

TO: GISB Board of Directors
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FROM: Jay Costan
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DATE: September 6, 2001

RE: Options for GISB Transition to EISB – Revised by the Board of Directors,
September 19, 2001

The Gas Industry Standards Board ("GISB") is currently involved in discussions with other industry groups on the formation of an Energy Industry Standards Board ("EISB") that would succeed GISB and be responsible for establishing business practice standards for both the gas and electric industries. As presently conceived, the proposed new EISB would be made up of four separate industry quadrants: (i) wholesale gas (i.e., successor of the current GISB), (ii) wholesale electricity, (iii) retail gas, and (iv) retail electricity. A proposal known as "Strawman 2.1" describing how the new standards board would be organized is now being circulated among industry representatives for consideration. Under the Strawman 2.1 proposal, each quadrant would be made up of a designated number of segments to be determined by the quadrant, which would have equal representation on the Board and on the Executive Committee for that quadrant. As discussions within the industry progress, Strawman 2.1 may evolve into Strawman 2.2, representing an industry consensus on the appropriate governing structure for a new EISB.

One of the major hurdles involved in moving from GISB to EISB is determining the most suitable organizational vehicle for making the transition. This memorandum discusses three possible alternatives for the transition from GISB to EISB. It assumes that the EISB entity will be based on the current GISB structure and, once established, will be the functional successor of GISB. The three transition alternatives are:

1. Amend GISB's Articles of Incorporation and By-laws to expand the existing structure to include the more comprehensive EISB structure;
2. Create a new EISB entity that would incorporate the existing GISB members and, upon reaching critical mass, dissolve GISB;
3. Create a new EISB entity that would merge with GISB.

A variety of factors can influence the selection of a particular alternative for the transition. These include the extent to which the alternative affords flexibility in the "ramping up" of the new organization; the extent to which the particular alternative requires submission of a new application for tax-exempt status under Section 501(c)(6) of the Internal Revenue Code and the extent to which the new organization would be perceived as representative of the entire industry, as opposed to a particular quadrant. Also, because GISB is expected to receive ANSI certification very soon, there is the additional issue of transferring such certification to a new entity.

Each of the three organizational alternatives is evaluated below.

Executive Summary

There is no advantage, in terms of Delaware corporate law, to creating a new entity, rather than adapting the existing GISB structure to include the new quadrants encompassed within EISB. In both cases, the goal is to have one entity that incorporates all energy sectors. The most straightforward and cost-effective way to accomplish this appears to be Option 1, which would involve using the existing GISB structure and transforming GISB into EISB through changes to GISB's Certificate of Incorporation and By-Laws to reflect the character and structure of the proposed EISB organization.

Several tangible steps seem necessary to accomplish this transition. First, the GISB Board would need to adopt a resolution reflecting its support for the Strawman 2.1 proposal, as well as its commitment to the consensus-building effort necessary to construct and populate EISB along the lines described in the Strawman 2.1 proposal. Second, depending on the perceived need to lend palpable substance to the transition process, the GISB Board at the same time could adopt a resolution amending the Certificate of Incorporation to permit the actual legal transformation of GISB into EISB. Third, and most critically, the Board would need to pass amended By-laws to reflect the character and function of the new EISB organization at the conclusion of the industry-wide consensus-building effort involving the Strawman proposal.

As part of the consensus-building effort, new members would be enlisted through letters of intent. Virtually simultaneously with the adoption of new By-laws at the end of the consensus-building effort, the letters of intent of subscribers would be exchanged for membership in the new organization. A timeline setting forth the various steps with an assumed September 2001 start date and a March 2002 date for actual commencement of operation of EISB is attached as an appendix.

