

**ENERGY BAR ASSOCIATION,
DISCUSSION REGARDING THE NERC AND
REGIONAL ENTITY HEARING
AND APPEAL PROCESSES**

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PROCEEDINGS

MS. WALSH:

Thank you all for coming here. We have a large group here in D.C. It looks like we have about fifty or more people here in the room, and I understand we have about sixty callers on the phone. My name is Linda Walsh, with Hunton & Williams, and I would like to welcome you all. We are very excited about our program today: The NERC and Regional Entity Hearing and Appeal Process, Advice from the Field.

We are fortunate to have six very talented and knowledgeable people here with us today, and I will introduce them each in a minute. First, I wanted to give you a little bit of background on how we are going to proceed today. We have, or we did have, some copies here of the presentation, but I see that they are all gone, but you should all have gotten a copy of them by email. We are going to go through each of the speakers in a row. We have a lot to cover in a short period of time, so we are going to save questions until the end of the program. We will have questions from the in-person audience here first and then we will take questions from callers on the phone. We have a conference call service that will put the calls in a queue and take them one at a time, and we will take as many as we can or as many as we have time for.

I would like to introduce briefly our speakers. We have some detailed bios that were emailed, so I will not go into a lot of detail. But, I would like to say a couple of things about each one of our speakers. We are very happy that they are here with us today.

Our first speaker is Mr. David Cook. He is here to give us the NERC perspective on the NERC hearing process and its role in the regional processes. Dave is the Vice-President and General Counsel at NERC, which is the North

American Electric Reliability Corporation. Dave has been with NERC since 1999, and during that time there he led NERC's efforts to secure passage of the Energy Policy Act of 2005. Prior to joining NERC, Dave was with FERC for a total of twenty years, spending the last ten as FERC's Deputy General Counsel.

Next, we will have Robert Wargo. He is a Manager of Enforcement for ReliabilityFirst Corporation. He will share with us his view from the regional entity prospective, from the early violation stage to the hearing process. Bob Wargo is responsible for all violation-related communications with registered entities, management of case and docket proceedings, assessment of mitigation plans and coordination of hearing proceedings at the regional level.

Next, we will have the view from the hearing officer's perspective. And we have two very experienced arbitrators who are both registered hearing officers with several of the registered entities. We have Ken Nickolai. Ken is a former administrative law judge with the Minnesota Office of Administrative Hearings. He is also a former Commissioner of the Minnesota Public Utilities Commission. He is currently under contract with several regional entities, including the Midwest Regional Organization and the ReliabilityFirst Corporation, RFC.

Next, we have Robert Wax. I would like to say a special thank you to him. Bob is the co-organizer of this event today. He is the Vice-Chair of the Energy Bar Association's ADR committee, and without Bob, we probably wouldn't all be here today. So thanks, Bob. Bob is a principal of Charter Resolution. He provides services as an independent arbitrator, mediator and hearing officer on energy and commercial matters. He is also under contract with several regional entities as a hearing officer, including SERC Reliability Corporation, Midwest Reliability Organization, Florida Reliability Coordinating Council, ReliabilityFirst Corporation and the Northeast Power Coordinating Council, Inc.

To discuss the role of NERC's Compliance and Certification Committee in the hearing process, which will be used for hearings where NERC is the enforcer, we have Thomas Burgess. Tom is the director of FERC quality and compliance for with FirstEnergy Corp. There he is responsible for the company's compliance with electric reliability standards and other FERC compliance matters. He also represents FirstEnergy's involvement with NERC and FERC in the development of reliability standards in compliance and enforcement programs. Tom is also a member of the NERC Compliance and Certification Committee, which we will hear more about today.

We also have with us today to discuss from the FERC perspective the challenges of enforcement and appeals, Kathleen Barrón, the Associate General Counsel for Energy Markets at FERC. She heads a large team of lawyers that provide legal and policy advice to the Commission on a host of electric, natural gas and other matters including electric reliability. We are very happy to have all these expert panelists speakers here today, and I would like to get started here right away. And Hopefully, at about 1:30, we will be able to start questions. So to start with, I would like to introduce Dave Cook.

PRESENTATION BY DAVID COOK

MR. COOK:

Thank you, Linda. Good afternoon. I appreciate very much this opportunity to talk with you about the NERC compliance and enforcement program. There are two presentations that are out with my name on them. The first is a background piece on NERC's role as the ERO. I'm not going to talk about that one today, but if there are questions about that, at the appropriate time, I would be happy to speak on those issues. The second piece, NERC's role in enforcement, is the one that I'm going to spend some time on today. As we discuss enforcement and reliability standards today, it's important to have in mind the big picture. Why do we have this program? What are we up to? What's the object of the game?

Blackouts are not accidents, in the sense that they are not unpreventable, random occurrences. One illustration: The precipitating event of the August 2003 event/blackout in northeastern U.S. and Canada was tree contact with an overhead transmission line. Tree contact was also the precipitating event for the July 1996 and August 1996 blackouts in the West and for the September 2003 outage that blacked out Italy. In 2007, we had sixteen category one vegetation contacts with transmission lines, that is, contacts from trees growing in the rights-of-way of transmission lines with line loadings below their normal ratings. That's unacceptable performance. NERC's mission is to drive down the risk of system disturbances by driving the known risks to zero. The compliance monitoring and enforcement program is one part of that larger effort along with standards development and event analysis, benchmarking, and assessments.

I recommend that you read a new book by Marc Gerstein, *Flirting with Disaster - Accidents are Rarely Accidental*. Though he never mentions the electric power system, his discussion of other catastrophes is spot-on to what we are doing, and we all need to mine that book for what it has to say about the nature of our work and how we need to go about it.

NERC's authority to carry out an enforcement program in the U.S. stems from its certification by FERC as the electric reliability organization under Section 215 of the Federal Power Act. NERC has authority to carry out compliance monitoring activities, find violations and impose penalties. NERC's enforcement actions don't become final until the thirty first day after NERC files a notice of penalty with the Commission. FERC may hear an appeal by a registered entity of that notice of penalty or it may review the notice on its own motion. FERC also has independent authority to initiate and carry out its own enforcement of reliability standards.

NERC works through regional entities for a number of its programs. The regional entities have the primary, first-line responsibility for carrying out the compliance and enforcement program. NERC has delegated its authority to the regional entities under delegation agreements that, along with the NERC rules of procedure, describe the nature and scope of the regional compliance programs. Those delegation agreements have been approved by the Commission.

On July twenty-first, NERC and the regions made their compliance filing in response to FERC's March 21, 2008 order on the delegation agreements. That compliance filing has the latest iteration of the delegation agreements and, most important to today's discussion, it has revisions to NERC's rules of procedure

that include revisions to the hearing procedures and related matters that we need to focus on. Those are not yet in effect, but I expect they will be once the Commission takes action on that compliance filing.

The NERC rules of procedure include a number of items related to the compliance enforcement program. In particular, Attachment 2 to the uniform compliance program document contains the hearing procedures that are followed in most regions. WECC has a somewhat different document; although, in substance, it's very similar. Each of the regions may have particularized that document, but, in sum and substance, that's where you will find the hearing issues dealt with.

NERC's July twenty-first compliance filing also covers the discovery issues in much more detail than the currently effective rules do. I think you will hear more about these procedures from other panelists as we go on. One of the key elements of the compliance program is the compliance registry. It identifies the owners, operators and users of the bulk power system who must comply with the applicable reliability standards. Entities are registered according to the functions that they perform. Each reliability standard has an applicability section that lists the functions to which that standard applies. NERC maintains on its website a matrix of the requirements of the reliability standards down, I think it is, on the vertical axis and the various functions on the horizontal axis, so it is easy to determine which particular requirements apply to the functions for which an entity is registered.

NERC has almost 1,900 entities registered in the compliance registry. Many perform multiple functions; many operate in more than one region. When an entity is first placed on the registry, there is notice and an opportunity to contest the registration. The region makes the initial determination. That determination may be appealed to NERC's board of trustees' compliance committee, and thereafter the committee's decision may be appealed to FERC. I think we are through most of the registration issues now. We probably had 100 contests of registration; maybe half of them were resolved informally. I think we've probably decided about twenty or twenty-five of those now. FERC has done maybe ten or so. So that's sort of the order of magnitude. So there are a few left to sort through. But we are very pleased to have this part done and a clear statement of who is responsible.

It's good for a couple of reasons. One, people know what they are responsible for, and two, when there are changes we know who we need to speak with to notify them of changes in the standards. The compliance registry does not necessarily contain all of the potential owners, operators and users of the system for a couple of reasons. One, it is dynamic. We may not have found everyone. If we should come across another entity that belongs on the list, we will place them there. From that point on, the entity would have an obligation to comply. Obviously, they have the procedural rights to contest the registration.

Second, FERC has not yet developed a final, definitive statement of the full scope of the bulk power system. In that sense the compliance registry can be seen as a subset of the entire list of possible owners, operators and users. But we do believe that what we have is the critical list, that we have everybody that we're aware of that has a material impact on the bulk system. And it starts at the top, with the reliability coordinators, the balancing authorities and the transmission operators, the folks who have the lion's share of the day-to-day,

operational reliability on the system, and then it moves down through some entities that historically have not had as much contact with NERC, but into the transmission owners, generator owners and operators and purchasing and selling entities and LSEs. But we basically have the folks that we think we need to have to assure reliable operation of the system.

NERC has three main roles in the compliance monitoring and enforcement program. First, we apply overall direction to the regional compliance programs. That comes in the form of the rules of procedure and the delegation agreements that call for fair, consistent and effective compliance programs. We foster the use of standardized approaches to various issues and procedures. We establish an annual compliance implementation plan, and we approve each region's annual implementation plan to deal with the NERC plan. Those plans establish the annual program goals. They identify the reliability standards that are being actively monitored in that year. Obviously, with the number of standards and requirements, it would not be prudent to spend a lot of time trying to monitor every single one, and we focus on the ones that we think have the most importance to the system, that present the most risk to the system. And, NERC provides informal guidance in lots of different ways to the regional entities along the way as issues arise.

Second, NERC oversees the regional programs by, for example, reviewing regional submissions for consistency and completeness. There is a lot of non-public reporting, of alleged violations and so on to the Commission, and we have worked hard to develop a uniform, consistent look and feel to that, so that we get standardized data and we get everybody dealing with common definitions and common sets of information, et cetera. NERC's staff participates, or may participate, in audits of particular registered entities that are conducted by the regions. NERC staff participates in compliance violation investigations that may be going on in a region. And depending on the circumstances, NERC staff may lead the audit or the compliance violation investigation. Finally, NERC is responsible for auditing the regional compliance programs to assure their effectiveness in implementation of the delegation agreement and the program.

