UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Standards of Conduct for Transmission Providers) Docket No. RM01-10-000

INITIAL POST-CONFERENCE COMMENTS OF THE NATURAL GAS SUPPLY ASSOCIATION

Pursuant to the procedural schedule in this proceeding, the Natural Gas Supply Association ("NGSA") submits these initial post-conference comments. As discussed below, NGSA supports the revised Standards of Conduct (referred to here as the Standards) proposed by the Commission, as supplemented by the April 25, 2002 Staff Notice, with certain revisions.

I. NGSA SUPPORTS THE COMMISSION'S EFFORTS TO EXPAND AND IMPROVE REGULATION AND OVERSIGHT OF PIPELINE-AFFILIATE RELATIONSHIPS

In the notice of proposed rulemaking ("NOPR") in this proceeding, the Commission correctly notes that, in view of changes in gas and power markets, the Standards need to be revised to deter preferential treatment of affiliates. The revised Standards proposed by the Commission, as supplemented by the Commission Staff's Notice, will go a long way toward minimizing the risk of abusive conduct by a pipeline to favor its affiliates.

The need for effective and comprehensive Standards simply recognizes the fact that pipelines face strong institutional pressures to work in tandem with affiliates to maximize profits. As the D.C. Circuit pointed out when it largely affirmed Order No. 497, "a pipeline has an obvious incentive to favor its own marketing affiliate [because]

profits to the affiliate are profits to the pipeline."[1] However, the current Standards cover only a narrow class of "gas marketing affiliates", which has been defined to exclude many types of affiliates that sell gas, as well as affiliates that are involved in transportation transactions on the pipeline (such as asset managers).

The danger of affiliate abuses is exacerbated by the growing market power exercised by pipelines. Some pipelines have asserted that interstate transportation is competitive, and that there are no market power concerns that could warrant changes in the current Standards.[2] This assertion ignores the realities of current markets. Market power exists throughout the pipeline industry. The issue of whether the market for interstate natural gas pipeline transportation services is competitive has been closed for some time. In recognition of the competitive nature of the gas commodity market, the 1989 Wellhead Decontrol Act deregulated that market. However, because of the substantial market power exercised by pipelines in the transportation market, Congress did not diminish the Commission's regulatory authority over transportation services. The legislative history of the Wellhead Decontrol Act plainly indicates continuing Congressional concern that the competitive commodity market for natural gas could be inhibited or strangled through the exercise of interstate pipeline monopoly power.[3] Therefore, Congress recognized the continuing need for active regulation by this Commission of interstate pipelines. Commissioner Massey has noted that "the Commission's fundamental approach to regulating pipeline companies is still premised

[1] *Tenneco Gas, et al. v. FERC*, 969 F.2d 1187, 1202 (D.C. Cir. 1992).
[2] See the Dec. 20, 2001 "Comments of the Interstate Natural Gas Association of America", pp. 2-9.
[3] "[C]onsumers still have a stake in how FERC handles gas pipeline transportation issues and allocates gas costs. This legislation does not deregulate gas pipelines, and the Committee will continue its oversight of the FERC to ensure that captive residential customers are not disadvantaged, and that the current competitive 'open access' pipeline system is maintained." (H.R. Rep. No. 29, 101st Cong., 1st Sess. 4, *reprinted in* 1989 U.S. Code Cong. & Admin. News. 51, 53 (1989)).

on the notion that, because of economies of scale and barriers to entry, pipeline companies are natural monopolies."[4]

The potential for abusive conduct has increased significantly due to the rapid consolidation of the gas and power industries. Pipelines have become consolidated, through mergers and acquisitions, into a significantly reduced number of corporate entities, as summarized in a recent U.S. Department of Energy study.[5] For example, Williams Companies, Inc. touts the fact that its four "interstate natural gas pipelines deliver[] approximately 16 percent of the natural gas consumed in the United States."[6] El Paso Corporation owns, in part or in whole, twelve interstate pipelines with aggregate capacity of over 31Bcf/d.[7] In addition, convergence mergers between natural gas companies and electric power companies have become common. Recent convergence mergers have involved (1) Koch Industries, Inc. and Entergy Corporation,[8] (2) CMS Energy Corporation and Panhandle Eastern Pipe Line Company, Trunkline Gas Company and Sea Robin Pipeline Company,[9] (3) Dominion Resources Corporation and Consolidated Natural Gas Company,[10] and (4) NiSource Inc. and Columbia Energy Group.[11] In other instances, pipeline-affiliates are purchasing ownership interests in

