

REPORT TO RRG

FROM: SUBGROUP A – Insurance, Liability and Risk Management
Legal Work Group

DATE: August 28, 2000

SubGroup A Participants

George Schreck	-	PacifiCorp
Jill Sughrue	-	Portland General Electric
Stephany Watson	-	Bonneville Power
Arlena Barnes	-	Bonneville Power
Doug Nichols	-	Portland General Electric
Richard Goddard	-	Portland General Electric
Don Stone	-	Avista Corporation
Gary Dahlke	-	Avista Corporation
Denise Hill	-	Trans Alta
Michael Early	-	DSI
Joe Phillips	-	Marsh
Jim Geltz	-	Marsh
Don Brookhyser	-	IPP Group
Jim Mosher	-	IPP Group
Connie Wiestad	-	Sierra Pacific
Darrell Hill	-	Marsh
Rod Ross	-	Bonneville Power
Ron Rodewald	-	Bonneville Power
Peter Feldberg	-	BC Hydro
Jeff Christian	-	BC Hydro
Shelly Richardson	-	NW Requirements Utilities
Carl Imperato	-	Power Marketers
Malcolm McClellan	-	Idaho Power Company

The participants listed above attended one or more of the SubGroup A meetings to date. The SubGroup has had seven (7) meetings. As a result of these meetings, the SubGroup is making the following recommendations. As used in this report, the acronyms listed below have the following meanings.

TO	=	Transmission Owner
RTO	=	Regional Transmission Organization (West)
LO	=	Distribution Owner
GO	=	Generation Owner

DSI	=	Direct Service Industry
WIES	=	Agreement Limiting Liability among Western Interconnected Systems
MP	=	Market Participant
OATT	=	Open Access Transmission Tariff
SC	=	Scheduling Coordinator

The only issue specifically directed to SubGroup A from the RRG is Issue 18, which asks whether the liability relationship between the TO and RTO proposed by IndeGO should be preserved and what liability may arise as the result of the RTO's violation of its tariff. The SubGroup, then composed primarily of filing utility representatives, initially answered the IndeGO question in the negative. A detailed discussion of the reasons for this conclusion is set forth in a White Paper entitled "Discussion Paper From Liability/Insurance Subgroup A of Legal Workshop, RTO West" which is posted on the RTO West website.¹ In place of the IndeGO solution, the SubGroup first proposed the indemnity provision discussed in the White Paper and previously forwarded to the Transmission Control Agreement SubGroup. While there was a consensus on this recommendation, relative to the Transmission Control Agreement, there was no consensus about extending the indemnity provision to the GO or LO contracts. Please note that the current Attachment A now deletes the indemnity provision (formerly proposed TCA Section 20.5).

Realization of this lack of consensus occurred when the SubGroup was requested to address several other liability relationships relating to the LO, GO, and DSI contracts. Consequently, the SubGroup considered, or is considering, not only the relationship of the RTO to the TO, GO, LO and DSI, but also relationships among these participating parties. The SubGroup also considered existing agreements, such as WIES, and the fact that some, but not all, assets will fall under RTO West control, leaving a need for these existing or other continuing agreements to be consistent with RTO contracts. This is an

¹ The White Paper can be accessed via the RTO West web page at <http://www.nwrto.org/> and then make the following menu selections: From the homepage select "Work Groups," then "Legal," then "Links to Working Subgroup Information," then "Liability and Insurance Subgroup (Subgroup "A")," then "White Paper Prepared by Liability and Insurance Subgroup [posted June 26, 2000]." Alternatively, the document can be directly accessed at the following address:

<http://208.55.67.64/Doc/Legal_LiabInsSubgroup_WhitePaper_June232000.pdf>

on going process. The task of identifying all possible liability relationships between the parties, and then choosing those appropriate to deal with on a contract basis is quite complex. The Subgroup is developing a matrix of types of claims and results to aid our analysis.

To make this task easier, the SubGroup is recommending that the liability relationship between all of these parties be set forth in a new multi-lateral agreement, notwithstanding that the GIA, LIA and TCA will be bilateral contracts. This will allow us to deal with the liability relationship among RTO participants in addition to RTO to TO, GO and LO contracts. Drafting of this agreement will commence if the RRG concludes that the general direction described here is acceptable.

