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UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Georgiana Sheldon, Acting Chairman; Matthew Holden, Jr., George R. Hall and J. David Hughes.

Alaskan Northwest Natural)
Gas Transportation Company) Docket No. CP78-123, et al.

ORDER TO SHOW CAUSE
(Issued December 15, 1980)

On February 2, 1979, Alaska Northwest Natural Gas Transporation Company (ANNGTC) filed an application for an order approving past expenditures and to establish procedures for continuing audit and approval of future expenditures and major commitments. Supplements to that application were filed on August 14, 1979 and July 16, 1980.

The President's Decision and Report to Congress on the Alaska Natural Gas Transportation System (Decision) contemplates contemporaneous auditing during the course of the project. Finance Condition 2, at page 37 of the Decision, provides in part that the project sponsors "shall . . . submit to the FPC for approval on a timely basis all components of construction work in progress." Section 9 of the Alaska Natural Gas Transportation Act of 1976 (ANGTA) (15 U.S.C. § 719g) mandates expedition.

On April 18, 1979, the Commission directed 1/ its Office of the Chief Accountant to audit expenditures incurred by the certificate holders of the Alaska Natural Gas Transportation

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1/ Directive to the Office of the Chief Accountant, Administrative Order No. 4, 7 FERC_____(1979).

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

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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. 95-158 (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 radification 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)

Cost Categories-Direct	Possible Future Value or Usefulness	No Future Value	Total
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	13,960,973	85,912,027	99,873,000
Direct Cost Ratios	13.98%	86.02%	100%
Cost Categories-General (Allocated Using Direct Cost Ratios Shown Above)			
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	108,247	666,053	774,300
Costs through Aug. 31, 1977	20,759,657	127,744,843	148,504,500
Cash Calls Required from Sept. 1, 1977 through Jan. 31, 1978 7/	-	6,345,000	6,345,000
Totals at Jan. 31, 1978	$20,759,657	$134,089,843	$154,849,500
Total Allocation	13.41%	86.59%	100%

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 ANNGTC Books	No Future Value 8/	Possible Future Value 9/
Pre-partnership Expenditures	$31,778,967	$27,517,407	$4,261,560
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	7,963,426	6,895,531	1,067,895
	$31,778,967	$27,517,407	$4,261,560

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%
	81.45%

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 CASGL 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:

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

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:

Month	Net Amount Reflected in Rate Base
1976 - November	$1,772,277
December	898,562
1977 - 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:

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

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.

Exhibit No. 1

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

	Pro Forma Balance 2-1-78	Staff Adjustments	Adjusted Balance 2-1-78
Assets			
Plant in Service	$ 175,617	$ -	$ 175,617
Less: Accrued Depreciation	(1,671)	-	(1,671)
Net Plant in Service	173,946		173,946
Construction Work in Progress:			
Northwest Alaskan Pipeline Co. Expenditures	18,874,241	(3,857,578) A/	15,016,663 B/
CAGSL Expenditures	38,366,883 C/	(38,366,883)	-
Total CWIP	57,241,124	(42,224,461)	15,016,663
Total Assets	$57,415,070	$(42,224,461)	15,190,609
Partners' Equity			
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	38,366,883 C/	(38,366,883)	-
Northwest Alaskan Pipeline Co.	19,048,187	(3,857,578) A/	15,190,609 B/
Total Partners' Equity	$57,415,070	$(42,224,461)	$15,190,609

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, Pempine 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 feasiblity 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.

Exhibit No. 3

CAGSL PARTICIPANTS AND PAYMENTS (CANADIAN DOLLARS)

Participating Companies	Date Withdrawn	Contributions and Fees Through Jan. 31, 1978
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 Realties	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		$154,849,479

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Alaskan Northwest Natural Gas Transportation Company	)))	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.

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.

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.

XII.

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 Z-1 attached hereto shows in detail the amounts and purposes for which "Qualified Expenditures" were made by Northwest. Exhibit Z-2 attached hereto shows in detail the amounts and purposes for which "Qualified Expenditures" were made by Northern, Pan Alaskan, Calaska and Pacific. Exhibit Z-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

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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.

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 E-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.

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, metallugical 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

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 E-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

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 Z-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 Z-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

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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.

to the FPC (FERC) for approval on a timely basis all components of construction work in progress.[5] 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 ANGTS 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.

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
1901 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

WHEREFORE, the Partnership respectfully requests that the Commission issue an order pursuant to ANGTA, 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) 862-6500

ATTORNEYS FOR
ALASKAN NORTHWEST NATURAL GAS
TRANSPORTATION COMPANY,
A PARTNERSHIP

VERIFICATION

THE DISTRICT OF COLUMBIA §

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
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 E-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/

	Total	Partners			
		Pan Alaska Gas Co.	Calaska 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
	6,402,175	1,613,971	1,568,017	1,615,879	1,604,308
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	13,917,264	3,508,505	3,408,608	3,512,652	3,487,499
	23,539,538	5,934,254	5,765,290	5,941,269	5,898,725
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	208,898	52,663	51,163	52,725	52,347
Sub-Total	31,778,967	8,011,392	7,783,286	8,020,863	7,963,426
6. AFUDC 2/	6,587,916	1,643,736	1,673,458	1,646,358	1,624,364
Total Qualified Expenditures Including AFUDC	$38,366,883	$9,655,128	$9,456,744	$9,667,221	$9,587,790

1/ Expenditures made prior to January 31, 1978.

2/ Includes only an interest component on funds spent.

Exhibit S-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.

"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 8-3

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	
			514,000
	Sub-Total		15,174,000
6.	AFUDC		6,595,000
	Total Actual Expenditures Including AFUDC 1/		$21,769,000

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. RM78-12, 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 2-1-78 1/	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	$15,190,609	$55,526,274	$(1,823,020)	$68,893,863
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	15,190,609	34,050,000	-	49,240,609
Partners' Equity:				
Retained Earnings	-	14,317,272	(1,823,020)	12,494,252
Total Partners' Equity	15,190,609	48,367,272	(1,823,020)	61,734,861
Accounts Payable and Other Liabilities	-	7,159,002	-	7,159,002
Total Partners' Equity and Liabilities	$15,190,609	$55,526,274	$(1,823,020)	$68,893,863

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.

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 appropropriate 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.

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 betweer 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 January 1 and December 31, 1979
With Staff Adjustments Thereto

	Adjusted Balance 1-1-79 1/	Activity 1-1-79 Through 12-31-79	Staff Adjustments 3/	Adjusted Balance 12-31-79
Assets				
Plant in Service	$ 587,147	$ 381,453	$ -	$ 968,600
Less: Accum. Deprec. and Amort.	(54,519)	(103,823)	-	(158,342)
Construction Work in Progress	57,753,759	53,432,508 2/	(995,107)	110,191,160
Total Gas Plant	58,286,387	53,710,138	(995,107)	111,001,418
Cash and Other Assets	10,607,476	(5,137,625)	-	5,469,851
Total Assets	$68,893,863	$48,572,513	(995,107)	$116,471,269
Partners' Equity and Liabilities				
Partners' Constributions Paid in:				
Calaska Energy Co.	$ 5,675,000	$ 5,061,667	$ -	$ 10,736,667
Pacific Interstate Trans. Co. (Arctic)	5,675,000	5,061,667	-	10,736,667
Pan Alaska Gas Company	5,675,000	5,061,667	-	10,736,667
Northern Arctic Gas Co.	5,675,000	5,061,667	-	10,736,667
United Alaska Fuels Corp.	5,675,000	5,061,667	-	10,736,667
Northwest Alaskan Pipeline Co.	20,865,609	5,061,667	-	25,927,276
Total Partners' Contributions.	49,240,609	30,370,002	-	79,610,611
Retained Earnings	12,494,252	12,301,507	(995,107)	23,800,652
Total Partners' Equity	61,734,861	42,671,509	(995,107)	103,411,263
Accounts Payable and Other Liabilities	7,159,002	5,901,004	-	13,060,006
Total Partners' Equity and Liabilities	$68,893,863	$48,572,513	(995,107)	$116,471,269

1/ This is the adjusted balance, as shown in the second staff audit report on ANNGTC, after the proposed disallowance of $42,224,461 pre-partnership expenditures and $1,823,020 partnership expenditures.

2/ Includes AFUDC of $11,920,788.

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

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UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Alaskan Northwest Natural Gas Transportation Company	Docket Nos. CP78-123 *et al.*

RESPONSE OF ALASKAN NORTHWEST NATURAL GAS TRANSPORTATION COMPANY TO ORDER TO SHOW CAUSE

February 13, 1981

TABLE OF CONTENTS

UNITED STATES OF AMERICA

BEFORE THE

FEDERAL ENERGY REGULATORY COMMISSION

Alaskan Northwest Natural Gas Transportation Company	))	Docket Nos. CP78-123, et al.

RESPONSE OF ALASKAN NORTHWEST
NATURAL GAS TRANSPORTATION COMPANY
TO ORDER TO SHOW CAUSE

Pursuant to Section 1.9(c) of the Commission's Regulations, Alaskan Northwest Natural Gas Transportation Company (Alaskan Northwest) hereby responds to the Commission's Order To Show Cause issued on December 15, 1980 in the above-captioned proceeding.

I. EXPENDITURES IN QUESTION

This proceeding began with the submission by Alaskan Northwest on February 2, 1979 of a request that the Commission review and approve for rate base purposes expenditures for the period prior to January 31, 1978 (Prepartnership expenditures) and from February 1, 1978 through July 31, 1978. Subsequent filings covered additional expenditures through March 31, 1980. In response to the original Alaskan Northwest filing, on April 18, 1979 the Commission issued Administrative Order No. 4 directing the Office of the Chief Accountant to conduct an audit of project expenses and report to the Commission. Three staff audit reports were attached to the above-referenced Order To Show Cause.

These reports summarized the auditor's recommendations with respect to the inclusion in the rate base of Alaskan Northwest of: (1) $38.4 million expended by four of the participants in "Arctic Gas," whose affiliates or subsidiaries are now partners in Alaskan

Northwest 1/; (2) $19.0 million expended by Northwest Alaskan Pipeline Company (Northwest Alaskan, now the operating partner of Alaskan Northwest) and its predecessor, Alcan Pipeline Company (Alcan); and (3) $72.7 million expended by the Alaskan Northwest partnership itself.

The three audit reports cover expenditures made by members of Arctic Gas, Alcan and Northwest Alaskan prior to the formation of the Alaskan Northwest partnership on January 31, 1978 (Audit No. 1), and expenditures made by the Alaskan Northwest partnership between February 1, 1978 and December 31, 1978 (Audit No. 2), and from January 1, 1979 through December 31, 1979 (Audit No. 3). The table set forth below summarizes the recommendations of the three audit reports. The Prepartnership expenditures (Audit No. 1) are shown separately for Northwest Alaskan and Gas Arctic, the latter being the partners covered by the audit who were participants in Arctic Gas through their respective affiliates. 2/

1/ The four partners in Alaskan Northwest whose affiliates were participants in the Gas Arctic Northwest Project Study Group (Arctic Gas), are as follows: Pan Alaskan Gas Company, an affiliate of Panhandle Eastern Pipeline Company; Calaska Energy Company, a subsidiary of Pacific Gas and Electric Company; Pacific Interstate Transmission Company (Arctic), a subsidiary of Pacific Lighting Corporation; and, Northern Arctic Gas Company, an affiliate of Northern Natural Gas Company, a Division of InterNorth, Inc.

Three other partners in Alaskan Northwest also participated in Arctic Gas: American Natural Alaskan Company, an affiliate of Michigan Wisconsin Pipe Line Company; Tetco Four, Inc., an affiliate of Texas Eastern Transmission Corporation and Transwestern Pipeline Company; and, Columbia Alaskan Gas Transmission Corporation, an affiliate of Columbia Gas Transmission Corporation. While the three audit reports do not deal with the Arctic Gas expenditures of these three companies, on September 19, 1980 and February 13, 1981, the Alaskan Northwest partnership requested rate base approval for the Arctic Gas expenditures of these companies. Accordingly, the comments contained in this document relative to the Arctic Gas costs covered by the audit are also applicable to such costs of those three companies.

2/ The amounts listed for Audit No. 1 are amounts expended by the five companies prior to January 31, 1978, plus an allowance for funds used during construction (AFUDC) component through the January 31, 1978 formation date of the Alaskan Northwest partnership. The amounts listed for Audit Nos. 2 and 3 do not include AFUDC. Ultimately, all of the audit amounts approved for inclusion in rate base will reflect AFUDC to the date of operation of the ANGTS.

	Accepted	Rejected	Needs Further Support
Audit No. 1			
Northwest Alaskan	$15,190,609	$ 193,236	$3,664,342
Gas Arctic Members	$ -	$38,366,833	$ -
Audit No. 2	$29,107,087	$ 652,294	$1,170,726
Audit No. 3	$40,794,243	$ 349,691	$ 645,416

Subsequent to the issuance of the show cause order, the auditors advised Alaskan Northwest that further support had been provided to justify inclusion of $4,387,770 in rate base, but that an additional $509,082 would be recommended for rejection as a lobbying expense. In addition, the auditors have informed Alaskan Northwest that $19,677 of the $193,236 previously rejected in Audit No. 1 and $130,931 of the $652,294 previously rejected in Audit No. 2 would now be recommended for acceptance. With these revisions, the following amounts have been or will be recommended for acceptance, rejection, or still require further support:

	Accepted	Rejected	Needs Further Support 3/
Audit No. 1			
Northwest Alaskan	$18,544,867	$ 413,057	$ 90,263
Gas Arctic Members	$ -	$38,366,833	$ -
Audit No. 2	$29,905,309	$ 655,962	$ 368,836
Audit No. 3	$41,180,141	$ 484,677	$ 124,532

II. SUMMARY OF POSITION

The projected capital cost of the Alaskan segment of the Alaska Natural Gas Transportation System is $8.2 billion, in 1980 dollars. The audit reports involve the portion of such amount -- approximately $130 million -- which was expended prior to 1980. That amount, and all amounts which must be expended to construct

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3/ Alaskan Northwest is in the process of providing the materials which support inclusion in rate base of this amount. Alaskan Northwest has been advised that the auditors will submit a further report to the Commission covering the revisions set forth above, plus expenses not yet finally categorized.

the pipeline, are totally at risk until the ANGTS is ready for operation.- Thus, the Commission's review and approval of these pre-1980 expenditures will establish a precedent for the rate base decisions to follow and, accordingly, is of great importance to the Alaskan Northwest partners. Because of the significance of this decision, it is imperative that the Commission keep in mind that the ANGTS is not a conventional pipeline which can be dealt with in a conventional manner.

The project is of great importance to the nation. It has encountered problems of unusual magnitude and unique nature; it has required many multinational approvals, including those by the President and Congress; and it has been the object of constant examination by a large number of public and private groups. Those unusual features have caused substantial expenditures. A decision allowing rate base treatment of such expenditures is appropriate for this unique venture. The treatment proposed here is consistent with the principles of just and reasonable ratemaking.

A. Expenditures By Arctic Gas Members

The expenditures of the former members of Arctic Gas, which as members of Alaskan Northwest continue to participate in the work necessary to complete the ANGTS, have made a direct contribution to ANGTS. Without such expenditures, the cost of that pipeline system would have been much larger, and its schedule delayed. Accordingly, inclusion of such expenditures in the rate base of Alaskan Northwest, and recovery of the expenditures by the Arctic Gas members, is just and reasonable.

The Arctic Gas expenditures were made for a broad scope of studies and presentations, as described in Section III below. The efforts to secure approval for a venture as huge and expensive as the Alaska gas pipeline were the subject of constant and active governmental and public attention. Full compliance with the requirements of all applicable statutes, regulations and judicial standards necessitated not only new, basic studies of the arctic environment, and of methods for the construction of pipelines and appurtenant facilities in such environment, but also the study and presentation for evaluation of all potentially feasible alternatives to the action proposed. Those requirements of a full examination of alternatives, and of detailed study of all aspects of the proposed project, were imposed by the National Environmental Policy Act, the Natural Gas Act, the Commission regulations under both Acts, and such court standards as those in City of Pittsburgh v. Federal Power Commission, 237 F.2d 741 (D.C. Cir. 1958). It was clear when Arctic Gas began its studies that the standards of those authorities would be strictly enforced by federal and state governmental authorities and the many private groups which participated in the decisional process. This proved to be even more true than anticipated, and the passage of the Alaska Natural Gas

Transportation Act of 1976 involved further requirements of study of alternatives and involvement of governmental agencies and other groups.

Accordingly, the work done by Arctic Gas was required, by law and legal processes, to be done before any Alaska gas pipeline could be approved. But the product of that work formed the basis of a thorough, searching decisional inquiry which resulted in the selection of a pipeline routing and configuration which will provide needed gas to consumers. The information developed and presented by Arctic Gas was used in the governmental examinations of an Alaska pipeline, and reduced the time and expense required for government studies. The adequacy of the decisional process met all legal standards. Thus, the Arctic Gas costs represent a portion of the necessary activities by the members of Alaskan Northwest which went into the process of selecting the route and other configurations of the Alaska gas pipeline, and of attempting to achieve the financing and construction of that pipeline. Those activities and costs have substantially contributed to the progress of the Alaska pipeline, and will continue to do so. They were prudent, good faith efforts and expenses of the companies involved, prudently undertaken to make possible the approval, financing and construction of an all-land pipeline to bring Prudhoe Bay gas to the contiguous states. The goal of the Arctic Gas members, like that of other participants in Alaskan Northwest, was and is to create such a pipeline in order to secure needed gas supply for the gas consumers which depend upon them.

The effort to build an Alaska pipeline continues and great progress has been made. A route and configuration for such pipeline has received federal governmental approvals in Canada and the United States, including such final federal approvals, and financing, necessary to construct portions of the southern Canadian and "lower 48" segments of the system on a "pre-built" basis. Construction has begun on these southern portions. The further steps necessary to secure final approvals and financing for the northern Canadian and Alaskan portions of the pipeline system are in progress. The costs which the Alaskan Northwest sponsors, including the Arctic Gas companies, have incurred and will hereafter incur, are part of the continuing efforts of those companies to secure gas from Alaska. Such costs are part of their continuing pipeline activities directed toward securing gas supplies for their customers. They have been, and will be, prudently incurred costs in legitimate, reasonable activities directed toward that goal.

It must be remembered that what Alaskan Northwest is seeking in this proceeding is inclusion of the subject expenditures in the rate base of the Alaska pipeline, which will only affect charges to consumers when that pipeline is ready to begin operations. That is the only request which has been made and thus is the only issue now involved in these proceedings. In view of the nature, quality and timing of the activities which

produced those costs, it is clear that it would be unjust and unlawful if the Arctic Gas companies were unable to recover the costs of the Arctic Gas activities. By having such recovery occur through inclusion of such costs in the rate base of the Alaska pipeline, those costs will be paid, as they should be, by those who purchase Alaskan gas. This is an entirely appropriate result.

Because of the process described in Section III, in which the early efforts of Arctic Gas, and then Alcan, each contributed to the necessary progress of the study, consideration and selection of a specific route and configuration of the Alaska pipeline, and the continuing efforts which those companies now are making to achieve the final approval, financing and construction of such pipeline, any past decision to disapprove unsuccessful project costs is not applicable here. This is not a situation in which efforts to build a pipeline to Alaska have been unsuccessful, with the result that the consumers of gas will not receive the benefits of gas from Alaska. Instead, the rate base treatment here requested will only occur when the Alaska pipeline is able to transport gas as a result of the efforts of the Alaskan Northwest sponsors.

The description of the course of efforts to achieve an Alaska pipeline which is set forth in succeeding sections of this document demonstrates that the efforts of the Arctic Gas companies, like those of Alcan, were a necessary part of, and prerequisite to, the work done by Alaskan Northwest to create the Alaska pipeline. The specific aspects of the way in which Arctic Gas met the requirements imposed by statutes and regulations of a full consideration of alternative routes for a pipeline to Alaska, and of methods alternative to pipelines for transporting gas from Alaska, will be shown fully below, as will the basic, generic research and planning carried on by Arctic Gas. Arctic Gas studied and presented the route proposed by Alcan, and it had been evaluated in an environmental impact statement and in hearings prior to the initial submission of the Alcan application in July, 1976. The result of the full compliance of Arctic Gas with all governmental requirements meant:

a. Alcan was able to file its route proposal, which was ultimately selected, with a relatively short preapplication time, and it was only because of that timing that such application was able to be considered during the decisional process.

b. Alcan was able to avoid the very large expense of study and documentation of the various alternative pipeline routes and transportation modes, so that the Prepartnership costs are much lower than they would have been if Alcan had done such work instead of Arctic Gas.

c. Alcan was saved the necessity of immediately forming and funding a large group to perform the same functions, considering that only a group of companies could afford such an expensive venture.

d. Alcan was not delayed in making its filing, due to the effort of Arctic Gas, which resulted in a substantial savings to consumers, as inflation and time value of money adds billions of dollars of cost. In relation to that, the rate base amounts here involved are small, indeed, and a very prudent investment in the Alaska pipeline.

The above examples, and those set forth in the subsections below, demonstrate two major factors in the issue here involved: (1) that the efforts of Arctic Gas, Alcan, the Arctic Gas companies, Northwest Alaskan and Alaskan Northwest, are all parts of the overall efforts to create an Alaska gas pipeline; and, (2) that the efforts of all of these parties made real and essential contributions to the vital national efforts to create such pipeline.

In both its Opinion No. 101, in Columbia Gas Transmission Corporation, Docket No. RP78-20, November 6, 1980, and its "Order Deciding Reserved Issues," Michigan Wisconsin Pipe Line Company, RP75-96 and RP76-100, December 19, 1980, the Commission considered the same costs incurred in Arctic Gas which are involved here. The Commission, in each case, stated a standard that would allow rate base inclusion of the Arctic Gas expenses by Alaskan Northwest: that such costs contribute to the project. The above discussion, and the more detailed description in Section III.A below, demonstrates that the activities of Arctic Gas, which produced such costs involved here, have contributed substantially to the progress of the ANGTS, and will continue to do so. Accordingly, it is just and reasonable that such costs be included in the rate base of Alaskan Northwest.

B. Prepartnership Expenditures Of Alcan And Northwest Alaskan, And The 1978 And 1979 Expenditures Of Alaskan Northwest

The Office of the Chief Accountant recommends that rate base treatment be rejected for approximately $1.4 million of lobbying and public relations expenditures made by Alcan, Northwest Alaskan, and Alaskan Northwest. These expenditures relate primarily to the issuance of the President's September 1977 Decision and Report and Congressional ratification thereof, the passage of the Natural Gas Policy Act of 1978, and financial participation in the ANGTS by the State of Alaska.

The Chief Accountant's recommendation is based upon application of normal accounting practices to a project that, as shown below, is unique insofar as the regulatory process is concerned. First, the implementation of the project has been the result of the passage

of ANGTA, which drastically altered the selection process under the Natural Gas Act. The efforts of the ANGTS sponsors in the ANGTA selection process are no different than the regulatory expenses normally permitted in rate base by the Commission.

Second, legislation enacted by Congress in the past five years, including the ANGTA, the President's Decision and Report and Congressional ratification thereof, Reorganization Plan No. 1 of 1979, and the Alaskan National Interest Lands Conservation Act, has had and/or will have a major impact on the design, construction and operation of the ANGTS. Alaskan Northwest was required to participate in the legislative process leading to the passage of these Acts to protect not only its interests but those of the future gas consumers dependent upon the ANGTS. Finally, lobbying and public relations efforts were mandated by the multinational nature of the project, and the Congressional review and approvals required; and the sheer attention and controversy attracted by the project resulting in multiple and unusually extensive examinations and approvals by a variety of bodies.

In the context of all of the relevant factors, Alaskan Northwest submits that rate base inclusion of the amounts expended for lobbying and public relations is clearly justified. The Commission should also reject the recommendation that recovery be denied for charitable contributions made by the partnership. As will be demonstrated below, the partnership is entitled to recover these expenses under prior Commission precedent.

III. ARGUMENT

A. The Payments To The Gas Arctic-Northwest Project Study Group By The Members Of That Group Which Are Participants In Alaskan Northwest Are Appropriate For Inclusion In The Alaskan Northwest Rate Base

1. The Nature of the Arctic Gas Expenses in Question

Before demonstrating, in subsection III.A.2 below, the reasons why the Arctic Gas costs involved here meet the standards for inclusion in the rate base of Alaskan Northwest, it is useful to describe the nature, extent and use of the detailed studies and presentations for which those costs were incurred. Such discussion shows the strong contribution of the Arctic Gas activities to the prompt and economic development of the ANGTS.

Prior to the formation of Alaskan Northwest, Arctic Gas members were engaged in substantial studies over a period of about ten years to determine the feasibility of and to create an Alaska

gas pipeline. Study of a northern pipeline was begun by certain members of Arctic Gas in 1967, and expanded thereafter to focus upon a pipeline from Prudhoe Bay, Alaska. The Arctic Gas group expanded from three to twenty-eight members, and later was reduced by withdrawals to sixteen, at all times consisting of United States and Canadian gas pipeline, distribution, and production companies. 4/ The large amount of study, planning and presentation work which was directed by Arctic Gas to the Alaska gas pipeline required expenditures of $154,849,500 (Canadian dollars). 5/ Only a portion of such costs are proposed to be included in the Alaskan Northwest rate base.

The Arctic Gas group made the first studies of the transportation of natural gas from Prudhoe Bay. The work involved in-depth studies of all aspects of the exceedingly complex gas transportation system. The application filed by Arctic Gas with the Federal Power Commission (FPC) in March, 1974, and accompanying applications filed with the Department of Interior and Canadian agencies, were the most extensive in history, and the hearing exhibits, testimony and data request responses filed thereafter, before, during and after the regulatory hearings, added huge additional amounts of information to the decisional process.