[4] Transcript of Nov. 13, 1998 speech at annual meeting of Independent Petroleum Association of America, p. 4.
[5] James Tobin, *Natural Gas Transportation-Infrastructure Issues and Operational Trends*, Energy Information Association, U.S. Department of Energy, pp. 16-17 & Table 4 (October 2001)(referred to here as the Tobin Report). The report is available on the EIA's website (http://www.eia.doe.gov/pub/oil_gas/natural_gas/analysis_publications/natural_gas_infrastructure-issue/pdf/nginfrais.pdf).
[6] See the Williams website at "www.williams.com".
[7] El Paso Corporation's SEC Form 10-K for the year 2001, p. 6.
[8] *Entergy Power Marketing Corp, et al.*, 93 FERC ¶61,219 (2000).
[9] *PanEnergy Lake Charles Generation, Inc., et al.* 87 FERC ¶ 62,360 (1999).
[10] *Dominion Resources, Inc., et al.*, 89 FERC ¶61,162 (1999).
[11] *NiSource, Inc., et al.*, 92 FERC ¶61,068 (2000).

power generation plants.[12] Indeed, acquisition of gas-fired power generation via merger or purchase of an ownership interest is now the focus of many pipeline-affiliates.

Mergers and corporate consolidations have decreased the universe of potential pipeline competitors, and have created a complex web of affiliations of energy companies that has led to a much greater risk of abuses.[13] At the same time, the increased size and scope of major interstate pipeline holding companies have increased the potential for abuses and have magnified the potential anti-competitive consequences of conferring advantages on pipeline-affiliates.

Citing these mergers, the U.S. Department of Energy observed that "the restructuring of the gas pipeline industry has brought about a major shift in pipeline ownership and in the business structure of many corporate parent companies. Indeed, there have been several large consolidations of pipeline assets under single corporate umbrellas. The corporate strategies behind these moves have varied, *but the outcomes have been profound*" because pipelines have a greater opportunity to exercise market power (Tobin Report at 17 (emphasis added)).

Concerns about affiliate abuses are very real, as reflected by the numerous enforcement actions that the Commission has had to take in response to affiliate abuses.[14] Indeed, earlier this month, an Administrative Law Judge found that Transcontinental Gas Pipe Line Corporation ("Transco") and its gathering affiliates "have acted in concert with

[12] For example, both El Paso Corporation and Duke Energy Corporation have acquired ownership interests in new power generation plants (*See* April 22, 2002 letter order in Docket Nos. ER02-1773-000, *et al.; see also Duke Energy Mohave, L.L.C.*, 95 FERC ¶61,256 (2001)).

[13] Tobin Report, "Shifts in Ownership of Major Interstate Natural Gas Pipeline Companies Since 1960", Table 4 (Attachment A).

[14] *Natural Gas Pipeline Company of America*, 82 FERC ¶61,038, *order on reh'g*, 82 FERC ¶61,300, *order on reh'g*, 83 FERC ¶61,197 (1998); *El Paso Natural Gas Co.*, 80 FERC ¶61,219 (1997); *Kinder Morgan Interstate Pipeline Co.*, 90 FERC ¶61,310 (2000); *Panhandle Eastern Pipe Line Co.*, 40 FERC ¶61,187, *order approving stipulation*, 50 FERC ¶61,398 (1990)

one another in offering gathering service on the North Padre system in a manner that frustrates the Commission's effective regulation of Transco."[15] As a result, the ALJ recommended that the Commission re-assert jurisdiction over the gathering affiliates.

The bottom line of the public conference is clear: the Commission's basic objectives remain sound, the Staff Notice addresses many of the issues of concern to NGSA in a constructive manner, and the Commission should continue its efforts in this proceeding expeditiously. A comprehensive set of revised Standards that clearly prohibits conduct by a pipeline that gives a preference to an affiliate will go a long way toward deterring abuses.

As discussed below, NGSA supports most aspects of the Commission's proposal, as supplemented by the Staff Notice. The Commission and Staff are proposing a common-sense and balanced approach that provides broad coverage of the various pipeline affiliations and the pipeline activities that are vulnerable to preferential treatment by the pipeline, but excludes those affiliations and activities where there is little opportunity for improper dealings.

