



UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

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W/DR/MLY

ENERGY AND MINERALS
DIVISION

AUGUST 27, 1979

B-178205

The Honorable Charles B. Curtis
Chairman, Federal Energy
Regulatory Commission AGC 01452



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Dear Mr. Curtis:

Pursuant to our authority under title V of the Energy Policy and Conservation Act of 1975 (EPCA), 42 U.S.C. 6381, et seq., the U.S. General Accounting Office has conducted a verification examination of information submitted to the Federal Power Commission (now the Federal Energy Regulatory Commission (FERC) within the Department of Energy) in liquefied natural gas proceedings by Trunkline LNG Company. The purpose of this letter is to advise you of our findings with respect to the accuracy, reliability and adequacy of the energy information which was the subject of our examination. Our work was limited to data considered by the Commission in deciding that liquefied natural gas (LNG) would not be marketable if offered to customers under the incremental pricing plan outlined in Opinion 796.

At the outset it should be noted that the question before the Commission in Opinion 796A--whether to require rolled-in or incremental pricing--has been decided by the Congress. The Natural Gas Policy Act of 1978, 15 U.S.C. 3301 et seq., requires that high-cost natural gas be incrementally priced to certain users. The act specifically excepts from this requirement, however, LNG imported under projects certificated by the Commission before May 1, 1978. While the Trunkline LNG project clearly is grandfathered by this legislation and while we do not challenge the correctness of the Commission decision to require rolled-in pricing in Opinion 796A, our examination led us to conclude that survey data submitted by Trunkline and relied on by the Commission in reaching its result was inadequate. Thus, we are reporting our conclusion as is required by EPCA, 42 U.S.C. 6382.

BACKGROUND

On June 30, 1977, the Commission issued Opinion 796A directing Trunkline to sell imported LNG at rates reflecting

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an averaging, or rolling-in, of the cost of the LNG with the cost of other gas supplies. This directive modified Opinion 796 wherein the Commission had ordered the imported LNG to be sold at rates reflecting its full, or incremental cost.

The Commission modified the pricing requirements of Opinion 796 because it determined that a supplemental gas supply project such as that proposed by Trunkline was in the public interest and that accordingly it owed a duty to ensure the financial viability of the project. Trunkline testified that if it was required to sell imported LNG at its incremental price, it would be unable to finance the project because too few of its customers were willing to commit themselves to buy at actual cost. The Commission concluded that rolled-in pricing was a necessary ingredient of the project's financeability. This conclusion was consistent with its decisions in Alaska Pipeline and in Columbia LNG, Opinion 786, and with the principle established in Columbia LNG that when gas is to be used as base load for high-priority users rather than as an "exotic" supplemental supply for lower priority users, rolled-in pricing should be used.

MARKETABILITY ASSESSMENT NEEDED

The ability to market incrementally priced LNG was a matter of controversy beginning with the initial hearings on the project and continuing through the Commission's last opinion. A financial witness for Trunkline testifying before the Administrative Law Judge during initial hearings contended that project financing could be jeopardized if the LNG had to be sold at an incremental price. His basic point was that under incremental pricing there was no firm market (no contracts) with potential customers. He indicated that with the large investment required by this project it would be necessary to have firm obligations from customers to purchase the incrementally priced LNG in order to secure the required investment in facilities and ships. This type of obligation was already present, he contended, under rolled-in pricing because the LNG could be sold under existing gas sales contracts. However, Trunkline presented no evidence that it had attempted to market the LNG to its customers under incremental pricing.

Commission staff witnesses argued that incremental pricing was necessary to provide a market test of whether customers would be willing to pay the true cost of the LNG. They contended that rolling in the cost of more expensive

gas with cheaper gas gives consumers incorrect signals regarding scarcity and costliness of additional gas supplies. In turn customers would not be induced to conserve gas as vigorously and would not invest as heavily in energy conserving technology.

The Administrative Law Judge approved rolled-in pricing, based on, among other things, his lack of assurance that the Trunkline project could be financed or implemented if incremental pricing were required.

The Commission staff objected to the Judge's approval of rolled-in pricing. In their legal brief summarizing these objections the staff acknowledged the Judge's conclusion that the LNG might not be purchased if priced incrementally and that this might make financing impossible. They stated, however, that unless the LNG is priced incrementally it will not be subjected to a market test of whether its users value it at least as much as the cost of supplying them with the gas, and there is a likelihood that the gas will not be used efficiently.

