



Statement of

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**At the Commissioner-Led Technical Conference on
Reliability Standards Development and
NERC and Regional Entity Enforcement**

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Mr. Chairman and other Commissioners, I am John A. Anderson, president and CEO of the Electricity Consumers Resource Council, or ELCON. ELCON is the national association representing large industrial consumers of electricity. Our members are multi-state, mostly multi-national, corporations from all segments of the manufacturing community. They have facilities in every region of the country. The common denominator of ELCON's members is that they all use a lot of electricity in the manufacturing of their products. While I believe my comments today represent the views of all ELCON members, they are my comments alone.

The reliability of the electric grid is of tremendous importance to industrial electricity consumers. Increasingly, the productive processes of industrial facilities, from steel to autos to oil refining, are dependent on highly reliable electricity supplies. However, especially in these very difficult economic times, we must be sure that expenditures, even those made in the name of reliability, are both cost effective and results oriented.

For this reason, ELCON has been a very active participant in the process that brought the authority to the North American Electric Corporation (NERC) to develop and enforce mandatory reliability standards. We participated in NERC long before the Energy Policy Act of 2005 was enacted. We currently participate in many NERC

committees and other activities. We are strong supporters of NERC as a fair, open and inclusive organization that develops reliability standards, subject to Federal Energy Regulatory Commission (FERC) approval, that balance the risk of outages with costs of assuring reliability. However, we are concerned that today there is not a good, working relationship between FERC, the regulator, and NERC. We believe that the lack of a good working relationship is not in the best interests of consumers.

Why Are We Here Today?

On March 18, 2010, FERC issued 12 Orders and notices that completely caught NERC and its stakeholders off guard – a real “wake-up call” by anyone’s definition. These Orders require specific changes in some Standards and set deadlines for NERC compliance. The Orders were particularly surprising since FERC had neither given advance notice of the very stringent Orders nor issued any response to even the four Reliability Standards Development Plans or the Three-year Performance Assessment that NERC had filed over the past four years where NERC had set forth, at least in my opinion, their assertions that they were meeting the challenges delegated to them. However, obviously, FERC did not believe that NERC was a “strong”¹ enough organization to assure the level of reliability that FERC believed necessary.

Several of the Orders are of considerable concern to and may have direct impact on ELCON members including (but not limited to):

- A requirement to change the definition of Bulk Electric System (BES) to include all facilities greater than 100 kV² – thus sweeping into mandatory compliance many industrial facilities with behind-the-meter generation.
- A mandate to change NERC’s Rules of Procedure (RoP) so that the NERC ballot body cannot delay or prevent NERC’s compliance with Commission directives – thus significantly impacting the fair, open and inclusive aspect of NERC’s standards setting process, and, in essence, making FERC rather than NERC, the standard setting entity.

¹ The term “strong” is from: Remarks of Joseph T. Kelliher, Executive Vice President – Federal Regulatory Affairs, FPL Group, Inc., “Reliability Primer for Lawyers and Energy Professionals,” Energy Bar Association, April 28, 2010, page 5.

² Although it does exempt loads served by radials.

- The issuing of a Penalty Guidelines Policy Statement placing increased emphasis on loss of load – thus changing the focus of system operators from maintaining reliability to avoiding significant penalties.

NERC’S Reaction to the March 18th Orders:

The March 18th Orders clearly got NERC’s attention and have resulted in substantial change including:

- Re-prioritized projects and developed a list of high priority projects
- Developed a new process to follow the status of the high priority projects
- Conducted a meeting with FERC staff to review work priorities, solicit FERC input to prioritization of projects and adjust its list of high priority projects
- Developed an action plan to address compliance with FERC Directives and Prioritized Projects as soon as practical including expedited processing of “noncontroversial” Directives where developing a new or modified requirement should be achievable without the need for industry debate on technical issues
- A webinar with drafting team chairs, vice-chairs and coordinators to inform the drafting teams of the SC’s expectations regarding project management and the offer of SC assistance in meeting project schedules
- An increase in NERC staff to allow NERC to address more issues in less time
- The development of an “Informal Guidance Procedure” to afford stakeholders a quicker and more consistent method of getting their questions answered while reducing resource requirements. It is expected that this Procedure eventually will lead to reduced numbers of Formal Interpretation Requests.
- Stepping up efforts on the “relational” database to provide stakeholders with better information.
- Developed a new Standards Development Process that has been filed with FERC dealing with a “Quality Check” process, informal comment periods, parallel activities and expedited process improvements.