II. THE AUTOMATIC IMPUTATION STANDARD SHOULD BE ADOPTED

A key aspect of the current Standards is that a pipeline cannot share with a gas marketing affiliate any operational information or confidential information about a shipper (Standard E). Staff recommends that the Commission find that if a shared employee of a pipeline and affiliate obtains operational information or confidential information about a shipper, the information is treated as if it is automatically transmitted to the affiliate (the so-called automatic imputation standard), thereby requiring the

[15] *Shell Offshore Inc. v. Transco, et al. ("Shell")*, Docket No. RP02-99-000, 99 FERC ¶63,034, mimeo. at 53 (June 4, 2002).

pipeline to immediately publicly disclose the information. Staff points out that the automatic imputation standard "is a clearer standard and easier to implement because it eliminates the opportunity for improperly sharing information." (Notice at 21).

NGSA supports the principle that a pipeline should not share information with its affiliate. But where sharing has occurred, NGSA agrees with Staff that the automatic imputation standard should be adopted. As noted by Staff, the automatic imputation standard is the only effective way of ensuring that the affiliate does not get an unfair advantage due to its access to information.

However, a narrow exception to the automatic imputation standard may be necessary to support system operations. Specifically, NGSA supports the ability of the employees of affiliated companies that are responsible solely for the physical operation of their systems (so-called infrastructure operators) to share operational information when this sharing of information is needed to reliably operate their systems. Infrastructure operators are distinct from operational employees, within the meaning of the current Standards, because an infrastructure operator is not involved with the daily administration of services. As a practical matter, infrastructure operators are in constant communication with interconnected entities, including point operators, gatherers, and local distribution companies, regarding operational conditions on their systems. Frequently a pipeline will ask an interconnecting entity to provide operational support to protect the integrity of the requesting party's system, such as by delivering gas into the other pipeline, taking delivery from the other pipeline, or adjusting pressures on its system. These informal cooperative activities are vital to the efficient operation of the interstate grid, and should be encouraged.

Often, however, there may be situations where it is difficult to distinguish the functions that should and should not be covered by the infrastructure operator exemption. Therefore, the functions that should be covered by the exemption will require further investigation. Once final Standards have been issued, the Commission should consider convening a public conference to address this issue.

But use of the no-conduit rule, even if only for infrastructure operators, still leaves the risk that the sharing of operational information could be used to give an advantage to an affiliate. For example, information about an upcoming constraint on a pipeline could be used by an affiliate to gain an unfair advantage in acquiring capacity that will not be affected by the constraint, or to gain an unfair advantage in the commodity market by engaging in a transaction that exploits changes in prices that could accompany public disclosure of the constraint. Staff notes that "a transmission constraint directly impacts the value of the commodity being transported and preferential access to information about such a constraint could provide a significant benefit to an affiliate trading in a commodity, even if the trade is not using the affiliated transmission provider." (Notice at 5). Hence, the Standards should incorporate express language that allows the limited sharing of operational informational but only when necessary to support a pipeline's operations; access to this information should be restricted to infrastructure operators. As implied by the no-conduit rule, an infrastructure operator cannot give this information to a non-infrastructure operator, and cannot use this information in a manner that favors an affiliate.

At the public conference, Staff asked how it could best ensure compliance with the no-conduit rule. We believe that there are several measures that can improve

compliance. Pipelines should establish periodic training programs to ensure that their infrastructure operators are aware of the restrictions on their ability to share operational information. In addition, each infrastructure operator should be required to sign an annual affidavit that attests to the operator's continued compliance with the no-conduit rule. Penalties for abusing the no-conduit rule should be at a level that is sufficient to deter abuses.

III. AN AFFILIATE THAT "ENGAGES IN OR IS INVOLVED IN" TRANSPORTATION SHOULD BE COVERED BY THE STANDARDS

Staff proposes that the definition of an "energy affiliate" include an affiliate that "engages in or is involved in transmission transactions in U.S. energy or transmission markets." (Notice at 8).

Some parties at the public conference said that the "engage or involved in" language in the definition of an "energy affiliate" is too broad. However, the "engaged or involved in" language is needed to cover affiliates that are indirectly involved in transportation transactions. In view of the new types of players that are constantly emerging in energy industries, any attempt to define with precision the contours of the "engaged or involved in" language would likely leave many of the new types of entities outside the reach of the Standards, even though these entities could be involved directly or indirectly in transportation on the pipeline.