The Commission reversed the initial decision in which the Judge approved rolled-in pricing, stating that, based upon evidence presented, the incremental method is the correct method. The evidence the Commission relied upon was the expected price increase in the rolled-in cost of Trunkline's gas with LNG. The Commission concluded that rolling in the cost of the LNG would produce a significant increase in the price of Trunkline's gas and that staff's views were therefore relevant regarding the necessity of using incremental pricing to subject the LNG to a market test. Thus, the Commission ordered Trunkline to sell the LNG on an incremental basis. Furthermore, to promulgate incremental pricing to the extent possible at each stage of LNG sale and resale, the Commission decided that (1) action would be taken under the Natural Gas Act to require that Trunkline's interstate pipeline customers, Panhandle Eastern Pipeline ~~—D~~ 2630 Company and Mississippi River Transmission Corporation, price LNG incrementally to their customers; and (2) State commissions would be encouraged to require local distribution companies to use the incremental pricing method.

Trunkline objected to the Commission's decision and requested that oral arguments be held. Prior to these oral arguments Trunkline and Panhandle Eastern, on their own initiative, met with their customers to determine their

willingness to make current commitments to purchase LNG priced incrementally under Opinion 796. When oral arguments were held, Trunkline told the Commission this survey of customers had disclosed that not enough of the LNG could be marketed on an incremental basis to make the project viable. However, in accepting this data into the record the Commission relied on Trunkline's oral testimony and did not seek specific data about the survey results. Rather, in their modifying decision the Commission said they had determined that the project was in the public interest. One of the primary factors leading them to this conclusion was the expected need for the LNG by high-priority customers. Accordingly, to ensure that this supply became available to the high-priority customers, the Commission approved rolled-in pricing as a "necessary" ingredient to the project's financeability and ultimate viability.

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The Office of Opinions and Reviews (OOR), FERC, is responsible for studying the initial opinions of the Administrative Law Judges to assist the Commission or individual Commissioners in arriving at decisions on the initial opinions. The Deputy Director, OOR, told us that the OOR study includes a review for sufficiency of evidence. The OOR attorney advisor who reviewed the initial decision on the Trunkline application stated that when he made his review, the OOR policy was to attach a transmittal memorandum to the Commission summarizing the results of the OOR review. The memorandum on the Trunkline initial decision was removed from the file under the normal practice of purging such memorandums after 1 year. The attorney advisor said that, according to his note, no comments were made about the sufficiency of evidence for the Trunkline marketability survey.

EXAMINATION OF DATA

The Commission's failure to request specific data concerning Trunkline's survey of customers led us to examine the accuracy, reliability, and adequacy of the data gathered by Trunkline. Trunkline's response to our request for books, records, papers, or other documents pertinent to this point disclosed that Trunkline had not prepared a detailed analysis of the survey results. Rather, they had orally summarized their perceptions of the survey results when testifying before the Commission. Trunkline had, however, retained the survey data and provided it to us for analysis.

Because of the limitations of the survey, we were not able to come to a firm conclusion about the marketability of the LNG under incremental pricing. However, we found that those customers who were not interested in purchasing the LNG under any form of incremental pricing accounted for a minority of the gas sold by Trunkline and Panhandle Eastern. Our analysis and its results are described in detail in the following paragraphs.

In May 1977, Trunkline and Panhandle Eastern, Trunkline's parent company and largest interstate pipeline customer, held a joint meeting with their customers to explain incremental pricing as called for in Opinion 796. These customers were asked to consider the impact of incremental pricing on their respective companies and decide how much LNG they were willing to commit themselves to purchase. Although more than 70 customers were invited to the meeting, only 35 customers expressed their views on purchasing LNG under the terms of Opinion 796.

The responses received from the 35 customers were in a narrative format which made analysis difficult. However, we were able to group the responses into five categories, and our analysis of the responses according to these categories disclosed the following:

<u>Customer response</u>	<u>Trunkline</u>	<u>Panhandle</u>
	Customers' share of Number of gas sales <u>customers</u> (<u>percent</u>)	Customers' share of Number of gas sales <u>customers</u> (<u>percent</u>)
Yes, will purchase LNG at an incremental price.	1 .62	2 4.31
Yes, will purchase at an incremental price if State commission will allow resale at a rolled-in price.	- -	6 14.15
No, not at this time, but might later.	- -	4 2.73
No, not at this time.	- -	5 19.68
No, will not purchase the LNG at an incremental price.	5 <u>8.71</u>	<u>14</u> <u>23.43</u>
Total	<u>a/6</u> <u>9.33</u>	<u>a/31</u> <u>64.30</u>

a/Two respondents were customers of both pipelines.