The third major role that NERC plays is as an appellate body. The board compliance committee hears appeals from the regions regarding the compliance registry. So far those have been paper proceedings. The board compliance committee also hears appeals by registered entities from regional entity determinations on enforcement matters. It also reviews settlements of enforcement matters that come up from the regions. Where NERC itself is the enforcement authority, the initial NERC enforcement decision will be made by the stakeholder-based compliance and certification committee, followed by an appeal to the NERC board compliance committee.

Just one example: The WECC organization carries out the reliability coordination function for WECC. NERC will handle all of the compliance, monitoring and enforcement activities for the WECC reliability coordination function, and if there is a need for hearing procedures or whatever, that would happen initially before the NERC compliance and certification committee. Finally, if a regional entity wishes to challenge an issue or finding that comes up in the course of a NERC audit of a regional program, the compliance and certification committee would also be the hearing body for that claim, followed by an appeal to the board compliance committee.

On a final note: where are we? The compliance program continues to evolve, but the procedures are largely untested yet. We have, I think, filed something like thirty-five or forty notices of penalty with FERC—thirty-seven—who is counting?—and that marks the end point of the NERC process. The Commission then reviewed them and issued an order on July third that provided quite a bit of guidance to us and the industry about how those things should be handled for the future. But that's all the notices of penalty that have gotten to the end of the NERC process at this point. We have some more that we are working on, but I think the number is something like 1,400 pending alleged violations that will need to work their way through the system. And on top of that there are reviews of mitigation plans, and so there is a lot of activity going on.

Under the law it is all nonpublic at this point until the point at which we file a notice of penalty with the Commission. So some of these things, especially the hearing procedures, have yet to be tested. There have been no hearings to date. We had a couple of cases that looked like they were headed toward hearing but those have recently settled. We have had final action on settlements, and I expect that there will be more of that in the coming weeks. The board compliance committee also has an initiative underway to review various aspects of the compliance monitoring and enforcement program. There are draft papers posted on the website on some issues. The committee has an open committee meeting on October fourteenth where some of those issues will be discussed, and I encourage your participation in those. Finally, FERC will soon issue an order on our latest compliance filing and that may require further changes in the order. I want to thank you very much, and I look forward to the discussion from the remaining panelists and then any questions.

MS. WALSH:

Dave, one question. You mentioned that there are some processes underway to review the CMEP, and you mentioned earlier that consistency is a goal, that the regions have consistent procedures. What processes are underway now and do you envision for the future for consistency among hearing procedures?

MR. COOK:

Well, we think, in terms of the procedures that are written down, we think we are pretty close in the sense that the six regions that are in the east collaborated on the set of hearing procedures that are now in place and the set of procedures that are pending at FERC. I think when the industry—a lot of what people are interested in is consistency of results, and the real way to start dealing with that is to have some results that we can start comparing, and we have had precious little of that at this point. I think one of the mechanisms, and the board has started a committee that has already exercised this kind of authority when reviewing settlements, is that the board has set some parameters for certain kinds of settlements, and if a proposed settlement falls outside of those parameters, then the board can and has remanded those settlements, saying that “Here is where this has to be.” And so that is one avenue. The regions are in discussion about how they are handling various issues. That's another avenue. Standardized audit work papers and so on is another avenue to move toward

consistency. But some of it is really going to be, let's exercise the process a little bit, let's get some results out and start comparing them and see where the outliers are and bring them in.

MS. WALSH:

Thanks, Dave. The next panelist is Bob Wargo.

PRESENTATION BY ROBERT WARGO

MR. WARGO:

Thank you. And I just want to thank the Energy Bar Association for inviting me. While Dave gave a very top-level, broad overview, NERC has been granted the responsibility for developing and implementing the compliance monitoring and enforcement program for reliability standards, the authority to initiate an enforcement action with regards to any particular violation is a function granted to the Regional Entities by virtue of the delegation agreement between NERC and the Regional Entities. Violations may be identified through any of the eight monitoring processes outlined in the Compliance Monitoring and Enforcement Program (CMEP) document adopted by NERC and all of the Regional Entities.

Various notices are issued by the Regional Entities throughout the enforcement process providing opportunities for responses from the registered entities that are the subject of those enforcement actions. In addition to the formalized regional hearing process, other alternative methods for issue resolution are available throughout the enforcement action process. The eight monitoring activities that can result in violations being uncovered include compliance audits, self-certifications, spot checks, compliance violation investigations, periodic data submittals, exception reports and complaints. Although compliance audits and FERC and NERC's participation in those audits have been discussed previously, the Regions also utilize self-certifications, whereby registered entities attest to their compliance to the various standards, on a regularly scheduled basis, to promote compliance awareness throughout the year.

Additionally, the more random spot-checking is used to focus on particular standards that might be common areas for previous violations or on registered entities that may have a history in having difficulties in achieving compliance in the past. Compliance investigations are commonly the result of events that may have occurred in the system. Self reports currently constitute the source of most violations. Self-reporting is the mechanism by which registered entities self-assess themselves on a continuous basis and come to a determination of whether they are complying with the standards. As is often noted in FERC orders, self-reporting is looked upon as the preferred mechanism for a Region to become aware of a violation.

Self reports indicate a culture of compliance whereby the registered entity themselves are looking with a critical eye to determine if they comply to the standards. A violation will progress through different phases as it is processed on the regional level. During the first phase, after an issue is first identified, the

term “possible violation” is used. The issue may arise from one of the compliance monitoring methods mentioned previously, such as from a compliance audit. The audit team might, during the course of a regularly scheduled audit, determine that a possible violation exists for a certain NERC Reliability standard and requirement.

Normally what the audit team will report back to the regional entity is that the registered entity has failed to provide sufficient evidence to lead the audit team to the determination that the registered entity is compliant to the standard and requirement in question. The identified possible violation is turned over to the regional entity enforcement group, for a rigorous investigation and determination of facts. During this phase, many questions will be asked, many documents will be requested and an extensive review of data will occur. After review of all relevant documents and data, a determination will be made as to whether there alleged violation may have occurred and therefore an issuance of a notice of alleged violation is warranted.

After issuance of the notice of alleged violation, the registered entity has an opportunity to provide a response indicating their decision to accept or contest the alleged violation. In the case where the registered entity accepts the violation (or additionally, if the violation is upheld in the hearing process), the alleged violation becomes a confirmed violation. The region will file a notice of confirmed violation with NERC, thus completing the hand-off of the violation from the region to the ERO. If NERC concurs with the regions that it is indeed a violation, NERC will file the notice of penalty with FERC, at which point the violation becomes public.

A possible violation is a set of facts which may potentially constitute a violation for which the regional entity has not completed a full fact and circumstance investigation. At this point there is only a possibility that a violation may exist. An example of this would be an audit team visiting a registered entity requesting evidence of compliance. If the registered entity fails to provide evidence of compliance, it is at that point, a possible violation will exist. The enforcement group at the regional entity will get involved and would look for evidence of a violation. As will be described in the hearing process later, the burden of persuasion at the hearing is on the compliance staff to prove that a violation exists. The audit team may uncover evidence of a violation or they may just uncover that there is a lack of evidence of compliance. In either case, the enforcement group will perform further investigation.

An alleged violation is a possible violation where the region has completed the fact and circumstance review and further investigation. It is at this point that the regions will make a determination whether sufficient evidence exists to support a violation of a reliability standard. Due to the amount of time necessary to construct meaningful and complete data and document requests, and likewise the amount of time to provide meaningful and complete responses, the time period involved before a possible violation transitions to an alleged may be quite long.

In many cases, several rounds of data and document requests and responses are need to develop the complete picture of a violation and to determine an appropriate penalty. The region is also, at this point, determining the exact breadth and scope of the violation, whether there may be other standards or requirements involved, the duration of the violation, the date of discovery of the

violation, the presence of any early mitigating activities on the part of the registered entity to correct the violation, and perhaps most importantly, any potential or actual risk to reliability that the violation may have caused. So this is really the time period when most of the work regarding the development of the facts and circumstances of a violation occurs.

A confirmed violation is an alleged violation for which a registered entity has either not responded within thirty days to the notice of alleged violation, or has accepted the region's finding that a violation occurred, or the violation has completed the appeals process within NERC, or the time for submitting an appeals to NERC has expired or, finally, the registered entity have not requested a hearing. Additionally, if a hearing has been requested a hearing, a confirmed violation is a violation that is upheld in the hearing itself. Although the exact number and title may vary from region to region, regional entities utilize several different types of violation notices to communicate essential information to the registered entity and to NERC. Because this is probably the one area where the regions receive the most questions, perhaps indicating the area of most confusion, *ReliabilityFirst* will typically call the entity before the notices are issued in order to try to prepare the registered entity in terms of describing exactly what the notice is, what it means and what their obligations or options are in terms of response. In many instances, the individuals who are the recipients of these notices are plant engineers or managers, who may not be as aware of the legal nature of these notices. Therefore, *ReliabilityFirst*, in all cases, will fully communicate the natures of these notices and will make people available to answer any appropriate questions that the registered entity may have.

The initial notice of alleged violation typically is issued within a short period of time when a possible violation is uncovered. The notice is very brief and does not contain many facts but does provide notice that the region believes a possible violation exists and notifies the entity to save all relevant documentation. As part of this initial communication, the registered entity, although under no obligation to do so, is encouraged to submit a mitigation plan. The correction of a violation at the earliest possible moment not only is looked on favorably by the regions from an enforcement penalty viewpoint, but more importantly corrects a situation within the system that may have a potential risk to reliability false.

The notice of alleged violation is a very formal written notification to the registered entity that a determination by the region has been made that an alleged violation exists. The notice will include a series of facts developed during the fact and circumstance review that form the basis of the finding of an alleged violation. The notice will also have information regarding the range of dates the region has determined the violation had occurred. This notice serves as a charging document, laying out the basic set of facts surrounding the violation. The notice will also include the penalty amount and a description of the general basis for how the penalty amount was determined including violation risk factors, violation duration and any extenuating circumstances involving the registered entity or the violation. The notice will also include any aggravating elements that may have been taken into account when determining the penalty amount, such as the presence of concealment or whether an intentional act to violate was involved. The notice of alleged violation begins formal enforcement

proceeding of the violation and serves as the transition from an investigative phase into the legal phase, where notices are issued and responses are expected.

