

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

**Standards of Conduct for
Transmission Providers**

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Docket No. RM01-10-000

**INITIAL COMMENTS OF PAN CANADIAN ENERGY SERVICES INC.
ON NOTICE OF PROPOSED RULEMAKING**

In connection with the Commission's invitation for public comment contained in the September 27, 2001 Notice of Proposed Rulemaking (NOPR) issued in the above-captioned proceedings,¹ Pan Canadian Energy Services Inc. (PCES) hereby submits its initial comments.

EXECUTIVE SUMMARY

PCES commends the Commission for its efforts in the NOPR both to simplify the Commission's current panoply of regulations governing the standards of conduct between gas and electric utilities and their affiliates, and to revise those regulations such that they conform to current market realities.

In this regard, PCES supports, subject to a few modifications discussed below, the majority of the specific changes to the Commission's regulations that are proposed in the NOPR. PCES does not, however, support the adoption of more draconian "structural" remedies (such as divestiture and divorcement), except in the most extreme case of a finding and decision of affiliate-transmission provider misconduct.

COMMUNICATIONS

Communications and correspondence concerning these Initial Comments should be directed to the following:

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¹ *Standards for Business Practices of Interstate Natural Gas Pipelines*, 96 FERC ¶ 61,334 (2001). In a subsequent Notice of Extension of Time, the Commission extended the due date for comments until December 20, 2001.

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BACKGROUND

On September 27, 2001, the Commission issued a NOPR proposing a comprehensive revision to its current regulations governing the conduct and relationships between regulated gas and electric utilities and their marketing affiliates.

INITIAL COMMENTS

As one of the nation's major energy marketers, PCES operates in numerous states and on nearly every major interstate pipeline in the nation. PCES competes vigorously in the nation's gas and electric markets with all manner of market participants, including marketersthatareaffiliatedwithinterstategas and electric transmission providers. Consequently, PCES has a strong interest in rigorous and effective affiliate codes of conduct, and relies heavily upon the Commission's regulatory oversight to ensure that PCES is able to compete fairly with affiliated marketers.

From this perspective, PCES offers the following comments upon the NOPR.

GENERAL COMMENT UPON THE INFORMATION POSTING REQUIREMENTS OF THE PROPOSED UNIFORM STANDARDS OF CONDUCT

Where the Commission has required the posting of certain information on a transmission provider's OASIS or Internet Website, PCES strongly encourages the Commission also to require transmission providers to install, operate and maintain an internet list service for the distribution of posted information updates and new postings. In this day and age of email and Internet communications, it is very inexpensive for transmission providers to employ the use of list service for all the informational posting updates, notices and announcements required under the proposed Standards of Conduct. Indeed, it is quite likely that all transmission providers subject to the NOPR's proposed regulations rule already use such list services for investor relations, marketing activities and possibly other functions where they

interface with stake-holders in their business activities. ²

COMMENTS UPON SPECIFIC REGULATORY PROVISIONS.

Definitions (New §358.3)

In this regulation, FERC proposes, among other things, to broaden the scope of its affiliate regulations by providing new definitions of (i) “Transmission provider” (FERC-regulated interstate gas companies and electric utilities that own, operate or control interstate gas and/or electric transmission facilities), and (ii) “energy affiliate” (any affiliate of a transmission provider that (a) engages in or is “involved in” transmission transactions, (b) “manages or controls” transmission capacity, (c) “buys, sells, trades or administers” gas or electricity, or (d) “engages in financial transactions related to the sale or transmission” of gas or electricity.)

PCES appreciates and supports the Commission’s effort to close regulatory gaps that have developed as the energy markets have evolved in the years since Order No. 497 was promulgated. In particular, PCES supports the Commission’s decision to define “energy affiliate” in such a manner that affiliated transmission providers are subject to the full measure of the Standards of Conduct regulations. As recognized by the Commission, in this age of mergers, a transmission provider is very likely to be affiliated and interconnected with another transmission provider. There is sufficient potential for sharing of operating and market information among affiliated transmission providers where one transmission provider may gain an advantage for scheduling, nominations, operations, and market expansion to the detriment of non-affiliated market participants. To the extent that affiliated transmission providers share non-public operating information or market data among themselves, they should be required to make that same information available to all market participants on the same basis.

