

Date: March 29, 2016

To: THE GOVERNANCE COMMITTEE

From: VICE PRESIDENT and CHIEF ETHICS & COMPLIANCE OFFICER

Subject: **Ethics and Compliance Program and NERC Reliability Standards Compliance**

ETHICS and COMPLIANCE

SUMMARY

The Office of Ethics and Compliance (“E&C Office”) advises NYPA’s trustees, officers and employees on the legal, regulatory and NYPA Code of Conduct ethics and compliance standards relating to NYPA’s employees and operations. It coordinates the investigation of allegations and concerns involving NYPA’s assets and employees. This report highlights significant developments in NYPA’s ethics and compliance program for the period December 17, 2015 to March 29, 2016.

BACKGROUND

The principal substantive issues arising under the NYS ethics laws and NYPA’s Code of Conduct investigated or researched since the most recent Governance Committee report on December 17, 2015 include various requests to engage in outside activities and employment and issues concerning conflicts of interest, post-employment analyses, policy reviews, gifts inquiries and new hire “reverse two-year-bar” employment restrictions questions.

The E&C Office provides annual training and Code of Conduct Certification to all trustees, officers and employees to reaffirm NYPA’s commitment to prevailing ethics principles and raise awareness of the laws and regulations with which all NYS public employees are required to comply. Annual review of and certification to the NYPA Code of Conduct is implemented as an additional measure to reinforce acceptable business and professional conduct. The E&C Office also coordinates required training for designated employees to comply with the Federal Energy Regulatory Commission’s (“FERC”) Standards of Conduct relating to transmission and energy marketing functions and FERC Rules designed to prevent manipulation of energy markets.

DISCUSSION

Ethics Caseload

The E&C Office reviewed 66 cases since the last report to the Governance Committee and handled 220 inquiries in calendar year 2015. The case totals for 2015 included the following categories: appearances of impropriety; conflicts of interest; gifts questions; outside activities and outside employment reviews; re-employment assessments for retirees; post-employment questions, issues related to unwarranted privileges and evaluations involving appropriate use of NYPA assets. These cases originated from all NYPA headquarters and operating facilities, with a concentration from the White Plains Office. Ethics inquiries were made by various trustees, officers, bargaining unit and salaried employees. The widespread and consistent outreach from all NYPA locations and employee classifications is a strong indicator of the E&C Office's employee engagement efforts. In addition, employees are comfortable engaging the E&C Office in open dialogue and receive comprehensive feedback to their concerns or inquiries.

Selected Cases

Outside employment reviews and approvals since the last report to the Governance Committee included ownership of a remote answering service for doctors' offices and taxi services, two village Trustee positions, a National Guardsman, travel agency ownership, two engineering consulting businesses, an adjunct professor at New York University, a wood carving business and a private electrical business. All were approved with guidelines employees must follow to avoid conflicts of interest and appearances of impropriety. As required by NYS regulations, the E&C Office coordinated the approval of the NYS Joint Commission on Public Ethics (JCOPE) for outside employment sought by employees holding designated policy-making positions.

Uncompensated outside activities reviewed and approved included a senior executive and an entry level associate engineer who were recruited to offer industry advice to three colleges developing curriculum related to the energy industry and several requests to review membership in external professional organizations which may have a nexus to NYPA's business. As with compensated outside employment scenarios, these outside activities were also approved with guidelines to assist employees in avoiding any conflicts of interest or other violations of the NYS Public Officers Law and NYPA Code of Conduct.

The E & C Office also provided guidance to two employees recently hired from NYPA business partners. These and other employees are subject to the "reverse two year bar," which restricts newly hired State employees from conducting business with their former private sector employers. The rationale for this restriction is to prevent the appearance that newly hired State employees may either give preferential treatment to or be unduly influenced by their former private sector employers. Both employees were interviewed and provided guidance directing them that they may not engage in NYPA business related discussions or transactions with their former employers for a period of two years from their date of hire.

Internal Collaboration

The E & C Office has been increasingly asked to participate in functional reviews of existing policies and the development of new policies or procedures for the organization. It collaborates with the Business Controls Group and is a member of the Corporate Policy Review Committee. The E & C Office provided analyses and drafted governance documents on issues related to onboarding of new hire employees, knowledge management through the Powernet's Communities of Practice and Interest, updated motor vehicle, patent, staff augmentation, overtime meals, tuition reimbursement and securities trading and confidential information policies. It also advised Customer Energy Solutions and Corporate Communications on appropriate business card branding for the newly created NY Energy Manager positions, which are staffed by agency contractors who represent NYPA in the implementation of energy services programs to state agencies.