The Arctic Gas studies included the entire range of topics which were required to create a pipeline to transport natural gas from Prudhoe Bay to the "lower 48" states. Thus, the work included extensive studies of: (a) a large number of routes for a pipeline through Alaska and Canada to the contiguous states; (b) a large number of methods, other than such a pipeline, for transporting Alaskan gas to the contiguous states; (c) multiple environmental topics, some specific to the various alternative routes and transportation methods studied, but most of which are of a generic nature which involve questions and answers applicable to any arctic gas pipeline; (d) multiple engineering topics, applicable to northern pipelines and/or the other methods of gas transportation studied; (e) the gas reserves in the Prudhoe Bay field, and deliverability from such reserves; (f) contractual methods by which the services of an Alaska pipeline could be rendered and charged for under an appropriate tariff mechanism; and, (g) methods of securing the huge financial requirements of an Alaskan gas transportation system.

4/ From 1976 on, Arctic Gas consisted of eight United States pipeline and distribution systems, seven of which are members of Alaskan Northwest, and eight Canadian companies.

5/ Such expenditures paid the costs incurred by the four corporations through which Arctic Gas carried out its activities: Alaskan Arctic Gas Study and Pipeline Companies, and Canadian Arctic Gas Study and Pipeline Companies.

These studies formed the backbone of the Arctic Gas applications filed in 1974.

After the filing of such applications, the studies continued and were directed to: (a) making further progress toward demonstrating the feasibility of the primary method for the transportation of Alaskan gas selected by Arctic Gas, including further development and presentation of a large volume of engineering, construction, financing, tariff, gas reserve and environmental studies and testimony; (b) making further progress in determining the precise, detailed methods by which a gas pipeline from Alaska could be financed, designed and constructed, including the optimum specifications and construction techniques of the pipeline; (c) demonstrating the superiority of a land pipeline over the combined pipeline, LNG tanker method, including a detailed study of that method of transportation of the Alaskan gas; (d) further examination of the land route alternatives proposed; and, (e) gathering and distributing the information required by legislative, executive and regulatory bodies of the federal government and the states.

In mid-1976, an application was filed to build a pipeline from Prudhoe Bay, using the route which was ultimately approved by the U.S. and Canadian governments. The filing was by Alcan, in concert with Canadian filings by two Canadian companies. The applications of those companies utilized the same routing, in southern Canada and the "lower 48" United States, as did the Arctic Gas proposal, with different routing in Alaska and northern Canada. The Alcan route in Alaska and northern Canada had been previously studied and described in filings and evidence by Arctic Gas as one of its alternative routings. The result was that the Alcan route was familiar to decisionmakers and had already gathered some support. Therefore, that routing proposal was able to be considered and adopted within the time available within the constraints of the ongoing hearing schedule prescribed at the Commission and in the later decisional procedures.

The overall process by which a pipeline to transport Prudhoe Bay gas was approved was very extensive. The Arctic Gas proposal was the subject of extensive hearings before the Federal Power Commission (FPC), along with a pipeline plus LNG tanker proposal of El Paso Alaska Company (El Paso). At the same time, Arctic Gas pursued applications to the Department of the Interior and other agencies in the United States, and before the National Energy Board (NEB) and other agencies in Canada. After those processes had proceeded, and certain groups in Canada and the United States had expressed opposition to the Arctic Gas proposal, Alcan and its Canadian cooperating companies filed their applications before the FPC and Canadian agencies, respectively. Hearings and other governmental proceedings relative to such applications, and those then pending, followed in both nations. All these procedures required extensive preparation and expense.

On October 22, 1976, the Alaska Natural Gas Transportation Act of 1976 (ANGTA) became law. That Act provided that the selection of the transportation system for delivery of Alaska natural gas to the contiguous states would be made by the President of the United States, subject to approval of the Congress. Provision was made for a recommendation to the President by the FPC, and comments thereon by private parties and other governmental agencies. Following the passage of ANGTA, the Commission continued its ongoing proceedings, resulting in an Administrative Law Judge proposal that the Arctic Gas "prime" routing be selected. Thereafter, the Alcan proposal was modified in light of considerations raised, and the selection process proceeded pursuant to the requirement of ANGTA. The first step in the ANGTA selection process was the "Recommendation To The President" of the FPC on May 1, 1977, in which two of the four Commissioners then in office recommended selection of the Arctic Gas routing, and the other two Commissioners recommended the Alcan routing. Comments on such decision were thereafter made by various agencies.

On July 4, 1977, the NEB granted authorization for the construction of a pipeline on the Canadian portion of the route proposed by the Canadian companies supporting the Alcan route. On September 22, 1977, the President selected the Alcan route, and that selection was thereafter approved by the Congress.

Since that time, Alaskan Northwest has been formed to construct the Alaskan portion of the ANGTS. The partners of Alaskan Northwest are Northwest Alaskan, affiliated companies of the seven members of Arctic Gas which were named earlier and whose Arctic Gas costs are the subject of this section, and three other companies.

In the following subsections, a description of the various studies and expenditures of Arctic Gas is set forth which shows the way in which such studies met governmental requirements and formed a part of the approval and developmental process of the ANGTS. Such studies included examination of alternatives to the Arctic Gas proposal, since evaluation of alternatives is a specific requirement of the relevant statutes and regulations.

a. Alternative Pipeline Routes

To choose the best route, demonstrate that choice, and comply with statutory and regulatory requirements described above, Arctic Gas studied a large number of potential routings for an all-land pipeline. Those studies provided the basis for governmental analyses and avoided time consuming legal disputes over the question of whether alternatives had been sufficiently considered and legal requirements met. Those studies resulted in presentation of the major routings listed below, but there were also multiple variations for each of such major routes.

i. The route proposed by Arctic Gas across the Arctic coastal plain and south along the MacKenzie River and on into Alberta. Several alternative variations of this route were among the required studies completed.

ii. A route offshore in the Beaufort sea, offshore Alaska and northern Canada, coupled with the MacKenzie River routing.

iii. A route through the Richardson Mountains south of the coastal plains in Alaska and northern Canada to a connection with the MacKenzie River route at a more southerly location.

iv. A routing south, rather than east, from Prudhoe Bay curving southeastward through the Yukon Flats, across into the Yukon and Northwest Territories, and into Alberta.

v. A routing south from Prudhoe Bay near the oil pipeline to a point near Fairbanks, then curving southeastward to the Alaska Highway and on into the southern Yukon, British Columbia and Alberta. This is basically the routing later urged as its primary route by Alcan and ultimately selected by the President and Congress as the route for the ANGTS, and was thus the subject of close examination by Arctic Gas.

vi. The pipeline routing south through Alaska to its southern coast, which was a part of the proposal to further transport the gas by LNG tanker from southern Alaska to California. This routing also was closely studied, since it was a focus of the first portion of the hearings, as proposed by El Paso.

These studies and the presentation of alternative routings were required and prudent for the Alaska pipeline and the decisional process related thereto. Such studies were particularly necessary under the requirements of the statutes and regulations described in section III.A.2 below, and under the requirements imposed in the hearing processes. Such factors, and the direct benefits of those studies to the governmental processes and to the choice of route ultimately made, will be described in subsequent sections.

b. Alternative Methods of Transporting Prudhoe Bay Gas

The studies by Arctic Gas of methods for transporting gas, other than by gas pipeline, included the various methods which had been suggested and which seemed potentially feasible. Those "alternative modes" were: (i) separate studies of carrying liquid natural gas (LNG) by surface ship, by railroad, by submarine, by airplane, and by heliafloat; (ii) a LNG pipeline; (iii) a pipeline to carry gas in a "dense-phase" (but not as LNG); (iv) a pipeline

to carry methanol, and means to convert the gas to methanol; and, (v) a system to convert the gas to electricity and transport it in high voltage electric lines.

Each of the above studies were necessary under governmental requirements, and involved substantial expenditures, in order to produce enough detail to satisfy statutory and regulatory requirements.

c. Environmental Studies and Presentations

The Arctic Gas project carried on extensive environmental studies. In terms of subject matter, they included:

i. Zoological matters. These included studies of the types and extent of animal (bird, fish, ground mammals) populations in various relevant general areas, and also basic studies to determine what activities disturb the presence, breeding and feeding of various species, and methods by which the effects of such disturbing activities can be negated or mitigated. Such work involved experimental activities, as well as observational studies, many conducted over a period of years, which have contributed to the basic knowledge in these fields.

ii. Botanical matters. The activities in this category involved surveys of existing vegetation in the relevant general areas, extent of likely disturbance from planned activities, and ways to avoid such disturbance by route relocation, construction techniques and timing, and other means. Even more extensive and basic, however, were the lengthy experimental studies carried on to determine the best methods for revegetation of disturbed areas. This included not only testing of multiple existing species, but also experimental development, and then production, of new strains.

iii. Geological matters. Extensive surveys of soil and topography in the general areas of the various alternative routes were conducted. More basic and extensive, however, were seminal studies of the nature of northern soils, including permafrost, and methods of access to, and construction and maintenance of, pipelines in such soils. These studies were carried on at multiple locations, including four test sites in differing areas of Alaska and Canada.

iv. Meteorological matters. Studies of weather patterns were carried on relative to development of methods for avoidance of animal disturbance, and for carrying on supply, construction, operation, inspection and repair of the pipeline.

v. Water quality. Base line studies of water quality were made, as were studies of the extent to which various foreign substances could be introduced or increased without environmental damage. Water availability surveys were also made.

vi. Air quality. Similar base line and disturbance studies were carried on relative to air quality.

The above types of studies and presentations encompassed a wide variety of separate activities, most of which are of a basic scientific nature applicable to any northern pipeline project; indeed, to any human activity in the arctic, subarctic and other northern areas. The studies are original scientific work which made a substantial contribution to the nation's information and understanding relative to the arctic environment. Such information is not limited in applicability, and are available to arctic projects and activities, both private and governmental.

In summary, the environmental work, categorized by subject matter above, was directed to the following general purposes.

i. Basic, generic environmental work which is applicable to most, if not all, areas of the arctic and/or subarctic. This work was not site specific, but was applicable to problems occurring on all of the alternative routes studied, including the route ultimately approved for Alcan.

ii. Environmental work applicable mainly to one of the various "alternative routes" studied by Arctic Gas. As noted, it was necessary for such work to be done by someone, and Arctic Gas did it. One of such alternative routes was the Alcan route.

iv. Environmental work applicable to the route proposed by Arctic Gas. That route became an alternative to the Alcan route which was ultimately selected, and was extensively studied by Arctic Gas.

Study of each of the above topics was needed to secure and expedite the governmental evaluations of the ANGTS which were required, and also produced information beneficial to the decisional processes and to the ANGTS.

d. Design, Engineering and Construction

The pipeline design, engineering and construction studies were devoted to the same basic categories listed above relative to the environment. A substantial amount of the studies involved generic work devoted to optimization of pipeline sizing, pressure and materials. Arctic Gas did basic research on various

gradations of pipeline pressure, working with unprecedented pressures of 1260, 1440 and 1680 pounds per square inch absolute, and intermediate stages. This work involved the construction of test sites to test pipeline reaction at various pressures and sizes. It also involved the financing of pipe burst tests at established pipe testing installations, all to examine the interaction of pipe size, gas pressure and temperature. Seminal work on longitudinal fractures in high pressure pipelines was sponsored, and methods developed to prevent and/or limit such fractures. Study of methods of controlling slumping in pipeline operation in permafrost resulted in development of techniques for refrigeration of gas during transport. This in turn, required development of methods to avoid or control frost heave as a result of general conditions combined with the presence of the cold gas. Arctic Gas also did basic work with large pipe sizes, investigating sizes up to 56 inch O.D. and the metallurgical aspects.

Arctic Gas also carried on innovative studies in the areas of arctic logistics and construction. Various methods of transport of material to Prudhoe Bay and to portions of Canada were developed, as were methods for welding large diameter pipe in arctic conditions.

Many more examples of original work by Arctic Gas are available. The point here is that such work by Arctic Gas saved Alcan the substantial time and expense of performing such studies and is largely usable directly by Alaskan Northwest. Any work which related to routes not approved was also a necessary part of the study of alternatives, but the bulk of the work was not site specific.

e. Gas Reserves and Markets

In order to determine the capacity of the pipeline required, and to demonstrate the feasibility of an arctic pipeline, Arctic Gas expended substantial costs relative to study of Prudhoe Bay gas reserves and the U.S. markets for Alaskan and Canadian gas. Such work was required for the feasibility studies and net economic benefit studies which were required by the Commission hearings and Department of Interior evaluations, and was drawn on by the Alcan project, as well as Arctic Gas. The expenses were thus necessary for the governmental proceedings, and still provide an information base for the Alaskan Northwest project.

The expenses relative to Canadian, MacKenzie Delta gas reserves were necessary for the study of a pipeline to carry both Alaskan and Canadian arctic gas together jointly. MacKenzie Delta gas reserves are of importance to the ANGTS, since the Dempster lateral (for which an application has been filed in Canada) was an important aspect of U.S./Canadian negotiations relative to approval of the Alcan project.

f. Tariff and Financial Matters

Arctic Gas developed and proposed as part of its filing before the FPC, original and unusual tariff provisions, including a transportation tariff in cost of service form. The provisions of this tariff developed by Arctic Gas have been largely adopted by Alaskan Northwest to meet the needs of ANGTS. Similarly, Arctic Gas carried on extensive surveys of capital markets, and techniques to provide security assurances to debt owners, and cash flow to equity owners. The results of such surveys and studies were presented and explained extensively to the Commission, the Department of the Treasury, other governmental agencies and potential investors. All of this work made the necessary governmental evaluations and decisions feasible, and more economical. The principles, concepts and relationships were all related to the ANGTS, have been used by Alaskan Northwest, and help form a basis for further financing steps. Even specific, complex computer models developed by Arctic Gas were used relative to the Alaska pipeline by the Commission and other governmental bodies during and after the route selection phase, and provided the basis and foundation for the models now used by Alaskan Northwest.

g. Regulatory and Legal Work

In the course of presenting its project, and exploring alternative projects, including the route ultimately chosen, Arctic Gas incurred substantial regulatory and legal expenses. This was required to present the basic information and various alternatives which were required if any project is to be built. The governmental proceedings in which such expenses were incurred resulted in changes to proposals made and to the final selection of the routing and configuration for ANGTS which was ultimately decided upon.

h. Governmental, Civic and Public Relations

Because the Alaska gas pipeline proposals, and their consideration, were determined to be so important to the nation, they came to generate unique interest by governmental agencies in addition to the Commission. Thus, expenditures were incurred by Arctic Gas in dealing with various federal agencies, including the Interior Department, Department of Transportation, Environmental Protection Agency, Council on Environmental Quality, State Department and Department of the Treasury. Arctic Gas filed the initial application with the Department of Interior for a right of way across federal lands and thus activated that Department, as well as the Commission, to produce the Environmental Impact Statements which were the primary basis of compliance with the statutory requirements for such statements and of the decision made.

Arctic Gas also took the initiative in pressing for a pipeline-treaty between Canada and the United States, and expended funds in the drafting of proposals and other work to bring it to fruition.

The Alaska pipeline selection process was ultimately conducted pursuant to the provisions of legislation: ANGTA. Arctic Gas initially urged Congress to initiate the first legislation relative to the process, and worked for its passage. It developed into the statute which was ultimately passed. Substantial expense and effort was incurred in the work for such necessary legislation. Such expense was clearly justified, since that Act had the effect of greatly speeding the decisionmaking process for selection of the pipeline routing and configuration, and for securing necessary approvals, and substantially limited the scope of, and time required for, court review. This acceleration of schedule, particularly during current periods of high inflation, will avoid substantial additional costs to consumers.

The Alaska pipeline involves the traversal of multiple states and provinces, and thus involved communication and work by Arctic Gas with multiple citizen groups and governmental agencies. Such work was necessary in order for any project to be built in the states and provinces which will be traversed by the ANGTS, in view of the size and prominence of the project. This is explained more fully in Section III.2.d below, in specific relation to the audit report proposal.

Additionally, some of the costs incurred in this category were for the development of training programs for employees, and particularly for minority groups. Such programs have produced results valuable to Alaskan Northwest, and the techniques and methods developed in such programs are available and useful to that project. Similarly, the sociological studies and presentations of Arctic Gas removed the necessity for similar work by other projects, and provided the information to governmental decisionmakers on the various alternative routes of transportation which is necessary under law.

i. Other Costs

To direct and support the above described activities, Arctic Gas incurred administrative expenses, including executive salaries, massive reproduction costs of the work products described above, travel costs and other general expenses. Since the project was not an operating entity, most of the services of the persons whose salaries were charged to general or administrative categories were actually performed on the various activities described earlier. Staff salaries (as opposed to consultant costs) were generally not distributed to operating categories (such as environmental, engineering, legal, financial, etc.), simply as an accounting convenience, even though the work was largely performed for those categories.

Additional costs were incurred by necessary support personnel, such as secretaries, clerks, personnel workers and accountants, but that staff was small in size, and was essential to support the direct activities. Filing fees to governmental agencies were also included in this category. Finally, certain costs were incurred in termination of the Arctic Gas project after governmental decisions. Such termination costs were unavoidable and were either to make final payments for the specific activities described earlier, or were of the overhead variety necessary to support such activities.

2. The Costs Incurred By Arctic Gas Meet All Standards For Inclusion In Rate Base

Alaskan Northwest submits that the above description of activities and costs shows that the Arctic Gas expenditures in question were prudently incurred, since, as described above and in Section d. below, they were made for necessary activities which benefited and greatly accelerated the selection process in both Canada and the U.S., and contributed to the Alcan project and the ANGTS itself, both in Alaska and in the "lower 48" states. As such, the costs meet the standards established by this Commission for inclusion in rate base and should be accorded such treatment.

a. The Arctic Gas Costs Were Prudent

The above description of the costs incurred by Arctic Gas demonstrate that such costs were prudently incurred in the effort to move from the general concept of an Alaska pipeline to an approved, completed pipeline. The larger part of the expenses were incurred to comply with governmental requirements, either to meet specific requirements of statutes and regulations, or to meet the information needs associated with the governmental approval process: to comply with data requests by government personnel and others, to provide required application information, and to meet the evidentiary requirements of the full hearing process. Those requirements were substantially increased by the huge size of the proposed project, and by the enactment of the National Environmental Policy Act and accompanying administrative supplementary action. The staffs of those agencies, and other parties, also participated actively in the proceedings, which contributed to the information testing and gathering process. Since multiple governmental approvals are necessary at both the federal and state (and provincial) levels, costs were also incurred in gathering and furnishing information needed to secure such approvals. The process of furnishing information for regulatory and other governmental processes involved work in depth to validate the plans made as being feasible and most appropriate, in practice as well as theory.

Unquestionably, the basic requirement for rate recovery -- that expenditures be prudently made for reasonable

activities -- has been met. It is appropriate that the recovery of such expenses be accomplished by inclusion of those expenditures in the rate base of Alaskan Northwest, since those expenditures were made as a part of the process of selection and ultimate approval of the routing of the ANGTS which will be utilized to bring Prudhoe Bay gas to markets in the lower 48 states.

b. The Benefits of the Arctic Gas Expenditures to the Decisional Process

The ultimate selection of the route proposed by Alcan came at the end of years of consideration of multiple alternatives: alternative methods of gas transportation and alternative routes and configurations for the gas pipeline method. As described earlier, all of those methods and routes were first presented by Arctic Gas. The other two proponents of projects alternative to the prime Arctic Gas proposal supported their individual projects, but Arctic Gas presented basic information on all of the reasonable alternatives. Thus, when governmental agencies were required to study the various possible methods and routes, their work was made substantially less extensive and expensive by the work done by Arctic Gas. This was true relative to the preparation of Environmental Impact Statements by the Department of Interior and the Commission, and of hearing presentations by the Commission staff on all of the topics covered, including environment, engineering, gas reserves, tariff and financing, markets and net economic benefits. Department of Interior economic studies utilized Arctic Gas developed costs and economic materials, and Treasury Department analyses used Arctic Gas presentations of facts and viewpoints. Submissions were also made by Arctic Gas to, and utilized by, the Department of Transportation, Department of State, Environmental Protection Agency and Council of Environmental Quality.

The Arctic Gas work was also used directly by decisional authorities, at the Commission and other agencies, and thus not only speeded the process but also contributed to the quality of the decisionmaking. The agencies which were aided by the Arctic Gas work, and related expenses, included not just the Commission, but also the Departments of Interior, Treasury, State and Transportation, the Environmental Protection Agency and the Council of Environmental Quality, and the Congress, plus state agencies in several states. The decisional processes of those agencies were also substantially improved to a very great extent by the unprecedented extensive efforts of the Arctic Gas project. The work -- and expenses -- of the Commission's staff was reduced as a result of the Arctic Gas work, as was the work of the other agencies. This saving of governmental expenses, to the taxpayers, is a very relevant factor here.

c. The Arctic Gas Activities and Costs Were and Continue to be a Necessary Ingredient of the ANGTS

As previously noted, the route proposed by Alcan and its Canadian counterparts ultimately authorized for construction by the United States and Canadian governments had been studied earlier by Arctic Gas. The southern portion, in Canada and the contiguous United States, was the same routing and configuration proposed by Arctic Gas as part of its primary proposal, while the Alaskan and northern Canadian routing was the Arctic Gas "Fairbanks Alternative." It was the presentation by Arctic Gas which had allowed governmental agencies and other parties to examine that "alternative." It is clear that the Arctic Gas work contributed directly to the creation of the routing ultimately chosen, and the Alcan proposal of such routing was built upon the earlier study of that route as a result of the Arctic Gas work.

In addition, the Alcan filing of the ultimately selected route could not have been made as early as it was, and thus could not have been made in time to be considered in the limited time remaining in the decisional process, if the Arctic Gas work had not been done earlier. That fact rests only partly upon the earlier Arctic Gas consideration of the routing proposed by Alcan, as described above. Even more important was the work done and presentations made by Arctic Gas relative to all of the other alternative routes for pipelines, the alternative methods of gas transportation, the basic northern environmental, design, logistic and construction methods, gas reserves and deliverability, tariff and related methodology, and financing matters. If those matters had not already been studied by Arctic Gas, Alcan would have needed to do the work.

Since all of these materials had been developed and presented by Arctic Gas, the Alcan application was able to be prepared and presented in a relatively short time. Such timing would have been impossible if Alcan had been required to study alternative routes and methods, since Alcan simply did not have sufficient time to do that between the time of its decision to advocate the Alaskan Highway routing and the time it was necessary to file the applications in order to have them considered along with the application of Arctic Gas and El Paso in the hearings which were almost completed by that time. However, Arctic Gas had already complied with the legal requirements by insuring full consideration of all feasible alternative methods of gas transportation and pipeline routings, including the route it proposed and the route proposed by Alcan. Thus, Arctic Gas had insured that the decisional processes which selected the Alcan routing were able to be in compliance with:

i. The requirement of the Alaska Natural Gas Transportation Act of 1976, P.L. 94-856, 90 Stat. 2904, 15

U.S.C. 719, et seq., that there be a full examination of the alternative methods of transporting Alaskan gas and other factors: volumes and deliverability of Alaskan gas, transportation costs, national gas supply and demand and alternative fuels, environmental impacts, safety and efficiency of design, construction schedules, financing feasibility, cost and expansibility of systems, impact on the national economy and national security, and international relations.

ii. The requirements of the National Environmental Policy Act of 1969, P.L. 91-190, 83 Stat. 852, 42 U.S.C. 4321, et seq., that the environmental consequences of major federal actions be fully evaluated, including an evaluation of the "alternatives to the proposed action."

iii. The requirements under the Natural Gas Act, 15 U.S.C. 717, that alternative proposals be considered, 6/ and under FPC regulations which require evaluation of all the factors relevant to pipeline location, design, construction and feasibility, including evaluation of the environmental consequences of proposals, and alternatives to proposals (18 C.F.R., Part 157, particularly Section 157.14).

In light of those requirements, the Arctic Gas activities were necessary and made a clear and major contribution to Alcan, and thus to the ANGTS, by enabling that routing to be selected. It was only because of the Arctic Gas activities earlier that the route ultimately selected was able to be presented for active consideration, and authorized.

The fact that Arctic Gas had done the large amount of work described above, so that Alcan avoided a duplicative effort, had a substantial effect upon the costs which Alcan was required to bear. The substantial amounts which Alcan expended would have been much larger if Alcan had been required to carry on the studies of alternative routes and alternative methods carried out by Arctic Gas, and the basic, generic work in environmental, design, construction, gas supply, financing, tariff and other relevant areas. Since the expenditures in the Alaskan Northwest rate base are much less than they would have been if Arctic Gas had not carried on its work, it is fair, and not burdensome to consumers, that the Arctic Gas costs be included in that rate base. The costs not only resulted from activities which reduced costs of others, but also made a major contribution to the selection and development of the Alaska pipeline, and will continue to do so.

6/ See, e.g., City of Pittsburgh v. Federal Power Commission, 237 F.2d 741 (D.C. Cir. 1958).

It also must be remembered that given the costs involved, a group of companies would have been required to do the Arctic Gas work if Arctic Gas had not done it. But formation of such a group at a later time, with subsequent performance of that work, would have delayed the Alaska pipeline substantially. And that delay, under the burden of constant inflation and money costs, would have added billions more dollars to the ultimate cost of the project.

The Arctic Gas costs thus clearly represent an economic savings in the construction of the Alaska pipeline, thus reducing the cost to gas consumers: incurrence of such costs avoided the addition of far larger sums to the ultimate cost of the project. Accordingly, it is equitable that the Arctic Gas costs included here, which are quite small relative to the total cost of the project, and are only a portion of the total Arctic Gas costs, be recovered by inclusion in the Alaskan Northwest rate base.

d. The Subject Audit Report Does Not Provide a Basis for Refusal to Include the Arctic Gas Costs in the Rate Base of Alaskan Northwest

The audit report states that the amounts which the Arctic Gas members expended and seek to include in the Alaskan Northwest rate base "were properly authorized in accordance with CAGSL (Arctic Gas) agreements, adequately documented and supported, and reasonably classified by cost categories." The report then goes on, however, to state its basic recommendation that not a single dollar of Arctic Gas costs should be allowed as rate base for the Alaskan Northwest pipeline.