To aid our discussion of the general liability relationships we categorized claims into six general categories. As to these categories, the SubGroup has a tentative consensus based upon what we know now. However, until the multilateral agreement is drafted it probably will not be possible to identify whether there are issues that fall out of the process, beyond those discussed below.

1. **Third-Party Personal Injury or Property Damage—Contact Claims of Contractors, Employees and the General Public.**

For contact with the lines or equipment of a TO, RTO, GO, or LO, the party that operates or maintains an electric system would be responsible for safety on the system that it operates or maintains (irrespective of who designed the system) and to the extent that its operation or maintenance results in personal injury or property damage from contact with lines or equipment, the operating or maintaining party would indemnify and hold harmless other parties for these claims. If an owner does not operate or maintain any transmission facilities, that owner would be absolved of design risk.

2. **Property damage, economic loss, consequential damages resulting from failure of electric service at the consumer level. Third Party Claim Such As End Users.**

Legislation is the first preferred alternative. Because RTO-West might not be able to recover from a single catastrophic event where liability exhausted insurance

coverage, the SubGroup is concerned about the viability of an RTO without legislative protection. The task in any legislative approach would be to preserve reliability, i.e. by a system of fines and penalties while at the same time limiting the RTO's exposure to class action lawsuits arising from wide spread black outs.

Absent legislation, there may still be an opportunity to limit the extent of RTO West liability exposure by seeking tariff limitations in the RTO West OATT. FERC limitation of liability is desired by the SubGroup, but may not be available or enforceable. To the extent tariffs allow damages against the RTO, the current proposal, absent legislative or tariff protection, is to allow those causes of action to be determined by state law and to require RTO West to purchase liability insurance. No contractual indemnification would be offered by RTO West to the TO, GO or LO. The absence of any contractual indemnification would not mean that RTO West would be relieved of any liability to these parties or to end-use customers. It would only mean that the parties would have to pursue their rights under state law or federal law, including the right, if any, for the TO, GO or LO to seek contribution or indemnification under common law for end-use customer claims it may be exposed to by virtue of participation in the RTO.

3. **First party property damage of RTO, TO, GO, LO.**

Parties will release each other and hold each other harmless from first party property damage claims. This will be accomplished in a new multilateral agreement which is written to replace (or be consistent with) the existing WIES, Agreement.² There are issues, however, with regard to whether a general property damage release should be given between RTO West and the TO, GO or LO. One issue involves a situation where RTO West issues no directive to the TO, GO or LO, but as a result of its actions or omissions property damage occurs on the TO, GO or LO systems. In such case, some SubGroup members, including PacifiCorp, argue for a property damage release. Other SubGroup members, including Bonneville, argue that the current WIES Agreement

² The current WIES Agreement is subscribed to by most Northwest generators and control area operators. It contains a full release and hold harmless for property damage. It also contains a release of liability for losses arising from electric disturbances, except for willful misconduct and provides for a separate insurance program for third-party claims. Finally, the Agreement provides for an arbitration procedure to remove the release as to any operating condition which a party believes is unsafe.

should not apply and that the property damage release should be inapplicable from the TO, GO or LO to RTO West. This issue is set forth as Issue No. 2 as discussed later in this Report.

Generators as well as LO's and TO's are willing to consider a mutual release for property damage liability conditioned on the ability of the generator not to comply with an RTO directive. The conditions currently being sought by the IPP Group for section 4.3 would read as follows:

4.3 Limits on Parties' Obligations Under Agreement and Applicable Tariff Provisions. In carrying out the requirements of this Agreement the GO shall not be required to take any action:

