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President Trump Issues Executive Order Prohibiting Certain Transactions in the Bulk-Power System Supply Chain

The Order prohibits the purchase or installation of certain bulk-power system electric equipment from foreign adversaries and those subject to their jurisdiction or direction.

Key Points:

- On May 1, 2020, President Donald J. Trump issued an Executive Order prohibiting certain types of transactions regarding bulk-power system electric equipment designed, developed, manufactured, or supplied, by persons owned by, controlled by, or subject to the jurisdiction or direction of a foreign adversary. The focus of the Executive Order is on electric equipment supplied from a foreign adversary or an entity subject to such foreign adversary's jurisdiction.

- Not all transactions for equipment supplied from a foreign adversary or an entity subject to such adversary's jurisdiction are prohibited. The prohibition applies only to those transactions that pose: (i) an undue risk of sabotage to or subversion of the design, integrity, manufacturing, production, distribution, installation, operation, or maintenance of the bulk-power system in the United States; (ii) an undue risk of catastrophic effects on the security or resiliency of United States critical infrastructure or the economy of the United States; or (iii) an unacceptable risk to the national security of the United States or the security and safety of United States persons.

- While the operative provisions in the Executive Order include some broad language that may be open to interpretation as to its scope, as a practical matter, the Executive Order:

    - May not have a material impact on many electric generating projects

    - Is unlikely to apply to upstream transfers of electric generating or transmission projects

    - Is not retroactive and applies only to applicable equipment transactions initiated after the May 1, 2020, date of the Executive Order

    - Is unlikely to require significant capital investment for existing electric generating or transmission projects that have already procured their electric equipment

    - Is unlikely to apply to most projects outside the United States

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- The Secretary of Energy is tasked with working with other executive agencies and departments to propose rules and regulations to implement the Executive Order, based in part on comments from interested parties.

Overview of the Executive Order

On May 1, 2020, President Trump issued an Executive Order on Securing the United States Bulk-Power System (the Executive Order) acting pursuant to his authority under the United States Constitution and the laws of the United States, including the International Emergency Economic Powers Act (IEEPA),[1] the National Emergencies Act (NEA),[2] and section 301 of title 3, United States Code.[3] In the Executive Order, President Trump determined that "the unrestricted foreign supply of bulk-power system electric equipment constitutes an unusual and extraordinary threat to the national security, foreign policy, and economy of the United States." The Executive Order acknowledged that "maintaining an open investment climate in bulk-power system electric equipment, and in the United States economy more generally, is important for the overall growth and prosperity of the United States," but found that "such openness must be balanced with the need to protect our Nation against a critical national security threat." In light of these findings, President Trump declared a national emergency with respect to the threat to the United States bulk-power system.

Prohibited Transactions Concerning Bulk-Power System Electric Equipment

The Executive Order prohibits "any acquisition, importation, transfer, or installation of any bulk-power system electric equipment (transaction) by any person, or with respect to any property, subject to the jurisdiction of the United States, where the transaction involves any property in which any foreign country or a national thereof has any interest (including through an interest in a contract for the provision of the equipment)."[4] The prohibition applies only to transactions as defined in the Executive Order that are initiated after the date of the Executive Order.[5] Further, such a transaction is prohibited only if the Secretary of Energy (Secretary), in consultation with other executive departments and agencies, has determined the following:

- The transaction involves **bulk-power system electric equipment**[6] designed, developed, manufactured, or supplied, by persons owned by, controlled by, or subject to the jurisdiction or direction of a foreign adversary;[7] **and**
- The transaction:
  - Poses an **undue risk of sabotage to or subversion of** the design, integrity, manufacturing, production, distribution, installation, operation, or maintenance of **the bulk-power system** in the United States;
  - Poses an **undue risk of catastrophic effects** on the security or resiliency of United States **critical infrastructure or the economy** of the United States; **or**
  - **Otherwise poses an unacceptable risk to** the **national security** of the United States **or** the **security and safety** of United States persons.[8]

The Executive Order's prohibition on such transactions remains effective notwithstanding any contracts, licenses, or permits that predate the issuance of the order.[9]

