

FEDERAL ENERGY REGULATORY COMMISSION  
WASHINGTON, D.C. 20426

In Reply Refer To:  
Office of Enforcement  
Docket No. PA12-9-000  
July 10, 2013

Steven Goodwill  
Vice President and General Counsel  
Western Electricity Coordinating Council  
155 North 400 West, Suite 200  
Salt Lake City, UT 84103

Dear Mr. Goodwill:

1. The Division of Audits (DA) within the Office of Enforcement (OE) of the Federal Energy Regulatory Commission (Commission) has completed the audit of Western Electricity Coordinating Council (WECC) for the period from August 23, 2006 through December 31, 2012. The enclosed audit report explains our audit conclusions and recommendations.
2. The audit evaluated WECC's responsibilities and compliance as a Regional Entity (RE), including its operations under: (1) the Delegation Agreement between the North American Electric Reliability Corporation (NERC) and WECC, (2) the WECC Bylaws, and (3) other obligations and responsibilities that the Commission has approved. Also, this audit evaluated WECC's budget formulation, administration, and execution. In addition, DA focused on the costs and resources used to achieve program objectives in fulfilling the duties delegated to WECC by the North American Electric Reliability Corporation as the Electric Reliability Organization under section 215 of the Federal Power Act.<sup>1</sup>
3. In its June 28, 2013 response, WECC stated it accepts all of the recommendations in the audit report and has already begun taking actions addressing some of the recommendations. A copy of your verbatim response is included as an appendix to this report. I hereby approve the audit report.
4. Within 30 days of this letter order, WECC should submit a plan to comply with the recommendations. WECC should make quarterly submissions describing how and when it plans to comply with the recommendations, including the completion date for

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<sup>1</sup> 16 U.S.C. § 824o (2012).

each recommendation. The submissions should be made no later than 30 days after the end of each calendar quarter, beginning with the first quarter after this audit report is issued, and continuing until all the recommendations are completed.

5. The Commission delegated the authority to act on this matter to the Director of OE under 18 C.F.R. § 375.311 (2012). This letter order constitutes final agency action. WECC may file a request for rehearing with the Commission within 30 days of the date of this order under 18 C.F.R. § 385.713 (2012).

6. This letter order is without prejudice to the Commission's right to require hereafter any adjustments it may consider proper from additional information that may come to its attention. In addition, any instance of noncompliance not addressed herein or that may occur in the future may also be subject to investigation and appropriate remedies.

7. I appreciate the courtesies extended to our auditors. If you have any questions, please contact Mr. Bryan K. Craig, Director and Chief Accountant, Division of Audits at (202) 502-8741.

Sincerely,

A handwritten signature in blue ink that reads "Norman C. Bay" followed by a stylized flourish.

Norman C. Bay  
Director  
Office of Enforcement

Enclosure



Federal Energy Regulatory Commission

**Audit of Regional Entity  
Responsibilities and Budgeting  
Practices for the Western  
Electricity Coordinating Council**

Docket No. PA12-9-000  
July 10, 2013

**Office of Enforcement  
Division of Audits**

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## I. Executive Summary

### A. Overview

On October 28, 2011, the Division of Audits commenced an audit of the Western Electricity Coordinating Council (WECC). Following the Division of Audits' 2009 audit of WECC under Docket No. PA09-5-000, the Commission stipulated a future audit of WECC in its approval of the audit report.<sup>2</sup> The current audit examined WECC's responsibilities and compliance as a Regional Entity (RE), including its operations under: (1) the Delegation Agreement between the North American Electric Reliability Corporation (NERC), the Commission's certified Electric Reliability Organization, and WECC,<sup>3</sup> (2) the WECC Bylaws,<sup>4</sup> and (3) other obligations and responsibilities that the Commission has approved. Also, this audit evaluated WECC's budget formulation, administration, and execution, and the resources used to achieve program results. This audit covered the period from August 23, 2006 to December 31, 2012.<sup>5</sup>

Audit staff observed WECC had many policies, procedures, and controls that facilitated WECC's carrying out, in an effective and efficient manner, its responsibilities under its Delegation Agreement and Bylaws, as well as of its budget obligations. In its Three-to-Five Year Strategic Plan, WECC outlined five core values, one of which was "Excellence - We strive for continuous quality improvement in all that we do."<sup>6</sup> To that

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<sup>2</sup> *Western Electricity Coordinating Council*, 132 FERC ¶ 61,149, at P 23 (2010).

<sup>3</sup> *North American Electric Reliability Council, et al.*, 119 FERC ¶ 61,060 (2007) (Delegation Agreements Order), *order on reh'g*, 120 FERC ¶ 61,260, *order on compliance filing*, 122 FERC ¶ 61,245 (2008) (Second Delegation Agreements Order), *order on compliance filings*, 125 FERC ¶ 61,330 (2008) (Third Delegation Agreements Order).

<sup>4</sup> WECC, *Bylaws of the Western Electricity Coordinating Council* (Mar. 1, 2012) (on file with author), available at [www.wecc.biz/library/WECC%20Documents/Business%20and%20Governance%20Documents/WECC%20Bylaws%202012.pdf](http://www.wecc.biz/library/WECC%20Documents/Business%20and%20Governance%20Documents/WECC%20Bylaws%202012.pdf).

<sup>5</sup> The scope of the WECC audit conducted under Docket No. PA09-5-000 did not include the budget component. Therefore, the audit period for the current audit encompassed August 23, 2006 through December 31, 2012 to allow audit staff the flexibility to review WECC's budgets back to and including the original filing, as necessary. However, this audit focused on the time period subsequent to August 20, 2010 (the date of the prior audit report issuance). Unless otherwise specified, all references to the audit period throughout this report refer to August 20, 2010 through December 31, 2012.

<sup>6</sup> WECC Strategic Plan, (Dec. 2, 2011)(on file with author), available at [www.wecc.biz/library/WECC%20Documents/Business%20and%20Governance%20Documents/WECC%20Three-to-Five%20Year%20Strategic%20Plan%20Final%202012-12-11.pdf](http://www.wecc.biz/library/WECC%20Documents/Business%20and%20Governance%20Documents/WECC%20Three-to-Five%20Year%20Strategic%20Plan%20Final%202012-12-11.pdf).

end, as detailed throughout this report, audit staff has identified areas where we believe improvements to WECC's policies and procedures could result in improved operations of its delegated functions, as well as in budgeting for its operations.

Specifically, within WECC's Compliance Monitoring and Enforcement Program (CMEP), audit staff identified potential improvements to WECC's policies and procedures for mitigation plan processing and its enforcement caseload. Further, we observed the need for enhancements to WECC's processes for reviewing conflict of interest forms. Also, audit staff identified potential improvements to WECC's budget development process. We next found that the opportunity exists for WECC to introduce additional controls over its employee business expense reimbursement process. Audit staff also had certain concerns with WECC's investment policies and its investments. Finally, WECC's budgeting for all regional criteria, which include not only reliability concerns but also rules governing consistency in business practices among WECC members, highlighted the need for it to implement a policy defining what constitutes a statutory activity.

Besides the areas where audit staff identified potential operational enhancements, we also address one other matter in this report. In addition to its responsibilities as an RE, WECC also performs two registered functions – the Reliability Coordinator (RC) and Interchange Authority (IA) functions. Audit staff noted that under WECC's methodology for paying penalties incurred by these registered functions, U.S. penalty monies are used to offset assessments to U.S. entities on a Net Energy for Load (NEL) basis. Instead of applying the penalty system-wide (as for the assessment of funds required to operate the RC function), only U.S. entities pay the settlement amounts.

## **B. Western Electricity Coordinating Council**

Under section 215(e)(4) of the Federal Power Act (FPA) the Commission may approve NERC's delegation of its authority to propose and enforce Reliability Standards to REs<sup>7</sup>. WECC, a not-for-profit organization, is one of eight REs in North America delegated such authority under section 215. WECC, headquartered in Salt Lake City, UT, holds responsibility to coordinate and promote Bulk-Power System (BPS) reliability in the Western Interconnection. WECC's service area covers nearly 1.8 million square miles and includes the provinces of Alberta and British Columbia, northern Baja California, Mexico, and all or portions of 14 western U.S. states. WECC is bordered by the Midwest Reliability Organization, Southwest Power Pool, and the Electric Reliability Council of Texas, all of which are interconnected with WECC only by direct current (DC) ties. This makes the Western Interconnection a single electric grid.

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<sup>7</sup> 16 U.S.C. § 824o (2006).

As an RE, WECC oversaw more than 450 registered entities in the Western Interconnection, with membership in WECC open to all entities with an interest in the operation of the BPS in the Western Interconnection. Within its footprint, NERC delegated to WECC these statutory functions:

- Reliability Standards Development;
- Compliance Monitoring and Enforcement;
- Organization Registration and Certification;
- Reliability Assessment and Performance Analysis;
- Event Analysis and Reliability Improvement;
- Training and Education;
- Situation Awareness; and
- Infrastructure Security.

### **C. Proposed Bifurcation of WECC**

Each September, the WECC Board of Directors (Board) holds a strategic planning session. After its 2011 planning session, WECC identified certain challenges it believed its current organizational structure caused. For example, as WECC's Chief Executive Officer (CEO) explained in WECC's 2012 Summer Newsletter:

The most evident challenge is WECC's current structure and what I refer to as WECC's duality of purpose (WECC is a Regional Entity and performs Registered functions – the Reliability Coordinator and Interchange Authority functions). This would appear to be the reason that WECC was excluded from the [recent Arizona-Southern California] post-event Inquiry. This exclusion prevents WECC from achieving its core reliability mission and its delegated duties as the Regional Entity in the Western Interconnection.<sup>8</sup>

To address these perceived challenges, WECC decided to focus its 2012 strategic planning session on evaluating alternative organizational structures, governance models, and funding mechanisms that would best allow it to carry out its mission. In preparation for the strategic planning session, WECC benchmarked the performance of its functions against other entities, and considered possible alternative organizational structures, as well as staffing and budget requirements, and incremental costs that would be incurred under an altered organizational structure.

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<sup>8</sup> WECC Summer 2012 Newsletter (on file with author), *available at* [www.wecc.biz/library/WECC%20Documents/Publications/Newsletters/Summer%202012%20WECC%20Newsletter.pdf](http://www.wecc.biz/library/WECC%20Documents/Publications/Newsletters/Summer%202012%20WECC%20Newsletter.pdf)

WECC presented the results of its review to the Board at its annual strategic planning session, and recommended pursuing bifurcation into two entities. One of these entities would contain RE functions such as the Reliability Standards Development and CMEP functions, while the other entity (non-RE) would contain registered entity functions such as the RC, IA, and other functions. During the September 2012 planning session, the WECC Board approved a resolution that WECC should pursue this course. The Board further directed WECC management to work with the Governance and Nominating Committee (GNC), Finance and Audit Committee (FAC), and Human Resources and Compensation Committee (HRCC) to complete work on proposed governance models of the new entities. In December 2012, the WECC Board considered additional input from the GNC, FAC, HRCC, WECC management, and other stakeholder groups. Ultimately, the Board passed several resolutions supporting bifurcation. On March 12, 2013, WECC made a filing with the Commission in Docket No EL13-52-000, requesting that the Commission issue a declaratory order confirming funding arrangements proposed by WECC in connection with its plan to establish a separate company to perform the RC and IA registered functions. This issue is currently pending before the Commission.

#### **D. Summary of Conclusions**

During the audit period, audit staff found these areas where WECC's operations could be enhanced:

- *Mitigation Plan Processing* – WECC's review of mitigation plans could be improved by strengthening its processes and documentation standards for the review, approval, tracking, and certification of mitigation plans registered entities submitted. This improvement would increase the efficiency and effectiveness of the process by making WECC and the registered entities more accountable and encouraging more timely and thorough implementation of mitigation measures, which in turn benefits the reliability of the BPS.
- *Enforcement Caseload* – WECC's policies and procedures could be improved to ensure enforcement staff adequately documents its review of potential Reliability Standard violations.
- *Conflict of Interest Disclosure Form Completion* – WECC's policies and procedures did not ensure timely and thorough completion of all conflict of interest disclosure forms it used to identify potential conflicts of interest within the CMEP.
- *Budget Development* – In certain instances, WECC budgeted for the same expenses in multiple program areas, which resulted in double budgeting for these amounts, although to date these amounts have not been material. Also,



audit staff identified two areas in the budget that we do not believe had sufficient transparency.

- *Employee Expense Reimbursement Policy and Controls* – WECC could enhance its processes for reviewing expenses submitted for reimbursement through standardized written procedures and criteria for the review of such expenses.
- *Investments* – WECC’s Investment Policy did not prohibit WECC from investing funds in registered entities, which could lead to possible conflicts of interest or independence concerns. Also, WECC assigned investment earnings to “statutory” and “nonstatutory” accounts (that is, accounts relating to funding WECC receives pursuant to FPA section 215 and accounts that relate to other sources of funding, respectively) based on FTEs, rather than actual earnings. To achieve stronger controls, audit staff believes WECC should segregate statutory and nonstatutory monies to prevent any possibility of cross-subsidization.
- *Funding of Regional Criteria under Section 215* – WECC did not have written policies, processes, procedures, or internal guidance for parameters to consider as a basis for determining whether a proposed or ongoing activity should be considered statutory or nonstatutory. This was demonstrated in WECC’s Regional Criteria which addressed not only reliability issues, but also consistency in business practices between WECC members. During the audit period, WECC initiated an assessment process regarding these criteria. Audit staff believes WECC should continue the development of processes to ensure activities it performs are appropriate to fund under section 215.

Audit staff also addressed the following other matter:

- *Payment of Penalties Incurred by WECC’s Registered Functions* – WECC performed two NERC-registered functions on behalf of all the loads in the Western Interconnection. As the Reliability Coordinator (RC), WECC incurred compliance penalties in its role as a registered entity. To pay for the penalties it incurred, WECC used monies it received through the assessment of penalties to U.S. registered entities in its role as the RE for the Western Interconnection. Whether this process complies with provisions in WECC’s Delegation Agreement regarding the distribution of penalty monies as a general offset to WECC’s budget requirements for U.S.-related activities is unclear.

