

ALASKA LEGISLATURE SPECIAL COMMITTEE / SUBJECT FILES 8672

1048 SCOMM 28: JOINT GAS PIPELINE COMMITTEE. 1981-82

System (ANGTS). 2/ The Commission directed the Chief Accountant to include in the reports his opinion as to whether "expenditures are properly assignable to the project and of a nature that would qualify the expenditures for eventual inclusion in the rate base, whether the accounting used by the sponsors meets the requirements of the Uniform System of Accounts and generally accepted accounting principles, and whether the project sponsors are in compliance with other accounting and reporting regulations and requirements of the Natural Gas Act, the Decision, and the certificate of public convenience and necessity." 3/

The Commission has, to date, received three audit reports from the Office of the Chief Accountant. 4/ The first report covers pre-partnership expenditures by five individual companies which later became partners in ANNGTC. Those expenditures include Allowance for Funds Used During Construction (AFUDC), expenses related to the preparation and presentation of applications for the construction certificate for the Alaskan pipeline, and expenses

2/ ANGTS was authorized by the ANGTA, 15 U.S.C. §§ 719-719o and the President's Decision and Report to Congress on the Alaska Natural Gas Transportation System, (Executive Office of the President, Energy Policy and Planning, September 1977), as enacted into law by H. J. Res. 621, Pub. Law No. 95-100 (November 2, 1977). The Commission, by an order issued December 16, 1977 in this docket, issued conditional certificates of public convenience and necessity to construct and operate the ANGTS. Several competing companies, including the Northwest Alaskan Pipeline Company (the successor in interest to the Alcan Pipeline Company, whose proposed pipeline route was selected by the President in his Decision), formed a partnership to construct and operate the Alaska section of the ANGTS on February 1, 1978. That partnership is known as the Alaska Northwest Natural Gas Transportation Company (ANNGTC). Expenses incurred before the formation of the partnership are referred to as "pre-partnership expenditures."

3/ Administrative Order No. 4, at 3.

4/ The reports are each entitled "Report on the Results of Audit of Expenditures by the Alaskan Northwest Natural Gas Transportation Company . . ." and were submitted in August and October 1980.

made through membership or participation in the Gas Arctic/Northwest Study Group. 5/

The second report covers expenditures incurred by ANNGTC partners from February 1, 1978 through December 31, 1978, including AFUDC.

The third report covers expenditures, including AFUDC, incurred from January 1, 1979 through December 31, 1979 and charged to various gas plant accounts of the partnership. In both the second and third reports, a substantial part of the AFUDC claimed is related to pre-partnership and other expenditures at issue in the first report.

The audit reports are attached to this order for review by interested persons.

The Commission orders:

Within 60 days of the issuance of this order, any interested person shall show cause why the Commission should not adopt, for purposes of rate base determination pursuant to the Natural Gas Act, ANGTA, and the President's Decision, the data and opinions set forth in the three Reports on Results of Audit prepared by the Office of the Chief Accountant.

By the Commission.

(S E A L)



Kenneth F. Plumb,
Secretary.

5/ Also known as the Canadian Arctic Gas Study Limited (CAGSL).

**REPORT ON
RESULTS OF AUDIT OF EXPENDITURES
BY PARTNERS
OF THE
ALASKAN NORTHWEST NATURAL GAS
TRANSPORTATION COMPANY
WHICH WERE
INCURRED PRIOR TO THE
FORMATION OF THE PARTNERSHIP
ON FEBRUARY 1, 1978
(DOCKET NO. CP78-123, et al.)**

**August 1980
Division of Audits
Office of Chief Accountant
Federal Energy Regulatory Commission**

REPORT ON RESULTS OF AUDIT OF EXPENDITURES
BY PARTNERS OF THE ALASKAN NORTHWEST
NATURAL GAS TRANSPORTATION COMPANY WHICH
WERE INCURRED PRIOR TO THE FORMATION OF
THE PARTNERSHIP ON FEBRUARY 1, 1978
(DOCKET NO. CP78-123, et al.)

INTRODUCTION

This is the first in a series of reports on the results of audits of expenditures related to the construction of the Alaska Natural Gas Transportation System (ANGTS)^{1/}. The audits and reports are being made pursuant to the directions contained in Administrative Order No. 4, issued April 18, 1979.

This report conveys the results of the staff's initial audit of expenditures charged to the Alaskan section of the ANGTS. The initial audit covered expenditures incurred prior to the formation of the partnership (Alaskan Northwest Natural Gas Transportation Company (ANNGTC)) on February 1, 1978, for the construction and operation of the Alaskan section.

Amounts charged to the Alaskan section for pre-partnership expenditures totaled \$57,415,070^{2/}.

^{1/} ANGTS was authorized by the Alaska Natural Gas Transportation Act of 1976 (ANGTA), 15 U.S.C. 719 et seq. and the President's Decision and Report to Congress on Alaska Natural Gas Transportation System, as enacted into law, H.J. Res. 621, Pub. L. No. 95-108 (November 2, 1977).

^{2/} See Exhibit No. 1.

SUMMARY

Prior to the formation of the partnership, for the purpose of construction and operation of the Alaskan section of the ANGTS under a Conditional Certificate of Public Convenience and Necessity issued by FERC on December 16, 1977 (Docket No. CP78-123, et al.), substantial sums were expended by the individual companies^{3/}.

One partner, Northwest Alaskan Pipeline Company (Northwest) was the original applicant for the route and pipeline proposal ultimately selected and conditionally authorized in Docket No. CP78-123, et al. Northwest's claimed pre-partnership expenditures of \$19,048,187 were related to the preparation and presentation of its application for the construction certificate for an Alaskan pipeline^{4/}.

Four other partners, Pan Alaska Gas Company (Pan Alaska), Calaska Energy Company (Calaska), Pacific Interstate Transmission Company (Arctic) (Pacific), and Northern Arctic Gas Company (Northern), claimed pre-partnership expenditures totaling \$38,366,883 which were made through their membership and/or participation in the Gas Arctic/Northwest Project Study Group, better known by its service organization name, Canadian Arctic Gas Study Limited (CAGSL)^{4/}.

^{3/} In some instances the expenditures were actually made by affiliated or other companies. For clarity in presentation, this report attributes such expenditures to the current partner company.

^{4/} See Exhibit No. 1.

CAGSL sponsors unsuccessfully applied to FERC and the National Energy Board of Canada for certificates to construct a gas pipeline to transport Alaskan gas to the United States via a predominantly Canadian route.

With respect to the pre-partnership expenditures claimed by Northwest, the staff concludes that:

1. Expenditures of \$15,190,609, including Allowance for Funds Used During Construction (AFUDC) of \$965,272, are properly assignable to the Alaskan section of the ANGTS and are of a nature that would qualify for eventual inclusion in rate base.
2. Expenditures of \$193,236, including AFUDC of \$12,278 are not of a nature that would qualify for eventual inclusion in rate base, and should be disallowed.
3. Expenditures of \$3,664,342, including AFUDC of \$232,847 may not be properly assignable to the Alaskan section of the ANGTS for eventual inclusion in rate base. Requests to Northwest for additional information on these expenditures have not been answered. Therefore, staff proposes that these expenditures be disallowed without prejudice to Northwest's reclaiming them upon submission of appropriate supporting information.

With respect to the pre-partnership expenditures claimed by the four other partners, the staff concludes that:

1. None of the claimed expenditures, totaling \$38,366,883, including AFUDC of \$6,587,916, are properly assignable to the Alaskan section of the ANGTs and such expenditures should be disallowed.
2. Calaska claimed \$1,300,277 in excess of its actual expenditures due to the method used to account for Canadian/United States dollar exchange differences. However, no separate adjustment for this item will be necessary if conclusion 1 above is sustained, since all claimed expenditures would be disallowed.
3. The parent companies of three of the partners, Pacific Lighting Service Company (Pacific Interstate Transmission Company (Arctic)), Panhandle Eastern Pipeline Company (Pan Alaska Gas Company), and Northern Natural Gas Company (Northern Arctic Gas Company) have already recovered significant portions of their pre-partnership expenditures via tariff charges to their existing customers. The staff is proposing that the claimed pre-partnership expenditures be disallowed to the extent that their parent companies had recovered such expenditures through January 31, 1978, and that any recoveries made after that date be credited against any of their remaining pre-partnership expenditures. However, no separate adjustments for this item will be necessary if conclusion 1 above is sustained, since all claimed CAGSL expenditures would be disallowed.

4. Pacific claimed \$23,375 in excess of its actual expenditures due to its failure to reduce such expenditures by interest reimbursements received. However, no separate adjustment for this item will be necessary if conclusion 1 above is sustained, since all claimed expenditures would be disallowed.
5. The parent companies of Pan Alaska, Northern and Pacific have already claimed the pre-partnership CAGSL expenditures as tax deductions for Federal income tax purposes. The staff is proposing that the deferred taxes resulting from this procedure be recorded on ANNGTC's books to assure that the tax benefits are properly associated with the CAGSL expenditures in making AFUDC computations, computing Federal income tax allowances, and establishing rate base. This item becomes moot if conclusion 1 above is sustained, since all claimed CAGSL expenditures would be disallowed.
6. AFUDC amounts are incorrectly computed and will require downward adjustment in the event that any portion of the pre-partnership expenditures are ultimately allowed. However, no separate adjustment for this item will be necessary if conclusion 1 above is sustained, since all claimed expenditures would be disallowed.

The bases for the conclusions cited above are discussed in the text of this report.

SCOPE OF AUDIT

The audit covered claimed pre-partnership expenditures totaling \$57,415,070, including AFUDC. Of these pre-partnership expenditures, \$38,366,883, including AFUDC, is related to disbursements made by four companies for their shares of the costs incurred by Canadian Arctic Gas Study Limited (CAGSL). Therefore, it was necessary for the staff to examine the total costs incurred by CAGSL \$154,849,479 (Canadian) to determine whether the partners' expenditures were properly assignable to the Alaskan section of the ANGTS.

The audit included an examination of the accounting and other records to the extent deemed necessary to determine whether:

1. The various financial statements and reports properly reflected the underlying records and documents,
2. The expenditures were adequately documented and supported,
3. The accounting for the expenditures met the requirements of the Uniform System of Accounts and generally accepted accounting principles, and
4. The expenditures were properly assignable to the Alaskan section of the ANGTS and were of a nature that would qualify for eventual inclusion in rate base.

RESULTS OF AUDIT

A. Northwest Alaskan Pipeline Company

Northwest claimed pre-partnership expenditures of \$19,048,187, including \$1,210,397 of AFUDC. The staff determined that

1. Expenditures of \$15,190,609, including \$965,272 of AFUDC, were made in the planning, researching, developing, formulating, testing and filing processes related to the successful application before the Commission to build the Alaskan section of the ANGTS. These expenditures were found to be properly assignable to ANNGTC, and of a nature that would qualify them for eventual inclusion in ANNGTC's rate base.

2. Expenditures of \$193,236 including \$12,278 of AFUDC are not of a nature that would qualify them for eventual inclusion in ANNGTC's rate base. These expenditures fall into the following categories:

a. Influencing Public Opinion

Expenditures of \$115,406, including \$7,333 of AFUDC relate to payments to various public relations firms for preparing and disseminating information about the Alcan Proposal and the two alternative proposals during the selection process. A review of the brochures, news ads and news articles resulting from these expenditures disclosed that they were intended and used to influence public opinion and the opinions of public officials during the selection process of the Alaskan Gas Project.

The Uniform System of Accounts requires that expenditures of this nature be recorded in Account 426.4, Expenditures for certain civic, political and related activities, a non-utility expense account.

b. Lobbying Activities

Expenditures of \$57,888, including \$3,678 of AFUDC relate to payments to two firms for lobbying services.

