

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

Quarterly Financial Reporting and Revisions to the Annual Reports) Docket No. RM03-8-000

**COMMENTS OF THE INDUSTRY COALITION
ON PROPOSED REVISIONS TO THE ANNUAL REPORTS**

Pursuant to the Notice of Proposed Rulemaking ("NOPR") issued by the Federal Energy Regulatory Commission ("Commission" or "FERC") in the above-captioned docket on June 26, 2003, the American Public Gas Association ("APGA"), the Canadian Association of Petroleum Producers ("CAPP"), the Independent Petroleum Association of America ("IPAA"), the Natural Gas Supply Association ("NGSA"), and the Process Gas Consumers ("PGC"), collectively the "Industry Coalition," files these initial comments regarding the Commission's proposals in this proceeding to require quarterly financial statements (Form 3-Q), to amend current annual financial statements (Forms 1, 1-F, 2, 2-A, and 6) for jurisdictional companies, and to require officer certification of these reports consistent with the Sarbanes-Oxley Act of 2002.

The Industry Coalition represents both major and independent suppliers that produce natural gas in the United States and Canada; over 594 municipal and other publicly owned local distribution systems in thirty-six states; and industrial companies employing millions of people and consuming over half a trillion cubic feet of gas annually.

The NOPR is one more step in a series of Commission actions¹ intended to enhance public confidence in the industry through improved transparency. The Commission is proposing to implement quarterly reporting for several reasons, one of which is to aid in evaluating the adequacy of existing traditional cost-based rates.² The Commission also encouraged those commenting to address any related matters or alternative proposals that parties may wish to raise. In response to this opportunity, the Industry Coalition urges the FERC to take steps to improve the quality of the existing information contained in annual Form 2 reports, which are the primary source for evaluating the adequacy of cost-based rates. Given the fact that gas pipelines are no longer required to file Section 4 rate cases on a regular basis, it is important that this threshold matter be addressed as soon as possible. This NOPR is an appropriate proceeding to implement the necessary improvements to the annual Form 2. If quarterly Form 3-Q financial statements are required to be filed with the Commission, they should be made consistent with the revisions to Form 2, where applicable.

A. Information Contained in the Annual Form 2 Reports Is Critical to Pipeline Customers.

For over a decade now, if a pipeline company does not make a voluntary Section 4 filing, the only recourse available to shippers seeking pipeline rate changes has been to file a Section 5 complaint. To compile a Section 5 case, the primary information available to customers is publicly available Form 2 data. Parties considering a Section 5

¹ Policy Statement on Natural Gas and Electric Price Indices, Issued July 24, 2003; Standards of Conduct for Transmission Providers NOPR, issued September 27, 2001; and reporting requirements in Order No. 637, issued February 9, 2000.

² NOPR at 3.

complaint must have a high level of confidence that a Section 5 complaint is indeed warranted. To provide that level of confidence that rate changes are needed, as well as to provide an adequate evidentiary showing to the Commission in support of these changes, pipeline customers and pipelines alike must be assured that Form 2 data allows pipeline customers to accurately assess the financial situation of each pipeline.

The Industry Coalition has a substantial interest in the quality of data provided in Form 2 reports. In fact, Form 2 data is used exclusively to develop an annual NGSA Pipeline Cost Recovery Study, which provides an annual assessment to the NGSA membership regarding the average rate of return on equity over a five-year period that many of the major natural gas pipelines have earned. In the process of developing this study and performing this analysis over the past four years, NGSA has become aware that there are deficiencies and lack of necessary detail in the Form 2 report, which make it difficult to assess whether a pipeline's rates are just and reasonable. As both pipeline customers and diverse segments of the natural gas value chain, the Industry Coalition is interested in ensuring that the non-competitive aspects of the natural gas industry are adequately regulated to ensure just and reasonable rates, and terms and conditions of services.

B. Changes to Form 2 Reports Are Critical To Determine Whether Pipeline Rates Are Just and Reasonable.

Only minimal changes to Form 2 reporting are needed in order to substantially improve the industry's ability to accurately assess this data and replicate the pipelines' costs of service for ratemaking purposes. Many of the needed improvements only involve creating breakouts that merely separate cost-of-service components from non-

cost-of-service components, rather than forcing the use of subjective judgment to determine what portions relate solely to the jurisdictional rates of the regulated companies. The rationale for improvement of the Form 2 is the same as the Commission points out for Form 3-Q in the NOPR; namely, that it will provide the public with “transparency of financial information from FERC-jurisdictional entities at a level of detail that is not obtainable from other sources.”³

Other improvements to Form 2 would simply require the pipeline to identify (or check) those items that it would consider as rate base components for ratemaking purposes and specify the individual cost components using terminology consistent with the headings identified in the Commission’s regulations instead of using the company’s own terminology. In many cases, the necessary information is already there, but assumptions have to be made as to whether it should be used for ratemaking purposes. This is often the problem when forced to rely solely on an accounting report for ratemaking purposes.

Attached hereto is a one-page list that documents the improvements that need to be made to Form 2 in order for parties to accurately and confidently assess pipeline rates, along with a brief explanation for why those changes are required. Additionally, the Industry Coalition requests the Commission to schedule a technical conference to further explore the proposed changes if the Commission believes further dialogue is necessary.

³ NOPR at 2.

C. If the Commission Adopts Quarterly Reporting, Form 3-Q Information Should Be Consistent with the Information Provided in Annual Reports.