This heightened sensitivity of the need to include ethics and compliance reviews prior to adopting new or updated policies and procedures indicates that NYPA's internal ethical culture is becoming more robust and embedded throughout all levels of the organization.

In addition, the E & C Office has been asked to work with the Internal Audit Department as it develops the scope and implementation plans for the quarterly audits and assessments. We will provide historical case data applicable to the subject areas and update the auditors on corrective actions which have been implemented to enhance internal controls. Data provided may include information related to the proffering or disclosing of gifts with business partners, questions surrounding unwarranted privilege requests like endorsements and references to Project Sunlight submissions. While this collaboration is developing, leveraging the historical information maintained by the E & C Office will provide Internal Audit the benefit of increased knowledge to assess fraud potential and give the E & C Office an opportunity to embed an ethics review into each audit conducted.

Collaboration with the New York State Inspector General's Office and Other External Agencies

NYPA continues to collaborate with the NYS Inspector General's Office and other external agencies in providing requested documentation or information related to ongoing investigations with those agencies. NYPA received one complaint referral from the Inspector General during this reporting period involving an employee's claim that NYPA did not properly process her sick leave related to a workers compensation workplace injury. The E&C Office coordinated an investigation of the complaint which was found to be unsubstantiated as NYPA provided all required information to the applicable external parties and is processing the employee's workers compensation claim in accordance with established protocols.

Training and Outreach

The E & C Office provides annual training to all employees. The training is delivered either via live, in-person sessions or electronically as a computer based program. In calendar year 2015, NYPA's Video Production Services Department produced a video containing training content focused on the NYS and NYPA Code of Conduct restrictions on outside activities and employment applicable to NYPA's employees. The video consisted of an edited portion of a prior presentation of the JCOPE Comprehensive Ethics Training course. This video was

delivered to employees via the Learning Management System and was well-received by staff both for its relevant content and efficiency in time management.

The E & C Office continued to provide the two-hour JCOPE Comprehensive Ethics Training Course (“CETC”) throughout calendar year 2015 to fulfill its mandate to educate all Trustees and employees who participate in the JCOPE Financial Disclosure program. The statutorily mandated Compliance Training Report was submitted to JCOPE on January 29, 2016, detailing those employees who received the required training in calendar year 2015.

The Public Integrity Reform Act of 2011 (“PIRA”) requires follow up training of those employees who have already completed the JCOPE’s CETC within three years of original certification. This second JCOPE training is under development and is approximately 90 minutes. It is expected to be delivered to all NYPA employees as NYPA’s annual training for calendar year 2016. This training is expected to be delivered in the third and fourth quarters of 2016, after receiving the training materials from JCOPE.

The E & C Office will be delivering a targeted survey to members of the Compliance Work Group to assess the effectiveness of the Ethics and Compliance programs. Results of the survey will be used to evaluate the responsiveness to inquiries and requests to collaborate, and to improve internal processes and procedures to help better serve our customers.

Financial Disclosure

As required by the Public Officers Law, NYPA completed and submitted its annual Financial Disclosure filer documents to JCOPE in February. All employees whose base salaries exceed \$91,821, exclusive of overtime or other benefits, or are designated as serving in ‘policy-making positions’ are required participants in the program.

Currently, there are 844 eligible participants in the Financial Disclosure program. 256 of the required participants have been granted either individual or title exemptions by JCOPE and are not required to submit an annual Financial Disclosure Statement. 167 of the remaining 588 participating employees have been designated as policy makers and may not apply for an exemption from the program.

JCOPE has implemented a new filing system for Financial Disclosure which will be housed on the NYS Office of General Services sponsored NY.GOV Online Services website. This website provides access to a number of statewide programs including the State’s Learning Management System (“LMS”). Executive branch employees automatically obtain accounts shortly after their date of hire. NYPA employees and Trustees are not enrolled in this system upon their hire, so we anticipate JCOPE’s guidance and assistance in registering NYPA employees in this statewide database and advising filers how to complete their statutory requirement. Employees who have transferred service from another state agency may already have accounts established in the NY.GOV Online Services website.

The E & C Office is collaborating with JCOPE and will work with all affected staff to ensure that they have access to electronically file their Financial Disclosure Statements in a timely manner. The annual deadline for filing is May 15. Should any issues arise with the electronic filing system, employees have the option to file a hard copy form.