## **E. Summary of Recommendations**

This section summarizes audit staff's recommendations to WECC where its operations could be enhanced. Detailed recommendations are in section IV of this report. Audit staff recommends that WECC:

1. Continue to enhance its policies and procedures to ensure that each proposed mitigation plan or application for certification of mitigation plan completion is accepted or rejected in a timely manner;
2. Enhance its policies and procedures to ensure revised mitigation plans are prioritized for review;
3. Strengthen its policies and procedures for tracking mitigation plans to completion. Such policies and procedures should include steps to track mitigation plan progress through quarterly updates;
4. Improve its policies and procedures to standardize its documentation and record retention requirements to ensure it retains adequate and accurate documentation for its review of mitigation plans. These policies should also ensure WECC's mitigation plan records are complete and accurate;
5. Continue to correct inaccurate data currently in its communication and data exchange tool used in CMEP activities (i.e., webCDMS);
6. Strengthen its policies and procedures relating to documenting its review of potential violations of Reliability Standards by enforcement staff. Such policies and procedures should include enhanced documentation requirements to ensure enforcement staff retains adequate information relating to its review;
7. Enhance its policies and procedures to ensure conflict of interest disclosure forms are completed and submitted in a timely and thorough manner;
8. Improve its policies and procedures for budget development. Such policies and procedures should include additional guidance to ensure items are not double budgeted and that all expenses are transparent;
9. Continue to enhance the Accounting department's review of departmental budgets;

10. Create policies and procedures and improve its controls to better inform managers as to expectations for their review of employee business expenses;
11. Work with NERC to adopt restrictions on investments in registered entities to ensure the appearance of conflicts of interest does not occur;
12. Strengthen its policies and procedures to ensure cross-subsidization does not occur between statutory activities and its nonstatutory activities (e.g., Western Renewable Energy Generation Information System (WREGIS));
13. Consider physically segregating its statutory and nonstatutory investments;
14. Adopt written criteria for evaluating whether activities should be funded under section 215;
15. As part of the next budget review process, provide detail surrounding WECC's regional business practice activities sufficient to ensure transparency to those responsible for evaluating the appropriateness of funding these activities under section 215; and
16. Make a separate filing, or include language in a currently planned filing such as the 2014 ERO budget filing or a filing regarding the separation of the WECC RE and WECC's registered functions, explicitly seeking Commission approval for WECC's method of paying compliance penalties incurred in its roles as a registered entity. Also, in this filing WECC should explain its proposed method for requesting a special assessment for paying penalties when it does not have sufficient funds.

## **F. Implementation of Recommendations**

Audit staff further recommends that WECC:

- Submit for audit staff's review its plans for implementing this report's recommendations. WECC should provide these plans to audit staff within 30 days of the issuance of this final audit report.
- Submit quarterly reports to the Division of Audits describing WECC's progress in completing each recommendation in the final audit report. WECC should make these nonpublic quarterly filings no later than 30 days after the end of each calendar quarter, beginning with the first quarter after the final audit report is issued, and continuing until WECC completes all recommendations.

Western Electricity Coordinating Council

Docket No. PA12-9-000

- Submit copies of any written policies and procedures developed in response to recommendations in this final audit report. These copies should be submitted for audit staff review in the first nonpublic quarterly filing after WECC completes these documents.

## II. Background

### A. Overview

Under section 215(e)(4) of the Federal Power Act (FPA), the Commission approved NERC's delegation of certain statutory functions to the REs.<sup>9</sup> Under a Delegation Agreement with NERC, WECC has been delegated certain responsibilities and authorities pursuant to section 215 of the FPA. The statutory functions NERC delegated include: Reliability Standards Development; Compliance Monitoring and Enforcement; Organization Registration and Certification; Reliability Assessment and Performance Analysis; Event Analysis and Reliability Improvement; Training and Education; Situation Awareness; and Infrastructure Security.

### B. Statutory Activities

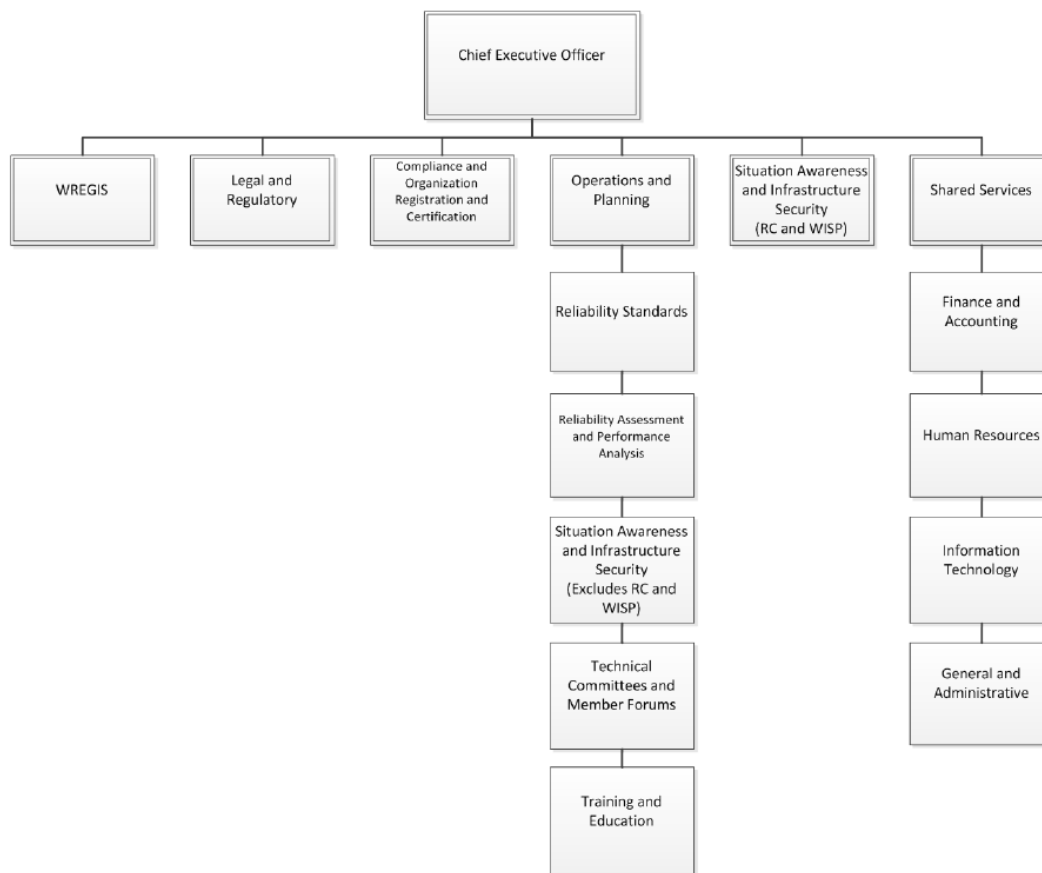
With only one exception, WECC considers all of its activities to be statutory; that is, carried out pursuant to FPA section 215 under its Delegation Agreement with NERC. The exception is the Western Renewable Energy Generation Information System (WREGIS), a renewable energy database for the Western Interconnection. WREGIS creates renewable energy certificates (RECs) for verifiable renewable generation from units registered in the database.<sup>10</sup>

WECC carried out its statutory responsibilities under its Organization Registration and Certification, and Compliance Monitoring and Enforcement Process (CMEP), and its Operations and Planning functional areas. To support these functional areas, WECC maintained employees in general and administrative areas, including Legal and Regulatory Affairs as well as Shared Services. An organizational chart is below, followed by descriptions of the statutory functions carried out under each of WECC's functional areas:

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<sup>9</sup> 16 U.S.C. § 824o (2006).

<sup>10</sup> See WREGIS' web site at [www.wregis.org/](http://www.wregis.org/).



### *Organization Registration and CMEP*

Under its Organization Registration and Certification function, WECC managed the NERC compliance registry for the Western Interconnection, which lists entities that are required to comply with one or more Reliability Standards approved by the Commission. Specifically, WECC facilitated the registration process, ensured that there were no gaps in registration, and helped resolve registration disputes. Under its CMEP, WECC monitored registered entities' compliance with Reliability Standards using eight methods. These were: compliance audits; self-certifications; spot checks; compliance violation investigations; self-reports; periodic data submittals; exception reporting; and complaints. Further, WECC's CMEP encompassed enforcement activities that included reviewing, monitoring, and verifying mitigation plans filed by registered entities for violations of the Reliability Standards; determining, as appropriate, proposed penalties for alleged violations; and conducting settlement negotiations with registered entities when requested.

WECC also engaged in other CMEP support activities, including participating in WECC and NERC hearings and appeals as needed, educating registered entities on

compliance issues, and performing international compliance monitoring activities. Specifically, WECC had entered into agreements with the Alberta Market Surveillance Administrator (MSA), the British Columbia Utilities Commission (BCUC), and Mexico's Comisión Federal de Electricidad (CFE), in order to help assure reliability across international borders within the Western Interconnection.

### *Operations and Planning*

WECC's Operations and Planning functional activities included Standards Development; Reliability Assessment and Performance Analysis (RAPA); Situation Awareness and Infrastructure Security; Technical Committees and Member Forums; and Training and Education. WECC's Standards Development activities are divided into two categories: participation in the NERC standards development process, and the development of WECC Regional Reliability Standards and Regional Criteria. WECC Regional Criteria are discussed later in this report.

Under RAPA, WECC conducted a variety of studies and assessments geared towards the reliable planning and operation of the BPS in the Western Interconnection. In addition, WECC compiled and distributed data and information that was used by its members to aid in local planning studies. RAPA included the following departments: Transmission Expansion Planning, Planning Services, and Reliability Assessments.

As a part of RAPA, WECC's Regional Transmission Expansion Planning (RTEP) program provided data, analysis, public participation, and analytic tools to stakeholders in the Western Interconnection. RTEP included the development of interconnection-based transmission plans, which began in 2010 with the receipt of a grant from the Department of Energy (DOE). WECC's Planning Services included, for instance, the preparation of a database of power flow and stability base cases that reflected various system configurations and operating conditions and the development of an annual study report to provide an ongoing transmission reliability assessment of the Western Interconnection. The Reliability Assessments group worked to create and analyze internal and external supply and demand assessments for the Western Interconnection.

WECC's RC and IA registered functions were included under the Situation Awareness and Infrastructure Security functional area. The WECC RC was responsible for the reliable operation of the BPS for the Western Interconnection. WECC maintained two Reliability Coordination Offices located in Vancouver, WA, and Loveland, CO. The Western Interconnection Synchrophasor Project (WISP) was included under the Situation Awareness functional area and, like RTEP, began in 2010 with the receipt of a DOE grant. WISP involved the installation of more than 300 new or upgraded Phasor Measurement Units (PMUs) designed to improve operators' situational awareness.

WECC's Technical Committees and Member Forums functional area included WECC's Board of Directors and Board-level committees, such as the WECC Compliance Committee (WCC), Finance and Audit Committee (FAC), Governance and Nominating Committee (GNC), and Human Resources and Compensation Committee (HRCC) during the audit period. Also, WECC had standing committees composed of its Members which advised and made recommendations to the Board. Finally, under WECC's Training and Education functional area, WECC provided education and training for system operators, schedulers, and dispatchers.

### **C. Governance and Management**

During the audit period, a 34-member Board of Directors governed WECC, of which 26 directors represented member classes. Seven directors held no affiliation with any WECC members or potential members; these directors sat on the WECC Board as independent directors. WECC's CEO was also a member of the Board. Board Committees recommended policy on various reliability issues or handled governance, finance, and human resources matters. For instance, the WCC provided WECC compliance staff the opportunity to seek advice and communicate with the WECC Board, and oversaw WECC's compliance function.<sup>11</sup> As another example, the FAC reviewed WECC's budgets and made recommendations to staff, and assisted the Board in overseeing WECC's financial reporting. Independent directors chaired key Board committees, including the WCC, FAC, GNC, and HRCC during the audit period.

Several organizational and management changes occurred within WECC in recent years. For example, in January 2011 WECC's current CEO assumed this position, having served as WECC's Chief Operating Officer. In the same month, WECC's Director of Stakeholder Relations and Compliance Outreach, and its Managing Director of Compliance switched roles as part of the organization's succession planning process. In the spring of 2012, WECC created and filled the position of Director of Finance and Accounting. Also in 2012, the individuals serving as WECC's Vice President (VP) of Operations and Planning, and VP of Shared Services, respectively, switched roles as part of WECC's succession planning process. Further, WECC promoted the Director of Compliance Audits and Investigations to the newly created position of VP of Reliability Coordination. Finally, WECC created the position of Director of Corporate Compliance, also in 2012.

In another recent change, WECC's CEO created the WECC Executive Steering Team (WEST), an executive-level committee consisting of WECC's CEO and its VPs. The CEO established WEST to provide a forum for senior management to meet and

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<sup>11</sup> The Division of Audits' 2009 audit of WECC under Docket No. PA09-5-000 discusses the WCC at length. See *Western Electricity Coordinating Council*, 132 FERC ¶ 61,149 beginning on page 23 of Attachment A (2010).

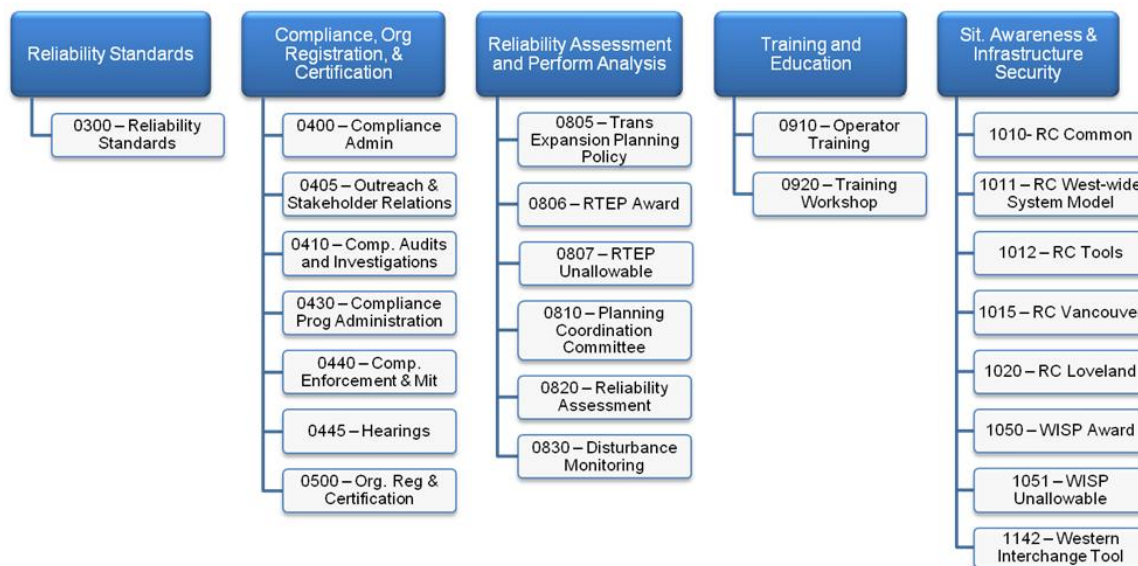


discuss WECC's performance, policy issues, budget matters, and personnel reviews. WEST meets at least monthly, and frequently meets more often if necessary. WEST also provides strategic direction, goals, and input throughout the development of the budget.