1. Amend GISB Documents to Expand Into EISB

This alternative would require amending GISB's Certificate of Incorporation to change the name to EISB and to expand the purpose of the organization to include

EISB objectives.¹ There are two ways to accomplish this. One is to file one or more certificates of amendment to the existing Certificate of Incorporation with the Delaware Secretary of State. The other is to file a restated Certificate of Incorporation that would include all amendments to the Certificate of Incorporation into a new complete certificate.² Since the purpose here is to transform the existing organization into something new, the development and filing of a restated Certificate of Incorporation would seem to be the more logical choice. The amendments would also require notifying the IRS of the expanded purpose to ensure that the expanded organization continues to qualify for tax-exempt status.

Probably the most challenging aspect of making the transition is developing the industry consensus and "comfort level" among all key participants to move forward. Important to this consensus-building process is the absence of any perception that the new organization is somehow controlled or directed by GISB. Thus, while GISB has invaluable experience in the standard-setting area that will be critical to the formation of a new organization, the governing documents of the new organization will need to reflect a cross-industry consensus effort. This concern has minimal effect in the case of the Certificate of Incorporation because the powers in the Certificate are broadly stated. However, it could be a significant issue in the case of the By-laws, where the functions and membership of each quadrant and of the Board and Executive Committee, as well as the organization's voting procedures, will be fleshed out in detail.

The process of building industry consensus takes time and makes it difficult to predict when the necessary support -- both philosophical and financial -- for a new organization will materialize. This timing issue, in turn, complicates any effort by GISB to make structural changes until support for the new organization is essentially a fait accompli. Two alternatives seem possible vis-à-vis GISB Board action.

The first of these would essentially contemplate that GISB take the lead in developing an organizational structure. Under this alternative, the Board would adopt the necessary amendments to its Certificate of Incorporation based on its perception that industry consensus is inevitable but that the consensus-building process needs a boost to spur the legal transformation from GISB into EISB. The first tangible step would be to adopt resolutions to (1) reflect GISB's support of the Strawman 2.1 proposal; and (2) amend GISB's Certificate of Incorporation to change its purpose to conform to the Strawman 2.1 proposal for an energy industry standards organization. At a later date (possibly at the December 2001 Board meeting), to further stimulate the industry-wide consensus-building process, the Board might wish to endorse a set of By-Laws for EISB. Once final industry consensus is reached, the GISB Board would adopt amended By-laws to reflect the industry consensus on EISB. It is contemplated that GISB would limit its standard-setting activity to wholesale gas markets served by

¹ Under Section 242(a)(2) of the Delaware General Corporation Law, "a corporation may amend its certificate of incorporation, from time to time, so as: (1) To change its corporate name; or (2) To change, substitute, enlarge or diminish the nature of its business or its corporate powers and purposes."

² See Delaware General Corporation Law § 245.

interstate pipelines until such time as industry consensus is reached on some version of Strawman 2.1 and new By-Laws are adopted to reflect such consensus. There is a possibility that the consensus-building process could be concluded as early as December of this year.

The second alternative would reflect a "GISB follow" approach. The GISB Board would adopt a resolution reflecting support for the Strawman 2.1 proposal currently under consideration and expressing support for formation of a new EISB that is substantially along the lines of Strawman 2.1. Under this scenario, industry negotiations would continue until a consensus is reached. This consensus could be reflected by letters of intent to support the new organization. Once the appropriate number of letters of intent were executed to reach critical mass, the GISB Board would vote to amend its Certificate of Incorporation and By-Laws to reorganize as EISB along the lines of the consensus industry proposal. Concurrently therewith, the membership of the new organization would be expanded consistent with the commitments in the letters of intent.

Of these alternatives, the first is probably superior because of the perceived need to take tangible steps now to move from the "talking" stage of Strawman 2.1 to the first stage of actual implementation. Industry discussions of creating an energy industry standards organization have now been ongoing since at least October 1999, and consensus on the need to create such an organization seems fairly clear. At the same time that industry consideration of creating an EISB has intensified, so has interest in, and support of, such an organization galvanized among federal and state regulators. Notably, the Chairman and two Commissioners of the FERC are on record as staunchly supporting formation of an EISB, sooner rather than later. Nevertheless, because the process of actually forming and populating such an organization will represent dramatic change for some of the affected industry sectors, there is a certain amount of inertia inherent in taking what is generally recognized as a very useful concept and transforming it into an actual functioning organization. To counter such inertia and help jump-start the legal transformation of GISB into EISB, a compelling argument can be made that GISB should take the lead and amend its Certificate of Incorporation to conform to Strawman 2.1 while the industry consensus-building process continues to refine the details of Strawman 2.1. Indeed, the persistent argument that GISB is now the only organization with sufficient credibility to attract broad industry support seems to underscore the need for GISB to act.