In my view, NERC certainly has demonstrated with both actions and words that it has heard the wake up call and is taking very significant actions to meet the challenges set forth by FERC.

FERC'S Reactions to NERC's Actions:

In reaction to NERC's filings requesting rehearing, clarification and extension of times on some of the Orders, FERC:

- Agreed to a rehearing request and scheduling a technical conference regarding RM-16-011 (BAL-003)
- Granted partial clarification (although denying rehearing and a request for a stay) regarding RM06-16-012 (TPL-002 - footnote b issue)
- Held this conference today – A very positive step in the right direction

I am optimistic, perhaps only cautiously optimistic, that FERC recognizes that NERC understands FERC's concerns.

Why Is The FERC – NERC Relationship So Difficult?

Obviously, FERC was justified to point out that NERC had not responded to hundreds of FERC directives for over three years, that many standards required improvements, and that the U.S. is still experiencing interruptions to the bulk power system. However, at least in my view, FERC went too far and, in essence, asserted control over the substance of reliability standards.

Reliability issues are very complex for several reasons including (but not necessarily limited to):

First: Who should be the primary reliability expert – FERC or NERC? The electric system in the North America is a very big machine with over 6,000 generators, 160,000 miles of high voltage transmission, and 10,000 dispatchers and power plant distributors. It is very complex and difficult to manage. While there certainly have been technological innovations, we still must rely on individuals – real people – making individual decisions and very specific and personal industry expertise. Most of that expertise lies within the electric industry as it works in and through NERC. FERC certainly has very technical and competent individuals on its staff. But FERC will never be able to, nor should it try to, duplicate the depth and breadth of the expertise of the

operators actually controlling the dispatch and the grid. Participation in NERC now is open to technical experts from all industry segments – a remarkable achievement, although it may be slowing the process somewhat.

Second: Can we afford 100% reliability? There seems to be a growing sentiment within FERC for 100% reliability. We must recognize that we will never have 100% reliability – it is impossible – and is far too expensive to even try. The objective should be to establish a bulk power system that minimizes outages and avoids both cascading outages and long term equipment damages while providing a level of reliability that meets the needs of consumers at a reasonable – or at least acceptable – cost. Establishing an acceptable balance between the degree of reliability and the costs of meeting the reliability standards is very difficult. If FERC actually believes that 100% reliability is required, we all must recognize that this is a paradigm shift and all parties must begin an intense dialogue – and soon.³

Third: What does the law require? There are significant conflicting and/or unclear mandates – Federal Power Act Section 215 requires that standards be developed under a process that assures “reasonable notice and opportunity for public comment, due process, openness, and balance of interests” and FERC must give “due weight to the technical expertise of the ERO” with respect to the content of a standard.⁴ NERC’s Rules of Procedure call for a supermajority 2/3 weighted segment ballot by the ten industry segments. However, Section 215(d)(5) also states that FERC may order the ERO to submit a proposed reliability standard or a modification to a reliability standard that addresses a specific matter if the Commission considers such a new or modified reliability standard appropriate to carry out Section 215. Some interpret the statutory language to say that: “FERC cannot actually direct NERC to submit a specific standard

³ Section 215(a)(4) defines “reliable operation” as meaning: “...operating the elements of the bulk-power system within equipment and electric system thermal, voltage, and stability limits so that instability, uncontrolled separation, or cascading failures of such system will not occur as a result of a sudden disturbance, including a cybersecurity incident, or unanticipated failure of system elements.” ELCON questions if this statutory language justifies even an attempt to assure 100% reliability.