#### D. NERC System of Accounts

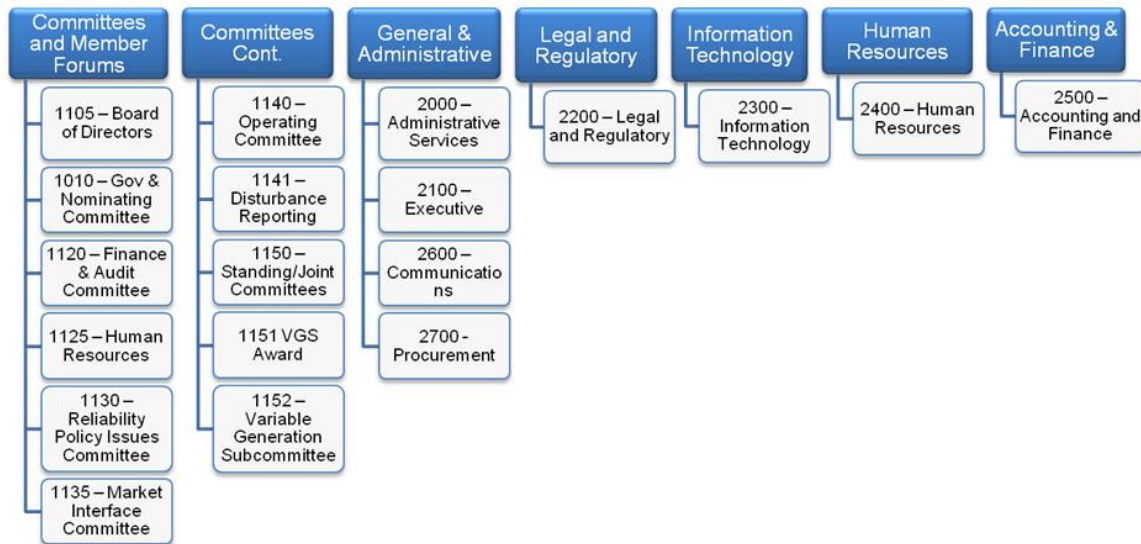
WECC, along with the other REs, followed the NERC System of Accounts (NSOA) in its budgeting. The NSOA had standard categories that segregated revenue and expenses based on functional categories within the NERC Rules of Procedure.<sup>12</sup> Certain categories related to functional activities while other categories related to overhead activities. For example, functional category 0300, Reliability Standard Development, included revenue and expenses for activities defined as functions required under section 300 of NERC's Rules of Procedure. Therefore, WECC, NERC, and the Commission can identify and compare budgeted versus actual amounts within each functional category among different REs.

Under these categories, WECC had numerous departments, denoted by four-digit department codes, each of which had a budget department manager and rolled up to NSOA functional categories. This chart shows which WECC departments rolled up into the functional categories within the NSOA, as presented in WECC's budgets:



<sup>12</sup> Each RE, including WECC, is required to comply with NERC's Rules of Procedure, as applicable to its delegated functions.

This chart shows the WECC departments that rolled up into overhead categories within the NSOA:



WECC management assigned each employee to a “home” department. This department accumulated costs (both budgeted and actual) associated with the employee (e.g., salary and benefits, travel expenses, and so on). In its budget filings, WECC allocated the overhead categories across functional categories and WECC’s sole nonstatutory activity, WREGIS, based on the full-time equivalent (FTE) positions in each department.

Besides establishing functional categories, the NSOA established the accounts for NERC and the REs to use. For instance, Account 47000, Workshops, a revenue account, was to record workshop fees collected from attendees. Account 51000, Direct Salaries, an expense account, was to include all charges for salaries paid to full- and part-time employees.

## E. Budget Process

WECC’s process for developing its budget began approximately one year prior to the budget year. WECC’s Accounting department developed a budget template for each of WECC’s budget departments to use. The budget template separately listed revenue and expense accounts the NSOA established. In late January, WECC’s Accounting department provided this template, with instructions, to each budget department manager. Budget templates included formulas, which could not be modified by the budget department manager, for merit increases for personnel, and benefit rates (the percentage contributions for employee benefit programs.) Benefit rates were determined in conjunction with WECC’s Human Resources department. Budget templates for each department were also pre-populated with that department’s actual revenues and expenses

for the prior year, as well as budgeted revenues and expenses for the current year. For example, because the budget process for 2012 occurred during 2011, the templates for the 2012 budget could only include actual revenues and expenses for 2010 and budgeted revenues and expenses for 2011.

From this starting point, budget department managers populated the templates for the next budget year. For example, department managers projected whether they would need to add positions, as well as their estimated salaries. Based on pre-populated salary formulas and any projected positions the budget department manager added, the salary expense for Account 51000 would automatically populate. WECC management asked budget department managers to describe any new planned initiatives for the upcoming budget cycle. For accounts where managers entered amounts, a description column allowed them to outline their reasoning.

In early February, budget department managers would send completed department budget templates to WECC's Accounting department, where they were reviewed, rolled up into NSOA functional and overhead categories, and sent to WEST for review. In mid-March, WECC's management submitted a first draft of the budget to the FAC for review and comment. WECC would address the FAC's comments and create a second draft of the budget for the FAC by mid-April. In mid-June, the budget would be submitted to the WECC Board for approval. In early July, WECC would submit the approved budget to NERC for review and approval, and in late August NERC would submit WECC's budget, along with its own budget and the budgets for the other REs, for Commission review.

The WECC Accounting department had an ongoing relationship with both the budget department managers and WEST. Each month, the Accounting department met with budget department managers to discuss variances between the current year's budget and actual results, the cause of variances, and budget forecasts. The Accounting department also consolidated and presented the variance reports to WEST for review. Reports identifying and explaining variances between actual and budgeted amounts were also submitted to NERC each quarter.

Audit staff believes that before this audit commenced, WECC took steps to improve its budget process, including development of WEST and the use of budget templates. Also, WECC has considered the need for policies and procedures governing changes to the budget during an ongoing budget cycle. WECC has a Delegation of Authority policy that entrusts spending authority to WECC management at various authorization levels. The policy specifically contemplates unbudgeted expenditures, which it defines as "an expenditure that was not individually identified in the Board-approved budget or causes the Cost Center to exceed its budget within an expense category." Audit staff is encouraged by the steps WECC has taken to improve its processes for budget development and administration.

## F. Employee Time Tracking

Under WECC's policies for employee time reporting in place during the audit period, WECC did not track time by project or department. Instead, within WECC, each employee's assigned home department accumulated costs (both budgeted and actual) associated with the employee (e.g., salary and benefits, travel expenses, and so on). Only nonexempt employees used WECC's timekeeping system to record their actual work start and stop times, and this was done after the work was performed. Exempt employees did not use this system to record actual hours worked.<sup>13</sup> Both exempt and nonexempt employees used the system to determine paid time off balances and submit requests and/or post absences for paid leave including sickness, vacation, floating holidays, bereavement, and jury duty. WECC noted that data is transferred from its timekeeping system to its payroll system, and that its payroll system did not allow for tracking an employee's actual hours by project or department. Under the payroll system, time could be split based on pre-set percentages, but not on actual hours worked during a given pay period.

Alternative avenues for tracking employee time were available to WECC outside of its formal timekeeping system. For example, certain employee time (as well as certain types of expenses) was not chargeable under the grants WECC received from the DOE. Since September 2011, WECC has used Microsoft SharePoint as an additional system for tracking time that applies only to the employees working on projects subject to its Federal grants. SharePoint allowed these employees to enter time (daily hours and overtime work) associated with specific grant activities. All grant-related time was recorded electronically and maintained on WECC's SharePoint site. Each employee recorded the total number of hours worked, including overtime, and major activities for the week. Recorded detail included grant activity, nonchargeable time, and paid time off and holiday time.

WECC noted that its employees (other than the shared employees located under overhead categories within the NSOA, which are allocated on an FTE basis) did not work on behalf of multiple statutory functions, with only one exception. The exception was WECC's Manager of Training, whose time was split 50/50 for budgeting purposes. Because employees did not work on behalf of multiple statutory functions, audit staff does not take issue with WECC's methodology for tracking time. However, we note there are benefits to tracking time on a detailed basis, such as enhancing WECC's ability to prioritize when dealing with time-sensitive deadlines. As explained later in this report, WECC set a goal of 45 days for accepting or rejecting mitigation plans. Audit staff believes tracking actual employee time could help ensure goals set are appropriate, met,

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<sup>13</sup> The terms "exempt" and "nonexempt" employees apply under the Fair Labor Standards Act (FLSA); nonexempt employees are entitled to overtime pay under the FLSA, where exempt employees are not.

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and any bottlenecks in the process are discovered and addressed quickly. Also, WECC evaluated employee performance annually, the results of which were indexed to the employee's annual goals. Detailed time tracking could help WECC enhance its processes to evaluate the efficiency of job performance.

### III. Introduction

#### A. Objectives

The Commission stipulated this audit in its order approving the Division of Audit's 2009 Audit Report of WECC under Docket No. PA09-5-000.<sup>14</sup> Besides evaluating WECC's implementation of the recommendations identified in the audit under Docket No. PA09-5-000, this audit addressed WECC's responsibilities and operations as an RE under: (1) the Delegation Agreement between the North American Electric Reliability Corporation (NERC) and WECC,<sup>15</sup> (2) the WECC Bylaws,<sup>16</sup> and (3) other obligations and responsibilities as the Commission approved. Also, the audit evaluated WECC's budget formulation, administration, execution, and the resources used to achieve program results. The audit covered the period from August 23, 2006 to December 31, 2012.

#### B. Scope and Methodology

Audit staff tested WECC's implementation of corrective actions in response to the Division of Audits' recommendations in the audit under Docket No. PA09-5-000 to ensure WECC addressed the issues the audit identified. Also, we evaluated WECC's operations with respect to its delegated functions. Further, audit staff evaluated WECC's budget formulation, administration, and execution, with a focus on whether WECC was achieving program objectives economically and efficiently.

To address these scope areas, audit staff completed these steps:

- Identified the standards and criteria used to evaluate WECC's compliance with each of the issues within the audit scope. These standards and criteria included Commission rules, regulations, letter orders, and other requirements.

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<sup>14</sup> *Western Electricity Coordinating Council*, 132 FERC ¶ 61,149, P 23 (2010).

<sup>15</sup> *North American Electric Reliability Council, et al.*, 119 FERC ¶ 61,060 (2007) (Delegation Agreements Order), *order on reh'g*, 120 FERC ¶ 61,260, *order on compliance filing*, 122 FERC ¶ 61,245 (2008) (Second Delegation Agreements Order), *order on compliance filings*, 125 FERC ¶ 61,330 (2008) (Third Delegation Agreements Order).

<sup>16</sup> WECC, *Bylaws of the Western Electricity Coordinating Council* (Mar. 1, 2012) (on file with author), available at [www.wecc.biz/library/WECC%20Documents/Business%20and%20Governance%20Documents/WECC%20Bylaws%202012.pdf](http://www.wecc.biz/library/WECC%20Documents/Business%20and%20Governance%20Documents/WECC%20Bylaws%202012.pdf).

- Reviewed the audit report under Docket No. PA09-5-000 and identified areas where follow-up was necessary to test WECC's implementation of recommendations that the Division of Audits made.
- Reviewed publicly available materials, filings WECC submitted to the Commission's eLibrary, Commission orders and formal complaints, the Enforcement Hotline, and local newspapers, and trade and academic press to identify significant items.
- Issued data requests and reviewed records to test WECC's compliance with Commission orders and statutes. Through phone conferences, the audit team clarified data responses and sought additional information.
- Conducted a site visit to WECC's headquarters in Salt Lake City, UT, in February 2012, during which we followed up on WECC's implementation of the Division of Audits' recommendations to address issues identified in the WECC audit under Docket No. PA09-5-000. Further, we interviewed the management personnel listed below to understand their job functions and any organizational changes that occurred at WECC after the audit of the WECC under Docket No. PA9-5-000 was completed:
  - President and CEO;
  - VP of Compliance;
  - VP and General Counsel;
  - VP of Operations and Planning;
  - VP of Shared Services;
  - Controller;
  - Grant Accountant;
  - Director of Compliance Audits and Investigations;
  - Director of Human Resources; and
  - Manager of Compliance Enforcement.
- Conducted a site visit to WECC's headquarters in September 2012, where we continued to learn about WECC's practices as they related to its operations as an RE. Specifically, audit staff interviewed employees about WECC's records management practices, mitigation plan processing, and enforcement caseload. Also, audit staff conducted interviews to better understand the relationships between event analysis and compliance processes as well as between the WECC RC and CMEP functions. Finally, audit staff continued its review of WECC's expenses and budget development, administration, and execution.

To facilitate audit staff's evaluation of WECC's budgeting practices and its operations as an RE, audit staff reviewed and tested WECC's processes, policies,

procedures, and controls. Specifically, audit staff conducted these activities related to the audit's major subject areas:

*Objectives of WECC, its Delegated Responsibilities, and Functional Organization*

- Reviewed WECC's organizational chart to understand its structure and the responsibilities of its various functional groups, including policies and procedures in place to ensure program objectives were achieved.
- Reviewed the responsibilities of each of WECC's functional units including duties delegated to WECC, as listed in Attachment E of WECC's Delegation Agreement, as well as any other programs each functional unit may have performed.
- Examined WECC's governance structure and meeting minutes from various committees to develop an understanding of the role WECC's Board had in WECC's fulfillment of its delegated responsibilities.
- Reviewed policies and procedures that ensured WECC's nonaffiliated directors met independence requirements.
- Reviewed documentation and conducted interviews with WECC's CEO related to WECC's strategic initiative and proposal to pursue bifurcation of WECC.

*Accounting and Recordkeeping*

- Reviewed WECC's accounting policies, procedures, and manuals as well as WECC's audited financial statements.
- Evaluated WECC's investments for consistency with its investment policy, and also reviewed how WECC tracked investments for both its statutory and nonstatutory funds.
- Examined the policies and procedures at WECC for submitting, reviewing, and paying expenses; and evaluated the oversight of those policies and procedures by the Accounting department and WECC management.
- Conducted reviews of a sample of expenses from WECC employees and directors on the WECC Board, and expenses from certain categories, including Board events, holiday parties, summer appreciation events, team building, and airline club memberships.



- Examined the process employees used to report their time, including the software used and how WECC ensured employee time was correctly reported.
- Tested WECC's policies and procedures for funding activities related to WECC's DOE grants including the treatment of unallowable expenses.
- Interviewed WECC's external accountant to understand the extent of work performed at WECC.

*Budget Formulation, Administration, and Execution*

- Examined the processes and procedures WECC used to develop its annual budget and identify resources needed to adequately achieve program goals and objectives.
- Evaluated the components of WECC's budget for its statutory functions to determine the breakdown for individual functions, including both those functions initially delegated by NERC and the statutory funding for the expanded list of functions WECC sought and was granted.
- Tested WECC's budget process by reviewing internal budget documents and conducting interviews to ensure that department budgets could be reconciled with WECC's Business Plan and Budget filed with the Commission, and to determine how WECC decided its budget priorities.
- Reviewed the detail of WECC's internal budget documents and its Business Plan and Budget filings to evaluate the granularity of the information presented in WECC's filed budgets.
- Examined how WECC used its budget throughout the budget year to support daily operations and contingencies.
- Reviewed WECC's procedures for monitoring its budget and conducting budget variance analysis throughout the budget year.
- Analyzed trends in WECC's Business Plan and Budget;
- Interviewed WECC staff to understand the process WECC used to reallocate funds from one functional unit to another within a budget year.

*Situation Awareness and Event Analyses*

- Reviewed event analyses WECC performed.
- Reviewed WECC's policies and procedures and interviewed WECC staff working on event analysis to understand the role of WECC's compliance staff in the process.
- Evaluated the practices WECC employed about the relationship between its compliance and enforcement activities and its RC.
- Interviewed WECC staff to understand the reason for using penalty monies collected from only U.S. entities to pay for settling alleged RC violations.