One firm performed services which involved legislative efforts to secure passage of the Natural Gas Policy Act of 1978. This emanated from President Carter's 1977 Energy Plan which proposed substantial changes to the Natural Gas Act. Northwest requested the firm to analyze the President's proposal and determine its impact on the Alaska Natural Gas Transportation System. After analysis of the President's proposal, the firm began contacting members of both the House and Senate and their staffs to inform them of the impact of gas pricing legislation on the Project. Position papers on the Project and letters to all Senators and Representatives were prepared and sent during the deliberations in both Houses on the pending legislation. The firm monitored all public sessions and met personally with conferees, and their staff on a regular basis through the 9-month conference. Numerous proposals and counter-proposals were offered by the conferees and this firm prepared position papers on the impact of the various

proposals on the Project. Once the conferees agreed on a compromise bill, the firm again contacted members of both the House and Senate urging passage of the compromise bill. The compromise bill was ultimately passed and was signed into law in November of 1978.

The second firm focused its efforts on gaining Congressional ratification of the President's Decision on the ANGTS.

The Uniform System of Accounts requires that expenditures of this nature be recorded in Account 426.4, Expenditures for certain civic, political and related activities, a non-utility expense account.

c. Celebration Costs

Expenditures of \$18,874, including \$1,199 of AFUDC, relate to payments for receptions held in Washington, D. C., Anchorage, Alaska, and Fairbanks, Alaska to celebrate President Carter's selection of the Alcan Project proposal to construct the Alaskan Natural Gas Pipeline.

The Commission, in various cases, has ruled that celebration-type expenditures are not properly expendable to the plant or operating expense accounts, but are of a nature that should be recorded in Account 426.5, Other deductions.

d. Donations

Expenditures of \$1,068, including \$68 of AFUDC, relate to a contribution to the Hubert Humphrey Institute of Public Affairs (University of Minnesota Foundation).

The Uniform System of Accounts requires that expenditures of this nature be recorded in Account 426.1, Donations, a non-utility expense account.

3. Expenditures of \$3,664,342, including \$232,847 of AFUDC, were not sufficiently supported to enable the staff to determine whether they are properly assignable to the Alaskan section of the ANGTS for eventual inclusion in rate base. Requests to Northwest for additional information on these expenditures have not resulted in responses which clearly document the nature and character of the items. These expenditures fall into two general categories:

- a. Amounts paid to a number of law firms for services which appear to include political lobbying or public relations efforts designed to influence public opinion concerning the project and, as such, would not be allowable in plant accounts under the provisions of FERC's Uniform System of Accounts.

- b. Amounts paid to a number of consultants where sufficiently competent evidential material (i.e. contracts, written agreements, vendor memoranda, etc.) either did not exist or were not made available. Therefore, there was no adequate basis upon which to evaluate the propriety of the assignment of the costs to the project, or their qualification for eventual inclusion in rate base.

The staff proposes that these expenditures be disallowed, without prejudice to Northwest's reclaiming them upon submission of appropriate supporting information.

B. Other Partners

The other four partners claimed pre-partnership expenditures totaling \$38,366,883, including AFUDC of \$6,587,916. All of these expenditures were related to their membership and/or participation in CAGSL.

1. Review of CAGSL's Expenditures

During its existence, CAGSL^{5/} expended \$154,849,479 (Canadian) in the planning, researching, developing, formulating, testing and filing processes in an unsuccessful attempt to obtain the necessary

^{5/} See Exhibit No. 2 for background data on CAGSL.

Canadian and U. S. governmental certificates and permits required to construct and operate a primarily Canadian routed Natural Gas Transmission Line to transport Alaskan and Canadian Gas to the lower 48 states. The staff has determined that the amounts expended were properly authorized in accordance with CAGSL agreements, adequately documented and supported, and reasonably classified by cost categories. The cost categories and staff's determinations regarding possible future value to the Alaskan section of the ANGTS are as follows:

CAGSL Expenditures (Canadian Dollars)

<u>Cost Categories-Direct</u>	<u>Possible Future Value or Usefulness</u>	<u>No Future Value</u>	<u>Total</u>
Engineering and Construction Planning	\$ 8,762,705	\$ 57,057,095	\$ 65,819,800
Environmental Studies and Research	3,988,166	14,569,834	18,558,000
Sociological	763,138	3,554,362	4,317,500
Public Affairs	-	3,202,200	3,202,200
Gas Reserves and Market Studies	446,964	1,547,436	1,994,400
Reproduction of Hearing Material and Application	-	2,134,800	2,134,800
Environmental Impact Study	-	2,335,600	2,335,600
Termination Costs	-	1,267,100	1,267,100
Working Capital Included in Equalization at Merger ^{6/}	-	243,600	243,600
Subtotal	<u>13,960,973</u>	<u>85,912,027</u>	<u>99,873,000</u>
Direct Cost Ratios	<u>13.98%</u>	<u>86.02%</u>	<u>100%</u>
 <u>Cost Categories-General (Allocated Using Direct Cost Ratios Shown Above)</u>			
Finance, Accounting, Legal and Other Advisors	2,329,250	14,332,050	16,661,300
General and Administrative	4,361,187	26,834,713	31,195,900
Depreciation and Amortization	<u>108,247</u>	<u>666,053</u>	<u>774,300</u>
Costs through Aug. 31, 1977	<u>20,759,657</u>	<u>127,744,843</u>	<u>148,504,500</u>
Cash Calls Required from Sept. 1, 1977 through Jan. 31, 1978 ^{7/}	-	6,345,000	6,345,000
Totals at Jan. 31, 1978	<u>\$20,759,657</u>	<u>\$134,089,843</u>	<u>\$154,849,500</u>
Total Allocation	<u>13.41%</u>	<u>86.59%</u>	<u>100%</u>

^{6/} The Working Capital Included in the Equalization at Merger was payable to the CAGSL participants.

^{7/} The expenditures incurred by CAGSL after August 31, 1977 and through January 31, 1978 were for termination payments related to activities after CAGSL's dissolution.

The \$134,089,843 (Canadian) of CAGSL expenditures which are listed above as having no future value are not considered to be properly assignable to the Alaskan section of the ANGTS or of a nature that would qualify for inclusion in rate base because they have one or more of the following disqualifying features:

- a. They have no specific direct provable relationship or future benefit to the approved Alaskan section of ANGTS. The type expenditures included in this category relate to specific design, location, siting, and other items unique to the unsuccessful route;
- b. They are duplicative to other expenditures specifically related to the approved Alaskan section of the ANGTS. This classification includes all types of duplicative filing fees and related payments to the various U. S. and Alaskan governmental bodies;
- c. Similar activities or task related expenditures have never been considered capitalizable items by the Commission in the past. Costs of this classification are related to political lobbying and public relations type of activities;

d. They specifically relate to Canadian:

- (1) line design or layout,
- (2) land or rights-of-way,
- (3) gas supply,
- (4) regulatory filings.

Application of the findings of our audit of CAGSL expenditures to the related American dollar amounts recorded in ANNGTC's books, exclusive of AFUDC amounts, gives the following results.

	CAGSL Costs Recorded on <u>ANNGTC Books</u>	No Future Value ^{8/}	Possible Future Value ^{9/}
Pre-partnership Expenditures	<u>\$31,778,967</u>	<u>\$27,517,407</u>	<u>\$4,261,560</u>
Pan Alaskan Gas Company	\$ 8,011,392	\$ 6,937,064	1,074,328
Calaska Energy Company	7,783,286	6,739,547	1,043,739
Pacific Interstate Transmission Company (Arctic)	8,020,863	6,945,265	1,075,598
Northern Arctic Gas Company	<u>7,963,426</u>	<u>6,895,531</u>	<u>1,067,895</u>
	<u>\$31,778,967</u>	<u>\$27,517,407</u>	<u>\$4,261,560</u>

^{8/} Based upon allocation of 86.59% developed above.

^{9/} Based upon allocation of 13.41% developed above.

While the audit indicated that \$4,261,560 of pre-partnership expenditures may have possible future value to the approved Alaskan section of the ANGTS, no value at all has yet been demonstrated. Therefore, staff concludes that none of the \$38,366,883 of pre-partnership expenditures associated with CAGSL activities (\$31,778,967 of CAGSL costs plus \$6,587,916 of AFUDC related thereto) and properly assignable to the Alaskan section of the ANGTS.^{10/}

^{10/} ANNGTC's justifications for assigning CAGSL expenditures to the Alaskan section of the ANGTS are included in an application to FERC dated February 2, 1979. See Exhibit No. 4, page 5 to end.

2. Calaska Energy Company - Improper Method of Accounting for Canadian/United States Dollar Exchange Differences

Calaska was established in December 1978 as a wholly-owned subsidiary of Pacific Gas & Electric Company to participate in the ANNGTC partnership as of February 1, 1978.

In July of 1972, Pacific Gas & Electric Company (PG&E), Pacific Gas Transmission Company (PGT) (53% owned by PG&E), Montana Power Company and Alberta Natural Gas Company (a Canadian company 45% owned by PGT) joined the CAGSL as a group liable for one participant's share of CAGSL's expenditures.

Under the terms of the group's agreement, all payments to CAGSL were made in Canadian dollars by Alberta Natural Gas Company, without reimbursement by the other members of the group. The expectation was that CAGSL's proposal(s) would be successful and that Alberta Natural Gas Company would recover its net CAGSL expenditures by claiming them as part of the cost of the project(s). The agreement also provided that, in the event Alberta Natural Gas Company was unable to recover, it could require the other members of the group to reimburse it for its net CAGSL expenditures as follows:

Pacific Gas & Electric Company	55.65%
Pacific Gas Transmission Company	18.55%
Montana Power Company	7.25%
	<u>81.45%</u>

To the extent that the net CAGSL expenditures were irrecoverable by any members of the group, the ultimate loss would be borne in the same percentages shown above, with Alberta Natural Gas Company bearing the balance, 18.55%, of such loss.

In December 1978, Alberta Natural Gas Company determined that it could not recover any of its net CAGSL expenditures and called upon the other three members of the group to reimburse it for their agreed upon shares of such expenditures.

On December 31, 1978, but as of February 1, 1978, Calaska claimed, as pre-partnership expenditures on behalf of the group, all of Alberta Natural Gas Company's net CAGSL expenditures, including AFUDC through January 31, 1978^{11/}. These expenditures totaled \$9,689,376 (Canadian). At December 31, 1978 conversion rates, the American dollar equivalent was \$8,156,517. However, instead of claiming that amount as pre-partnership expenditures, Calaska computed their claim on a hypothetical basis, using conversion rates that were in effect at the time each Canadian dollar payment was made by Alberta Natural Gas Company to CAGSL.

^{11/} Cash reimbursements by the group to Alberta Natural Gas Company also included AFUDC from February 1, 1978 to December 31, 1978, but these amounts were not claimed because Calaska will accrue AFUDC on the claimed expenditures commencing February 1, 1978.

As a result, Calaska claimed pre-partnership expenditures of \$9,456,744, whereas the actual American dollar amount which would have been required at December 31, 1978 to repay Alberta Natural Gas Company for all of its net expenditures to CAGSL through January 31, 1978 was only \$8,156,517, or \$1,300,227 less.

While Calaska's pre-partnership expenditures are overstated by \$1,300,227 because of the improper method used to account for Canadian/American dollar exchange differences, no separate adjustment for this item will be necessary if staff's position with respect to disallowance of all claimed CAGSL expenditures is sustained (see item 1 above).