“Project Sunlight”

Project Sunlight is a database maintained by the NYS Office of General Services to promote transparency and which allows members of the public access to information concerning meetings (“covered appearances”) between NYPA representatives and external parties under five qualifying categories, including procurement, rate-making and rule-making matters. NYPA submitted 248 appearances in calendar year 2013 (the first year of implementation), 167 entries in calendar year 2014 and 203 occurrences in 2015. The E&C Office maintains the Project Sunlight policy, frequently asked questions and internal reporting form on the NYPA PowerNet and conducts targeted business unit group training to reaffirm compliance with this statewide initiative.

RELIABILITY STANDARDS COMPLIANCE

SUMMARY

This report highlights important aspects of NYPA’s reliability standards compliance management program for the period December 18, 2015 to March 8, 2016. A brief background statement is followed by discussion of specific reliability standards-related topics affecting the enterprise.

BACKGROUND

Background information related to the origin of the North American Electric Reliability Corporation (NERC) mandatory standards for reliability and NYPA’s obligations to demonstrate compliance with the standards has been presented in previous reports to the Governance Committee.

DISCUSSION

NERC Reliability Standards Compliance Enforcement Actions

During the reporting period, there were no new possible violations of the NERC Reliability Standards reported to the Northeast Power Coordinating Council (NPCC).

Investigations of Possible Violations

During the reporting period, Technical Compliance initiated three (3) investigations of possible violations of the NERC Reliability Standards. The investigation teams determined that there were no possible violations of Reliability Standards associated with two (2) incidents; the remaining investigation is on-going. This internal process is viewed by the regulator as evidence that NYPA has a strong internal compliance program.

Risk-Based Evidence Management Program

Effective in late 2015, NPCC revamped the self-certification process to a risk-based model. The new process is referred to as the Guided Self-Certification program. This program will be administered to entities in the NPCC region in lieu of the previous annual self-certification program. In response, Technical Compliance has implemented a Risk-Based Evidence

Management Program for identifying areas of risk and appropriate frequency for compliance evidence updates and evaluation for the NERC Reliability Standards applicable to NYPA. This process ensures that NYPA's compliance program is in-line with NERC's risk-based Compliance Monitoring and Enforcement Program and the NPCC guided self-certification process. RSC has identified fifty-three (53) NERC Reliability Standards whose evidence will be reviewed and updated in 2016.

Guided Self-Certification of Compliance

NYPA was not required to self-certify compliance for any of the NERC Reliability Standards applicable to NYPA during this reporting period. Technical Compliance has established a rigorous process to ensure that compliance evidence is updated before NYPA self-certifies compliance.

NERC Risk-Based Compliance Monitoring and Enforcement Program

In January, NYPA and NPCC held a conference call to review and discuss the draft NYPA Internal Controls Evaluation (ICE) report. Based on this conference call, Technical Compliance submitted additional internal controls information regarding *EOP-004-2- Event Reporting* for NPCC to evaluate with the intent of further reducing NYPA's future Operations and Planning Standards audit scope. NPCC plans on finalizing the draft NYPA ICE report in March/April 2016 with a follow up site visit tentatively planned for July 2016. Based on the draft results of NPCC's evaluation of NYPA's internal controls, the scope of the 2017 Operations and Planning Standards audit may be reduced by over 90%.

Technical Compliance continues to work on developing internal control process flow diagrams for the NYPA core and standard-specific controls for NPCC's ICE. It is anticipated that draft ICE process flow diagrams for the standard-specific controls will be complete in April 2016.

Bulk Electric System (BES) Definition

As stated in earlier reports, the Federal Energy Regulatory Commission (FERC) approved the new Bulk Electric System (BES) definition and that NYPA has identified over 50 new BES elements that will be subject to the NERC reliability standards in July 2016. The new definition applies essentially to any transmission assets operated at or above 100 kV.

During the reporting period, NYPA continued to participate in meetings with the New York State Independent System Operator ("NYISO") and the other NY Transmission Owners to assess new state-wide functional registration and compliance management impacts and actions pursuant to the new BES definition.