This is typically the point at which legal counsel from the registered entity, if not already involved, becomes involved. And, although the regions try to explain as precisely and completely as possible, what the notices mean and what the obligations are on the part of the registered entity in terms of response options, the registered entity is at the point where decisions in terms of how they are going to proceed with the allegation of the violation need to be made and understanding the significance of those decisions is the registered entity's responsibility. Within the notice of alleged violation, information is provided indicating that the registered entity has three options, one of which must be selected within thirty days.

The registered entity can agree with the alleged violation and the penalty, or agree to the alleged violation and agree to submit and implement a mitigation plan but contest the penalty or, thirdly, can contest both the violation and the penalty amount. The important detail to note is that a registered entity has thirty days to make that selection. If a registered entity does not make a selection within thirty days, then it will be deemed to have accepted the violation including the proposed penalty. If the registered entity contests the alleged violation and/or the penalty, the registered entity must submit a response to the notice of alleged violation, explaining their position, together with any supporting information within those thirty days.

In the event that either the violation or the penalty, or both, are contested, the regional entity will schedule a conference with the registered entity within ten business days. This conference serves as the last-ditch effort to try to come to some resolution in terms of the violation. Normally what happens is that the registered entity will come in and will once again argue the case, why they feel it is not a violation or why they feel that the penalty is incorrect. Sometimes new information surfaces at this point. In any event, the ten day conference is really the last effort outside the hearing space or the settlement arena to resolve the issue. If resolution is not achieved at the ten day, the registered entity has forty days, from the date of their response to the notice of alleged violation, to request a hearing.

In their request for hearing, the registered entity may elect either to have the hearing conducted according to the short form procedure or the full hearing procedure. In the event that the alleged violation becomes a confirmed violation, the region will issue the notice of confirmed violation to NERC and to the registered entity. The notice of confirmed violation looks very much like the notice of alleged violation. The notice of confirmed violation will normally have the same set of facts and circumstances and dates as in the notice of alleged violation. The notice will also include the proposed penalty amount, how it was arrived at, the duration of the violation, and that the proposed penalty is subject to review and possible revision, either by NERC or by FERC. The notice of confirmed violation will also indicate that NERC will, after their review process, file the notice of penalty with FERC with their determination.

Once the notice of confirmed violation is issued by the region, the registered entity has five business days to submit to NERC a statement that will accompany the notice of confirmed violation. So those are the notices and how violations are processed on the regional entity level. At any time during that

process, a registered entity may request that settlement discussions be initiated. As FERC indicated in the July third order, and in various other orders, settlement is looked upon very favorably as a method to resolve enforcement actions. Settlements have the advantages in terms of efficiency and effectiveness, but, most importantly, settlements serve to bring the registered entity into compliance quickly while avoiding what may be a long and lengthy hearing and appeals. The settlement process also provides the regional entity and the registered entity an opportunity to work together, and for the registered entity to come up with positive actions that will not only mitigate the violation in question but perhaps will enhance reliability of the bulk power system in other ways.

Settlement discussions can occur at any time until a notice of penalty is filed with FERC. They indeed may even occur before a notice of alleged violation is issued by the region or even after a hearing proceeding is requested, underway or after a decision has been rendered. Also, settlement discussions may occur more than once before final resolution is reached. Initial settlement discussions may not reach successful resolution but subsequent settlement discussions may yield a successful agreement.

How are settlement discussions initiated? The entity requests settlement discussions in writing to the region. Normally, there is an initial meeting in the regional entity's offices and then subsequent discussions can be held by phone, webex or in other locations.

Who participates in settlement discussions? The registered entity must designate in writing the name of the person who may negotiate and enter into a settlement agreement on their behalf. For *ReliabilityFirst*, as the director of compliance has the authority to negotiate and enter into a settlement agreement on the region's behalf. The designated negotiators of the registered entity may bring additional personnel, including counsel, into the discussions if they are going to be helpful to arriving at a settlement agreement. Once settlement discussions begin, the regions will notify NERC in writing, and NERC, at their discretion, may participate. *ReliabilityFirst* will normally issue a document entitled "Guidelines for Settlement Discussions," to the registered entity that will describe the settlement discussion process, name those who are designated to negotiate on behalf of each party, the time period (if any) that the region agrees to toll or suspend the due date for the next enforcement action, and other essential information. Are settlement discussions confidential? Absolutely, all settlement discussions are confidential and statements made during the settlement discussions will not be subject to discovery or admissible into evidence in any adversarial proceeding. Exclusions do apply, and *ReliabilityFirst* does have their settlement procedures published on their website, for detail on those exclusions.

Documents exchanged during the settlement discussion process must be marked properly in order that they are recognized as for settlement discussion purposes only. Although the settlement process may vary slightly from region to region, *ReliabilityFirst* reviews the terms of an offer for settlement from the viewpoint of a return to a compliant state and any further enhancement of reliability.

Credit is given for mitigating type actions that resolve the violation, but for a substantial reduction in penalty, the registered entity must offer to take actions that they would not be normally obligated to take in a mitigation plan that go

above and beyond those actions that would constitute a minimally acceptable mitigation plan. An emphasis is made that the settlement discussion arena is not the proper venue to argue or debate whether a violation actually occurred. Rather, whether a violation has occurred or not is set aside in order that an agreement that enhances the reliability system and resolves the issue successfully can be made.

Once the settlement is reached between the compliance staff and the entity, the details are reduced to writing and presented to the president of ReliabilityFirst for his approval. Once that occurs, the ReliabilityFirst board compliance committee is notified about the settlement, and the settlement is submitted to NERC. Notices of confirmed violation, when they are filed with FERC as notices of penalty, are made public. Settlement agreements will also be made public at the time of filing by NERC to FERC.

MR. WAX:

This is Bob Wax. Linda Walsh had to step out for a minute. But our next speaker is Ken Nickolai.

PRESENTATION BY KEN NICKOLAI

MR. NICKOLAI:

My role here is to talk about basics, so I will be going through this pretty quickly. But before I start, I wanted to say as a hearing officer so far. I feel a little bit like the Maytag repairman. I keep waiting for the call. But I can't tell you how excited I am to see so many of you lawyers here today and on the phone, because any time you get this many lawyers involved in a topic, there's going to be litigation. So thanks for all of you being here.

I'm going to start out by just reminding you that the 2005 Energy Policy Act established the system of penalties for violation of mandatory reliability standards, but also created the right to notice and an opportunity for a hearing to contest alleged violations. There's been some reference to these hearing procedures, and in Dave's presentation, he mentioned a bit about it. But where do you find them?

You find them in Attachment 2 to the Compliance Monitoring and Enforcement Program. Keep in mind, though, there are regional differences. For example, you won't find an Attachment 2 containing hearing procedures for MRO because they have simply adopted the NERC Attachment 2 by reference. But RFC and others do have their own separate Attachment 2 with some variations. And I will try to point out a couple of them just to give you a flavor of things to look for.

Now, my discussion is going to reflect the changes in the hearing processes that were filed by NERC and the regions on July 19, 2008. That filing was made in response to the March 21, 2008 FERC order. Let's take a quick overview of the process. The evidentiary hearing is generally held at the regional level. The

exception—and you're going to hear more about this—is if the regional entity has some operational responsibility potentially involved in an alleged violation, then it's going to be a NERC hearing. If an appeal is taken from the decision that arises from the hearing, then what you're going to have is a review of the record de novo by NERC and a review of the record de novo by FERC. When can you ask for a hearing? Well, the hearing procedures—and I will throw out a couple of numbers, but they are all in my materials—hearing procedures 1.3.1, to request a hearing in response to a notice of proposed violation and/or penalty. And as Bob just mentioned, you do that within a forty-day window depending on the particular act. After the compliance staff rejects your revised mitigation plan, you can also request a hearing, and again you have this forty-day window. And you can also request a hearing to contest a remedial action directive. And for that, I will give you the reference: it's 1.9.1 to the hearing procedures. The important thing to keep in mind there is that you have a two-day window to make your request for a hearing. There are several different kinds of hearings available under the hearing procedures. There's the full hearing. Those of you who have been involved in state and federal and administrative proceedings, it's real similar. Written witness testimony is going to be filed. It is going to be filed in advance. It is going to be subject to cross-examination. There are going to be briefs filed. But there's also a shortened hearing procedure. No oral testimony, only written submissions, and with a limited pre-hearing process. There's also a special, unique procedure for remedial action directive hearings, with shortened time frames, oral witness testimony, opening statements, closing arguments, staff rebuttal, and no briefs.

So make sure you think about the type of hearing that you can either request or that you are going to be in as you start moving down this road. Now, one of the questions is, and since this is a brand new system people have been wondering about, whether or not there were some safeguards in here to really assure that this was going to be a fair and impartial process. I'm just going to briefly mention a few of these, and Bob Wax is going to talk about some of this in more detail. But, yes, there is a prohibition on ex parte contacts.

There is a process for filing challenges and for the disqualification of both the hearing body members and the hearing officer; there are disclosure requirements for both the hearing officer and the technical advisor. There are ethical standards for conflicts of interest. And as I mentioned, Bob is going to talk about some of this in a little more detail.

Now, one thing that you won't see often is the use of a technical advisor. These hearing procedures do allow either the hearing officer or the hearing body to use a technical advisor. They do require that a technical advisor shall not have been involved in or consulted at any time in regard to any compliance staff investigation, initial determination of alleged penalty, et cetera, et cetera, with this case. One thing that's going to be different from your state or federal practice is that these hearings are closed to the public. Only members of the hearing body, the participants, the hearing officer or technical advisor are allowed to participate in or obtain information related to the proceeding. And interventions are not permitted.

Now, what about what type of evidence can you be using once you do get a hearing? Evidence is admissible if it's of a type, quote, commonly relied upon by reasonably prudent persons in the conduct of their affairs. The more stringent

traditional legal rules of evidence do not apply. Who has the burden? The burden of persuasion to establish the alleged non-compliance, the reasonableness of proposed penalty, the insufficiency of the proposed mitigation plan, or the compliance of the remedial action directive shall be required rests on the compliance staff. And of course the standard of proof is the preponderance of the evidence. These are all concepts very familiar to those of us who have been in administrative law for a number of years. Now, under these procedures, the hearing officer and the hearing body have the right to require a participant to address specific issues in testimony, evidence or briefs. It also has the right to require that they produce further evidence that is material and relevant to any issue, and the hearing body may issue questions or requests for information to any participant or witness at any time.