3. Pacific Interstate Transmission Company (Arctic) -
Interest Reimbursements

Pacific's claimed pre-partnership expenditures include AFUDC on payments made to CAGSL by an affiliated company. However, such expenditures were not reduced by \$23,375 of interest reimbursements received by the affiliated company when various equalization payments were received as new companies joined the CAGSL group. Accordingly, Pacific's claimed pre-partnership expenditures are overstated by \$23,375 and staff proposes that such amount be disallowed. No separate adjustment for this item will be necessary if staff's position with respect to disallowance of all claimed CAGSL expenditures is sustained (see item 1 above).

4. Recovery of CAGSL Expenditures Via Tariff Charges

The parent companies of three of the partners have already recovered significant portions of the claimed CAGSL pre-partnership expenditures through tariff billings to existing customers. Additionally, two of the partners' parent companies have recovered the carrying costs associated with some of the CAGSL pre-partnership expenditures.

a. Northern Arctic Gas Company

As of June 30, 1979, Northern, through the rates charged by its parent, Northern Natural Gas Company, had recovered at least \$2,333,261 of its pre-partnership CAGSL expenditures. These expenditures were allowed in determining Northern Natural Gas Company's cost of service as follows:

<u>Docket No.</u>	<u>Amount</u>
RP74-80	\$ 243,840
RP75-39	243,840
RP77-56	577
R&D Tracker	1,845,004
	<u>\$2,333,261</u>

In addition to the amounts shown above, \$353,289 of expenditures relating to CAGSL regulatory costs, along with other regulatory costs, have been and are being amortized as charges to gas operating expenses. Therefore, there is a presumption that the \$353,289 has been or will be recovered by Northern Natural Gas Company's tariff rates.

Northern's claimed pre-partnership CAGSL expenditures do not give recognition to the recoveries that have been made by its parent company.

Prior to October 31, 1976, all payments to CAGSL, less related accumulated deferred income taxes, were recognized in Northern Natural Gas Company's rate base and rates. Beginning November 1, 1976, only the amounts listed below were allowed in rate base:

<u>Month</u>	<u>Net Amount Reflected in Rate Base</u>
<u>1976</u> - November	\$1,772,277
December	898,562
<u>1977</u> - January	1,037,081
February	1,151,974
March	1,261,157
April	1,321,863
May	1,429,392
June	1,515,412
July	1,623,665
August	1,798,420
September	1,835,996

While various portions of the CAGSL expenditures were included in rate base, and at least \$2,333,261 has been recovered in cost of services through June 30, 1979, AFUDC was accrued and capitalized by Northern based on the total CAGSL expenditures without giving recognition to the rate treatment afforded part of these same expenditures. As a result, AFUDC related to the CAGSL pre-partnership expenditures is also overstated.

b. Pan Alaska Gas Company

As of June 30, 1979, Pan Alaska, through its parent, Panhandle Eastern Pipeline Company, had recovered \$4,160,970 of its pre-partnership CAGSL expenditures. These expenditures were allowed in determining Panhandle Eastern Pipeline Company's cost of service as follows:

<u>Year</u>	<u>Amount</u>
1973	\$ 685,727
1974	1,095,763
1975	1,778,005
1976	206,220
1977	206,220
1978	189,035
	<u>\$4,160,970</u>

Pan Alaska's claimed pre-partnership CAGSL expenditures do not give recognition to the recoveries that have been made by its parent company.

In addition, Pan Alaska has computed AFUDC on the total CAGSL expenditures without giving recognition to the cost of service rate recoveries made by its parent company. As a result, AFUDC related to CAGSL pre-partnership expenditures is overstated.

c. Pacific Interstate Transmission Company (Arctic)

As of June 30, 1979, Pacific, through its affiliate, Pacific Lighting Service Company, had recovered \$1,148,044 of its pre-partnership CAGSL expenditures. These amounts have been recovered since January 1, 1978 through rates established by the California Public Utilities Commission.

Pacific's claimed pre-partnership expenditures do not give recognition to recoveries that have been made by its affiliated company.

In addition, all of Pacific's claimed CAGSL expenditures have been allowed in rate base, on a net-of-tax basis, by the California Public Utilities Commission. However, Pacific has computed AFUDC on total CAGSL expenditures without giving recognition to the rate base treatment allowed its affiliated company for such expenditures. As a result, AFUDC related to CAGSL prepartnership expenditures is overstated.

The staff proposes that the claimed pre-partnership expenditures of Northern, Pan Alaska and Pacific be disallowed to the extent that their parent companies had recovered such expenditures through January 31, 1978, and that any recoveries made after that date be credited against any remaining pre-partnership expenditures.^{12/} However, no separate adjustments for this item will be necessary if staff's position with respect to disallowance of all claimed CAGSL expenditures is sustained (see Item 1 above).

^{12/} By letter dated April 19, 1979, to the Secretary, FERC, the attorney for ANNGTC stated that a portion of the pre-partnership expenditures claimed by Northern and Pan Alaska had been recouped. The letter states that the then outstanding balance for Northern was \$6,427,926 (a reduction of \$3,159,864) and for Pan Alaska was \$4,227,681 (a reduction of \$5,427,447). The reduced claimed outstanding balances reflect the recoveries through tariff billing by the parent companies discussed on pages 21-23 and lower AFUDC claims resulting from the lower outstanding balances. The attorney for ANNGTC proposed that appropriate adjustments, to avoid over-recovery by Pan Alaska and its affiliates and by Northern and its affiliates, be made at such time as the ANNGTC tariff becomes effective, and revenues are generated thereby.

5. Federal Income Tax Benefits Derived from CAGSL Expenditures
Need to be Associated with Claimed CAGSL Pre-Partnership
Expenditures

The parent companies of Pan Alaska, Northern, and Pacific have already claimed the pre-partnership CAGSL expenditures as tax deductions for Federal income tax purposes, thereby reducing their tax liabilities for prior years.^{13/} This procedure will result in higher tax liabilities in future years (deferred taxes).

ANNGTC is a partnership and, as such, will not pay Federal income taxes. However, ANNGTC tariff rates will include allowances for Federal income taxes which will be paid by the individual companies or their parent companies. Such tax allowances should not include any amounts for the higher tax liabilities resulting from the parent companies' use of the tax benefits associated with costs capitalized as part of the ANNGTC project. Accordingly, to assure this result, staff believes that the tax benefits already realized by the parent companies (represented by deferred taxes) should be recorded on the books of ANNGTC.

In addition, the deferred taxes balances represent a reduction in the net cost of CAGSL expenditures. Staff believes that this reduction in cost should be reflected in ANNGTC's AFUDC computations during the construction period and in ANNGTC's rate base during the period of operations by reducing the base for such computations by the deferred tax balances relating to the CAGSL expenditures.

^{13/} IRS has consistently challenged these claimed tax deductions but the dispute has not yet been resolved.

Recommendations

The staff recommends that:

1. \$15,190,609, including AFUDC of \$965,272, of Northwest's pre-partnership expenditures be allowed as charges properly assignable to the ANNGTC project and be determined as qualified for eventual inclusion in the rate base of ANNGTC.
2. \$193,236, including AFUDC of \$12,278, of Northwest's pre-partnership expenditures be disallowed as costs qualified for eventual inclusion in the rate base of the ANNGTC.
3. \$3,664,342, including AFUDC of \$232,847, of Northwest's pre-partnership expenditures be disallowed as costs properly assignable to the ANNGTC project for eventual inclusion in rate base, without prejudice to Northwest's reclaiming them upon submission of appropriate supporting information.
4. All of the \$38,366,833, including AFUDC of \$6,587,916 relating to the CAGSL pre-partnership expenditures of Calaska, Northern, Pan Alaska and Pacific be disallowed as costs properly assignable to the ANNGTC project.
5. \$1,300,227 of Calaska's claimed pre-partnership expenditures, relating to Canadian/United States dollar exchange differences, be disallowed. No separate adjustment for this item will be necessary if recommendation number 4 is adopted, since all claimed CAGSL expenditures would be disallowed.

6. \$23,375 of Pacific's claimed pre-partnership expenditures, recovered by interest reimbursements received, be disallowed. No separate adjustment for this item will be necessary if recommendation number 4 is adopted, since all claimed CAGSL expenditures would be disallowed.
7. The claimed pre-partnership expenditures of Pacific, Pan Alaska and Northern be disallowed to the extent that their parent companies had recovered such expenditures through tariff charges to their customers through January 31, 1978. Any such recoveries by the parent companies after January 31, 1978, should be credited against any remaining pre-partnership expenditures. No separate adjustments for this item will be necessary if recommendation number 4 is adopted, since all claimed CAGSL expenditures would be disallowed.
8. The deferred taxes arising from Pan Alaska, Northern and Pacific's parent companies' use of CAGSL expenditures as deductions for Federal income tax purposes be recorded on ANNGTC's books.
This recommendation becomes moot if recommendation number 4 is adopted, since all claimed CAGSL expenditures would be disallowed.

9. All AFUDC amounts included as pre-partnership expenditures by Pacific, Pan Alaska, Northern and Calaska be recomputed and reduced to reflect the recommendations in this report. ---

This recommendation becomes moot if recommendation number 4 is adopted, since all claimed CAGSL expenditures would be disallowed.

Alaska Northwest Natural Gas
Transportation Company
Pro Forma Balance Sheet
As of February 1, 1978
With Staff Adjustments Thereto

	<u>Pro Forma Balance 2-1-78</u>	<u>Staff Adjustments</u>	<u>Adjusted Balance 2-1-78</u>
<u>Assets</u>			
Plant in Service	\$ 175,617	\$ -	\$ 175,617
Less: Accrued Depreciation	(1,671)	-	(1,671)
Net Plant in Service	<u>173,946</u>	<u>-</u>	<u>173,946</u>
Construction Work in Progress:			
Northwest Alaskan Pipeline Co. Expenditures	18,874,241	(3,857,578)A/	15,016,663B/
CAGSL Expenditures	<u>38,366,883C/</u>	<u>(38,366,883)</u>	<u>-</u>
Total CWIP	<u>57,241,124</u>	<u>(42,224,461)</u>	<u>15,016,663</u>
Total Assets	<u>\$57,415,070</u>	<u>\$(42,224,461)</u>	<u>15,190,609</u>
<u>Partners' Equity</u>			
Calaska Energy Company	\$ 9,456,744	\$(9,456,744)	\$ -
Pacific Interstate Transmission Co. (Arctic)	9,667,221	(9,667,221)	-
Pan Alaska Gas Company	9,655,128	(9,655,128)	-
Northern Arctic Gas Co.	9,587,790	(9,587,790)	-
United Alaska Fuels Corp.	-	-	-
Subtotal	<u>38,366,883C/</u>	<u>(38,366,883)</u>	<u>-</u>
Northwest Alaskan Pipeline Co.	<u>19,048,187</u>	<u>(3,857,578)A/</u>	<u>15,190,609B/</u>
Total Partners' Equity	<u>\$57,415,070</u>	<u>\$(42,224,461)</u>	<u>\$15,190,609</u>

A/ Includes \$245,125 of AFUDC
B/ Includes \$965,272 of AFUDC
C/ Includes \$6,587,916 of AFUDC

BACKGROUND DATA

CANADIAN ARCTIC GAS STUDY GROUP LIMITED (CAGSL)

CAGSL, also known as the Gas Arctic/Northwest Project Study Group, was a consortium of United States and Canadian energy companies (see Exhibit 3 for a list of the members and their contributions) which attempted to obtain the necessary certificates and permits required of the Canadian and U. S. Governments to build a pipeline transversing Alaska and Canada.