The reasons why such audit report recommendation is wholly unjustified are apparent from the information set forth earlier in this document. It is also apparent, from a reading of the few relevant pages of the audit report, 7/ that incorrect factual conclusions have been reached, in part because of application of inappropriate policy and legal standards.

The table on page 13 of the report sets forth the total costs expended by Arctic Gas, divided into various "direct" and "general" cost categories, totaling almost $155 million. Alaskan Northwest seeks to include in its rate base only that portion of such costs which were incurred by the former members of Arctic Gas which are now members of the Alaskan Northwest partnership. The table then purports to divide the total Arctic

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7/ Only pages 13-16 and recommendation 4, page 27, deal with the basic subject of the Arctic Gas costs.

Gas costs into categories of "Possible Future Value or Usefulness" and "No Future Value," and to apply the overall relative percentages in each such category to the costs of the Arctic Gas members which are participants in Alaskan Northwest (table on page 15 of the subject report). Each of these steps is incorrect, as explained below.

The development of the two categories noted, which relate to "future value," shows a basic defect of the subject audit report. There is no requirement, in law or equity, that costs can only be recoverable if they are for activities which have future usefulness. Of what future use is a FERC filing fee, or an environmental impact statement for an already certificated projec', or studies of rejected alternatives, or, for that matter, any costs expended for past activities? They have no "future value" if that term is erroneously interpreted as restrictively as the audit report does. More accurately, however, they all have the same future value: that the project in question, which will produce future value, would not have come into being, or would have been delayed and made more expensive, if the costs had not been incurred. The Arctic Gas costs fall into that latter category. As demonstrated fully above, they were expended for activities which were an integral and necessary part of the overall process of creation of the ANGTS. The governmental processes would have been delayed and more expensive if Arctic Gas had not done its work, which would have added to the cost of the Alaska pipeline. Further, a pipeline along the now approved routing would not have been certificated without the Arctic Gas activities, and if those activities had been less extensive than they were, the Alcan proposal would have not only been more expensive, but also delayed and not in time for consideration in the decisional processes. In this regard, the Arctic Gas studies required almost ten years, while the Alcan application, building upon Arctic Gas work, was prepared in a relatively short time. The Arctic Gas activities thus clearly, to use the Commission's formulation of the standard, "contributed" to the creation of the Alaskan Northwest pipeline. In that more accurate sense, those activities have both past and future value to the Alaska pipeline, so that when such pipeline comes into being, the costs in question should be included in its rate base.

The Audit Report does not define its "future value" standard. It is impossible to know just how the categorization of costs was done by the audit, since no detail has been presented in the report. 8/ However, examination of the four reasons given

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8/ The auditors presumably made decisions as to the multitude of Arctic Gas cost items, to fit each into the audit report categories. Examination of those decisions, even if the information which would allow such examination were now available from the auditors, would not be productive, since those categories are not correct or appropriate, and thus not relevant.

at pages 14 and 15 of the report for viewing costs as having "no future value" gives some indication of the rationale used. Those standards are not appropriate.

The first "disqualifying feature" discussed (a), rules out expenditures which "relate to the specific design, location, siting, and other items unique to the unsuccessful route." Such expenditures are alleged to "have no specific direct provable relationship or future benefit to the approved Alaskan section of ANGTS." That formulation rests upon the erroneously restrictive standard discussed above. As has been explained, it was legally necessary for any Alaska pipeline to be approved, that all feasible alternatives be examined and presented. The route later proposed by Alcan was earlier studied and presented by Arctic Gas. The Arctic Gas routing later became an alternative to the routing proposed by Alcan, which was ultimately selected, and like all the alternative routings presented by Arctic Gas, was necessary to the decisional process. No pipeline could have been approved without such presentation of alternatives, which allowed selection of the route chosen. Moreover, it must be recognized that if Alcan had had the time to do the work, the costs of such work would be in the Alaskan Northwest rate base on that basis, at the higher level of costs which the burden of inflation would have caused, with increased cost to the consumer. Thus, it is totally inappropriate to allege that Arctic Gas expenditures relative to the route it proposed, or any other route, had no "relationship or future benefit" to the Alaskan Northwest pipeline.

Such a conclusion also totally overlooks the basic scientific nature of much of the work done by Arctic Gas. Since the proportions of the costs which the audit report classifies as having "Possible Future Value" is so small, it is obvious, even without detailed information, that the cost of most, if not all, of such basic, generic work done by Arctic Gas has been classified as of "no future value." That conclusion is inaccurate, too, and also overlooks the contribution of such activities to the decisionmaking process.

The second allegedly "disqualifying feature" (b) listed by the audit report is that some expenditures are purportedly "duplicative to other expenditures specifically related to the approved Alaskan section of the ANGTS," and specific reference is made to "filing fees and related payments to the various U.S. and Alaskan governmental bodies." Again, this category does not recognize the historical development of the proceedings, nor the importance of the Arctic Gas activities to the final selection of an approved routing. As described above, the early filings by Arctic Gas, which produced the governmental fees in question, were a necessary part of the selection process, and made the approved route possible. Without Arctic Gas, the entire process would have

been greatly delayed, and different. For example, the environmental impact statement process centered very heavily upon the Arctic Gas filing and the bulk of the governmental fees resulted from that activity. The result was that the time and fees relative to the Alcan proposal, when later filed, were vastly reduced. Thus, such necessary expenditures in the process of the approval of an Alaska pipeline -- paid by Arctic Gas, as well as Alcan and later Alaskan Northwest -- are valid rate base items for Alaskan Northwest.

The third category of "disqualifying features" (c) proposed by the audit report stems from a conclusion that "similar activities or task related expenditures have never been considered capitalizable items by the Commission in the past." The report states that such costs "are related to lobbying and public relations type of activities." It is not known what amount of Arctic Gas costs the report puts into each of those categories. What is clear is that the singling out of those activities discloses a lack of information as to the activities which it was necessary for Arctic Gas -- and Alcan and now Alaskan Northwest -- to carry out in order to have an Alaska pipeline approved and constructed. As discussed in more detail in Section III, Part B below, the ANGTS, like its oil predecessor, has been surrounded by publicity and controversy since it was conceived. Opposition to any Alaskan gas pipeline arose almost immediately, and remained active for an extended period. State agencies, including legislatures, held hearings and expressed interest in regulating and changing the line, or imposing requirements short of "regulation" in such areas as procurement and employment. Other private groups and state agencies wholly approved of an Alaska pipeline, but supported the Arctic Gas or Alcan or El Paso routings, and requested information from the project they favored. Those groups repeatedly contacted federal agencies and legislators, and multiple examinations of all aspects of the pipeline proposals were made by various federal agencies and legislative committees. The passage of ANGTA, which expressed congressional recognition of the critical need for Alaskan gas, and which altered the method for selecting a single project and route, heightened the need to deal with all the private and governmental groups and agencies which involved themselves in the decisional process. If such activities had been avoided there would be no Alaska pipeline; opposition and pressure for constant change would have smothered the effort, and governmental agencies which had a legal right to be informed would have been unsatisfied, and would not have acted. In this context, the public and governmental affairs expenditures of Arctic Gas, Alcan, Northwest Alaskan, and Alaskan Northwest were an essential part of the process of having approved and constructed the largest private construction project in history.

Arctic Gas also developed the concept of an agreement between the governments of Canada and the United States relative to the Alaska pipeline and provided initial drafts and worked for

adoption of the concept by the two governments. Such an agreement was devised and executed by the governments and forms a basis for the ANGTS. Finally, the governmental and public affairs expenses of Arctic Gas included efforts which led to and supported passage of the ANGTA. Effort was needed to achieve passage of such unique legislation to provide for a single gas project, and to assure that its terms did not make creation of the pipeline impossible. The selection and limited judicial review features of such act speeded the process of selection, and thus reduced the cost of the ANGTS. In fact, the existence of ANGTA emphasizes the point made here. The Alaska pipeline is a unique project, and the activities necessary to bring it into being -- and the costs therefor -- are unusual and extensive. The audit report does not take account of that fact.

The final "disqualifying feature" (d) proposed by the audit report relates to expenditures which the report states "specifically relate to Canadian: (1) line design or layout, (2) land or rights of way, (3) gas supply, (4) regulatory filings." Such a category is not justified, as will be explained here. But initially, it raises the question of whether there has even been an accurate identification of what Arctic Gas expenditures actually "relate to Canada." This is because in order to understand the funds expended by the Arctic Gas project "in Canada," it is necessary to understand the basic organization of that project. For reasons partly historical and partly relating to the relative mileages in Alaska and Canada, the Arctic Gas project was organized initially and mainly in Canada. The portion of the staff which was physically located in Canada was about five times as large as that located in the United States, while the major engineering and environmental consultants were also Canadians. Thus, Canadian staff and organizations did much of the work described above, relative to both the United States and Canada. This included pipeline design, including the nonsite specific (generally applicable) work done, as well as the generic and seminal environmental work described above. Financial planning was coordinated in Canada for both U.S. and Canadian portions, and substantial portions of the necessary executive and support personnel were in Canada. Canadian witnesses testified extensively before the Commission, relative to both Canadian and U.S. portions of the project, and before other executive agencies and before Congress. Most of the work performed and developed by the Canadian, as well as American, staff and consultants of Arctic Gas, was presented in both the Canadian and U.S. regulatory proceedings and was necessary for a full evaluation of the various alternative projects. What is necessary to note here is that the site of preparation of work, and the nationality of the worker, are irrelevant to the question of the necessity and usefulness of the work, and resultant work product, to the Alaska pipeline project and to the necessary processes which were required before such project could be approved.

Even if, however, there were an accurate, and not overstated, identification of work which actually was related "only" to Canada, such categorization would be illusory, because the Alaska pipeline is a joint United States, Canadian project, to carry Alaskan gas and later Canadian gas. The project could not exist without approval of the Canadian, as well as United States, portion of the line. Thus, the design, land rights, regulatory proceedings and approvals of the NEB and other governmental agencies, and all other aspects of the Canadian portion of the pipeline, are essential parts of the overall Alaskan project. Therefore, the planning work was essential, as were the extensive proceedings both before the NEB of Canada and the "Berger Commission," including comparative hearings, as in the United States. Just as the U.S. proceedings necessarily considered the Canadian, as well as U.S., portions of the pipeline, as well as the principles, information, and procedures common to both, so did the Canadian proceedings consider the U.S. parts of the project and the common matters.

The Arctic Gas proposal was not for the principal benefit of Canada. The proposal was to carry Alaskan gas to the United States, Canadian gas to Canada, and any surplus Canadian gas to the United States. There were benefits to Canada under the Arctic Gas proposal, just as there are from the ANGTS, but the United States is the primary beneficiary of both proposals, as is made clear by the net economic benefit studies presented by Arctic Gas and governmental agencies. That leads to another important fact. Consideration of the Canadian portions of the project by U.S. governmental authorities was necessary and extensive. United States authorities even took the position that the environmental effects of the project on Canada must be considered. In addition, the feasibility of the design, configuration, construction and financing, and the costs, of the Canadian portion of the pipeline were scrutinized as fully by U.S. authorities as were such features relative to the United States portions of the pipeline. Therefore, the work done relative to Canadian portions and aspects of the pipeline was as essential a prerequisite to the approval and construction of the U.S. portions of the pipeline as was examination of the U.S. portions (and as was examination of the U.S. as well as Canadian portions in Canada).

That is equally true relative to work done regarding routes in Canada other than the route ultimately selected, and regarding Canadian gas reserves and deliverability. Canadian gas was an essential element in the routes which were alternative to the route ultimately approved, since the plans for the "Dempster Lateral" connection in Canada to connect northern Canadian gas reserves to the Alaskan Northwest pipeline are an integral part of the approvals of the Alaska pipeline by Canada. All of the routings in Canada -- that ultimately chosen and the alternatives -- were a necessary part of the planning, selection and approval processes,

as explained earlier. It must again also be recognized that much of the generic, basic work done by Arctic Gas will be used on any arctic project and the location of the work done is irrelevant.

Finally, it should be noted that the table on page 13 of the audit report shows almost $14 million of expenditures as having "Possible Future Value or Usefulness," while at page 16 of the audit report, it is stated that even though "the audit indicated that $4,261,560 of prepartnership expenditures may have possible future value to the approved Alaskan section of the ANGTS, no value at all has yet been demonstrated." From that terse and unsupported statement, the audit report moves to the conclusion that none of the Arctic Gas costs should be included. It is totally unclear what kind of showing the audit report envisages to "demonstrate" "future value," so that it is unclear what the ultimate position of the audit staff on such amounts will be. However, as shown earlier in this document, the "future value" rationale is not applicable and the audit categorization of costs is not applicable or accurate.

3. Prior Recovery Of Arctic Gas Costs By Arctic Gas Companies And Their Use Of Such Costs As Tax Deductions

The treatment of Arctic Gas costs in the rates of the Arctic Gas companies has differed between companies and for differing periods of time. Some of the companies have recovered a portion of such costs, but none has recovered all of its Arctic Gas costs. The efforts of Arctic Gas companies to recover, in their own rates, some or all of the expenditures which they have made for Arctic Gas costs does not detract from the fact that it is appropriate that such costs be treated as a part of the rate base of Alaskan Northwest. However, the Arctic Gas members do not intend, nor have they ever intended, to attempt to recover more than their investment in Arctic Gas, plus AFUDC; and, they will take the necessary steps to avoid that result when it is possible to know what those steps are. They have been forced to pursue multiple methods for recovery of such costs, because it has never been certain that any one method would be successful. It is still not certain that the method proposed herein will be successful, and the method will only be effective when the Alaska segment of the ANGTS is ready for operation. Accordingly, certain Arctic Gas members have felt it necessary to continue to attempt to recover such costs in their own rate proceedings in the meantime, and still believe such is necessary, because to abandon such efforts could be to waive rights which they may have a duty to exercise.

For purposes of these proceedings, however, it is the following facts which are significant.

i. The Arctic Gas costs should be recoverable in gas rates, because they are the costs of prudent, necessary activities which were reasonably directed to the securing of natural gas supplies for gas consumers served by each Arctic Gas member. Thus, recovery in the rates of each of those companies would be appropriate.

ii. However, the most appropriate method of recovery is for Alaskan Northwest to include such costs in its rate base, so that such costs will be recovered in the rates paid for Alaskan gas by the consumers of such gas in proportion to their share of the Alaskan gas supply.

iii. When that occurs, and the Arctic Gas members are assured recovery of their costs, each of such Arctic Gas members or their affiliates will take such steps, by reduction of their own rates or refunds or both, as is appropriate to their circumstances, to return to their customers any amounts which the customers have paid relative to such Arctic Gas costs which are to be recovered through inclusion of the Arctic Gas costs in the Alaskan Northwest rate base. This assures no "double recovery" of the costs in question.

The Arctic Gas members would have no objection to the inclusion by the Commission, in any order approving inclusion of the Arctic Gas costs in the Alaskan Northwest rate base, of an appropriate condition which would direct that the steps discussed in iii. above be taken to avoid any over-recovery. Such condition would need to be flexible enough to provide for the individual circumstances of each Arctic Gas member. Such a condition would, in a different manner, achieve the goal of avoidance of "double recovery" which underlies Recommendation No. 7, at page 28, of the subject audit report.

The subject audit report recommends that the "tax benefits already realized" by certain Alaskan Northwest partners (the report lists "the parent companies of Pan Alaskan, Northern, and Pacific") which have "claimed the prepartnership CAGSL (Arctic Gas) expenditures as tax deductions for Federal income tax purposes, thereby reducing their tax liabilities for prior years" be reflected in Alaskan Northwest's rate base. The issue of the deductibility of such expenditures is being considered on a national basis by the Internal Revenue Service and the audit report recognizes that "the dispute has not yet been resolved" (footnote 13, page 26 of Show Cause Order). When there is a final resolution, the Arctic Gas companies will then propose appropriate steps for Commission consideration, if any are needed to avoid "double recovery."

4. Calaska Expenditures Exchange Rate

The audit report recommends disallowing rate base treatment for $1.3 million of Calaska's Prepartnership expenditures on the theory that the wrong exchange rates were applied to value the investment in U.S. dollars. Alaskan Northwest opposes this recommendation for the following reasons. First, Calaska's percentage share of the investment in, and assets of, Arctic Gas is identical to that of the other Alaskan Northwest partners which are seeking recovery of their or their affiliates' respective investments in Arctic Gas through the partnership. All of the Arctic Gas participants, whether Canadian or U.S. companies, made their investment in Arctic Gas in Canadian dollars. The sole difference between Calaska and the other partners seeking recovery of their Arctic Gas investment is that unlike the other partners, the Arctic Gas investment claimed by Calaska was made through a Canadian affiliate (Alberta Natural Gas Company Ltd. [Alberta Natural]) in Canadian dollars and recorded on Alberta Natural's books in Canadian dollars. In the case of the other partners, the investment was made through U.S. affiliates -- also in Canadian dollars, but recorded on their books in U.S. dollars based on the exchange rate in effect at the time each Canadian dollar contribution was made.

Second, Alaskan Northwest proposes to value Calaska's share of the Arctic Gas investment on the same basis as that of the other partners seeking recovery of their Arctic Gas investment through the partnership -- i.e., based on the exchange rate in effect at the time each Canadian dollar contribution in Arctic Gas was made by Alberta Natural. This valuation methodology is justified by the fact that the investment in Arctic Gas attributable to Calaska and these other partners was shared in equal proportions among their affiliates as members of Arctic Gas, and the ownership of the Arctic Gas assets is still in such equal proportions.

Third, the audit report has ignored the fact of equally shared ownership and interest in Arctic Gas. The report looks solely to the question of the exchange rate in effect at the time a separate and distinct, albeit related, transaction concerning Alberta Natural's investment in Arctic Gas took place -- namely, the reimbursement of Alberta Natural in Canadian dollars by three U.S. companies (Pacific Gas and Electric Company, Pacific Gas Transmission Company and The Montana Power Company) for approximately 81.5% of the Arctic Gas contributions made by Alberta Natural, pursuant to a side agreement among the four companies. Contrary to the audit report, the timing of that reimbursement transaction, involving an exchange of U.S. to Canadian dollars, is not relevant to the proper valuation of Calaska's share of the investment in Arctic Gas.

Finally, adoption of the audit report recommendation would result in reducing the value of one partner's assets (i.e., Calaska's) solely because of the difference in the timing of U.S. to Canadian dollar exchange transactions that, in any case, were intended to accomplish different purposes (an investment in Arctic Gas in the case of the other partners versus partial reimbursement for that investment in Calaska's case). The audit report proposal would have the effect of arbitrarily transferring a part of the assets attributable to Calaska to the other partners affiliated with Arctic Gas and now seeking recovery of their investment through Alaskan Northwest. However, Calaska's share of the Arctic Gas investment is the same as that of each of the other similarly situated partners and should be so recognized.

5. Pacific's Interest Reimbursement

In their report to this Commission, the auditors recommended a reduction of $23,375 in Pacific's Prepartnership, Alaskan Northwest accounts due to interest reimbursement received by Pacific. Inadvertently, such a reduction had not been previously recorded. Therefore, Pacific does not object to the proposed reduction of $23,375 and its future Alaskan Northwest accounts will be adjusted accordingly.

6. Conclusion As To Arctic Gas Costs

The Arctic Gas companies undertook the original efforts to create an Alaskan gas pipeline. Those efforts have become part of a continuous effort of the Arctic Gas members of Alaskan Northwest, other companies, and governmental agencies to achieve that result. The costs of the Arctic Gas activities were prudently incurred for work which was essential to the planning and approval process, providing required information to government agencies and to other participants in Alaska pipeline efforts. Such work reduced the expenses of Alcan, and thus of Alaskan Northwest, and materially advanced the date that the ANGTS could be approved and constructed, thus reducing the cost of the pipeline.

By any standard, the Arctic Gas activities made a clear contribution to Alcan and the ANGTS. It is not only appropriate that the costs of such activities be included in the Alaskan Northwest rate base, but it would be totally unjust if the Arctic Gas members were required to bear such costs. They were expended in an effort to secure Alaskan gas for the nation, and that result has been approved by the government as a national goal. Those companies have never been recompensed in their rates for any risk of being forced to bear such costs: the limited, regulated return allowed to such companies does not allow them to undertake such risks. To require the Arctic Gas companies to bear such costs

themselves would not only be unlawful 9/ but would discourage the bearing of risks in their continuing contribution to the Alaska pipeline effort and to other innovative gas supply efforts.

It is only when the Alaska segment of ANGTS is ready for operation that the costs in question will be recovered under the proposal here in question. Recovery in that way will be no windfall: it will provide the companies with a much less favorable result than they could have achieved through an alternative investment. They have contributed to creating an Alaska gas pipeline, and it is fully justified that the consumers of Alaskan gas bear the costs of the Alaska pipeline, including the costs here involved.

Alaskan Northwest believes that the facts set forth above show that the Arctic Gas costs meet the standards for inclusion in its rate base. However, we stand ready to furnish further information relative to the nature and extent of such costs, and the reasons they were incurred, if the Commission so desires, and reserve the right to do so if the Commission believes that further information is required to grant the relief requested herein. Alaskan Northwest believes, however, that it has demonstrated that the Arctic Gas work constituted a very substantial contribution to the ANGTS, and that the costs of such work were prudently incurred. It is submitted that oral argument should be held before the Commission if there is any doubt on that question.

Accordingly, it is respectfully requested that Alaskan Northwest be allowed to include in its rate base the costs paid to Arctic Gas by the partners in Alaskan Northwest which are members of Arctic Gas, plus AFUDC.

9/ Since the costs paid by Arctic Gas members were prudently incurred in a reasonable effort to secure gas for their customers, they must be recoverable either from Alaskan Northwest, and thus from consumers of Alaskan gas, or from the consumers served by each of the Arctic Gas members. Recovery of such costs cannot be denied. See, e.g., Mississippi River Fuel Corp. v. FPC, 163 F.2d 433, 437 (D.C. Cir. 1947), Pub. Serv. Comm'n. of N.Y. v. FPC, 467 F.2d 361, 370 (D.C. Cir. 1972); Bluefield Waterworks & Improvement Co. v. Pub. Serv. Comm'n. of W. Va., 262 U.S. 679, 692-93 (1923), FPC v. Hope Natural Gas Co., 320 U.S. 591, 603 (1944), Permian Basin Area Rate Cases, 390 U.S. 747, 756-762 (1968).

B. Rate Base Treatment For The Prepartnership Expenditures Of Alcan, Northwest Alaskan, And The Alaskan Northwest Partnership Expenditures For 1978 And 1979 Should Be Allowed

1. Lobbying Activities

The Chief Accountant recommends that lobbying expenditures of Alcan, Northwest Alaskan and Alaskan Northwest, totalling $1,056,587, be disallowed and recorded in Account 426.4, a non-utility expense account. These expenditures relate to: (1) the passage of ANGTA and the approval of the President's Decision; (2) passage of the Natural Gas Policy Act of 1978; (3) State of Alaska participation in financing the Alaskan segment of the ANGTS; and, (4) general efforts on behalf of the project before Congress, such as the Alaska Lands bill.

This recommendation fails to acknowledge the changes in the regulatory process brought about by ANGTA and other congressional actions, such as approval of the President's Decision, acceptance of Reorganization Plan No. 1 of 1979, and the special treatment accorded Alaskan gas and Alaskan gas costs in the NGPA. Part of this legislative process involved the preparation and presentation by the sponsors of considerable information, studies, reports, and briefings in response to requests from concerned legislators, their staffs, and congressional committees with oversight responsibilities. While these actions may have been before Congress, and were therefore categorized by the auditors as lobbying, the Commission should adopt a policy for the ANGTS which recognizes that expenditures on such matters should be allowed rate base treatment, just as if the sponsors had performed the same tasks in answer to questions posed by the Commission or its staff. In the unique situation of ANGTS, in which Congress plays such an important role either as a legislative body or through congressional staff inquiries and requests, these expenses should be perceived as the functional equivalent of Commission and Commission staff efforts during a certification proceeding. This is most certainly true of expenditures associated with the lobbying activities questioned by the Chief Accountant.

a. The Passage of ANGTA and Approval of the President's Decision

ANGTA was designed to ensure expeditious completion of the ANGTS, thereby reducing the cost of gas to consumers. In view of this end result, it is difficult to imagine a more acceptable type of cost for rate base treatment than the expenses associated with approval by Congress of the ANGTA. Additionally, because ANGTA drastically amended the normal certification process

by requiring a Commission recommendation, Presidential Decision, and Congressional approval, the outcome of the competitive application procedure was in doubt until Congress acted by Joint Resolution. Alaskan Northwest has no doubt that recovery of the costs incurred in pursuing the selection process to conclusion, had it taken place before the Commission instead of Congress, would be allowed. Congressional approval under ANGTA was the same type of procedure, only before a different forum, and this change of venue was the choice of Congress in ANGTA, not the election of the sponsors. Thus, since these lobbying costs were identical to precertification regulatory expenses normally allowed by the Commission, such costs should be permitted in rate base as legitimate rate base expenditures.

b. NGPA

Coincident with the ANGTS selection process before the Commission and the Congress in 1977, the Congress was engaged in a lengthy debate concerning the future price of natural gas, including sales from Alaska. Specifically, in April, 1977 the President submitted to Congress the National Energy Act, a portion of which dealt with natural gas matters. Because the two houses approved divergent pieces of legislation on this subject (H.R. 8444 and S.2104), the two bills were submitted to conference. After a protracted debate, the conferees were able to agree on a compromise proposal, and on November 9, 1978 Congress passed the Natural Gas Policy Act of 1978. Title I, Section 109(c)(4) of that Act established the price for the sale of natural gas produced at Prudhoe Bay, Alaska, and Title II, Section 203(a)(8) and (9) and Section 208 exempted for the most part the cost of producing, transporting and distributing Alaskan gas from the incremental pricing provisions of the NGPA. That Act also addressed the issue of Alaskan gas production-related costs, including establishing the parameters for Commission review and approval of the costs of processing and conditioning Alaskan gas. 10/

The Commission is well aware of the wide variety of natural gas pricing issues considered during the lengthy and far ranging debate that resulted in the enactment of the NGPA. Simply by referring to the economic analyses in the President's Decision (pp. 44-46, 174-180), it is obvious that any pricing question concerning Alaskan gas has a vital impact on the project. Consequently, since Congress was the forum in which this decision was to be made, and since the decisions affected the ANGTS, Alaskan Northwest found it necessary to participate in all aspects of the NGPA congressional debates. As shown below, the cost of this effort is a legitimate rate base expenditure under the Commission's accounting regulations.