Now, that's the general provision on this. I want to talk to you for just a second about a regional variation, just to help give you a sense that you've got to be looking for these regional variations. And this is a regional variation in *ReliabilityFirst*. They are providing at 1.4.3(4): Any member of the hearing body may offer information or documents for submission into the record by motion provided, however, that the parties have fourteen days to object to the motion and may present testimony and other evidence related to the information offered through the motion. Well, once you get through the hearing, the evidentiary piece of the hearing, then the responsibility shifts to the hearing officer to come up with an initial opinion. The hearing officer will issue this initial opinion based on the evidence present, admit it into the record, and, yes, we're supposed to include the traditional findings of fact and conclusions of law and reasons for them and all recommended orders to dispose of the case. It is at that point that exceptions may be taken to the hearing body. Those exceptions are to be filed twenty-one days after the initial opinion is issued and replies can be filed fourteen days later. Notice that exceptions go to the hearing body. It's the hearing body that's the decisional body within each regional entity. I'll give you a couple of examples.

The *ReliabilityFirst* hearing body is composed of three independent directors and two stakeholder directors. But if you are in TRE, the hearing body is the Texas Public Utilities Commission. So, again, there are regional variations. Now, under the general process, the hearing body does have the option to hear oral argument but is not required to. The hearing body has authority to adopt, modify, amend or reject the initial opinion in its entirety or in part. The hearing body may, of course, remand the matter back to the hearing officer for further work if it wishes to.

What about some time limits? The hearing body is to "strive" to issue its final order within thirty days of the oral argument or the conclusion of briefing. It has only ten days to issue a decision in the remedial action directive case and thirty days after that to issue a full written decision. Now, how do you get this final decision of the hearing body? Well, there is a hearing clerk within the regional entity that will serve the final order on all parties with a notice of their right to appeal to NERC.

Now, the appeal is made under Section 1410 of NERC's rules and procedure and may be taken by an owner/operator or user of the bulk power system. And as has been mentioned, further appeal can be taken to FERC from the NERC decision. And if FERC does decide to review the case, they've

indicated they'll review the record de novo. So that's a very quick introduction to the basics, and I will turn this over to Bob Wax.

PRESENTATION BY ROBERT WAX

MR. WAX:

Thank you, Ken. I am part two of our agenda segment today on the hearing process at the regional entities. Ken just did an excellent job of giving you the nuts and bolts. His materials are a good primer. My assigned task is to deal with a number of selected issues and potential challenges in this arena, particularly with respect to so-called general hearings.

I'm going to give a couple caveats first before I provide my remarks. As my bio reflects, and as Linda introduced me, I'm a full-time professional neutral who is going to be an independent neutral hearing officer on these cases as they unfold. Specifically, I'm already contracted with five of the eight regional entities. For that reason, any thoughts or comments that I make today should not be viewed by anybody as binding determinations or opinions on any procedural or substantive question that might come before me in an actual case. I'm also not speaking for any particular RE or anyone else, for that matter, other than myself.

My remarks today are based solely on, first of all, my reading of the forty page rules and procedures currently in force in nearly all the organizations; conversations that I have had with regional entity compliance committee members or staff and fellow hearing officers; what I observed in a mock hearing that was conducted at one RE about eight, or ten months ago; my long-time experience in FERC litigation; and, more importantly, in large energy industry arbitrations, including those at RTOs and ISOs. I'm well aware that a number of people in the audience and on the phone are architects of the hearing procedures and are more knowledgeable about them than I am at this point. So bear with me if I misstate something in that arena. And, then the last caveat: as Dave Cook pointed out, there have been no actual hearings; therefore, I have not actually handled one yet, so my observations, by definition, are purely speculative. I hope it is well-informed speculation, but, again, nothing I say is binding. Turning to the topics I will cover today, and I will go over this briefly.

First, I'm going to talk about where are the hearing officers coming from, and, more importantly, what practitioners' expectations should be as to their independence, integrity and impartiality, which is a very important consideration in this process. Next, I'm going to address how I think the hearing officers are going to interface with the hearing bodies that you've heard about. After that, I will discuss how I now envision a pre-hearing conference will proceed. Then, I will talk a little bit about discovery and how I think that is going to unfold. Next, I'm going to mention a potentially thorny issue out there on interlocutory review of hearing officer decisions. And, lastly, I will briefly discuss whether the formal, alternative dispute resolution mechanisms, like mediation, will and should have a role in these kind of cases.

Turning to independence and integrity, my first sub-topic: how will the litigants know that the hearing processes will involve a fair hearing in full compliance with due process, as in the courts, with FERC and its ALJs, and with arbitrators in a contractual, commercial environment. The first answer is the

procedure and rules require it, and they were specifically designed to do just that, and that is being done by requiring the regional entities to contract with or employ independent neutral hearing officers bound by strict codes of ethics and conflicts.

The second answer to the question of how do we know this is all going to be fair is related to the evolving mechanisms at many of the REs to create a pool—and I put that in quotation marks—of hearing officers like me; like Ken Nicholai, who you just heard from—a former ALJ and State commissioner; like Steve Shapiro, who is here today with us, a former FERC ADR guru; and like Jack Lotus who is a former FERC ALJ. All of us have been designated as hearing officers at one or more of the regional entities at this point. And in addition to that, each RE has done something a little different to assure independence and neutrality, but all, to my observation, are following the rules and creating the proper mechanisms. They have safeguards against selection or appointment in specific cases to assure that there are no undue ties between the RE's compliance staff, the prosecutor, as Bob Wargo alluded to, and the judge, the hearing officer.

My third answer about impartiality is that there are mechanisms in the rules and at the REs—and Ken alluded to these—by which the hearing officers will make full disclosure of their specific qualifications and any arguable conflicts they might have in any particular case that is assigned to them. It seems to me that coupled with the procedure, allowing the participant to move to disqualify and for the hearing body to replace the assigned hearing officer if a real issue exists, which I don't think it will in most cases give, in my view, extra assurance of fairness of the process. Obviously, there are no guarantees, and ultimately history will tell if the procedures work and that neutrality is fully maintained in all cases. But as an individual who guards his independence and neutrality with great care, as my sole “stock in trade”, I have every reason to believe that the mechanisms are complete, they are fair, and they will work to protect the impartiality of the process.

My next area of discussion is how the hearing body and the hearing officer are going to interrelate. The first question here is, will there always be a hearing officer or might the hearing body sit alone as a committee of the whole or a sub-committee to adjudicate a case without a hearing officer, which the rules certainly permit? My simple guess on this question is there will be a hearing officer in all or nearly all cases. I base that on my discussion with at least three hearing bodies, typically the regional entities compliance committee or a subpart, and they realize, I think, that those committees are mostly made up of non-lawyers with other full-time jobs, and, generally will need to have an experienced hearing officer to deal with the complex litigation and give them an initial decision to review. And rest assured, in my view, if a given hearing body decides to do one of these cases alone without a hearing officer, that they ultimately will become so occupied, so frustrated, and so overwhelmed by the litigation world that everybody in this room knows about, that when it comes their way, again in the next case, they will have a hearing officer aboard for that proceeding.

The next question in this arena is: are members of the hearing body going to attend the hearings when they are conducted? Again, based on my contacts with potential hearing body members to date, I think the answer is probably yes,

particularly in the first cases at any particular regional entity, before the hearing body becomes fully comfortable with the process, before they become comfortable with their role, and mostly before they become comfortable with the expertise of their hearing officers. But I think that once the hearing bodies and the subparts of them see how “sausage” is made in a litigation environment such as this, they, or probably many of them, will not want to come to a future case. That’s at least my guess.

That gets me to the next question: if some or all of the hearing body is there and there is a hearing officer, what’s the role of the hearing body at the hearing? I think this is going to vary a bit from regional entity to regional entity, from hearing officer to hearing officer, and from case to case. The rules make it clear that the hearing body can attend, and in the RFC rules it goes on and talks about them submitting questions to any participant, witness, et cetera. The way I imagine this evolving in cases in which I’m going to be involved is after discussion with the hearing body and the participants will be to have the hearing body submit questions and requests for briefing topics through me, which will then be passed on to witnesses who are on the stand or the lawyers at the end of the case. If it involves questions in the examination context, counsel will then have an opportunity to obviously ask any follow-up they want on cross or redirect. I recognize that this is an area that’s going to need some delicacy. There’s going to be some evolution to make it work right between the hearing officer, the hearing body and the participants, but I’m confident that ultimately it will work out smoothly and fairly to all.

Finally, keep in mind that in this area of the hearing body and the hearing officer interface, the rules provide that it’s the hearing officer who issues a proposed ruling if a request is made to disqualify a member of the hearing body in a given case. That’s the way it works under RFC, for example. That reflects my view of the close way that the hearing bodies and the hearing officers are going to have to work together as these cases evolve.

Let’s talk for a minute about the pre-hearing conference in one of these cases, the crucial first step in shaping the entire process. This is probably a good place for me to comment on what do I think these cases are going to look like, in general, when they actually take place. Simply put, I think they are going to look like a cross between a fully-litigated FERC case, with which probably most of the people in the room and on the phone are familiar, and a complex arbitration such as at the ISOs or at the regional transmission organizations. And why do I think that? One, that’s how the rules and procedures are structured. They were drafted by FERC litigators largely. Two, practitioners who will be called on to do these cases come from that world; hence, the significant turnout of those we have in the room and on the phone. So we are likely to see multiple witnesses, expert witnesses, prepared direct testimony, pre-filed exhibits, a tough cross-examination, a detailed redirect examination, preliminary motions, pre- and post-hearing briefs, and lots of to and fro between the counsel for the regional entity and the respondent party’s attorney. I think this will basically adapt to a FERC type model, just as the regional transmission organization, and ISO arbitrations have. You can just ask Linda Walsh, who litigated one of those cases in front of me about three and a half to four years ago, and that’s basically the model that it took on in many ways. That all makes the pre-hearing conference in these cases crucial once there is one. The discovery rules will

have to be set, how preliminary matters are going to be handled, the overall scheduling, et cetera. My guess is in the first few cases, if not always, those pre-hearing conferences are probably going to be in person, probably at the location of the regional entity involved, because there's going to be so much to discuss to shape the case.