The project had its beginning in 1967 when Trans Canada Pipelines Limited, Michigan Wisconsin Pipeline Company and Natural Gas Pipeline Company of America organized the Northwest Project Study Group (NPSG) to conduct engineering and feasibility studies for a natural gas pipeline system to transport natural gas from the Canadian Northwest Territories to gas markets in the United States. In June of 1969, the NPSG was expanded to include studies for a pipeline from Alaska and the Mackenzie Delta. The consortium membership was expanded to include Standard Oil Company of Ohio, Atlantic Richfield Company and Humble Oil & Refining Company (Exxon).

In 1969, Alberta Gas Trunk Line Company Limited, undertook studies which resulted in its sponsorship of the Gas Arctic Project (GAP). The initial proposal considered was the construction of a 1,550 mile pipeline from Prudhoe Bay, Alaska, to connect with Alberta Gas Trunk Line's facilities near Grande Prairie, Alberta. The other initial members of

this group were Canadian National Railways, Columbia Gas Systems, Inc., Northern Natural Gas Company and Texas Eastern Transmission Corporation. Pacific Lighting Gas Development Company joined the group in 1971.

Studies for both projects were conducted independently until July of 1972. At that time, the GAP (with its six members) and the NPSG (with its six members) merged and became the Gas Arctic - Northwest Project Study Group, better known by its service corporation name of Canadian Arctic Gas Study Limited (CAGSL). At the time of the merger, four additional companies joined CAGSL; Canadian Pacific Investments, Gulf Oil Canada Limited, Imperial Oil Limited, and Shell Canada Limited. When this consolidation took place, NPSG had spent \$11,481,944 (Canadian) while the GAP Group had spent \$7,483,980 (Canadian). The combined expenditures of \$18,965,924 (Canadian) became known as CAGSL pre-inception costs. Under the Joint Research and Feasibility Study Agreement of 1972, \$1,185,370.25 (Canadian) of pre-inception costs were allocated to each of the sixteen members of the Group.

Additional members continued to join, each time causing a reallocation of the total contributions through the respective entry dates. The following companies joined CAGSL in late 1972 and early 1973 bringing the total participants to twenty-eight: Canada Development Corporation, Canadian Superior Oil Limited, Canadian Utilities Limited, Colorado Interstate Gas Company, Pampine Pipelines Limited, Sunoco Exploration and

Production Limited, Transcontinental Gas Pipe Line Corporation, Alberta Natural Gas Company, Consumers Gas Company, Panhandle Eastern Pipeline Company, Polaris Pipelines and Union Gas Limited.

CAGSL divided its corporate organization into four units: CAGSL, Alaskan Arctic Gas Study Company (AAGSC), Canadian Arctic Gas Pipeline Limited (CAGPL) and Alaskan Arctic Gas Pipeline Company (AAGPC).

CAGSL was responsible for completing the necessary research and general studies required to indicate project feasibility and to cause to be prepared an application to the NEB and other Canadian government departments for a permit to construct and operate a pipeline in Canada. It managed the day-to-day activities of the total project and assured coordination between themselves and AAGSC. It provided service to AAGSC on an "as needed" basis.

AAGSC was responsible for carrying out the development activities of the project in Alaska. AAGSC prepared the required application for filing with state and federal authorities for authorization to build a pipeline in Alaska.

CAGPL was responsible for making application for Canadian governmental authorizations necessary for construction and operation of the pipeline in Canada. If the project had been successful, it would have constructed and operated the pipeline as a Canadian Inter-Provincial Pipeline Company.

AAGPC was responsible for making application to the U. S. and Alaskan Governments for authorizations necessary to construct and operate the pipeline in Alaska. If the project had been successful, it would have constructed and operated the pipeline section in Alaska.

On March 24, 1974, when the applications were filed with the Federal Power Commission and the Canadian National Energy Board (CNEB) for certificates and permits to build a pipeline through Alaska and Canada known as the Arctic Project, 27 participants remained in the Arctic project. Only Transcontinental Gas Pipe Line had withdrawn. Shortly thereafter, however, other members began to withdraw. The most significant was the withdrawal on September 16, 1974 of Alberta Gas Trunk Line Company Limited, the original sponsor of the Gas Arctic Project. By November 1975, when Atlantic Richfield withdrew, the CAGSL Group was down to fifteen participants, the number that remained for the duration of the project.

In the Spring of 1975, Alberta Gas Trunk Line joined with Westcoast Transmission Company Limited to prepare the Foothills Project. They developed the Foothills (Yukon) Project (sometimes called the "Alaska Highway Project") to move Alaskan gas reserves to the United States. This project was the successful applicant before the CNEB in July 1977 and now is an integral part of the Alaska Natural Gas Transportation System.

After the CNEB decision in July 1977, the CAGSL Group terminated active operation. By that time, \$148,504,479 had been expended. Subsequent cash calls to cover the finalization payments of the group were \$6,345,000 which brought CAGSL expenditures to \$154,849,479 Canadian, the amount covered by this audit.

CAGSL PARTICIPANTS AND PAYMENTS (CANADIAN DOLLARS)

<u>Participating Companies</u>	<u>Date Withdrawn</u>	<u>Contributions and Fees Through Jan. 31, 1978</u>
Alberta Gas Trunk Line	09/16/74	\$ 2,249,285
Atlanta Richfield Company	11/30/75	4,183,524
Canada Development Corporation	10/31/75	4,000,383
Canadian National Realities	05/31/74	2,004,713
Canadian Pacific Investments	02/28/75	2,657,282
Canadian Superior Oil Limited	07/31/75	3,448,043
Canadian Utilities Limited	05/31/75	3,100,655
Colorado Interstate Gas Company	10/15/74	2,317,357
Exxon Company, U.S.A.	02/28/75	2,657,282
Pembine Pipelines Ltd.	10/21/74	2,332,100
Standard Oil (Ohio)	09/30/74	2,282,035
Sunoco E & P Limited (Numac Oil & Gas)	04/30/75	2,908,625
Transcontinental Gas Pipe Line	12/07/73	1,613,072
Alberta Natural Gas Company	N/A	8,020,533
Columbia Gas Transmission Corporation	N/A	8,020,533
Consumers Gas Company	N/A	8,020,533
Gulf Oil Canada Limited	N/A	8,020,533
Imperial Oil Limited	N/A	8,020,533
Michigan Wisconsin Pipe Line	N/A	8,020,533
Natural Gas Pipeline Company	N/A	8,020,533
Northern Natural Gas Company	N/A	8,020,533
Pacific Lighting Gas Development Co.	N/A	8,020,533
Panhandle Eastern Pipeline Company	N/A	8,020,533
Polaris Pipelines (Northern & Central)	N/A	8,020,533
Shell Canada Limited	N/A	8,020,533
Texas Eastern Transmission Corporation	N/A	8,020,533
Trans Canada Pipelines Limited	N/A	8,020,533
Union Gas Limited	N/A	8,020,533
Gross Contributions and Fees		156,062,351
August 1977 Cash Call Overpayment		(1,212,872)
Net Contributions and Fees through January 31, 1978		<u>\$154,849,479</u>

FILED
OFFICE OF THE SECRETARY
FEB 2 2 57 PM '79
FEDERAL
POWER COMMISSION

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Alaskan Northwest Natural
Gas Transportation
Company

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Docket No. CP78-123, et al.

APPLICATION OF
ALASKAN NORTHWEST NATURAL GAS TRANSPORTATION COMPANY
FOR AN ORDER APPROVING PAST EXPENDITURES AND
TO ESTABLISH PROCEDURES FOR CONTINUING AUDIT AND
APPROVAL OF FUTURE EXPENDITURES AND
MAJOR COMMITMENTS

Alaskan Northwest Natural Gas Transportation Company (the Partnership), pursuant to the Alaska Natural Gas Transportation Act of 1976 (ANGTA), the Natural Gas Act, and the Commission's Order Vacating Prior Proceedings and Issuing Conditional Certificate of Public Convenience and Necessity issued December 16, 1977, hereby applies for an order approving, for inclusion in rate base, expenditures made prior to August 1, 1978 ^{1/} for pre-construction activities necessary to place the Alaskan section of the Alaska Natural Gas Transportation System in service. These expenditures are reflected in the capital accounts of each Partner, Northwest Alaskan Pipeline Company (Northwest), Northern Arctic Gas Co. (Northern), Pan Alaskan Gas Company (Pan Alaskan), Calaska Energy Company (Calaska), ^{2/} Pacific Interstate Transmission Company (Arctic) [Pacific] and United Alaska Fuels Corporation (United). The Partnership also requests that the Commission establish procedures to review and approve, on a continuing basis at regular quarterly intervals, completed activities and both actual and conditionally committed expenditures necessary to place the Alaskan section of the Alaska Natural Gas Transportation System in service.

-
- ^{1/} Partnership expenditures from August 1, 1978 through December 31, 1978 will be submitted to the Commission for review and approval as soon as practicable.
- ^{2/} Calaska is successor to the interests of Natural Gas Corporation of California and the interests of Natural Gas Corporation of California were transferred to Calaska as of November 28, 1978.

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In support thereof, the Partnership would show as follows:

I.

Background

The Commission initiated a new phase of the proceedings contemplated in ANGTA by its order dated December 16, 1977, issuing a Conditional Certificate of Public Convenience and Necessity as mandated by the Decision and Report to Congress on the Alaska Natural Gas Transportation System issued by the President of the United States on September 22, 1977, and approved by the Congress on November 22, 1977. 3/

Subsequently, on June 30, 1978, the Commission transferred the Conditional Certificate of Public Convenience and Necessity from Alcan Pipeline Company to the Partnership.

II.

Basis for Authorization Requested Herein

A. In the Decision and Report, the President provided that certain "general terms and conditions shall be appropriately incorporated into any certificate, right-of-way, lease, permit or authorization directed to be made by any Federal Officer or agency" (Section 5, page 26). Among such general terms and conditions is the requirement that the Partnership must "submit to the FPC (FERC) for approval on a timely basis all components of construction work in progress." (Finance Condition, page 37; emphasis added.) The order requested herein is necessary to implement this mandate.

B. In the Commission's order issued December 16, 1977, the Commission recognized that it would have either exclusive or coextensive jurisdiction over the President's terms and conditions concerning finance matters, which included the condition described above. Further, the Commission adopted the Partnership's suggestion that quarterly progress reports are appropriate. Thus, the Commission has already moved toward implementation of the above-cited requirement of the Decision and Report and has recognized that authorization of the type requested herein is appropriate.

3/ Pub. L. 95-158, 91 Stat. 1268.

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C. In its Notice of Succession in Interest and Application for Transfer of Certificate of Public Convenience and Necessity filed April 19, 1978, the Partnership indicated that it "...stands ready to report to the Commission, or its Delegate, on all matters relating to the Alaskan Natural Gas Transportation System, and particularly the status of preconstruction planning, funds expended to date, budgeted and anticipated costs for the balance of 1978, financial planning, and system engineering and design. Such other information and reports as the Commission, or its Delegate, may desire will, to the extent of the Partnership's abilities, be furnished in such form and manner as the Commission, or its Delegate may direct. The Partnership requests the institution of a mechanism for review and approval of cost expenditures and budgets for the Project on a regular and recurring basis."

D. The General Partnership Agreement 4/ (the Agreement) envisions Commission review and approval of actual expenditures. The relevant provisions are found in Sections 4.1.1, 4.1.2, 4.1.3 and 4.1.4, which provide a procedure for determining the Qualified Expenditures 5/ of each Partner. Northwest's Qualified Expenditures are \$19,163,000; those of Northern are \$9,587,790; those of Pan Alaskan are \$9,655,128; those of Calaska are \$9,456,744; and those of Pacific are \$9,667,221. 6/ All of these are expressly subject to review and approval by FERC.

In summary, there is ample basis in the Decision and Report and in prior Commission orders, as well as the Partnership Agreement, for the Commission to consider and grant this application.