The above table shows that one of Trunkline's and two of Panhandle's customers would purchase the LNG at incremental prices without reservation. Another six of Panhandle's customers said that they would purchase the LNG at such prices if the State commissions would approve their resale of LNG on a rolled-in basis. Opinion 796 "encouraged" but did not require State commissions to implement incremental pricing of LNG.

Although Panhandle is one of Trunkline's major customers, representing 43.25 percent of Trunkline's sales, Panhandle did not prepare a letter of commitment to purchase the LNG. However, Panhandle had previously testified before the Commission that they might purchase the LNG at an incremental price. One other major customer of Trunkline, Consumers Power Company, Jackson, Michigan, did not prepare a letter of commitment, but did testify before the Commission they would probably purchase the LNG at an incremental price if they could resell the gas on a rolled-in basis. This customer accounted for 43.01 percent of Trunkline's gas sales. Taken all together (the two customers and the study responses), customers for about 87 percent of Trunkline's gas sales left open the possibility that they might purchase LNG at incremental prices. Furthermore, Trunkline's study showed that nine of Panhandle's customers left open some possibility to purchase LNG at a later date. Their desire for the LNG depended upon their need for the gas to meet high priority needs (one customer), uncertainties about various unresolved issues (five customers), and future decisions by State commissions (three customers). These nine customers accounted for about 22 percent of Panhandle's gas sales.

The remaining customers who responded, 5 from Trunkline and 14 from Panhandle, said they were not interested in purchasing the LNG under Opinion 796. Trunkline's five customers purchased almost 9 percent of Trunkline's gas. Panhandle's 14 customers purchased over 23 percent of Panhandle's gas.

CONCLUSION

The Commission's decision on the marketability issue could have been better supported if it had required additional support for claims made in oral testimony. The Commission appropriately placed the burden of proof of marketability upon Trunkline but failed to verify the evidence presented by Trunkline on the issue.

Trunkline's examination into this matter, while useful, was not the comprehensive study of marketability that should have been required by the Commission. While Trunkline's study did show that customers who responded were not eager to make current commitments to purchase the LNG, it also showed that only 5 of Trunkline's and 14 of Panhandle's customers were not interested in purchasing the LNG. These customers accounted for only 8.7 percent of Trunkline's and 23.4 percent of Panhandle's total gas sales.

When the Commission is presented with information on which it will rely to decide complex issues, we believe it should independently verify that information. Here, the Commission should have requested the specific data on which the survey results were based. We believe that data should have been checked for accuracy, reliability, and adequacy before being relied on by the Commission.

We believe that prior to reaching its decision in the Trunkline case a carefully designed marketability study of LNG under Opinion 796 would have enabled the Commission to make a more informed decision. Some of the more important questions that needed to be addressed include

- customers' projected demands for LNG to meet anticipated needs,
- fuel options available to these customers,
- price ranges for these optional fuels, and
- uses that will be made of the LNG.

COMPANY AND AGENCY COMMENTS
AND OUR EVALUATION

In commenting upon a draft of this report both Trunkline and the Commission (see encs. I and II) questioned the importance of the survey of customers in reaching the decision expressed in Opinion 796A. Trunkline stated that "neither the survey, the responses, nor even a precise analysis of the various responses of the various customers was presented." The Commission said that we overstated the survey's influence because "the question of whether this long-term need exists is independent of the near-term marketability of LNG under incremental pricing." However, Opinion 796A states, "One of the Commission's primary concerns is in the financeability of the project." In this regard, the Opinion clearly states that the Commission gave consideration to oral arguments and indicates by reference to the

statements of Trunkline's counsel that it was particularly thinking of Trunkline's survey when it determined that the project would be unfinanceable under incremental pricing.