This is probably the appropriate moment for me to comment on one early case matter, and that is the subject of motions for summary disposition. The rules permit it in 1.5.3, and hypothetically I guess we're talking about an argument that somebody has that one of the applicable standards is faulty or unclear or, even worse, unconstitutional, or one just can't apply that standard to the facts of a given case, for whatever reason, and there is no dispute as to the facts. The rules will permit it. I suspect that some of these will be filed in early cases, particularly. That's a pattern that I've come to see in major commercial arbitrations and it's happening in almost every one of these cases. It's a function largely of the fact that litigators now are doing arbitrations, and I think that really is the reason that it will come here as well. Sometimes such motions can be quite legitimate tools, and I recognize that. But I urge counsel as these reliability standards cases unfold to think carefully about such motions at the beginning of the cases, and particularly ask yourself a few questions before you file one of these if there is a typical contested matter. Are you doing it just to educate the hearing officer? If you are doing it for that reason, keep in mind that he or she probably is a very experienced and knowledgeable person about the subject area and really doesn't need to have that tool for their education. They are going to have that in a pre-hearing brief.

Next, ask yourself how likely are such motions to prevail, or is it most likely that the hearing officer will do what is probably the most prudent thing to do, and that is to await a hearing to make such a definitive ruling, particularly for any facts that are arguably at issue at all. And, lastly, having thought about those two things, I would urge people to consider whether the cost of doing such a summary disposition for your clients really outweighs the potential of ultimate success in your minds. Obviously, counsel needs to do what it needs to do, depending on the facts in a given case. And I'm not opining one way or another about how I would view such a motion in any particular case.

Next topic, discovery. I'm going to brush over this lightly due to the time constraints, and maybe there will be some questions at the end. First, what is this going to look like in this setting? They are going to look like FERC discovery "games and adventures," because the rules say that. Suffice it to say, I expect there's going to be lots of interest in lots of discovery. I expect that the hearing officers are going to be called upon to impose limitations on some aspects such as depositions and to move a case along, and that may be indeed necessary, because there are time frames in here that are tough to meet. That is, there's a goal in the rules to have an initial decision within six months, so something's going to have to give as these cases evolve, particularly if they're complex. I suspect there are going to be discovery disputes that the hearing officers are going to need to decide, but I think the real answer on this question just won't become clear until a number of cases unfold.

Next item, interlocutory review. Again, I will only touch upon this lightly. By the rules, the hearing body needs to take up any interlocutory review request from the hearing officer's determinations, either preliminary or as the course of

the hearings evolve. And there are some very tight time frames that you can find in the rules for that, seven days, fourteen days, et cetera. My guess is that in early cases, the hearing body is going to be tested by the litigants and a number of these are going to come up. Whether they are to educate the hearing body early, to slow down the case, or for whatever reason, I think we are going to see some of these. But I also guess that over time, as the hearing bodies again gain confidence in their hearing officers and become, frankly, tired of doing these kinds of interlocutory appeals, the numbers are going to greatly drop off and simplify the litigation process, and I think that because particularly in light of the standard that's in the rules, which is 1.4.4, of how a hearing body is supposed to rule on one of these. That requires "extraordinary circumstances," which make a prompt review necessary to prevent prejudice. So it seems to me that this is a standard by which that if the hearing body wanted to duck things—and I use those words advisedly—it probably could and let the underlying issue "go with the case" for decision at the end.

That gets me to my last slide, alternative dispute resolution. I felt I needed to comment on that today for two reasons: one, the EBA's ADR section is, after all, a co-sponsor of this session, and I'm vice-chair of that section, so I didn't think I could get away without saying something on this subject. Tom Burgess, when he speaks after me in a moment will address this topic and discuss explicit reference in NERC's procedures for the use of mediation in these cases. But when it comes to using something like formal facilitative mediation in the regional entity hearing cases, I can be corrected, but I'm not aware of anything in the rules or the mechanisms in place or currently being planned that really call for that. We all know there is plenty in the process for settlement. Bob Wargo described that at length, and it is at the heart of the process, as he described, but there is nothing explicit about the opportunity for formal mediation or an akin tool. As an experienced mediator of disputes in this industry, I find that disappointing, because I think it could be a very helpful addition to the process. It can be a powerful tool to lead to settlements. But I suspect this is a topic for the future, not for now, at the regional entities as the world evolves, and I would just, for one, urge folks like Bob Wargo and others to keep that topic and idea in the front of their minds for future focus as a means of getting a better process and result in their cases.

And with that, I'm going to turn it back to Linda. But before I do that, as co-chair of this program, I would be remiss if I did not thank Linda and Hunton & Williams on behalf of all of us for providing this wonderful space for the meeting and the great technical assistance which was really called upon and worked, and having us here today. Thank you. With that, I will turn it back to Linda.

MS. WALSH:

Thanks, Bob. The next speaker here is Tom Burgess from FirstEnergy.

PRESENTATION BY TOM BURGESS

MR. BURGESS:

Thanks, Linda. Thank you, everybody, on my behalf and for the opportunity to provide some insight into the development of some of these

different types of approaches to dealing with disputes and their resolution. What you heard thus far has been what I would refer to as the direct process that's associated with moving through the hearings and the alleged violations and so forth, whether those arise from the regions or from NERC's compliance monitoring and enforcement perspective. What I'm going to refer to really is kind of a second route through an analogous process, which is one way of looking at it, or as an alternative mechanism that is in place that allows in certain cases for the NERC Compliance and Certification Committee to stand in the role as the hearing body itself. There are a number of situations where that arises, and I will give you some examples of those.

Let me set the stage for why the NERC CCC, the Compliance and Certification Committee, is at all called upon to be serving in the role of a hearing body. Really, its genesis lay in the Certification Order of the ERO by FERC, which recognized that there was a need for an entity to have some authority for oversight for the programs, the procedures and the processes that NERC and the regions were using to conduct their activities according to their Rules of Procedure, and that there was a need to have these types of hearing procedures. And so explicit recognition was given in those orders for the CCC to serve in that capacity. So, primarily, where this comes into play is in situations where NERC is doing the direct enforcement of the reliability action at hand. And there are a number of those circumstances that can arise. As a member of the CCC, I helped frame up how these procedures really are intended to function, and so what I would like to do is describe how those have come to be structured, what those look like, how they are intended to function, and what you might want to have as some take-away information. I've provided most of that in the slides, and so you can refer to those at your leisure.

I want to caveat what I'm going to describe, however, because these are currently in the form of fledgling procedures. They have been formalized, they've been approved by the Compliance and Certification Committee, they are currently out for comment, and we expect that the NERC Board of Trustees would, in fact, approve these by the end of the month. So while they are not in force as of the moment, we expect that shortly they will be in force and will become effective within the rule of procedure filing made by NERC. So when NERC is the enforcer of reliability compliance action at hand, there are a couple of situations which arise when the CCC can step in to serve as the hearing body. One is in which the regional entity itself is performing certain reliability functions. As Dave mentioned by example, Western Electricity Coordination Council (WECC) is performing the reliability coordinator functions. So they are an active reliability entity, and to the extent that there are issues that arise in their execution of that function and a dispute emerges, then the CCC is the body that is called upon to serve as the hearing body. Another situation is when there are appeals from a certification proceeding by a registered entity.

So why don't I shift and talk a little bit about the makeup of the CCC, as a lot of you may not be familiar with this group. It's a board-appointed stakeholder committee, so these individuals are all elected to serve on this committee. They are representative of different sectors of the industry. This group serves and reports directly to the Board of Trustees and it advises the Board Compliance Committee. It has a number of roles, among them are to monitor NERC's adherence to certain reliability standards that apply to NERC

itself. It also has a role to oversee NERC's adherence to various Rules of Procedure relating to how the Compliance Monitoring and Enforcement Program is conducted, how the Organizational Registration and Certification Program is conducted, and how the Reliability Standards Development Procedure is implemented. So it has the functions and roles of providing oversight and perspective from a stakeholder view as to how these various programs are conducted. It also advises the Board of Trustees about stakeholder perceptions of the effectiveness of the overall Compliance and Monitoring Enforcement Program. And then lastly it serves in this hearing body capacity.

So what are some examples of the situations where the CCC would have a role to play as the hearing body? One of those is where NERC is directly monitoring an entity for compliance. There is a provision in the rules of procedure where a registered entity itself could be directly monitored by NERC for compliance enforcement or reliability enforcement. That can also occur where there is an agreement with the regional entity. Now, while that provision is currently present in the Rules of Procedure, I don't anticipate that there are very many, if any, situations in which that would come to pass.

The second possibility is where NERC is directly monitoring a regional entity for adherence with the approved standards that apply to the region itself. That's a situation where the regional entity is actually performing some operational functions, some reliability functions, for example in the case of WECC performing the reliability coordinator function or in the case of other regional entities performing similar reliability functions. I believe that approximately half of the regions are performing some type of reliability function, which means that compliance with reliability standards follows. And so these are clearly situations where this could arise. This second situation is a more likely situation that could arise.

The next circumstance is where NERC has made a decision on certification, and the entity seeking registration or certification is contesting or disputing that decision. In that case, the CCC would be the hearing body. My personal perspective suggests that is probably a medium situation. As Dave mentioned, there are presently 1,900 registered entities already in place. Many of those key registered functions, the balancing authority, the transmission operator and the reliability coordinator, already have been certified so there's not very many situations where disputes would arise.

And lastly, where NERC is actually conducting a compliance audit of the Compliance Monitoring Enforcement Program of a regional entity and there is a dispute as to the conclusions of that audit between the region and NERC. While those audits have not been initiated yet, I understand that NERC is beginning process this year and probably the many regional entities would be audited during next year. So what does the procedure itself look like? Well, it's modeled, frankly, to align very closely to the existing NERC compliance hearing procedures. The one exception or the one major difference then is that the CCC is the body that hears that proceeding. Procedurally, there are many of the same features are in place: The pre-hearing conferences, evidentiary procedures, post-evidentiary procedures, a variety of options for settlement and so forth. All very similar to the type of procedural set-up that is present in the NERC hearing proceedings.

How does the panel get formed? Well, the CCC is comprised of a group of Board of Trustees-appointed stakeholder individuals, and what happens is there is an nomination of candidates to serve on the panel, there's a determination by the Officers of the CCC, and as many as five members plus alternates who serve on this panel. There are provisions to recuse or excuse individuals with conflicts of interest. The one feature that's relevant to the formation of the panel is that it is set up in such a way that no single industry segment (that is, of the comprised CCC members) could block whatever is the conclusion or the decision of the hearing body.

In terms of the disposition of the matter, the CCC acts just like a hearing body. It issues a final order to the Board of Trustees Compliance Committee. The final order includes statements of fact, findings and conclusions, reasons or bases for findings, penalties, sanctions, remedial actions, et cetera. These final orders, so-called final orders, then can be appealed to the NERC Board of Trustees' Compliance Committee. So the procedural underpinnings of the CCC's hearing processes are very similar to, and in fact modeled after, those that are present in the hearing procedures that Ken and Bob spoke of; the major distinction being the body itself is comprised of the members of the CCC.