*WECC's Compliance with its CMEP*

- Reviewed processes for monitoring enforcement items and mitigation plans, and evaluated the tools for performing this monitoring by observing their functionality as WECC demonstrated.
- Reviewed audit procedures to ensure WECC enforcement staff was able to modify or change conclusions of WECC compliance staff's audits of registered entities.
- Reviewed a sample of mitigation plans and quarterly updates from registered entities and WECC's documentation of its review of those mitigation plans to evaluate WECC's implementation of its policies and procedures.
- Tested a sample of mitigation plan reviews for compliance with CMEP requirements.
- Reviewed enforcement caseload documentation for a sample of violations to evaluate WECC's implementation of its policies and procedures.
- Evaluated WECC's use of the standards development process as it related to its regional criteria.

*Staffing and Organizational Responsibilities*

- Evaluated WECC's policies and procedures for personnel management, including descriptions of positions on its organizational chart, hiring procedures, performance management, and compensation practices.

- Reviewed the process WECC used to budget for bonuses and other incentive compensation.
- Reviewed compensation studies performed for WECC and evaluated any changes WECC implemented as a result.
- Reviewed WECC's policies and procedures for relocation expenses, signing bonuses, and tuition reimbursement.

## IV. Conclusions and Recommendations

### 1. Mitigation Plan Processing

WECC's review of mitigation plans could be improved by strengthening its processes and documentation standards for the review, approval, tracking, and certification of mitigation plans registered entities submitted. This improvement would increase the efficiency and effectiveness of the process by making WECC and the registered entities more accountable and encouraging more timely and thorough implementation of mitigation measures, which in turn benefits the reliability of the BPS.

#### Pertinent Guidance

In its June 13, 2007 order clarifying NERC procedures on mitigation plans, the Commission noted that "where a user, owner or operator of the Bulk Power System is found by NERC to be in noncompliance with a Reliability Standard, NERC's Rules of Procedure require that entity to submit to NERC for approval a mitigation plan with a timeline addressing how the noncompliance will be corrected."<sup>17</sup>

In its July 3, 2008 Guidance Order on Reliability Notices of Penalty, the Commission noted that it "attaches great importance to the successful, timely completion of mitigation plans for the purpose of bringing into compliance registered entities that violate Reliability Standards ... The Regional Entities and NERC have responsibility for reviewing proposed mitigation plans to ensure that they, in fact, are designed to bring a registered entity back into compliance within a reasonable time."<sup>18</sup>

Exhibit D of WECC's Delegation Agreement, Compliance Monitoring and Enforcement Program, states in part:

#### 1.0 Regional Compliance Monitoring and Enforcement Program

WECC will implement the NERC Compliance Monitoring and Enforcement Program, Appendix 4C to the NERC Rules of Procedure...

Appendix 4C of the NERC Rules of Procedure, Uniform Compliance Monitoring and Enforcement Program of the North American Electric Reliability Corporation (NERC CMEP), states in part:

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<sup>17</sup> *Order Clarifying Procedures*, North American Electric Reliability Corporation, 119 FERC ¶ 61,274, at P 5 (2007).

<sup>18</sup> *Guidance on Filing Reliability Notices of Penalty*, North American Electric Reliability Corporation, 124 FERC ¶ 61,015, at P 35 (2008).

### Section 6.3, Timetable for Completion of Mitigation Plans

The Mitigation Plan shall be completed in time to have a reasonable potential to correct all of the violation(s) prior to the next applicable compliance reporting/assessment period after occurrence of the violation for which the Mitigation Plan is submitted. In all cases the Mitigation Plan should be completed without delay.

### Section 6.5, Review and Acceptance or Rejection of Proposed Mitigation Plans

Unless extended by the Compliance Enforcement Authority, it will complete its review of the Mitigation Plan, and will issue a written statement accepting or rejecting the Mitigation Plan, within thirty (30) days of receipt; otherwise the Mitigation Plan will be deemed accepted

... The Compliance Enforcement Authority will notify the Registered Entity within ten (10) business days after receipt of a revised Mitigation Plan whether the Compliance Enforcement Authority will accept or reject the revised Mitigation Plan ...

### Section 6.6, Completion/Confirmation of Implementation of Mitigation Plans

The Registered Entity shall provide updates at least quarterly to the Compliance Enforcement Authority on the progress of the Mitigation Plan. The Compliance Enforcement Authority will track the Mitigation Plan to completion and may conduct on-site visits and review status during audits to monitor Mitigation Plan implementation.

Upon completion of the Mitigation Plan, the Registered Entity shall provide to the Compliance Enforcement Authority certification, signed by an officer, employee, attorney or other authorized representative of the Registered Entity, that all required actions described in the Mitigation Plan have been completed and shall include data or information sufficient for the Compliance Enforcement Authority to verify completion. The Compliance Enforcement Authority shall request such data or information and conduct follow-up assessments, on-site or other Spot Checking, or Compliance Audits as it deems necessary to verify that all required actions in the Mitigation Plan have been completed and the Registered Entity is in compliance with the subject Reliability Standard ...

## Section 6.7, Recordkeeping

The Compliance Enforcement Authority will maintain a record containing the following information for each Mitigation Plan:

- Name of the Registered Entity.
- Date of the violation.
- Monitoring method by which the violation was detected.
- Date of notification of violation and sanction.
- Expected and actual completion date of the Mitigation Plan and major milestones.
- Expected and actual completion date for each required action.
- Accepted changes to milestones, completion dates, or scope of Mitigation Plan.
- Registered Entity's completion notice and data submitted as evidence of completion.

## Background

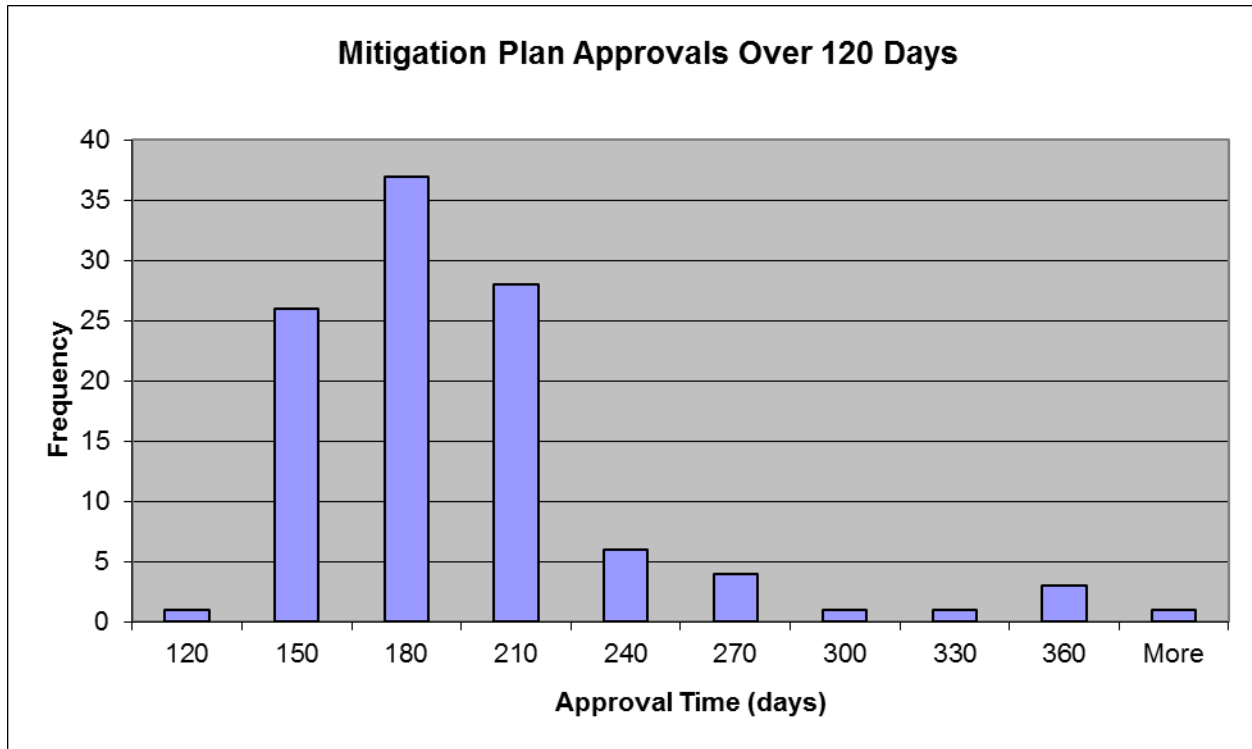
Under its Delegation Agreement, WECC must monitor and enforce compliance with Reliability Standards. When a registered entity is found to be in violation of a Reliability Standard, the entity is required to file a proposed mitigation plan outlining specific actions it proposes to for correcting the violation. WECC's responsibilities include review and approval of proposed mitigation plans, as well as ongoing monitoring of plans and eventual verification of completion. Audit staff tested WECC's policies and procedures for mitigation plan processing. Audit staff found areas for improvement relating to mitigation plan acceptance or rejection; certification of completion; review of mitigation plan milestones; and documentation and recordkeeping.

### *Mitigation Plan Acceptance or Rejection*

WECC's role in processing mitigation plans, as clarified in the Commission's July 3, 2008 Guidance Order on Reliability Notices of Penalty, is to review proposed mitigation plans to ensure that they are: (1) sufficient to bring the registered entity back into compliance; and (2) that they do so in a reasonable timeframe. The reliability of the BPS benefits when registered entities act quickly to implement mitigation measures and comply with Reliability Standards. Similarly, the reliability of the BPS benefits when WECC acts promptly to review and approve (or reject) mitigation plans and ensure registered entities implement mitigation measures to comply with required standards.

Audit staff reviewed approximately 520 mitigation plans submitted and accepted during the audit period. Audit staff notes that the CMEP required only that WECC

accept or reject the mitigation plan, or extend its review period within 30 days. WECC met this requirement in all but a handful of cases where a notice of extension was inadvertently not sent. While audit staff has no concerns with WECC's compliance with the CMEP in this area, we focused our review on evaluating whether WECC has opportunities to further improve its processes and procedures for mitigation plan processing. Of 520 plans, audit staff found that for approximately 260 plans, WECC extended its review period beyond 30 days. To illustrate this point, this graph depicts only those plans that took WECC longer than 120 days to approve:



The review period necessary for any particular mitigation plan can vary based on several factors, including the plan's scope and technical complexity and whether WECC needed to perform an additional inquiry to understand the scope of a violation. To test WECC's processes, audit staff requested supporting documents and communications for 59 mitigation plans. Our analysis focused on factors that might have contributed to the length of WECC's review period. Most often, we found the length of time for the reviews sampled appeared justified. However, we identified 12 instances that did not appear justified. Audit staff asked WECC to justify the timeframes. In nine of the 12 instances, WECC conceded that no extenuating circumstances justified the length of its reviews. This represented approximately 15 percent of the plans we sampled, or less than two percent of the 520 plans reviewed. Audit staff noted this is a small percentage and also that the CMEP does not require WECC to review mitigation plans in any particular time period. Nevertheless, because of the importance of WECC's timely review of all

plans to the reliability of the BPS, we believe this illustrates an opportunity for further enhancement to WECC's processes and procedures.

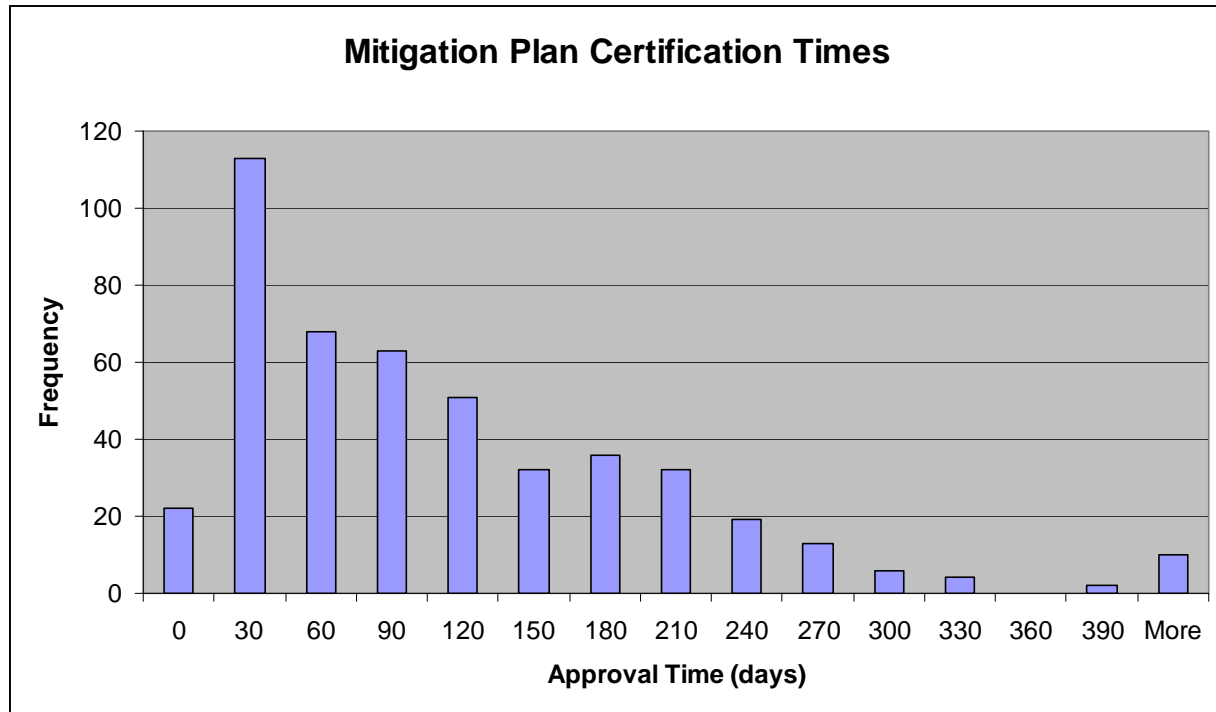
Also, audit staff found WECC did not always follow the timeframes the CMEP established. Section 6.5 required the Regional Entity to accept or reject revised mitigation plans within 10 business days. Audit staff identified several instances where this timeframe was not followed. WECC explained that several factors can complicate a review and require extra time for mitigation plans that have been initially rejected. These factors could include technical complexity or a disagreement with the entity over proper mitigation measures for a potential violation. However, WECC noted that changes in its system capabilities now allow it to flag revised mitigation plans for priority review. Audit staff is encouraged by this change, and believes WECC should strive to review resubmitted plans as soon as practicable, while still ensuring a thorough review.

#### *Verification and Acceptance of Certification of Completion*

After implementing its mitigation plan, a registered entity must certify the plan as complete. Upon receiving this certification, section 6.7 of the CMEP required WECC to request information and conduct a follow-up assessment to verify completion of the plan. The CMEP does not require WECC to certify completion within any particular time period. Therefore, again, audit staff does not have concerns with WECC's compliance with the CMEP in this area, but we note that the BPS benefits when WECC acts promptly to verify completion.

