July 15, 2015

NERC Business Plan & Budget – Draft 1
Management Response to Comments Received
by CEA, IESO, and EEI

1. Canadian Electricity Association

a. *Risk-Based Strategies*

i. The development and implementation of risk-based strategies has and is expected to continue to produce efficiencies within NERC and the Regional Entity operations that will mitigate the need for additional resource additions to support emerging reliability needs and enhance the ERO's ability to stabilize assessment increases. For example, as noted in NERC's draft business plan and budget, the reduction in legal and enforcement headcount allowed NERC to reallocate open budgeted resources to support emerging reliability assessment needs[1], as well as provide greater resource support to the ES-ISAC, the need for which has been strongly supported by industry. This resource allocation was all accomplished without increasing NERC's overall FTE budget. In fact, without risk-based strategies, additional resource additions would likely be required.

ii. In addition to providing efficiencies supporting resource allocation needs, risk-based strategies also reinforce and support the common ERO and industry objective of focusing on the most important factors affecting reliability and mitigating unnecessary costs to registered entities while maximizing the efficiency and effectiveness of NERC and RE resources.

b. *Proposed Budget and Assessment Increases*

Further details regarding the allocation of assessments between the U.S., Canada and Mexico is outlined in the final draft of NERC's business plan and budget and accompanying presentation materials for the July 22, 2015 webinar. As further detailed in the cover memo accompanying the posting of the revised draft of NERC's business plan and budget, the net effect of the revisions to NERC's proposed 2016 budget is a total increase of $537k

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[1] For a further discussion of these needs please refer to Section A of NERC's business plan and budget under the Reliability Assessment and Performance Analysis department.

over 2015. This represents a year-over-year increase of less than 1% and a decrease of $1.6M (2.3%) from the initial draft. After taking into account preliminary projections of credits to certain Canadian entities pursuant to NERC's Expanded Policy on Allocation of Certain Compliance and Enforcement Costs, the total NERC Canadian assessment will increase by $35,993 (less than 1%) over the 2015 assessment. In addition, 2016 NERC assessments for the IESO and New Brunswick are projected to decrease below 2015 levels.

c. *General and Administrative Department Increase*

   i. The increase in the General and Administrative (G&A) department budget is more a reflection of how NERC's organizational structure has historically been budgeted, and not necessarily about common overhead functions and costs. NERC's G&A includes normal departments you typically see in overhead – accounting, finance, human resources, etc. However, it also includes the Executive, Legal, and IT departments as well as NERC's Chief Reliability Officer (CRO)[2] and support staff for all of those. The Executive, Legal, and IT departments, as well as NERC's CRO, are extensively involved in NERC's day to day operations.

   ii. The company recently put in place a time accounting and cost allocation system that tracks time and allocates costs by activity. With this new system the company can now compare the time, resources and costs to support various major activities to how the company budgets. For example, time and associated costs incurred by standards department personnel, attorneys and other personnel on various standards activities can now be grouped and compared to the traditional departmental budget categories. In general and as expected, preliminary reports show total general and administrative costs running lower than what's reflected in the G&A budget based on work actually being performed by personnel within the G&A departments. Management has been refining activity code descriptions and groupings, as well as training personnel on the appropriate activity codes to record their time. Summary information from these reports will be made available to stakeholders as part of the 2017 business planning cycle.

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[2] The CRO has oversight of most operating departments within NERC

    d. ES-ISAC

        i. Senior management is committed to assessing the ability to reallocate resources internally prior to seeking incremental increases in a department's budget or NERC's overall budget. This was clearly the case during 2015 in connection with the re-allocation of existing resources to emerging resources needs in the security (ES-ISAC), reliability assessment (RAPA) and compliance assurance areas without increasing NERC's overall budget.

       ii. Ensuring adequate funding for the ES-ISAC in the future, including the review of funding needs and mechanisms, will continue to be a priority focus for the company throughout the annual business planning process, with ongoing opportunities for stakeholder consultation and input.

    e. Budget Performance and Format

    NERC will continue to provide historic year over year trending of actual to budgeted and projected costs for key functional areas for both NERC and the Regional Entities. This information has historically been provided in connection with the company's submittal of its final recommended business plan and budget to the NERC Finance and Audit Committee. During the year NERC also provides quarterly and year-end variance reports for both NERC and the Regional Entities.

2. Independent Electricity System Operator

    a. NERC Program Spending

        i. The changing nature of the bulk power system, including changing generation resource, are placing increased demands on the resources required to support the work performed by the RAPA and Event Analysis departments. Further information regarding the work being performed by these departments and priorities for 2016 is contained in the departmental descriptions in Section A of the NERC business plan and budget.

       ii. Management has updated the ES-ISAC section of NERC's business plan and budget, has recently hired a Senior Vice President and Chief Security Officer in charge of the ES-ISAC and has allocated additional personnel

to support ES-ISAC operations. Management is also working diligently to fill open positions within the ES-ISAC.

iii. As further described in the company's response above to the comments of the Canadian Electricity Association, the increase in the G&A department budget is more a function of what NERC includes in G&A and how they have been historically budgeted, and less about a true increase in normal overhead costs.