⁴ On August 8, 2005, the U.S. Congress enacted the Energy Policy Act of 2005 allowing FERC to approve an “Electric Reliability Organization” (ERO) to create and enforce reliability standards that, once approved by FERC, would be mandatory in the U.S. It was clearly expected that the ERO would be North American in scope as the bulk power system spans several countries. The legislation: requires FERC to give due weight to the technical expertise of the ERO, restricts the ability of FERC to change the text of a standard reflecting the sensitivity of Canada to avoid FERC regulation, and limits the scope of NERC to reliability (not markets or commercial).

or modification...” In fact, the language suggests that: “NERC has a duty to only file standards and modifications that it believes meet the statutory test... If the ERO does not believe a particular standard is ‘just, reasonable, not unduly discriminatory or preferential, and in the public interest’ it should not file that standard with FERC – in fact it has a duty to withhold filing.”⁵ However, others believe that FERC orders that NERC has no choice but to submit the specific standard or modification desired by FERC on a timeline established by FERC.

Fourth: Is NERC a North American ERO or an American ERO? The bulk power system covers the U.S., Canada and some of Mexico – and power flows freely across international boundaries. Clearly, FERC has jurisdiction over public utilities engaged in sales for resale and interstate transactions in the U.S. However, FERC does not have jurisdiction over either Canadian or Mexican entities. The ERO must develop standards that obtain buy-in from entities throughout North America. There is a real concern that if FERC exerts excessive regulation over U.S. entities, Canadian or Mexican regulators may be pushed into establishing their own standards. Such a situation would not be good for anyone.

Fifth: How high must penalties for violations of reliability standards be set? There seems to be substantial differences in broad objectives between FERC and NERC. NERC is trying to re-invent itself into a learning organization built on a culture of compliance through standards that are risk- and results-based. But FERC’s Orders, possibly inadvertently, seem to be pushing NERC and its stakeholders into being overly concerned over loss of load with stringent penalties, while making entities subject to the standards hesitant to share information. Understandably, FERC places primary focus on avoiding blackouts, thus perhaps overreaching while industry is concerned over both reliability and costs.

Sixth: What are the real priorities? FERC and NERC seem to have different views on priorities. As simply an example, shortly after NERC filed its initial set of standards (“Version O”), FERC directed NERC to change many of them and add “missing pieces” so that compliance could begin, requiring a substantial amount of industry resources.

⁵ Remarks of Joseph T. Kelliher, op. cit. page 5.

These efforts were followed by directives to replace all the levels of noncompliance with Violation Severity Levels (VSLs), but the guidelines for the VSLs were not established by FERC until after the Violation Risk Factors (VRs) and VSLs were filed. There are other such examples. While there probably are very good reasons for such actions, the fact is that NERC had to devote considerable resources making adjustments to compliance elements of the standards, rather than allocating time to improving existing requirements in a manner that addresses the reliability-related directives in Order 693. If FERC and NERC could agree in advance on priorities, NERC would be able to move much more efficiently and faster.

Finally: Are we really focusing on the right entities? NERC proposed, and FERC approved in its July 20, 2006 Order, a registration process for users, owners and operators of the Bulk Power System based on fourteen primary functions defined in NERC's Functional Model. As ELCON emphasized in its comments in that filing, over-registration is as pernicious a result from the standpoint of enforcing reliability as under-registration. Over-registration will distract the compliance staff at both NERC and the regions. FERC agreed with the rationale of NERC and other commenters "...that, at least initially, expanding the scope of facilities subject to the Reliability standards could create uncertainty and might divert resources as the ERO and Regional Entities implement the newly created enforcement and compliance regime."⁶ ELCON agrees with Section 501 of NERC's Rules of Procedure that requires only entities that have a material impact on the bulk power system to be in the NERC Registry, and thus subject to the reliability standards. We are concerned with the growing pressure to include additional entities in the NERC Registry, thus making them subject to the standards. In fact, one FERC staff is well known for advocating the registration of all loads of 1 MW or more and eliminating registration criteria based on voltage. Such proposals would significantly increase the number of entities that would be required to register and sweep into the Registry many entities that have no material impact on bulk power system reliability.