Implementation of the Executive Order

The Executive Order empowers the Secretary, in consultation with other agencies and departments, to design or negotiate measures to mitigate concerns that would warrant prohibition. These measures may "serve as a precondition to the approval by the Secretary of a transaction or of a class of transactions that would otherwise be prohibited pursuant to this order."[10] In addition, the Secretary may publish criteria for

recognizing particular equipment and vendors as pre-qualified for future transactions, and may publish a list of pre-qualified equipment and vendors.[11]

More broadly, the Secretary is tasked with adopting rules and regulations to implement the Executive Order, and is authorized to "direct[] the timing and manner of the cessation of pending and future transactions" prohibited by the Executive Order.[12] The Secretary's rules and regulations may determine what countries or persons constitute "foreign adversaries," identify particular equipment or countries that warrant the scrutiny of a transaction, establish a licensing process for transactions, and identify a mechanism and relevant factors for the negotiation of agreements to mitigate concerns raised in the Executive Order.[13] The implementing rules or regulations shall be published within 150 days of the date of the Executive Order.

Impact on Existing Bulk-Power System Equipment

The Executive Order instructs the Secretary to work with other agencies to identify bulk-power system electric equipment that poses the types of risks associated with prohibited transactions.[14] The Secretary is directed to work with relevant agencies to "develop recommendations on ways to identify, isolate, monitor, or replace such items as soon as practicable, taking into consideration overall risk to the bulk-power system."[15] The Executive Order instructs the Secretary to complete these tasks "[a]s soon as practicable."[16]

Task Force on Federal Energy Infrastructure Procurement Policies

The Executive Order creates a Task Force on Federal Energy Infrastructure Procurement Policies Related to National Security (Task Force), which is chaired by the Secretary and comprises several Executive Branch agency heads, including the Secretary of Defense and the Secretary of the Interior.[17] The Task Force will recommend energy infrastructure procurement policies and procedures for agencies, evaluate methods and criteria used to incorporate national security considerations into energy security and cybersecurity policymaking, and conduct studies and develop additional recommendations as instructed by the Secretary.[18] The Task Force is required to submit a report to the President within one year of the Executive Order, and a subsequent report at least annually thereafter, summarizing its progress, findings, and recommendations.[19] The Task Force must submit its recommended energy infrastructure procurement policies and procedures to the Federal Acquisition Regulatory Council, which has 180 days to consider proposing for notice and public comment an amendment to the applicable provisions in the Federal Acquisition Regulation implementing such recommendations.[20]

Authority and Remedies

The Executive Order was issued pursuant to the President's authority under the United States Constitution and various federal laws, including the IEEPA and the NEA. The IEEPA provides for both civil and criminal penalties; civil penalties require only a violation of the law, whereas criminal penalties require willful conduct.[21] Thus, violation of the Executive Order or the rules and regulations implemented with respect to it could potentially result in either civil or criminal liability. As discussed below, while the May 15, 2019 Executive Order on Securing the Information and Communications Technology and Services Supply Chain (Communications Order) included similar potential for both criminal and civil liability, there has been no effort to specify any potential criminal penalties in the rules proposed by the Commerce Department with respect to the Communications Order.

Practical Implications for the Power Industry

While some of the language in the Executive Order is quite broad, there are some important limitations that deserve mention, including as discussed below. Based on the Communications Order and a pending

rule developed by the North American Electric Reliability Corporation (NERC) addressing bulk-power system supply chain issues, the impacts of the Executive Order, while important, are not likely to be as far-reaching as the broad language in the Executive Order may, at first reading, suggest.

The Executive Order may not have a material impact on many electric generating projects.

Although most utility-scale electric generating projects are generally considered to be a part of the bulk-power system, the Executive Order may not meaningfully impact many individual electric generating projects, particularly existing generating projects.

- The Executive Order appears to be more targeted toward equipment in transmission facilities (*e.g.*, substation transformers and voltage regulators, high voltage circuit breakers) that are more likely to have a potentially adverse impact on the bulk-power system (and system-wide vulnerabilities) than individual electric generating projects.