4/ Reviewed by the Commission and approved in its Order issued June 30, 1978 (Docket No. CP78-123).

5/ Expenditures to acquire information, knowledge, studies, tests, computer programs or governmental authorizations by any Partner or corporate affiliate of a Partner, in the course of activities reasonably related to the selection of a transportation system for the delivery of Alaskan natural gas, if such expenditures were made by such Partner or corporate affiliate prior to January 31, 1978.

6/ The totals shown include an interest component on funds spent.

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III.

Authorization Requested

A. The Partnership requests that the Commission review and verify (1) the expenditures made by each Partner incurred prior to the formation date of the Partnership which have been determined to be "Qualified Expenditures" and therefore appropriately included in the Partners' capital accounts; and (2) \$15,174,000 in expenditures of the Partnership for the period of February 1, 1978, through July 31, 1978. The Partnership further requests that the Commission, by order, approve acceptance of all such expenditures for inclusion in rate base, subject only to "completion and commissioning of operation of the system," a necessary precondition specified on page 38 of the Decision. Exhibit 2-1 attached hereto shows in detail the amounts and purposes for which "Qualified Expenditures" were made by Northwest. Exhibit 2-2 attached hereto shows in detail the amounts and purposes for which "Qualified Expenditures" were made by Northern, Pan Alaskan, Calaska and Pacific. Exhibit 2-3 attached hereto shows in detail the amounts and purposes for which Partnership funds were expended from February 1, 1978 through July 31, 1978.

B. The Partnership also requests that the Commission institute procedures to audit and approve actual expenditures on a continuing quarterly basis throughout the pre-construction and construction periods of the project.

C. In addition to the audits and approvals of actual expenditures made, the Partnership also requests the Commission to include within the scope of its reviews, upon specific request of the Partnership, certain major financial commitments that are covered by an executed contract for which payment may be due at some future date subject to certain conditions having been met. 7/ In such cases, the Partnership requests that the Commission by order give provisional approval to the obligation or conditional expenditure, subject to later audit and approval by the Commission

7/ The project management contract, the project labor agreement, agreements for purchase or use of Alyeska camps and/or data, and the contracts for purchase of line pipe are expected to have sufficient impact on project costs to warrant advance regulatory review.

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of actual expenditures made. No commitments of this nature are included in the period from February 1 through July 31, 1978.

The Partnership stands ready to make available its books and records at the convenience of the Commission to permit such reviews and field audits as may be required to issue the order requested herein.

IV.

Justification for the Authorizations
Herein Requested

A. Qualified Expenditures

Prior to the formation of the Partnership, substantial funds were expended by the individual companies, or their affiliates, for reasonable and necessary expenditures related to the ultimate construction and operation of the Alaskan segment of the Alaskan Natural Gas Transportation System. Because the factual circumstances surrounding the expenditures made by Northwest differ from the factual background and circumstances relating to the expenditures by Northern, Pan Alaskan, Calaska, and Pacific; each category of pre-Partnership expenditures is treated separately:

1. Pre-Partnership Expenditures of Northwest. Northwest, through its predecessor company, Alcan Pipeline Company, was the original applicant for the route and pipeline proposal ultimately selected by the President and the Congress under the terms and conditions of the Alaska Natural Gas Transportation Act. The reasonable and necessary costs to Northwest of presenting to the Federal Power Commission, and later to the President and the Congress, the Alaska Highway Project through the date of formation of the Partnership, was \$19,163,000, including interest. The details of these expenditures are set forth in Exhibit 2-1 and such expenditures were reasonably and prudently made as necessary to the preparation and presentation of Northwest's application for a certificate of public convenience and necessity, Northwest's presentation to the President and the Congress for selection of the Alaska Highway Project as the desired route, and selection of Northwest as the company to construct the Alaskan segment of the ANGTS. All of such expenditures are appropriate for inclusion in the capital account of Northwest as a Partner, and inclusion in the rate base of the Partnership pipeline project.

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2. Pre-Partnership Expenditures of Others.

Northern, Pan Alaskan, Calaska and Pacific made expenditures prior to the formation of the Partnership through their membership and participation in the Gas Arctic/ Northwest Project Study Group (Gas Arctic). Gas Arctic was the result of a combination of two groups which had begun studies long before any other study group was formed, and before any of the subsequent applicants for a certificate of public convenience and necessity to transport Alaskan and Canadian gas to lower U.S. 48 markets made any indication that they would file an application. The total paid by participants in the Gas Arctic Study Group through January 31, 1978 was approximately \$154.8 million. The costs were shared by as many as 26 participants, and after a number of participants had withdrawn, the group narrowed to 15 members. Each of these 15 members had paid in \$8,020,533 (Canadian) through January 31, 1978.

Included in the expenditures of the Gas Arctic Group were the following major categories of costs:

Engineering & Construction Planning	\$65.8 million
Environmental Studies and Research	18.6 million
Finance, Accounting, Legal and Other Advisors	16.7 million
General and Administrative	31.2 million
Sociological	4.3 million

The expenditures for the items listed above include basic research such as that done with respect to an Arctic ditcher, metallurgical questions, cost effects, slope stability, the environmental impact on fish, mammals, birds and vegetation, and training programs which might be used in connection with the use of native labor in the project. In addition, substantial amounts were spent developing computer models to be used in engineering and financial analysis, and some of these are currently in use.

The knowledge and information developed by the Gas Arctic Study Group will be useful and of significant importance to the Alaska Highway Pipeline Project. The design and construction of the Alaska

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project will be materially aided by the basic research which was performed into environmental and engineering issues, and the development of computer analysis techniques which resulted from Study Group activities and expenditures. Relevant portions of the information, data, and computer programs developed will be, as a consequence of the Partnership's approval of the "Qualified Expenditures" of Northern, Pan Alaskan, Calaska and Pacific, available to the Partnership for its continuing use in development of the project.

It must be emphasized that the Arctic Gas Project and the Alaskan Highway Pipeline Project were considered as alternatives by governmental authorities at all levels of the decision-making process in both the United States and Canada prior to the time of the President's Decision and Report in September of 1977. If only a single applicant had proposed an Alaska Natural Gas Transportation System, that applicant would nonetheless have been legally compelled at substantial cost to develop and present information on alternative routes, and such costs would clearly have been includable in the rate base of the authorized project. The costs presented here by the Partners who were members of the Study Group were just as necessary to the decision-making process as the costs of the hypothetical single applicant, and should be afforded the same regulatory treatment.

In accord with the Partnership Agreement, the pre-formation expenditures of Northern, Pan Alaska, Calaska, and Pacific have been reviewed by the Board of Partners and a determination made with respect to whether such constituted "Qualified Expenditures." An extract from the Board of Partners' minutes relating to this is appended to this application as part of Exhibit 8-2.

The nation and U.S. gas consumers have benefited from the thorough analysis of transportation alternatives which the Partners' "Qualified Expenditures" made possible. The hearing process before the Federal Power Commission, and the subsequent Presidential selection of a route that is preferable from an environmental and economic standpoint, were materially advanced by the efforts of Northern, Pan Alaska, Calaska and Pacific. Therefore, it is appropriate that those companies who continue to participate in the development of this project to connect Alaskan natural gas be allowed to include those costs as part of the rate base of the Alaskan portion of the system. These

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costs, although significant in relation to the revenues and assets of each sponsoring company, will be less than one percent of the total investment in the Alaskan system.

The details of the pre-Partnership expenditures by Northern, Pan Alaska, Calaska, and Pacific are set forth in Exhibit 2-2 appended hereto. The pre-Partnership expenditures of the four Partners named above were clearly reasonable and necessary to the Partnership pipeline project, and are properly includable in the capital accounts of each such Partner, and in the rate base of the Partnership pipeline project.

B. Partnership Expenditures

The six Partners who have funded the Partnership's pre-construction activities since the formation date of the Partnership have provided \$21,769,000 in funds which were expended prior to August 1, 1978. ^{8/} The details concerning such Partnership expenditures are set forth in Exhibit 2-3 appended hereto. All of such expenditures were reasonable and necessary to proper planning for, and design of, the Alaskan segment of the Alaska Natural Gas Transportation System, and securing all necessary governmental authorizations, permits, certificates, and rights-of-way. All of such expenditures are properly includable in the capital accounts of the respective partners, and properly includable in the rate base of the Partnership's pipeline project.

C. "Provisional Approvals"

With respect to the request for "provisional approval" of certain contractual obligations and conditional expenditures, we believe that the Commission has the authority to take such action, which would be entirely consistent with Sections 9(a) and (b) of ANGTA, and the provisions of the President's Decision calling upon the Partnership to "submit

^{8/} This total includes AFUDC but the Partnership does not seek, through this application, approval of the AFUDC rate inasmuch as the Commission has stated its intention to determine this issue in Docket No. RM78-12, Order No. 17-A, issued January 17, 1979. Expenditures, without AFUDC, through July 31, 1978, total \$15,174,000.

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to the FPC (FERC) for approval on a timely basis all components of construction work in progress.³ The spirit of the latter requirement reasonably can be construed to include certain major potential expenditures covered by an executed contract for future conditional payment. The Partnership does not in any way expect to seek provisional approval for all future expenditures. Rather, it would make such a request on a selective basis where it appears that such an approval would materially reduce uncertainty, and have a correspondingly salutatory effect on the Partnership's ability to obtain private financing. It is presently contemplated that such major cost items as the project management contract, the project labor agreement, contracts for line pipe, and contracts for the acquisition and/or use of Alyeska camps and data will be of sufficient magnitude and will have sufficient impact on project costs, to warrant advance regulatory review and approval.

V.

Argument

It is essential that the audit and approval process for determination that the expenditures of Alaska Natural Gas Transportation System reasonably and necessarily made be implemented on a current and continuing basis. The magnitude of ANGSTS is such that delayed review and approval of expenditures will pose insurmountable administrative problems for the Commission and the sponsors. Periodic, and frequent, review and approval of expenditures will reduce the task to manageable proportions; uncertainty will be reduced; and potential problem areas can be promptly identified and necessary corrections made. The authorizations and procedures suggested here will materially enhance cost consciousness on the part of the government, the sponsors and all interested parties.

Further, it is important that the Commission create a positive regulatory environment in order to help assure realization of private financing of this major undertaking. Banks and other potential institutional lenders are carefully observing the regulatory climate surrounding the early stages of project implementation and a prompt, and favorable, consideration of this application will help reassure not only the sponsors themselves, but also potential lenders, that all that the government can possibly do to reduce uncertainty and support this critically important project is being done.

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The sponsors of the Alaskan segment of the ANGTs have already exposed themselves to substantial risk by the advancement of pre-construction dollars in pursuit of a project still beset by major uncertainties and delays. Reassurance to the project sponsors that their faith in the regulatory process has not been misplaced is important at this juncture, particularly in view of the continuing uncertainties which surround the incentive rate of return procedures under consideration in Docket No. RM78-12.

One final reason exists for the Commission's prompt and affirmative action on this application: such action will serve as tangible evidence to those pipeline companies not presently members of the Partnership that their previous Gas Arctic expenditures may reasonably be considered as appropriate for inclusion in the Partnership's rate base if those companies, or any of them, decide on active participation in support of the project as a partner. The Partnership clearly needs a broader base of membership and equity support, and favorable early action on this application by the Commission would be a positive inducement to other prospective partners who have also expended substantial sums in the development and presentation of alternative systems for North Slope gas transportation to join the Partnership.

VI.