- (a) that is not within the physical capabilities of the Party's Electric System (or any part of another party's Electric System that the applicable Party has the legal right to cause to comply with this Agreement);
- (b) that it believes in good faith will create serious and immediate risks to human health or safety; *provided, however,* that interruption of Transmission Service shall not in itself necessarily be deemed to create serious and immediate risks to human health or safety;
- (c) that it believes in good faith will create an immediate risk of serious damage to facilities or equipment within its Electric System or will cause it to operate any part of its Electric System in an unsafe manner;
- (d) that would violate any provision of the reliability criteria, standards, guidelines and operating procedures of NERC or the WSCC, any FERC or State regulatory agency licenses with which it is obligated to comply, any applicable Nuclear Regulatory Commission licenses or requirements, the terms of any applicable permits issued by a governmental authority, or any applicable governmental laws or regulations; or
- (e) that conflict with any non-power requirements with which the Party is obligated to comply (including without limitation any obligations under environmental laws, regulations, court and administrative orders, or biological opinions).

Final wording of Section 4.3 of the GIA has been referred to this SubGroup A. The IPP and Marketer Groups have requested that Item (f) be added to the above list which would read as follows:

- (f) to comply to an operating instruction issued by the RTO where such operating instruction is not within the RTO's authority under the RTO tariff.

In principle, the Filing Utility members of SubGroup A do not resist the notion that there should be compensation for an unauthorized dispatch order. However, the Filing Utility Members believe that Item (f) is misplaced here, as authority under the tariff is not especially relevant to a property damage release given that Section 4.3(c) allows a GO to refuse an order for reasons stated to prevent property damage whether or not the order is otherwise authorized by the remainder of the RTO tariff. We are assuming that the GIA interconnection requirements will be a part of the tariff filing under recent FERC orders and cannot be superceded by other tariff provisions or subsequent revisions. We still need to resolve whether proposed item (f) has to be placed here in Section 4.3 of the GIA, or whether it may be placed in a separate section dealing with direct actual damages. In any case, the Subgroup's recommendations are premised on the right not to comply with RTO dispatch orders that are not authorized by the RTO Tariff. Note also that as currently drafted, the generator proposal to recover "demonstrable costs" discussed in section 5 below includes "equipment damage costs". See Issue No. 1.

4. **RTO, TO, GO, LO consequential damages.**

All owners and operators of the electric system would waive all consequential damage claims against each other for failure of performance under the RTO tariffs or agreements. Ideally this would also include market participants (MP's) for the RTO if FERC will permit waiver of consequential damages. There is one issue with regard to this waiver which involves the question of whether generators may recover opportunity costs from the RTO (see Issue No. 1 statement following this Report).

5. **First party direct actual damages of TO, GO, LO, including cost of cover or replacement power costs (but not including property damage).**

RTO liability would be covered by insurance. A self insured retention would be set. The self insured retention would be placed in a bank deposit account. Claims, whether arising in contract or tort, or both against the RTO for failure to provide proper service under the RTO tariff and any associated agreements would be paid from this fund. Claims would not be limited to the fund. The fund would be under the authority of the RTO General Counsel. Insurance amounts and self insured retention would be set initially by the RRG and minimums would be in the individual RTO to TO, GO and LO contracts. Current AEGIS (Associated Electric & gas Insurance Services, Ltd.) insurance is on a reimbursement basis, so the fund would have to be established with sufficient reserves to manage claims until reimbursement occurs. The scope of insurance coverage and the waiver of typical exclusions of coverage (e.g., for service interruption) will have to be negotiated with potential insurers.

Included within first party actual damages would be the cover costs or replacement power costs (also including opportunity costs depending on the resolution of Issue No. 1) of GOs that are given dispatch orders by RTO West which are not true emergencies and thus, are not within the RTO's authority under the RTO Tariff. Were RTO West to issue a directive to a TO, GO, LO or SC deemed invalid, but obeyed under protest, damages would be paid by RTO West. A dispute resolution process is needed for this purpose.

The situation described above is distinct from the Pacific Northwest Security Coordinator ("PNSC") in its present form, where no compensation is paid for an emergency directive, whether or not the directive is considered "valid". We are assuming that PNSC will continue to function separately from RTO West and that future PNSC directives will go first to RTO West and then be re-issued by RTO West to the GO. If an exception is created from damage payments for situations where the directive came first from PNSC in a true emergency, and was only conveyed by RTO West, a method would be needed to fairly spread the impact of the directives among those chosen to receive the directive within the region. Presently, there is no such method in PNSC which depends upon a thirty (30) day termination notice to self-police the fairness issue. The Filing

Utility SubGroup members would recommend that an exception for payment of any first party non-property damages be made for a PNSC directive under Paragraph 6 of the current PNSC Agreement, and that an apportionment mechanism be adopted to fairly spread the impact of such directives among impacted generators.