- While the definition of "bulk-power system electric equipment" includes generation equipment, the definition of "bulk-power system" only includes energy from generation facilities to the extent "needed to maintain transmission reliability."[22]

- Even if certain equipment for generating projects (such as solar panels, inverters, or turbines) are sourced from foreign adversaries or entities subject to their jurisdiction, how such equipment would present the kinds of risks to the bulk-power system, infrastructure, the economy, national security or safety on which the Executive Order is focused remains unclear.

- Given significant and negative COVID-19-related impacts on the United States economy, the Secretary would not likely seek to impose unnecessary restrictions on the United States power generation industry that could further impair and delay the timely development and commercial operation of electric generating projects.

The prohibition on certain bulk-power system supply chain transactions is unlikely to apply to upstream transfers of electric generating or transmission projects.

Pursuant to Section 1(a)(i), the Executive Order covers only transactions involving bulk-power equipment "designed, developed, manufactured or supplied" by persons owned or controlled by a foreign adversary or subject to such adversary's jurisdiction or direction. The Executive Order does not on its face apply to the direct or indirect transfers of ownership or control of electric generating or transmission projects. Such transfers may already require prior authorizations or clearances from a range of federal and state regulatory entities, including by the Committee on Foreign Investment in the United States (CFIUS), the Federal Energy Regulatory Commission (FERC), and state public utility commissions. Moreover, as discussed below, while the Communications Order included similarly broad language about the types of transactions implicated, there has been no effort to apply its prohibition to direct or indirect transfers of ownership or control of projects that use such technology or services.

The Executive Order does not apply retroactively.

Section 1(a) of the Executive Order states that the prohibition on certain bulk-power system supply chain transactions applies only "where the transaction was initiated after the date of this order." At the same time, Section 1(c) of the Executive Order states that these prohibitions apply "notwithstanding any contract entered into or any license or permit granted prior to the date of this order." Rather than having any retroactive effect, this language indicates that such a previous contract or regulatory authorization would not exempt an otherwise prohibited supply chain transaction initiated after the date of the Executive

Order from needing to comply with the Executive Order. In other words, if the purchaser of covered bulk-power system equipment had previously obtained authorization to acquire, import, or install equipment prohibited under the Executive Order after May 1, 2020 (the date of the Executive Order), such authorization would not act as a shield against the prohibitory impacts of the Executive Order.

The Executive Order is unlikely to require significant capital investment for existing electric generating and transmission projects.

Section 2(d) of the Executive Order states that the Secretary will develop recommendations on ways to "identify, isolate, monitor, or replace [applicable bulk-power system equipment] as soon as practicable, taking into consideration overall risk to the bulk-power system." On its face this language could be read as a prohibition on the current or continuing use of certain *existing* bulk-power equipment for which the acquisition, import, transfer, or installation would have been prohibited under the Executive Order and require a "rip and replace" of such equipment. However, such a "rip and replace" scenario seems unlikely. No executive order, by its nature, can give the Executive Branch new powers; rather, under Article II of the United States Constitution, an executive order can only guide the execution of authority separately conferred by the United States Constitution or some other federal law. As a result, federal courts have struck down executive orders that exceed the President's authority under a federal statute or conflict with other federal statutory provisions.[23] The authors have not identified any federal law that would authorize the Department of Energy or the Commerce Department to prohibit existing uses of bulk-power equipment lawfully acquired, imported, transferred, or installed.

The Executive Order is unlikely to apply to most projects outside the United States.

The Executive Order could theoretically apply to projects located outside the United States. However, that would only be the case if the project outside the United States could satisfy one of the express conditions by presenting an undue risk of sabotage to or subversion of the bulk-power system in the United States, posing an undue risk of catastrophic effects on the security or resiliency of United States critical infrastructure or the economy of the United States, or otherwise posing an unacceptable risk to national security. Therefore, a project located outside the United States would not likely meet the relevant standards in the Executive Order.