iv. The Compliance Assurance department increase is primarily due to two factors. First, we transferred auditor positions from the former Critical Infrastructure Department to Compliance Assurance to more closely align audit functions and further separate ES-ISAC operations from NERC's compliance functions. Second, NERC increased the allocation of indirect expenses to this program area based on the increase in departmental FTEs. Indirect costs are allocated among program areas based on the ratios of that department's FTE budget to total budgeted FTEs.

v. The Compliance Enforcement department budget is expected remain relatively flat. Reductions in personnel were generally offset by increases in overall personnel costs which are included in both direct and indirect expenses.

vi. With respect to NERC's investment in a document management system, this investment was discussed and reviewed with the NERC Standards Oversight and Technology Committee (SOTC) and Finance and Audit Committee (FAC) in open session in May 2015. Extensive background documentation was included regarding the justification, cost and benefits, as well as benchmarking costs against other companies[3]. With respect to IT investments in general, as part of the annual business plan and budget development process, management also reviews proposed plans and spending with SOTC in open session, including both short and long term projections.

b. *ERO Programs and Priorities*

i. NERC and Regional Entity management review total and allocated resources requirements and budgets on an ongoing basis to ensure consistency with statutory and delegated responsibilities. While there

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[3] Please also see references under response to comments regarding IT infrastructure investments.

are always opportunities for improvement, considerable efforts are undertaken to review and discuss each Regional Entity's business plan and budget prior to NERC management recommending approval by the NERC Board of Trustees.

ii. While budgets vary considerably among regions based upon the nature and scope of the function they perform, a consistent format was developed for presentation of each entities' business plan and budget in order to facilitate year of over year comparisons.

iii. Each Regional Entity business plan and budget is also subject to review by the Regional Entity board and stakeholders prior to submittal to NERC.

iv. NERC reviews each Regional Entity business plan and budget on a departmental basis. This review includes, but is not limited to, assessing (1) whether departmental resources are adequate to perform their delegated functions, (2) whether departmental and overall activities are aligned with the ERO Enterprise Strategic Plan, (3) the format and content of financial and supporting schedules, (4) compliance with any outstanding regulatory directives or requirements (5) ensuring no overlap between NERC and Regional Entity capital spending, (6) cost control and efficiency initiatives.

v. In connection with the NERC FAC review and recommendation of Board approval of the NERC and Regional Entities' annual business plans and budgets, NERC management provides the FAC with a memorandum summarizing its review of the Regional Entity business plans and budgets, together with supporting materials providing comparisons of year over year budgets by entity and department. This information is posted on NERC's website and publicly available. NERC's annual business plan and budget filing with the FERC also includes various NERC and Regional Entity budget metrics.

vi. NERC and Regional Entity management are committed to continuing to build on these efforts with the goal of further improving the efficiency and effectiveness of ERO Enterprise operations.

c. *IT Infrastructure Investments*

i. NERC has made considerable efforts over the past two years to increase the transparency and information provided to stakeholders regarding IT

capital spending plans and budgets. This information is posted and reviewed publicly as part an open SOTC agenda, prior to finalization of NERC's business plan and budget. The investment in the proposed document management system was subject to extensive review by both the SOTC[4] and FAC[5] at their May 2015 open meetings prior to FAC and Board approval of the use of reserves to initiate this important program in 2015.

ii. Management will continue to make efforts to maintain transparency and provide detail requiring proposed capital spending needs and resource requirements.

d. *Budget Implications of ES-ISAC Strategic Review*

i. Management is not recommending an increase in the 2016 NERC budget or that the current ES-ISAC or CRISP funding model be changed at this time based on the ESCC's findings and recommendations.

ii. Consistent with the evaluation of resource allocation in support of all program area needs and priorities, management will undertake an evaluation of both intra and inter departmental needs, work load and priorities in an effort to mitigate the need for incremental increases in NERC's overall or individual department budgets. Despite these efforts, there is always the possibility that departmental and overall NERC resource requirements and funding needs will increase. In these circumstances management will make every effort to make sure that stakeholders, including registered users of the ES-ISAC, are properly informed regarding the need and have an opportunity to provide input.

e. *Process Improvements*

i. Management will continue to work with the RISC to ensure alignment between RISC and ERO project and program prioritization timelines and NERC's business plan and budget schedule.

ii. A year-end true up report based on audited financial results for both NERC and the Regional Entities is filed with FERC each year on or about May 31st and is publicly available on NERC's website under the page entitled Filings and Orders. NERC and the Regional entities review this

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[4] See Standards Oversight and Technology Committee Agenda Package-May 6, 2015
[5] See Finance and Audit Committee Agenda Package May 6, 2015

information in connection with the development of their budgets for the following year. NERC will include information regarding year-end audited results in future drafts of its business plan and budget.

iii. Management will continue to provide ongoing reporting regarding Enterprise IT Application development projects, benefits, budgets and spending.

iv. Building on the experience gained to date in the development of a number of Enterprise IT applications, management will explore opportunities to further enhance stakeholder engagement in IT capital spending plans and application development.

v. Management will recommend that the Regional Entities consider preparation of an accountability matrix similar to NERC.

3. Edison Electric Institute

a. *Alignment of resources with reliability risks*

NERC will continue to ensure that resources are aligned with reliability risk and advancing consistency in multi-regional registered entity compliance and enforcement.