There is an expedited version of the proceedings, and it's applicable when there is a question or dispute about the certification of an registered entity. Certification is required currently for reliability coordinators, balancing authorities, and transmission operators. It's a streamlined version of the above described hearing procedures with a very condensed type of process. In addition to the hearing procedures, an additional feature that is encouraged for parties and is in place under the CCC umbrella ensures that there are explicit provisions for a mediation procedure. It's a voluntary procedure where there are disagreements between NERC and the regional entities. Those disputes can be handled with this voluntary mediation process. In that setting, the CCC would appoint three disinterested (those without conflicts of interest) members of the CCC to serve as the mediation panel to help facilitate resolution of the matter. There's also provisions to allow a hearing officer to help facilitate the mediation process. And, again, the results of the mediation process would culminate in a formalized settlement agreement which would then be binding on the parties. At the same time, if the mediation proceedings are unsuccessful and don't reach closure, it is always possible to revert to one of the different types of hearing proceedings.

A couple of key aspects about this combination of CCC hearing and mediation procedures: first of all, I mentioned that these procedures, while they've been formalized to mirror the NERC proceedings, they are not as of this moment approved. However, the NERC hearing procedures provide a good guideline about how these proceedings would be conducted. And while we on the CCC expect that approval before long, it is important to keep in mind that they are in a state of pre-approval, at this time. There is some fluidity associated with how the CCC appeals and the mediations processes would unfold, in part because you are dealing with a body of stakeholders, which on an annual basis that body of stakeholders does undergo some rotations, so there is some fluidity there. At the same time, there is a fair degree of certainty associated with it in that the procedural underpinnings are very much mirrored after the way that NERC itself has formulated the proceedings, and the expectation is that

Administrative Law Judges in most cases would be retained to procedurally guide the processes.

One last aspect involves confidentiality, which can be a particularly challenging issue in these kind of proceedings. The CCC has also developed a confidentiality protocol that covers how to tackle and deal with all of those types of issues that arise during the course of one of these proceedings.

Ultimately, in closing, I think that FERC envisions some important roles for the CCC both in an oversight capacity of monitoring the things that NERC itself was undertaking, as well as to serve as another resource for hearing and mediating disputes that may arise where NERC itself is the enforcing body. I think that there's an increasing likelihood that the CCC is going to be called to play a bigger role as some of these enforcement actions move their way through the pipeline. As the audit processes with the regional entities begins to unfold, I think we are going to see a likely increased use of these proceedings. Hopefully before year end, we will have these formalized, approved by the Board of Trustees and eventually FERC, and ultimately effective for NERC, registered entities, and practitioners. And with that, I would like to hand it over to Linda to entertain your questions.

MS. WALSH:

Thank you, Tom. Next, we have Kathleen Barrón at FERC. Thank you.

PRESENTATION BY KATHLEEN BARRÓN

MS. BARRÓN:

Good afternoon. I am thrilled to be here and to have the opportunity to hear the thoughts of my co-panelists. Those of you who have been there know that 888 First Street is pretty far from an ivory tower. It would need better coffee if it were. But at times, it can feel like one. We spend a huge amount of time reading the paper that is submitted to us, but because of our ex parte and general conflict-of-interest concerns, we are not able to talk to folks or to see all of the orders that we've been working on come to life. It is obvious from what you've heard today that the registered entities and the regions and NERC are spending a tremendous amount of time putting this hearing and appeals process together to unfold in the coming years. And it's amazing, since it's been three years since the legislation was passed and more than a year since the mandatory standards took effect, that we are still at the very, very beginning of this process, and from the Commission's perspective, having really only received that first group of thirty-seven notices of penalty that Dave alluded to, we really are at the very beginning of the enforcement side of this program.

While it is clear that the companies and the reliability organizations have spent years and years and years taking seriously the reliability of the grid, we at the Commission are somewhat new to this, and the law firms are even newer to it. The Energy Bar has somewhat of a learning curve to climb, and I think programs like this are a great opportunity to get people familiar with what the CVIs and NAVs and all the other acronyms we heard about earlier mean, and

also to prepare your clients, to the extent you are retained to do so, for a CVI at a regional entity or an investigation at the Commission.

So I thought I would take a step back before I jump into what we are doing on the enforcement side to talk about what FERC is doing generally in the reliability program. Our primary statutory function, of course, is to approve standards and rules that the industry develops through NERC. We've adjudicated a number of registry appeals from entities that were not pleased with the registrations that they received; we approve the budgets for NERC and the regions; we opine on standard interpretations; our reliability staff participates in event analyses from time to time; and of course we are participating in and, in some cases, conducting audits. The last two elements of our role are what we are here today to discuss. First, the review of notices of penalty, including the mitigation plans that are developed, that come to the Commission after working their way through the process you heard about and second, in some cases, the independent investigation of violations.

The Commission's activity is centered in three of our five program offices. First, the Office of Electric Reliability, most of which is comprised of engineers who were trained and worked at many of your clients. These are the technical advisors to the Commission, both in standards development and then pertinent here to the adequacy of the mitigation plans that are submitted along with the notices of penalty. Second, our Office of Enforcement has a subset of our reliability program workload in developing the procedural rules that you heard about today, and then in participating in audits, and then on certain occasions conducting investigations. Clearly, they have been investigating rule violations for a long time, so they bring to the table the Commission's expertise in discovery and data collections, sorting out what happened and how what happened fits with the Commission's rules. And then my office is the Office of the General Counsel. We are there to advise the Commission when it takes official action. In the most narrow sense, we are responsible for the legal sufficiency of the Commission's position and with advising the Commission on the likelihood that its position will survive court review. Obviously, lawyers are not—on the standards drafting teams or doing event analyses, but to the extent the Commission takes official action on a standard or rule or budget or a registry appeal or a notice of penalty, my office would be advising the Commission on the legal basis of its actions. But it's important to emphasize that the primary responsibility for enforcement of the reliability standards, just like the primary responsibility for developing the reliability standards, is with the regions and NERC and registered entities participating in that effort. We are sort of the top of a triangle of the primary actors in this arena, and I think that's important to recognize; this concept of subsidiarity, that the entity that's the least centralized, competent authority, the one that is closest to the actor, should be the one taking action, and that's why this process has been set up so that the regions and NERC are the primary enforcers.

Turning to the first of the two functions I'm going to discuss today; this year has been hopefully somewhat illuminating for the bar. The Commission has issued two orders to further elucidate what it intends to do when notices of penalty and mitigation plans are submitted to the Commission. The process is pretty simple. The paradigm is that most notices of penalty that come to the Commission should take effect by operation of law after thirty days. Again, this

is founded in the notion of subsidiarity; that the people who are on the ground enforcing the standards are going to do the best job at figuring out what happened and figuring out what the consequence should be and in most cases the Commission should let the notice of penalty take effect by operation of law. However, if the entity subject to the notice of penalty or the Commission on its own decides that that thirty day clock should be stopped, the rules do permit that to happen. Alternatively, if the Commission can't make that determination in thirty days, it did reserve to itself the ability to issue a tolling order to give itself a little more time to decide whether to initiate review. But if review is initiated either by the subject of the NOP or the Commission, there will be a process such as an answer and the possibility for intervention and then hopefully Commission action within sixty days. In the order the Commission issued in April, it discussed which NOPs it expected that it would elect to review on its own motion. And when I say review, there may be some confusion about what Commission review means. Obviously, every notice of penalty that gets sent to the Commission will get reviewed in some capacity, but review in this context means reviewed more closely or with more in-depth scrutiny.

There are a number of factors the Commission expected would lead to a Commission review. Obviously, this will evolve over time. We have had so few of these. And it may be that these can be more refined as time goes by. But clearly a critical factor will be the violation severity level and violation risk factor associated with the violation. Presumably, most of you are familiar with what those two terms mean. If you're not, you can ask me in the question-and-answer period or ask anyone else up here. But, secondarily, the next three factors are quite general: The risk to reliability of the bulk power system; a review to ensure that, in general, penalties are being applied consistently; and then sort of a catchall, to the extent review is necessary to improve compliance which is, of course, the purpose of the enforcement program generally. And, in general, the Commission has stated that it will stay any proposed penalty that it elects to review if it's a monetary penalty and if it is later affirmed, it would be paid with interest.

With respect to the standards that are applicable to Commission review of a notice of penalty, the statute gives us one: the penalty shall bear a reasonable relation to the seriousness of the violation and shall take into consideration the efforts of the registered entity to remedy the violation in a timely manner. NERC and the industry, working together, have developed, as you know, an enormous number of guidelines, the sanction guidelines and others, to determine exactly how a penalty is to be assessed. Violation risk factors and violation severity levels are a big part of that, the penalty amount table is a big part of that, and then there are a number of factors such as the history of the company's compliance and its compliance program in general which is, of course, quite an important factor for the Commission, cooperation, attempts to conceal, and so on. There are a host of factors that play into how this general statutory standard is to be interpreted and applied at the regional entity and NERC level, and having approved those factors and having them consistent with the Commission's enforcement policy generally, they will also be considered by the Commission on review of notices of penalty. The Commission also said that it would review de novo to ascertain whether the record contains adequate evidence for the penalty determination. Even among my expert co-panelists,

there is some confusion about what that means. And it was perhaps an unartful way to reflect what I think the Commission will do. While I cannot speak for the Commission, to the extent that people think *de novo* means *trial de novo*, I don't believe that is the Commission's expectation, to retry from the beginning and start over, throw out the record and have all the witnesses come in and take the stand again, although, of course, there is the capacity to remand the case or to set it for hearing if the facts are not adequate in the record. But *de novo* in this context, I think, means this sort of generic Latin "let's look at it fresh, let's look at it anew, and let's look at the record closely." So, hopefully, that puts your mind at ease that all your work will not be in vain.