10/ See 124 Cong. Rec. S. 16257 (daily ed. Sept. 17, 1978).

The Office of the Chief Accountant recommends disallowance of rate base treatment for the costs associated with the above lobbying effort, and the proposed assignment of such costs to Account 426.4. This ignores the fact that Account 426.4 provides that such account:

> shall not include such expenditures which are direc ly related to appearances before regulatory or other governmental bodies in connection with the reporting utility's existing or proposed operations. (Emphasis added.)

This is a perfect description of Alaskan Northwest's lobbying activities on the NGPA. Furthermore, if the Commission, rather than Congress, had set a producer price for the sale of Alaskan gas, Alaskan Northwest would have participated fully in that proceeding to insure that the rate allowed would not adversely affect the marketability of the gas and the financeability of the project. The expenditures by the partnership before the Commission for this purpose would have been allowed rate base treatment. The fact that Congress exercised its authority to regulate sales of gas in interstate commerce, rather than delegating such authority to the Commission, should not cause a different result. Therefore, the lobbying costs connected with the NGPA should be capitalized.

c. State of Alaska

The Commission considers project financing when reviewing a certificate application under Section 7(c) of the Natural Gas Act. (18 C.F.R. § 157.14(a)(14).) In addition, Section 5(c)(8) of ANGTA, 15 U.S.C. § 719c(c)(8) required the Commission to discuss the "feasibility of financing" in making its May 2, 1977 Recommendation to the President, and also required other agencies to discuss the "sources of financing for capital costs," in their July 1, 1977 comments to the President on the Commission's formal recommendation. See ANGTA § 6(a)(5), 15 U.S.C. § 719d(a)(5). Taking these concerns into account, the President's Decision includes a direction that the successful applicant must ". . . make the final arrangement for all debt and equity prior to the initiation of construction." 11/ The Decision also found that a significant financial participation by the State of Alaska to the ANGTS would be ". . . in the interest of the State, the Nation and the expeditious construction of the project." 12/

11/ Decision at 36.

12/ Id. at 119.

In view of the President's findings, the project sponsors attempted to convince the State of Alaska, through the legislative process, to provide financial support in aid of project financing. Under Alaskan law, this type of activity may not be undertaken without approval of the state legislature. 13/ As with the lobbying costs discussed earlier, it seems apparent that the auditors would not have recommended inclusion of these costs in Account 426.4 if the Alaskan legislature had been a state regulatory body. The fact is, however, that a regulatory agency, as contrasted with a legislative body, is not normally empowered to ensure project financing guarantees. 14/ Therefore, the partnership attempted to satisfy the Presidential finding on debt support before the only forum with the requisite authority, the Alaskan state legislature. Actions in compliance with the President's Decision are not imprudent. Consequently, the expenses incurred in lobbying in Alaska for a state commitment of funds in aid of project funding should be included in rate base.

d. General

The Office of the Chief Accountant recommends that costs associated with lobbying efforts relating to matters of general interest to the ANGTS sponsors, specifically the Alaska lands bill, be disallowed. Consistent with the proper treatment for the other lobbying costs, these expenses should be given rate base treatment. The sponsors' participation in the Alaska lands bill debate focused on the preservation of the proposed pipeline route through Alaska. Section 1327 of the Alaskan National Interest Lands Conservation Act recites that the Act does not impose additional requirements on the ANGTS and, 15/ consistent with this provision, the Alaska right-of-way was granted by the Department of Interior on December 2, 1980.

Alaskan Northwest expects to incur similar costs during the course of completion of the Project. Congressional oversight will continue during both the construction and operation of the pipeline system. Alaskan Northwest should be encouraged not discouraged from complete and thorough involvement with the congressional process, and the costs associated therewith should be recoverable.

13/ Alaska Const., Art. 9, §13.

14/ See Office of Consumer's Counsel v. Federal Energy Regulatory Commission, No. 80-1303, D.C. Cir., decided December 8, 1980.

15/ Pub. L. 96-47.

2. Public Opinion/Public Relations

In its audit, the Office of the Chief Accountant has distinguished between costs for influencing public opinion (Audit 1) and expenditures for public relations (Audits 2 and 3). The staff recommends that neither cost be capitalized, but does suggest that the latter costs be expensed. It is important to first understand that the recommendation of different treatment is not warranted. "Influencing public opinion" involves $115,406 expended by Northwest Alaskan for the preparation and dissemination of information concerning the three alternate proposals during the selection process. The staff accountants believe this material was used to influence public opinion and the opinions of public officials during the selection process, and recommends that the amounts involved be assigned to Account 426.4, a nonutility account. Public relations, by contrast, consists of $197,897 for the preparation and distribution of information to the press, members of Congress and the public, for the preparation of films on the Alaska pipeline, and for media coverage. According to the Office of the Chief Accountant, this amount belongs in Account 930.1, "General advertising expenses," which is a utility expense account.

The purported distinction between costs associated with what the staff labels as "influencing public opinion" and public relation costs is wholly artificial. The purpose of the sponsors' activities was the same throughout -- to inform the public generally and governmental decisionmakers in particular of the nature of the Alaskan Northwest proposal, its progress through the approval process, and the prospects for future advancement. Thus, the costs for "influencing public opinion" should be placed in Account 930.1 as utility expenses. 16/

This resolution represents an accounting solution, not a rate-making decision. Alaskan Northwest believes that these expenses should be granted [illegible]e base treatment, because in contrast to normal Commission practice, the ANGTA approval process, both for selection of a successful applicant and continued congressional oversight, involved many levels of Federal officials, including members of Congress. The sponsors had to make their case in a fashion that would convince the decisionmakers of the benefits of the Alaskan Northwest project. Since it was not always possible to obtain direct access to decisionmakers, other recognized methods of influencing opinion were utilized, such as the dissemination of brochures, pamphlets, films, newspaper advertisements and

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16/ A natural gas pipeline company that had rates currently in effect would record all such costs in Account 930.1 and recover them in rates as operating and maintenance expenses.

articles. These activities were made necessary by the unique regulatory/decisionmaking process associated with this project -- a process that required the sponsors to prosecute their case in a manner that used less traditional means than the staff would accept without direction from the Commission. Alaskan Northwest urges the Commission to recognize these changed circumstances and accept the public opinion/relations costs for inclusion in rate base.

If the Commission elects not to allow full rate base treatment of these costs, and instead allows recovery as an operating expense, the Commission must take into account that unlike the normal operating pipeline that recovers its operating expenses on a timely basis through rate filings, ANGTS will not become operational until late 1985; and these types of costs will continue to occur throughout the engineering and construction stages of the project. Thus, an amount expensed in Account 930.1 cannot be recovered on a current basis. For this reason, if full rate base treatment is not afforded, Alaskan Northwest urges the Commission to permit Alaskan Northwest to record these expenditures in a deferred account, such as Account 186, and allow carrying charges on the amounts in such account at the equivalent AFUDC rate until the Alaskan segment of the ANGTS is ready for operation. At that time the total in the deferred account would be amortized over a period to be determined in the future, subject to Commission approval. 17/

3. Charitable Contributions

The Commission staff auditors have identified certain project expenditures as donations and recommended that these costs be assigned to Account 426.1, as a nonutility expense. 18/ This assignment should not determine the treatment of these costs for ratemaking purposes. Charitable contributions booked in Account 426.1 would normally be considered as operating expenses and recovered as an above-the-line figure. The instant expenditures should be treated the same, with the adjustment noted above to compensate Alaskan Northwest for the disparity between the timing of expenditure and recovery.

17/ Alaskan Northwest requests this treatment for all expenses where rate base treatment is denied but costs are still assigned to a utility expense account. Otherwise, the accounting designation would equate to disallowance.

18/ These items include contributions to: Hubert Humphrey Institute of Public Affairs (University of Minnesota Foundation), the Anchorage Community YMCA, Alaska Foundation of Native Youths, Iditarod Trail Committee, Inc., Alaskans for the Gas Pipeline, Citizens for Management of Alaskan Lands, Inc., and Close-Up Foundation.

Alaskan Northwest is entitled under Commission precedent to reimbursement for these contributions. The standard for judging charitable contributions was established by the Commission in Opinion No. 428, United Gas Pipe Line Company, 31 F.P.C. 1180, 1189 (1964):

> [W]e believe that contributions of a reasonable amount to recognized and appropriate charitable institutions constitute a proper operating expense. Corporations have an obligation to the communities in which they are located and they are expected to recognize this obligation. It is our opinion that these contributions have an important relationship to the necessary costs of doing business. (Footnote omitted) 19/

The Commission went on to note that the type of charity contemplated as "recognized and appropriate" was one that met the criteria established in the Internal Revenue Code. 20/

The charitable contributions by the project sponsors set forth above meet the criteria established in United. Each is a recognized charity located in areas of importance to the ANGTS. For this reason, the Commission should permit Alaskan Northwest to record the amount of such contributions in a deferred account, and allow carrying charges on such amounts, until the Alaska segment of the ANGTS is ready for operation. At that time the accumulated total would be expensed under the terms of the Alaskan Northwest tariff.

4. Other Expenditures

The auditors recommend disallowance of $69,613, comprised of expenditures for purposes other than those previously referenced in Section III.B. above. Alaskan Northwest does not oppose this recommendation. The costs of these activities were inadvertently included in the accounts of Alaskan Northwest and these types of costs will not appear in future Alaskan Northwest accounts.

19/ All of these organizations are recognized by the IRS as exempt from taxation under Section 501(c)(3) of the Internal Revenue Code.

20/ See also, Opinion No. 609, Union Electric Company, 47 F.P.C. 144 (1972).

IV. CONCLUSION

For the foregoing reasons Alaskan Northwest respectfully requests the Commission take the following action:

1. Approve the inclusion of the requested Arctic Gas expenditures in the Alaskan Northwest rate base.

2. Include in the rate base of Alaskan Northwest all lobbying expenditures of Northwest Alaskan and the Alaskan Northwest partnership.

3. Treat costs incurred by Northwest Alaskan for influencing public opinion the same as the expenses for public relations by Alaskan Northwest, and allow such amounts in the rate base. In the alternative, permit Alaskan Northwest to record these amounts in a deferred account, such as Account 186, that will accumulate carrying charges equivalent to the applicable AFUDC rate, until the Alaska segment of the ANGTS is ready for operation.

4. Treat all charitable contributions as in the alternative set forth immediately above.

Respectfully submitted,

ALASKAN NORTHWEST NATURAL GAS TRANSPORTATION COMPANY

By: Darrell B. MacKay

Darrell B. MacKay
Vice President - Regulatory and Governmental Affairs
Northwest Alaskan Pipeline Company
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Suite S-700
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February 13, 1981

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon all parties of record in Docket No. CP78-123, et al. in accordance with the requirements of § 1.17 of the Rules of Practice and Procedure.

Dated at Washington, D.C. this 13th day of February, 1981.

Darrell B. MacKay

VERIFICATION

UNITED STATES OF AMERICA)
) ss.
DISTRICT OF COLUMBIA)

DARRELL B. MACKAY, being duly sworn, on oath, says that he is a Vice President of Northwest Alaskan Pipeline Company, operating partner of Alaskan Northwest Natural Gas Transportation Company; that he has read the foregoing Response of Alaskan Northwest Natural Gas Transportation Company to Order To Show Cause and he is familiar with the contents thereof; that he has executed the same for and on behalf of said Company with full power and authority to do so; and that the matters set forth therein are true to the best of his information, knowledge and belief.

Darrell B. MacKay

SUBSCRIBED AND SWORN TO
before me this 13th day
of February, 1981.

Notary Public

My Commission Expires:

My Commission Expires January 1, 1985

PLEASE NOTE: THE PRECEDING PAGES WERE TREATED AS A UNIT IN THE ORIGINAL DOCUMENT.

PLEASE NOTE: THE FOLLOWING PAGES WERE TREATED AS A UNIT IN THE ORIGINAL DOCUMENT

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Georgiana Sheldon, Acting Chairman; Matthew Holden, Jr., George R. Hall and J. David Hughes.

Northwest Alaskan Pipeline Company) Docket No. CP78-123, et al.

Northern Border Pipeline Company) Docket No. CP78-124

Pacific Gas Transmission Company) Docket No. CP79-60

ORDER PROPOSING CONDITIONS TO CERTIFICATES

(Issued December 19, 1980)

The Commission is proposing the adoption of a condition to be appended to the final certificates of public convenience and necessity (for construction and operation of the Alaska Natural Gas Transportation System) issued by the Commission to Pacific Gas Transmission Company (PGT) and Northern Border Pipeline Company (Northern Border) in its orders of January 11 and April 28, 1980 in Docket No. CP78-123, et al., 1/ as well as to the conditional certificates issued December 16, 1977 in the same docket.

In light of the limited number, nature and scope of the proposed conditions, as well as the statutory mandate of Section 9 of the Alaska Natural Gas Transportation Act (ANGTA), 15 U.S.C. §719g, that certification of the Alaska Natural Gas Transportation System (ANGTS) be expedited, the Commission has decided to use notice and comment procedures to consider the condition. In addition to other applicable law, this order is issued pursuant to Section 7(e) of the Natural Gas Act, 15 U.S.C. §717f(e), Section 9 of the ANGTA, the President's Decision and Report to Congress on the Alaska Natural Gas Transportation System (Decision), 2/ Paragraph 7 of the Agreement Between the United States of America and Canada on Principles Applicable to a Northern Natural Gas Pipeline, and Section 402(a) of the Department of Energy Organization Act, 42 U.S.C. §7172(a).

A. Background

The ANGTS is designed to transport natural gas from the North Slope of Alaska to the lower 48 states. The pipeline will be

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1/ 10 FERC ¶61,032 and 11 FERC ¶61,088.

2/ Executive Office of the President, Energy Policy and Planning, September 1977.

constructed through Canada, and will separate into two legs (Western and Eastern) just north of Calgary, Alberta. The Western Leg will enter the United States near Kingsgate, British Columbia and terminate at Antioch, California. The Eastern leg will enter the United States near Monchy, Saskatchewan and terminate at Dwight, Illinois.

The April 28, 1980 3/ order authorized Northern Border to "pre-build" a portion of the Eastern Leg of the ANGTS, consisting of 809 miles of 42-inch pipeline from Monchy to Ventura, Iowa. The January 11, 1980 order 4/ authorized, inter alia, the early construction of a portion of the ANGTS by PGT, consisting of 160.5 miles of the Western Leg from the point of importation near Kingsgate, British Columbia to Stanfield, Oregon.

The Commission has found that the ANGTS is not a purely domestic project, but is an international project undertaken jointly by the U.S. and Canada. 5/ The Agreement between the United States of America and Canada on Principles Applicable to a Northern Natural Gas Pipeline (the Agreement on Principles) was signed by representatives of the two governments on September 20, 1977 (TIAS 9030). It was then incorporated into the Decision (at pages 47-83); inasmuch as the Decision was approved by a Joint Resolution of the Congress (on November 8, 1977), the Agreement on Principles, as a part of the Decision, has the legal force and effect of a federal statute.

3/ 11 FERC ¶61,088. The April 28 order became effective June 20, 1980 when the Commission issued its Order Granting Applications for Rehearing in Part, in the above-referenced docket. 11 FERC ¶61,302.

4/ The January 11 order became effective June 13, 1980 when the Commission issued its "Supplemental Order Issuing Certificates of Public Convenience and Necessity and Authorizing the Importation of Natural Gas, and Order on Rehearing," in the above-referenced docket.

5/ "Supplemental Order Issuing Certificates of Public Convenience and Necessity and Authorizing the Importation of Natural Gas, and Order on Rehearing," Northwest Alaskan Pipeline Company, Docket No. CP78-123, et al., June 13, 1980, 11 FERC ¶61,279, mimeo at p. 45.

The Agreement on Principles states, in Paragraph 7(a), that "having regard to the objectives of this Agreement each Government will endeavor to ensure that the supply of goods and services to the Pipeline project will be on generally competitive terms." In weighing competitiveness, the elements to be considered include price, reliability, servicing capacity and delivery schedules. Paragraph 8 of the Agreement provides for consultation between senior officials of the two governments on the implementation of principles relating to the construction and operation of the pipeline.

The responsible U.S. 6/ and Canadian officials have been discussing methods of implementing Paragraph 7 of the Agreement on Principles. The result is a reciprocal arrangement between the United States and Canada on a procedure to govern the procurement of certain designated items by the pipeline companies before contracts are awarded. That agreement between the two governments is embodied in a formal exchange of diplomatic notes, signed June 10, 1980, and is effective subject only to the necessary regulatory action in each country.

By a letter dated August 4, 1980, the Federal Inspector has forwarded to the Chairman of the Commission an official copy of the diplomatic notes. A copy of the letter, including the diplomatic notes, is attached to this order for reference. In his letter, the Inspector requests the Commission to implement the notes by attaching appropriate conditions to the project sponsors' certificates.

In this regard, the exchange of notes provides that the agreed procurement procedures are subject to approval through regulatory processes of the two countries. Within the U.S., such approval is defined in terms of amending the project sponsors' certificates:

> "In fulfillment of this agreement, the United States agrees to adopt the procurement procedures contained in the Annex to this note. It is understood that the procedures in the Annex are subject to regulatory approval in the United States, specifically the amendment of the conditional certificates of the Alaskan Northwest Natural Gas Transportation Company, of the Pacific Gas Transmission

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6/ The responsible U.S. Official is the Office of the Federal Inspector (OFI). The OFI was created by Reorganization Plan No. 1 of 1979, which became effective July 1, 1979, pursuant to Executive Order 12142 of June 21, 1979, 44 F.R. 36927 (June 25, 1979).

> Company, and of the Northern Border Pipeline Company by the Federal Energy Regulatory Commission of the United States. It is further understood that Canada will also adopt the procurement procedures contained in the Annex to this notice, and bring them into force with Canadian regulatory process."

Thus, attaching the proposed condition to the certificates would complete the process envisioned in the exchange of notes, thereby implementing the executive agreement set forth in the notes.

B. Proposed Condition

The text of the agreement set forth in the diplomatic notes is self-explanatory, and is the product of extensive deliberations and negotiations by the two governments. Accordingly, the Commission is reluctant to attempt to recast that language into detailed conditions of the style and form generally used in drafting certificate conditions. Instead, the Commission proposes to attach to the certificates a shorter and more generalized condition that simply requires the certificate holders to comply with all requirements in the agreement that are applicable to them, and to co-operate fully with the Federal Inspector in his interpretation and implementation of the agreement.

C. Comment Procedures

The Commission invites the parties of record in Docket Nos. CP78-123, et al., to submit written data, views, comments and other information concerning the matters set forth in this order. An original and 14 conformed copies should be filed by January 16, 1981, with service of copies on all parties. Parties of record may also file reply comments pursuant to the same procedure, by February 6, 1981. Comments and reply comments should be submitted to the Office of the Secretary, Federal Energy Regulatory Commission, 825 North Capitol Street, N.E., Washington, D. C. 20426, and should reference Docket Nos. CP78-123, et al. All written submissions will be placed in the Commission's public files and will be available for public inspection in the Commission's Office of Public Information, 825 North Capitol Street, N.E., Washington, D. C., during regular business hours.

The Commission orders:

(A) Parties of record in Docket No. CP78-123, et al., may submit comments and reply comments on the condition that the Commission proposes to append to the certificates of public convenience and necessity issued (for construction and operation of the ANGTS) by the Commission to the ANGTS project sponsors in the Commission's orders of January 11 and April 28, 1980, as well as to the conditional certificates of public convenience and necessity issued December 16, 1977 in that docket, as described more fully above. The proposed condition is set forth in an attachment to this order. Comments may be filed on or before January 16, 1981, and reply comments may be filed on or before February 6, 1981. Copies of all comments and reply comments should be served on all parties of record in Docket Nos. CP78-123, et al.

(B) Copies of this order shall be served on all parties in Docket No. CP78-123, et al.

By the Commission.
(S E A L)

Kenneth F. Plumb

Kenneth F. Plumb,
Secretary.

APPENDIX

PROPOSED CONDITION

The certificate holder shall comply with all of the requirements imposed on ANGTS project sponsors by the executive agreement set forth in the exchange of diplomatic notes between the United States and Canada, dated June 10, 1980, as those requirements are set forth in the "Procedures Governing the Procurement in Canada and the United States of America of Certain Designated Items for the Alaska Highway Gas Pipeline" adopted in said agreement. The certificate holder shall co-operate fully with the Federal Inspector in his interpretation and implementation of the agreement.

Docket No. CP78-123, et al.

THE FEDERAL INSPECTOR
ALASKA NATURAL GAS TRANSPORTATION SYSTEM
ROOM 2413. POST OFFICE BUILDING
1200 PENNSYLVANIA AVENUE
WASHINGTON. D C 20044

August 4, 1980

Honorable Charles B. Curtis
Chairman, Federal Energy
Regulatory Commission
825 N. Capitol Street, N.E.
Room 9000 Washington, D.C. 20426

Dear Chairman Curtis:

I have attached a copy of formal diplomatic notes, exchanged between the United States and Canada on June 10, 1980. This exchange of notes effectuates reciprocal procedures governing the procurement in Canada and the United States of designated items for the Alaska Highway Gas Pipeline, the U.S. portions of which represent the Alaska Natural Gas Transportation System. These procedures, by their terms, are to be administered by my office and the Northern Pipeline Agency.

Of particular interest to the Federal Energy Regulatory Commission is the following aspect of the U.S. diplomatic notes:

> It is understood that the procedures in the Annex are subject to regulatory approval in the United States, specifically the amendment of the conditional certificates of the Alaskan Northwest Natural Gas Transportation Company, of the Pacific Gas Transmission Company, and of the Northern Border Pipeline Company by the Federal Energy Regulatory Commission of the United States.

In this regard the Office of the Federal Inspector, as the administering agency in the U.S., is requesting that the Commission incorporate these reciprocal procedures as conditions to the aforementioned conditional certificates issued by the Commission on December 16, 1977, in Docket Nos. CP78-123, et al. In this manner these officially established and currently effective procurement review procedures may be administered by this agency also through Section 102(d) of Reorganization Plan No. 1 of 1979.

Thank you for your assistance in this manner.

Sincerely yours,

John T. Rhett
Federal Inspector

cc: John Adger
FERC
Michael Lucy
State Department
Darrell MacKay
Northwest Alaskan
Philip Reynolds
PGT
Carl Schulz
Northern Border
Trish Lortie
Canadian Embassy
Barry Yates
Northern Pipeline Agency

Enclosure 1

Docket No. CP78-123, et al.

Canadian Embassy Ambassade du Canada

No. 224 10 June, 1980

Sir,

I have the honour to refer to your Note of today's date concerning procurement procedures designed to implement the provisions of the Agreement between Canada and the United States of America on Principles Applicable to a Northern Natural Gas Pipeline, signed at Ottawa on September 20, 1977.

I have the honour to inform you that these proposals are acceptable to the Government of Canada, and to confirm that your Excellency's Note, together with the attached statement on Procedures Governing the Procurement in Canada and the United States of America of Certain Designated Items for the Alaska Highway Gas Pipeline, and this reply, which is equally authentic in English and French, shall constitute an agreement between our two governments which shall enter into force on the date of this reply.

Accept, Sir, the renewed assurances of my highest consideration.

The Secretary of State
Washington, D.C.

Docket No. CP78-123, et al.

DEPARTMENT OF STATE
WASHINGTON

June 10, 1980

Excellency:

I have the honor to refer to Paragraph 7 of the Agreement between Canada and the United States on the Principles Applicable to a Northern Natural Gas Pipeline (Pipeline Agreement) and the recent discussions between representatives of the Government of the United States of America and representatives of the Government of Canada regarding procedures to ensure procurement on a generally competitive basis for the Alaskan Natural Gas Transportation System.

As a result of these discussions, the Government of the United States agrees to enter into an agreement with the Government of Canada permitting the mutual and reciprocal implementation of procedures governing the purchase of specified items for the Alaskan Natural Gas Transportation System.

In fulfillment of this agreement, the United States agrees to adopt the procurement procedures contained in the Annex to this note. It is understood that the procedures in the Annex are subject to regulatory approval in the United States, specifically the amendment of the conditional certificates of the Alaskan Northwest Natural Gas

His Excellency

Peter Towe,

Ambassador of Canada.

Transportation Company, of the Pacific Gas Transmission Company, and of the Northern Border Pipeline Company by the Federal Energy Regulatory Commission of the United States. It is further understood that Canada will also adopt the procurement procedures contained in the Annex to this note, and bring them into force with Canadian regulatory process.

In the event of disputes regarding implementation of the procurement procedure in the United States of America or in Canada, either country may request consultations in accordance with paragraphs 7 (b) and 8 of the Pipeline Agreement.

If the foregoing is acceptable to the Government of Canada, this note and its Annex, together with your note in reply, shall constitute an agreement between the two Governments with effect from the date of your reply.

Accept, Excellency, the renewed assurances of my highest consideration.

