



January 13, 2006

Mr. David Cook
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North American Electric Reliability Council
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Subject: ERO Comments

Dear David:

NERC has asked for industry comments on both its draft Electric Reliability Organization Application and its draft Reliability Standards Application. While the Canadian Electricity Association ("CEA") appreciates the opportunity to provide comments, the development of an adequate response to the issues raised by the draft requires additional time. Nevertheless, we are mindful of the time constraints under which NERC is operating. Accordingly, we are providing in this letter a brief discussion of our core concerns. We mean these comments to be constructive and commit to working with NERC to address these issues. We understand that there will be additional drafts and we will submit more detailed comments at that time. We do wish to note, however, that the drafts are missing some important work of the PLSC stakeholder groups, and we recommend that NERC consider carefully the work of these groups before dismissing those recommendations.

The ERO Application Needs to Better Reflect the International Nature of the ERO

CEA recognizes that the draft ERO application is drafted to be responsive to U.S. requirements. CEA encourages NERC to work with Canadian authorities to develop the processes and means to achieve recognition in each of the relevant Canadian provinces, based on the differing reliability authorities and responsibilities within each province. Nevertheless, because the ERO is intended to be an international organization, NERC's organization documents and procedures contained within the FERC application must be drafted to ensure that the resulting organization will both receive the approval of the relevant Canadian provinces and will be able to operate effectively on an international basis.

In the Overview, NERC recognizes that the ERO will be international in scope and states that it will closely coordinate activities with FERC and provincial authorities. To that end, NERC will concurrently request each Canadian provincial authority to similarly recognize the ERO when it submits its certification application with FERC. NERC recognizes that, to be effective, it must closely coordinate standards development, compliance and enforcement, reliability assessments, and other ERO functions with FERC and Canadian provincial authorities.

Although NERC makes this commitment to create an international organization, the draft filing appears to be a direct response to what NERC anticipates will be FERC regulatory requirements and does not appear to be "international" in nature. While there is some language surrounding provisions of Canadian law, the documents are not written with multiple authorities in mind. For example, the draft rules of procedure require that a reliability standard may be approved by a regulatory authority if that authority finds that the standard is "just, reasonable, not unduly discriminatory or preferential, and in the public interest." This is a FERC standard imposed through the U.S. reliability legislation, as opposed to a particular standard of review required by any of the Canadian provinces. In another example, the rules require that entities within a province continue to follow a tariff provision where a conflict between a tariff provision and a standard is discovered. Such processes may reflect the requirements in U.S. legislation, but may not be consistent with provincial requirements or authorities. The rules of procedure must be developed to allow for differences in approaches as reflected in the requirements and authorities of the different regulatory systems.

Drafting problems appear to be most evident with regard to the enforcement of reliability standards language. The U.S. legislation provides the ERO with the authority to both develop reliability standards and enforce those standards. CEA anticipates that, following the submission of documentation to be recognized as an ERO by each of the relevant Canadian provinces, the approved ERO will be recognized as the entity to develop mandatory reliability standards related to the bulk power system on an industry-wide basis. However, the ability of the ERO to enforce reliability standards in any of the Canadian provinces is less clear. Following submission of its applications for recognition, the ERO may be provided some enforcement authority in some provinces, but no authority in other provinces. Until the extent of the ERO's enforcement authority in each of the Canadian provinces is known, the draft ERO application must be drafted to recognize that enforcement of reliability standards may be different north of the border.

Similarly, CEA is troubled with the rules that provide for procedures for the reporting and disclosure of violations. The rules provide that each region shall report all violations, confirmed and unconfirmed, of all ERO and regional reliability standards to the ERO, and the ERO shall send each confirmed violation to the applicable regulatory authority. Moreover, when due process is complete, the ERO shall publicly post each confirmed violation, penalty or sanction, and audit or investigation report on its Web. This process assumes that both the regional entity and the ERO will identify the violation and confirm that a violation occurred. However, in the provinces, determinations of standards violations may be made by the provincial authority. If that is the case, the ERO's reporting and disclosure processes will need to be modified to be consistent with provincial enforcement authorities.

ERO Standard-Setting Authority Appears to be Overly Broad

The U.S. legislation provides NERC with the authority to set reliability standards for users, owners, and operators of the bulk-power system. However, that legislation limits NERC's ability to set standards, for example, with regard to adequacy. NERC's draft suggests that NERC will be performing functions beyond their mandate. For example, NERC's proposal to address "situation awareness" would allow NERC to engage in activities beyond the scope of development of reliability standards. CEA members believe this is overreaching and should not be permitted.

CEA is also concerned that implementation of this broad responsibility will result in a substantial augmentation of NERC staff, resulting in substantial additional costs. Such an escalation of costs is unwarranted and unnecessary. NERC is presently operated with heavy reliance on a pool of volunteer-based industry experts, many of whom actually chair the NERC committees. While we recognize some changes and increased costs are inevitable (more stringent audits, for example), the draft implies significant and direct NERC involvement in

areas that are not required or necessary to have a “strong ERO.” Instead, such substantial increases in personnel would result in significant industry inefficiencies and duplication in activities, thereby undermining the intent of industry efforts to establish a “self-regulating” reliability organization that relies on the expertise of industry-based participants.

Funding Proposal Not Reflective of Funding Obligations

NERC proposes that the ERO funding mechanism for all statutory functions be based on net energy for load, so that the costs are allocated to all end-users on an equitable basis. Costs will also be equitably allocated between countries participating in the electric reliability organization. In addition, each regional entity shall submit to the ERO its annual funding requirement for all delegated functions, which the ERO will have responsibility for approving. Accordingly, all regional budgets for delegated functions shall be funded through the ERO.

NERC’s proposed funding mechanism raises a number of concerns for CEA members. The U.S. legislation provides the ERO with the responsibilities of both developing reliability standards and enforcing those standards. While CEA expects that all the relevant provinces will recognize the ERO as the standard-setting body, it is unclear whether all provincial authorities will provide the ERO with enforcement authorities. Accordingly, with respect to Canadian entities in certain provinces, the ERO may have standard-setting responsibilities and compliance monitoring, for example, but any alleged standards violations would be issued and enforced by the provincial authority. NERC’s proposed funding mechanism assumes cost recovery of all its functions from all users, owners, and operators of the bulk-power system in North America. To the extent the ERO performs no enforcement functions with regard to Canadian entities within a particular province, the end-users within that province should not be expected to pay for the ERO’s overall enforcement responsibilities.

NERC’s funding proposal is also problematic with respect to the funding of regional entities. Funding for regional entities relates only to those delegated functions, which are the ERO’s enforcement functions. Assuming a province has not provided the ERO with enforcement authority (so that such authority could not then be delegated to the regional entity), the regional entity -- at least in theory -- should have no responsibilities for which it will be seeking funding from such a province. Nevertheless, CEA recognizes that regional entities have served and will continue to serve important roles for CEA members, and expects that their members will continue to fund the regional entities. The funding issue must be further explored to ensure that Canadian entities pay only for those activities that are consistent with the relevant provincial mandates. Moreover, to the extent a province has no process in place for approval of the ERO budgets, the regional entity may remain the entity responsible for assessing costs with respect to the end-users in that province.

Yours sincerely,

CANADIAN ELECTRICITY ASSOCIATION



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