During the reporting period, NYPA continued to engage the NYISO in discussions regarding NYPA's request of the NYISO to add some of NYPA's newly identified BES elements to its list of controlled assets for Transmission Operator (TOP) compliance purposes. NYPA took a position that since it does not operate most of its newly identified BES assets, in a NERC functional model sense, that it will not be registered as a TOP. On March 3, 2016, after nearly three (3) years of attending meetings and negotiations with the NYISO and the other NY Transmission Owners, the Coordinated Functional Registration (CFR) Agreement for

management of the Transmission Operator and Transmission Planner functions for the new BES assets in New York that are now subject to the NERC Reliability Standards was signed.

The only obligation NYPA has under the agreement, since NYPA will not be a registered Transmission Operator, is to ensure that the Energy Control Center system operators are NERC certified; they currently are required to have this certification under a NYPA internal control. In addition most of the Transmission Planner compliance obligations for NYPA's new BES assets were assigned to the NYISO. However, NYPA did need to register as a Transmission Planner for a few of the Transmission Planner requirements that are applicable to its assets. NYPA and the NYISO are executing a separate MOU that clarifies the Transmission Planner responsibilities between NYPA and the NYISO. This agreement will be finalized before July 2016.

With these agreements, NYPA has avoided substantive non-recurring and recurring work to manage compliance with what could have been over 500 requirements under the Transmission Operator and Transmission Planner registrations.

The Moses-Alcoa 115kV transmission lines and the Plattsburgh 115 kV capacitor banks 5 and 6 BES exclusion exception requests (EER) completed the initial review stage and were moved to substantive review stage by NPCC. Discussions with NERC, NPCC, Alcoa and NYPA on the Moses-Alcoa 115kV transmission lines EER has resulted in the temporary suspension of the EER to allow NPCC to evaluate the reliability impact of these and other transmission lines on the BES.

NYPA staff continued discussions with NY Transmission Owners to reach agreements that clarify the roles and responsibilities for compliance management for the Transmission Owner (TO) standards related to NYPA assets operated and maintained by others.

NYPA signed a Memorandum of Understanding (MOU) for this purpose with National Grid on March 7, 2016 pertaining to the NYPA Capacitor Bank located in the Edic Substation East. NYPA's discussions with these organizations also focused on reaching agreements, before April 2016, for managing compliance with the Version 5 Critical Infrastructure Protection (CIP) cyber security standards for assets owned by NYPA but that reside in facilities owned by others.

Critical Infrastructure Protection (CIP) Standards - Version 5 (V5)

During the reporting period, NYPA's CIP V5 implementation project team continued to execute the transition plan to achieve compliance with the new cyber security standards requirements before the enforcement date. FERC has granted the Trade Associations' request to delay CIP V5 implementation for High and Medium impact BES Cyber Systems until July 1, 2016, which brings CIP V5 implementation into alignment with the implementation date for CIP V6. The implementation date for Low Impact BES Cyber Systems remains April 1, 2017.

An assessment by NPCC's CIP V5 Outreach team was conducted on NYPA's approach for transitioning and commended NYPA for the substantial progress that has been made to date.

The project implementation team is focusing on the completion of priority activities required for compliance with CIP requirements ahead of compliance objectives (cyber security best practices and initiatives) in the following areas:

- Updating of CIP policies and procedures,
- Identification and classification of all of BES Cyber Systems,
- Implementation of physical security controls, and
- Upgrades to the work management tools.

Following the completion of the above tasks, the team will start conducting Internal Readiness Assessments on NYPA's CIPv5 compliance posture transition. These efforts will continue beyond the initial CIP V5 standard July 1, 2016 enforcement date into 2017 and include the completion of the compliance objectives, addressing the remaining CIP V5 requirements by the April 1, 2017 enforcement date and other compliance program enhancements to achieve CIP compliance sustainability.

Physical Security Standard

As a result of information about an April 2013 coordinated physical attack on a Pacific Gas and Electric Corporation substation, several US Senators requested FERC and NERC to consider whether NERC should establish and enforce standards for physical security for critical electric facilities. As a result, NERC developed a new physical security standard (CIP-014-2 – Physical Security) which was approved by FERC on November 20, 2014 and became effective October 1, 2015.

The NYISO, acting as the independent third party verifier under Requirement 2 of the CIP-014-2 Physical Security Standard, completed its review of the NYPA Transmission station/substation risk analysis and provided NYPA with a report on December 18, 2015. The NYISO confirmed NYPA's transmission station/substation risk analysis is consistent with the agreed upon study methodology and the NYISO's own results. NYPA Physical Security has completed the preliminary Threats and Vulnerability (T&V) assessments for these Bulk Electric System assets.