For the Secretary of State:

Enclosure:

Annex: Procurement Procedures for the Alaskan Natural Gas Transportation System

PROCEDURES GOVERNING THE PROCUREMENT IN CANADA AND THE UNITED STATES OF AMERICA OF CERTAIN DESIGNATED ITEMS FOR THE ALASKA HIGHWAY GAS PIPELINE

Introduction

The Agreement between Canada and the United States of America on Principles Applicable to a Northern Natural Gas Pipeline, which was signed in Ottawa on September 20, 1977, states in its preamble that one of the principal objectives of the project is to "maximize related industrial benefits of each country." It further states in Clause 7(a) that "having regard to the objectives of this Agreement, each Government will endeavor to ensure that the supply of goods and services to the Pipeline will be on generally competitive terms." The same clause stipulates that the elements to be taken into account in weighing competitiveness will include price, reliability, servicing capacity and delivery schedules. Clauses 7(b) and 8 provide for coordination and consultation between the two governments with respect to the achievement of the objectives of the Agreement with respect to procurement.

In order to implement these principles, the Governments of Canada and the United States of America agree that the following procedures with respect to the procurement of certain designated items of supply for the Alaska Highway Gas Pipeline will be adopted on a reciprocal basis by the appropriate regulatory authority in each country, namely, the Northern Pipeline Agency in Canada (NPA) and the Office of the Federal Inspector in the United States (OFI).

1. Qualification of Bidders

The project companies in each country will submit a list of qualified bidders they propose to invite to tender

on any of the items designated in Schedule I to the appropriate domestic regulatory authority, which will expeditiously convey copies of any such lists to the regulatory authority of the other country both directly and through normal diplomatic channels. The regulatory authority of the other country will have 14 calendar days following its receipt in which to review the bidders' list and to propose to its counterpart the addition of any firm or firms which it considers should also be invited to tender. If any such modification is proposed, it is to be communicated to the originating project sponsor by the responsible regulatory authority in that country. Should the project sponsor not be prepared to accept the additional bidder or bidders proposed by the regulatory authority of the other country, the reasons for its position shall be communicated to that authority by the responsible domestic authority.

The project sponsors may, but are not required to, place advertisements inviting interested suppliers to prequalify as bidders for particular supplies. In the event that such advertisements are decided on for designated items, they shall be placed in appropriate trade journals or other publications in both Canada and the United States.

2. Technical Specifications and Tendering Documents

Prior to the actual solicitation of bids on designated items listed in Schedule I, the project sponsors in each country will submit technical specifications and tendering documents to the appropriate domestic regulatory authority, which will first expeditiously review the solicitation information for possibly restrictive language that would prohibit open competition and then expeditiously convey

copies of such information on a confidential basis to the regulatory authority of the other country both directly and through normal diplomatic channels. The regulatory authority of the other country will have 14 calendar days following its receipt to review such information and to submit any proposed modifications in the technical specifications or tender document to the responsible regulatory authority, which in turn will communicate such representations to the originating project sponsor. Should the project sponsor not be prepared to accept the modification of the technical specifications or tender document proposed by the regulatory authority of the other country, the reasons for its position shall be communicated to that authority by the responsible domestic authority.

3. Recommended Decisions to Purchase or Negotiate

Following the receipt and evaluation of bids on designated items listed in Schedule I, the project sponsor will submit its conclusions in a report satisfactory to the domestic regulatory authority with respect to the purchase of supply, or of entering into negotiation with one or more firms for the purpose of reaching contract agreement, to the responsible domestic regulatory authority. After expeditiously reviewing these submissions for general competitiveness, the domestic regulatory authority shall prepare and submit to the regulatory authority of the other country a meaningful summary of the report and of its conclusions. Such information shall include an outline of the factors which were taken into account by the project sponsor in arriving at its conclusions, and, in cases where consideration of industrial benefit were involved, demonstrate that they came within the framework of general competitiveness.

While maintaining the confidentiality of proprietory commercial information, including the tender prices of individual bidders, such summaries should be designed to make possible an assessment of the extent to which the proposed procurement conforms with the stated objectives of the Canada-United States Agreement. In cases where bids submitted by either Canadian or United States firm on tenders called by sponsoring companies in the other country have been rejected or accepted only in part, the conclusions of the project sponsor and the reasons for them as outlined in the project sponsor's report will be communicated by the responsible domestic regulatory authority to the regulator authority of the other country as part of the meaningful summary.

In the event the regulatory authority in the other country wishes to raise questions with respect to the conclusions or the summary containing the factors which led to those conclusions, or wishes to initiate formal consultations as provided for under Clause 7(b) of the Canada-United States Agreement on Principles, it will be required to provide notification to the responsible domestic regulatory authority within a period of 14 calender days.

Should consultations as provided for under the Agreement be invoked with respect to any aspect of the procurement process, it is recognized by the Governments of both Canada and the United States that they should proceed expeditiously so as to avoid causing any undue delay in the timely completion of the project.

4. Award of Contract

Although no specific requirement for consultation should be necessary at this time in view of the extensive provisions at earlier stages, a short delay may be required to advise the other country's regulatory authority of any significant changes that resulted during negotiations with the selected vendor(s).

Schedule 1

Designated Items

1. Line Pipe - Main Line Pipe 36 inches and over.
2. Gas Turbine/Compressor Packages.
3. Valves - 20 inches interior diameter and over (both block valves and station valves).
4. Pipe Fittings - 20 inches interior diameter and over.

PLEASE NOTE: THE PRECEDING PAGES WERE TREATED AS A UNIT IN THE ORIGINAL DOCUMENT.

RHL
Witton

FEDERAL ENERGY REGULATORY COMMISSION
WASHINGTON, D. C. 20426

August 18, 1981

MEMORANDUM TO: Honorable Philip R. Sharp
Chairman
Subcommittee on Fossil & Synthetic Fuels
Committee on Energy and Commerce
House of Representatives

Honorable Clarence J. Brown
Ranking Minority Member
Subcommittee on Fossil & Synthetic Fuels
Committee on Energy and Commerce
House of Representatives

FROM : Charles A. Moore
General Counsel
Federal Energy Regulatory Commission

RE : Proposal by Sponsors of the Alaskan Natural Gas Transportation System (ANGTS) for Congressional Waiver of Sections 4, 5, 7 and 16 of the Natural Gas Act in Certain Respects Pursuant to Section 8g of the Alaskan Natural Gas Transportation Act of 1978

Questions Presented

By letter of July 24, 1981, to C. M. Butler III, Chairman, Federal Energy Regulatory Commission, 1/ you requested a legal memorandum addressing the following questions:

1/ Hereinafter, the term "Commission" refers to the Federal Power Commission at all times before October 1, 1977, and the Federal Energy Regulatory Commission at all times thereafter.

(a) The full implications of the proposed waiver quoted hereinbelow, (b) whether there have been past Commission actions which justify the desires of the sponsors to have Congress provide the waiver, (c) hypothetical situations which would work to the injury of the pipeline sponsors of ANGTS or other participants in the project should no such waiver be provided by Congress, (d) hypothetical situations which might work to the injury of resale customers and consumers should such a waiver be provided by Congress, and (e) the reasonable likelihood of the hypothetical situations actually occurring.

The text of the waiver request, as set forth in your letter, is as follows:

> Authority to Modify or Rescind Orders
>
> Waive Sections 4, 5, 7, and 16 of the Natural Gas Act to the extent that such sections would allow the Commission to change the provisions of any final rule or order approving (a) any tariff in any manner that would impair the recovery of the actual operation and maintenance expenses, actual current taxes, and amounts necessary to service debt, including interest and scheduled retirement of debt, for the approved transportation system; or (b) the recovery by shippers of Alaska gas of (1) all costs related to the purchase of such gas at just and reasonable rates, and (2) transportation of such gas pursuant to an approved tariff.

We are advised that this text is currently a topic of discussion at staff levels in the Administration and the Congress, and that the text may be revised in one or more respects. Accordingly, the memorandum is expressly limited to the preceding text, although I will be pleased to respond as expeditiously as possible to any questions you might have in connection with material changes in such text.

Discussion

1. Background

As you know, the ANGTS is an international project created to transport natural gas from the North Slope of Alaska, through Canada, to the lower 48 states. The United States portion of the system consists of three segments: (1) the Alaska segment, running from Prudhoe Bay on the North Slope to the Yukon border; (2) the Western Leg, running from the British Columbia border to California; and (3) and the Northern Border pipeline, running from a point on the Canadian border near Monchy, Saskatchewan, to Dwight, Illinois.

The ANGTS is unlike any other gas pipeline in the United States in that it is governed by a unique legal framework. The Alaska Natural Gas Transportation Act (ANGTA), 15 U.S.C. section 719, et seq., enacted by Congress in 1976, supplements (but does not replace) the Natural Gas Act; certificates are issued under the Natural Gas Act pursuant to procedures mandated by ANGTA.

Pursuant to Section 7 of ANGTA, the President, in September of 1977, submitted his Decision and Report to Congress on the Alaska Natural Gas Transportation System (Executive Office of the President, Energy Policy and Planning) which designated both the project sponsors and the route for the ANGTS as well as many conditions for its construction. Congress approved the President's Decision by Joint Resolution, which became law on November 8, 1977. H.R.J. Res. 621, Pub. L. No. 95-158, 91 Stat. 1268, 95th Cong., 1st Sess. (1977).

The ANGTS is also governed by two international agreements with Canada, both of which have the force and effect of law. The "Agreement Between the Government of the United States of America and the Government of Canada Concerning Transit Pipelines," entered in force October 1, 1977 after ratification by the Senate, applies to all pipelines in both countries whenever one country's pipeline carries the other country's gas or oil. The treaty mandates nondiscriminatory treatment.

The "Agreement Between the United States of America and Canada on Principles Applicable to a Northern Natural Gas Pipeline," signed by representatives of the two governments on September 20, 1977, is an executive agreement that was made part of the President's Decision (pages 47-83). Inasmuch as the Decision was approved by Congress, it (including the Agreement) has the legal status of a statute. The Agreement specifies the route of the ANGTS, and contains numerous conditions. Pursuant to the Agreement, our Commission has consulted with the National Energy Board of Canada in coordinating respective certification of the various ANGTS segments in the U. S. and Canada, including related imports of Canadian gas to support the "prebuilding" of the lower half of the system.

One other relevant item of legislation is Reorganization Plan No. 1 of 1979, which was submitted by the President to the Congress and not disapproved by the Congress. The Plan establishes the Office of the Federal Inspector, which reports directly to the President. The Inspector is responsible for monitoring the construction of the pipeline, and for coordinating all federal permitting and certification of it. The Plan transfers to the Inspector the Commission's Natural Gas Act Sections 3 and 7 jurisdiction to enforce the Commission's certificates and import authorizations issued to the ANGTS project sponsors.

Two categories of tariffs are involved. The project sponsors will own and operate the various segments of the ANGTS, but will not buy or sell the gas transported through it. The shippers will buy the gas at the Prudhoe Bay Field, ship it through the sponsors' facilities, and sell it somewhere at the other end of the pipeline. The sponsors will have tariffs authorizing charges to the shippers. The shippers will in turn have tariff provisions authorizing charges to their customers for the sale of the gas, which charges will include in some form reimbursement of the shippers for the transportation charges paid by the shippers to the sponsors, as well as reimbursement for the costs of purchasing the Prudhoe Bay Field gas.

Thus, for example, if a shipper buys gas at Prudhoe Bay for sale in Detroit, the shipper would incur separate transportation charges billed by the respective sponsors of the Alaska segment, the Canadian segment, and the Northern Border segment of the system. That shipper would request

a tariff authorizing "flow through" to its customers of the full amount of transportation charges paid to the sponsors of each of the three pipeline segments through which the gas was transported, as well as the full cost of the gas itself.

The "flow through" issue is often referred to as "tracking" of charges. Tracking of gas purchase costs is authorized by the Commission's regulations, through purchased gas adjustment clauses. (See 18 C.F.R. 154.38.) Tracking of transportation charges has been authorized in certain instances on a case by case basis.

In Order Nos. 31 and 31-B, 2/ the Commission approved in principle the tracking by ANGTS shippers of transportation charges billed by U. S. certificated ANGTS project sponsors (i.e., the sponsors of the Alaska, Northern Border and Western Leg segments), but reserved for later resolution the issue of tracking the charges of Foothills Pipe Lines (Yukon) Ltd. (Foothills), the sponsor of the Canadian segment. The unresolved tracking issues (including tracking of Foothills' charges that have been approved by the National Energy Board of Canada) are currently under study by the Commission's Alaskan Delegate, who is preparing a report to the Commission.

The sponsors' and shippers' initial tariffs are approved by the Commission pursuant to Section 7 of the Natural Gas Act upon issuance of the certificates. Alaskan Northwest's pro forma tariff was approved in Order Nos. 31 and 31-B. Section 7 provides a "public convenience and necessity" standard. While the Commission may establish initial rates that meet the more rigorous "just and reasonable" standard in Sections 4 and 5 of the Act, it is not required by law to do so. The Commission must only find that the initial rates are in the "public convenience and necessity" and may reserve for later determination what the "just and reasonable" rate should be.

2/ Order No. 31, "Order Setting Values for Incentive Rate of Return, Establishing Inflation Adjustment and Change in Scope Procedures, and Determining Applicable Tariff Provisions," issued June 8, 1979 in Docket No. RM78-12; Order No. 31-B on rehearing, issued September 6, 1979, in the same docket.

Section 7(e) of the Natural Gas Act gives the Commission authority to attach conditions to certificates. The courts have construed broadly the Commission's responsibility under the Natural Gas Act to condition certificates with respect to rate terms and other matters affecting the public convenience and necessity. See, e.g., Atlantic Refining Co. v. Public Service Commission of New York, 360 U.S. 378 (1959); FPC v. Hunt, 376 U.S. 515 (1964). But see Panhandle Eastern Pipe Line Co. v. F.E.R.C., 613 F.2d 1120 (D.C. Cir. 1979), cert. denied, 101 S. Ct. 247 (1980).

Section 4 of the Act requires that all rates and charges be "just and reasonable." After certification, all changes in the initially approved tariffs and rates must be filed with the Commission pursuant to Section 4. The Commission, pursuant to prescribed standards and procedures, may "suspend" such changes for up to five months pending a hearing. If the changes are suspended, the prior approved tariffs and rates remain in effect during the period of suspension. The changes may take effect after the suspension period but subject to refund (with interest) depending on the outcome of the hearing process on contested issues or other disposition by the Commission.

Section 5(a) of the Act authorizes the Commission to institute a proceeding on its own initiative, to consider the justness and reasonableness of a certificate holder's rates and tariffs, and to determine new rates or tariff provisions if the existing ones are determined to be "unjust, unreasonable, unduly discriminatory, or preferential." Such changes can only be prospective; in a Section 5 proceeding the Commission cannot suspend rates or order refunds.

Section 16 of the Natural Gas Act authorizes the Commission to modify or rescind its orders after they have been issued. This authority, under appropriate circumstances, may be utilized for a variety of purposes, ranging from correction of mistakes to modification of certificate terms and conditions in light of changed circumstances.

2. Nature of the Financing

The subject waiver is sought from Congress by the project sponsors of ANGTS in connection with the financing of the project. The financing mechanism selected by the sponsors

has been referred to as "project financing." The propriety of project financing has been addressed by the Commission on a number of occasions, most recently in Ozark Gas Transmission System, FERC Opinion No. 125, Docket No. CP78-532 (July 28, 1981). In that opinion, the Commission described project financing generally as follows:

> Project financing differs from conventional financing mainly in connection with loan security. Security generally takes one of two forms in a conventional financing. First, the project sponsor, or borrower, has sufficient unencumbered assets that the lender feels secure in making a loan on the basis of the borrower's general credit. The loan agreement, in such cases, may require any of a number of different undertakings on the part of the borrower to maintain his creditworthiness. Secondly, if the borrower does not have unencumbered assets sufficient to secure the borrowing, the lender may require the pledge of specific assets to be funded by the borrowing as collateral for the loan. As Judge Litt pointed out in his initial decision on the Alaskan Natural Gas Transportation System, this is itself a kind of project financing. In this case the lender is secure in the knowledge that the borrower has put enough money into the project that the economic value of the project, less equity and liquidation costs, will yield sufficient funds for the lender to recover the principal value of the loan and accrued interest. A convenient example of this kind of financing is the mortgage of a building.
>
> A project financing, as it has come to be known in energy projects before the Commission, is a financing in which the general creditworthiness of the borrower is either insufficient or allegedly unavailable to secure the borrowing, and the underlying economic value of the assets to be financed are also insufficient to assure the lender that he will not lose his money. The latter inadequacy will presumptively obtain in the case of any pipeline financing, since the salvage value of the pipeline to be built should, in all cases,

be less than the loan obligation. 21/ In this case, an optional financing vehicle is the stream of income to be generated by the project. However, that vehicle is only available in the event that the income stream can be assured whether or not the project should fail. Such assurance is sought in this case in the form of the so-called minimum bill. The minimum bill has been structured in a fashion which will yield sufficient revenues to cover debt service (both principal and interest payments), whether the project is successful or not. In the event the project were to fail, the minimum bill would be levied on the customers of the shippers in the form of a surcharge for gas they do not receive.

21/ In this regard Ozark's witness, Gary, states, 'Today we all recognize a mortgage on a pipeline is virtually worthless, except for one aspect, in making a legal investment.' Tr. 12/1064

Slip opinion, at 10-11 (footnotes omitted in part).

As the Commission pointed out in the Ozark case, substantial policy justification should be found in certificate applications before the Commission pursuant to which project financing is sought. In the case of the ANGTS, such justifications have already been considered by both the Executive and Legislative Branches of the Federal Government, as well as the Commission, and have been found sufficient to permit the project financing of the ANGTS. 3/

Some of the justifications have included the substantial amount of natural gas to be delivered by the project, the potential for displacement of large quantities of foreign oil, reduction of pressure on the U. S. balance of payments, net national benefits to both the U. S. and Canada, and the anticipated average cost of gas over the project life.

3/ See, generally, Federal Power Commission, Recommendation to the President, Alaska Natural Gas Transportation Systems (May 1, 1977).

3. Reason for the Proposed Waiver

The waiver has a rather singular purpose. It is intended to assure lenders for the project that the income stream which serves as security for their loans will not be reduced below the level necessary to retire the principal of the loan and to pay the interest thereon. It would accomplish this purpose by precluding the Commission from changing the rules of the game, so to speak, in a manner which would undercut the security for the loan. This objective would be achieved by withdrawing from the Commission its authority under the Natural Gas Act to change the project tariffs in such a manner as to reduce project revenues below the level necessary to service project debt. The request for the waiver evidences that certainty of the security is essential, i.e., in this instance that the lenders will rely heavily and to their detriment on the orders of the Commission granting the certificate and establishing the tariffs as preconditions to the sponsors' take down of the construction loans.

All of the foregoing has been explicitly recognized by the Commission in FERC Order No. 31. 4/ In that order the Commission stated:

> The project sponsors have earnestly sought that this Order, especially as it relates to the tariff structure, provide assurance to prospective equity investors and lenders. The concern of the sponsors is wellfounded. The Commission fully recognizes that equity investors and lenders will make critical decisions respecting the financing of the construction of ANGTS in reliance on this Order.
>
> The Commission has articulated in great detail its rationale for this Order. Where reasoned alternatives were available, we have provided a thorough analysis of the issues and the basis for our conclusions. This thoroughness provides the investor's best security in relying on this Order.

4/ Supra, note 2, at 4 (mimeo).

The fact of the request for a waiver suggests that the project sponsors and the lenders feel that they need greater assurance than has been provided to date. The Chairman and I feel compelled to agree with that assessment. As the subsequent discussion and legal analysis shows, with the objective of "security" in mind, a waiver is clearly a far better assurance than an order of the Commission. For example, previous efforts by sponsors to secure additional certainty for lenders by attempting to obtain estoppel findings in Commission orders have been unsuccessful. 5/

5/ Applicants in the Great Plains case asked the Commission to make a very explicit estoppel case against itself by including certain statements in its order. Great Plains Gasification Associates, et al., FERC Opinion No. 69 (November 21, 1979) (reversed on other grounds, Office of Consumers' Counsel v. F.E.R.C., ___ F.2d ___ (D.C. Cir. 1980), Case No. 80-1303, decided December 8, 1980). The estoppel option will be discussed in the text, infra. In its initial brief to the Presiding Administrative Law Judge, Great Plains claimed the following:

> ". . . The lenders have indicated that they will require that the authorizations obtained [from the Commission] by the project companies contain [as a condition to take down of the loan for the project]:
>
> (1) A statement of the Commission's intention not to revoke or modify the tariff provisions approved by it for this project during the term of the bank loan;
>
> (2) A statement of the Commission's understanding that the lenders would not commit funds for this project without assurances that these provisions would continue in effect without modification during the term of the bank loan;
>
> (3) A statement of the Commission's intent to suspend the application as to this project of any future rule, order, or decision of general applicability which might affect the approved tariff provisions until after the conclusion of a full evidentiary hearing to determine the propriety and

(Footnote 5 continued on next page)

Important in the context of ANGTS financing is that a waiver would provide clear assurances and signals to foreign, as well as domestic, lenders. We are advised that a sizeable portion of the borrowing must be acquired from foreign investors because of legal lending limits and other institutional obstacles faced by domestic lenders.

4. Regulatory Risk

The regulatory risk perceived by lenders consists of two separate, but not unrelated, sets of events. They are: (1) that the Commission would change the tariffs initially approved on a claim of changed circumstances, and (2) that a subsequent Commission, composed of a majority with a different view of the public interest than the collective view of the Commission originally approving the tariffs, would change the tariffs to the detriment of the lenders in order to reflect their different views. The Commission's ability to change the tariffs in either of these events is not clear as a matter of law. It is not unlimited, but our analysis indicates that it is fairly broad. The effect of the proposed waiver would be to eliminate in material part the Commission's options -- to the extent they exist -- to change the tariffs in either of these cases.

5/ Footnote continued from prior page

lawfulness of such Commission action as it affects the tariff provisions on which the financing is based . . . ." Initial Brief of Great Plains Gasification Associates and the Customer Pipeline Companies, Docket Nos. CP78-391, et al., January 29, 1979, at 70-71.

Five other admissions were sought from the Commission, but those quoted are exemplary of what the lenders sought. Both the law judge and the Commission refused to provide them. See Opinion No. 69, at 63.

Similar estoppel findings were requested by the ANGTS sponsors in the proceeding that culminated in Order No. 31; however, they were refused in favor of the language quote at page 10, supra. As discussed hereafter, it is questionable whether such findings would achieve the desired or intended result.

5. Constitutional Question

Implicit in the questions articulated in your letter is the issue of whether the waiver is a reasonably necessary mechanism to provide the lenders with the certainty they seek. The threshold issue, in this respect, is whether there is any constitutional bar to the Commission taking the kind of action described in the subsequent paragraphs. If such a bar exists, the waiver would not be necessary. Our research indicates that this question has not been authoritatively answered by the courts. That is, there are no clear constitutional limits regarding the Commission's power to change tariffs, where parties have substantially changed position in reliance on such tariffs, and the Commission had prior, actual knowledge of such reliance. The Chairman and I believe that a respectable case could be made that it would violate basic constitutional principles of due process for the Commission to change tariffs not explicitly conditioned to permit change, when the Commission is fully aware that the tariffs form the basis of project financing, and the changes will in one way or another undercut that basis. However, there is an absence of authority to support such a proposition. 6/

6/ The question whether legislative or quasi-legislative action with retroactive effect works to deprive an owner of property without due process is somewhat analogous. Unfortunately, there are no clear principles, and the cases go both ways. See generally, text and cases collected in Cong. Research Service of Library of Congress, The Constitution of the United States of America: Analysis and Interpretation (1972), at 1165, et seq.

A case strongly suggestive that the principles of estoppel do not apply to federal agencies is Federal Crop Insurance Corp. v. Merrill, 332 U.S. 380 (1947). In that case, certain farmers were assured by a local agent of the federal corporation that a certain type of crop could be insured. In fact, rules of the corporation provided that such crops could not be insured, although neither the agent nor the farmers had actual knowledge of the regulations. Relying on the agent's advice, the crops were planted and subsequently destroyed.

(Footnote 6 continued on next page)

6/ Footnote continued from prior page

In holding that the farmers could not collect insurance for the crops despite the payment of premiums therefor and the inducement of the local agent's assurances, the Court indicated that knowledge of the rules contrary to the agent's advice would be imputed to the farmers because the rules were published in the Federal Register. Despite the difference of the facts in the Merrill case (farmers had relied on apparent rather than actual authority), the Court used strong language to suggest in dicta that the government corporation would be treated as an agency of the United States and would be immune from doctrines like estoppel. Id. at 384-85.

These dicta have led one commentator to take the following position:

> Merrill indicates that estoppel will not be used to protect an individual who has changed his position in reliance on administrative advice: 'It is settled law that no estoppel can arise against the government.' [Citing, Chapman v. Santa Fe Pac. R., 198 F.2d 498, 519 (D.C. Cir. 1951) (dissenting opinion), cert. denied, 343 U.S. 964 (1952).] B. Schwartz, Administrative Law (1976), at 133, et seq.

Professor Schwartz agrees with the Merrill-type result when the agency has acted in excess of its statutory authority. However, he goes on to say:

> . . . Both reason and policy argue that prejudicial reliance warrants invoking the doctrine of estoppel against the government in other cases: 'when the sovereign becomes an actor in a court of justice, its rights must be determined upon those fixed principles of justice which govern between man and man in like situations.' Id., at 135 (footnote omitted), citing Ritter v. United States, 28 F.2d 265, 267 (3d Cir. 1928).