Trunkline did not believe that the categories into which we placed the responses were appropriate, suggesting instead that they should have been counted as (1) firm commitments to purchase on an incremental basis, (2) conditional commitments to purchase, (3) refusal to purchase on an incremental basis, and (4) uncertainty of position. If the responses were categorized in this manner the numbers would be slightly different than we show in this report, but they would not alter our conclusion that the survey was inadequate as evidence of marketability. As Trunkline points out, there would still be the same percentage of firm commitments. The conditional commitments and refusals would also remain the same. The only responses which might be reclassified are those of five customers, representing 19.68 percent of Panhandle's gas sales, who neither absolutely refused nor conditioned their responses to a later determination. These were, however, customers of Panhandle, which had previously indicated that it might purchase LNG under incremental pricing.

We do not agree with Trunkline's contention that its survey and testimony were not 'energy information' as contemplated by title V of the Energy Policy and Conservation Act. The term "energy information," as used in the act, includes energy distribution and consumption and data

"* * * relating to energy and fuels, such as corporate structure and proprietary relationships, costs, prices, capital investment, and assets, and other matters directly related thereto. * * *"

The statements of Trunkline's counsel concerning the survey were considered by the Commission in fulfilling its responsibilities. Trunkline's survey data pertained to energy distribution and was directly related to the cost, prices, and capital investment associated with Trunkline's LNG project.

We agree with Trunkline's position that the Commission's decision on this LNG project is not in question, and that the project is grandfathered under the Natural Gas Policy Act. A marketability study as described in this report, however, would have provided qualification of customers' need for the LNG and, as the Commission acknowledged, would have aided in deciding whether or not the LNG could have been sold under different pricing structures.

The Commission said that its decision was, in the end, a policy decision based upon qualitative evaluation of the efficient use of resources. We believe information such as that which would have been obtained from a carefully designed marketability study of LNG under Opinion 796 is an essential part of policy deliberations. Such information forms a broader base for policy decisions and helps us to assure that the decisions are economically sound.

RECOMMENDATION

We recommend that the Chairman, FERC, independently verify data presented to the Commission by interested parties when that data pertains to critical issues in its decisionmaking process.

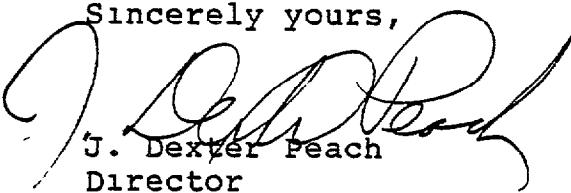
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As you know, section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the Senate Committee on Governmental Affairs and the House Committee on Government Operations no later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report.

Copies of this report are being sent to the Secretary of Energy; the Director, Office of Management and Budget; the Senate Committee on Governmental Affairs; the House Committee on Government Operations; the House Committee on Appropriations; the Senate Subcommittee on Public Works, Committee on Appropriations; and other interested Members of Congress.

We appreciate the courtesy and cooperation extended to our staff during the review.

Sincerely yours,



J. Dexter Peach
Director

Enclosures - 2

TRUNKLINE GAS COMPANY
3000 BISSONNET AVENUE
P O BOX 1642
HOUSTON TEXAS 77001

HARRY S WELCH
SENIOR VICE PRESIDENT
AND
GENERAL COUNSEL

March 28, 1979

Mr. J Dexter Peach, Director
Energy and Minerals Division
U S. General Accounting Office
441 G Street, N.W.
Washington, D.C. 20548

Attention: Mr. Gerald Elskens
Energy Regulation Branch
Room 3007
941 North Capitol St., N.E.

Dear Mr. Peach:

This letter is written on behalf of Trunkline Gas Company and Trunkline LNG Company in response to your letter dated March 8, 1979, addressed to Mr. Richard L. O'Shields and forwarding for comments a portion of a draft report by the GAO applicable to the Trunkline LNG Company and Trunkline Gas Company consolidated certificate proceedings before the FPC. The portion of the draft report submitted is limited to the issue of pricing the revaporized LNG to Trunkline Gas Company's customers on an incremental basis or a rolled-in basis. In a telephone conversation with Mr. John D. Townsend on March 21, Mr. Elskens granted an extension until March 30, to respond.

Your files will reflect correspondence to and from Trunkline with respect to this matter dated February 14, 1978, February 21, 1978, March 8, 1978, March 14, 1978, April 19, 1978, April 28, 1978, May 23, 1978, May 30, 1978, and June 9, 1978. At all times Trunkline has expressed continuing concern that the study being conducted is a collateral reexamination of a final certificate proceeding on a formal record made in public hearings, inconsistent with the Administrative Procedure Act and the Natural Gas Act, and is not a verification examination of energy information as contemplated by Title V of the Energy Policy and Conservation Act. As hereinafter discussed, we believe the draft report shows our concern to be well founded.