The names, titles and mailing addresses of the persons to whom all correspondence and communications concerning this application should be addressed are as follows:

Darrell B. MacKay
Vice President
Northwest Alaskan Pipeline Company
1801 K Street, N.W.
Suite 901
Washington, D. C. 20006

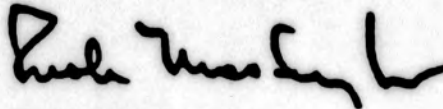
Jack D. Bachman, Esquire
General Counsel
Northwest Alaskan Pipeline Company
P. O. Box 1526
Salt Lake City, Utah 84110

Rush Moody, Jr., Esquire
Vinson & Elkins
1101 Connecticut Avenue, N.W.
Suite 900
Washington, D. C. 20036

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WHEREFORE, the Partnership respectfully requests that the Commission issue an order pursuant to ANCTA, the Natural Gas Act, and the President's Decision, giving final approval to the expenditures described herein for ultimate inclusion in the rate base for the Alaskan section of the Alaska Natural Gas Transportation System. The Partnership further requests that the Commission establish procedures for continuing audit and approval of actual and conditionally committed expenditures.

Respectfully submitted,



Rush Moody, Jr.

Vinson & Elkins
1101 Connecticut Avenue, N.W.
Suite 900
Washington, D. C. 20036
(202) 852-6500

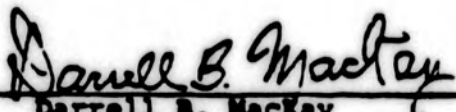
ATTORNEYS FOR
ALASKAN NORTHWEST NATURAL GAS
TRANSPORTATION COMPANY,
A PARTNERSHIP

VERIFICATION

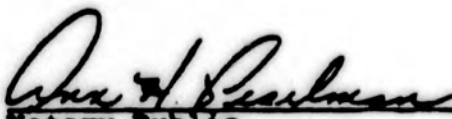
THE DISTRICT OF COLUMBIA S

I, DARRELL B. MacKAY, being first duly sworn on his oath, deposes and says:

That he is Vice President of Northwest Alaskan Pipeline Company and is duly authorized to make this affidavit, that he has read the foregoing and is familiar with the contents thereof, and that the facts and allegations contained therein are true and correct to the best of his information, knowledge and belief.


Darrell B. MacKay

Subscribed and sworn to before me this 2nd day of February, 1979.


Notary Public

My Commission Expires;
MY COMMISSION EXPIRES JAN. 1, 1984

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the official service list compiled by the Secretary in this proceeding in accordance with the requirements of § 1.17 of the Rules of Practice and Procedure.

Dated at Washington, D.C. this 2nd day of February, 1979.


Rush Moody, Jr.

Exhibit 2-1

ALASKAN NORTHWEST NATURAL GAS TRANSPORTATION COMPANY
NORTHWEST ALASKAN PIPELINE COMPANY
QUALIFIED EXPENDITURES ^{1/}

1.	FILING FEE	\$1,671,000	
2.	OFFICE EQUIPMENT	144,000	
3.	TRANSPORTATION EQUIPMENT	30,000	\$1,846,000
4.	COMPANY SERVICES		
	Salaries and Related Benefits	1,347,000	
	Employee Expenses	697,000	
	Office supplies	210,000	
	Equipment Use	1,631,000	
	Recruitment and Relocation	28,000	
	Rents	107,000	
	Other	247,000	
			4,267,000
5.	OUTSIDE SERVICES		
	Legal	3,415,000	
	Executive	188,000	
	Finance	1,524,000	
	Regulatory, Environmental & Civic Affairs	96,000	
	Administration	99,000	
	Public Relations	89,000	
	Engineering	5,996,000	
	Other	153,000	
			11,560,000
6.	DEPARTMENT OF INTERIOR		165,000
	Sub-Total		17,838,000
7.	AFUDC ^{2/}		1,325,000
	Total Qualified Expenditures Including AFUDC		\$19,163,000

^{1/} Expenditures made prior to January 31, 1978.

^{2/} Includes only an interest component on funds spent.

**ALASKAN NORTHWEST NATURAL GAS TRANSPORTATION COMPANY
GAS ARCTIC/NORTHWEST PROJECT STUDY GROUP-NOW ANNGTC PARTNERS
QUALIFIED EXPENDITURES 1/**

		Partners			
	Total	Pan Alaska Gas Co.	Alaska Energy Co.	Pacific Interstate Trans. Co.	Northern Arctic Gas Co.
1. GENERAL & ADMINISTRATION					
Direct Operations	\$ 5,275,777	\$1,330,009	\$1,292,140	\$1,331,582	\$1,322,046
Indirect Operations	1,126,398	283,962	275,877	284,297	282,262
	<u>6,402,175</u>	<u>1,613,971</u>	<u>1,568,017</u>	<u>1,615,879</u>	<u>1,604,308</u>
2. OUTSIDE SERVICES					
Legal	1,626,919	410,142	398,464	410,627	407,686
Executive	156,299	39,402	38,281	39,449	39,167
Finance	968,765	244,223	237,269	244,512	242,761
Regulatory, Environmental & Civic Affairs	5,711,181	1,439,774	1,398,779	1,441,475	1,431,153
Administration	501,939	126,537	122,935	126,687	125,780
Public Relations	657,171	165,671	160,954	165,867	164,679
Engineering	<u>13,917,264</u>	<u>3,508,505</u>	<u>3,408,608</u>	<u>3,512,652</u>	<u>3,487,499</u>
	<u>23,539,538</u>	<u>5,934,254</u>	<u>5,765,290</u>	<u>5,941,269</u>	<u>5,898,725</u>
3. TERMINATION AND CLOSE-OUT COST	1,562,191	393,824	382,611	394,290	391,466
4. GOVERNMENT AGENCIES	66,165	16,680	16,205	16,700	16,580
5. OTHER COSTS	<u>208,898</u>	<u>52,663</u>	<u>51,163</u>	<u>52,725</u>	<u>52,347</u>
Sub-Total	31,778,967	8,011,392	7,783,286	8,020,863	7,963,426
6. AFUDC 2/	<u>6,587,916</u>	<u>1,643,736</u>	<u>1,673,458</u>	<u>1,646,358</u>	<u>1,624,364</u>
Total Qualified Expenditures Including AFUDC	<u>\$38,366,883</u>	<u>\$9,655,128</u>	<u>\$9,456,744</u>	<u>\$9,667,221</u>	<u>\$9,587,790</u>

1/ Expenditures made prior to January 31, 1978.

2/ Includes only an interest component on funds spent.

Exhibit 2-2
Page 2

Extract from the Minutes of a meeting of the Board of Partners, Alaskan Northwest Natural Gas Transportation Company, a Partnership, held November 28-29, 1978:

* * *

"(10) The Board of Partners next considered the qualified expenditures of the partners other than Northwest Alaskan. By letter dated November 15, 1978, a copy of which is appended, Calaska Energy Company requested that its capital account be credited with the total of \$9,456,744 pursuant to Section 4 of the Partnership Agreement; a similar request, by letter dated November 16, 1978, a copy of which is appended to these minutes, was made on behalf of Pacific Interstate Transmission Company, with the requested capital account credit for that partner being \$9,667,221. A similar request on behalf of Pan Alaskan Gas Company, by letters dated September 27 and November 27, 1978, copies of which are attached to these minutes, requested capital account credit for that partner of \$9,655,128. A similar request on behalf of Northern Arctic Gas Company by letter dated November 27, 1978, a copy of which is appended to these minutes, requested capital account credit for that partner of \$9,587,790.

"Prior to the meeting of November 28-29, those partners requesting capital account credit for qualified expenditures had submitted to all partners substantiation for the amounts claimed, and had further tendered in support of the request for capital accounts credit summary reports prepared by Arthur Andersen & Co. under dates of October 5, 1977 and November 10, 1978. Copies of these reports are appended to these minutes.

"The Board of Partners discussed fully and completely the nature of the expenditures made, the value to the Partnership of such expenditures, and the reasonableness and necessity of the amounts expended. It was noted that the prior expenditures by Calaska, Pan Alaskan, Pacific Interstate, and Northern Arctic encompassed basic research into environmental and engineering issues, and the development of computer analysis techniques which will be of material benefit to the Partnership's activities. It was further noted that the expenditures by Partners other than Northwest were made in conjunction with the study of an alternative route for the movement of Alaskan gas to the lower 48 states, and such expenditures, if not made by the Arctic gas participants, would have been required of the Partnership prior to final approval of the Alaskan Highway routing; the expenditures relating to an alternative route were of significant benefit to the governmental decision-making process in both the United States and Canada.

Exhibit 2-2
Page 3

"Mr. McMillian made inquiry as to whether the materials developed as a result of the claimed qualified expenditures would be made available to the Partnership, and he was assured that Northwest and the Partnership would have the benefit of such.

"Mr. McMillian reported that Northwest had made a detailed study of the available Canadian Arctic gas design information, and had concluded that there were a number of items of information and data which would be of extreme value to the Partnership in its ongoing efforts; the results of Northwest's preliminary evaluation of the specific gas design information which should prove to be of value to the Partnership is set forth on the appended list denominated "List of Canadian Arctic Gas Design Information," and each item on this listing refers to specific data and/or information which the Partnership will review to insure that no duplication of expenditures for design and research occurs.

"On motion of Mr. McMillian, seconded by Mr. Smith, the Board of Partners unanimously approved the requests of Calaska, Pacific Interstate, Pan Alaskan and Northern Arctic for inclusion in the respective capital account of each such partner the qualified expenditures submitted on behalf of each such partner; in connection with this approval, it was the expressed determination of the Board of partners that the expenditures made by each of such partners was reasonable and necessary to the conduct of the business of the Partnership, that such expenditures were prudently incurred, and that the Partnership received full value, in an amount at least equal to the amounts credited to the capital accounts pursuant to the instant approval. The Board of Partners further determined that the expenditures claimed by each of the four partners named were expenditures to acquire information, knowledge, studies, tests, computer programs or governmental authorizations by one or more of such partners or corporate affiliates of such partners, in the course of activities reasonably related to the selection of a transportation system for the delivery of Alaskan natural gas, and that each such expenditure was made by such partner or corporate affiliate prior to the formation date of the Partnership."

Exhibit 2-3

ALASKAN NORTHWEST NATURAL GAS TRANSPORTATION COMPANY
ACTUAL EXPENDITURES FOR THE PERIOD
FEBRUARY 1, THROUGH JULY 31, 1978

1. OFFICE EQUIPMENT	\$ 470,000	
2. TRANSPORTATION EQUIPMENT	27,000	\$ 497,000
3. COMPANY SERVICES		
Salaries and Related Benefits	2,158,000	
Employee Expenses	345,000	
Office Supplies	129,000	
Equipment Use	887,000	
Recruitment and Relocation	307,000	
Rents	444,000	
Other	315,000	4,585,000
4. OUTSIDE SERVICES		
Legal	1,459,000	
Executive	253,000	
Finance	996,000	
Regulatory, Environmental & Civic Affairs	251,000	
Administration	466,000	
Public Relations	178,000	
Engineering	5,902,000	
Other	73,000	9,578,000
5. GOVERNMENT AGENCIES		
Federal Bureau of Land Management	471,000	
State of Alaska:		
Fish & Game	26,000	
Office Pipeline Coordinator	17,000	
		<u>514,000</u>
Sub-Total		15,174,000
6. AFUDC		<u>6,595,000</u>
Total Actual Expenditures Including AFUDC 1/		<u>\$21,769,000</u>

1/ This total includes AFUDC but the Partnership does not seek, through this application, approval of the AFUDC rate inasmuch as the Commission has stated its intention to determine this issue in Docket No. EM78-12, Order No. 17-A, issued January 17, 1979.