6. **Third party (other than failure of service) damages not limited by tariff provisions.**

An example is the case where negligent failure of RTO-West to provide transmission causes a first party transmission customer to interrupt a sale to a third party (a generating utility other than the first party or marketer) and the third party purchases replacement power. Third party damages (other than failure of service described in item 2 above) would be obligations of RTO-West to the extent that a basis for liability exists. Absent legislation, tariff protection or a waiver of consequential damages (item 4 above), there is no limit to these claims, and to the extent that insurance is not available, the obligation would fall to RTO-West to pay any valid claims.

Concerning these recommendations, the SubGroup has not been able to resolve a few issues, or would like RRG direction that the approach described is acceptable. In addition, if any of the consensus recommendations are called into question by the RRG, the SubGroup wishes to be so advised, so that it can regroup and consider alternatives. We have listed two recommendations and two issues for review:

Recommendation 1: RTO West should seek to limit liability in its OATT.

Recommendation 2: RTO West should carry appropriate levels of insurance and self-insured retention.

IL&RM Issue 1: Whether generators should recover demonstrable opportunity costs resulting from the RTO's negligent acts or failure to follow its tariff and what are demonstrable opportunity costs?

IL&RM Issue 2: Whether RTO West should be released from property damage liability to a TO, GO or LO under circumstances where RTO West issued no directive to such TO, GO or LO, but nevertheless its actions or omissions resulted in property damage on a TO, GO or LO system.

A discussion of each issue, with statements in support of each position follow. Where there was no opposition, but the SubGroup desires RRG approval of the direction stated, the position is stated as a Recommendation.

The SubGroup also has additional work to complete which is not included in the report. This work includes:

1. Liability at RTO West Seams
2. Scheduling Coordinator Agreement Liability provisions
3. Other insurance requirements, beyond E&O and Comprehensive liability insurance.
4. DSI Transmission Contract liability provisions, and other existing transmission contracts.

With respect to the existing DSI transmission contracts or other existing transmission contracts that have liquidated damages provisions, the SubGroup has been asked to review those contracts and determine whether the provisions would remain, or whether they would be subsumed in a new multi-lateral agreement or new RTO West agreements. This is a very recent assignment. In general, the consensus was that for existing contracts, as of some fixed date that has already occurred, there is little or no option but for RTO West to accept assignment, assumption or performance of these contracts with an offer of indemnity back to the TO for performance of that contract. However, new liability or liquidated damages agreements in contemplation of RTO West should not be allowed at this point in time.

The consequence of grandfathering existing transmission contracts which will be assigned to or assumed by RTO West for performance under an indemnity promise for the existing liability language, but not offering any indemnity for contract liability at the distribution level necessarily creates a difference in treatment. On the one hand it is not financially possible for RTO West to accept liability under distribution contracts it did

not negotiate, especially for new agreements. On the other hand a TO may not be able to join RTO West unless existing transmission contract holders, such as the DSIs, either agree to new contracts or RTO West indemnifies the TO for existing transmission contract provisions such as liquidated damages. In any case, the proposal is that no indemnity be offered for any distribution contract whether entered into by a TO or LO.

With respect to the subject of liability provisions for the SC, the SubGroup was not prepared to recommend specific contract language until it was finally determined exactly what the function and role of an SC would be. Further, it was not clear whether there would be a bilateral contract between RTO West and an SC or simply an application and certification process. In any case, the liability provisions could be placed in the bilateral contract, if there was one, or in the RTO West Tariff, in which event if they were placed in the Tariff they would be subject to unilateral modification by RTO West. Assuming that the SC acts only as an agent for GOs and LOs in matching generation and loads the SubGroup initially saw no reason why the same liability provisions set forth in Sections 1 through 6 above would not also apply to the SC where applicable. In some cases, however, the principals are not applicable, as for example, in the case of a mutual release of liability for property damage to electric systems, as the SC does not own any part of an electric system. In any case, this subject will require further work which is likely to extend beyond September 1, 2000.