Given that the information proposed to be collected in Form 3-Q is not as detailed or comprehensive as that provided in Form 2, the Commission should continue to ensure that the information filed in those reports complies with the same reporting format as the schedules used in the annual reports. It appears the proposals in this NOPR are consistent as proposed, however, if quarterly Form 3-Q financial statements are required to be filed with the Commission, they should be made consistent with the revisions to Form 2, where applicable.

CONCLUSION

The Industry Coalition requests the Commission to adopt the requested improvements to Form 2 Reports as shown in the attachment. These improvements will substantially improve the quality of the information provided in those reports, which are the primary source of information available to industry participants for purposes of assessing the adequacy of natural gas pipeline rates.

Respectfully Submitted,

American Public Gas Association
Canadian Association of Petroleum Producers
Independent Petroleum Association of America
Natural Gas Supply Association
Process Gas Consumers

ATTACHMENT

***Suggested Changes to the FERC Form 2:
Information Needed to Evaluate Pipeline Rates***

Rate of Return Computation

A calculation of the pipeline's earned return on equity investment for the utility based on a predetermined formula. This would exclude non-utility transactions.

Rate Base Information

- Identification of which components of deferred tax and regulatory asset and liability balances are included in the pipeline's rate base for ratemaking purposes (Account Nos. 182, 190, 254, 282 and 283).
- A detail page for miscellaneous current and accrued assets (Account No. 174), similar to that included for miscellaneous current and accrued liabilities (Account No. 242), so imbalance receivables as well as payables can be identified.

Cost and Revenue Information

- Detail concerning gas purchase and sale accounts, particularly Account Nos. 480-484, 488, 495, 805, 806 and 813. If gas purchases and sales include imbalances and/or fuel gas retained from shippers, the detail should include volumetric and dollar reconciliation with the accounts in which these activities are recorded. Any revenues not associated with the pipeline's cost of service should be identified.
- List of breakouts for Account 495 stated in the same manner as the regulations so that reviewer does not have to use personal judgment to determine what is meant by the pipeline's terminology.
- A calculation of the pipeline's current effective overall state income tax rate.
- Identification of any costs recorded in Account Nos. 750-798 that are included in the pipeline's regulated cost of service.
- Detail concerning assigned and allocated corporate administrative (shared service) costs, including the amounts charged by FERC account number.
- Identification of revenues associated with negotiated rate contracts.
- Identification of costs and revenues associated with at-risk facilities, given that the Commission requires that these costs be kept separated from all other jurisdictional facility costs. At a minimum, a listing of the certificate proceedings (and related docket numbers) where facilities were put at risk.

Capital Structure Information

- Information concerning the company or entity whose capitalization is reflected on page 218 of the Form 2, and an indication of whether that company's capitalization is used by the pipeline for ratemaking purposes. If another company's or a hypothetical capitalization is used for rates, a statement of that company's or the hypothetical debt/equity capitalization ratio.

*Suggested Changes to the FERC Form 2:
Explanation of Why Additional Information is Needed*

As the Commission has noted in its Docket No. RM03-10 Notice of Proposed Rulemaking (NOPR) at page 2, one of the reasons timely financial and operating information is needed from pipelines is to enable the Commission to accurately evaluate the adequacy of a pipeline's existing rates. It is this same evaluation that prompts the reporting changes recommended on the preceding page.

In the current reporting format of the FERC Form No. 2, several categories of information contain components that are not related to or reflected in a pipeline's cost of service and rates. For instance, components of deferred taxes and regulatory assets and liabilities are recorded for book accounting purposes, but are not included in the rate base on which a pipeline's return and income taxes are calculated for cost of service purposes. However, even where some pipelines report detailed breakouts, there is no way to determine which components would be included in rate base. Thus, the pipeline's current rate base cannot be calculated, which prevents an accurate assessment of whether the pipeline's current rates are adequate, and whether the pipeline is over or under-recovering on a current cost basis.

Similarly, there are components of revenues and costs that are included in reporting and calculating the pipeline's net operating income that would not be included in the pipeline's cost of service and therefore would not factor into the analysis of a pipeline's earnings under its existing rates. For example, the revenues reported on pages 300-301 and carried over to page 114 include revenues from sales of gas, which for many pipelines is a significant source of revenues. Costs for purchases of gas are also included in operating expenses on pages 319-320 and 114. One difficulty is that there is no supporting information to determine the nature and basis of these activities. But in addition, purchases and sales of gas, such as cash outs, do not impact the return a pipeline earns from its approved rates. Discrepancies between costs and revenues for purchased gas could reflect temporary misalignments between imbalance payables and receivables, or over-recovery of fuel that must be returned to shippers in a future fuel adjustment filing. As it stands now, there is no way to accurately remove these costs and revenues in order to assess whether the pipeline's rates themselves continue to be just and reasonable.

The suggested changes can be implemented with only a minimal amount of additional reporting requirements. For the most part, items related to the regulated rate base or cost of service can be identified with a simple mark on the appropriate page in the Form 2. A few additional pages may be needed, to reconcile items such as gas purchases and sales for purposes of distinguishing them from the costs and revenues associated with a pipeline's underlying rates, but the additions would be modest. The additional information is needed to enable the Commission and other interested parties to accurately evaluate the pipeline's operations as they relate to that pipeline's currently effective cost of service and rates.

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