The downside of any such action is the possibility that EISB will be perceived as GISB-controlled, which might interfere with the consensus-building process. The counter to any such perception, however, is the recognition that GISB lacks the power to exert any such control. GISB is just one quadrant of what will ultimately be a four-quadrant organization. Until the industry-wide consensus-building process is concluded, GISB, through its annual plan, will limit its standard-setting activity to wholesale gas standards. As GISB's entire history demonstrates, its sole concern is to support an effective consensus-building effort and, in the case of EISB, once critical mass has been reached in support of an industry-wide proposal, to lend its

organizational structure and tax-exempt status to the new organization for a quicker and less costly start.

A timeline illustrating how the "GISB lead" option would work under optimal conditions using a September 2001 start date and a March 2002 completion date is appended hereto.

Depending upon the pace at which the industry is willing to move, it is possible that not all quadrants will have sufficient members at the time the new organization is started. Indeed, the organizers of EISB may choose to add quadrants one at a time, ensuring that each is running smoothly before moving to the next quadrant. The initial By-laws could be devised to accommodate four "active" quadrants, allowing for the possibility that a quadrant could be dormant until it reached critical mass, which could be defined in the organizational documents.

Advantages: Creating EISB by way of using the existing organizational structure of GISB has several advantages. It would save time and expense over creating a new entity. The existing entity already has a Section 501(c)(6) certificate, avoiding the time and expense of filing a new application for tax-exempt status. Although notice of the changes must be provided to the IRS, the existing tax-exempt status would continue without interruption unless the IRS takes action, which is not viewed as likely. Also, GISB has an experienced staff well-versed in the processes and procedures that are critical for a successful industry standards organization. The intellectual capital available from GISB's experience would tend to lower substantially the start-up costs of a new organization, minimize mistakes and avoid replowing ground that has already been covered before. Finally, GISB is very close to receiving final certification from ANSI, which involved a six-year application process and lends significant stature to GISB as a standards-setting organization.

Disadvantages: The chief drawback of using the existing GISB organization as the platform is that it might be perceived as being subject to the direction or control by GISB. This perception, however, could be dispelled fairly easily by continuing to allow EISB to develop on a parallel track through the industry-wide consensus-building process and voting to amend the By-laws of GISB only after the industry-wide consensus building effort evidences that the time to do so is ripe. Given what has gone into Strawman 2.1, and the support it has enjoyed up to this point, it is possible, if not likely, that the industry-wide consensus-building effort could be completed this fall in time for the December 2001 Board meeting.

2. Create New EISB Entity and Dissolve GISB

This alternative would require incorporating an entirely new organization, including the filing of a new Certificate of Incorporation and By-laws. Once the new EISB organization was running, GISB members would need to vote to dissolve GISB. Members of GISB would make up the Wholesale Gas Quadrant of EISB. Also, EISB would have to file a new Section 501(c)(6) application for tax-exempt status.

Dissolution of GISB would require the filing of a certificate of dissolution³ and transfer of GISB's assets to EISB. GISB would need to ensure that all assets are transferable to the new entity, i.e., that the assets themselves do not have limitations preventing transfer to the new organization.

Advantages: This alternative may avoid the complications of amending and transitioning the existing GISB structure to the new EISB structure, by allowing potential members to start from scratch. In addition, starting a new organization from scratch might be perceived as more "independent" than using the GISB organizational structure as the foundation.