A pipeline's dealings with an affiliate that serves as an agent for a shipper in arranging transportation services provide a good example of the need for the "engaged or involved in" standard. A pipeline has an incentive to favor a shipper that pays an affiliate of the pipeline to serve as agent. Indeed, the current requirement in the Standards that a pipeline that offers a discount to an affiliate must provide the discount to similarly-

situated non-affiliates (the so-called correlative discount requirement) expressly covers "a transportation transaction at a discounted rate in which an affiliated marketer is involved", such as when the affiliate is just an agent of a shipper (18 C.F.R. §161.3(h)(2)). The Commission explained why the Standards must encompass an affiliate that is involved in a transportation transaction:

> When a pipeline is aware that its affiliate is involved in a transportation transaction, [the pipeline] may offer a selective transportation discount to the actual shipper in order to ensure that the shipper does business with the affiliate.[16]

The revised Standards need to go one step further by covering an affiliate-agent regardless of whether the pipeline is aware that the affiliate is involved. A regulatory requirement cannot be effective unless it can be easily administered. It would be too difficult to implement Standards that focus on the subjective awareness of a pipeline. The Commission would be drawn into the morass of having to figure out who knew what and when. In view of the strong incentive for a pipeline to favor an affiliate, the only feasible approach is to simply assume that the pipeline is aware of its affiliate's involvement in transactions.

IV. CLARIFICATION IS NEEDED WITH RESPECT TO CORPORATE RISK MANAGEMENT GROUPS

Several pipelines at the public conference suggested that internal management oversight groups, including corporate risk management groups, should not be covered by the Standards. Parties cited a 1998 opinion letter by the then-General Counsel of the Commission, which provides some guidance about management groups that involve both

[16] Order No. 566, FERC Statutes and Regulations (Preambles) ¶30,997 at 31,068, *order on reh'g*, Order No. 566-A, FERC Statutes and Regulations (Preambles) ¶31,002 at 31,126 (1994).

a pipeline and affiliated entities.[17] However, during the course of this discussion, it was unclear what type of information is reviewed by risk management groups.

Depending on the type of information that is reviewed, there could be a substantial risk that a risk management group could be a vehicle for sharing confidential information that could result in an unfair preference for an affiliate. For example, at a risk management group meeting, a pipeline might share information with an affiliate about plans to expand the pipeline's system. This advance notice of an expansion would give the affiliate an unfair advantage in acquiring gas supplies that are accessed by the expansion. Because an expansion can have a major impact on the price of gas that will be accessed by the expansion, the advance notice could also give the affiliate an unfair advantage in gas commodity markets. Advance notice could also give the affiliate an unfair advantage in securing markets that can be served by the expansion. In view of this risk of abuse, the revised Standards should expressly define what is and what is not permissible conduct by an internal management group in which a pipeline and its affiliates are involved.

V. THE STANDARDS SHOULD APPLY TO AFFILIATED GATHERERS AND PROCESSORS

Commission policy is that a pipeline cannot tie its services to the upstream field services (such as gathering and processing) provided by the pipeline or an affiliate.[18] But as a practical matter, upstream services and transportation services on a pipeline are frequently offered as a single package by pipelines or their affiliates. This *de facto* rebundling of transportation and upstream services allows a pipeline to leverage its

[17] Office of the General Counsel, letter to William G. Von Glahn of The Williams Companies, dated Nov. 12, 1998.
[18] *Colorado Interstate Gas Co.*, 63 FERC ¶61,101 at 61,534, *order granting rehearing in part, and approving settlement*, 64 FERC ¶61,277 (1993).

market power in the transportation market to gain an advantage in upstream markets. This obviously impairs competition. The risk of abuses in dealings between a pipeline and an affiliated gatherer or processor is underscored by the recent ALJ finding (cited above) that Transco and its gathering affiliates are acting together in a way that frustrates the Commission's effective regulation of Transco.[19]

Application of the Standards to affiliated gatherers and processors will establish concrete standards to minimize the risk of a *de facto* tying of transportation and other upstream services. Consequently, it is imperative that the Standards cover affiliated gatherers and processors.