Audit staff reviewed data relating to WECC's certification of completion. We evaluated whether opportunities existed for WECC to further improve its processes and procedures surrounding certification. Of 520 submitted and accepted plans audit staff reviewed, WECC completed the verification and acceptance of certification for approximately 470 plans. The following graph shows the time for WECC to verify and accept the certification of completion for mitigation plans during the audit period. Since most of the verification work was performed in the 30- to 60-day range, the graph demonstrates WECC's commitment to rapidly processing mitigation plan certifications to ensure the measures necessary for reliability have been properly implemented. However, it also shows further improvements could continue to reduce the number of instances in which protracted review periods occurred:





To test WECC's processes, audit staff sampled 59 verifications. Of these, audit staff identified 10 certifications that took a long time to process. Many of these instances were for the same mitigations as the 12 lengthy reviews discussed above. Based on our review of WECC's records, audit staff could not find a justification for the protracted review period in these instances. Audit staff requested that WECC further research these incidents and provide more information as to why it believed the time to verify each mitigation plan was appropriate. In seven of the 12 instances, representing approximately 12 percent of our sample, or less than two percent of the 480 plans reviewed, WECC conceded no extenuating circumstances justified the time for its review. Audit staff notes again that this is a small percentage and not an issue of compliance with the CMEP, but rather another area where audit staff believes WECC could further enhance its processes and procedures.

Audit staff concluded that WECC's processes, procedures, and controls in place during the audit period for accepting, rejecting, or extending its review period of mitigation plans, as well as the certification of completion process, could be improved. WECC acknowledged room for improvement, and has already made changes to its processes. Before 2010, WECC auditors were primarily responsible for reviewing proposed mitigation plans and verifying their completion, besides their duties conducting compliance audits. With the introduction of Critical Infrastructure Protection (CIP) standards, the number of violations reported and in need of mitigation rose rapidly. Due to constraints on auditors' time, WECC extended mitigation plan review periods. To address this situation, in 2010 WECC transferred responsibility for reviewing CIP mitigation plans to a dedicated team of CIP enforcement subject matter experts (SMEs).

WECC believed this approach was successful, and in April 2012 it created a similar group of enforcement SMEs to facilitate the reviews of mitigation plans for operations and planning standards.

WECC believes these changes aid reduction of processing times. WECC has set a goal to review mitigation plans within 45 days. Audit staff is encouraged by these efforts. Mitigation plan processing is an essential part of WECC's role. Effective and efficient processing in turn contributes to BPS reliability. Therefore, we believe WECC should continue enhancing its policies, procedures, and controls for mitigation plan processing.

### *Tracking Mitigation Plans*

Section 6.6 of the CMEP required registered entities to update WECC at least quarterly on the progress of their mitigation plans. Further, section 6.6 required WECC to track mitigation plans to completion. WECC informed audit staff that, as a matter of process, it did not track or review mitigation plan milestone reports registered entities submitted. WECC also did not perform any verification of registered entity completion of mitigation plan milestones. However, WECC said it does issue reminder email notices about two weeks before a scheduled mitigation plan completion date. WECC also said it is assessing the potential to use a mitigation plan and milestone activities tool available in webCDMS.<sup>19</sup> This tool could help track the status of a specific mitigation plan, the scheduled completion date of a plan, and milestone completion dates.

While CMEP section 6.6 does not state that WECC must track and review milestone updates, WECC must track mitigation plans to their completion, and the timely completion of milestones is an integral part of the plan process. Because the CMEP required registered entities to submit milestone updates, audit staff believes WECC should perform a risk-based review of these updates to verify implementation progress. This would act as a control to ensure that mitigation plan implementation stays on schedule, which in turn would help ensure BPS reliability.

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<sup>19</sup> WebCDMS is software application used to facilitate communication as well as the exchange of CMEP data between registered entities and REs. REs can use webCDMS to notify entities about CMEP actions, document data submittals (e.g., mitigation plan, certification of mitigation plan completion, and so on) and track milestones and other correspondence relating to those submittals.

*Documentation and Record Retention*

Section 6.7 of the CMEP required WECC to retain records for processing mitigation plans, as well as for the enforcement process more generally. Audit staff found WECC had policies and procedures for retaining many primary documents related to the review of mitigation plans, such as mitigation plan submission forms and letters approving mitigation plans. However, besides these types of documents, there could be less formal elements to the mitigation review process. For example, WECC could send emails with questions on a mitigation plan to a registered entity, or could conduct teleconferences to request clarifying information. In our sample of mitigation plans, staff noted an absence of documentation about these types of communications. WECC explained that it had no policy for centrally documenting and retaining materials related to emails and conference calls with registered entities regarding mitigation plans. WECC enforcement staff said many of these communications were not formally kept in its official files for each mitigation plan, and were generally stored on individual computers.

Audit staff believes WECC's policies and procedures should standardize documentation requirements to ensure adequate and accurate documentation for WECC's review of mitigation plans, including informal communications such as emails and conference calls. To the extent these are nontrivial discussions that affect WECC's disposition of a matter, salient points should be documented in writing and centrally retained to ensure a full and complete record of WECC's decision making process. This also would ensure that in the event of employee turnover, it is still possible to find this information.

Also, audit staff found certain incorrect data in WECC's mitigation plan records. On June 17, 2011, during the transition to OATI's webCDMS platform for compliance monitoring, WECC shut down the WECC Compliance Portal and changed its Compliance Information Tracking System (CITS) to a read-only system.<sup>20</sup> All relevant records and dates for open violations were migrated to OATI for use in webCDMS. WECC explained that there was a "NERC data issue related to revised Mitigation Plans." WECC said it was working to backfill webCDMS with revised mitigation plan information. Audit staff believes WECC should ensure its records are accurate, and we encourage WECC to continue with this process.

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<sup>20</sup> CITS was a user interface WECC used internally to store compliance data, such as violation reviews, case notes, dates, and mitigation plan information. It provided tracking for data registered entities submitted through self-reports, mitigation plans, extension requests, and certification of mitigation plan completions.

**Recommendations**

Audit staff recommends that WECC:

1. Continue to enhance its policies and procedures to ensure that each proposed mitigation plan or application for certification of mitigation plan completion is accepted or rejected in a timely manner;
2. Enhance its policies and procedures to ensure revised mitigation plans are prioritized for review;
3. Strengthen its policies and procedures for tracking mitigation plans to completion. Such policies and procedures should include steps to track mitigation plan progress through quarterly updates;
4. Improve its policies and procedures to standardize its documentation and record retention requirements to ensure it retains adequate and accurate documentation for its review of mitigation plans. These policies should also ensure WECC's mitigation plan records are complete and accurate; and
5. Continue to correct inaccurate data currently in webCDMS.

## 2. Enforcement Caseload

WECC's policies and procedures could be improved to ensure enforcement staff adequately documents its review of potential Reliability Standard violations. Inadequate documentation could inhibit efforts by WECC's management to ensure enforcement staff consistently performs quality reviews. Further, the lack of standardization in documentation requirements could complicate enforcement staff's efforts and hinder effective operations.

### Pertinent Guidance

Exhibit D of WECC's Delegation Agreement, Compliance Monitoring and Enforcement Program, states in part:

#### 1.0 Regional Compliance Monitoring and Enforcement Program

WECC will implement the NERC Compliance Monitoring and Enforcement Program, Appendix 4C to the NERC Rules of Procedure...

Appendix 4C of the NERC Rules of Procedure, Uniform Compliance Monitoring and Enforcement Program of the North American Electric Reliability Corporation, states in part:

#### Section 5.0, Enforcement Actions

The Compliance Enforcement Authority shall determine (i) whether there have been violations of Reliability Standards by Registered Entities within the Compliance Enforcement Authority's area of responsibility, and (ii) if so, the appropriate remedial actions, and penalties and sanctions, as prescribed in the NERC Sanction Guidelines ...

The WECC Enforcement Procedure, section 2.2, processing the Notice of Alleged Violation and Proposed Penalty or Sanction (NAVAPS), includes the following requirements:

2.2.1. Preparation: The Compliance Enforcement Analyst performs the following checks:

- Check to see if there are any other outstanding violations by the Registered Entity that can be grouped with the assigned violation(s); including, but not limited to:

- Violations in the database that have not yet been assigned
  - Violations that have not yet been entered into the database
  - Violations that could result from an upcoming Audit or Spot-Check
- Check to see if any violations may also result in the violation of any other Reliability Standards
  - Check to see if any violations are repeat violations of the Standard.
  - Check to see if any of the violations are event- or request-driven or on the FERC Unenforceable list.
  - Check to see if the Registered Entity has self-certified compliant with any of the Standards (e.g., in a previous time period).

2.2.2. Determining an Alleged Violation: The Compliance Enforcement Analyst is responsible for reviewing all applicable information, including but not limited to: (1) source documents; (2) WECC subject-matter expert (SME) findings, including violation review worksheets or Reliability Standard Audit Worksheets (RSAW); (3) data requests; (4) mitigation plans; (5) entity correspondence, etc., to determine if the identified possible violation is an Alleged Violation.

## Background

Audit staff tested WECC's policies and procedures for enforcement staff's review of potential violations, and the amount of time involved for reviews. Audit staff found WECC had not developed standardized requirements for enforcement staff's documentation of certain information during its review of possible Reliability Standard violations.

WECC had an enforcement procedure outlining the steps staff should perform in evaluating the existence and extent of potential Reliability Standard violations. When compliance monitoring processes identified a potential violation, enforcement staff assigned a violation ID. WECC grouped violations into cases, each of which consisted of one or multiple violation IDs. Cases were then assigned to an enforcement analyst for review. Under the enforcement procedure, each enforcement analyst had to, among other actions, evaluate whether any violation might have resulted in any other Reliability Standard violations, or consisted of a repeat standard violation. The enforcement analyst also had to review all applicable information about the potential violation, including source documents, SME findings, RSAWs, data requests, mitigation plans, and entity correspondence. This process allowed WECC enforcement analysts to examine all relevant evidence in determination of whether a violation occurred and if so, send a NAVAPS to the registered entity.

To evaluate implementation of WECC's enforcement process, audit staff requested all documents on 35 sampled violations WECC enforcement staff processed. The sample included both violations WECC fully processed (i.e., they had been submitted to NERC, and then to the Commission and were approved), and a small number of alleged, and later dismissed, violations. Audit staff intended to review the documents and communication to determine the level of work each review required, and then, based on the unique facts and circumstances related to each enforcement case, evaluate the time to process each violation.

WECC had difficulty producing the requested documentation for multiple reasons. First, WECC said documentation related to the review by enforcement staff was on WECC's networked W: drive. WECC said it did not keep a predetermined list of all documentation maintained on the W: drive for each violation. Also, analysts might not have saved all documentation on the W: drive. WECC also confirmed that it had no way to determine exactly what documentation had been reviewed by an enforcement analyst for any particular violation ID, which further complicated WECC's efforts to produce the requested documentation.

Audit staff observed that documentation varied greatly from one enforcement analyst assigned to review the violation IDs to another. For example, some enforcement analysts saved documents such as teleconference notes, informal data requests, or email relating to particular violations, while other enforcement analysts did not move similar documents to the W: drive from their personal computers. As a result, audit staff found it challenging to evaluate the extent of the review WECC conducted for each violation sampled. Because audit staff could not determine what activities WECC undertook based upon information and documents located on the W: drive, audit staff could not evaluate the total processing time for each violation.

Ensuring adequate documentation of the review of potential Reliability Standard violations is important for multiple reasons. Audit staff requested that WECC explain all controls dictating what should be reviewed by enforcement staff. WECC said it is Enforcement's practice to review all relevant information during a violation review. However, absent thorough documentation, audit staff believes it would be extremely difficult for WECC management to ensure enforcement staff consistently performs quality reviews. Further, the lack of standardization in documentation requirements could complicate Enforcement staff's efforts and hinder operational efficiency. For instance, WECC's enforcement procedure required enforcement analysts to determine if any violations are repeat violations of a standard. Inadequate documentation, particularly in light of possible employee turnover, could inhibit an enforcement analyst's ability to determine the existence and extent of prior violations in evaluating a current violation.

Audit staff believes WECC should institute policies, procedures, and standardized documentation requirements to apply to Enforcement's review of potential violations of

Reliability Standards. Specifically, WECC should ensure that any communication, documents, and decisions that affect the disposition of the alleged violation are centrally retained to maintain a full and complete record. This may include communication generally regarded as “informal,” such as email exchanges or conference call notes.

### **Recommendation**

Audit staff recommends that WECC:

6. Strengthen its policies and procedures relating to documenting its review of potential violations of Reliability Standards by enforcement staff. Such policies and procedures should include enhanced documentation requirements to ensure enforcement staff retains adequate information relating to its review.



### **3. Conflict of Interest Disclosure Form Completion**

WECC's policies and procedures did not ensure timely and thorough completion of all conflict of interest disclosure forms it used to identify potential conflicts of interest within the CMEP. Although audit staff did not identify any instances where independence was impaired, appropriate policies and procedures are important to ensure the forms act as an effective control to help WECC ensure CMEP independence.

#### **Pertinent Guidance**

Section 6 of WECC's Delegation Agreement, Enforcement of Compliance with Reliability Standards, Part (h) states:

As part of its compliance monitoring and enforcement program, WECC shall maintain a conflict of interest policy that assures the integrity and independence of such program, including the integrity and independence of the persons or decision-making bodies making final determinations in compliance enforcement actions under Section 5.0 of the NERC Compliance Monitoring and Enforcement Program.

The NERC Rules of Procedure, section 403.7.1, states that "The Regional Entity shall have procedures defining the allowable involvement of industry experts and regional entity members." It further states that these procedures "shall address applicable antitrust laws and conflicts of interest."

WECC's internal procedures for compliance audits and compliance investigations, both effective January 29, 2011, include confidentiality, conflicts of interest, and related form requirements. The WECC Standard Operating Procedures for Compliance Audits, section 1.4 states, "All participants must sign applicable confidentiality agreements and conflict of interest forms." Further, section 2.1.1 of this procedure requires that an audit team leader verify that no team member has a conflict of interest and verify all appropriate confidentiality agreements and regional, NERC, and FERC code of conduct statements have been signed by each audit team member.

Similarly, the WECC Standard Operating Procedures for Compliance Investigations, section 1.4 states, "All participants must complete applicable confidentiality agreements and conflict of interest forms." Further, section 2.2.1 requires the team lead to verify that no team member has a conflict of interest.

The WECC Compliance Committee (WCC) charter, effective June 22, 2011, states:

Committee members who have a direct business relationship, direct financial interest in, or other affiliation with a Registered Entity in the WECC footprint that is subject to enforcement under the CMEP, must disclose those relationships to the Committee and update that disclosure quarterly.

## **Background**

WECC required WECC Compliance Committee (WCC) members and contractors working on CMEP activities to complete conflict of interest disclosure forms. By allowing WECC to identify and document actual or perceived conflicts of interest, these forms become an important control to help ensure CMEP independence. Because of their importance, audit staff reviewed these disclosure forms.

During our review, audit staff found WECC's policies and procedures insufficient to ensure completion of the forms in a timely and thorough manner. The WCC charter required members with direct business relationships or interests in WECC registered entities to complete these forms quarterly. However, audit staff found WECC did not monitor the submission of these quarterly updates, and WCC members did not complete numerous quarterly updates. Further, audit staff found a WCC member left the field on the form for disclosure of employment blank. WECC said some committee members thought if WECC was already aware of their employment or if their situation had not changed, they did not need to complete this section. Also, audit staff found some contractors working on CMEP activities did not complete the section of their form requiring previous employment information. WECC said it was unsure why this omission occurred, but it was possible contractors may have misread the form or entered pertinent information in one place but not in another because they believed it to be duplicative.