Notwithstanding that the definition of "United States person" in this Executive Order includes "foreign branches" of entities organized under the law of the United States,[24] that term (which is in fact common to Executive Orders issued under the IEEPA) has generally been understood to refer only to the foreign division of a US corporation. However, the term "United States person" has no relevance to the *jurisdictional bounds* of the prohibitions in the Executive Order, which apply specifically to "any person ... subject to the jurisdiction of the United States."[25] The term "United States person" is used only in identifying who might be *harmed* by foreign adversaries.[26]

Comparison With Other Bulk-Power System Reliability Laws and Regulations

NERC Supply Chain Risk Management Reliability Standards

On October 18, 2018, FERC issued a final rule approving supply chain risk management Reliability Standards submitted by NERC.[27] The Reliability Standards, CIP-013-1 (Cyber Security – Supply Chain Risk Management), CIP-005-6 (Cyber Security – Electronic Security Perimeter(s)) and CIP-010-3 (Cyber Security – Configuration Change Management and Vulnerability Assessments) (collectively, NERC Reliability Standards), were meant to have an effective date of July 1, 2020. FERC has since delayed their implementation by three months, to October 1, 2020, at the request of NERC due to impacts associated with the ongoing pandemic.[28]

The NERC Reliability Standards are designed to increase security controls for energy infrastructure supply chain vendors. Specifically, CIP-013-1 requires Responsible Entities[29] to develop supply chain cybersecurity risk management plans. Responsible Entities must develop these management plans for high and medium impact Bulk Electric System (BES) facilities.[30] These risk management plans must include a number of elements, including processes to address:

- Procurement of BES Cyber Systems to identify and assess cybersecurity risk(s) to the Bulk Electric System from vendor products or services resulting from procuring and installing vendor equipment and software, and transitions from one vendor(s) to another vendor(s);
- Notification by the vendor of vendor-identified incidents related to the products or services provided to the Responsible Entity that pose cybersecurity risk to the Responsible Entity;
- Coordination of responses to vendor-identified incidents related to the products or services provided to the Responsible Entity that pose cybersecurity risk to the Responsible Entity;
- Disclosure by vendors of known vulnerabilities related to the products or services provided to the Responsible Entity; and
- Verification of software integrity and authenticity of all software and patches provided by the vendor for use in the BES Cyber System.[31]

Responsible Entities must implement the risk management plans and receive approval for them at least once every 15 months.[32] In addition, implementation of the risk management plans does not require the Responsible Entity to renegotiate or abrogate existing contracts.[33] The severity of penalties for violations of CIP-013-1 varies depending on factors such as the degree to which a Responsible Entity's risk management plan addressed each of the required considerations.[34] Violations of Reliability Standards can result in civil penalties of up to US$1 million per day per violation.[35]

The NERC Reliability Standards, specifically CIP-013-1, share some similarities with the Executive Order. Both attempt to address security concerns associated with equipment necessary to maintain the BES. In addition, both CIP-013-1 and the Executive Order attempt to address these concerns primarily on a going-forward basis; that is, they do not penalize or invalidate transactions with equipment vendors that have already occurred.

While the regulations implementing the Executive Order have yet to be developed, thus far, CIP-013-1 appears to represent a more targeted approach than the Executive Order. CIP-013-1 explicitly cabins scrutiny to larger (high and medium impact) BES facilities. In addition, CIP-013-1 tasks the Responsible Entities themselves with preparing a risk management plan, whereas the Executive Order represents more of a top-down regulatory approach wherein particular vendors and pieces of equipment are either prohibited or allowed by the Secretary. One additional point of comparison between the two regimes is the potential liability for violations. NERC provides a scale with different degrees of severity for violations of CIP-013-1, and violations of Reliability Standards have the potential to result in civil liability.

Despite their differences, the NERC Reliability Standards and the Executive Order do not appear to conflict. Once implemented, they may serve as complementary regulatory tools to improve the security of the bulk-power system in the United States.

Lessons From Last Year's Communications Executive Order

The Executive Order is similar in language and approach to the Communications Order, and the regulatory efforts following the Communications Order may provide a useful guide as to what to expect with respect to the Executive Order.