VI. CONDITIONS SHOULD APPLY TO DISCLOSURE OF INFORMATION PROVIDED BY PRODUCERS

Both the proposed Standards and the Staff proposal would bring affiliated producers within the coverage of the Standards. NGSA does not challenge this position. However, information about a producer's production profile is commercially-sensitive and, hence, must be protected. For example, geological studies to support production in a new geographic area entail substantial time, expense and expertise. If a pipeline is required to disclose negotiations with an affiliated producer to expand the pipeline system to access new production by the producer, competing producers could take unfair advantage of this information. For example, competing producers could use this information to determine the location and scope of the affiliated producer's reserves. That would allow the competing producers to compete for drilling rights in the same geographic area in which the affiliated producer is operating. Thus, premature disclosure would put the affiliated producer at a serious competitive disadvantage. For this reason,

[19] *Shell*, 99 FERC ¶63,034, mimeo. at 53.

producers invariably require a pipeline to sign a non-disclosure agreement to preclude the pipeline from disclosing the production information that is provided during the negotiations.

Indeed, in view of the proprietary nature of production profiles, Congress carved an exemption from the public disclosure requirements in the Freedom of Information Act to expressly cover "geological and geophysical information and data, including maps, concerning wells." (5 U.S.C. §552(b)(9)). Congress explained that "disclosure of the seismic reports and other exploratory findings of oil companies would give speculators an unfair advantage over the companies which spend millions of dollars in exploration."[20] This exemption is incorporated in the Commission's regulations (18 C.F.R. §388.107(h)).

Hence, if affiliated producers are covered by the Standards, a pipeline should not be required to disclose potential plans to expand its system to attach production by an affiliated producer. This simply ensures that an affiliated producer is treated the same as a non-affiliated producer in acquiring capacity. But if for some reason the Commission finds that disclosure is required, the pipeline should be allowed to delay disclosure at least until there is a binding agreement between the pipeline and producer.

VII. THE STANDARDS SHOULD COVER A PIPELINE THAT HOLDS CAPACITY ON AN AFFILIATED PIPELINE

The revised version of the Standards proposed by Staff excludes from the definition of an "energy affiliate" a pipeline that holds capacity on an affiliated pipeline

[20] H. Rep. No. 1947, 89th Cong., 2d Sess., *reprinted in* 1966 U.S. Code Cong. & Admin. News 2418, 2428; *see Pennzoil Co. v. FPC*, 534 F.2d 627 (D.C. Cir. 1976)(the court, in remanding a Commission decision requiring disclosure of producers' production data, noted that "one of the major incentives for gas exploration is the opportunity to obtain exclusive knowledge concerning potential gas reserves."); *Mobile Bay Pipeline Projects*, 49 FERC ¶61,006 at 61,022 (1989)("… there is substantial competition among gas producers for information concerning the location, quantities, and deliverability of reserves … . Public disclosure [of this information] would cause substantial harm to the competitive position of the party from whom the information is obtained.").

(for ease of reference, the pipeline that holds the capacity is referred to here as the pipeline-shipper)(Notice at 6). Staff states this exclusion "is because the transmission activities of gas pipelines and power transmission providers are adequately regulated under the open access rules."

NGSA supports the comments by Dynegy, Inc. at the public conference, and NGSA questions the rationale for excluding pipeline-affiliates to the extent that the affiliates hold capacity on each other's systems. Pursuant to the Commission's *Texas Eastern* policy, a pipeline can purchase capacity on an affiliated pipeline (referred to here as off-system capacity). The rationale for this policy is that the affiliated pipeline must make the off-system capacity available to all shippers on a non-discriminatory basis, in accordance with the Commission's open access policies. However, there is the risk that the pipeline-shipper might get an unfair advantage in marketing services that use the off-system pipeline capacity. For example, the pipeline-shipper might have special access to information about the availability of capacity on the affiliated pipeline, as well as information regarding the operational flexibility (such as flexibility in hourly deliveries) and the types of services that this capacity can support. That would give the pipeline-shipper a competitive advantage over other shippers in marketing services that use the off-system capacity. To prevent this abuse, a pipeline-shipper should be treated as an energy affiliate.

VIII. POWER AFFILIATES OF A PIPELINE SHOULD BE COVERED BY THE STANDARDS

Both the proposed rule and the Staff proposal would cover a power generation affiliate of a pipeline. This expansion of the coverage of the Standards is needed. Over 90% of the additional generation capacity that is currently planned is gas-fired. The U.S.