Audit staff noted that WECC has since improved its review processes for conflict of interest forms. In September 2011, WECC implemented a process requiring a WECC staff liaison to obtain updated conflict of interest forms from the necessary WCC members during in-person meetings on at least a quarterly basis. WECC has informed WCC members that they should fill in all requested information on the form, irrespective of any changes in their situation. Further, WECC said WECC management will review the forms completed by contractors working on CMEP activities to ensure completeness and correctness.

Audit staff is encouraged by this effort, as conflict of interest disclosure forms, when timely and thoroughly completed, are an important control that can increase

transparency and help ensure the independence of the RE's CMEP functions by identifying actual or perceived conflicts of interest.

**Recommendation**

Audit staff recommends that WECC:

7. Enhance its policies and procedures to ensure conflict of interest disclosure forms are completed and submitted in a timely and thorough manner.

#### **4. Budget Development**

In certain instances, WECC budgeted for the same expenses in multiple program areas, which resulted in double budgeting for these amounts, although to date these amounts have not been material. Also, audit staff identified two areas in the budget that we do not believe had sufficient transparency. Appropriate and transparent budgeting is essential to ensuring that NERC, the Commission, and stakeholders are able to properly evaluate WECC's budget, and that funding amounts are appropriate.

##### **Pertinent Guidance**

The Federal Power Act (FPA), as amended by the Energy Policy Act of 2005, added section 215 on Electric Reliability. Section 215(c)(2) states the Commission may certify an entity as an ERO if, among other things, the Commission determines that the ERO "... has established rules that allocate equitably reasonable dues, fees, and other charges among end users for all activities under this section."

##### **Background**

WECC's budget development process, explained in the audit report background, underwent enhancements in recent years. The WECC Executive Steering Team (WEST) met regularly and provided centralized oversight of the budget process. Further, for its 2012 budget, WECC introduced a budget spreadsheet template for each of its budget department managers to facilitate the budget development process. These spreadsheets were completed, reviewed, and eventually rolled-up into the NERC functional areas. Audit staff believes that the use of budget spreadsheets allows the opportunity for WECC to improve its granularity in budgeting. We focused our testing on the 2012 budget, where WECC's total funding requirement totaled \$69,788,290. This amount included U.S. statutory assessments, assessments to Canada and Mexico, grant funding, and WREGIS' nonstatutory funding. U.S. statutory assessments in 2012 totaled \$31,301,737.

In our review of WECC's 2012 budget, audit staff identified two areas that we believe point to improvement opportunities. First, some department managers included certain expenses in their budget spreadsheets when they were also budgeted organization-wide in the General and Administrative department budget. This led to double budgeting of these expenses, although to date these amounts were immaterial. Second, audit staff believes WECC should continue to enhance its policies and procedures to increase budget transparency.

##### *Double Budgeting*

Audit staff identified two areas where WECC inadvertently included expenses in its organization-wide General and Administrative budget while certain other budget

department managers also included these expenses in their budget spreadsheets, although the result was immaterial. First, WECC double budgeted for certain employee bonuses in its 2012 and 2013 budgets.<sup>21</sup> Besides the General and Administrative department, which budgeted for discretionary and incentive bonuses for all WECC departments, other departments included \$51,000 in bonuses. In 2013, the General and Administrative department again budgeted for bonuses, while other departments also included \$114,200 in bonuses. Because the General and Administrative and department budgets all rolled up into WECC's approved budget, this resulted in double budgeting for bonus amounts, totaling \$51,000 and \$114,200 in 2012 and 2013, respectively.

Similar to bonuses, WECC also double budgeted for certain tuition reimbursement expenses in 2012.<sup>22</sup> Besides the General and Administration department, which budgeted for tuition reimbursements for all WECC departments, several individual departments also budgeted separately for tuition reimbursements, which cumulatively totaled \$30,000. Again, because the General and Administrative and department budgets rolled up into WECC's approved budget, this resulted in double budgeting for these tuition reimbursements. WECC confirmed no double budgeting related to tuition reimbursement occurred in 2013.

Audit staff believes these instances of double budgeting occurred because budget department managers did not realize WECC centrally budgets for these types of expenses, and as a result inadvertently included the same types of expenses in their own department budgets. Although to date these amounts have been immaterial, audit staff believes these instances illustrate the need for policies and procedures with improved guidance from the Accounting department. We also believe this issue indicates an opportunity for the Accounting department to continue to enhance its review process so errors like this are identified and corrected before filing of the WECC budget with NERC and the Commission.

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<sup>21</sup> WECC has processes to reward employee performance, including merit-based salary increases, discretionary bonuses, and annual incentive bonuses for positions at or above the VP level.

<sup>22</sup> WECC also has a tuition reimbursement program that allows employees to obtain additional education or training to increase their competence in their current position and prepare for possible advancement within WECC. If an employee leaves WECC within a year of receiving reimbursement, the policy requires that employee to repay the amount he or she received.

*Transparency in Budgeting*

In reviewing WECC's filed budgets, audit staff identified two areas that we believe had insufficient transparency. First, as mentioned in the audit report background, WECC received certain grants under the American Recovery and Reinvestment Act (ARRA). WECC included these grants under the statutory activities section of its budgets. For example, the 2012 budget stated, "WECC will receive \$24.5 million in DOE grant funding for WISP. The funds directly offset increases in expenditures related to the WISP project."<sup>23</sup> Further, "WECC will receive \$2.9 million in DOE grant funding for the RTEP project. The funds directly offset increases in expenditures related to the RTEP project."<sup>24</sup> However, certain expenses are not reimbursable under the grants. These include indirect costs, and other unallowable costs such as certain types of travel, meals, and payments for alcohol, among other restrictions. Audit staff notes that WECC's representation in its budget that grant funding directly offsets grant expenses is accurate only to the extent there are no unallowable or indirect costs. Audit staff believes such costs should be broken out in a transparent way so those responsible for approving the budget can properly deliberate.

The second area audit staff identified where transparency could be increased was WECC's use of airline club memberships. WECC said it provided airline club memberships for employees who traveled frequently for WECC business, and that access to club facilities in airports enabled employees to be more productive when traveling. However, WECC said authorization for such memberships was up to each employee's manager. WECC stated further that it implicitly included airline club memberships in department budgets. Audit staff identified several club memberships purchased during the audit period. Audit staff believes this is another example of a type of expense that should be specifically contemplated in department budgets to ensure transparency. Audit staff believes WECC should adopt a consistent policy for managers to follow when granting approval for and explicitly budgeting for airline club memberships.

**Recommendations**

Audit staff recommends that WECC:

8. Improve its policies and procedures for budget development. Such policies and procedures should include additional guidance to ensure items are not double budgeted, and that all expenses are transparent; and
9. Continue to enhance the Accounting department's review of departmental budgets.

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<sup>23</sup> 2012 Business Plan and Budget at pg 37.

<sup>24</sup> *Id* at pg 28.

## 5. Employee Expense Reimbursement Policy and Controls

WECC could enhance its processes for reviewing expenses submitted for reimbursement through standardized written procedures and criteria for the review of such expenses. Although audit staff believes WECC's accounting staff thoroughly reviewed employee business expenses, centralized guidance to managers as to expectations for their review would be helpful as an additional control towards ensuring all employee business expenses that are reimbursed are appropriate.

### Pertinent Guidance

The Federal Power Act (FPA), as amended by the Energy Policy Act of 2005, added section 215 on Electric Reliability. Section 215(c)(2) states the Commission may certify an entity as an ERO if, among other things, the Commission determines that the ERO “... has established rules that allocate equitably reasonable dues, fees, and other charges among end users for all activities under this section.”

WECC's Travel Expense and Corporate Credit Card Policy outlined the following conditions that must apply for expenses to be reimbursable:

- Any travel expense should comply with the WECC Travel Expense Policy.
- The expense is reasonable and customary and is incurred in the performance of WECC business.
- The expense must have a specific, detailed business purpose and include documentation with the amount, date, and location.
- An original receipt must be submitted (itemized receipts for group meals and hotel charges), names and organizations of those attending should be noted.
- Costs must be allowable under any specific requirements (i.e., Federal grant awards), if applicable.

The policy also sets the following parameters around reimbursable expense documentation:

Reimbursable expenses must be supported by original receipts and the expense report must be signed by the employee and approved by the manager before being submitted to the accounting department. While original receipts are only required for expenses over \$25, employees are encouraged to submit all receipts, regardless of the amount ... In all cases, there must be a clear trail from the amounts on the receipts to the amounts claimed on the expense reimbursement report.

## Background

Audit staff obtained and reviewed the policies and procedures surrounding WECC's payment of employee business expenses. WECC's Travel Expense and Corporate Credit Card Policy (Employee Expense Policy) contained numerous controls over the reimbursement of expenses that WECC employees incurred. Audit staff believes all of these parameters and controls are beneficial. However, WECC told audit staff that it did not have documented policies and procedures for reviewing employee expense reports. Further, WECC does not provide training for new managers when they assume responsibility for reviewing and approving employee business expenses. Audit staff believes a standardized policy would be beneficial and provide another control over WECC's employee expense review process.

WECC's Employee Expense Policy says, "WECC will pay or reimburse reasonable business travel expenses for employees who are expected to travel out of their home location on behalf of WECC." Where employees travel frequently or have other business needs that require a credit card, they are issued a corporate card, which WECC pays for. The policy contained parameters and controls over payment of employee business expenses. For instance, when traveling for business, airline tickets were to be purchased at the most economical, nonrefundable coach fare. If an employee chose to drive rather than fly, the employee would only be reimbursed up to the cost of that coach fare. The policy stipulates that "moderate class hotels" should be used whenever available. Also, the most economical means of transportation, whether rental car, taxi, or shuttle, should be used. Regarding meals, detailed receipts were required, and an itemized list of all attendees was to accompany a receipt. Notably, the policy required original receipts for all expenses greater than \$25, and encouraged the submission of receipts for all expenses, even those under \$25.

Employees must submit monthly reconciliations of their credit card use, including an itemized receipt to support each transaction on their monthly credit card statements. An employee's manager and then a member of WECC's accounting staff reviewed and approved expenses. Audit staff requested evidence that WECC reviewed employee expense reconciliations for appropriateness and to ensure employees included adequate documentation. Absent written procedures, audit staff observed several instances where WECC approached employees to question certain expenses, and also ensured adequate inclusion of supporting documentation. However, audit staff identified areas where managers approved employee expenses with missing documentation, although WECC accounting staff later caught these instances. Audit staff believes centralized guidance to managers as to expectations for their review of expenses would be helpful as an additional control over WECC's expense review process.

It is important to emphasize that audit staff believes WECC accounting staff did thoroughly review employee expenses for reasonableness and appropriate documentation.



Audit staff believes a standardized written policy for employee expense review, including centralized guidance as to expectations for management's review, would be beneficial as another process control. Clear and specific guidelines for reviewing expense submissions would make it easier for managers to maintain consistency across WECC. By implementing policies and procedures outlining expectations for managers' reviews in terms of their review of expense reasonableness and documentation, WECC could ensure that it captures instances of noncompliance with the Employee Expense Policy before submittals to WECC's accounting staff.

**Recommendation**

Audit staff recommends that WECC:

10. Create policies and procedures and improve its controls to better inform managers as to expectations for their review of employee business expenses.

## 6. Investments

WECC's Investment Policy did not prohibit WECC from investing funds in registered entities, which could lead to possible conflicts of interest or independence concerns. Also, WECC assigned investment earnings to "statutory" and "nonstatutory" accounts (that is, accounts relating to funding WECC receives pursuant to FPA section 215 and accounts that relate to other sources of funding, respectively) based on FTEs, rather than actual earnings. To achieve stronger controls, audit staff believes WECC should segregate statutory and nonstatutory monies to prevent any possibility of cross-subsidization.

### Pertinent Guidance

#### *WECC's Investment Policy*

Section 403.1, Independence, of the NERC Rules of Procedure, states:

Each regional entity's governance of its compliance enforcement program shall exhibit independence, meaning the compliance enforcement program shall be organized so that its compliance monitoring and enforcement activities are carried out separately from other activities of the regional entity. The program shall not be unduly influenced by the bulk power system owners, operators, and users being monitored or other regional entity activities that are required to meet the reliability standards.

Section 6 of WECC's Delegation Agreement, Enforcement of Compliance with Reliability Standards, Part (h) states:

As part of its compliance monitoring and enforcement program, WECC shall maintain a conflict of interest policy that assures the integrity and independence of such program, including the integrity and independence of the persons or decision-making bodies making final determinations in compliance enforcement actions under Section 5.0 of the NERC Compliance Monitoring and Enforcement Program.

#### *Statutory and Nonstatutory Investments*

Order No. 672 developed procedures for the establishment, approval and enforcement of electric Reliability Standards. In Order No. 672, the Commission states in part:

Section 215 of the FPA generally provides for Commission authorization of funding for statutory functions, such as the development of Reliability Standards and their enforcement, and monitoring the reliability of the Bulk-Power System. The Final Rule clarifies, however, that while the ERO or a Regional Entity is not necessarily precluded from pursuing other activities, it may not use Commission-authorized funding for such activities.<sup>25</sup>

In the 2009 WECC audit report, which was accepted by the Commission on August 20, 2010, recommendation 4 required WECC to “Revise its existing accounting system to properly classify and track statutory and nonstatutory activities and funding for these activities.”<sup>26</sup>

In its audit implementation plan submitted October 19, 2010, WECC explained that it addressed this recommendation as follows:

In 2009, WECC implemented a new fund accounting system that allows for the separate tracking of costs and funding related to statutory and nonstatutory activities. This system implementation included the incorporation of the NERC system of accounts ... WECC uses the functional category code 9500 for its sole nonstatutory activity, the Western Renewable Energy Generation Information System (WREGIS).

## Background

Audit staff reviewed WECC’s investment policies to determine whether the potential for conflicts of interest existed. Audit staff noted that WECC’s policies did not prohibit WECC from investing funds in registered entities, which could lead to the appearance of conflicts of interest. Also, audit staff reviewed WECC’s processes for ensuring WECC kept statutory and nonstatutory monies separate and found WECC’s methodology allowed intermingling of statutory and nonstatutory investments, and WECC allocated investment earnings according to FTEs rather than actual earnings.

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<sup>25</sup> *Rules Concerning Certification of the Electric Reliability Organization; and Procedures for the Establishment, Approval, and Enforcement of Electric Reliability Standards*, Order No. 672, 114 FERC ¶ 61,104 at P 34 (2006), *order on reh’g*, Order No. 672-A, 114 FERC ¶ 61,328 (2006), *modified*, 123 FERC ¶ 61,046 (2007).

<sup>26</sup> *Western Electricity Coordinating Council*, 132 FERC ¶ 61,149 at P 23 (2010).

*WECC's Investment Policy*

Although WECC used two investment managers to oversee its investments and did not direct the investment in particular entities, WECC did receive detailed information on its investments. Specifically, WECC had online read-only access to all of its investment accounts. WECC said each investment manager's online portal provided statements, trading activity, portfolio holdings reports, income details, risk summaries, and graphs and charts. Much of this information was available daily. Further, each quarter WECC and its investment managers met to discuss investment performance and generally discuss investment strategies.