The next slide is about record development generally. This is absolutely critical to the Commission, having just explained what I think *de novo* means. The record that the Commission receives is paramount in its ability to do its job. And in the July third order, the Commission gave some good guidance for the regional entities and to NERC, but the practitioners, I think, really need to pay attention to this as much as anyone. If you are thrilled and overjoyed with the result of your proceeding at the regional entity because you came out with the exact result you wanted but the record doesn't address the things that I'll go through in a minute, in other words, it isn't otherwise substantial enough to support the outcome that you received, you know, you might not be happy at the end of the day. So it is in everyone's interest to make sure that the record that is put together is as complete as possible on these issues and any other issues that the Commission has highlighted in its orders. But as I alluded to, in the July third order, the Commission elected not to review the first thirty-seven notices of penalty, but took the opportunity to give some guidance on some issues. The first of which is making clear what violation is being addressed. If the notice of penalty doesn't explicitly say what was violated and when it was violated, the Commission is going to be scratching its head. Did the RE apply the requirement that each individual violation be considered individually? This is just one of the things you want to have checked the box, that you explain exactly what happened, how often it happened, and how you took that into account in the way you developed both the mitigation plan and any potential penalty.

The second issue is making sure that if you have a violation that involves a standard that has a high violation risk factor and a high violation severity level that you, the regional entity and NERC, have accurately explained how that has translated into the recommendation or into the penalty that has resulted. In the July third order, there was an example given by the Commission of a statement in one of the particular notices of penalty that a violation was inconsequential, but the violation involved a standard that had a high violation risk factor, which by definition is something that if this standard was violated it could cause or directly contribute to bulk power system instability. In that kind of situation, you are going to want to have explained how those two potentially conflicting statements were reconciled in the mind of the decision-maker and are reflected in the recommendation in the notice of penalty. One potential explanation for that may be this concept of first violations, which appears in the sanctions guidelines and allows the regional entity to have a zero penalty when it's the first incidence of a violation, the impact is inconsequential, and other factors do not increase the likelihood that there could have been harm.

Next, the Commission discussed the idea that when a notice of penalty is submitted to the Commission, there should be a clear explanation of the factors that were considered in reaching that penalty and how they relate to the violation that's at issue in the notice of penalty. As opposed to having a list of fifteen factors and the result, the idea is that there should be more of a discussion of how the different factors affected the conclusion that was reached in a way that is individual to each particular event. Not every event is the same, not every factor should be weighed the same way in every case, and so there needs to be some recognition that each one is looked at individually and the factors are considered appropriately each time.

The next issue is really, in my mind, one of the most important elements of the notice of penalty. The mitigation plans are the whole point of this process. If they are not optimal and if they haven't actually been complied with, if the regional entity does not verify that they have been complied with, then the Commission is left scratching its head as to whether the problem been solved or not. So, enough facts about what the plan was, how it remedies the violation, and what's been done to verify that it's been completed are all going to be critical. In general, the culture of compliance among the companies is something that the bar can help your clients demonstrate. This is, as I mentioned earlier, incredibly important to the Commission and is something that if it comes through in a notice of penalty it gives the Commission a sense that the violation will not occur again. And the consistency is something Linda asked about earlier. It's the last point I made on record development but it's the first point on my next slide which is about challenges. This is a very important role that NERC and the Commission play, and it's very challenging, particularly when we have so few cases that have made their way through. But for the registered entities, I expect that this is one of their primary concerns, that they want to see this program being implemented consistently across the regions, particularly for those who do business across multiples REs. It doesn't do anybody any good when there is not a clear understanding of what can be expected in the different regions.

The next challenge is just the sheer volume. You've heard enough about this today from NERC's last budget filing. We understand that there are 1,400 alleged violations still moving their way through the pipeline, and having only received 105 of them, we are certainly a little worried about that. I know NERC is a little too. Pushing those through and getting them resolved is something that we are focusing on. Just the newness of this whole process is sort of a theme we have had heard today, and particularly from me, from the Commission's perspective, the newness of this process, in general, the relatively small number of compliance investigations that are underway, and the fact that we have had no hearings means we feel like we are making something new up, that we are always addressing a new situation. And that will change over time, obviously, but it is a challenge for us as we work through this process. And then, lastly, keeping the focus on compliance and mitigation plans. That's, as I said, that's what we are here for.

I'm going to talk just for a second about the second function that I alluded to earlier, and that is the Commission's conduct of its own investigations. Obviously, I can't discuss that in any detail. But I do think these issues are, in general, relevant both for CVIs, for compliance violation investigations, that

your clients may be involved with at the regions, as well as FERC investigations under part 1(b) of our regulations. The first point is that these cases are all ones of first impression. The standards took an enormous amount of time to develop, and many of them are still under development. Each time you have to interpret one and apply to it a set of facts, you are making law, and that's a challenge.

Another point is that these cases, in particular, are different in that they involve, in many cases, physical activities, so you may see investigators coming out quickly on site. It's not the kind of thing where you can schedule a meeting or a deposition or a tabletop discussion in three weeks. You are going to want to go out right away and find out exactly what happened, and you are going to want to look at that equipment, because, obviously, the registered entity is going to want to get that equipment fixed and back in service. And so your observation opportunities of what happened are going to go away quickly.

That to me relates to another issue in investigations, which is that the people who actually know something—not the lawyers—the engineers and the people who operate the system, are going to be looking at an events analysis or just generally what happened, what went wrong, how do I fix it. They are not the kind of people, like us, who are collecting evidence or preserving a chain of custody or developing a record or the kinds of things that you would have to do if you were expecting to be in court some day. So it is sort of a mismatch between the two different types of analyses of these events and the physical nature of them, and I think it's a challenge that we have as you advise your clients and as the regions' compliance staffs endeavor to put these cases together. The Commission, in its orders, did reserve the ability to do joint investigations with the regions. I don't really think you have to think about that for five minutes to realize that it will be challenging to investigate with multiple entities involved in the same activity. So that's all I will say about that.

And then, lastly, with the standards having over a thousand different requirements, when you add them all up, there is a potential for overlap. And so there's the need to figure out exactly what you are focusing on. And, again, this is the difference between how a lawyer might approach an investigation and how an engineer doing an event analysis might approach it. Instead of just figuring out what went wrong, the lawyer needs to figure out which standard or standards are involved, what happened, and then assign the violation severity level to it; in other words, if it was violated, how badly it was violated.

So what's next? The Commission has a number of cases pending before it, including rehearing on the violations severity levels; the order on the last CMEP compliance filing; we are expecting that in due course notices of penalty for the post-December 31, 2007 period will hit our door. As you recall, for the first roughly six months of the reliability standards being mandatory and enforceable, the Commission asked the regions to use their discretion in enforcement, so post-December 31, 2007 will be after that six-month period. There will be some audit results. And then the ERO is due to submit a performance assessment to the Commission in June 2009. And one of the many—sorry, Dave, there's a lot of things that have been put into that assessment -- but one of them is the efficacy and fairness of the hearing procedures to the extent there have been any hearings by June 2009.

MR. COOK:

That may be the easiest one to deal with.

MS. BARRÓN:

Right. So there will hopefully be an opportunity, to the extent the hearings have occurred, to take a step back and look at whether they did their job. So, in closing, I look forward to your questions. I don't think I can overstate the idea that the Commission takes this new responsibility under FPA very seriously and is committed to recruiting the highest quality staff that we can to help us implement these responsibilities and advise the commissioners. But we are at the beginning and this will need to play out. So I would urge you to stress to your clients that it is important to keep the lines of communication open with the Commission, and since this process is evolving, many of the things I've said today could change, so get involved if you want to have an impact. Thank you.

MS. WALSH:

Well, thank you to all of our speakers. I think they did a very good job. And we are going to take some questions from the folks here in the room, and then we will take questions from callers. And if the operator could maybe get that started. We will start with questions here in the room. Does anyone have a question for any one of the six panelists? Ken?

MR. BARRY:

Yes, I want to ask Dave something. Starting with that remarkable number of 1,400 alleged violations pending—and I assume that number will go down as you go from alleged to confirmed and notices of penalty, but still there's a lot of them there—Dave, you've been here during the transition from the voluntary regime to a mandatory regime, and my question is, you would hope that putting this whole structure in place would have a deterrent effect on violations occurring in the first place. So do you feel that that has happened, and is the large number in part due to more self-reporting because of the mandatoriness?

MR. COOK:

There are a few factors. I think the overall program is producing good results in the sense the internal compliance programs that the companies are developing are very positive developments. Companies that had those kind of things for OSHA violations, for environmental violations for a long time, typically, it has not been in place for reliability concerns, and now, they are moving in that direction, so that's a very positive thing. There are a lot more people involved, a lot more entities involved, than used to be. In the old voluntary regime, we were dealing with about 200 entities. We now have 1,900. So a lot of them are very new to this kind of thing, and a lot of the violations on that list of the 1,400 are start-up kinds of things. The most violated standard is CIP 1—I think they are CIP 1—the potential for sabotage reporting. You need to have a relationship with local law enforcement and the FBI. Lots of people didn't. Lots of new people to the whole program didn't. Well, that is likely a one-time thing, in the sense you will move past that. That having been said, we are still seeing too many significant violations of very important standards,

vegetation, and the next major emphasis would be relaying, so I would assume it's having a deterrent kind of effect there and we will continue to see that. But, again, it is early. We will be counting and measuring and seeing where we go.

MS. WALSH:

We have a question down here at the end.

MR. KATZ:

This is Andy Katz at Northeast Utilities. I have a question for Kathleen. You had mentioned that in reviewing an NOP, FERC would look at a registered entity's compliance program. Just a question about, has the Commission staff thought about any of the indicia that has been put out about compliance programs in general and identified any specific indicia that would be particularly important for a registered entity to consider in developing a compliance program?

MS. BARRÓN:

Well, I can answer that question generally about compliance programs, and I think, as well, with respect to reliability compliance. The Commission had a conference earlier this year to hear from folks out there in the field who have been developing compliance programs for the regulations generally. And we got an enormous amount of helpful suggestions at that conference, which we have considered. And I think you should expect that the Commission will be working on this and doing its best to try to provide guidance in the near future to companies as to how we will assess this issue of the nature of the company's commitment to compliance, its efforts to develop a compliance program, and what one of those should look like. Obviously, we are not in the business of coming up with and issuing a compliance program ourselves. All the companies are different and they have different needs and they have different things that they are subject to. But we are aware that the industry is looking for more guidance from the Commission as to how to go about developing a compliance program and what it means to have a good compliance program in terms of how the Commission considers that factor among all the other factors, and so you should expect some guidance in the future from the Commission on that.

MS. WALSH:

Anybody else?

MR. MEYER:

I have a question for any of the speakers today. It has to do with the scope of the hearing being closed. When an entity is going through one of these hearings and they are told that the hearing is closed, my sense is that they are not going to be sure what that means. And if they want to talk to their trade association about it, for example, or a lawyer involved with the hearing wants to talk to the EBA reliability committee about his or her experience, they might feel that they are not allowed to do that. Do any of you all take the fact that the hearing is closed in some way to prohibit people from talking about it in those circumstances, or do you mean it - or is it intended to be closed in the sense that

a grand jury investigation is closed in which case no one is allowed to talk about it?