RECOMMENDATION 1: RTO-West Should Attempt to Include Tariff Protection for Continuity of Service Limiting Liability for Negligence.

In Transmission Access Policy Study Group v. FERC, 2000 WL 762706 *56-57 (D.C. Cir.)(June 30, 2000) FERC took the position that the refusal to approve OATT *pro forma* language requiring the transmission customer to “indemnify, defend and save the Transmission Provider harmless from any and all damages . . . except in cases of negligence or intentional wrong doing” was neither intended to adopt any particular liability standard distinct from indemnification, nor to adopt a new, simple negligence standard of liability for transmission.

As noted in this decision, prior to unbundling, retail tariff provisions in most states permitted utilities to limit their liability for service interruptions to instances of

gross negligence or willful misconduct. Courts have upheld these limitations on the public policy grounds that they balanced lower rates for all customers against the burden of limited recovery for some, and that the technological complexity of modern utility systems and resulting potential for service failures unrelated to human errors justified liability limitations. FERC has also previously allowed electric utility tariffs to explicitly limit a utility's liability for service interruptions to instances of gross negligence or willful misconduct.

Conclusion: Given this recent precedent, RTO-West should attempt inclusion of limitations of liability in a continuity of service provision in the OATT. Such limitation of liability is essential for the RTO to undertake regional transmission operations at proposed tariff rates assuming the availability of liability insurance at reasonable cost. It is also doubtful that insurance would be ultimately available, or if available, with adequate limits, should a single catastrophic regional event occur for which there was liability under any simple negligence standard. Single application to FERC is also preferred in lieu of application to each individual state in which the RTO will conduct transmission operations.

RECOMMENDATION 2: The Appropriate Liability Coverage and Limits for RTO-West.

It is the consensus of Legal Subgroup A that the RTO obtain General Liability and Errors and Omissions (E & O) coverage “consistent with industry practice,” and that at a minimum provides: coverage limits of \$150M for General Liability; separate \$150M for E & O, and a maximum self-insured retention of not more than \$2M.

Many Transmission Owners have coverage limits in excess of this amount. It is uncertain what levels of insurance GOs and LOs currently carry. Unconfirmed information from other ISOs/RTOs suggests that liability limits of up to \$400-\$500M may be available. It is further the belief that individual ISO's may have structured liability assumption and risk transfer differently. Our Marsh USA Broker Representative recommends that the General Liability limit and E & O Coverage limit both be at the

same amounts (\$150M minimum each). In the second FERC NY ISO Order the cost of insurance was recognized as a recoverable cost of doing business.

It is specifically recommended that “interruption of service” be included with liability coverage should liability result from such claims. AEGIS presently provides “Failure to Supply” coverage, but contains exclusions specific to “intentional acts” and imposes 10% excess capacity requirements not pertinent to RTO-West function. E & O coverage, necessary to offer potential coverage for economic loss without the event of “property damage” will also likely require specific negotiation of a “Designated Services Endorsement” inclusive of RTO-West planning, design, operation and maintenance activities.

Historically, there is a limited insurance market available to energy providers, with AEGIS and EIM (Energy Insurance Mutual) being principal providers to the industry. The London market may be available to provide additional excess coverage. WSCC was able to negotiate waivers of coverage limitations in obtaining coverage required for the NW Security Co-ordination Agreement (\$100M Liability/\$75M E & O).

It should be recognized that the availability of insurance coverage at reasonable premium, particularly without tariff limits on liability, can not be guaranteed into the future. Liability for any single major outage event would likely result in damage exposure in excess of \$500M and likely result in the future non-availability of insurance and/or significant future increases in premium. Tariff protection and/or legislated immunity is the preferred vehicle for making long-term protection available to the RTO. It has also been suggested that, in the event of an insurance market failure, the RTO could self-insure and spread these costs to all transmission users. Such socialization of self-insurance costs is consistent with the FERC NYISO Orders and is a valid option in the absence of tariff protection or legislated immunity, however, self-insurance may not be acceptable to regional parties that are at risk of joint and several liability with RTO West.