WECC's investment policy did not prohibit WECC from investing funds in registered entities. While WECC delegated custody and management of its investments, WECC could provide direction to its two investment managers to invest in particular entities. However, WECC said while it has the ability to direct its investment managers to modify their strategy or the securities in which they invest, WECC deferred to the expertise of the managers, within the boundaries the investment policy established. Therefore, WECC said it did not direct investments in individual stocks and bonds.

Audit staff is concerned that this arrangement does not ensure sufficient independence and protect against the potential for the appearance of conflicts of interest. Further, audit staff found that during the audit period, WECC's investment managers selected two investments in registered entities. Audit staff did not identify any instances where WECC's investments in any way influenced the fulfillment of its CMEP responsibilities. However, WECC's Delegation Agreement directs it to maintain a conflict of interest policy for its CMEP function. Audit staff believes, absent restrictions against investments in registered entities, independence could be impaired and the appearance of conflicts of interest might exist.

*Statutory and Nonstatutory Investments*

The Western Renewable Energy Generation Information System (WREGIS) is a renewable energy database for the Western Interconnection. WREGIS creates renewable energy certificates (RECs) for verifiable renewable generation from units registered in the database.<sup>27</sup> WREGIS was the sole nonstatutory activity listed in Exhibit E of WECC's Delegation Agreement, and was also the sole nonstatutory activity in WECC's annual budget filings. As the Commission explained in Order No. 672, WECC is not prohibited from pursuing activities unrelated to Reliability Standard development and enforcement, and monitoring BPS reliability. However, such activities must not be funded under section 215.

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<sup>27</sup> See WREGIS' web site at [www.wregis.org/](http://www.wregis.org/).

During our examination, audit staff sought to verify whether cross-subsidization occurred between statutory activities and WREGIS. WECC explained that it pools monies received under section 215 (statutory reserves) and reserves generated by WREGIS (nonstatutory reserves) for its investments. Further, WECC said it tracks nonstatutory monies through its accounting system, SAGE Fund Accounting, by designating them to a separate fund code. Specifically, WECC used Fund Code 10 to designate all statutory activity within its general ledger, and used Fund Code 90 to designate all nonstatutory activity. WECC also said it processes WREGIS financial data in a separate system (Quickbooks), with monthly reconciliations to the SAGE system.

However, to assign investment earnings to the statutory and nonstatutory reserves, WECC followed the same FTE method it uses to allocate indirect expenses to statutory and nonstatutory functions. Audit staff has concerns about the practice of allocating investment earnings based on FTEs rather than directly assigning the actual earnings based on how these monies were invested. WECC said it received all of its assessments for statutory activities at the beginning of the budget year. This resulted in higher balances in WECC's statutory operating funds and, as a result, WECC's interest earnings were higher at the beginning of the year as opposed to the end of the year. This peak in interest earnings was not associated with WREGIS reserves. Also, WECC informed audit staff that WREGIS' reserves were maintained in liquid investments, which were earning a much lower rate than average. For these reasons, audit staff is concerned the methodology could result in cross-subsidies. Audit staff believes WECC should directly assign investment earnings to statutory and nonstatutory reserves based on actual returns achieved on its investments of funds received from statutory and nonstatutory activities.

## **Recommendations**

Audit staff recommends that WECC:

11. Work with NERC to adopt restrictions on investments in registered entities to ensure the appearance of conflicts of interest does not occur;
12. Strengthen its policies and procedures to ensure cross-subsidization does not occur between statutory activities and its nonstatutory activities (e.g., WREGIS); and
13. Consider physically segregating its statutory and nonstatutory investments.

## 7. Funding of Regional Criteria under Section 215

WECC did not have written policies, processes, procedures, or internal guidance for parameters to consider as a basis for determining whether a proposed or ongoing activity should be considered statutory or nonstatutory. This was demonstrated in WECC's Regional Criteria which addressed not only reliability issues, but also consistency in business practices between WECC members. During the audit period, WECC initiated an assessment process regarding these criteria. Audit staff believes WECC should continue the development of processes to ensure activities it performs are appropriate to fund under section 215.

### Pertinent Guidance

In Order No. 672, the Commission stated:

Section 215 of the FPA provides for federal authorization of funding limited to the development of Reliability Standards and their enforcement, and monitoring the reliability of the Bulk-Power System. However, the ERO or a Regional Entity is not precluded from pursuing other activities, funded from other sources.<sup>28</sup>

WECC used the same standards development process as it used to develop regional Reliability Standards as provided for under the section 215 process. This process was used to develop, adopt, and modify its regional criteria, which include measures to ensure consistency in business practices between WECC members. WECC has indicated in its budget filings that regional criteria development and modification were included as statutory as a part of the Standards Development function:

The WECC standards development process is also used for the development of WECC Regional Criteria. Regional Criteria are requirements that are approved by the WECC Board. They do not require NERC or FERC approval. WECC will follow the same process for developing documents to meet the requirements of NERC Fill-in-the-Blank Standards as needed.<sup>29</sup>

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<sup>28</sup> Rules Concerning Certification of the Electric Reliability Organization; and Procedures for the Establishment, Approval, and Enforcement of Electric Reliability Standards, Order No. 672, FERC Stats. & Regs. ¶ 31,204 at P 202, order on reh'g, Order No. 672-A, FERC Stats. & Regs. ¶ 31,212 (2006).

<sup>29</sup> 2012 *Business Plan and Budget* at pg 11.

## Background

WECC regional criteria were requirements developed through the standards development process and approved by the WECC Board. However, unlike new Reliability Standards and revisions to existing Reliability Standards, regional criteria were not reviewed or approved by NERC or the Commission. Regional criteria had multiple purposes. For example, some regional criteria were intended to enable entities to comply with mandatory NERC “Fill-in-the-Blank Standards” while other criteria were designed to establish consistency in business practices among WECC member entities.<sup>30</sup> Regional criteria were developed, adopted, and modified under WECC Reliability Standards development procedures. WECC implemented 25 regional criteria, effective during audit staff’s review, and implemented another eight that were effective during a part of the audit period but which had since been retired. Audit staff reviewed these criteria and found WECC had not demonstrated that they all related to development and enforcement of Reliability Standards, or monitoring BPS reliability and adequacy, as audit staff believes is required for funding under section 215 absent explicit Commission authorization. However, during the course of the audit WECC had begun to review and evaluate its regional criteria for potential reclassification.

Audit staff’s review of regional criteria determined that they related to categories that were not specifically tied to reliability. For example, WECC previously defined regional criteria as, “A WECC Board approved document whose purpose is to establish consistency among WECC member entities with respect to business practices, technical procedures, documentation procedures or administrative procedures.” WECC had included a brief description of regional criteria under the statutory section of its budget, but had not provided strong linkage to the section 215 statutory guidance.

In light of Commission guidance on section 215 funding in Order No. 672, audit staff sought to review WECC’s demonstration that each and every regional criterion should be appropriately considered as a statutory activity. Audit staff’s concerns were increased when WECC stated that it has no written policies, processes, procedures, or internal guidance for parameters to consider as a basis for determining whether a proposed or ongoing activity should be considered statutory or nonstatutory.

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<sup>30</sup> “Fill-in-the-blank standards” require a registered entity to act according to individual criteria enacted by its Regional Entity. Only a small subset of WECC’s regional criteria were developed under these “fill-in-the-blank standards.” *See Mandatory Reliability Standards for the Bulk Power System*, Order No. 693, FERC Stats& Regs. ¶ 31,242, at P 287-303 (2007), *order on reh’g, Mandatory Reliability Standards for the Bulk-Power System*, 120 FERC ¶ 61,053 (Order No. 693-A) (2007) (Order No. 693). The Commission noted that Regional Entities should implement criteria for these fill-in-the-blank standards as a matter of “good utility practice.” (Order No. 693) at p 297.

Despite not having any written policies, processes, procedures or internal guidance regarding the basis upon which to determine whether an activity should be considered statutory, WECC did review its regional criteria to determine whether they were appropriately classified within WECC's Document Categorization Policy, which identifies the purpose, approval process and applicability of the different types of documents that WECC maintains. First, WECC reviewed the other seven REs' use of regional criteria. WECC determined that four other REs did not have regional criteria (RFC, SPP, MRO, and SERC) while three had regional criteria (NPCC, FRCC, and TRE). Audit staff noted that the three REs with regional criteria used nonstatutory funding for regional criteria development that were related to reliability functions.

In March 2011, several months before this audit commenced, the WECC Reliability Policy Issues Committee established the Regional Criteria Working Group (RCWG) to evaluate WECC's regional criteria for possible elimination or reclassification. Among other things, the assessment was intended to make recommendations for the potential elimination of Regional Criteria that did not significantly support reliability functions, and the elevation of other Regional Criteria to Reliability Standards when appropriate. In April 2012, the RCWG posted a white paper for comment outlining recommendations for the future of WECC's regional criteria. In July 2012, the RCWG posted a revised draft of this white paper, and in August 2012 it posted a "final" version for Board consideration.<sup>31</sup> In this white paper, the RCWG proposed guidelines to transition some criteria into Regional Reliability Standards. The guidelines directed that a requirement should be contained in a national or Regional Reliability Standard if the requirement affects system operations (i.e., real or reactive power flows or voltage levels, system frequency, or facility ratings) or if the requirement affected system planning (i.e., establishment of real and reactive system operating limits). The RCWG recommended keeping the category of regional criteria, but limiting them to the set of documents necessary to comply with NERC Fill-in-the-Blank standards or Regional Reliability Standards.

Also, the RCWG recommended the creation of a new document category, WECC regional business practices, to include documents needed for consistency that do not directly impact reliability. Included in the category of WECC regional business practices are the interchange-related (INT) regional criteria. However, the white paper recommending the reclassification of regional criteria to regional business practices did not take into consideration how to fund business practices not directly impacting reliability. Finally, the RCWG recommended that seven WECC regional criteria have Standard Authorization Requests drafted to evaluate reclassification. The WECC Board approved the RCWG recommendations during its annual meeting in September 2012.

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<sup>31</sup> WECC Regional Criteria White Paper, (Aug. 8, 2012)(on file with author), available at [www.wecc.biz/committees/BOD/20120905/Lists/Minutes/1/06d%20Regional%20Criteria%20White%20Paper%20120820.pdf](http://www.wecc.biz/committees/BOD/20120905/Lists/Minutes/1/06d%20Regional%20Criteria%20White%20Paper%20120820.pdf).



WECC's reclassification resulted in regional criteria consisting of activities, including only those associated with NERC fill-in-the-blank standards or under evaluation for promotion to a Regional Reliability Standard, which clearly should be funded under section 215. However, audit staff believes that the determination of the continued inclusion of activities which are primarily regional business practices as statutory should be made more transparent in the budget process and subject to approval by means of this process.

Audit staff believes WECC's efforts to review regional criteria for potential reclassification were a positive step toward ensuring only those activities that WECC demonstrates as statutory were funded and undertaken. Audit staff also believes that more broadly written criteria governing which WECC activities should be funded under section 215 would be beneficial so, in the future, WECC can better determine whether an activity is statutory before including it in the statutory section of its budget and funding under section 215, or before undertaking the activity between budget approval periods.

### **Recommendations**

Audit staff recommends that WECC:

14. Adopt written criteria for evaluating whether activities should be funded under section 215; and
15. As part of the next budget review process, provide detail surrounding WECC's regional business practice activities sufficient to ensure transparency to those responsible for evaluating the appropriateness of funding these activities under section 215.

## V. Other Matter

### 8. Payment of Penalties Incurred by WECC's Registered Functions

WECC performed two NERC-registered functions on behalf of all the loads in the Western Interconnection. As the Reliability Coordinator (RC), WECC incurred compliance penalties in its role as a registered entity. To pay for the penalties it incurred, WECC used monies it received through the assessment of penalties to U.S. registered entities in its role as the RE for the Western Interconnection. Whether this process complies with provisions in WECC's Delegation Agreement regarding the distribution of penalty monies as a general offset to WECC's budget requirements for U.S.-related activities is unclear.

#### Pertinent Guidance

WECC's Delegation Agreement, Exhibit E – Funding, section 5, Application of Penalties, states in part:

Except as otherwise approved by the Commission, all penalty monies received by WECC, other than penalty monies received from an operational function or division or affiliated entity of WECC, shall be applied as a general offset to WECC's budget requirements for U.S.-related activities under this Agreement for a subsequent fiscal year.

WECC's Delegation Agreement, Exhibit E – Funding, section 7, Amended or Supplemental Business Plans and Budgets, states in part:

During the course of the fiscal year, if WECC determines it does not or will not have sufficient funds to carry out its delegated functions and related activities, WECC shall submit to NERC one or more proposed amended or supplemental business plans and budgets and requests for approval of supplemental assessments, reflecting costs, cost increases or funding shortfalls not provided for in WECC's approved business plan and budget for the fiscal year. NERC shall review and approve the proposed amended or supplemental business plan and budget and proposed supplemental assessment, or shall direct WECC to make such revisions as NERC deems appropriate prior to approval. NERC shall submit WECC's approved amended or supplemental business plan and budget and proposed supplemental assessment to the Commission for approval.

WECC's Delegation Agreement, section 9, Funding, states in part:

(b) WECC and NERC agree that the portion of WECC's approved budget for the functions and activities described in Sections 5, 6 and 7 and listed on Exhibit E that is to be funded by assessments, will be equitably allocated among end users within the geographic boundaries described in Exhibit A and recovered through a formula based on Net Energy for Load, or through such other formula as is proposed by WECC and approved by NERC and the Commission.

## **Background**

As the RE responsible for implementing the CMEP for the Western Interconnection, WECC had the authority to assess and collect penalties from registered entities for violations of Reliability Standards. Under WECC's Delegation Agreement, it is to use all such penalty monies as a general offset to its budget requirements for U.S.-related activities.

WECC itself performed two registered functions: the Reliability Coordinator (RC) and Interchange Authority (IA) functions, on behalf of all the loads in the Western Interconnection. By registering for these functions WECC could have been (and in fact has been) required to pay civil penalties resulting from alleged violations of Reliability Standards applicable to the functions for which it is registered. During the course of the audit, WECC explained to audit staff that it would pay any civil penalty incurred by its registered functions with funds received from the imposition of civil penalties on U.S. registered entities in its role as RE. Audit staff believes WECC's methodology of using civil penalties collected from U.S. entities for the specific purpose of paying penalties related to its registered functions may not align with the provision in WECC's Delegation Agreement that these penalty monies should be used as a general offset to the budget requirements for U.S.-related activities. This is because, in audit staff's view, the WECC registered functions against which the penalties were assessed were performed grid-wide, and were not limited to U.S.-related activities.

In addition, WECC stated that only if the amount of a civil penalty levied against WECC were to be greater than the amount of penalties it had collected from U.S. registered entities, would WECC initiate a special assessment under its section 215 authority to recoup the difference from U.S. loads. Exhibit E of WECC's Delegation Agreement outlines the process for WECC to submit to NERC a request for approval of supplemental assessments. Audit staff noted that Exhibit E does not outline a process for requesting a special assessment to be levied by WECC on any basis other than on an interconnection-wide Net Energy for Load (NEL) basis.