Much of the text of the draft report reviews, on a narrow, selective and inaccurate basis, some of the evidence and proceedings. The entire proceeding was, of course, an adjudicatory hearing under the Administrative Procedure Act and the Natural Gas Act, with all the procedural characteristics of such hearings, including

notice, formal hearing procedure, and right of cross-examination. These proceedings culminated in an Initial Decision of the Administrative Law Judge and thereafter Opinions 796 and 796-A of the Commission. The orders and the Certificate of Public Convenience and Necessity issued with Opinion No. 796-A have long since become final and non-appealable, and many millions of dollars have been, and will be, expended to construct and place in operation during 1980 the projects involved. Although interim financing has been arranged for the Trunkline LNG facilities, permanent financing must yet be arranged.

Under the circumstances, we believe the GAO should recognize the sensitivity of a project in this stage to the unexpected and unintended outcomes of adverse or critical reports and publicity. In this case any unfortunate outcome would seem most unfair and undeserved since the "criticism" in the draft report appears to be both mild and not directed at either our project or our companies. Accordingly this letter has a dual intent (1) to point out areas of difference; and (2) to request that no report be made.

We believe that GAO should conclude that its investigation into incremental pricing was precluded as to Trunkline's project by the passage of the Natural Gas Policy Act of 1978, which foreclosed the need for review of projects certificated before May 1, 1978 [see section 207(a) of Title II of the NGPA]. Without question the Trunkline LNG project is grandfathered by such legislation. Since Congress has spoken in this regard incremental pricing is no longer an issue. Since the original investigation was overtaken by events it should be set to one side as we thought had occurred. The original investigation has little utility, since the Congressional plan bears no relationship to the proposal discussed in the Trunkline LNG proceedings. If the GAO wishes to influence the implementation of the Congressionally chosen incremental pricing mechanism, it can freely participate in the current and future proceedings being conducted by the FERC in accordance with the requirements of the NGPA.

Turning to substantive comments on the contents of the draft report, we note it attempts to summarize the position of Trunkline, the FPC Staff and the FPC itself with respect to the economic theories involved in incremental versus rolled-in pricing. It does not explain the specific incremental pricing plan proposed by the FPC Staff, which was tested both by cross-examination of the proposing witnesses and by independent study and testimony by rebuttal witnesses. The Staff plan presented in the hearings would make the purchaser's entitlement for long-term gas subject to possible pre-emption on a periodic (6 months) basis. The obvious impossibility of getting a purchaser to commit to purchase gas on a long-term basis when it could be taken away at any time, thus making the project unfinancible, was pointed out on rebuttal. Since the draft report contains no discussion of the inadequacy of the

specific plan proposed to implement incremental pricing, let alone its differences from the plan ultimately adopted by Congress, it is incomplete to the point of being misleading since the reader might well assume a viable plan had been proposed

The Presiding Administrative Law Judge rejected the Staff proposal for several reasons, only one of which related to financing. The FPC's initial reversal of the Law Judge in Opinion No. 796, to which one member dissented, seemed to be predicated upon the price differential between LNG and conventional supplies and established an incremental pricing method which would have (1) required Trunkline Gas Company to sell the LNG purchased from Trunkline LNG on an incremental basis under separate rate schedules and tariff, (2) required both Panhandle and Mississippi River, large customers of Trunkline, to similarly sell LNG on an incremental basis under separate rate schedules, and (3) encouraged state commissions to require local distribution companies purchasing gas from such companies to incrementally price LNG to the ultimate consumers. The Commission also requested all state commissions in the affected states to send comments to the Commission respecting this plan. In other words, the incremental pricing method required by the Commission was in effect an incremental project contracting plan.

