

**BEFORE THE
EXECUTIVE COMMITTEE
OF THE WHOLESALE GAS QUADRANT OF THE
NORTH AMERICAN ENERGY STANDARDS BOARD**

**Comments of the Process Gas Consumers Group and
American Forest & Paper Association
Regarding Pipeline Creditworthiness Standards**

Pursuant to the “workplan” established by the North American Energy Standards Board (“NAESB”), Wholesale Gas Quadrant (“WGQ”), Business Practices Subcommittee (“BPS”), the Process Gas Consumers Group (“PGC”) and the American Forest & Paper Association (“AF&PA”) (collectively referred to herein as the “Industrials”) submit the following comments addressing the “Proposed Standards” on pipeline creditworthiness dated April 21, 2003, as well as other relevant issues for consideration by the Executive Committee (“EC”) at its May 20, 2003 meeting.

Although, we are not NAESB members, the Industrials meaningfully participated at almost every meeting and conference call discussion during the six month BPS pipeline creditworthiness standards drafting process. The Industrials worked diligently with several other end user, services and producer representatives to draft and propose reasonable creditworthiness standards for consideration by the BPS participants. Therefore, we believe that our first-hand experience and significant participation in the NAESB creditworthiness standards drafting process qualifies us to submit the following comments for the EC’s consideration. We respectfully request that the EC consider these comments and endorse the recommended actions.

I. Summary

The Industrials’ comments herein will:

(1) provide the EC with pertinent information about how the standards were formed and identify the major problems facing the BPS participants when trying to develop pipeline

creditworthiness standards. The Industrials believe that it is imperative that the EC inform the NAESB Board of Directors and the Federal Energy Regulatory Commission (“Commission” or “FERC”) of the significant hurdles that the BPS participants faced during the standards drafting process in order to prevent these types of obstacles to standardization from occurring in the future, whether or not in the realm of pipeline creditworthiness standards.

(2) provide support for many of the standards proposed in the April 21, 2003 document as many of them represent a fair balance of the pipeline risks and the shipper burdens to demonstrate creditworthiness. Moreover, our comments will provide examples where language needs to be changed or developed within a particular standard. Additionally, the Industrials will object to the language included in three of the proposed standards and recommend that those standards be altered. If those standards are not altered as proposed by the Industrials, we will recommend that the EC not approve them.

(3) provide support for new standards that adopt FERC’s policies regarding: (1) the creditworthiness “timeline”; (2) the three months maximum “security” (either prepayment, collateral, letter of credit or guarantee) requirement that a pipeline can obtain from a non-creditworthy shipper; and (3) how a pipeline determines that a shipper is non-creditworthy. The Industrials endorse many of the standards proposed by EnCana Corporation in its comments submitted to the EC on May 13, 2003, as well as many of those recommended by Calpine Corporation its comments submitted to the EC on May 14, 2003. Accordingly, we request that the EC make efforts to include these types of standards in the NAESB June 1 Report to FERC.

II. The Development of Pipeline Creditworthiness Standards at the BPS

As any participant at the WGQ BPS pipeline creditworthiness standardization meetings can tell you, the standardization process was, above all, incredibly frustrating.

Unfortunately, the majority of the BPS participants' time was spent discussing what could be or could not be discussed – i.e., what is policy and what is not policy? As a result, the BPS process was terribly inefficient and led to a waste of valuable time and resources. The Industrials believe that the significant flaws in the process must be flagged and brought FERC's attention immediately. Accordingly, the Industrials request that, in its June 1 Report to FERC, NAESB detail some of the problems experienced at the BPS level so that this type of problem does not occur again. Although, ultimately, the Industrials do believe that the hard work of all the BPS participants led to the development of several good standards, we also believe that much more could have been accomplished had FERC provided more concrete policy directives from the beginning.

Critically, FERC sent the creditworthiness issue to NAESB prematurely. FERC's policies had not been fully fleshed out and, at a minimum, a generic proceeding (resulting in a Policy Statement on pipeline creditworthiness) should have been convened before FERC sent any standardization request to NAESB. As a result, some of the threshold creditworthiness issues were not addressed or were omitted from the workplan – i.e., the timelines for the creditworthiness process, the appropriate maximum amount of collateral that a pipeline could request from a non-creditworthy shipper and “how” a shipper's creditworthiness status would be determined by the pipelines. Unfortunately, because of the never-ending debate over what was policy and what was not policy, the BPS ran out of time and could not set standards on certain issues, even though FERC had clearly articulated Commission policy on those issues.¹

¹ Although, practically speaking, the BPS did “run out of time,” the pipeline and distribution segments fought hard against trying to make the time to include a discussion of these topics. For example, suggestions to ask FERC for an extension of time (which likely would have been granted) to complete our work at the BPS were rejected outright.