To date, there have been two civil penalties imposed upon WECC as the RC for the Western Interconnection. In Docket No. IN11-1-000, the Commission approved a stipulation and consent agreement in which WECC settled alleged violations of NERC Reliability Standards during a power system event in 2008 by the Pacific Northwest Security Coordinator, an RC for which WECC provided funding and established policies in 2008.<sup>32</sup> Under the agreement, which the Commission approved on July 7, 2011, WECC agreed to pay a total of \$350,000 in penalties, half to NERC and half to the U.S. Treasury.<sup>33</sup> WECC agreed to make the payments by July 17, 2011. WECC also agreed to pay \$100,000 in penalties to NERC with respect to a Notice of Penalty, Docket No. NP11-259-000, that NERC filed with the Commission on August 11, 2011. In this Notice of Penalty, WECC settled alleged violations of Reliability Standards by the Rocky Mountain Desert Southwest RC and the California Mexico RC. WECC's payment to NERC was due by September 29, 2011.<sup>34</sup>

WECC's Delegation Agreement says that penalty monies it collects as the RE "shall be applied as a general offset to WECC's budget requirements for U.S.-related activities." The Delegation Agreement does not explain how WECC should handle instances where its registered functions incur a compliance penalty. Although not explicitly addressed in WECC's Delegation Agreement, a portion of WECC's methodology for paying RC civil penalties was included in WECC's 2012 Business Plan and Budget as follows<sup>35</sup>:

In this budget, and in subsequent budgets as necessary, WECC proposes using penalty monies collected from U.S. registered entities within the Western Interconnection to pay compliance penalties incurred by the WECC registered functions as a result of alleged non-compliance with NERC mandatory reliability standards or WECC regional reliability standards. This will ensure that only U.S. entities contribute to the payment of WECC registered function penalties paid to NERC and/or FERC under Section 215 of the Federal Power Act.<sup>36</sup>

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<sup>32</sup> WECC previously provided funding and established policies for three RCs in the Western Interconnection: the Pacific Northwest RC, the Rocky Mountain Desert Southwest RC, and the California Mexico RC. WECC consolidated these three RCs into one entity and assumed responsibility for their operation in 2009.

<sup>33</sup> *Western Electricity Coordinating Council*, 136 FERC ¶ 61,020 (2011).

<sup>34</sup> NP11-259-000 Notice of Penalty at 13. The Commission issued a notice on September 9, 2011 that it would not further review this Notice of Penalty, 136 FERC ¶ 61,168 (2011).

<sup>35</sup> Audit staff notes that the intention to levy a special assessment on only U.S. registered entities was not included in this filing.

<sup>36</sup> *WECC 2012 Business Plan and Budget* at 63 (filed with the Commission on August 24, 2011 in Docket No. RR11-7-000).

The 2012 WECC Business Plan and Budget also shows a proposed \$450,000 deduction from penalties received from registered entities on or before June 30, 2011 “to pay compliance penalties incurred by the WECC registered functions as a result of alleged non-compliance with NERC mandatory Reliability Standards or WECC Regional Reliability Standards.”<sup>37</sup> The filing does not make it clear that the two penalties in question had already been incurred, and that WECC had already agreed to make penalty payments by July 17, 2011 and September 29, 2011, as discussed above. The Commission accepted WECC’s 2012 Business Plan and Budget, along with those of all other Regional Entities and of NERC, but did not address WECC’s proposal in its order.<sup>38</sup>

Audit staff noted that timing of WECC’s payment of these penalties was not outlined in its Business Plan and Budget for 2012. Although the penalties had already been paid by the time WECC submitted its business plan and budget for review, WECC did not clearly spell this out. WECC should ensure that in future budget filings it clearly discloses when it will pay penalties assessed against its registered functions, and with what funds. Further, the Commission has not yet addressed whether the manner in which WECC used penalty monies collected from U.S. registered entities within the Western Interconnection to pay compliance penalties incurred by the WECC registered functions was consistent with WECC’s obligation to use penalty monies as a general offset to WECC’s budget requirements for U.S.-related activities for a subsequent fiscal year.

Accordingly, audit staff believes WECC should make a filing with the Commission to determine the appropriate manner in which to pay penalties assessed to WECC’s registered functions. In this filing WECC should request clarity on the use of monies the WECC RE received through the assessment of penalties to U.S. registered entities, as well as the proper manner in which to allocate any penalties by means of a special assessment.

## Recommendation

Audit staff recommends that WECC:

16. Make a separate filing, or include language in a currently planned filing such as the 2014 ERO budget filing or a filing regarding the separation of the WECC RE and WECC’s registered functions, explicitly seeking Commission approval for WECC’s method of paying compliance penalties incurred in its roles as a registered entity. Also, in this filing WECC should explain its

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<sup>37</sup> *Id.* at 64.

<sup>38</sup> *North American Electric Reliability Corp.*, 137 FERC ¶ 61,071 at P 18-19 (2011) (2012 Budget Order).

proposed method for requesting a special assessment for paying penalties when it does not have sufficient funds.

## Appendix



Steven F. Goodwill  
Vice President and General Counsel

801-883-6857  
sgoodwill@wecc.biz

June 28, 2013

***Sent via electronic mail and FedEx overnight delivery***

Bryan K. Craig  
Director and Chief Accountant  
Division of Audits  
Office of Enforcement  
Federal Energy Regulatory Commission  
888 First Street, NE, Room 5K-13  
Washington, D.C. 20426

**RE: PA12-09-000 WECC Comments to FERC Audit Report**

Dear Mr. Craig:

The Western Electricity Coordinating Council ("WECC") provides the following response to the May 22, 2013 Draft Audit Report as revised June 20, 2013 ("Draft Report") of the Division of Audits of the Federal Energy Regulatory Commission's ("FERC" or "the Commission") Office of Enforcement ("Audit Staff") related to WECC's responsibilities and budgeting practices as the Regional Entity for the Western Interconnection.

WECC appreciates the professionalism, thoroughness, and cooperative spirit of the Audit Staff throughout the course of FERC's Audit of WECC. As discussed further herein, WECC accepts all of the recommendations in the Draft Report. In addition, WECC believes that actions it has undertaken addressing some of the recommendations are already enhancing WECC's operations, and that those actions, in conjunction with future actions to fulfill the balance of the recommendations, will continue to do so.

### **I. SUMMARY OF WECC'S RESPONSE**

WECC generally accepts all of the facts, conclusions, and recommendations in the report. However, WECC herein provides clarification for the following three items: (1) Recommendation 11; (2) the facts and conclusions related to Recommendations 14 and 15; and (3) the facts and conclusions related to Recommendation 16.



## II. WECC'S RESPONSE TO DRAFT REPORT FACTS, CONCLUSIONS, AND RECOMMENDATIONS

The Draft Report includes facts, conclusions, and recommendations related to Mitigation Plan Processing, Enforcement Caseload, Conflict of Interest Disclosure Form Completion, Budget Development, Employee Expense Reimbursement Policy and Controls, Investments, Funding of Regional Criteria under Section 215, and Payment of Penalties Incurred by WECC's Registered Functions. WECC's response to each of these categories is discussed more fully below.

### a. Mitigation Plan Processing, Enforcement Caseload, and Conflict of Interest Disclosure Form Completion

WECC accepts the facts, conclusions, and recommendations related to Mitigation Plan Processing, Enforcement Caseload, and Conflict of Interest Disclosure Form Completion. WECC has already taken actions to fulfill Recommendations 1 through 6 associated with Mitigation Plan Processing and Enforcement Caseload. WECC has taken certain actions and is in the process of taking other actions to fulfill Recommendation 7 related to Conflict of Interest Disclosure Form Completion.

### b. Budget Development and Employee Expense Reimbursement Policy and Controls

WECC accepts the facts, conclusions, and recommendations related to Budget Development and Employee Expense Reimbursement Policy and Controls. WECC is in the process of taking certain actions and is currently planning other actions to fulfill Recommendations 8 through 10 associated with Budget Development and Employee Expense Reimbursement Policy and Controls.

### c. Investments

WECC accepts the facts and conclusions related to Investments. WECC also accepts Recommendations 12 and 13. WECC accepts Recommendation 11 based on Audit Staff's subsequent clarification regarding the focus of their concerns related to WECC's Investment Policy, as set forth below.

***Recommendation 11: Work with NERC to adopt restrictions on investments in registered entities to ensure the appearance of conflicts of interest does not occur.***

WECC discussed possible means of strict compliance with Recommendation 11 with its investment managers. Subsequently, WECC raised the concern to Audit Staff that strict compliance with the recommendation could prove administratively infeasible. WECC agrees





that any actual or apparent conflicts of interest should be avoided to the extent WECC can ensure such avoidance, and to the extent that WECC may be aware of such holdings. However, given the fluid nature of mutual funds and the holdings of various companies, it may be administratively impossible to know with absolute certainty that no fraction of a percent of a Registered Entity's stock is ever held by WECC indirectly.

WECC discussed these concerns with Audit Staff and proposed to limit direct investments in Registered Entities through the prohibition of investments in commercial paper and corporate notes. Audit Staff clarified that the main area of Audit Staff concern was direct investment in Registered Entities. Further, after Audit Staff discussions with the North American Electric Reliability Corporation ("NERC"), Audit Staff indicated that the specifics of how WECC should appropriately revise its Investment Policy to address its conflict of interest concerns would be best addressed through WECC working with NERC. WECC appreciates the clarification from Audit Staff and looks forward to working collaboratively with NERC to ensure that appropriate restrictions are included in WECC's Investment Policy.

#### **d. Funding of Regional Criteria under Section 215**

WECC accepts the facts and conclusions related to the Funding of Regional Criteria under Section 215 with one clarification set forth below related to the purpose of WECC's Regional Criteria Work Group ("RCWG"). WECC accepts Recommendations 14 and 15 and is currently planning actions to fulfill these Recommendations.

With respect to the underlying facts regarding the RCWG, WECC clarifies that the purpose of the RCWG's reclassification effort was to analyze whether documents considered Regional Criteria under WECC's Document Categorization Policy were appropriately categorized as Regional Criteria, whether they should be elevated to Regional Reliability Standards, or whether they should be reclassified as Regional Business Practices or to another category within the Document Categorization Policy.<sup>1</sup>

<sup>1</sup> "The purposes of the RCWG are to (1) make recommendations to RPIC for possible recommendation to the WECC Board for the elimination of Regional Criteria that are no longer necessary to support reliability or needed for regional consistency, (2) make recommendations to RPIC for possible recommendation to the WECC Board for the conversion of Regional Criteria to enforceable Reliability Standards when it appears either that consistency, or anticipated level of consistency, of action by WECC members is not sufficient to support reliability. (3) maintain a current list of Regional Criteria that have been adopted (approved?) by the WECC Board for the purpose of supporting and enhancing reliability through anticipated consistency of action by WECC members, and (4) develop procedures that are as minimally burdensome of WECC members as possible for determining the extent to which the requirements of each such Regional Criterion are being adhered to." RCWG Charter (March 16, 2011) <http://www.wecc.biz/library/Documentation%20Categorization%20Files/Policies/Document%20Categorization%20Policy.pdf>.



#### e. Payment of Penalties Incurred by WECC's Registered Functions

WECC generally accepts the facts and conclusions related to the Payment of Penalties Incurred by WECC's Registered Functions with the clarifications set forth below regarding WECC's 2012 Business Plan and Budget, and the discussion of penalty monies therein. WECC accepts Recommendation 16 and is currently planning actions to fulfill the recommendation.

WECC began the multi-step process of formulating its proposed 2012 Business Plan and Budget in January 2011. This process includes public posting and discussion in various open meetings, and WECC's development process ends with the approval of the Business Plan and Budget by WECC's Board of Directors ("Board"). In 2011, the Board approved the proposed WECC 2012 Business Plan and Budget on June 22, 2011.

As discussed in the Draft Report, the Order Approving Stipulation and Consent Agreement regarding a system disturbance on February 14, 2008 was not issued by the Commission until July 7, 2011,<sup>2</sup> and the Abbreviated Notice of Penalty regarding system disturbances on November 7, 2008 and December 26, 2008 was not filed by NERC with the Commission until August 11, 2011.<sup>3</sup>

Thus, at the time the Board approved WECC's proposed 2012 Business Plan and Budget, the enforcement actions underway regarding WECC's Reliability Coordinator function were confidential and non-public. WECC did not know with certainty when those actions would come to a conclusion, or when specifically WECC's agreed upon penalty payments would come due.

WECC agrees with Audit Staff's conclusion that WECC should be transparent regarding penalties in its Business Plan and Budget. In this instance, given the public nature of portions of the budget preparation process, the timing of the approval of the 2012 WECC Business Plan and Budget, and the confidential and non-public nature of the pending enforcement action, WECC did not believe it was possible to be more transparent than the descriptions and information WECC did include in its proposed 2012 Business Plan and Budget. Further, WECC understands, that as a part of transparency, Audit Staff indicates concern that the timing of the payment of penalties was not included in WECC's proposed 2012 Business Plan and Budget. However, given the timing as clarified herein, WECC did not know with certainty when the payments would come due during the Business Plan and Budget development process.

<sup>2</sup> *Western Electricity Coordinating Council*, 136 FERC ¶ 61,020 (2011).

<sup>3</sup> *NERC Abbreviated Notice of Penalty regarding Western Electricity Coordinating Council*, Docket No. NP11-259-000 (Aug. 11, 2011); *North American Electric Reliability Corporation*, 136 FERC ¶ 61,168 (Sept. 9, 2011) (stating that the Commission would not further review, on its own motion, the Notice of Penalty).



Finally, the reason that WECC discussed its approach to payment of penalties in the 2012 Business Plan and Budget was because WECC was using penalty monies collected between July 1, 2010 and June 30, 2011. Pursuant to NERC's Policy<sup>4</sup> related to usage of penalty monies, those monies were then relevant to the assessments to U.S. entities in 2012, and thus WECC's usage of a portion of those monies was appropriately discussed in its 2012 Business Plan and Budget.

### III. CONCLUSION

WECC reiterates its appreciation of Audit Staff's professionalism throughout the course of the Audit, and looks forward to working with Audit Staff and NERC in fulfilling the recommendations contained in the Draft Report.

If you have any questions regarding WECC's comments, please do not hesitate to contact me ((801) 883-6857 or [sgoodwill@wecc.biz](mailto:sgoodwill@wecc.biz)), or WECC Senior Legal Counsel Heather Ebert ((360) 567-4069 or [hebert@wecc.biz](mailto:hebert@wecc.biz)).

Sincerely,

A handwritten signature in black ink, appearing to read "SFG", is written over a horizontal line.

Steven F. Goodwill  
Vice President and General Counsel

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*NERC Policy: Accounting, Financial Statement, and Budgetary Treatment of Penalties Imposed and Received for Violations of Reliability Standards.*

WESTERN ELECTRICITY COORDINATING COUNCIL • WWW.WECC.BIZ  
155 NORTH 400 WEST • SUITE 200 • SALT LAKE CITY • UTAH • 84103-1114 • PH 801.582.0353 • FX 801.582.3918

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