Upon rehearing the FPC changed its mind in Opinion No. 796-A for the various reasons stated in pages 2 to 9 inclusive of its opinion, only one of which is discussed in the report. The Commission heard arguments and had the assistance of briefs from many parties taking various positions on various issues. It is difficult to assign any one element of reasoning as being essential to the Commission's decision, especially when the Commission did not do so, nevertheless the draft report at page 5 refers to Trunkline's survey as being "a key factor in the Commission's decision to revoke incremental pricing . . ." However the Commission discussed and relied upon other reasoning and expressly stated a primary factor was the need for the LNG to be available on the Trunkline Gas system as insurance to protect Priority 1 loads and Priority 2 plant protection requirements (mimeo, p. 7). On the issue of incremental pricing, it is pertinent to note that in petitions for rehearing and oral argument, most of the parties addressed the issue and all save the Staff and one other party opposed incremental pricing (mimeo, p. 2). Furthermore, of the State Commissions in the affected states, responding to the Commission's request, none indicated that they would require incremental pricing of the LNG to the ultimate consumers and the state Commissions of Indiana, Illinois, Kansas, Michigan, Missouri and Ohio supported the rolled-in method (mimeo, p. 4). No discussion or mention of the other grounds for the decision are contained in the draft report which thus is incomplete to the point of being misleading since the reader might well assume any defects in the survey would necessitate a reversal. That obviously would not be the case since alternate grounds were stated and relied upon.

Trunkline believes the GAO misunderstands the presentation of the survey to the Commission. First of all, neither the survey, the responses, nor even a precise analysis of the various responses of the various customers was presented. Since none of such material was presented to the Commission, it cannot be "energy information", the analysis contained in the draft report is irrelevant, and the draft report should be dismissed from consideration since there is no statutory justification for either the investigation or the report.

Trunkline's counsel did no more than report Trunkline's perception of the total situation in which it found itself, with the survey being only one aspect. Indeed, counsel could do no other, since both Trunkline, the Commission and the other parties were limited by the well accepted principle, to which he alluded at page 2777, that argument is to be limited to matters on the record. He did have the duty to inform the Commission of Trunkline's current position on the total situation, i.e., without changes the project as originally certificated was unacceptable. Since an applicant may refuse a certificate following its issuance, this distinction was not lost on the Commission which states at mimeo page 7 of its opinion.

Upon consideration of the arguments raised by the parties on rehearing, in the comments, and at oral argument, as well as a reconsideration of the record in this case and of Opinion No. 796, the Commission is convinced that the incremental pricing method should not be used herein and that the rolled-in method should be used in its stead. One of the Commission's primary concerns is in the financeability of the project. Trunkline has stated that the incremental pricing provision, if upheld on rehearing, would probably render the project unfinanceable. 4/ Trunkline has further stated that with incremental pricing, there is not enough present firmness of demand to warrant going forward with the project on an incremental basis. The response of Staff and EDF, et al to this statement is that if the demand on the Trunkline system does not exist for LNG at its "true market cost", then the gas should not be imported and the project should be allowed to fail because there is not enough market demand for the LNG to justify the project. The evidence in this proceeding indicates that the true issue facing the Commission is not whether to certificate this project and require incremental or rolled-in pricing, but rather whether to certificate this project with rolled-in pricing or to, in effect, kill the project by using incremental pricing, an action tantamount in result to denying Trunkline's request for certification of the project. Given the record in the proceeding, and considering all factors, the Commission finds that certification of this project is in the public interest.

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- 4/ See statement of Trunkline Counsel, Tr 2776
In addition, Trunkline argues that the fixed rate provision, and to a lesser extent, the minimum bill provision and lack of approval of the escalation in the purchased gas supply and the shifting contracts jeopardize the financeability of the project. These matters will be discussed later in the opinion.

The foregoing indicates the Commission did not regard a mention of the survey as being outside the bounds of proper argument. More importantly, it shows the emphasis given in the draft report to be undue when taken out of context. It also shows why the survey is not "energy information".

Even if the draft report's analysis of the survey responses is deemed relevant, it is flawed in several respects. First, it implicitly assumes, without justification we believe, that the non-responding customers would desire to purchase incrementally. Certainly a business man could not so conclude. A more logical conclusion would be the non-responding customers had either already expressed their views or were so adverse and disinterested that they did not even desire to respond. Second, we cannot intellectually fit the responses into the five categories of customer responses exactly as the summary does. Third, we strongly feel the categories are misleading as stated. Instead the responses should be viewed from the standpoint of a business man who must decide whether to proceed ahead or stop a project involving the commitment of millions of dollars. (1) firm commitments to purchase on an incremental basis, (2) conditional commitments to purchase -- often critical of incremental pricing and often conditioned upon the customer being allowed to sell on a rolled-in basis without certainty such will be the case, (3) refusal to purchase on an incremental basis, and (4) uncertainty of position -- often critical of incremental pricing. On such basis only the first category -- 62 percent of Trunkline's sales and 431 percent of Panhandle's sales using the draft report's analysis -- would be committed to purchase. This would hardly be justification for entering into a new, expensive project. The draft report simply cannot hold water as a satisfactory analysis upon which to base a business decision.