Moreover, NAESB must make FERC aware that once we did receive policy directives from the Commission in its *Tennessee Gas Pipeline Co.*² and *Northern Natural Gas Co.*³ decisions, the standardization process again was held hostage – this time because FERC’s creditworthiness decisions in the individual pipeline proceedings were “on rehearing” and, therefore, according to some BPS participants, did not constitute policy directives that could be considered for standardization. Not surprisingly, the pipeline and distribution segments voted against the inclusion in the workplan of several fundamental creditworthiness policy issued clarified by FERC.

Therefore, the Industrials believe that it is essential that NAESB report to FERC that the Commission must implement the important shipper creditworthiness standards that were not developed at NAESB because either, (1) time ran out (timelines were on the workplan but not discussed), or (2) some segments refused to address them (maximum collateral amounts and creditworthiness criteria were not meaningfully discussed). Because of the segments’ inability to reach a consensus on what is policy or not, NAESB should request that the remaining creditworthiness policies, issues and standards be resolved at FERC, not through another series of BPS meetings – lest we all not waste more valuable time.

III. Comments on the Standards Presented for the EC’s Review

Before the Industrials address our specific problems with a few key proposed creditworthiness standards, we would like to briefly recap for the EC the Industrial viewpoint on creditworthiness provisions and discuss some of the proposed standards that we support as consistent with FERC policy.

² 102 FERC ¶ 61,075 (2003)(herein “*Tennessee*”).

³ 102 FERC ¶ 61,076 (2003)(herein “*Northern*”).

Primarily, the Industrials believe that every pipeline creditworthiness tariff provision or standard must represent a fair balancing between the risks that a pipeline actually faces and the burdens that a shipper faces in meeting pipeline requirements to obtain transportation service. When the individual FERC proceedings began last summer, the Industrials expressed grave concern that many of the proposed tariff changes related to creditworthiness did not accurately represent the risks that pipelines were facing in today's energy industry. For example, in the individual FERC cases, the pipelines failed to demonstrate a need for tightening their creditworthiness requirements, as many of the purported problems stemmed from the Enron "debacle". Plainly, the evidence presented in the individual proceedings failed to demonstrate that the pipelines were facing a serious default problem. Furthermore, the Industrials, along with other concerned shippers, argued that any risk that the pipelines is facing, is mitigated by the pipeline's FERC-approved rate of return.

As such, the Industrials expressed concern in the individual pipeline proceedings that the pipeline proposals were unjustified, overly punitive, overly-broad, unduly discriminatory and gave too much discretion to the pipelines. Above all, however, the "star chamber" evaluation process gave us the most heartburn.

Fortunately, FERC heard many of our concerns and through its orders issued in *Tennessee, Northern, Natural Gas Pipeline Co. of America*,⁴ *PG&E Gas Transmission, Northwest Corp.*⁵ and *Gulf South Pipeline Co., LP*⁶ set forth policy that embodied both the Industrials' and the pipelines' concerns, and refined a creditworthiness policy that "balances the

⁴ 102 FERC ¶ 61,335 (2003)(herein "*NGPL*").

⁵ 103 FERC ¶ 61,137 (2003)(herein "*GTN*").

⁶ 103 FERC ¶ 61,129 (2003)(herein "*Gulf South*").

need to assure that all shipper have a reasonable opportunity to obtain pipeline services with [the pipeline's] need to ensure the creditworthiness of its shippers.”⁷

With this threshold policy in mind, the Industrials believe that the following proposed standards meet the Commission's creditworthiness policies and should be adopted without modification.