(Footnote 6 continued on next page)

6/ Footnote continued from prior page

The following cases support Professor Schwartz's policy proposal: Brandt v. Hickel, 427 F.2d 53, 56-57 (9th Cir. 1970); Chapman v. El Paso Natural Gas Co., 204 F.2d 46, 53-54 (D.C. Cir. 1953); United States v. Lazy FC Ranch, 481 F.2d 985, 988-989 (9th Cir. 1973); Oil Shale Corp. v. Morton, 370 F. Supp. 108, 124-127 (D. Colo. 1973).

The decision in the Lazy FC Ranch case, supra, indicates that a line of federal estoppel cases may be emerging, and that such is required by elementary notions of fairness. 481 F.2d at 989. The Chairman advises that his view is consistent with that of Professor Schwartz and the Court in Lazy FC Ranch. However, absent an authoritative pronouncement on the matter by the United States Supreme Court, or specific federal legislation, I cannot render an opinion as General Counsel of the Commission that the Commission would in all or substantially all cases be estopped by its orders from changing the ANGTS tariffs in such manner as to impair the underlying security for the financing of the ANGTS. In my judgment, the best opinion that could be rendered would simply agree that the Commission is constitutionally prohibited from setting a confiscatory rate of return. As stated by the Supreme Court in Bluefield Water Works & Improvement Co. v. Public Service Commission of West Virginia, 262 U.S. 679, 690 (1923):

> Rates which are not sufficient to yield a reasonable return on the value of the property used at the time it is being used to render the service are unjust, unreasonable and confiscatory, and their enforcement deprives the public utility company of its property in violation of the Fourteenth Amendment.

See also, F.P.C. v. Hope Natural Gas Co., 320 U.S. 591, 603 (1943). As the subsequent discussion reveals, short

(Footnote 6 continued on next page)

6. Statutory Question

The foregoing is not to suggest that there are no Supreme Court cases dealing with regulatory estoppel. To the contrary, there are two cases of considerable relevance; however, both are based on interpretations of the enabling legislation of other agencies. In the first of these, United States v. Seatrain Lines, 329 U.S. 424 (1946), the Court held that the Interstate Commerce Commission lacked the authority to alter the certificate of a water carrier on its own motion. The holding was based on the express statutory language which permitted such action with respect to motor carriers, and the absence of correlative statutory authority in the case of water carriers, in the Interstate Commerce Act.

6/ Footnote continued from prior page

of this constitutional limitation, the Commission has considerable latitude in the exercise of its jurisdiction under Sections 4, 5, 7 and 16 of the Natural Gas Act.

The fact that the lenders have induced the project sponsors to ask for the waiver may well indicate that an unqualified legal opinion cannot be obtained from lenders' counsel to the effect that a constitutional bar exists to provide an estoppel defense. A similar conclusion may be deduced from the request for estoppel admissions in the Great Plains case, supra, note 5.

In Civil Aeronautics Board v. Delta Air Lines, Inc., 367 U.S. 316 (1961), the Supreme Court considered a similar question. The Court determined that Section 401(g) of the Federal Aviation Act prohibited the CAB from altering a certificate of public convenience and necessity, even where the certificating order purported to reserve jurisdiction prior to certification to make summary modifications pursuant to petitions for reconsideration. Reaching this result, the Court's analysis was founded on the plain meaning of the language in the enabling statute and its legislative history.

The Delta case is of particular importance to the subject of this memorandum for two reasons. First, the Court clearly explained the nature of the problem with the following statement:

> Whenever a question concerning administrative, or judicial, reconsideration arises, two opposing policies immediately demand recognition: the desirability of finality, on the one hand, and the public interest in reaching what, ultimately, appears to be the right result on the other [footnote omitted]. Since these policies are in tension, it is necessary to reach a compromise in each case . . . . Id. at 321.

The second key element of the Delta case is the recognition by the Court that the limitations placed on the CAB under the Federal Aviation Act resulted from Congressional concern during the passage of its predecessor, the Civil Aeronautics Act of 1938, over the reliance on, and consequent expenditure by airlines of large sums of money on the basis of the CAB's certificate (route) decisions. In this connection, the Court stated:

> In short, our conclusion is that Congress wanted certificated carriers to enjoy 'security of route' so that they might invest the considerable sums required to support their operations; and, to this end, Congress provided certain minimum protections before a certificated operation could be cancelled. We do not think it too much to ask that the Board furnish these minimum protections as a matter of course, whether or not the Board in a given case might think them meaningless. It

might be added that some authorities have felt strongly enough about the practical significance of these protections to suggest that their presence may be required by the Fifth Amendment. See Seatrain Lines v. United States, 64 F. Supp. 156, 161; Handlon v. Town of Belleville, 4 N.J. 99, 71 A. 2d 624; see also 63 Harv. L. Rev. 1437, 1439. Id., at 331-332.

7. The Natural Gas Act

The Seatrain and Delta cases teach that the starting point in determining the practical necessity of the waiver as a security device is the language of the relevant enabling statute, the Natural Gas Act. Sections 4 and 7 are relevant, but the key provisions are Sections 5(a) and 16. Section 16 reads in pertinent part:

> The Commission shall have power to ... prescribe, issue, make, amend, and rescind such orders, rules or regulations as it may find necessary or appropriate to carry out the provisions of this act.

Section 5(a) provides, in pertinent part, that if the Commission:

> ... [S]hall find that any rate, charge, or classification demanded, observed, charged, or collected by any natural gas company in connection with any transportation or sale of natural gas, subject to the jurisdiction of the Commission, or that any rule, regulation, practice or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate, charge, or classification rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order. [emphasis supplied]

These statutory pronouncements are mandatory as opposed to precatory. The broad language of Section 16, when employed in conjunction with Section 5, has permitted the Commission to alter and amend conditions to certificated service with full approval by the

courts. Section 5(a) has been interpreted as giving the Commission authority to alter the terms and conditions of certificated service even though the affected parties, acting alone, could not have changed them. F.P.C. v. Louisiana Power and Light Co., 406 U.S. 621, 646-647 (1972). In Opinion No. 754-A, Docket No. RP71-119, issued August 17, 1976, aff'd on other grounds, Hercules, Inc. v. F.P.C., 559 F.2d 1208 (3rd Cir. 1977), the F.P.C. concluded, with court approval, that it could exercise its Section 5 authority to promulgate new terms and conditions attached to certificates authorizing initial service.

The combined effect of Sections 5(a) and 16 is to require the Commission to amend terms and conditions of a certificate if those terms and conditions prescribe tariff provisions subsequently found to result in rates or charges which are not just and reasonable. As the United States Court of Appeals for the District of Columbia Circuit stated in American Smelting and Refining Company v. F.P.C., 494 F.2d 925, 940-941 (1974), cert. denied sub nom., Southern California Gas Co., et al., v. F.P.C., 419 U.S. 882 (1974), once the Commission finds that an existing rate or charge is unjust or discriminatory, 7/ it "must prescribe the remedy for that condition." 8/ If the existing illegal rate or charge is the result of the operation of a certificate condition, the remedy clearly will lie in the revocation or alteration of the order prescribing that condition, and thus the certificate itself.

7/ The Commission's authority to find that a tariff (previously determined to be just and reasonable) no longer functions in a reasonable manner has been upheld by the U.S. Court of Appeals for the District of Columbia Circuit in Pacific Gas Transmission Co. v. F.P.C., 536 F.2d 393 (1976).

8/ The D.C. Circuit has also taken this position in Pacific Gas Transmission Co. v. F.P.C., supra., where it stated at page 396 that "[a]fter such a finding, the Commission had not only the power but a solemn duty to take immediate action."

Furthermore, the unique nature of the Alaskan Northwest tariff provisions may subject them to amendment on another basis. Because they were developed in a rulemaking, the provisions of Order No. 31 arguably are not the result of the Commission acting in a judicial capacity, but in a legislative one, formulating and applying policy. The distinction is important because where the Commission acts in the former capacity, applying law or policy to past facts, a decision on the merits as to a disputed, and litigated issue of fact becomes final. United States v. Utah Construction and Mining Co., 384 U.S. 354, 421-422 (1966); Davis, Administrative Law Treatise, §18.09 (1970 Supp.). In the latter case, the Commission is free to take appropriate steps without being bound by its prior actions. Permian Basin Area Rates Cases, 390 U.S. 747, 789 (1968); Public Service Commission, State of New York v. F.P.C., 511 F.2d 338, 353 (D.C. Cir. 1975). The policy determination in this case has been that the public convenience and necessity required the assurances to investors in the ANGTS provided for by the tariff provisions of Order No. 31. Arguably, the Commission has determined that as a matter of policy, at least under present circumstances, a tariff designed to meet the conditions of Order No. 31 will be just and reasonable. The same reasoning might also apply to the shipper tracking provisions in the event that such provisions are adopted by the Commission through rulemaking procedures. Although it is questionable whether the rulemaking-adjudication distinction would be given great weight in the context of the facts at hand, it might be enough to convince a future Commission that it could, within the law, conclude that a different policy determination better serves the public interest.

From the foregoing it is clear that there is a plausible case for Commission authority to subsequently alter the tariff conditions of Alaskan Northwest's certificate, relying on Sections 16 and 5(a) of the Natural Gas Act and judicial pronouncements authorizing agencies to make changes in policy. The foundation for that case is the general principle that a policy determination made by a present Commission cannot preclude a future Commission from making a policy determination to the contrary, provided that in doing so it adequately explains the reasons for its new position, Consolidated Gas Supply Corp. v. F.P.C., 520 F.2d 1176 (D.C. Cir. 1975), whether or not there has been a change of circum-

stances. Greater Boston Television Corp. v. F.P.C., 444 F.2d 852 (D.C. Cir. 1970). A corollary to that principle is that a present Commission cannot bind a future Commission so as to preclude the prospective operation of Section 5. Optional Procedure for Certificating New Producer Sales of Natural Gas, 48 F.P.C. 218, 223 (1972); Pacific Gas Transmission Co. v. F.P.C., supra. These rules are analogous to those applicable to the legislature: namely, this Congress cannot preclude legislation, or amendments to legislation, by the next Congress.

8. Reasonableness of the Waiver Request

This line of analysis suggests several important conclusions, which bear ultimately on the recommendation of this memorandum. First, the presence or absence of a constitutional ban to the impairment by this or a future Commission of the tariffs upon which the lenders will rely is unclear. Second, there appears to be no statutory bar, such as was found to exist in the Seatrain and Delta cases, which would preclude the Commission from changing the tariffs. Even though it is clear that commentators, the Courts, at least by way of dictum, and the past and probably current Commissions accept the principle that elementary notions of justice should allow the project lenders to rely in good faith on the decisions of the Commission in making their loans, the request of the project sponsors indicating their "desires . . . to have these provisions waived" appears to be based on a concern as to the certainty of the federal estoppel doctrine under the Natural Gas Act. The questions that remain are those that are directly raised by your letter. They ask in essence whether there are either historical or predictable future facts which support or impugn the legislative request. That is, assuming that the waiver request is not patently unreasonable, is there a historical legal perspective from which the Congress could judge the future and find sound public reasons to grant or deny the waiver.

9. Past Commission Actions

For the moment I will defer to subsequent paragraphs the question of "the full implications of the waiver" and turn to your second specific question: whether there have been past Commission actions which justify the desires of the sponsors to have the subject sections of the Natural Gas Act waived. In this connection, the following contains a summary of recent cases, representative of past Commission actions, which involved issues of claimed detrimental reliance. Having done so I will leave it to the Subcommittee to conclude from these decisions whether or not the project sponsors' request is justified.

A. Jurisdiction: Distrigas Corporation, et al. v. F.P.C., et al., 495 F.2d 1057 (D.C. Cir. 1974), cert. denied, 419 U.S. 834 (1974).

This proceeding involved, in pertinent part, a filing by Distrigas Corporation and its affiliates, Distrigas of New York Corporation and Distrigas of Massachusetts, (Distrigas) which requested the Federal Power Commission to grant Distrigas the authority under Section 3 of the Natural Gas Act to import liquefied natural gas (LNG) from Algeria. 9/ The filing also contained a request by Distrigas for the FPC to issue a disclaimer of the Commission's jurisdiction under Section 7 of the Natural Gas Act. 10/

9/ Following regasification, more than 80 percent of the gas was to be sold in the state of importation to distributors and direct customers and the remainder to distributors in neighboring states.

10/ The imported LNG was to be delivered and regasified at facilities at Staten Island, New York and Everett, Massachusetts.

The Commission in a three to two vote granted the requested Section 3 authorization without condition but, noting that this was a novel situation, reserved the right to add conditions in the future if circumstances should change. The Commission noted that Section 3 of the Natural Gas Act specifically provided for such future amendments. However, the Commission did not find Section 7 jurisdiction over the regasification facilities and service nor over the facilities and services involved in the sale of the regasified LNG in the state of importation. 11/ The result of the decision was that there was no jurisdiction under Section 7 or Section 3 (by way of conditions to the import authorization) over the regasification facilities and service nor over the intrastate facilities and service. The Commission indicated its hope that this disclaimer of jurisdiction would make the project more attractive to private investors and "lead to more gas at a lower price to the consumer than if [the Commission] controlled every detail and decision related thereto." Two Commissioners dissented, arguing that the Commission should take jurisdiction under Sections 3 and 7 of the Natural Gas Act over the regasification facilities and the "intrastate" facilities.

Following the Commission's decision, Distrigas "assertedly in reliance on the Commission's limited jurisdictional disclaimer, . . . proceeded to construction of its Everett and Staten Island facilities, expending very substantial sums on each." In a new filing, Distrigas also applied for Section 3 authorization to import significant additional quantities of natural gas and for Section 7 authorization to sell these additional volumes, as well as certain of the originally authorized volumes, in interstate commerce.

11/ The Commission did take jurisdiction under Section 7 of the Natural Gas Act over the sales of gas which was ultimately destined for resale in interstate commerce. However, it found that jurisdiction over such sales attached only at the tailgate of the regasification plant.

Meanwhile, at the Commission two of the original three person majority had left and had not been replaced. Therefore, the two dissenting Commissioners were now a majority. In response to Distrigas' applications, they found that circumstances had changed since Distrigas' original application had been acted upon by the Commission. Specifically, they stated that the original Distrigas application proposed new and increased sales for resale in interstate commerce. Therefore, the Commission held that Section 7 certification was mandated for all of Distrigas' facilities.

On appeal, Distrigas argued, among other things, that once the Commission's previous decision on the jurisdictional issue was final and Distrigas had subsequently acted in reliance on that decision by (1) contracting with its customers and (2) constructing its facilities, the Commission was foreclosed from changing its mind and asserting jurisdiction where it had previously declined to do so. Distrigas cited the Seatrain case, 12/ where the Supreme Court had overturned the Interstate Commerce Commission's attempt to revoke a certificate previously granted to a water carrier.

The Court found that the Commission had the authority to issue the order it had issued under Section 3 of the Natural Gas Act but remanded for additional proceedings before imposition of any requirements to certification under Section 7. The Court distinguished Seatrain on the basis of lack of statutory authority in that case, and noted that both Section 3 of the Natural Gas Act as well as the Commission's previous order specifically contemplated changes and amendments. The Court further found that if Distrigas had relied on an interpretation of the original Commission order to the contrary (i.e., that the original Commission order granted Distrigas a permanent immunity from regulation), Distrigas' reliance was misplaced.

12/ Supra, at 15.

As part of its basis for rejecting the estoppel argument, the Court concluded that Distrigas' claim of injury was at that point hypothetical in nature since Distrigas had not demonstrated that the Commission would not ultimately authorize Distrigas' proposal.

On remand, the Commission granted Distrigas' application subject to certain conditions.

The Distrigas case is one where the Court approved a changed Commission's reversal of a previous Commission's ruling upon which the company and its lenders had arguably relied to their detriment. As a basis for that approval the Court stated, "any 'right' to non-regulation that the Commission's previous decision can be supposed to have vested in Distrigas was entirely contingent on the Commission's continuing to view such non-regulation as in the public interest." However, two facts tend to distinguish Distrigas from the ANGTS. One is the conditions cited by the Court in the original Section 3 authorization, which arguably placed Distrigas and its lenders on notice that the rule could change. The other distinguishing fact was that the Court found that the Commission's decision had not yet injured Distrigas and that it might not in the future. Presumptively, the matter was resolved at the Commission level in a way which did not adversely affect Distrigas or its lenders. Nonetheless, one could conclude that the uncertainty caused by the Commission's reversal is the type of action the ANGTS lenders seek to protect themselves against.

B. Cost of Service Tariff: Pacific Gas Transmission Co. v. F.P.C., et al., 536 F.2d 393 (D.C. Cir. 1976), cert. denied, 429 U.S. 999 (1976).

This case involved a Commission order which, pursuant to Section 5(a) of the Natural Gas Act, changed in

part Pacific Gas Transmission Company's (PGT) cost-of-service tariff after a full hearing. Prior to the Commission decision, PGT had been permitted to adjust its rates automatically on a monthly basis to reflect all changes in its costs, including amounts for gas purchased from Canadian producers for resale in the United States. This tariff had been in effect since PGT was first authorized to import gas from Canada in 1960. 13/

In 1974 and 1975, after a hearing under Section 5(a) of the Natural Gas Act, the Commission modified PGT's cost-of-service tariff to provide that changes in the cost of gas purchased by PGT from Canadian suppliers could be passed on to PGT's customers only after PGT had applied for the rate increase pursuant to Section 4 of the Natural Gas Act, and after any suspension period imposed by the Commission thereunder. The Commission revised the tariff to provide that such filings would be subject to suspension by the Commission pursuant to Section 4 of the Natural Gas Act and, if suspended, subject to refund and possible reduction as provided in Section 4 of the Natural Gas Act. The Commission justified the revised tariff by stating that Canadian authorities had recently begun to require that significantly increased prices be charged for Canadian gas sold for resale in the United States. Furthermore, Canadian authorities had changed their pricing policy by referencing it to prices for alternate energy sources (primarily oil products) in markets served by Canadian gas. This formula change signaled further significant increases in the cost of gas purchased by PGT from Canadian producers (as much as four times higher than prior to the Section 5 proceeding). The Commission found that these changed circumstances rendered PGT's existing tariff "unjust and unreasonable" and required prior Commission review of rate increases for Canadian gas before they could be passed on to consumers in the United States.

13/ See Pacific Gas Transmission Company, 24 FPC 134 (1960).

On appeal, PGT argued in part that the Commission-ordered modification of its tariff could result in delay or outright denial of its recovery of increased Canadian purchased gas costs which, in turn, would financially destroy PGT. PGT also argued that the Commission was without power to modify the cost-of-service tariff which a previous Commission had approved in 1960 when PGT was originally authorized to commence the importation of Canadian natural gas.

The Court denied all of PGT's claims and affirmed the Commission order and its action revising the tariff under Section 5(a). In support of its holding, the majority noted that the Commission had granted prompt authorization under Section 4 for Canadian gas rate increases which took effect after the disputed tariff change. The majority opinion indicated that failure of the Commission to include such increases might well be to "abdicate" its responsibilities under Section 4. However, Judge Bazelon in a dissenting opinion directed considerable criticism towards the Commission for injecting uncertainty into PGT's financial position. As the dissent stated: ". . . the FPC concedes that had PGT been required to absorb even the initial 32 cent price increase for a short period of time it would have been driven out of business, and 2,000,000 consumers would have been deprived of 40% of their gas supply." (536 F.2d at 397.)

C. Advance Payments (30 day rule): Tennessee Gas Pipeline Co., et al. v. F.E.R.C., et al., 606 F.2d 1094 (D.C. Cir. 1979), cert. denied, 447 U.S. 922 (1980); Natural Gas Pipeline Co. v. F.E.R.C., 590 F.2d 664 (7th Cir. 1979); United Gas Pipe Line Co. v. F.E.R.C., 597 F.2d 581 (5th Cir. 1979); Trunkline Gas Co. v. F.E.R.C., 608 F.2d 582 (5th Cir. 1979).

These cases involve interstate natural gas pipelines which, pursuant to a series of Commission rulemakings, including most notably Order Nos. 465 and 499, made interest-free loans (advance payments) to natural gas

producers as exploration and development investments which were to be repaid by future delivery of gas. Pursuant to these Commission Orders the pipelines were allowed to include such advances in their rate bases, for rate of return purposes, as exploration and development investments. This policy was advanced by the Commission as an incentive for the addition of gas supplies. The Commission's rulemaking orders spelled out in detail the requirements for inclusion of advance payments in Account 166. However, insofar as the "timing" of the expenditures by the producers versus the date of the pipelines investment, the Commission was silent, except to the extent the orders stated that amounts included in Account 166 could receive favorable rate base treatment where they were found to be "reasonable and appropriate." Subsequent to these Orders, pipelines invested at least $5.5 billion in "advance payments" with producers. However, after these investments had been made, the Commission, acting under FPC Order No. 465, pursuant to the "reasonable and appropriate" language, disallowed rate base treatment for certain advances because they were made to the producers and included in the pipelines' rates more than "thirty days" before they were spent by the producers. As a result large amounts of advance payments were retroactively disallowed on a deferral basis for inclusion in pipeline companies' rate bases.

On appeal to three different Circuit Courts, the pipelines claimed serious injury and voiced loud complaints that the general language of Order Nos. 465 and 499 had offered no notice of the new specific timing rule imposed by the Commission. As acknowledged by the D.C. Circuit Court, ". . . substantial sums were involved and deferral has resulted in considerable losses for the pipelines' stockholders." (606 F.2d at 1108.)

The pipelines argued that, at the invitation of the Commission rulemaking orders, pipelines were encouraged to make advance payments to promote exploration and development of natural gas reserves for the interstate market. Pursuant to those orders, the pipelines argued, they had invested substantial sums of money in the advance payment program. Thus, they argued that it was unfair and illegal for the Com-

mission, pursuant to the reasonable and appropriate standard, to establish in individual pipeline rate cases decided after the rulemaking orders had issued and after the advance payments contracts had been executed, that rate base treatment of advance payments would not be allowed more than thirty days in advance of when they were spent by the producers.

The three separate circuit courts reversed the Commission orders decided on this basis. However, the D.C. Circuit in Tennessee rejected the pipelines' claims of retroactive ratemaking and detrimental reliance and directed the Commission on remand to develop a timing relationship supported by substantial evidence. The Fifth Circuit in the United and Trunkline cases and the Seventh Circuit in the Natural case found that it was impermissible retroactive ratemaking to impose a timing requirement on Order No. 465 advances and that the pipelines had relied to their detriment on the absence of a timing requirement in the Order when they made advances to producers. Therefore, they reversed the Commission decision on the Order No. 465 advances and directed inclusion of the designated amounts in the respective pipelines' rate bases. Since Order No. 499 contained at least an ambiguously general reference to a timing relationship, those portions of the Commission decision were remanded because of a lack of substantial evidence supporting that portion of the Commission orders. Although the Commission was reversed in these cases, language from the Court's opinion in Tennessee is illustrative of the "regulatory risk" inherent to an industry subject to the Commission's jurisdiction.

> We find that petitioners' arguments in support of their interpretation (of estoppel facts) are undercut by consideration of the character of the advance payment program as an experimental departure from well accepted and understood regulatory law. (606 F.2d at 1108.)

* * *

One of the risks incurred by the pipelines has been the 'regulatory risk' that an experimental program such as advance payments might miscarry, and that administrative readjustment would not prevent substantial adverse impact. (606 F.2d at 1120.)

D. Dedication of Gas Reserves: Air Products & Chemicals, Inc. v. F.E.R.C., ___ F.2d ___ (5th Cir. 1981), Case No. 78-2011, decided July 16, 1981.

This case involves a Commission order which ended a prior Commission policy under the "Chandeleur incentive doctrine" (of approximately seven years duration) which allowed offshore natural gas producers to reserve for their own use a portion of gas reserves which otherwise would have been dedicated to the interstate market. The prior policy had allowed these reservations as an incentive to producers to expedite the exploration and development of offshore reserves of natural gas. The Commission, in its final order, found that the reservation incentive was no longer needed because, among other things, the interstate market was suffering severe curtailments and thus the gas which would be reserved by the producers was needed to serve the interstate market.

On appeal the producers argued, among other things, that they relied to their detriment on the prior FPC policy allowing reservations and that it was unfair and illegal for the Commission to reverse its policy in an adjudicated case instead of a rulemaking proceeding to be applied prospectively.

The Court remanded the case to the Commission because of the improper way in which the Commission relied on extra-record evidence to support its decision, but it rejected the producers' arguments of detrimental reliance on the prior Commission policy. The Court noted that the old Commission policy was continually attacked by consumer groups in various cases and that it was, at its inception, described by the FPC as experimental. In sum, the Court found that the policy was

never "well established" enough to have caused detrimental reliance thereon by producers or anyone else. The Court noted further that the producers were not precluded from selling the gas in interstate commerce for a fair price but rather were prohibited from reserving the gas for their own use.

E. Unsuccessful Project Costs: Tennessee, et al. v. F.E.R.C., 606 F.2d 1094 (D.C. Cir. 1979), cert. denied, 447 U.S. 922 (1980).

This proceeding involved, among other things, an attempt by Transcontinental Gas Pipe Line Corporation (Transco) to recover costs associated with four unsuccessful projects related to the production of synthetic natural gas (SNG). The Commission denied recovery of these costs because they were not "used and useful" in providing service and could not be charged to ratepayers. 14/

On appeal, Transco argued that it had spent $22 million on these ultimately unsuccessful projects in purported reliance on a Commission policy allowing recovery of the costs of the projects if they proved to be unsuccessful. The Court found that the Commission had no policy allowing recovery of these costs and then affirmed the Commission's decision.

14/ A possible concern of the lenders is that a dogmatic application of the "used and useful" maxim would result in similar treatment of the ANGTS if the project were to suspend operation after completion or, through no fault of the sponsors they were unable to commence operation after completion. The need for assurances to the contrary (the minimum bill) provides a major impetus for project financing as opposed to conventional financing.