⁶ Order No. 693, 118 FERC ¶ 61,218, March 16, 2007.

So Where Are We?

Reliability regulation is a work in progress, and it will be for some time. With the March 18th Orders, FERC asserted, out of a real sense of duty, a larger role than many stakeholders expected given the history and the actual words of the Energy Policy Act of 2005. However, while perhaps technically FERC should not, or can not, direct NERC to submit a specific standard or modification to a standard on a timeline established by FERC, the reality is that the regulatory agency has such flexibility to get what it wants – either directly or indirectly.

FERC has the responsibility to regulate in a manner that will assure adequate reliability of the bulk power system. FERC has expressed on several occasions significant concerns with NERC's standards – certainly going as far back as the 2006 Staff Report⁷ and then again in Order 693 in 2007 it specifically specified 550 directives for change – and several hundred of these have not been fixed even today.

NERC has the responsibility to prove to FERC that it is a “strong organization” (as defined by former FERC Chairman Joe Kelliher).⁸ However, NERC must operate in a manner that complies with Section 215 including, among other requirements, assuring a fair, balanced, open and inclusive Standards Development Process. Further, NERC must operate primarily with industry volunteers representing very diverse constituencies – a situation often close to “herding cats.”

⁷ *Federal Energy Regulatory Commission Staff Preliminary Assessment of Proposed Reliability Standards*, May 11, 2006.

⁸ Remarks of Joseph T. Kelliher, op.cit., pages 2 – 3. In these remarks, former Chairman Kelliher lists five criteria that he thinks the present Commission should use to define a “strong” NERC. These points serve as a good starting point to evaluate the strength of NERC.

WHAT CAN BE DONE TO IMPROVE THE FERC – NERC RELATIONSHIP?

What is needed is a very good working relationship between FERC, NERC, and industry stakeholders. In my view:

NERC has made, and is continuing to make, very substantial progress in the transition from a utility-dominated voluntary organization to an ERO that is responsive to broader stakeholder interests. But NERC also must show more sensitivity to the fact that the EAct 2005 requires FERC oversight of NERC. NERC must respond explicitly to FERC orders and directives in a timely manner. Leaving hundreds of FERC directives, no matter how minimal, unresolved for over three years is unacceptable, especially when there were no requests for rehearing or clarification made when the directives were issued. NERC should be more specific where it has differences of opinions with FERC orders by filing for rehearing and/or clarification. NERC also can and should make every attempt to increase communication and dialogue by requesting Technical Conferences and direct meetings with FERC staff to help both parties understand their positions. NERC must prove that it is able to accept the very difficult challenge of assuring a reliable bulk power grid.

FERC also can and should take some specific actions. At least to me, it is not in FERC's interests, much less the interest of NERC and its stakeholders, for FERC to attempt to over-regulate. FERC should show a greater understanding that reliability regulation is a work in progress – and will take some time to adequately develop. FERC also should show greater sensitivity to the fact that EAct 2005 requires FERC to give “due weight to the technical expertise of the [ERO] with respect to the content of a proposed standard or modification to a reliability standard...”⁹ FERC also should indicate more explicitly its consideration of the reliability and cost impacts of directed revisions both in developing its directives and timelines. And FERC, given the international nature of the bulk power system, should ensure that its directives are kept within its mandate to approve and remand standards approved by NERC.

⁹ Section 215(d)(2), EAct 2005.

Former FERC Chairman Joseph Kelliher stated that FERC initially asserted a larger role than expected “out of a sense of duty.” However, Mr. Kelliher then stated: “...this larger FERC role was intended as a temporary measure only.”¹⁰ The real question, to me, is that once NERC actually demonstrates that it is a “strong organization,” will FERC accept a reduced role and rely more on NERC? Is it a simple disagreement that can be worked out over time with better communication or is it a systemic flaw in the relationship between the regulator and the regulated? I certainly hope it is the former – and ELCON looks forward to working with all parties to make the ERO model work for all stakeholders.

Thank you for the opportunity to appear before you today.

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¹⁰ Ibid., page 2.