- Proposed Standard 0.3.zA: this proposed standard is intended to enumerate all the different types of information that a Transportation Service Provider (“TSP”) should allow the Service Requester (“SR”) to provide to demonstrate its creditworthiness. **Our support for this standard is conditioned, however, on our understanding that the SR will not be required to provide all the information included on this list. Instead, the listing is designed to standardize the types of information that an SR could elect to furnish for use in a credit evaluation process on any pipeline.** Furthermore, the Industrials understand that an SR cannot be forced to obtain one of the items listed, such as bank and trade references, if they do not already have them. Notably, this list includes “such other information as may be mutually agreed to by the parties” which provides flexibility and allows the TSP to consider the individual circumstances of the SR. The Industrials support this standard because it give the SR a reasonable basis to know what type of information can be requested by the TSP so that the SR can demonstrate creditworthiness across the interstate grid.
- Proposed Standard 0.3.zB: this proposed standard is intended to provide the SR with a reason why the TSP has requested additional information to demonstrate the SR's continued creditworthiness after service has been initiated. The Industrials support this standard because it eliminates one element of the “star chamber” concern surrounding the creditworthiness process and allows the SR to immediately pinpoint and address the TSP's concern.
- Proposed Standard 0.3.zC: this proposed standard is intended to let the TSP know that the SR has received a request for information to demonstrate creditworthiness. The Industrials support this standard because it lends support to a fluid and open creditworthiness evaluation process.
- Proposed Standard 0.3.zD: this proposed standard is intended to require the SR to provide information within the time period request, but allows for flexibility because the SR is able to provide a reason why the information is not being provided. Again, the Industrials support this standard because it leads to a transparent process and promotes open communication between the SR and TSP.

⁷ GTN at P 1.

- Proposed Standard 0.3.zE: this proposed standard is intended to provide the SR with notification that the TSP has received the requested information to perform a creditworthiness evaluation (or correspondence why the information cannot be provided by the requested date). The Industrials support this standard because it lends support to a fluid and open creditworthiness evaluation process.
- Proposed Standard 0.3.zF: this proposed standard is intended to require the SR to provide to the TSP the information of those persons that should be contacted about creditworthiness issues. The Industrials support this standard because it lends support to a fluid and open creditworthiness evaluation process.
- Proposed Standard 0.3.zI: this proposed standard is intended to require the SR to provide requested credit information to the TSP within 3 business days or an explanation why such information is not available within the time period. The Industrials support this standard because it is a first step toward implementing the “timeline” for creditworthiness. (Unfortunately, the rest of the timeline was not developed.) The Industrials support the flexibility included in the standard and are not opposed to 3 business days because it takes into account weekends and holidays.
- Proposed Standard 0.3.zK: this proposed standard is intended to allow an SR to request a re-evaluation of creditworthiness at any time by providing updated information that the SR believes could lead to change in the SR’s credit status. The Industrials support this change because it promotes flexibility in the creditworthiness process and would prevent a TSP from retaining security in the event an SR’s status changed.

Although there are many standards that we support, there are also several standards that we request that the EC either (1) require that additional language be implemented or, (2) reject the standard as proposed. Our specific objections include:

- Proposed Standard 0.3.zG: although we support the concept that a TSP will explain why a shipper is deemed non-creditworthy, we do not believe that this standard gets to the heart of the matter – how is creditworthiness defined. The Industrials request that this standard be altered to include the “how”. *See* Section V (3), below.
- Proposed Standard 0.3.zH: this proposed standard is intended to provide the TSP with relevant information regarding the SR’s creditworthiness status. The Industrials generally support this standard because it is limited to real credit concerns such as bankruptcy and liquidation concerns. For the most part, this standard does not try to obtain overly subjective information such as information about pending lawsuits. However, the Industrials propose one important clarification that we believe is imperative for this standard to work. In particular, a downgrade should be reported only if it is “below investment grade”. Shippers with good credit records and past payment histories should not be subject to scrutiny simply because they were downgrade from AAA to AAA-. This standard must be clarified as such.

- Proposed Standard 0.3.zJ: although we support the concept that the parent should be apply to supply financial information where an affiliate SR does not have the requested financial information publicly available, the Industrials object to the language in the standard that states that the parent’s information could be supplied “to the extent that such documents contain the required information pertaining to the SR.” This requirement is particularly troublesome as explained in detail below. *See* Section IV, below.
- Proposed Standard 0.3.zL: contains blanks to fill in the number days for a pipeline to reply to a shipper who has requested a re-evaluation of creditworthiness (this was purposely left blank because the BPS thought that we would address it in the general timelines discussion, however, we ran out of time). The Industrials suggest 5 business days for pipeline to reply that it has received information and that the re-evaluation is ongoing, and a maximum of 20 business days to provide a re-evaluation result to the shipper. We note that this is consistent with the comments supplied by EnCana Corporation on May 13, 2003 and recommend that the EC vote to approve this addition.
- Proposed Standard 0.3.zO: this proposed standard is intended to require the TSP to include the amount of collateral a non-creditworthy SR must provide to receive service. The Industrials believe that this standard does not go far enough – it should require the TSP to include language in its tariff that three months of service charges is the maximum amount collateral that can be required from a non-expansion shipper SR. *See* Section V (2), below.
- Proposed Standard 0.3.zP: this proposed standard is intended to require the TSP to pay interest when it collects cash collateral from a SR. The Industrials support this standard as generally consistent with FERC policy but request that it be clear in the standard that the interest rate will be the FERC interest rate.
- Proposed Standard 5.3.z.F: specifically, we object to part (4) of this standard, which would require a pipeline to notify a releasing shipper any time it requested credit information from a replacement shipper. This is objectionable because it is overly broad (the information may be requested so that a shipper can have its creditworthiness status reinstated, not because of downgrade) and it could lead to the release of proprietary business information or other sensitive information that the replacement shipper may not want the releasing shipper (who may be a competitor) to have access to. The releasing shipper should have its own duty to evaluate the creditworthiness of its replacement shipper and should not rely on the pipeline to do so. If this language is not removed, we recommend that the EC vote against this standard.

