



# PHMSA Ditches Controversial Gas Transmission IM Change

The Pipeline and Hazardous Materials Safety Administration (PHMSA) made some changes to both its hazardous liquid and natural gas transmission integrity programs in July. But the agency declined to make the change interstate pipelines really want: extending the interval for reassessing pipeline segments.

Both PHMSA and the U.S. Government Accountability Office have testified that assessment intervals for natural gas transmission pipelines should be established based on technical data, risk factors and engineering analyses. That is not the case now. Currently, the interstate gas IM rule requires pipelines to inspect all segments running through sensitive areas within 10 years, starting in 2003. Those segments must then be re-inspected seven years later. However, in the final rule PHMSA issued on July 17, the agency said making changes to gas transmission reassessment intervals was "outside the scope" of this rulemaking.

The good news is that PHMSA backed off its proposal to require an operator of a gas transmission or hazardous liquid pipeline to notify PHMSA when it reduces pressure on an IM program segment (to remediate a defect) and to provide a justification for the pressure reduction. This new requirement was part of the proposed rule PHMSA issued in December 2005. Industry players contended the proposed notifications would impose a significant, undue and problematic administrative burden on industry. Several comments suggest that many discretionary pressure reductions are part of voluntary, normal and circumstantial events unrelated to remediation scheduling requirements.

## FERC NG price reporting proposal stirs discontent

No one in the natural gas industry seems satisfied with FERC's proposed rule on natural gas transparency, which comes at a time when Congress is holding hearings on natural gas price manipulation. The comments arriving at FERC in July differed to some extent with FERC's intent to require intrastate pipelines to post daily flow information at major receipt and delivery points and mainline segments.

This would be the first time intrastates would be subject to FERC regulatory authority. Not surprisingly, they are fighting the commission tooth and nail, hoping either for the commission to forget the whole idea, which is unlikely given congressional pressure on the issue, or for FERC to more narrowly tailor its requirement, which if finalized as proposed would require intrastates to spend considerable sums on metering equipment, costs that would undoubtedly be passed along to consumers.

The FERC proposed rule, which came out last April, implements additional authority Congress

gave the commission in the 2005 Energy Policy Act – authority Congress felt was needed in the wake of the 2000-2001 California crisis. That law tells FERC "to facilitate price transparency in markets for the sale or transportation of physical natural gas in interstate commerce." Congress's thinking in 2005 was perhaps validated in the fall of 2006 when Amaranth Traders, the hedge fund, appeared to have manipulated the natural gas market. So now, Congress is breathing down FERC's neck, waiting for the commission to implement the 2005 authority.

While the FERC proposed rule was technically confined to reporting by intrastate pipelines, FERC did ask the industry to comment on whether interstate pipelines also should be required to post actual flow data, and whether posting that data would "provide useful information regarding actual capacity use, for instance, by providing information regarding no-notice service?" Under current commission regulations, interstate pipelines are not required to publish on their websites actual flow data, but instead must publish a variety of capacity information, such as the availability of capacity at receipt points, on the mainline, at delivery points and in storage fields, and whether the capacity is available directly from the pipeline or through capacity release.

INGAA doesn't think interstates should have to publish flow data, too. The capacity information that pipelines currently post on a daily basis is adequate for the commission's transparency purposes, according to Joan Dreskin, INGAA's general counsel.

The Natural Gas Supply Association disagrees, and is pushing for interstate inclusion in any new reporting system. Jennifer B. Deegan, director of energy markets, says, "Actual flow data could lead to an even more accurate and near real-time indication of underlying market supply and demand fundamentals." This is particularly true, she adds, where there is a heavy reliance on "no-notice" volumes and pipeline imbalance tolerances. Because "no-notice" volumes and imbalance tolerance flows are not "scheduled" without pipeline flow information, regulators cannot see the entire transportation picture.

Given the specter of first-time FERC regulation, many intrastates are vehement about warding off FERC-imposed price reporting. Lee Baskin, director, regulatory, Kinder Morgan Texas Intrastate Pipeline Group, states, "The KM Intrastate Pipelines are not aware of any problems in the marketplace that warrant additional regulation."

On the other hand, the American Gas Association thinks some intrastates should have to report, but those totals should not include retail sales or volumes transported for others under retail choice programs. Andrew K. Soto, an AGA official, also says the commission should make

it clear that the reporting requirements only apply to "intrastate pipelines" and not Hinshaw pipelines, LDCs, and distribution companies with Commission-approved service area determinations.

## FERC considering reversal of MLPs in pipeline rate cases

In a move destined to set interstate pipelines and their shippers at each other's throats, the FERC proposed changing its policy to allow inclusion of master limited partnerships (MLPs) in the proxy groups the commission uses to determine whether a pipeline's requested rate of return is reasonable under its long-established Discounted Cash Flow (DCF) model. FERC declined to include MLPs in the proxy group for the high-visibility Kern River rate case it decided last fall, a decision which displeased INGAA.

FERC's tentative decision to placate INGAA and the interstates comes at a time when energy companies are increasingly using MLPs, a trend highlighted by Williams' announcement on July 20 that it is creating a new MLP composed of its Northwest Pipeline.

FERC has included MLPs in proxies for oil pipeline rate cases, but not gas transmission cases. That is because MLPs do not qualify under one of the three standards FERC uses to determine who should qualify for inclusion in a proxy group: that a company's pipeline business account for, on average, at least 50 percent of a company's assets or operating income over the most recent three-year period.

However, fewer and fewer pipelines meet this standard. If the new policy statement becomes final, master limited partnerships and other pass-through entities would be included in proxy groups if their cash distributions are capped at their reported earnings for purposes of determining the dividend yield that is one component of determining their return on equity under the DCF mechanism. The commission also proposes that parties in rate cases will be required to demonstrate the master limited partnerships included in a proxy group have reasonably stable earnings.

Samuel Brothwell, managing director, equity research-power & gas utilities at Wachovia Securities, says, "We would expect that shippers (who have challenged the inclusion of MLPs in recent gas pipeline rate cases) would be vocal opponents to this change."

Joan Dreskin, general counsel for INGAA, says her group is pleased by the proposed change, although she points out that INGAA may have something to say both about the two yardsticks FERC is proposing for inclusion of MLPs and about whether local distribution companies should continue to be included in proxy groups. "We would like to see LDCs barred from proxies," Dreskin says. ■