The Communications Order similarly prohibited transactions involving the "acquisition, importation, transfer, installation, dealing in, or use of any information and communications technology or service" designed, developed, manufactured, or supplied by a foreign adversary that poses "undue risks of sabotage to or subversion of" information and communications technology and services in the United States or that otherwise threatens the resiliency or national security of the United States.

The Communications Order authorized the Department of Commerce, in consultation with other relevant agencies, to make determinations about the transactions that may be prohibited by the Communications Order, in particular whether certain transactions involve information and communications technology or services manufactured or supplied by a foreign adversary or pose an undue risk to US national security. The Communications Order had no enforceable impact on its own. Rather, enforceability only will occur in conjunction with the Commerce Department's rules, which the Communications Order required to be issued within 150 days of the Communications Order, as well as any other actions implementing the Communications Order, but which have not yet been finalized. Similarly, the authors would not be surprised if the Secretary's implementing regulations take longer than the 150 days set forth in the Executive Order.

The Communications Order raised the same potential retroactive concern identified here. However, the proposed rules to implement the Communications Order apply only prospectively.

The Communications Order presented the same concern identified here regarding potential application to pre-existing equipment. However, the proposed rules do not appear to authorize a broad "rip and replace" approach to equipment that was in use before the May 15, 2019, effective date. Rather, they contemplate a case-by-case approach that includes a CFIUS-like governmental consultation process that appears focused on new business transactions that could pose a serious threat to critical infrastructure, the digital economy, or national security, rather than pre-existing lawful transactions. Furthermore, the prospective application of the proposed rules allows the Commerce Secretary to target upgrades, add-ons, and new services — but not core existing uses of equipment. Moreover, as here, the authors do not believe that, as a practical matter, such entities' existing uses of equipment are likely to be viewed as threats to US national security (though that prospect cannot be eliminated entirely).

The Communications Order had the same broad potential jurisdictional sweep, raising the possibility of application outside the United States. However, nothing in the proposed rules discusses extraterritorial application, and the authors believe that the Communications Order is unlikely to be applied outside the United States, primarily because entities outside the United States are unlikely to be considered persons "subject to the jurisdiction of the United States" (and nor is their property subject to US jurisdiction).

The Communications Order presented the same potential penalty risks identified here. The proposed rules set forth potential civil penalties of up to US$302,584 (adjusted for inflation), but did not propose any specific criminal penalties.

Next Steps

The Secretary and others involved in the process of drafting the implementing regulations are likely to seek out input from industry experts on these topics. Industry feedback is likely to be a critical component to ensuring that the implementing regulations and rules are fair, transparent, and not unduly burdensome on those whose businesses depend on the continuing access to bulk-power system equipment supply.

Latham & Watkins will continue to monitor the ongoing developments and implementation of these rulemakings and policies, and is prepared to assist businesses in complying with this Executive Order. If you have questions about this *Client Alert*, including with respect to the types of equipment transactions discussed in the Executive Order, please contact one of the authors listed below or the Latham lawyer with whom you normally consult:

Tyler Brown
tyler.brown@lw.com
+1.202.637.3326
Washington, D.C.

Steven P. Croley
steven.croley@lw.com
+1.202.637.3328
Washington, D.C.

Michael J. Gergen
michael.gergen@lw.com
+1.202.637.2188
Washington, D.C.

Natasha Gianvecchio
natasha.gianvecchio@lw.com
+1.202.637.1079
Washington, D.C.

Jeffrey B. Greenberg
jeffrey.greenberg@lw.com
+1.213.485.1234
Los Angeles

Matthew L. Henegar
matthew.henegar@lw.com
+1.212.906.1814
New York

David L. Schwartz
david.schwartz@lw.com
+1.202.637.2125
Washington, D.C.

Christopher M. Randall
christopher.randall@lw.com
+1.202.637.2189
Washington, D.C.

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Endnotes

1 50 U.S.C. 1701 *et seq*.

2 50 U.S.C. 1601 *et seq*.

3 3 U.S.C. 301.