IV. Proposed Standard 0.3.zJ Must be Revised

As noted above, the Industrials object to the requirement that a parent can supply publicly available financial information on behalf of an affiliate SR only “to the extent that such documents contain the required information pertaining to the SR.” This clause essentially

renders the flexibility that this standard is intended to provide meaningless and must be removed. The Industrials' objection can best be illustrated by a real-world example from one of our member companies.

Some large industrial end users have corporate structures in place where the affiliate SR (not the parent company) contracts for and receives natural gas transportation service from the TSP. However, as an affiliate of a parent company, the SR does not have the same publicly available financial information as the parent company. Furthermore, the parent company's publicly available financial information does not contain financial information about the affiliate SR. The information is omitted because of very serious confidentiality and competitive concerns.⁸

Furthermore, due to the corporate structure in place, even if available, the financial information about the affiliate SR would be irrelevant. This is because, under the corporate structure in place, the affiliate SR has no debt, nor any revenues, associated with its operations. Although the SR receives the bills for transportation service, the parent company pays the bills and, in turn, receives the revenues associated with the affiliate SR's operations. Practically speaking, the debt and cash flow responsibilities lie with the parent company – not the affiliate SR. Therefore, the publicly available information of the parent should be sufficient to satisfy a creditworthiness evaluation of an affiliate SR. Accordingly, the Industrials request that Proposed Standard 0.3.zJ be revised to omit the clause “to the extent that such documents contain the required information pertaining to the SR.” If this is not omitted, the Industrials recommend that the EC reject this standard.

⁸ Industrial companies do not want their individual plants' financial information publicly disclosed out of the fear that competitors will be able to use that information to target certain plants to compete against, directly.

If proposed standard 0.3.zJ is passed in its current form, there are some industrial companies, which due solely to their corporate structure, could always be deemed non-creditworthy even though they are financially healthy. Moreover, many of these same companies have corporate structures that prohibit the use of parental guarantees. Therefore, when considering the plight of an affiliate SR for which there is no publicly available information, the Industrials request that, at a minimum, the past payment history of the affiliate SR not be overlooked. Instead, the Industrials urge the TSP to give the long-standing business relationship great consideration when an evaluation of creditworthiness is being conducted. The Industrials would recommend that a standard be adopted that embodies this concept.

V. Recommendation that NAESB EC Consider and Adopt Standards That Are Not Included in the Package

Although we lend significant support to a number of standards that have been proposed for EC approval, there are some standards that are not being proposed as part of the BPS package that, the Industrials believe, are noticeably absent. Therefore, we propose those standards for consideration by the EC.

(1) Timelines Must be Standardized

As noted above, the standardization of timelines for the creditworthiness process was included on the BPS workplan. However, due to the time limitations placed on our deliberations, the timeline issues was not fully addressed. Therefore, the Industrials request that the EC adopt timelines that are consistent with the FERC policy directives set forth in *Tennessee*, *Northern*, *NGPL*, *Gulf South* and *GTN*.⁹

⁹ *Tennessee* at P 18; *Northern* at PP 49-50; *NGPL* at P52-53; *Gulf South* at PP 49-52; and *GTN* at PP 49-51.

In short, in the event a shipper is deemed non-creditworthy, FERC's timeline in those orders provides that:

- Within 5 business days:
 - shipper must provide prepayment for one month of service plus any outstanding amounts due
 - If not provided within 5 business days, service may be suspended immediately
 - If service is suspended, shipper cannot be held liable for future charges
 - Upon suspension, pipeline can provide simultaneous notification that service will be terminated within 30 days if the shipper fails to provide adequate security. Termination notice must also be sent to the Commission.