Other cases in which the Commission is currently under criticism for assertedly changing policies to the detriment of jurisdictional companies include (i) applications for rehearing of Commission Opinion No. 90 15/ and Order No. 94, 16/ and (ii) the oil pipeline cases where revision of the ratemaking methodology formerly employed by the Interstate Commerce Commission is under consideration. 17/

However, these cases should not be taken as a suggestion that the Commission never accords finality to its orders. In Texaco, et al., Docket No. CI77-329, et al., 13 FERC ¶ 61,222 (1980), for instance, a United States Senator filed a pleading on July 21, 1980, seeking to reopen a case settled on February 10, 1978. Part of the Senator's argument was that changed circumstances justified reopening the case, but the Commission refused to grant the intervention and declined to disturb its earlier order.

Arguably, cases such as those described above represent a possible "justification" or reason why the sponsors have now sought the waiver from Congress. At the same time, however, these decisions and others of a similar nature have generated some sympathy in the courts and have begun to establish the proposition that estoppel is available as a defense against the government if the government's wrongful conduct threatens to work a serious injustice and if the public's interest would not be unduly damaged by the imposition of estoppel. Lazy FC Ranch, supra, 481 F.2d at 989. Nevertheless, because the estoppel doctrine has not been fully developed under the Natural Gas Act, it is fair to state that only a waiver would provide the lenders with the same sense of legal certainty that a firmly established "regulatory estoppel doctrine" would afford these investors. Whether this legal uncertainty "justifies" the requested waiver is a value judgment best left to Congress. With this in mind, it is appropriate to consider your questions as to hypothetical situations creating injury to project participants.

15/ 12 FERC ¶ 61,080 (1980).

16/ 12 FERC ¶ 61,080 (1980); FERC Statutes and Regulations, ¶ 30,178 (1980).

17/ Trans Alaska Pipeline System (TAPS) (Phase I), Docket Nos. OR78-1, et al.; Williams Pipe Line Company (Phase I), Docket Nos. OR79-1, et al.

10. Hypothetical Injuries to Project Participants

Our analysis has produced four general sets of hypothetical circumstances which might induce a Commission response changing the tariff provisions related to the project, absent the waiver. They are:

(1) a changed economic environment resulting in materially different costs of capital (i.e., interest rates and return on equity) from those extant at the time of initial approval;

(2) changed amounts of natural gas available to be transported resulting in a materially different economic life for the transportation system;

(3) changed economics of the gas to be delivered by the system, relative to other sources of energy supplies, warranting an altered revenue pattern in order to avoid more serious economic dislocations, and

(4) premature project failure.

As a consequence of these general events, the following hypothetical Commission actions might take place:

(a) Upon a finding of changed circumstances the Commission could determine, pursuant to Sections 5, 7 and 16 of the Natural Gas Act, that the cost-of-service tariff (which provides that Alaskan Northwest's rates will be adjusted twice a year by a formula that requires Alaskan Northwest to change its rates to reflect actual costs in its charges to shippers) was no longer appropriate. The Commission could then require Alaskan Northwest to charge a stated rate, such as a flat rate per MMBtu of natural gas transported, and require a filing pursuant to Section 4 of the Natural Gas Act to be made prior to the effectuation of any increase in that stated rate. The rate increase filing could be suspended for up to five months, and the proposed rates thereafter collected could be subject to possible reduction and refund with interest.

The risks to Alaskan Northwest in the event of a Commission-ordered change to a stated rate form of tariff involve the adverse economic impacts resulting from the regulatory lag attendant to putting into effect a proposed

rate increase under Section 4 of the Natural Gas Act. The regulatory lag consists of the sum of: (1) the time necessary to prepare a Section 4 rate filing plus (2) the one-month notice requirements between the time the filing is made and the earliest possible effective date (absent a waiver of the notice requirements) plus (3) a suspension period of up to 5 months beyond the proposed effective date. During the lag period, Alaskan Northwest sponsors would not be able to recover all of the costs previously covered by operation of the cost-of-service tariff.

As noted previously, the FPC modified in part the cost-of-service tariff of Pacific Gas Transmission Company to require Section 4 filings to recover increased Canadian purchased gas costs. However, the Court concluded that the result was justified inasmuch as the Commission had, pursuant to Section 4, allowed a "non-niggardly" flow-through by the company of increased gas costs, notwithstanding the dissent's concern that delay would have resulted in adverse consequences.

(b) Alternatively, the Commission could decide at a future time to leave the cost-of-service tariff intact but remove the minimum bill (which guarantees recovery of actual operation and maintenance expenses, actual current taxes and debt costs). 18/ The consequence of this action could

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18/ The minimum bill provides for the recovery of actual operation and maintenance expenses, actual current taxes, and all amounts necessary to service debt including interest and scheduled retirement of debt. Under no circumstances would debt service be impaired.

Recovery of equity investment and return on equity investment is, however, treated differently. The "90 percent billing adjustment ratchet" reduces charges to eliminate return on equity investment and associated taxes for any service diminution below 90 percent of tendered gas. This tariff provision would be applicable in instances when the reduction in service for any one month was greater than 10 percent. The reduction in charges to reduce the return on equity and

(Footnote 18 continued on next page)

be that during periods of interruption exceeding thirty days Alaskan Northwest would bear all of the financial consequences of the interruption because it would not be able to charge the shippers for any costs incurred during the period of interruption. 19/

(c) Another hypothetical involves a situation wherein the ANGTS project fails some time after the date construction had commenced. Assume further that upon review of

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18/ Footnote continued from prior page

associated taxes would be proportional to the percentage of volumes tendered but not transported. The pipeline would be permitted to recoup any such billing adjustments by transporting volumes in excess of the contract level in subsequent months. The charge for such "Billing Adjustment Gas" transportation would be computed by using the same billing adjustment (i.e., the same dollar per Dekatherm). Any service reduction below 100% but more than 90% would be accounted for as "No Billing Adjustment Gas." As such, this gas would be transported in subsequent months at no added charge to the shipper.

The "90 percent billing adjustment ratchet" also operates during periods of interruption of service. It ceases to be operative, however, for any period of total cessation of service for more than 30 days. Beginning with the thirty-first day of any total cessation of service, the portion of the charges attributable to "equity costs" would be collected subject to refund pending a showing by Alaskan Northwest that it should be permitted to retain equity costs collected during the period of cessation of service. Equity costs, in this context, are defined to be "that portion of depreciation expense not necessary for debt service and associated taxes." (Order No. 31, at 181-182.)

The above discussed ANGTS tariff provisions differ substantially from lower-48 pipeline tariff provisions in a number of important respects. It is fair to state that the ANGTS tariff contains unique, "first-of-a-kind", provisions which have not been previously granted by the Commission.

19/ This assumes that in eliminating the minimum bill the Commission would also eliminate the opportunity to collect equity costs subject to refund and to make a showing pursuant to the provisions described in note 18, supra.

the circumstances surrounding the project failure, a future Commission decided, pursuant to Sections 5, 7 and 16 of the Natural Gas Act, to reverse a previous decision in principle to require consumers to pay all debt costs regardless of the circumstances once final certification had been granted and debt servicing obligations had commenced. Thus, the partners of Alaskan Northwest (including sponsor-shippers) would be required to absorb all Alaskan Northwest debt costs as well as other (such as equity) Alaskan Northwest costs. Such a Commission decision would have an immediate severe financial impact on Alaskan Northwest, with the degree of severity being a function of the financial health of its partners.

(d) The Commission could decide several years in the future, pursuant to Section 5 of the Natural Gas Act, to direct the shippers of the gas to remove from their respective tariffs the rate adjustment (tracking) provisions which permit the shippers to flow through increases in transportation costs without the necessity of making a full filing under Section 4 of the Natural Gas Act (reflecting all current costs and revenues, not merely the increased costs of transportation). 20/ In these

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20/ While the Commission has decided in principle to allow the shippers to track in a timely manner amounts reflecting transportation costs paid to the ANGTS sponsors under tariffs approved by the Commission, the Commission has not yet decided what kind of tracking of these costs by the shippers would be permitted. For example, the tracking provision could require a periodic rate filing under Section 4 reflecting only the change in transportation cost, similar to the shipper's current purchased gas cost adjustment clauses. Or the provision could permit the shippers to adjust their rates automatically on a simultaneous basis to reflect changes in ANGTS transportation costs. Such a provision would be similar to fuel cost adjustment clauses permitted in rate schedules and tariffs of electric utilities for transactions which are subject to this Commission's jurisdiction.

It should also be noted that no decision has yet been made by the Commission governing pass-through by the shippers of transportation costs incurred under tariffs subject to the jurisdiction of Canadian authorities.

circumstances, the shippers could be subject to under recovery of the Alaskan Northwest transportation costs because of the same regulatory lag discussed above.

(e) If additional reserves of natural gas were found in Alaska sufficient to lengthen the economic life of the ANGTS beyond the 25-year life now inherent in the proposed depreciation rate, the Commission might at some future time reduce the depreciation rate so as to more accurately spread the recovery of the plant investment over the useful life of the project. 21/ Alaskan Northwest might oppose such a change on the ground that the resultant reduced amount of depreciation expense recovered on an annual basis would impair their ability to service debt having a shorter term.

(f) In the event of a premature end to the viability of the project after it had commenced operation (because of physical, market or other forces), the Commission might find that a faster write-off of debt was appropriate, rather than continued operation of the minimum bill provisions. This could cause financial harm to Alaskan Northwest if the debt-holder refused to allow Alaskan Northwest to accelerate repayment of its debt, particularly if the interest rate to be paid to the lenders on the debt is higher than the general level of interest rates being paid for comparable investments. Alternatively, absent a waiver, a future Commission could determine, based on either a change in policy perception or based on facts attributing fault to the sponsors for the project failure, that the sponsor-investors (as opposed to the consumers) should bear some part, or all, of the risk of loss of recovery of debt, and then appropriately adjust the tariff or minimum bill provisions.

(g) In the event that Alaskan Northwest transportation costs and the costs of Prudhoe Bay and other natural gas, increase significantly, a shipper's resale rate could be increased so as to adversely affect the marketability of a shipper's gas. Under this scenario, the shippers (particularly the non-sponsor shippers) might argue for a reduction in the Alaskan Northwest transportation charges so that the shippers could continue to market their gas. Absent a waiver the Commission would have the power to

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21/ See, Memphis, Light, Gas and Water Division v. FPC, 504 F.2d 225 (D.C. Cir. 1974).

order some sort of temporary or indefinite reduction to Alaskan Northwest's charges. In response, Alaskan Northwest, or some other party, might argue that the reduction in Alaskan Northwest's charges (regardless of the reason therefor) impaired the recovery of Alaskan Northwest's "minimum bill" costs and thus jeopardized the financial health of the project.

(h) Another hypothetical involves the pipeline-shippers' current purchased gas cost adjustment (PGA) clauses, which, as now written, would permit the shippers to pass through Alaskan purchased gas costs to their customers. If the Commission should decide to revoke or modify the PGA clauses, the shippers would be subject to regulatory lag in recovering Alaskan and possibly other purchased gas cost increases. To the extent that such a lag caused a financial strain on the shippers, it could affect the cash flow to the ANGTS.

(i) In Order No. 31, the Commission stated its intention to periodically review Alaskan Northwest's rate of return on common equity. Absent the waiver, the Commission's authority to conduct such periodic reviews would provide a basis to adjust the return on common equity downward to reflect any lowering of the cost of common equity to Alaskan Northwest. Such a lowering of common equity costs would most likely result from a general overall improvement in the economy resulting in an improvement in the financial markets, leading to a reduction in the return on equity needed by Alaskan Northwest to continue to render adequate service in the public interest. The argument that a reduction in equity return could impair collection of all debt costs in violation of the proposed waiver language would presumably be an argument by lenders and others that the interest coverage must be greater than one (i.e., 1.5, 2.0, etc.) in order to ensure that Alaskan Northwest's ability to pay debt is not impaired.

11. Hypothetical Injuries to Consumers

You have asked "what hypothetical situations there might be which would work to the injury of resale customers and consumers should the waiver be granted." At bottom the most injurious risk that could be borne by the consumer is that the project might be abandoned either before or after completion, and that the consumer, through the resale customer, would be surcharged for the investment in the project

but would not receive gas from it. Next most injurious is the risk that the consumer will have to pay for gas not received during sustained periods in which the pipeline is out of service. Arguably, for each risk which would exist to the sponsors and/or shippers in the absence of a waiver, there would exist a concommitant risk to the resale customers and/or consumers in the event a waiver is granted. However, in fairness these risks should be properly placed in the context of the facts of the proceeding and the legal status of the ANGTS project to date.

President Carter in his formal Decision, the Congress in its approval of the President's Decision and international agreements, and the Commission in its Recommendation to the President and in existing orders, have each concluded that this project is in the public interest. These approvals have led to the existing tariff, minimum bill and other provisions applicable to the ANGTS as described above. The project sponsors and lenders have nonetheless responded by seeking further assurance that the unique features of these determinations, as well as the Commission's final orders and rules, will not be altered or modified after adoption. Relevant here are the existing decisions of various authorities that the ANGTS may be project financed and that certain portions of the investment should be recoverable from consumers in events, including project interruption, where consumers do not receive the benefit of delivered gas. Thus, decisions have been made that impose risk on the consumers regardless of the waiver. Further, the Commission's ultimate orders and rules will allocate the remaining risks among the parties after consideration of all factors consistent with or affecting the public interest. Accordingly, an argument can be made that once the legal foundation for the ANGTS places the risks, the waiver would impose no substantial additional risk on the consumers, but only provide a method for assuring implementation of the federal decisions made. The extent to which a waiver would place additional onus on the consumers would include the implications of removing the "regulatory risk" from the sponsors. In other words, the consumers would then face the risk that a future Commission could not, based on changed circumstances or different policy perception, modify the ultimate ANGTS orders or rules within the parameters of their final issuance.

12. Reasonable Likelihood of These Events Occurring

From a legal standpoint, the likelihood that a future Commission would take or decline to take action of the type inquired about in your letter would appear to depend upon (a) whether a reconsideration of past policy determination occurs, and/or (b) the future existence of facts which would produce a policy response by the Commission. The likelihood of such facts occurring is a prediction or assessment that, presumably, has been made in connection with all federal determinations to date. In issuing the final orders and rules, the Commission is legally charged with the responsibility of weighing the risks, to both the sponsors and consumers, attendant to investing the sums necessary to complete the project. The risks are exceptionally difficult to quantify because of the infinite set of variables that exist, and in the end the question is one of judgment. Either the risks are too great for the consumers to be asked to bear (i.e., the project is not in the public interest), or they are not. The Commission may well be required to make that determination as part of its final certification of the project. 22/ Appropriately, the Congress must decide, through adoption or rejection of the waiver, whether to eliminate the "regulatory risk" inherent in continued Commission jurisdiction after final certification.

I am advised by the Chairman that he will support passage of a waiver designed to assure project financing of the ANGTS consistent with the positions expressed in this memorandum. 23/

22/ See President's Decision, Finance Condition No. 2, at pages 36-37.

23/ In this connection, the text of the ultimate waiver language, if any, is a matter of continuing interest to the Chairman, myself and the Office of the General Counsel. Without addressing any of the complexities involved with the final language, please be advised that we would welcome the opportunity to provide your Committee and other interested persons with any technical assistance or advice that may be requested.

Hopefully the foregoing provides you with an adequate response to your inquiry given the length of time taken and the resources available to prepare this memorandum. Please understand that this response is not intended, nor should it be taken, as an official Commission position. Rather, this memorandum represents the combined efforts of the Office of the General Counsel and other Commission staff members, as well as opinions of the Chairman and myself.

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Alaskan Northwest Natural Gas Transportation Company	)	Docket No. CP80-435

MEMORANDUM OF THE STATE OF ALASKA REGARDING RECOVERY OF MONITORING AND SOCIO-ECONOMIC EXPENDITURES AND SUBMISSION OF REVISED ESTIMATE OF SUCH COSTS

The State of Alaska ("Alaska") submits this memorandum in support of its position that certain costs of mitigating the socio-economic impacts of the Alaska Natural Gas Transportation System ("ANGTS" or "the project") in Alaska, as further described below, are properly included in the Certification Cost Estimate ("CCE") and borne by the project. As an appendix to this legal memorandum, the State is submitting a summary of its most current budgetary information describing the cost and nature of the monitoring and socio-economic impact assistance programs that the ANGTS will be asked to support.1/ The budgetary information does not include data as to highway impact costs which are still being formulated nor does it include any costs associated with the socio-economic impact of the conditioning plant which, according to Order 45, is not part of ANGTS.2/ Generally stated, Alaska's position is that the Commission has already ruled that prudent socio-economic impact costs should be included in

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1/ Alaskan Northwest Natural Gas Transportation Company ("Northwest") will formally submit this material as an amendment to its cost estimate as a substitute for the earlier information now in that application. Alaska will supply to the Commission Staff, Northwest, and the Office of the Alaskan delegate a copy of the basic budgetary data from which the impact cost figures are drawn. Should any other party on the restricted service list request a copy, Alaska will supply a copy of this data.

2/ Any costs associated with these issues will be formulated and supplied at an appropriate time.

the cost estimate and hence that they are properly borne by the ANGTS; that the recovery of such costs from the project is well supported legally, economically, and socially; and that the objection of the Commission staff to the recovery in principle of such costs is neither timely nor well-founded.

Alaska's concerns with the socio-economic impacts of the ANGTS are neither newfound nor casual. They spring directly from Alaska's traumatic experience with the construction of the TransAlaska oil pipeline. Dramatic increases in almost every category of undesirable economic and social behavior occurred. These included but were not limited to housing shortages, rampant inflation in the local cost of goods and services, an explosion in domestic problems such as divorce and child- and spouse-abuse, an increase in crime generally as well as the importation of crimes not seen before in Alaska, and destruction, at least short-term, of some of the amenities that attracted many early Alaskans to the State. The shock of this activity was amplified by its occurrence over a small period of time -- the construction years -- but, several years later, the wound has not healed completely and the scar tissue of Alaskans is tender.

That is not to say that there are not benefits to Alaskans from petroleum development. Alaska's wealth has increased and the State government has attempted to bring the benefit of this new wealth directly to its citizens although these efforts have met at least temporary obstacles.3/

3/ In 1980, Alaska enacted legislation providing for the distribution of "dividends" to Alaska residents to be paid from part of the Permanent Fund. The Fund is comprised of a percentage of the State's rentals, royalties and lease sale proceeds received from oil and gas development in the State. Although all dividends are of equal amount, the number of dividends received by each Alaska resident corresponds to the number of years he or she has been a resident since statehood. The Alaska Supreme Court upheld the dividend program in a challenge to its constitutionality on equal protection grounds. Williams v. Zobel, No. 2201 (Alaska Sup. Ct., Oct. 24, 1980). However, distribution of the dividends was stayed by the U.S. Supreme Court pending disposition of an appeal from the Alaska Supreme Court's decision. Zobel v. Williams, No. 80-1146 (U.S. Sup. Ct., Order of November 17, 1980).

Money alone is not the answer; the answer is a concentrated effort to avoid or mitigate the impact of any new major projects in Alaska.

For these reasons, when proceedings were initiated before the Federal Power Commission to consider the competing proposals for the transportation of Alaska natural gas to the Lower Forty-Eight states, Alaska did not stop with announcing its favored proposal but identified as one of its critical concerns the socio-economic impacts of any Alaska gas pipeline and asked that the costs of preventing and remedying those social ills be placed on the pipeline. Alaska said that, "unless ... they are internalized to the project, natural gas consumers in the Lower Forty-Eight states would have an undeserved bargain at the expense of the taxpayers and residents generally of Alaska." Statement of Position of the State of Alaska, El Paso Alaska, et al., docket number CP75-96 et al. at 2 (April 7, 1975).4/ This statement of concern was made quite apart from the issue of selection of a particular pipeline proposal. It is a concern that Alaska maintains to this day.

The question of the recovery of socio-economic impact costs was next raised in the Commission's Incentive Rate of Return rulemaking (RM78-12). The Upper Tanana Development Corporation proposed that socio-economic expenditures should constitute a fifth category of change in scope events. The Commission chose a different approach:

> "For the reasons discussed below, prudent expenditures of that nature should be included in the certification cost estimate at the outset, and should not be included in the change in scope mechanism." Order 31, at 125 (June 8, 1979).

The Commission staff applied for rehearing of this order on many points but nowhere in its 78 page application did it raise or even mention the Commission's determination on socio-economic costs. See generally, Application for Rehearing of the Commission Staff, Docket RM78-12 (July 24, 1979). Moreover, the Commission did not modify its determination in any regard in Orders 31-A or 31-B.

4/ In the El Paso Alaska proceeding, Alaska presented testimony on the socio-economic impact of TAPS and the projected impact of ANGTS.

For that reason, when Alaska Northwest Natural Gas Transportation Company was in the process of preparing its certification cost estimate, it approached Alaska through the State Pipeline Coordinator's Office and asked for an estimate of third party monitoring and socio-economic impact assistance costs. Since the formal State budgetary process that would generate and review such costs had not begun, Alaska's Pipeline Coordinator asked the various state agencies what their best estimate was of the socio-economic impact costs of the ANGTS. These estimates were compiled and supplied to Northwest and they were included in Northwest's application.

When these figures became a point of controversy in the informal proceedings conducted by the Office of the Federal Inspector and the Alaskan Delegate with regard to the certification cost estimate (Docket CP80-435), Alaska informed all parties that revised figures would be filed upon completion of the State budgetary process. By letter of November 24, 1980, Alaska informed all parties that it would supply revised figures no later than December 15, 1980, following the State budget process. By subsequent letter of December 14, 1980, the parties were informed that the budget process was still continuing and a new target date early in January was projected. Now the process is complete and revised numbers are available. Alaska regrets the delay but believes the additional time it spent will ultimately advance the process in which the Commission is engaged.

The revised figures, explained further below, are in 1980 dollars, $51,255,900 for surveillance, and $19,784,100 for socio-economic impact assistance in the nature of specific programs, as opposed to the creation of a general fund, for a total of $71,040,000.5/ Socio-economic impact assistance costs have been requested only for impact costs incurred directly as a result of pipeline construction workers and their families, not for the induced impact that will be caused by those attracted to Alaska but not employed by the project. These numbers do not include highway indemnification costs nor do they include such socio-economic impact assistance costs as may be associated with the construction of the conditioning plant.

The Staff position is asserted in its comments of November 7, 1980, which state that third party monitoring (surveillance) costs should remain in the cost estimate unless the statutory basis for those costs is upset by the federal or state courts. Beyond that, the Staff objects to the inclusion of socio-economic impact mitigation costs as

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5/ In actual dollars (as spent), these figures are $72,697,100 for surveillance, $28,312,700 for socio-economic impact assistance, and a total of $101,009,800.

"not required by statute and may be more properly supported by tax and royalty revenues from the project" and asks that they be deleted from the CCE. Staff Comments, Docket CP80-435, at 4 (November 7, 1981).

Northwest's position is that both monitoring and socio-economic costs should be retained in the CCE but, as to the latter, assets that they be retained in the CCE pending a determination by the FERC of their "allowability." As to both costs, Northwest agrees that the cost performance ratio should be adjusted to reflect actual costs. Report of Alaskan Northwest Natural Gas Transportation Company on Its Understanding of Agreements Reached With the Commission Staff Regarding the Certification Cost and Schedule Estimate, at 1-2 (December 22, 1980).

ARGUMENT

1. The Commission Has Already Ruled That Socio-Economic Impact Costs Should Be Included in the Certification Cost Estimate.

At the outset, Alaska does not believe that, in principle, the propriety of inclusion of socio-economic costs in the cost estimate is unresolved. Order 31 is quite definite in directing that prudent costs of this nature be included in the cost estimate. Order 31 at 125. A fortiori, this is a determination that in principle such costs are properly assignable to the project. Alaska recognizes that a determination whether particular categories of socio-economic expenditures are prudent requires further rulings but the principle of recovery of certain of these costs from the project has been decided. That order is final, both as to rehearing and as to judicial review. The Commission staff had its opportunity to seek rehearing on this point but did not do so. Thus, the principal issue raised by Staff -- whether such costs should be part of the CCE -- is decided and the Staff's arguments should not be heard now except perhaps insofar as they relate to the recovery of particular costs rather than to the permissibility of including any costs of this nature. Further, the appropriate time to address the prudency of such costs would not appear to be this proceeding since determinations of prudency generally are made after, not before, expenditures of funds by a natural gas company. Nonetheless, given the special nature of this proceeding, Alaska will endeavor to address this issue now.

2. That Alaska Will Suffer Adverse Socio-Economic Impact Is Indisputable.

There is and can be no dispute that Alaska will suffer substantial socio-economic impact from construction

of the ANGTS. Construction will last only a few years but it will attract to Alaska not only thousands of construction workers and their families but many others seeking work in peripheral activities related to the project or opportunities in Alaska they may never realize. According to the budget information developed by the State government, more than 35,000 job seekers will come to Alaska in hopes of finding project related employment. As many as 13,171 workers are expected to be employed directly on construction. Yet Alaska's entire population is only 400,481. (1980 census, Preliminary Count). Much of its population is located in the Anchorage SMSA (173,992, 1980 Census, Preliminary Count). But the communities that will experience the most impact are much smaller and nearer the pipeline corridor. For these, the effect of a sudden increase in activity and population from the pipeline can be a severe and immediate shock. Moreover, the level of services necessary to accommodate the impact is not generally that which state and local government are typically called upon to provide, for it is necessary for the few years of the construction period only. It makes no sense for Alaska governments to expand staff and construct permanent facilities for an impact of but a few years duration.

Population increases, housing shortages, local economic changes and sudden and heavy demands on limited public services as a result of increased crime, alcoholism and family problems are all expected as a result of construction of the Alaskan Natural Gas Transportation System. These effects were addressed in the environmental impact statements for ANGTS and more recent studies by the State continue to document their occurrence. No party, not even Staff, disputes that these effects will occur and that they will occur as a result of construction of the ANGTS. Thus, the basic question is of responsibility for mitigating the acknowledged impact.

