FERC Clarifies Guidance on Reliability Penalties

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On June 21, 2012, the Federal Energy Regulatory Commission ("FERC") denied requests for rehearing of its March 17, 2011 Order affirming an $80,000 penalty assessed against the Turlock Irrigation District ("Turlock") by the Western Electricity Coordinating Council ("WECC") for the violation of several reliability standards resulting from a power outage. North American Electric Reliability Corp., 139 FERC ¶ 61,248 (2012). The vegetation-caused transmission outage occurred in August 2007 and caused 40,000 customers of the Turlock and Modesto Irrigation Districts to lose power. A number of parties, including the North American Electric Reliability Corporation ("NERC"), several Regional Entities, and a group of electric industry trade associations, sought rehearing or, in the alternative, clarification with respect to four issues: (i) load loss; (ii) self-reporting; (iii) size and nature of the registered entity; and (iv) adequacy of the record filed with penalty notices. Although FERC denied the requests for rehearing, it clarified several issues relating to the assessment of penalties for violations of reliability standards.

(I) LOAD LOSS

In its March 2011 Order, FERC explained that the penalty assessed for a violation of a reliability standard should take into account lost load and harm to customers because these factors are relevant to the seriousness of the violation. But in its June 21 Order, FERC clarified that it did not intend to dictate how these factors should be assessed, stating that enforcement agencies "retain the discretion to determine how best to consider lost load and harm to customers, resulting from a violation, as long as they consider these factors in some form and the resulting penalty 'bears a reasonable relation to the seriousness of the violation,'" as required by the Federal Power Act. FERC also reiterated its prior determination that while load loss is considered a relevant factor when assessing reliability penalties, this consideration should not have a "chilling effect" on system operators shedding load to maintain the overall integrity of the bulk power system because shedding load in itself is not a violation. FERC emphasized that a penalty may only be imposed for conduct that violates a reliability standard. Thus, load shedding is only considered a factor in penalty determinations when it results from a violation of a reliability standard.

(II) SELF-REPORTING

FERC also upheld its prior decision not to provide Turlock self-reporting credit for reporting the reliability violations of the August 2007 outage because it was already legally obligated to report the event. FERC clarified that while self-reports are relevant in the calculation of penalties, not all self-disclosures necessarily warrant self-reporting credit. FERC identified these situations to include when a registered entity reports facts related to a possible violation under an existing reporting obligation before making a self-report, or where a registered entity self-reports after the commencement of a compliance audit, spot check or other compliance process. In these circumstances, FERC does not believe these entities are entitled to a credit. Self-reporting credit is more appropriate when the registered entity voluntarily discloses a violation in advance of any required report because learning of the violations at an early stage facilitates an enforcement agency's review of the facts. Consistent with this directive, enforcement agencies should consider the timing of self-disclosure of a violation and whether or when they could have detected the violation prior to such disclosures. FERC also affirmed that a separate cooperation credit may be warranted for entities that provide additional, useful information—beyond what it is obligated to provide—about the facts and circumstances surrounding a potential violation.

(III) SIZE AND NATURE OF REGISTERED ENTITY

FERC's June 21 Order clarified that it did not intend to instruct NERC on how to interpret and apply its Sanction Guidelines related to the size and nature of registered entities when determining penalties. FERC stated that given NERC's statutory obligation under the Federal Power Act to ensure that penalties for violations of reliability standards "bear a reasonable relation to the seriousness of the violation," the size and nature of a registered entity are relevant but should not be an overriding factor when assessing penalties. FERC also upheld the finding in its March 2011 Order that a registered entity's size should be measured by multiple factors, including the number of employees and annual revenue and profits, and should not be solely determined by the number of miles of transmission lines an entity operates and its interconnections to the bulk power system.

(IV) ADEQUACY OF THE RECORD

FERC clarified in its June 21 Order that it continues to endorse streamlined approaches to notice of penalty submissions, even though its March 2011 Order had stated that NERC should "file a complete and accurate record for each notice of penalty, whether it reflects an adjudicated determination or a settlement with a registered entity." FERC reiterated that it encourages the use of flexible approaches and more streamlined processes to achieve efficiency in the enforcement process, particularly when addressing minor violations. However, FERC expects serious violations, such as loss of load, to be processed as full notices of penalty. To be adequate, the record for each such notice of penalty must be complete and accurate and not exclude facts that are critical to the assessment of a penalty and to subsequent efforts to improve compliance and reliability.
MESSAGE TO REGISTERED ENTITIES

FERC clarified that its March 2011 Order was intended to be consistent with its prior efforts regarding reliability enforcement. It appears FERC wants to allay concerns that it is going to conduct regular reviews of proposed penalties where the enforcement agencies and violators have entered into a settlement agreement. At the same time, FERC confirms that the “guidance” provided in its March 2011 Order was intended to ensure NERC meets its statutory obligations, while also leaving it up to NERC to decide how to accomplish this. The June 21 Order can be read as confirming that FERC recognizes the split of responsibility and authority created in the Energy Policy Act of 2005, which established the mandatory reliability standards.

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