Disadvantages: This alternative would require the filing of all new documents to create a new non-profit entity, thus increasing the time and expense involved. Also, a new Section 501(c)(6) application would take longer to process. Further, the pending ANSI certification would expire with the dissolution of GISB, requiring a reapplication at some future date and leading to uncertainty as to when and if such certification might be forthcoming (it has taken GISB six years to obtain certification). Finally, the new entity would need to hire its own staff independently from GISB, thus duplicating some costs and foregoing the savings made possible through the GISB staff's experience in running a standards organization.

3. Continue GISB, Create New EISB Entity, Then Merge Both Entities

As in the previous alternative, this alternative would require incorporating an entirely new organization, including the filing of a Certificate of Incorporation and the creation of a new set of By-laws. However, the two organizations would be merged, rather than GISB dissolving. The merger process would require the filing of articles of merger, which would amend the Articles of Incorporation, and would also require the merger of all financial systems and other administrative systems,⁴ although this process could be simplified if the new entity were created with the merger as a goal after a certain period of time or upon EISB's reaching a critical mass.

Advantages: There is no particular advantage to creating an entirely new entity and merging that entity with an existing entity when the existing entity can either be expanded to cover a more comprehensive purpose and to include more segments, or be dissolved.

Disadvantages: This alternative would be slightly more complex and costly than option two without any discernible advantages.

³ See Delaware General Corporation Law §§ 275 and 276.

⁴ See Delaware General Corporation Law § 255.

Conclusion

There is no discernible advantage to creating a new entity, as opposed to adapting the existing GISB structure to include the new quadrants encompassed within an EISB. The ultimate goal is to have one entity that incorporates all energy sectors, and the most straightforward and cost-effective way to do that appears to be Option 1, which would involve transforming GISB into EISB. Specifically, this would entail (i) a resolution by the GISB Board at the outset showing support for the Strawman proposal, (ii) helping to jump-start the transition to a new organization with a resolution by the Board adopting amendments to the Certificate of Incorporation to revise its purpose consistent with Strawman 2.1, and (iii) then building the necessary consensus for an EISB organization through letters of intent. Once critical mass is reached to support the consensus proposal, the GISB Board would vote to amend the By-laws to change its structure and function to reflect the consensus industry proposal. Concurrently with that action, the letters of intent submitted by subscribers would be exchanged for membership in the new organization. A timeline illustrating how this approach might be implemented over a September 2001 through March 2002 timeframe is attached.

APPENDIX

Possible Timeline for EISB Approval Process

September 19, 2001	Adoption of GISB Board Resolutions endorsing Strawman 2.1 proposal, supporting industry consensus-building effort, amending Certificate of Incorporation to allow for functional transformation to EISB beginning January 1, 2002, and directing GISB General Counsel to draft amended By-Laws consistent with Strawman 2.1 proposal
Post September 19, 2001	Continuation of consensus-building effort across the gas and electricity industries to build critical mass in support of strawman proposal; solicitation/execution of Letters of Intent by companies interested in joining EISB organized along lines reflected in strawman proposal
December 5, 2001	Adoption of GISB Board Resolution endorsing Strawman 2.1 By-Laws reflecting the results of the industry consensus-building effort, changing name of GISB and making conforming changes to Certificate of Incorporation
January - March 2002	Conversion of Letters of Intent into membership in new organization; formation and organization of additional Quadrants and election of members to constitute a functioning Board of Directors and Executive Committee for EISB; consideration by Board of Directors of any additional conforming amendments to Certificate of Incorporation or By-laws to reflect industry consensus proposal on EISB

Assumptions:

The progress of events reflected in this timeline assumes (1) consensus among the GISB Board on support of the Strawman 2.1 proposal at the time of the September 2001 Board meeting; (2) indications of strong industry support for the strawman proposal through trade association and individual company responses at the time of the September 2001 GISB Board meeting; and (3) cooperation of counsel for interested parties in the drafting of any changes to the Certificate of Incorporation or Strawman By-Laws during the last quarter of 2001.