² The list service to be adopted by the transmission providers would allow market participants monitoring the transmission provider’s posting to subscribe and unsubscribe from the service at their will. In the event that a subscriber fails to notify the transmission provider of a change in email address and such email address is returned undeliverable, the transmission provider would be free to remove the email address from the subscription list.

PCES does, however, recommend that the Commission consider further expanding its proposed “Definitions” provision to include in the definition of “Transmission Provider” the major intrastate gas transmission facilities to the extent they provide FERC-regulated NGPA Section 311 services. These Section 311 companies have significant impacts on the wholesale energy markets, providing large quantities of transportation capacity used in interstate commerce, as well as fuel supplies for many wholesale electric generators. Many of these Section 311 companies have marketing affiliates that can easily engage in conduct violative of the proposed code of conduct. To eliminate this potential threat to the nation’s energy markets, the Commission should expand the definition to cover these major Section 311 service providers.³

Identification of Affiliates (New § 358.4(b))

FERC proposes that electric and gas transmission providers post (i) the names and addresses of their sales and marketing units and their energy affiliates, (ii) a complete list of shared facilities and their addresses, and (iii) an organizational chart of employees and their job descriptions for the transmission provider and its energy affiliates. This information must be posted on OASIS or the gas utility’s website (as applicable) and must be updated within 3 business days of any change.

PCES supports the Commission’s proposal to require transmission providers to post their potential merger partners on the OASIS or Internet Website. This posting, however, should be the same type of notice that is now required by the SEC for similar activities. Moreover, in addition to posting the notice of potential merger partners, the transmission providers should be required to distribute this notice via its internet list service. (See PCES’ general comment above regarding the use of a list service as an

³ It may be appropriate to limit the application of affiliate conduct rules to “major” (emphasis added) intrastate pipelines offering NGPA Section 311 services, since there are many small intrastate pipelines and storage operators (e.g., those providing service at market-based rates) offering NGPA Section 311 services whose operations have little or no significant impact on the interstate markets. At this time, PCES has no specific recommendation for a definition of “major” intrastate pipeline, but such a definition could be based on total throughput, total peak day demand, or the percentage of intrastate versus interstate quantities transported.

additional means of disseminating all posted information.)

Transfer of Employees (New §358.4(c))

This proposed regulation parallels the existing electric standard of conduct allowing transfers of employees between (i) the transmission provider and (ii) its marketing or sales function or its energy affiliate only if the Commission's standards of conduct are not circumvented. (This provision is generally interpreted as prohibiting "cycling" of employees between the affiliate and the parent utility, and to require certain safeguards be implemented to prevent the disclosure or use of transmission-related information by transferred employees). The Commission proposes to require notices of all job transfers be posted on the website or the OASIS.

The information posted on transfer of transmission provider employee to its affiliate must be sufficient for a third party to determine whether the transferred employee had access to information in his or her former position that would be of competitive value in the new position. At a minimum, then, the information should include:

1. The name of employee,
2. The title and description of job function of employee at transmission provider (the employee's title alone may be sufficient if the transmission provider has included position titles in its posted organizational chart),
3. The time that the employee was at his or her last position at transmission provider (if time is very short— for example, less than 6 months— then prior titles and job descriptions should be required until one year of service is covered),
4. The transferred employee's new title and name of affiliate, and
5. The transferred employee's prior employment history (titles and service periods) with any transmission provider and/or its affiliates for the past 5 years.

Written Procedures (New §358.4(e))

This proposed regulation imposes the existing requirement that gas and electric transmission providers file with the Commission their procedures for implementing the Commission's standards of conduct.

The Commission should clarify that the transmission provider's explanation of measures it uses to implement the standards of conduct should be in the form of a Compliance Plan that is subject to the review and comments of market participants and subsequent approval of the Commission. Once approved, the Plans should be posted on the transmission provider's OASIS or Internet Website.