Conclusion: That authorization be given to negotiate General Liability and separate E & O policy coverage at a minimum of \$150M, with authorization to explore incremental cost associated with additional coverage limits and policy terms satisfactory to RTO-West, and to report back to the RRG at a future date.

ISSUE 1: GENERATOR OPPORTUNITY COSTS.

Statement of Issue: Whether generators should recover demonstrable opportunity costs resulting from the RTO's negligent acts or failure to follow its tariff and what are demonstrable opportunity costs.

Arguments in Favor of Denying Opportunity Costs: Damages from lost opportunities can be speculative and difficult to measure. A generator could allege it had all kinds of opportunities available whether or not the generator could have actually taken advantage of the opportunity, and without a scheduled transaction, the generator could pick the most lucrative opportunities. Even if the opportunity cost is demonstrable, if the lost opportunity is due to a wide spread system failure, price spikes could arise which the generator could claim as high cost lost opportunities. This circular argument could mean that the very event that the generator claimed caused a lost opportunity actually caused the opportunity to exist to begin with. Furthermore, in order to claim lost opportunity, the measure of the opportunity would be the lost margin, and to calculate this, the generator would need to furnish cost information. Any agreement to compensate generators will require their agreement to furnish this information.

Arguments in Favor of Allowing Opportunity Costs: The RTO should be held liable for all Demonstrable Costs³ (which include opportunity costs) that result from the RTO's negligence or willful actions. In particular, the RTO should be held liability for the Demonstrable Costs incurred by SCs and Generators as result of compliance with RTO dispatch orders which are wrongful, negligent or otherwise inconsistent with the RTO's authorities under the RTO Tariff.

³ Proposed definition of Demonstrable Costs: Demonstrable Costs are defined to be all costs, including variable production costs, equipment damage costs and the costs of foregone opportunities, incurred by an SC in providing a service to the RTO or in complying with an RTO operating instruction; provided that: (a) the SC must provide reasonable justification to support its claims of costs, which may include direct cost data or indirect data such as published market prices or indices; (b) such costs may be subject to caps or floors imposed by contracts or by FERC or other regulatory authorities; and (c) the final determination of whether a cost has been sufficiently demonstrated will be subject to dispute resolution under the terms of the RTO Tariff.

1. Opportunity costs are legitimate costs that are incurred by market participants and it would be inappropriate to require individual market participants to bear the burden of the RTO's wrongful or negligent actions, rather than spreading the burdens stemming from the RTO's actions across the broader community.⁴
2. Opportunity costs are not uncertain. They are calculable. An aggrieved party should be entitled to demonstrate its opportunity costs, accepting the burden of proof to demonstrate the purported opportunity costs. As an administrative efficiency, an aggrieved party could also choose to accept a "default" opportunity cost calculated from the RTO's real-time Balancing energy prices. The price of Balancing Energy is calculated by the RTO and is therefore completely discoverable. The rationale for the latter alternative is that under most RTO/ISO tariffs (and thus far in the RTO West development process) Scheduling Coordinators (as representatives of Generators) have the right and the economic opportunity to sell into/purchase from the RTO's real-time Balancing Energy market. These sale/purchases need not be the result of predetermined contractual agreements. If the RTO orders a decrease or an increase in an SC's or generator's schedule, the SC or generator will therefore lose a clearly definable sale or purchase opportunity in the RTO's real-time Balancing Energy market.
3. Releasing the RTO from such liability would provide a disincentive to the RTO to operate within its legal authorities.

Finally, the circumstances in which opportunity costs would be in contention are narrowly defined. RTO liability would be circumscribed by allowing recovery only for "Demonstrable Costs incurred as result of compliance with a wrongful dispatch order of the RTO."

⁴ NOTE: This issue applied not only to Generators but to Scheduling Coordinators as well. In fact, because RTO dispatch orders will be issued primarily to SCs rather than Generators, the major concern is for the impacts on the SCs.