Government has noted that "[t]he major factor in the anticipated heavy increase in natural gas demand in the next 20 years is the continuing growth in gas-fired power generation plants."[21] The power generation load is expected to be a major component of overall demand growth. It is anticipated that between 4.3 and 5.6 Bcf/d of new pipeline capacity will be needed to serve just the gas fired power plants that will be installed during 2002.[22] Moreover, as noted, convergence mergers are escalating. As a result, there is an increasing level of affiliations between gas and power companies.

This, in turn, introduces the risk that a pipeline will give preferential treatment to a power generation affiliate that is interconnected with the pipeline, as noted by the Federal Trade Commission in its December 20, 2001 comments in this proceeding. For example, the gas needs of power generators fluctuate widely throughout the day as generation ramps up and down in response to power demand. This can put a big burden on a pipeline's resources. Hence, there is a risk that a pipeline might give an affiliated generator advance notice of operational conditions that could affect service for the generator. That would give the generator an unfair advantage in acquiring alternative services on the affiliated pipeline or another pipeline. Alternatively, a pipeline might be tempted to devote more resources to serving a generator-affiliate than a non-affiliate even where both shippers receive service pursuant to the same Rate Schedule. The best way to minimize the risk of this abusive conduct is to apply the Standards to power generation affiliates.

IX. AFFILIATED REGULATED ENTITIES IN THE GAS AND POWER INDUSTRIES SHOULD BE COVERED BY THE STANDARDS

As pointed out in the Staff Notice, pipelines have argued for an exemption for

[21] Tobin Report, p. 22.
[22] Tobin Report, p. 22.

affiliated pipelines from the definition of an "energy affiliate". Pipelines asserted that the Standards "would restrict the joint operations of jurisdictional transmission facilities and would mandate unnecessary duplication of jointly operated facilities." (Notice at 6). For this reason, Staff proposes that an affiliated pipeline and power transmission company not be treated as energy affiliates if both companies are regulated by the Commission.

There is no justification for exempting regulated affiliates that operate in different industries. Unlike affiliated pipelines, an affiliated pipeline and power transmission company do not share joint operations. Thus, there is no need for an exemption. Staff says that it does not "appear that communications between regulated gas transmission providers and regulated electric transmission providers would be a problem." (Notice at 6). But Staff overlooks the risks of abusive dealings between an affiliated pipeline and power transmission company. As noted, there has been a rapid convergence of pipelines and power transmission companies. In addition, the rapid growth of gas-fired power plants means that there can be a close commercial nexus between the pipeline's delivery of gas to a power plant, and the plant's delivery of power into the transmission company's facilities.

This could lead to abuses. For example, a power transmission company would have an incentive to offer more favorable interconnection terms and other terms of service for a plant that agrees to purchase gas transportation service from a pipeline affiliated with the power transmission company. Likewise, a pipeline that is competing to serve a power plant could arrange for its affiliated power transmission company to coordinate with the pipeline (via a special sharing of information between the two entities) the gas transportation service and power transmission service that the plant uses

if the plant agrees to take service from the pipeline. In view of the risk of these and other abuses, affiliated pipelines and power transmission companies should be covered by the Standards.

X. THERE MUST BE COMPREHENSIVE MONITORING OF PIPELINE CONDUCT AND EFFECTIVE ENFORCEMENTACTION IN RESPONSE TO VIOLATIONS OF THE STANDARDS

A crucial component of effective implementation of the Standards is comprehensive monitoring by the Commission of pipeline dealings with affiliates. This will allow the Commission and shippers to ensure that pipelines are abiding by the Standards. Commissioner Brownell has pointed out that "strengthening the Commission's market monitoring and enforcement capabilities must be a top priority. As markets change, market monitoring and enforcement capabilities become an even more critical piece of the regulatory puzzle."[23] In addition to the proposals in the NOPR and the Staff Notice, NGSA urges the Commission to enhance the reporting requirements adopted in Order No. 637 so that industry participants can analyze reported data in a user-friendly, standardized format. As NGSA pointed out in its December 20, 2001 comments in this proceeding, pipelines should be required to report actual usage and non-usage of scheduled capacity. Where energy affiliates hold pipeline capacity, the Commission should require the pipeline to file the following information:

1) The amount of capacity held by others that the affiliate manages[24];
2) The amount of capacity released by each affiliated firm shipper each month by term of release; whether the capacity is sold for more than the maximum rate; and whether it is recallable, with capacity releases by an affiliate separately identified;
3) The amount of capacity released and not recalled during peak periods (*e.g.*, the consecutive three-day peak or some other measure of peak demand periods);

[23] Sept. 20, 2001 prepared testimony before the Subcommittee on Energy and Air Quality, of the Committee on Energy and Commerce, U.S. House of Representatives.
[24] As used in this section, the term "capacity" includes mainline capacity and capacity at receipt and delivery points (including at points of interconnection with other interstate pipelines).