Discounts (New §358.5(d))

This new provision sets forth a consolidated procedure for gas and electric utilities to handle discounts. In the new regulation, utilities will be required to post all discounts on the OASIS or its website, as applicable, *contemporaneously with the offer* of the discount.

This proposed regulation is problematic. PCES agrees that any time a transmission provider "offers" a discount, it should post the relevant information related to such offer on its OASIS or Internet Website. In PCES' interpretation of this requirement, however, these "offers of discounts" are *general* expressions by the transmission provider of the value of its services, as opposed to specific discount offers that are solicited by individual market participants. (And, as explained earlier, these generalized discount offers should be disseminated *via* the transmission provider's internet listserv for Standards of Conduct information.) PCES also agrees that transmission providers should post and send information on discounts granted to their affiliates at the time the discounts are agreed to between the transmission provider and its affiliates.

However, PCES adamantly opposes the requirement that the transmission service provider "announce" all individually-negotiated discounts to all potential customers *via* OASIS or Internet *at the time* the discount offer is made. The purpose of the posting and sending of information on affiliate

transactions to monitor and uncover affiliate abuse on or after the discount is used. The posting of discounts is simply beyond the scope of the Standards of Conduct requirements and this proceeding, and it intrudes into the area of market monitoring of highly-sensitive commercial information. *all*

At first blush, it may seem fair from a market perspective to require transmission providers to reveal both affiliate and non-affiliated discounts. However, requiring universal disclosure of such discounts at the time they are offered goes beyond the standards of conduct venue, and will very likely lead to a significant decrease in the willingness of transmission users or transmission providers to negotiate discounts at all. If the Commission's overarching goal is to ensure parity in the discount treatment of affiliates and non-affiliates, the better alternative would seem to be to retain the current requirement where discounts granted to affiliates and non-affiliates are posted no later than the time of the first nomination under a transaction.

ADDITIONAL POLICY CHANGES: REQUEST FOR GENERAL COMMENTS

In the NOPR, the Commission invites interested parties to comment upon a number of more general affiliate conduct issues. PCES notes that the bulk of these issues were fully ventilated in the Commission's recent generic inquiry into affiliate relationships (Docket No. PL00-1), and most were deemed inadvisable as general regulatory requirements by the majority of the industry participants. In considering additional generic affiliate remedies, the Commission must be extremely careful to address only general, market-wide affiliate problems so as to avoid creating additional unwarranted and unnecessary administrative burdens for all industry participants.

As such, PCES concurs with the Commission's observation in the NOPR that most of the additional "policy changes" upon which the Commission seeks comment are more appropriate as targeted remedies to specific instances of affiliate misconduct, not as industry-wide rules. Below, PCES provides the Commission with comments on several of the Commission's specific proposals.

1. **Capacity Restrictions on Affiliates** : Should the Commission limit the amount of capacity an affiliate can hold on its affiliated transmission provider?

Comment: There should be no limit on the amount of capacity (by volume or percentage) an affiliate can hold on a transmission provider. As long as the means to obtain the capacity is fair and non-discriminatory for all market participants, there should be no preset limitations for any market participant. Nevertheless, PCEC does believe a limitation may be appropriate where a transmission provider's employee is transferred to an affiliate and that former employee is able to use his or her knowledge of the transmission provider's integrated system operation to the detriment of other market participants.

2. **Size Restrictions on Capacity Awards** : Should the Commission require capacity to be awarded to numerous different shippers in hopes of minimizing the potential for an affiliate to acquire and exercise market power over large blocks of capacity?

Comment: The Commission should not revise its capacity allocation policies to impose artificial restrictions on the size of capacity awards. Again, as long as capacity allocation process is fair and non-discriminatory for all market participants, there should be no need for preset allocations for any market participant.

3. **IT Bumping** : Should the Commission revise its policies regarding IT bumping?