- Within 30 days:
 - shipper must provide prepayment for the next three months of service
 - If not provided within 30 days, service may be suspended immediately
 - If service is suspended, shipper cannot be held liable for future charges
 - Upon suspension, pipeline can provide simultaneous notification that service will be terminated within 30 days if the shipper fails to provide adequate security. Termination notice must also be sent to the Commission.

The Industrials believe that the timelines suggested by the Commission in its recent series of creditworthiness orders strike the proper balance between the risks facing the pipeline and the need to provide shippers with adequate time to meet the pipeline's credit requirements in order to obtain transportation services. We urge the EC to adopt a standard at the May 20, 2003 meeting that incorporates FERC's timeline policy above.

(2) Maximum Collateral Requirements for Non-Expansion Shippers – Proposed Standard 0.3.zO Must Be Revised

As with the timelines above, FERC policy is clear – in many circumstances, three months worth of service charges is the maximum value of collateral that a TSP can require a non-creditworthy SR to supply to receive service.¹⁰ Specifically, the Industrials support the

¹⁰ *NGPL* at PP 29-30; *Gulf South* at PP 34-36; and *GTN* at PP 31-33.

NEW Proposed Standard 0.3.zM2 submitted by EnCana Corporation on May 13, 2003 and ask that it replace Proposed Standard 0.3.zO:

The Transportation Service Provider (TSP) should determine a credit exposure for a Service Requester (SR) equal to the total estimated transportation costs under all the SR's service agreements with the TSP for the term of service under the agreement(s); provided for this credit exposure no term of service should exceed three (3) months unless such limitation is waived by the Federal Energy Regulatory Commission (or equivalent) for construction, expansion, acquisition or lease of new facilities.

The EC should be made that a substantially similar standard was proposed, discussed and voted on at the last conference call/meeting and, although the standard failed to pass, the vote was very close. Moreover, not all the segments were fully represented and, therefore, we would like the EC to reconsider the standard since all segments will be represented at the May 20, 2003 EC meeting. This standard embodies FERC policy and, furthermore, is merely an expansion of Proposed Standard 0.3zO that requires pipelines to include in their tariffs language regarding the amount of credit assurances, but fails to provide a maximum amount.

(3) Objective Criteria – The “How” – Proposed Standard 0.3.zG Must Be Revised

The Industrials believe that there must be a clear definition of “non-creditworthy”. Numerous debates during the BPS deliberations focused on whether or not the “how” of a TSP creditworthiness evaluation process could be added to the workplan. Unfortunately, after three very close votes (in December, February and March), “how” a TSP would evaluate an SR's creditworthiness failed to be included in the BPS discussions. The Industrials believe that, like the timelines and collateral requirements highlighted above, the “how” gets to the very essence of the creditworthiness debate and it is disappointing that the BPS participants refused to address

this issue head-on. However, our disappointment only grows to frustration in light of the fact that FERC clearly has spoken on this issue – pipelines must include “objective criteria” in their tariffs¹¹ – and still the BPS participants refused to discuss this issue. Accordingly, the Industrials request that the EC adopt the revisions to proposed standard 0.3.zG proposed by Calpine Corporation in its May 14, 2003.

Importantly, providing shippers with a detailed explanation of why the shipper was deemed non-creditworthy, including “all financial analyses and ratios relied upon, as well as any subjective factors that went into the non-creditworthy determination” is vital to the shipper. Furthermore, providing information promotes transparency to the process (eliminates the “black box”) and allows the SR to consider how it might demonstrate creditworthiness in the future. Moreover, providing a reason why an SR is not creditworthy could signal the SR that it did not provide the correct credit information or could lead the SR producing other documentation to meet the TSP’s concerns. The Industrials support this standard as revised by Calpine.

VI. Conclusion

In the event that the EC is unable to make the revisions to the proposed standards identified above or pass the new standards requested by the Industrials, we request that NAESB should request that the remaining creditworthiness policies, issues and standards be resolved at FERC, not at NAESB through another series of BPS meetings.

¹¹ *Tennessee* at P 41; *NGPL* at P 69; *Gulf South* at P 24; and *GTN* at P 67.

For the foregoing reasons, the Industrials requests that the NAESB WGQ Executive Committee adopt our recommendations and take action consistent with our comments set forth above.

Respectfully submitted,

Kirstin E. Gibbs

Dena E. Wiggins
Kirstin E. Gibbs
SUTHERLAND ASBILL & BRENNAN LLP
1275 Pennsylvania Avenue, NW
Washington, DC 20004-2415
(202) 282-0100 (phone)
(202) 637-3593 (fax)

On Behalf of:

*Process Gas Consumers Group and
American Forest & Paper Association*

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