**REPORT ON
RESULTS OF AUDIT OF EXPENDITURES
BY THE
ALASKAN NORTHWEST NATURAL GAS
TRANSPORTATION COMPANY
WHICH WERE
INCURRED FROM
FEBRUARY 1, 1978 THROUGH DECEMBER 31, 1978
(DOCKET NO. CP78-123, et al.)**

**August 1980
Division of Audits
Office of Chief Accountant
Federal Energy Regulatory Commission**

REPORT ON RESULTS OF AUDIT OF EXPENDITURES
BY THE ALASKAN NORTHWEST
NATURAL GAS TRANSPORTATION COMPANY WHICH
WERE INCURRED FROM FEBRUARY 1, 1978
THROUGH DECEMBER 31, 1978
(DOCKET NO. CP78-123, et al.)

INTRODUCTION

This is the second in a series of reports on the results of audits of expenditures related to the construction of the Alaska Natural Gas Transportation System (ANGTS)^{1/}. The audits and reports are being made pursuant to the directions contained in Administrative Order No. 4, issued April 18, 1979.

The first report conveyed the results of the staff's initial audit of expenditures charged to the Alaskan section of ANGTS. The initial audit covered expenditures incurred prior to the formation of the partnership (Alaskan Northwest Natural Gas Transportation Company (ANNGTC)) on February 1, 1978, for the construction and operation of the Alaskan section of ANGTS. Amounts charged to the Alaskan section for pre-partnership expenditures totaled \$57,415,070, including Allowance for Funds Used During Construction (AFUDC) of \$7,798,313.

1/ ANGTS was authorized by the Alaska Natural Gas Transportation Act of 1976 (ANGTA), 15 U.S.C. 719, et seq. and the President's Decision and Report to Congress on the Alaska Natural Gas Transportation System, as enacted into law, H.J. Res. 621, Pub. L. No. 95-108 (November 2, 1977).

In the first report, the staff recommended the disallowance of \$42,224,461, including AFUDC of \$6,833,041 of the total claimed pre-partnership expenditures of \$57,415,070^{2/}.

This report conveys the results of the staff's audit of partnership expenditures charged to the Alaskan section of ANGTS for the period February 1, 1978 through December 31, 1978. Partnership expenditures charged to the gas plant accounts during this period totaled \$44,918,798, including AFUDC of \$13,988,691. The staff's findings and recommendations in this report do not cover the \$13,988,691 of AFUDC claimed during the period. A large part of the AFUDC claimed is related to pre-partnership expenditures which are at issue in our first audit report. Upon disposition of the audit findings and recommendations in that report, AFUDC claimed for the period February 1, 1978 through December 31, 1978 will be recomputed and adjusted as appropriate.

SUMMARY

With respect to the partnership expenditures made during the period February 1, 1978 through December 31, 1978 (\$30,930,107, exclusive of AFUDC), the staff concludes that:

1. Expenditures of \$29,107,087 are properly assignable to the Alaskan section of ANGTS

^{2/} These proposed disallowances have been reflected in Exhibit No. 1.

and are of a nature that would qualify for eventual inclusion in rate base.

2. Expenditures of \$652,294 are not of a nature that would qualify for eventual inclusion in rate base and, therefore, should be disallowed.
3. Expenditures of \$1,170,726 may not be properly assignable to the project for eventual inclusion in rate base. Requests to ANNGTC for additional information on these expenditures have not been answered. Therefore, the staff proposes that these expenditures be disallowed without prejudice to ANNGTC's reclaiming them upon submission of appropriate supporting information.
4. Corrective action is needed to eliminate discrepancies between the accounting records and the financial statements.

SCOPE OF AUDIT

The audit covered claimed partnership expenditures charged to the gas plant accounts totaling \$30,930,107, exclusive of AFUDC, for the period February 1, 1978 through December 31, 1978.

The audit included an examination of the accounting and other records to the extent deemed necessary to determine whether:

1. The various financial statements and reports properly reflected the underlying records and documents.
2. The expenditures were adequately documented and supported.
3. The accounting for the expenditures met the requirements of the Uniform System of Accounts and generally accepted accounting principles.
4. The expenditures were properly assignable to the Alaskan section of ANGTS and were of a nature that would qualify for eventual inclusion in rate base.

5. The other accounting and reporting regulations and requirements of the Natural Gas Act, the Decision and the Certificate of Public Convenience and Necessity were complied with.
6. The policies, procedures, and controls appear adequate to ensure the efficient and economic construction of the project.

RESULTS OF AUDIT

ANNGTC claimed partnership expenditures of \$30,930,107, excluding AFUDC. With respect to these expenditures, the staff has determined that:

1. Expenditures of \$29,107,087 were for engineering studies and plans, environmental studies, governmental fees, legal and consultant fees related to the preparation of an application for a Certificate of Public Convenience and Necessity to construct the Alaskan section of ANGTS. These expenditures are properly assignable to the Alaskan section of the ANGTS and are of a nature that would qualify for eventual inclusion in rate base.

2. Expenditures of \$652,294 are not of a nature that would qualify for eventual inclusion in ANNGTC's rate base and should be disallowed. These expenditures fall into the following categories.

- a. Lobbying Activities

Expenditures of \$513,171 relate to payments made to various public relations firms, consultants and legal firms.

Three public relations firms were involved in a campaign to develop public and legislative support for a financial plan proposed by ANNGTC. This financial plan proposal provided for State of Alaska participation in the project through the issuance of \$1 billion in tax-exempt revenue bonds or an equity interest in the project. Legislative action was needed for either proposal.

Three other firms lobbied on the Company's behalf regarding its proposed financial plans, the question of whether Alaskan gas should be incrementally costed, the wellhead prices of Prudhoe Bay gas, and proposed legislation affecting exploration of certain lands in Alaska.

- Another law firm performed services which involved legislative efforts to secure passage of the Natural Gas Policy Act of 1978. This emanated from President Carter's 1977 Energy Plan which proposed substantial changes to the Natural Gas Act. This firm analyzed the President's proposal and contacted members of the House and Senate and their staffs to inform them of the impact of gas pricing legislation on the project. The firm was involved in urging the passage of the compromise bill which was ultimately signed into law in November 1978.

The Uniform System of Accounts requires that expenditures of this nature be recorded in Account 426.4, Expenditures for certain civic, political and related activities, a non-utility expense account.

b. Public Relations

Expenditures of \$91,416 relate to payments made to three public relations firms. One firm, located in Washington, D. C., distributed

information to the press, members of Congress and the public. A consultant was paid a retainer to provide technical expertise in developing and implementing film projects documenting construction activities. The third firm was an agency which monitored the media and handled liaison work in Canada.

The Commission, in various cases, has ruled that public relations-type expenditures are not properly assignable to the plant accounts, but are of a nature that should be recorded in Account 930.1, General advertising expenses.

c. Non-Project Expenditures

Expenditures of \$21,208 represent payments made to a law firm which provided services to ANNGTC and Northwest Alaskan Pipeline Company (Northwest), the managing partner of ANNGTC. Charges for legal services for Northwest were erroneously recorded on the books of ANNGTC as a project construction expenditure.

The Uniform System of Accounts provides for the use of Account 143, Other accounts receivable, to correct this error.

d. Fishing Trip

Expenditures of \$19,363 relate to payments for a chartered fishing trip and riverboat reception held subsequent to an ANNGTC partnership meeting in Fairbanks, Alaska.

The Uniform System of Accounts requires that expenditures of a nonoperating nature be recorded in Account 426.5, Other deductions, a non-utility expense account.

e. Country Club Dues

Expenditures of \$5,221 relate to payments to various country clubs, luncheon and dinner clubs and athletic clubs for membership dues.

NARUC Interpretation No. 49 requires that club dues of this nature be recorded in Account 426.5, Other deductions, a non-utility expense account.

f. Donations

Expenditures of \$1,915 relate to contributions made to the Anchorage Community YMCA, Alaska Foundation of Native Youths and the Iditarod Trail Committee, Inc.

The Uniform System of Accounts requires that expenditures of this nature be recorded in Account 426.1, Donations, a non-utility expense account.

3. Expenditures of \$1,170,726 were not adequately supported; therefore, the staff was unable to determine whether they are properly assignable to the Alaskan section of the ANGTS for eventual inclusion in rate base. Requests to ANNGTC for additional information on these expenditures have not resulted in responses which clearly document the nature and character of the items. These items fall into two general categories:

- a. Amounts paid to a number of law firms for services which appear to include political lobbying efforts designed to influence

public opinion concerning the project and, as such, would not be allowable in the plant accounts under the provisions of the Uniform System of Accounts.

- b. Amounts paid to a number of consultants where sufficiently competent evidential material (i.e. contracts, written agreements, vendor memoranda, etc.) did not exist or were not made available. Therefore, there was no adequate basis upon which to evaluate the propriety of the assignment of the costs to the project or their qualification for eventual inclusion in rate base.

Therefore, the staff proposes that these expenditures be disallowed, without prejudice to ANNGTC's reclaiming them upon submission of appropriate supporting information.

4. Monthly financial statements prepared by ANNGTC reported and compared actual project expenditures with budgeted project expenditures. The accounting records supporting

these financial statements did not agree with the reported actual project expenditures in many instances and adequate reconciliations were not available. The scope of the staff's audit was expanded due to the differences noted and the staff was able to satisfy itself as to the validity of the expenditures by additional testing of transactions. However, the staff was not able to attest to the reasonableness of the recorded or reported classification of expenditures by work orders or cost elements. Some improvements were made by ANNGTC the spring of 1979. However, some control deficiencies remain which must be eliminated from the accounting system prior to active construction.

The Uniform System of Accounts requires that the accounting records be maintained in a manner that permits ready analysis by the prescribed accounts and preparation of financial statements directly from the accounting records. Further, since this project will be subject to the incentive rate of return (IROR) mechanism^{3/}, it is imperative that the actual construction costs be readily identifiable and verifiable.

^{3/} Pursuant to Order No. 31, Docket No. RM78-12, issued June 8, 1979.

Otherwise it will be difficult, if not impossible, to audit costs for compliance with the IROR mechanism and to issue timely audit reports.

RECOMMENDATIONS

The staff recommends that:

1. \$29,107,087 of partnership expenditures be allowed as charges properly assignable to the ANNGTC project and be determined as qualified for eventual inclusion in the rate base of ANNGTC.
2. \$652,294 of partnership expenditures be disallowed as costs qualified for eventual inclusion in the rate base of the ANNGTC.
3. \$1,170,726 of partnership expenditures be disallowed as costs properly assignable to the ANNGTC project for eventual inclusion in rate base, without prejudice to ANNGTC's reclaiming them upon submission of appropriate supporting information.
4. Corrective action be taken to permit the preparation of financial statements directly from the accounting records. Until such corrective action is implemented, ANNGTC should prepare reconciliations of differences

between the recorded and reported actual expenditures.
These reconciliations should list each reconciling
amount, the source of original entry, and explain the
reason for the reconciling item.