MR. COOK:

Under our rules and the Commission's rules, particular enforcement matters are non-public until such time as the notice of penalty is filed at the Commission, and that's the source of it being closed. I mean it is non-public to protect the registered entity that's charged with having violated it. If the registered entity wants to go talk to people about it, I suppose that that's not—you know, that's not prohibited by the rules, the proceeding itself. And I think it is appropriate for there to be discussion about the general nature of the proceedings so long as they are not disclosing identities and individual violations and that sort of thing. But I think it would be useful as we get some experience to have some exchanges among people about the nature of the process without getting into particulars. I mean, I think that's consistent. I don't know whether that helps. I don't know whether any others have a different view.

MR. MOHLER:

One comment I can make. When you look at the provisions in the procedures, 1.2.1(3), it specifically says that no notice, ruling, order or other issuance of the hearing officer or any transcript shall be publicly released, so any notice or order may be publicly released unless the ERO, and then it goes on from there. So that is something that is worth thinking about what the intent is here.

MR. WAX:

And the only thing I would add is that the answer might turn on whatever the confidentiality order is that is ultimately imposed in the case. I'm not sure that will prohibit talking to your trade association or, et cetera, but I think it's an area that would have to be further defined.

MR. NICKOLAI:

And there is probably potentially one other factor, and that is that in some of the more complicated kinds of reliability events that might occur, there could be instances where there would be more than one participant, and so there's an expectation of preservation of the confidentiality as among the participants that are in the proceeding or in the matter that's before the hearing body.

MS. WALSH:

Cindy?

MS. BOGORAD:

This was the subject I was thinking about as a number of people were speaking. People were saying that, well, you know, after the first set of appeals or of hearings we will know something. Well, I'm not sure most of us will know anything. And I think it is worth trying to think about in this context of closed hearings how to share the experience, because otherwise, information you know, it may well be very limited, NERC will know, but certainly from the

practitioner's standpoint, unless you yourself have been in a case, you won't be able to even share in that information. So I think so that we can all learn and progress in this new area, there needs to be some vehicle, consistent with all the needs to protect confidentiality, to share the experience so that we aren't recreating the wheel every time someone has a case. I'm not sure what the answer is, but that's the only way you are going to get the evolution you are talking about is if there is some dissemination of the information, which is a tough nut to crack in a closed hearing context.

MS. WALSH:

Steve, you had a question.

MR. SHAPIRO:

Yes, for Kathleen. Do you anticipate that if the enforcement staff is participating in the investigation, there is some cooperative arrangement that gets worked out, that they will also then participate in the hearing, and then once and if there is a review at the Commission, then presumably those same folks are going to be recused from any of the appellate role the Commission will be taking?

MS. BARRÓN:

Yes, I think that's one of the category of things we are going to need to work out as the investigations are completed. It remains to be seen, if there is a joint investigation, whether at the end of the process there will be a hearing at the RE or instead a proceeding at FERC. If it is the latter, you don't have that issue. To the extent there is a settlement, it goes away; if there is a show cause order, the enforcement trial staff are walled off from advising the Commission. So I think we are going to have to see how that plays out.

UNIDENTIFIED SPEAKER:

I have a question about the eight different CMEP processes. The question is if there—it might best be asked through a hypothetical. From what I understand, audits are performed based on how the entity is registered. It might be three years or six years. And the question is, what is the value of going through self-certifications and then receiving a spot-check, which is supposed to determine compliance but on a specific subset of what was self-certified, what will—I guess the question is, how will that hold up in an audit that might take place five years from now? Will the spot-check be determinative for that period of time that it covered or—and then the audit will assume that the spot-check was accurate, and then totally go—fully review the remaining five years, or is the audit the end all, be all, and that's the one that everyone needs to shoot for because it is that full period that will be covered regardless of the other ongoing CMEP processes?

MR. WARGO:

I will answer that. This is Bob Wargo. In case somebody missed the question, it was basically the eight methods of monitoring compliance, how they fit together and how they work together, specifically spot-checks and compliance

audits and self-certs in terms of the auditing to the registered functions of a particular registered entity. I guess that question is pretty detailed or an answer would be pretty detailed because, number one, the registry is dynamic. So registered functions are added/subtracted, companies are merged/sold, so although the registration is somewhat stabilized, there's always changes. So registered functions change quite often. For a particular registered entity, a compliance audit does look at all the standards and all the requirements that are applicable to that registered entity for the period of time since the last audit, or in this case, if the audit were to occur within the next couple of years, back to June, eighteenth of 2007.

Spot-checks are normally conducted in a focused manner, whether it be towards a certain requirement or standard; there might be a problem across the whole industry. It might be focused on the particular registered entity that was having difficulties complying with a certain standard or requirement. In terms of the timing, a spot-check is like a very focused audit, so we would look backwards in time to a certain relevant date, whether it is back to the last audit or back to June eighteenth. If a registered entity that is the subject of a spot-check that was conducted this year is the subject of a compliance audit next year, that doesn't really affect what the compliance audit will look at. The compliance audit will then look at all the standards that are applicable. The compliance team would have available the spot-check report and the results from that spot-check and they will look at what the results were. So in terms of double jeopardy or the people looking at the same thing twice, I don't think that is a concern.

MS. WALSH:

It would only be a concern if an entity self-certifies that they have done everything in a certain way and they say they believe they are in compliance, and then the spot-check will choose a limited portion of that and verify it. The question is what if that entity continues to perform in the same manner in reliance on the fact that they believe they are in compliance.

MR. WARGO:

Self-certifications are obviously an assessment. We will certainly go ahead and verify that compliance. If we do see problems in terms of self-certifications where an entity might certify compliance and then we go in and we find evidence of non-compliance, then that might mean that other self-certs are suspect perhaps in the same general areas, whether it's TPL standards or PRC standards. So self-certs are a tool. You know, they are a tool to have a registered entity look at themselves, but they are not, you know, a final determination of compliance to the standard.

MS. WALSH:

I think we had one or two more questions. Deborah and Walter. How about Deborah first?

MS. CARPENTIER:

Deborah Carpentier. This question is for Dave Cook. Bob Wargo mentioned that NERC may, at its discretion, be involved in settlement negotiations between an RE and a registered entity. And I was wondering sort of

what factors NERC may consider in being involved in that, and would NERC view its role sort of as brokering a settlement in that situation or observing or....

MR. COOK:

My guess is it would be a combination of things. It might be the seriousness of the case; how widespread the case is. If it is something involving multiple regions, that might be—and the role that NERC would play would be an advisory role. It could be helping to get the settlement. It may be that, you know, a particular case has policy issues, they may want to get senior people involved in it to make sure it happens. You may have people involved more generally just so that there is some ability to get consistency on how we are approaching matters through settlement. It will vary in the circumstances. I think what we have in place are mechanisms for separation of functions, so that if someone is involved in the settlement discussions, you know, they are not subsequently advising the compliance committee on the same matter.

MS. WALSH:

Walter?

MR. HALL:

Yes. We had a discussion of a number of different levels at which potential hearings, if they do take place, are to occur: One, at the regional entity and then up at NERC and up at FERC, and the indication was that the FERC hearing will be de novo. My question is, has there been any thought given to whether or not there will be any deference by the higher levels to decisions that are made by the lower levels as you move through the process, or does the indication that the FERC hearing is de novo suggest that each of these is going to be a de novo hearing?

MR. COOK:

I think the statute—the de novo hearing at the Commission is permissive, and, you know, Kathleen can fill in a bit more about how the Commission is looking at that currently. But if you look at our rules, there is at least an implication that the record made at the regional level is the record that comes to the board compliance committee. It's not a substantive hearing on new facts.

MS. BARRÓN:

And, likewise, FERC has said the Commission expects in those cases not to reopen the record to facts that weren't submitted at the RE level. But it does reserve the right to do so if it finds the record inadequate.

MR. WAX:

All hearing officers will make sure a perfect record is established so there is no issue.

MS. WALSH:

Did I miss anyone here? Any other questions before we go to the phone? Okay. Can we take questions from callers.

MR. ALAN (last name not audible):

This is Alan (inaudible) with the power administration. I had a question regarding intervention. There's a potential situation which has been raised by the ISOs where another entity (inaudible) violates a reliability standard and the registered entity may (inaudible) the path on any penalty (inaudible). In that situation would the hearing officers be willing to consider intervention?

MR. WAX:

We are all pointing at Kathleen because the rule says no one except FERC can order that.

MR. COOK:

Right. That intervention would be at the Commission's discretion. I can imagine, though, a situation where there may be alleged violations against a couple of different entities, and those could be consolidated, I think that works under the rules. That doesn't involve the Commission having to give permission, and that may be one avenue to deal with that question. We have said that to the ISOs and RTOs in response to that question that we would in the process of the investigation make sure that there is a complete record about what happened.

MS. BARRÓN:

Right. And there was an order the Commission did on the last agenda that deals directly with this question. To the extent the question was about ISOs and RTOs—I'm not sure if that was the prior caller's concern particularly—but to the extent that the RTO is going to seek to tag an entity that has not been assessed a penalty by the region through NERC, it's going to have to have provisions on file at the Commission that will allow it to do that. And PJM received approval to do that last month, under very limited circumstances, one of which is that the entity that is now being sought to be tagged by the RTO was given the opportunity to participate at the hearing at the RE. If that entity did not have the opportunity to participate, then the RTO is not going to be able to pass through a cost or to assign a penalty to that entity.

MS. WALSH:

And, Kathleen, just to follow up on that point. I guess I would assume then that FERC realizes that if there is a request for a third party to participate, that request could be for involuntary participation on the part of the third party. For example, there could be a situation where an RTO requests that a subpoena be issued to a third party who doesn't want to participate. Will there be provisions for compelling third-parties to participate? I don't know if that would be a question for you or for Dave.

MR. COOK:

That would be presuming a Commission decision. We don't have authority to do that. Our authority would be through charging that third party with the violation, and that may be that that's the mechanism. As a practical matter, as

we work through these things, we are going to know what happened, what the factual circumstances are of the case, there may be a dispute about, given those facts, who ought to be responsible, but it may be that that's the mechanism.

MS. WALSH:

Next caller on the phone. Are there any other questions from the callers? Okay. That's it. Thank you all very much.

(Whereupon, the proceedings were concluded at 2:19 p.m.)