4) The amount of secondary firm capacity at selected delivery points;
5) The amount of secondary firm capacity interrupted each day, and the point(s) of interruption;
6) The volume of interruptible transportation that was nominated but did not flow; and
7) The amount of the affiliate's primary firm transportation that was nominated and scheduled for the beginning of the day and did not flow (due to re-nomination or any other factor). This information is necessary to determine whether a dominant affiliate capacity holder deliberately is bumping competitor deliveries.

The Commission should also establish expeditious enforcement actions when there are signs that a pipeline might have violated the Standards. Last but not least, the Commission must be willing to impose substantial penalties on any pipeline that violates the Standards. The Standards will not be effective without a strong, highly visible and vigilant enforcement program. Penalties should be developed that are sufficient both to compensate those injured by violations of the Commission's regulations and to deter future violations. Even under the new rules proposed in the NOPR, affiliate transgressions will remain difficult to detect. In testimony on the need for effective enforcement of Commission policies in power markets, Commissioner Massey noted:

> Refunds alone are not a sufficient deterrent against bad behavior. Simply giving the money back if you are caught is not enough. The consequences of engaging in prohibited behavior must be severe enough to act as a deterrent.[25]

This principle applies with equal force to gas markets. Thus, there must be vigorous enforcement of the Standards.[26]

[25] Sept. 20, 2001 prepared testimony before the Subcommittee on Energy and Air Quality, of the Committee on Energy and Commerce, U.S. House of Representatives.

[26] A recent General Accounting Office ("GAO") report on the Commission's regulatory programs recommends that Congress "consider providing FERC with the appropriate range of authorities to levy civil penalties against market participants that engage in anticompetitive behavior and violate market rules." ("Energy Markets: Concerted Actions Needed by FERC to Confront Challenges That Impede Effective Oversight" (June 2002)). In his comments on the report, Chairman Wood agreed with this suggestion and asked Congress to "increase civil and criminal penalties under the Federal Power Act (FPA) and the Natural Gas Act (NGA)." (*see* Appendix III of the report).

XI. THE D.C. CIRCUIT'S *DOMINION RESOURCES* DECISION DOES NOT UNDERMINE THE BASIS FOR THE NOPR

The D.C. Circuit vacated and remanded case-specific Standards imposed by the Commission as a condition for approval of a convergence merger. The Standards covered all "energy affiliates" of the merging companies. Significant here is that the court clarified that it was not prejudging the issues in this rulemaking proceeding:

> Of course, if the Commission has a general case for broader restrictions, it can make that case in the rule-making that is has launched to expand the generic Standards of Conduct to "govern the relationships between the transmission providers and all of their energy affiliates, not just those engaged in marketing or sales functions." [*Dominion Resources, Inc. v. FERC*, 286 F.3d 586, 593 (2002)]

Therefore, the *Dominion* decision leaves the door wide open for the Commission to adopt improved Standards in this proceeding.

XII. CONCLUSION: COMPLIANCE SHOULD NOT BE IN THE EYES OF THE BEHOLDER

During the public conference, a number of participants, including the Ad Hoc Marketers Group, complained that their own operations were consistent with current guidelines. However, in the course of explaining those operations -- particularly in the context of "risk management" groups -- they raised more questions than they answered. This underscores a central problem that the proposed rule addresses and would eliminate: compliance with the Commission's regulations governing utility-affiliate relationships should not be left to the eye of the beholder. Decisions should not be left in the dark, without benefit of clear rules and standards, subject only to the risk of an infrequent audit or the complaint of the rare customer willing to risk loss of regulated service at reasonable rates in exchange for potential relief after years of litigation under Section 5 of the NGA.

Let the rules be stated clearly and applied fairly. Let the regulatory solution be tailored to the scope of the problem. And let the industry and all those who depend on it have confidence that the market rules have been set by the Commission and will be enforced.

For the reasons stated above, NGSA whole-heartedly supports the proposed rule and the Staff Notice, with the limited revisions outlined above.

Respectfully submitted

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