm, utilities, cyber threats, and the like.

9 There were more questions raised than
10 answers I would think, but it is on our radar screen
11 I would say.

12 MR. McMAHON: My name is Kevin McMahon,
13 and I represent Calpine Corporation. I am the chief
14 compliance officer for the company.

15 I heard a lot of discussion today around
16 the NRC and the programs they have in place for
17 auditing. In my prior roles at other companies, I
18 have worked in those program.

19 I would also suggest working through the
20 concept of the OIG work plan, which basically gives
21 a framework for entities to go about reviewing their
22 own self-audit process and ensuring that they are
23 going after the most critical matters as designated
24 by both FERC and NERC.

25 One of the major labor issues for us is

1 understanding the audit process. As the chief
2 auditor for the company as well, I would like to ask:
3 What is the effort being made by either FERC or NERC
4 around standardization of the audit process to
5 mirror some outside agency such as the IIA or the
6 AICPA, one of those bodies where the governance
7 around evidence and audit process is standardized
8 rather than recreating the wheel each time we have
9 an audit?

10 That is my question. Are we moving or
11 suggesting moving toward a standardized audit
12 process and audit evidence that is published either
13 through generally accepted principles of some other
14 agency?

15 MR. CAULEY: Well, we have -- Gerry Cauley
16 with NERC -- a preliminary cut at that I think in
17 the startup of our program. We did have operator --
18 I mean, auditor training in terms of the conduct of
19 the audit, ethics, and generally the technical
20 issues around the audit.

21 From a getting to first base perspective,
22 I think we accomplished what we needed to, to get
23 started. I think that Dan Skaar, who is a fellow
24 audit expert, is sort of our conscience in terms of
25 where we need to go and in terms of upping our game

1 in the audit arena.

2 We are looking at both how do we
3 incorporate the risk model into our audits. But the
4 degree of rigor around some of the suggestions that
5 the gentleman had, we also realize that our training
6 at this point for auditors is fairly rudimentary, to
7 parse a word, but it is simple and straightforward.

8 But we need to elevate something of a
9 qualification, a certification, for our auditors
10 that at a beginning level and maybe a more senior
11 level. We will be looking to put that program
12 together.

13 If I get my wish, we would actually make
14 some of that material and training available more
15 broadly to compliance folks in the registered
16 entity, so they could also benefit from sort of
17 pre-preparing themselves in terms of how to conduct
18 audits. We would have a NERC credential on
19 auditors. That is in our plans. We have got goals
20 emerging on developing that.

21 COMMISSIONER LA FLEUR: Thank you,
22 Mr. Cauley.

23 Norman Bay?

24 MR. BAY: Yes. The Division of Audits
25 tries to work very closely with NERC and with the

1 Regional Entities. We have gone on a number of
2 observation audits where we go with the RE's audit
3 team, observe what they do, and provide them with
4 some feedback in an attempt to provide the kind of
5 consistency that I believe the gentleman was asking
6 about.

7 MR. CAULEY: We agree with that.

8 COMMISSIONER LA FLEUR: Thank you.

9 COMMISSIONER SPITZER: Commissioner?

10 (No verbal response.)

11 COMMISSIONER SPITZER: I understand the
12 frustration of the questioner but the fact is, Gerry
13 alluded to it, if we are looking at the AICPA
14 analogy, the statute, our statute has been operative
15 for five years. We have had GAAP for hundreds of
16 years. Rome wasn't built in a day I would think.

17 COMMISSIONER LA FLEUR: Well, seeing no
18 further questions from the audience, I will do what
19 I prematurely did a few minutes ago and turn to
20 Chairman Wellinghoff.

21 CHAIRMAN WELLINGHOFF: I will start again
22 by rethanking this panel and the previous panel, and
23 just making two points. In quick conclusion, I
24 certainly am very encouraged by the willingness of
25 us all to work together, and I want to continue to

1 do that.

2 A second point is the two areas that I
3 think we have touched upon in these panels that I
4 would like to move quickly with would be of course
5 the traffic ticket type process for the minor
6 violations, and the second would be anything again
7 that we could do to assist in the National
8 Transmission Forum work. Thank you all. I
9 appreciate it.

10 COMMISSIONER LA FLEUR: Thank you,
11 Mr. Chairman.

12 Mr. Moeller, anything?

13 COMMISSIONER MOELLER: (Moving head from
14 side to side.)

15 COMMISSIONER LA FLEUR: (No microphone.)
16 Sorry. I thought I just turned it on, and I turned
17 it off.

18 Well, I will start again and thank both
19 panels that we have heard from this afternoon for
20 your thoughtful participation and the candor and
21 quality of your comments.

22 I think you gave us all a lot to work on,
23 but it was very encouraging that there were some
24 real themes that are much easier to work on and
25 really approach together.

1 Today is really a series of technical
2 conferences, starting with the one that I was not at
3 when I was a lady-in-waiting in July. I guess we
4 are going to have one with the topics to be
5 determined with NERC and others early in the new
6 year and really look forward to continuing the
7 discourse.

8 Thank you everyone who attended the
9 session also. Thank you. Thank you to the staff
10 from OE and OER, especially Roger Morie, who put it
11 together.

12 (WHEREUPON, at 4:49 p.m., the technical
13 conference was concluded.)

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