ISSUE NO. 2: PROPERTY DAMAGE RELEASE

Statement of Issue: Whether RTO West should be released from property damage liability to a TO, GO or LO under circumstances where RTO West issued no directive to such TO, GO or LO, but nevertheless its actions or omissions resulted in property damage on a TO, GO or LO system.

Arguments in Favor of Property Damage Release: The RTO should be released from property damage caused to TO, GO or LO facilities, unless such damage is caused by gross negligence or willful misconduct of the RTO.

A TO, GO or LO is in the best position to assess the risk to their facilities and protect them in the most cost effective way. In addition, many parties carry insurance for property damage and can make a claim for such damages against their policy. If the RTO is held responsible for such damage, then the RTO would also have to carry insurance for such claims, and there would be two policies purchased for the same claim, one by the generator and one by the RTO. Only one insurance policy would pay the claim, so there would be inefficient duplicate insurance costs, which would be passed to users of the transmission system through the transmission rates. In effect, users of the transmission system could end up paying for their own insurance and also paying for RTO insurance through the transmission rates. If it were believed that releasing the RTO could cause the RTO to be careless, parties can address detrimental conduct by complaining to the stakeholder board or FERC. Either of these entities would be in the position to review the RTO's actions and demand appropriate action by the RTO board.

Arguments in Favor of Holding RTO West Accountable for Property Damage: If the RTO is not held accountable for property damage, it has no financial incentive to avoid causing such damage. In general, there should be an alignment of responsibility and accountability.

In order to participate in the RTO, BPA has needed to deal with some issues concerning submitting federal assets to the control of a non-federal entity such as the RTO. There may be a real or at least a perceived problem with

allowing the RTO to have control over federal assets and also releasing the RTO from liability for damage to the federal assets.

Relying on the TO,GO,LO's ability to influence the RTO board of directors to take action when needed may be difficult, especially if the roles and responsibilities of the various parties are cloudy and/or the parties have different opinions on the priority of programs. Trying to influence the decisions of the RTO board could prove to be very costly in dollars, time, resources, and political relationships. BPA's relationship with Energy Northwest (formerly Washington Public Power Supply System) may be a good example of this. Hopefully there are some lessons to be learned here.

In past years a primary purpose of the hold harmless agreements was to reduce the number of lawsuits between the many Control Area Operators when an electrical disturbance traveled across more than one Control Area and caused property damage. In the new world of the RTO there will be only one Control Area Operator, the RTO, and therefore identifying the liable party for property damage should be relatively easy.

In past years hold harmless agreements worked reasonably well because each control area operator had its own assets as well as its neighbors assets at risk. There was a natural incentive for each Control Area to operate the system safely and reliably so as to not cause damage to its own system or its neighbors system. The RTO will not own transmission assets.

The financial impact of "duplicate insurance coverage" may not be as simple as previously discussed. For example, many utilities carry property insurance and have a high self insured retention (deductible). If in a hypothetical example, a TO suffers a \$10 million property loss resulting from a substation fire and has a property insurance policy with a \$1 million deductible, the TO would recover \$9 million for the loss. However, if a RTO liability insurance policy was in force to cover the same loss, it could pay the full \$10 million. Some TO, GO, or LO companies may be able to successfully argue to their insurance carrier for reduced property insurance premiums due to less exposure or they may choose to purchase different deductibles if the RTO assumes liability and carries insurance.

The additional cost of insurance premiums for the RTO for coverage of property damage to TO,GO,LOs when spread among the members may be a relatively small expense.

Unlike the voluntary WIES program, if release from property damage liability is granted to the RTO it is likely to be permanent and irreversible.