Comment: The Commission's IT bumping policies are not germane to the Commission's regulation of pipeline/affiliate relationships. The current policies, now reflected in the GISB standards, were developed over time with input from all market participants, and they are not unfair or biased in favor of pipeline affiliates.

4. **Profit-Sharing Transactions** : Should transmission providers be banned from entering into profit-sharing arrangements with their energy affiliates and with non-affiliates?

Comment: Absolutely not. PCEC strongly opposes the suggestion that the Commission

should place limits on capacity arrangements between market participants and transmission providers. Any such limitation will serve only to diminish the marketability of capacity, not enhance it. Furthermore, as long as the transmission provider negotiates these capacity arrangements in a fair and non-discriminatory manner with all participants, there is no need to place selective restrictions upon entering into these arrangements with the provider's affiliates.

5. **Call Options** : Should pipelines be limited in selling call options on capacity to their energy affiliates?

Comment: Again, the Commission should not limit a pipeline's ability to sell call options to its energy affiliate, for the same reasons stated in item number 4 above.

6. **Disgorgement of Profits** : Should the Commission require pipelines to disgorge revenues paid by affiliated marketers in excess of the pipelines' opportunity costs?

Comment: The disgorgement options should be one of several penalty options to be invoked only upon a finding by the Commission (after notice and hearing) that there was affiliate abuse underlying the revenues for a specific transaction. For instance, if the price paid by the affiliate to the transmission providers significantly exceeded the reasonable market value of the service at the time of the auction such that other market participants were economically precluded from participating in the service auction, then the Commission could make a finding that the transmission provider's auction was a nullity and that the affiliate's winning bid was a sham transaction. In such a case, the penalty for a finding of a sham transaction would be disgorgement of profits by the affiliate.

7. **Physical Separation** : Should the Commission require that transmission providers and their affiliates be physically separated?

Comment: Requiring the geographic (physical) separation of transmission providers and their energy should also be one of several penalty alternatives for the Commission upon a finding

of affiliate abuse under these Standards of Conduct. This alternative should be imposed as soon as possible if any market participant furnished credible information that improper communications or meetings have occurred between affiliate employee(s) and transmission provider employee(s).

8. ***Ban on Interconnection*** : Should pipelines be banned from interconnecting with affiliated merchant generators?

Comment: PCEs oppose a general ban on interconnections between pipelines and their generation affiliates. While this ban might be a reasonable remedy for especially egregious violations of the Commission's standards of conduct, so long as these interconnections are negotiated and awarded in a fair and non-discriminatory manner, there should be no limitation or prohibition on interconnection with any market participant, including the pipeline's generation affiliates.

9. ***Structural "Remedies"*** : Whether the Commission's "behavioral remedies" (standards of conduct, complaint procedures) are sufficient to limit anti-competitive behavior, or should the Commission instead require structural remedies, such as (i) requiring transmission providers to spin-off their affiliates (divestiture) or (ii) prohibiting affiliates from doing business on their affiliated pipeline (divorcement)?

Comment: At this time, there is no evidence that the Commission's current enforcement protocol—its "behavioral remedies"—is inadequate to limit the anti-competitive behavior of transmission providers in favor of their energy affiliates. Structural remedies should thus be imposed only as penalties for specific instances of particularly egregious violations of the Commission's affiliate regulations.

10. ***Public Utility Codes of Conduct*** : Should the Commission codify its codes of conduct applicable to power sales by public utilities and their marketing affiliates?

Comment: In the absence of a significant number of formal complaints alleging the abuse of these codes of conduct, the Commission need not codify them. Moreover, in the event there are such abuses, the state regulatory agency with jurisdiction over the investor-owned public utility may take steps to address such abuse in an appropriate proceeding before that agency.

CONCLUSION

PCES appreciates the opportunity to provide the Commission with its views upon the Commission's proposed changes to its regulations governing affiliate standards of conduct, and urges the Commission to condition the regulations in a manner consistent with PCES' comments above.

Respectfully submitted,

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Dated at Houston, Texas: December 20, 2001