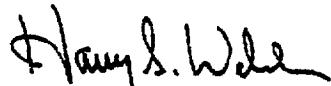
Finally the draft report's conclusion is defective in that it implies that a final determination of marketability was made upon the data obtained by the survey. Nothing in the record indicates that to be the case, either by Trunkline or the Commission. The record and the Commission's decision are awash with other considerations relating to this issue, some of which are pointed out in this letter.

In conclusion we feel the draft report is inaccurate or misleading in its analysis of the survey and the report thereof made to the Commission, invites further investigation which can have no valid purpose and could have adverse results, misconstrues the meaning of "energy information", does not report on energy information, and therefore should not be made. If you nevertheless conclude to submit it, we hereby request an opportunity to present our views in person in a meeting held for such purpose prior to adoption and publication of the Report. In any event, if such a report is to be issued, we request that the letter responses discussed therein be attached and that this letter be also attached in its entirety.

To facilitate communication within your organization, we are sending copies of this letter to Messrs. Tehas and Scott

Yours very truly,

TRUNKLINE GAS COMPANY



Harry S. Welch
Senior Vice President

FEDERAL ENERGY REGULATORY COMMISSION
WASHINGTON D C 20426

OFFICE OF THE CHAIRMAN

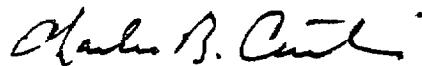
APR 4 1979

Mr. Kevin Boland
Associate Director
Energy and Minerals Division
United States General Accounting Office
Washington, D. C. 20548

Dear Mr. Boland:

Thank you for giving the Federal Energy Regulatory Commission an opportunity to review the General Accounting Office's draft letter report on Trunkline LNG and the Federal Power Commission's Opinion Nos. 796 and 796-A. Enclosed are staff comments on the report.

Sincerely,



Charles B. Curtis
Chairman

Enclosure

FERC Staff Comments on GAO's Draft Letter Report on the FPC's Actions in the Trunkline LNG Proceeding (CP74-138, et al.)

GAO's draft letter report on Trunkline LNG (Docket Nos. CP74-138, et al.) and FPC Opinion Nos. 796 and 796-A focuses on the principal issue of the marketability of the LNG if offered to customers at rates reflecting its full, or incremental, cost. The report concludes that the Federal Power Commission was remiss in conducting its duties and should have ordered a thorough marketability study of the LNG before deciding the incremental pricing question.

We would suggest that a marketability study is not the appropriate vehicle for determining whether gas should be priced on an incremental or rolled-in basis. This is largely a policy issue, involving primarily the question of efficient use of resources. Empiricism will not help to resolve this issue. At best a marketability study would have determined whether or not the LNG could have been sold under different pricing structures. Such information might have been helpful to the Commission in deciding whether or not to certify the project, but it would have been irrelevant for purposes of choosing the appropriate pricing structure.

Just as important, the FPC was deliberating the Trunkline case at the very time that Congress was debating the President's energy plan. As you know, the issue of incre-

mental pricing of natural gas was a prominent part of that debate. Against the prospect that the Congress would soon resolve this matter, it seemed particularly inappropriate for the Commission to make any radical change in its policies and create additional uncertainty through the Trunkline case. Significantly, the gas pricing design adopted in the Natural Gas Policy Act differed substantially from that initially ordered in Opinion No. 796.

The GAO contends that the FPC relied on the results of Trunkline's survey of customers in reaching a decision favoring rolled-in pricing in Opinion No. 796-A. The misleading manner in which the results were presented by the applicants, together with what is characterized as unquestioning acceptance of the results by the FPC, form the foundation for the GAO's criticism of the FPC's approval process.

We believe that the GAO has exaggerated the importance which the FPC attached to the applicant's survey of its customers. As noted in the GAO report, one of the primary factors in the FPC's approval of rolled-in pricing was the expected need over the long-term for LNG by high-priority customers. To a considerable extent, the question of whether this long-term need exists is independent of the near-term marketability of LNG under incremental pricing. GAO's letter report does not differentiate these short

versus long-term consideration, and thereby fails to note the fundamentally qualitative basis for the FPC's policy decision regarding long-term need.