AGREEMENT

BETWEEN

RTO AND TRANSMISSION OWNER

20. INSURANCE AND LIMITATION OF LIABILITY

To promote cooperation between the Parties, to avoid duplication of costs, and to carry out the purposes of this Agreement, the Parties agree to the following provisions for limited liability, insurance, and indemnification:

20.1 Limitations of Liability. Except as otherwise provided under the RTO OATT, the Transmission Owner shall not be liable (whether based on contract, indemnification, warranty, tort, strict liability or otherwise) to the RTO or any other party for any damages whatsoever, including without limitation, special, indirect, incidental, consequential, punitive, exemplary or direct damages resulting from any act or omission in any way associated with this Agreement, except to the extent the Transmission Owner is found liable for gross negligence or intentional misconduct, in which case the Transmission Owner shall not be liable for any special, indirect, incidental, consequential, punitive or exemplary damages.

20.2 Additional Limitations of Liability. Except as otherwise provided under the RTO OATT, the Transmission Owner shall not be liable for any indirect, consequential, exemplary, special, incidental or punitive damages including, without limitation, lost revenues or profits, the cost of replacement power or the cost of capital, even if such damages are foreseeable or the damaged party has been advised of the possibility of such damages and regardless of whether any such damages are deemed to result from the failure or inadequacy of any exclusive or other remedy.

20.3 Insurance; Waiver of Subrogation Rights

20.3.1 RTO Insurance Coverage Requirements. Throughout the term of this Agreement, the RTO shall maintain insurance coverage consistent with prudent industry practice and that at a minimum:

- (1) provides general liability and errors and omissions insurance with respect to RTO's performance under this Agreement;

- (2) provides for maximum per-occurrence self-insured retention of not more than \$2 million;
- (3) provides general liability coverage limits of not less than \$150 million and separate errors and omissions coverage limits of not less than \$100 million;
- (4) provides an agreement or endorsement under which the insurance cannot be terminated, canceled, allowed to expire, non-renewed, or materially altered without 90 days= prior written notice to RTO and provides that such policy is primary over any other insurance; and
- (5) provides that RTO=s insurer shall be bound by any waivers of the insurer=s rights of subrogation granted by RTO.
- (6) names the Parties to this Agreement as an Additional Insured(s) under such insurance.

20.3.2 Annual Review. Insurance requirements shall be reviewed by the RTO Board on an annual basis for consistency with prudent industry practice, but shall be no less than the above referenced specific coverage and limits. Alternative risk financing arrangements sufficient to cover these responsibilities will require written approval of the majority of Transmission Owners executing Agreements with the RTO.

20.4 RTO=s Obligation to Notify Parties with Respect to Insurance. RTO shall not consent to or allow the insurance required under Section 20.3.1 above to be terminated, canceled, allowed to expire, or materially altered without Transmission Owner=s written consent. Non-renewal of insurance shall also not occur without providing at least 60 days= advanced notice to Parties to this Agreement.

20.5 Claims by Employees and Insurance. A Party shall be solely responsible for and shall bear all of the costs of claims by its own employees, contractors, or agents arising under and covered by, any workers' compensation law. A Party shall furnish, at its sole expense, such insurance coverage and such evidence thereof, or evidence of self-insurance, as is reasonably necessary to meet its obligations under this Agreement. Each Party hereby agrees to indemnify, defend and hold the other Party harmless from any such claims, and hereby expressly waives protections afforded by worker=s compensation law as necessary to effect the terms of this agreement.

20.6 Third-Party Claims. In the event third-party claims are made against another Party to this Agreement arising out of this Agreement or its performance, or with the occurrence of an event from which it is reasonably anticipated that claims may be made, the Parties agree that:

20.6.1 In the event of any such claim, or even from which third party claim(s) are anticipated, a Party shall provide immediate notice to the other Party pursuant to Section [25.1 IndeGO Section reference]; shall make such immediate efforts as necessary to preserve evidence and/or protect against default judgment; and shall provide notice to the RTO General Counsel at the address designated for such purpose with a copy to the broker of record with respect to the insurance policy described in Section 20.3.1 above. The RTO General Counsel shall provide notice to all other Transmission Owner, and assure that notice as necessary is given to insurance carrier(s). Failure to provide such notice shall not prejudice the right of a party to bring a subsequent claim against the RTO, and shall not subject such party to any damages for failure to notify the RTO.

20.7 Survival. The provisions of this Article, " Insurance and Limitation of Liability@ shall survive the termination or expiration of this Agreement or the RTO Tariffs.