EXHIBIT

Alaskan Northwest Natural Gas Transportation Company
Adjusted Balance Sheet
As of February 1 and December 31, 1978
With Staff Adjustments Thereto

	Adjusted Balance ^{1/} 2-1-78	Activity 2-1-78 Through 12-31-78	Staff Adjustments ^{3/}	Adjusted Balance 12-31-78
Assets				
Plant in Service	\$ 175,617	\$ 411,530	\$ -	\$ 587,147
Less: Accrued Depreciation	(1,671)	(52,848) ^{2/}	-	(54,519)
Construction Work in Progress	15,016,663	44,560,116	(1,823,020)	57,753,759
Total Gas Plant	15,190,609	44,918,798	(1,823,020)	58,286,387
Cash and Other Assets	-	10,607,476	-	10,607,476
Total Assets	<u>\$15,190,609</u>	<u>\$55,526,274</u>	<u>\$(1,823,020)</u>	<u>\$68,893,863</u>
Partners' Equity and Liabilities				
Partners' Contributions Paid In:				
Calaska Energy Co.	\$ -	\$ 5,675,000	-	\$ 5,675,000
Pacific Interstate Trans. Co. (Arctic)	-	5,675,000	-	5,675,000
Pan Alaska Gas Company	-	5,675,000	-	5,675,000
Northern Arctic Gas Co.	-	5,675,000	-	5,675,000
United Alaska Fuels Corp.	-	5,675,000	-	5,675,000
Northwest Alaskan Pipeline Co.	15,190,609	5,675,000	-	20,865,609
Total Partners' Contributions	<u>15,190,609</u>	<u>34,050,000</u>	-	<u>49,240,609</u>
Partners' Equity:				
Retained Earnings	-	14,317,272	(1,823,020)	12,494,252
Total Partners' Equity	<u>15,190,609</u>	<u>48,367,272</u>	<u>(1,823,020)</u>	<u>61,734,861</u>
Accounts Payable and Other Liabilities	-	7,159,002	-	7,159,002
Total Partners' Equity and Liabilities	<u>\$15,190,609</u>	<u>\$55,526,274</u>	<u>\$(1,823,020)</u>	<u>\$68,893,863</u>

^{1/} This is the adjusted balance, as shown in the initial staff audit report on ANNGTC, after the proposed disallowance of \$42,224,461 pre-partnership expenditures.

^{2/} Includes AFUDC of \$13,988,691.

^{3/} Staff adjustments do not cover AFUDC for reasons explained in the introduction of this report.

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**REPORT ON
RESULTS OF AUDIT OF EXPENDITURES
BY THE
ALASKAN NORTHWEST NATURAL GAS
TRANSPORTATION COMPANY
WHICH WERE
INCURRED FROM
JANUARY 1, 1979 THROUGH DECEMBER 31, 1979
(DOCKET NO. CP78-123, et al.)**

October 1980
Division of Audits
Office of Chief Accountant
Federal Energy Regulatory Commission

REPORT ON RESULTS OF AUDIT OF EXPENDITURES
BY THE ALASKAN NORTHWEST
NATURAL GAS TRANSPORTATION COMPANY WHICH
WERE INCURRED FROM JANUARY 1, 1979
THROUGH DECEMBER 31, 1979
(DOCKET NO. CP78-123, et al.)

INTRODUCTION

This is the third in a series of reports on the results of audits of expenditures related to the construction of the Alaska Natural Gas Transportation System (ANGTS).^{1/} The audits and reports are being made pursuant to the directions contained in Administrative Order No. 4, issued April 18, 1979.

The first report conveyed the results of the staff's initial audit of expenditures charged to the Alaskan section of ANGTS. The initial audit covered expenditures incurred prior to the formation of the partnership (Alaskan Northwest Natural Gas Transportation Company (ANNGTC)) on February 1, 1978, for the construction and operation of the Alaskan section of ANGTS. Amounts charged to the Alaskan section for pre-partnership expenditures totaled \$57,415,070 including Allowance for Funds Used During Construction (AFUDC) of \$7,798,313.

The second report conveyed the results of the staff's audit of partnership expenditures charged to the Alaskan section of ANGTS for the period February 1, 1978 through December 31, 1978. Partnership expenditures charged to the gas plant accounts during this period totaled \$44,918,798 including AFUDC of \$13,988,691.

^{1/} ANGTS was authorized by the Alaska Natural Gas Transportation Act of 1976 (ANGTA), 15 U.S.C. 719 et seq. and the President's Decision and Report to Congress on the Alaska Natural Gas Transportation System, as enacted into law, H. J. Res. 621, Pub. L. No. 95-108 (November 2, 1977).

In the first report, the staff recommended the disallowance of \$42,224,461, including AFUDC of \$6,833,041, of the total claimed pre-partnership expenditures of \$57,415,070.^{2/}

In the second report, the staff recommended the disallowance of \$1,823,020 of the total claimed partnership expenditures.^{2/}

The staff's findings and recommendations in that report did not cover \$13,988,691 of AFUDC capitalized during the period.

This report conveys the results of the staff's audit of partnership expenditures charged to the Alaskan section of ANGTS for the period January 1, 1979 through December 31, 1979. Partnership expenditures charged to the gas plant accounts during this period totaled \$53,710,138, including AFUDC of \$11,920,788. The staff's findings and recommendations in this report do not cover the \$11,920,788 of AFUDC claimed during the period. A large part of the AFUDC claimed is related to pre-partnership and other expenditures which are at issue in our first two audit reports. Upon disposition of the audit findings and recommendations in these

^{2/} These proposed disallowances have been reflected on the Exhibit.

reports, AFUDC claimed for the period January 1, 1979 through December 31, 1979 will be recomputed and adjusted as appropriate.

SUMMARY.

With respect to the partnership expenditures made during the period January 1, 1979 through December 31, 1979 (\$41,789,350 exclusive of AFUDC), the staff concludes that:

1. Expenditures of \$40,794,243 are properly assignable to the Alaskan section of ANGTS and are of a nature that would qualify for eventual inclusion in rate base.
2. Expenditures of \$349,691 are not of a nature that would qualify for inclusion in rate base and, therefore, should be disallowed.
3. Expenditures of \$645,416 may not be properly assignable to the project for eventual inclusion in rate base. Requests to ANNGTC for additional information on these expenditures have not been answered. Therefore, the staff proposes that these expenditures be disallowed without prejudice to ANNGTC's reclaiming them upon submission of appropriate supporting information.
4. Corrective action needs to be implemented to eliminate discrepancies between the accounting records and the financial statements.

SCOPE OF AUDIT

The audit covered claimed partnership expenditures charged to the gas plant accounts totaling \$41,789,350, exclusive of AFUDC, for the period January 1, 1979 through December 31, 1979.

The audit included an examination of the accounting and other records to the extent deemed necessary to determine whether:

1. The various financial statements and reports properly reflected the underlying records and documents.
2. The expenditures were adequately documented and supported.
3. The accounting for the expenditures met the requirements of the Uniform System of Accounts and generally accepted accounting principles.
4. The expenditures were properly assignable to the Alaskan section of ANGTS and were of a nature that would qualify for eventual inclusion in rate base.
5. The other accounting and reporting regulations and requirements of the Natural Gas Act, the Decision and the Certificate of Public Convenience and Necessity were complied with.

6. The policies, procedures, and controls appear adequate to ensure the efficient and economic construction of the project.

RESULTS OF AUDIT

ANNGTC claimed partnership expenditures of \$41,789,350, excluding AFUDC. With respect to these expenditures, the staff has determined that:

1. Expenditures of \$40,794,243 were for engineering studies and plans, environmental studies, governmental fees, legal and consultant fees related to the preparation of an application for a Certificate of Public Convenience and Necessity to construct the Alaskan section of ANGTS. These expenditures are properly assignable to the Alaskan section of ANGTS and are of a nature that would qualify for eventual inclusion in rate base.
2. Expenditures of \$349,691 are not of a nature that would qualify for eventual inclusion in ANNGTC's rate base and should be disallowed. These expenditures fall into the following categories:
 - a. Lobbying Activities
Expenditures of \$158,962 to three firms engaged in lobbying

activities on behalf of ANNGTC regarding; D-2 legislation affecting lands in Alaska designated as a national reserve, an amendment to Section 103 of the Internal Revenue Code concerning the State of Alaska issuance of tax exempt bonds, and meetings with members of the U. S. Congress and members of the Alaskan legislature on various legislation affecting the project.

The Uniform System of Accounts requires that expenditures of this nature be recorded in Account 426.4, Expenditures for certain civic, political and related activities, a non-utility expense account.

b. Donations

Expenditures of \$90,002 relate to contributions to the following organizations: Alaskans for the Gas Pipeline, Citizens for Management of Alaskan Lands, Inc., and Close-Up Foundation.

The Uniform System of Accounts requires that expenditures of this nature be recorded in Account 426.1, Donations, a non-utility expense account.

c. Public Relations

Expenditures of \$74,572 to four public relations firms. One firm was located in Washington, D. C. and distributed information to the press, members of Congress and the public. Another firm provided media coverage in New York on the Alaskan gas pipeline. The third firm produced a film documenting progress on the gas pipeline. The fourth firm monitored the media and handled liason work in Canada.

The Commission in various cases has ruled that public relations type expenditures are not properly assignable to the plant accounts but are of a nature that should be recorded in Account 930.1, General advertising expenses, a utility expense account.

d. Photo Prints, Ski Lessons, and Fishing Arrangements

Expenditures of \$14,450 relates to photo prints of the "Old Salmon Cannery",

ski lessons and charter fishing arrangements which were provided to various Board of Partners representatives subsequent to their meetings in February, March and April of 1979.

The Uniform System of Accounts requires that expenditures of a nonoperating nature be recorded in Account 426.5, Other deductions, a non-utility expense account.

e. Country Club Dues

Expenditures of \$8,047 to various country clubs, luncheon and dinner clubs and athletic clubs for membership dues.

NARUC Interpretation No. 49 requires that club dues of this nature be recorded in Account 426.5, Other deductions, a non-utility expense account.

f. Gifts

Expenditures of \$3,658 relate to gifts to satisfy the oriental business custom of exchanging gifts resulting from ANNGTC's business ties with Japan.

The Uniform System of Accounts requires that expenditures of a nonoperating nature be recorded in Account 426.5, Other deductions, a non-utility expense account.

3. Expenditures of \$645,416 were not adequately supported; therefore, the staff was unable to determine whether they are properly assignable to the Alaskan section of ANGTS for eventual inclusion in rate base. Requests to ANNGTC for additional information on these expenditures have not resulted in responses which clearly document the nature and character of the items. These items fall into two general categories:

- a. Amounts paid to a number of law firms for services which appear to include political lobbying efforts designed to influence public opinion concerning the project and, as such, would not be allowable in the plant accounts under the provisions of the Uniform System of Accounts.
- b. Amounts paid to a number of consultants where sufficiently competent evidential material (i.e. contracts, written agreements, vendor memoranda, etc.) did not exist or

were not made available. Therefore, there was no adequate basis upon which to evaluate the propriety of the assignment of the costs to the project or their qualification for eventual inclusion in rate base.

Therefore, the staff proposes that these expenditures be disallowed without prejudice to ANNGTC's reclaiming them upon submission of appropriate supporting information.

4. Monthly financial statements prepared by ANNGTC reported and compared actual project expenditures with budgeted project expenditures. The accounting records supporting these financial statements did not agree with the reported actual project expenditures in many instances and adequate reconciliations were not available. Corrective action implemented by ANNGTC in 1979 were not fully successful in that the new procedures sometimes created a lag in recording a charge to the proper work order and resulted in further reporting discrepancies.

The Uniform System of Accounts requires the accounting records be maintained in a manner that permits ready analysis by the prescribed accounts and preparation

of financial statements directly from the accounting records.

It is imperative on this project that the actual construction costs be readily identifiable and verifiable. Otherwise, it will be difficult, if not impossible, to audit costs and to issue timely audit reports.

RECOMMENDATIONS

The staff recommends that:

1. \$40,794,243 of partnership expenditures be allowed as charges properly assignable to the ANNGTC project and be determined as qualified for eventual inclusion in the rate base of ANNGTC.
2. \$349,691 of partnership expenditures be disallowed as costs qualified for eventual inclusion in the rate base of ANNGTC.
3. \$645,416 of partnership expenditures be disallowed as costs properly assignable to the ANNGTC project for eventual inclusion in rate base, without prejudice to ANNGTC's reclaiming them upon submission of appropriate supporting information.