4 Executive Order, Sec. 1(a).

5 Executive Order, Sec. 1(a).

6 The term "**bulk-power system**" is defined as "(i) facilities and control systems necessary for operating an interconnected electric energy transmission network (or any portion thereof); and (ii) electric energy from generation facilities needed to maintain transmission reliability. For the purpose of this order, this definition includes transmission lines rated at 69,000 volts (69 kV) or more, but does not include facilities used in the local distribution of electric energy." Executive Order, Sec. 4(a).

The term "**bulk-power system electric equipment**" is defined as "items used in bulk-power system substations, control rooms, or power generating stations, including reactors, capacitors, substation transformers, current coupling capacitors, large generators, backup generators, substation voltage regulators, shunt capacitor equipment, automatic circuit reclosers, instrument transformers, coupling capacity voltage transformers, protective relaying, metering equipment, high voltage circuit breakers, generation turbines, industrial control systems, distributed control systems, and safety instrumented systems. Items not included in the preceding list and that have broader application of use beyond the bulk-power system are outside the scope of [the Executive Order]." Executive Order, Sec. 4(b).

7 The term "**foreign adversary**" is defined as "any foreign government or foreign nongovernment person engaged in a long-term pattern or serious instances of conduct significantly adverse to the national security of the United States or its allies or the security and safety of United States persons." Executive Order, Sec. 4(d).

8 Executive Order, Sec. 1(a) (emphasis added).

9 Executive Order, Sec. 1(c).

10 Executive Order, Sec. 1(b).

11 Executive Order, Sec. 1(d).

12 Executive Order, Sec. 2(a).

13 Executive Order, Sec. 2(b).

14 Executive Order, Sec. 2(d)(i).

15 Executive Order, Sec. 2(d)(ii).

16 Executive Order, Sec. 2(d).

17 Executive Order, Sec. 3.

18 Executive Order, Sec. 3(c).

19 Executive Order, Sec. 3(f), (g).

20 Executive Order, Sec. 3(h).

21 50 USCS § 1705. The NEA governs termination of a declared emergency, and does not specify the form of liability for violation of a national emergency. Likewise, 3 USCS § 301 authorizes the President to delegate functions to the heads of departments and agencies, and does not specify liability for violations of delegated functions.

22 Executive Order, Sec. 4(a), (b).

23 *See, e.g.*, *City and County of San Francisco v. Trump*, 897 F.3d 1225 (9th Cir. 2018) (striking down executive order issued by President Trump withholding federal grants from sanctuary cities on ground that Congress had not authorized the President to withhold funding appropriated by the legislature); *Chamber of Commerce v. Reich*, 74 F.3d 1322 (D.C. Cir. 1996) (striking down executive order issued by President Clinton barring the hiring of replacement workers during a strike based on conflict with National Labor Relations Act).

24 Executive Order, Sec. 4(g).

25 Executive Order, Sec. 1(a).

26 Executive Order, Sec. 1(a)(ii)(C) (providing that a finding of "an unacceptable risk to the national security of the United States or the *security and safety of United States persons*" will be a justification for action by the Secretary of Energy to prohibit a transaction involving a foreign adversary's equipment).

27 165 FERC ¶ 61,020 (2018).

28 171 FERC ¶ 61,052 (2020).

29 This term encompasses balancing authorities, certain distribution providers, generator operators, generator owners, reliability coordinators, transmission operators, and transmission owners.

30 High and medium impact BES cyber systems are defined in CIP-002-5, Attachment 1, Sec. 2. Generally, these terms encompass larger network-type facilities. For example, commissioned generation, by each group of generating units at a single plant location, with an aggregate highest rated net Real Power capability of the preceding 12 calendar months equal to or exceeding 1500 MW in a single Interconnection qualifies as "medium impact".

31 CIP-013-1(B)(R1).

32 CIP-013-1(B)(R2), (R3).

33 CIP-013-1, Rationale, Requirement R1.

34 CIP-013-1, Violation Severity Levels.

35 *See* https://www.ferc.gov/enforcement/reliability.asp (last updated March 13, 2020).