3. Reimbursement of Socio-Economic Impact Costs Is Prudently Undertaken By The ANGTS

The duty to identify and mitigate socio-economic impact, and to expend funds to that end, is no different in principle then the now well accepted responsibility to identify and mitigate harm to the physical environment. 18 C.F.R. Sections 2.69, 2.80, 2.82. This duty arises not only from the National Environment Policy Act (NEPA) but from the public interest standard itself. No one today would suggest that any major project licensed by the Commission could leave impact to the physical environment unredressed by saying it belonged to the landowners and governments at the site of the project. Injury to the social environment, while less

tangible, also properly comes within the duty to mitigate harm to the "environment."6/

That there is an obligation by Commission licensees to address socio-economic impact7/ is recognized in Commission precedent. In Virginia Electric and Power Company (VEPCO), the presiding Administrative Law Judge referred to the requirements of NEPA as "[carrying] with . . . [them] a duty to take reasonable steps within the agency's jurisdiction to ensure that adverse impacts [on the social environment] are mitigated as far as possible." See Limited Decision Issuing License for the Bath County Pumped Storage Project, issued September 20, 1976, Project No. 2716, at p. 48, approved and adopted by the Commission, Opinion 785, January 10, 1977. At issue was whether an applicant for a license to construct power-generation facilities could be required by the Federal Power Commission to bear certain costs associated with the socio-economic impacts anticipated from a large influx of construction-related people. The Administrative Law Judge was persuaded that the applicant should bear some of those costs and that it was the obligation of the Commission to ensure that such impacts were properly mitigated. The Administrative Law Judge ruled that:

> the license should be conditioned to require the licensee to extend financial assistance to Highland County to mitigate the impact upon the County's fisc resulting from the influx of project workers, their families and others who accompany them . . . during the period of project construction. The assistance is necessary in the following areas of additional costs, to the extent they are not covered by increased tax revenues and fees attributable to the presence of project workers or increased financial assistance from other levels of government: (1) education; (2) law enforcement; (3) solid waste disposal; (4) general

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6/ The nature of socio-economic impact from a particular project will vary according to its size, nature, and location. Nonetheless, Alaska knows, based upon its TAPS experience, that such impact can be identified and predicted, especially in as unique a social environment as Alaska.

7/ NEPA is not limited to concern with the physical environment. Hanley v. Mitchell, 460 F.2d 640, 647 (2d Cir.), cert. denied, 409 U.S. 990 (1972). Accord, Chelsea Neighborhood Associations v. U.S. Postal Service, 516 F.2d 378, 388 (2d Cir. 1975); Monarch Chemical Works, Inc. v. Exon, 466 F.Supp. 639, 655-56 (D.Neb. 1979).

government costs; and (5) welfare and other social services. VEPCO Limited Decision, at 56.

This decision does not stand alone. See, e.g., Appalachian Power Company, Opinion and Order of the Commission Granting a License for the Construction of the Blue Ridge Project, issued June 14, 1974, Project No. 2317 (mitigation measures required in the form of financial assistance for moving expenses, personal property losses, and increased mortgage interest costs); Pacific Alaska LNG Company, et al., initial decision, issued August 13, 1979, Docket No. CP75-140 (applicant required to establish experimental bus program and identify and protect cultural values of native Americans). In fact some of the costs that are recognized by the Commission's rules and regulations as standard pipeline cost items are properly characterized as socio-economic impact costs.8/

Thus, Commission precedent recognizes a duty to address socio-economic impact although the particular means that the applicant must select naturally varies according to the circumstances.

The effect of this duty is to ensure that socio-economic costs are "internalized" to a major energy project such as the ANGTS. The "costs" of a major energy project are not limited to impact upon the physical environment alone and mitigation costs also should not be so limited. The "internalization" of social costs is comparable to, and makes just as much sense as, the inclusion of the costs of environmental mitigation, which the President has identified as part of the cost of pipeline construction. See as to environmental costs, President's Decision, at pp. 33-36; 18 C.F.R. Section 2.69, 18 C.F.R. Section 2.80; 18 C.F.R. Section 2.82.

On economic policy grounds, socio-economic costs are also properly a responsibility of the project. Recent Congressional enactments requiring the conservation and efficient use of our natural resources establish that the price of energy resources provided to the public actually

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8/ See, e.g., The Instructions for Carrier Property Accounts, "3-3, Cost of Property Constructed" include as costs: (6) protection, including "amounts paid to municipal corporations for fire protection ... and analogous items;" (8) privileges and permits, including "compensation for ... use of private or public property or of streets, in connection with construction work;" (10) rent, "including quarters used for construction work;" and (5) cost of contract work performed by others.

should reflect the full cost of their production and transportation, including social and environmental costs. See, e.g., National Energy Conservation Policy Act, Title I, Section 102, 42 U.S.C. Section 8201; Powerplant and Industrial Fuel Use Act of 1978, Title I, Section 102, 42 U.S.C. Section 8301; Public Utility Regulatory Policies Act of 1978, Section 2, 16 U.S.C. Section 2601. Unless these costs are included in the price to the consumer, the result will be an artificially low price which does not reflect actual costs or conform to national policy. Stated more succinctly, "if external social costs are not somehow incorporated in the costs of production, demand may be distorted by reason of incorrect price signals reflecting only internalized costs." Energy Law Service, M5A.74 (Callahan & Co. 1979). Thus, the price to consumers should reflect a true cost of producing a depleting resource. Artificially reducing the price by excluding these costs tends to distort the price signal consumers receive. Conservation and efficient use of our natural resources require that all costs, including the cost of mitigating socio-economic impacts, be included in the "rate base" for the computation of the pipeline tariffs. Only in this manner will the true cost of an energy resource be spread among its recipients.

These policy considerations support the Commission's determination in Order 31 that prudent socio-economic costs be included in the certification cost estimate. Having made that determination, the question pending in this proceeding is the appropriateness of the particular programs as a means of addressing the socio-economic impact of ANGTS. And it is to that question we now turn.

4. The Costs Alaska Has Described Are A Reasonable Response to ANGTS' Duty To Mitigate Socio-Economic Impact

Once the duty to address socio-economic impact is acknowledged, a question of prudency may still arise as to the particular expenditures that are proposed. The programs must be reasonably related to the objective of mitigating impact and likely to achieve that goal. Also relevant may be the scope of the programs --are they focused on project impact or are they aimed at the population at large? Scrutiny of Alaska's programs demonstrates that they meet these tests.

Funds requested are limited to those necessary to address solely impact associated with construction workers and their families, not that from the far larger population attracted to Alaska because of real or perceived opportunities on the pipeline. Stated another way, the State seeks funds only to cover those socio-economic costs directly related to providing natural gas to the Lower Forty-Eight.

The nearly twenty million dollars9/ that ANGTS will bear is for programs to be administered by the Departments of Natural Resources, Public Safety, Health and Social Services, and Labor.

Approximately 30% of these funds will be expended by the Department of Natural Resources. It will establish Impact Information Centers and a Citizen's Socio-Economic Advisory Council as a means of informing citizens along the pipeline corridor of the expected impacts and to assist communities and citizens in meeting those impacts as well as providing a channel for Northwest, State, and local officials to work together on meeting the common problem of socio-economic impact. These activities are aimed at preventing sudden shocks from pipeline construction by providing those most likely to be affected with adequate advance information and guidance so that they can anticipate and perhaps avoid the worst part of negative socio-economic impact. These centers are regarded by the State as a direct response to avoiding the surprises of the Alyeska experience and it is believed that they will be effective in implementing ANGTS's duty to mitigate adverse socio-economic impact.

The programs of the Department of Labor to address socio-economic impact are directed to the more than 13,000 workers who will be employed directly on the pipeline in the peak period. It is estimated by the Department of Labor that more than 35,000 job seekers will come to Alaska in search of employment on the project. Department of Labor impact assistance funds will be spent for safety inspections, to enforce occupational and health regulations, to process and, as necessary, adjudicate employment compensation claims for work-related injuries, and for retraining workers injured on the gas line. The balance of the Department of Labor funds will be used to handle administrative services for pipeline-related applications such as unemployment claims.

Department of Public Safety funds would be expended on additional personnel and equipment necessary to enforce vehicle size and weight laws and to license the additional vehicles of workers coming into the State as a result of the pipeline construction. This increased activity will directly benefit ANGTS because it will promote the free flow of truck traffic essential to pipeline construction.

9/ Since there has been no significant controversy regarding reimbursement for permitting, monitoring and surveillance programs, this memorandum focuses on the socio-economic programs question principally. The twenty million dollars is for socio-economic mitigation only, not monitoring, as is made clear above.

The Department of Health and Social Services would expend its impact assistance funds for health services, such as inspection of x-ray equipment, monitoring for communicable diseases in pipeline camps and emergency medical services along the pipeline corridor, and for alcoholism and drug abuse programs along the pipeline corridor. Funds will also be expended for social services. The Department estimates that the influx of pipeline workers and their families will give rise to 500 additional cases of child abuse and child neglect. It expects related needs for foster care (29,200 days per year) and institutional care (7,300 days per year), all for pipeline workers and their families. Finally, a small pipeline liaison office will be created to assist in the administration of these programs.

It bears emphasis that the funds sought are but a small fraction of the socio-economic impact costs identified in the State budget process10/ and likewise much less than the impact in quantifiable terms that the State expects from construction of the Alaska Natural Gas Transportation System. Alaska is prepared to absorb the cost of the more general, "Type II", impacts.

What this means is that there will be a sharing of the burden of socio-economic impact between ANGTS and the responsible governments in Alaska. Such a sharing is not only consistent with the principles established by VEPCO, supra, but is also a recognition that the problem is mutual. The actual division of expenditures between the project and the Alaska government, while soundly based in this case, is less important than the assumption by the project of at least some of the impact it is causing. It is fitting that the impact most directly caused by, and identified with, the project -- that of the pipeline construction workers and their families -- is the share of the burden that ANGTS is asked to assume.

Also, none of these dollars will go toward the creation of a special fund or funds to be distributed as grants to Alaska citizens as general "compensation" for project-caused disruption. Instead, specific programs have been designed, consistent with the mandate of NEPA and the Commission's responsibility to serve the public interest, to mitigate or avoid adverse socio-economic impact.

10/ The Type I impact funds described herein are about 20% of the total impact funds needed to respond to total pipeline impact, according to State agencies.

5. Payment Of These Funds Would Not Trigger The U.S. - Canadian Agreement On Principles

The specific programs for impact caused by construction workers and their families, described above, are quite different in nature than the general fund or funds which the U.S. - Canadian Agreement on Principles is intended to guard against.11/ That agreement limits inclusion in the cost of service to U.S. shippers of indirect socio-economic costs for the Yukon Territory and bars public authorities from requiring a special fund or funds in connection with the construction of the pipeline in the Yukon. The exception to that agreement is what may be thought to raise a question. It states: "should public authorities in the State of Alaska require creation of a special fund or funds, financed by contributions not fully reimbursable, in connection with construction of the pipeline in Alaska, the Governments of Canada or the Yukon Territory will have the right to take similar action." President's Decision at 56-57.

The question is the meaning of a "special fund" as used in the Agreement on Principles."12/ The meaning of the limitation on "special funds" is best understood by reference to the Canadian proposals -- pre-dating the Agreement on Principles -- for the creation of special funds to be borne by the pipeline and passed on to United States consumers to mitigate Canadian socio-economic impact. Specifically, Dean Kenneth M. Lysyk had conducted an inquiry into the social and economic impact of a gas pipeline through the southern Yukon at the direction of the Canadian Government. Dean Lysyk filed the report of his board on July 29, 1977. The report, which followed the decision of the Canadian National Energy Board, specifically recommended that $200 million be paid by the pipeline to capitalize a Yukon Heritage Fund to be administered by and for Yukoners. The $200 million was to meet "unquantifiable socio- and economic costs and for changes following in the wake of the pipeline that would detract from the quality of life in the Yukon." The fund was not directed at mitigating pipeline related projects nor "as a response to any specific impact, but to improve aspects

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11/ "Agreement between the United States of America and Canada on Principles Applicable to a Northern Natural Gas Pipeline," see President's Decision at 47-66.

12/ The term "fully reimbursable" is also ambiguous because it conceivably could refer to reimbursement from the cost of service.

of the quality of life in the Yukon." Lysyk Report, 149.13/ The fund was in addition to "regulatory measures and responsive government programs" directed at minimizing the negative impacts of the project. Id.

Thus, prior to the negotiations with Canada, United States gas consumers appeared to be facing the prospect of supporting new general purpose funds in the Yukon which would be in the nature of a bonus payment to Yukon residents for the disruption caused to their life by the pipeline. Thus, the subsequent provisions of the agreement between the United States and Canada limiting special funds can fairly be read as aimed at preventing the sort of general fund proposed by the Lysyk inquiry unless the State of Alaska should require such a fund to be established.

As is demonstrated by the specific socio-economic costs which have been described above, Alaska is not seeking such a general purpose fund. It is seeking to recover in a limited way some, but by no means all, of the costs of the expanded State services necessary to accommodate construction workers and their families during the period of construction of the ANGTS. As such, Alaska's proposals do not fall within the literal language or intent of Section 5(b)(ix) of the Agreement on Principles.14/

6. The Staff Position Is Not Well-Founded

Despite the clear and unequivocal order of the Commission that "socio-economic expenditures" be included in the Certification Cost Estimate, the trial staff has commented that the socio-economic costs described by the State are not

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13/ The earlier decision of the NEB had also recommended a $200 million fund, exclusive of the costs of the monitoring authority, to encompass identifiable indirect socio- and economic costs of the pipeline project north of the 60th parallel. NEB, Reasons For Decision, 1-147-48. Although the details were vague, this fund appeared to be somewhat more closely related to specific impact assistance needs.

14/ Annex IV of the Agreement contains examples of direct charges by public authorities that are permissible within the meaning of Paragraph 11 of the Agreement, a related provision. These include "other items specified in environmental stipulations." The socio-economic assistance programs to be funded by the pipeline will be required by the environmental stipulations attached to the right-of-way lease of the State of Alaska and so may be considered direct rather than prohibited indirect charges.

required by statute and "may be more properly supported with tax and royalty revenues from the project." Staff Comments, Docket CP80-435, at 4 (November 7, 1981). In fairness to the Staff, Alaska notes that these comments were made with respect to the early estimates of the State and incorporated by Northwest in its application. The Staff may well reconsider its position in light of the revised information and authority contained in this memorandum. The Staff should reconsider it position for the following reasons.

First, the Staff has not responded to the direct command of Order 31 that socio-economic costs be included in the cost estimate. That Order is a sufficient answer to the Staff's request that such costs not be included in the CCE.

Second, the reliance upon a statutory requirement vel non is misplaced. An expenditure can be prudently incurred regardless of whether a statute requires its payment. An example would be expenditures to mitigate damage to the physical environment such as those for revegetation. No one would assert a statutory requirement as a test for the prudency of such expenditures. Alaska has, on repeated occasions, indicated to Northwest that the ANGTS will be required to assume a share of socio-economic impact costs. If nowhere else, these expenditures could be required as part of the right-of-way leasing process. Alaska could enact legislation directed to this subject but it is plainly not necessary to do so.15/

Third, staff does not give fair recognition to the fact that Alaska, its citizens, and its subordinate governments will bear a large share of the socio-economic impact costs of this project and are seeking from the project only a small share of the total impact caused by the project. Thus, some Alaska tax revenues inevitably will be devoted to ameliorating the impact caused by ANGTS despite the Northwest contribution. The question is whether ANGTS should stand a share of impact costs.

Further, Staff's suggestion that royalty revenues should support these costs is misdirected. Royalties are paid for the privilege of occupying or exploiting the property of the State. Magruder v. Supplee, 316 U.S. 394 (1942). The royalties to be paid by the producers constitute consideration to the State as the landowner of mineral rich property. To require the State to expend its royalty revenues for the mitigation of socio-economic impacts is to take from the State the only

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15/ If the issue were presented to the Alaska legislature, it is quite likely, although not certain, that ANGTS would be required to bear a far greater share of the impact it causes.

compensation it is to receive for allowing the exploitation of its natural resources. Mitigation of such impact is not the purpose of royalties generally nor is it consistent with the purposes for which those lands were given to Alaska.

A major purpose of the Statehood Act was to enable Alaska "to achieve full equality with existing States, not only in a technical juridical sense, but in practical economic terms as well." H.R. Rep. No. 624, 85th Cong., 1st Sess. 2 (1957). One of the ways this was to be achieved was by "making the new State master in fact of most of the natural resources within its boundaries." Id. at 2. It was expected that Statehood would

> the economy of the Territory than would be possible under territorial status. Many witnesses have testified to the Committee regarding the wealth of untapped resources in Alaska." (Id. at 10).

The Senate shared the purposes expressed in the quotations above from the House Report. Alaska was to be admitted into the Union "as a full and equal sovereign State." The lands and resources transferred from Federal to state ownership were intended "to permit the new State to earn its continuing economic independence and growth." Sen. Rep. No. 1163, 85th Cong. 1st Sess. 1 (1957). A national interest in Alaska's self-sufficiency is thus well established. And the dedication of vast national resources to Alaska was implicitly a commitment to Alaskan economic self-determination: Alaskans would be allowed to decide how best to use those resources for their own healthy growth in the manner that they saw fit.16/

16/ The policy encapsulated in Section 13(b) of the Alaska Natural Gas Transportation Act of 1976, P.L. 94-586, is but another expression of the national interest in Alaskan self-sufficiency and economic self-determination. Section 13(b) is a Congressional recognition of Alaska's proper entitlement to use its gas for its own purposes. Congressman Young of Alaska explained the rationale for including this provision in the Act:

> "Use of Alaska's royalty gas within Alaska may help end Alaska's status as a ward of the Federal government. The national interest in the self-sufficiency of Alaska was expressed in the Alaska Statehood Act as well as in other declarations of national policy. Under that Act, Alaska was permitted to select large quantities of land from the Federal domain with the hope that the land so selected -- and the minerals which it contained -- would provide a basis for building a healthy economic order in Alaska." Cong. Rec. E5808 (October 26, 1976).

It cannot be said that dedicating Alaska's royalty or even severance tax revenues to alleviating short term impact from this national project is consistent with the purposes of the severance and royalty taxes or the grant of ownership of public lands to the State of Alaska. For these revenues would be expended upon a social service infrastructure, which would have outlived its usefulness upon the completion of the project. They would not contribute to Alaska's self-sufficiency nor return a long range benefit to its citizens.

That is not to say Alaska and subordinate governments will not receive tax revenues from the ANGTS. Tax revenues probably will be generated although their amount and nature are uncertain because of pending litigation involving the corporate income tax and the possibility of changes in Alaska's tax regime generally.17/ But, revenues from such taxes as then may exist will help meet the cost of impact from the ANGTS that it is not being asked to fund and the unfunded amount is, according to today's best estimates, far larger than what the ANGTS is asked to bear. See p. 11, n. 10 supra. Thus, Alaska's government and citizens will bear a large share of the impact this project will create. But, Alaska's extraction taxes and revenues properly should not be diverted to this purpose and a share of the direct socio-economic impact costs of the ANGTS is properly borne by it.

CONCLUSION

For the foregoing reasons, the ANGTS properly should bear a share of the burden of mitigating the adverse socio-economic impact it will cause, inclusion of the State's

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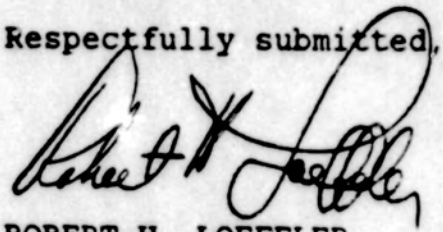
17/ State severance taxes are also being challenged in a case pending before the U.S. Supreme Court.

revised estimate of such costs in the Certification Cost Estimate is procedurally correct, and the costs of the programs therein described are prudently incurred.

Respectfully submitted,



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February 13, 1981.

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REA-81-1026
February 13, 1981

Mr. John Adger
Alaskan Delegate
Federal Energy Regulatory Commission
Room 3004
941 North Capitol Street, N.E.
Washington, D.C. 20426

RE: Docket No. CP80-435, Alyeska Pump Station Camp Number 1

Dear Mr. Adger:

On November 6, 1980, the Federal Energy Regulatory Commission's Staff propounded the following interrogatory (No. 25):

> "Does Applicant intend to remove the $1.548 million entry from the CCSE as filed now that it no longer intends to purchase Pump Station No. 1?"

This interrogatory was raised primarily as a result of discussion between Northwest Alaskan Pipeline Company (Northwest Alaskan) and the Staff, at the October 22, 1980 Certification Cost Estimate technical conference (see transcript summaries at pp. 12, 13, and 18), in the above-referenced docket. Northwest Alaskan indicated at such conference that the Alyeska Pump Station Camp No. 1 had been sold to others and was not going to be acquired by Alaskan Northwest Natural Gas Transportation Company (Alaskan Northwest).

By this letter Northwest Alaskan is informing the Alaskan Delegate, Staff and the parties to the instant proceeding that Alyeska Pump Station Camp No. 1 has not been sold to others. Such camp is physically in the Pump Station Camp inventory and included in the agreement 1/ that is near consummation between Alaskan Northwest and Alyeska for the acquisition of nine (9) Pump Station Camps and sixteen (16) Pipeline Camps.

1/ This agreement is for the acquisition of Alyeska camps only. Alaskan Northwest is still in the process of negotiating for the acquisition of certain Alyeska Data. Upon the execution of that agreement, Alaskan Northwest will be presenting the agreement with attendant costs to the Office of the Federal Inspector for his review and approval as a design change. It is respectfully requested that the Alaskan Delegate's report recognize this likelihood.

Previous discussions during the technical conferences wherein it was indicated that Pump Station Camp No. 1 was not going to be purchased by Alaskan Northwest are incorrect. Therefore, the $1.5 million ($900,000 in 1980 dollars) cost should appropriately remain in the CCE.

As established during the technical conferences, Alaskan Northwest will require all of the acquired Alyeska camps in order to assure that adequate bed space is available for overall camp requirements, including any loss or damage that might be incurred during the relocation and renovation of such camps.

If there are any questions relative to this matter, please contact me.

Very truly yours,

NORTHWEST ALASKAN PIPELINE COMPANY

Cuba Wadlington, Jr.
Director, Regulatory Affairs

cc: Richard Berman, Division Director/OFI
Restricted Service List, Docket No. CP80-435

CW:paw

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Alaskan Northwest Natural Gas)
Transportation Company) Docket Nos. CP78-123, et al.

RESPONSE OF
COLUMBIA GAS TRANSMISSION CORPORATION
TO ORDER TO SHOW CAUSE

Columbia Gas Transmission Corporation (Columbia), pursuant to the Commission's order to show cause, issued December 15, 1980, in the above-captioned proceedings, hereby responds to such order, to urge that the Commission approve Columbia's pre-partnership expenditures made through its membership and participation in the Gas Arctic/Northwest Project Study Group (Gas Arctic) for reflection in the capital account of its affiliate, Columbia Alaskan Gas Transmission Corporation (Columbia Alaskan) and inclusion in the rate base of Alaskan Northwest Natural Gas Transportation Company (Alaskan Northwest). In support hereof, Columbia respectfully states as follows:

Columbia is an interstate pipeline making sales of gas to some 71 customers for resale in the States of Kentucky, Maryland, New Jersey, New York, Ohio, Pennsylvania, Virginia, West Virginia and in the District of Columbia. As noted in Exhibit No. 3 to the First Audit Report of the Office of the Chief Accountant, attached to this Show Cause Order, Columbia was a participant and sponsor of the Gas Arctic project which applied to the Commission and to the National Energy Board of Canada for certificates to construct a pipeline to transport Alaskan gas to the United States. Columbia's contributions to Gas Arctic amounted to $8,004,329.

In Columbia Gas Transmission Corp., Opinion No. 101, Docket No. RP78-20, issued November 6, 1980, the Commission found that Columbia was not entitled to recover in its own rates approximately $6,000,000 which Columbia contributed to Gas Arctic for expenditures subsequent to Gas Arctic's filing for a certificate with the Commission. However, the Commission held that:

> "The decision herein is without prejudice to Columbia's status as a successful participant in the Alaska [sic] Northwest Natural Gas Transportation Company, the successor in interest to Alcan. The same expenses may be recovered where it can be demonstrated that they contribute to the project and are, therefore, analogous to successful project costs." (p. 10)

By order issued in these proceedings on December 15, 1980, the Commission approved amendments to the partnership agreement which permitted Columbia Alaskan to join the Alaskan Northwest partnership. Therefore, Columbia has become a successful participant in the Alaskan Northwest project.

Alaskan Northwest is filing today a Fourth Supplemental Application to its Application of February 2, 1979 (Exhibit No. 4 to the First Audit Report) seeking, inter alia, Commission approval, for inclusion in rate base, of qualified expenditures made by Columbia in Gas Arctic. If approved, these qualified expenditures will become part of Columbia Alaskan's equity contribution into the Alaskan Northwest partnership.

By this response, Columbia seeks an expansion of the Commission's Show Cause Order to cover the expenditures made by Columbia in Gas Arctic. Further, the Commission's ultimate determination of this Show Cause proceeding must permit Columbia's Gas Arctic expenditures to be included in the Alaskan Northwest rate base to the same extent as the expenditures made by other former Gas Arctic participants who are now partners in the Alaskan Northwest project.

In order to avoid undue repetition and duplication, Columbia adopts and supports the response submitted herein by Alaskan Northwest insofar as it demonstrates that all of the Gas Arctic expenditures made by the Alaskan Northwest partners should be reflected in the capital accounts of these partners and included in Alaskan Northwest's rate base.

WHEREFORE, for the foregoing reasons, Columbia submits that the Commission should expand this Show Cause proceeding to cover Columbia's Gas Arctic expenditures, and approve

the inclusion of all such expenditures in Alaskan Northwest's rate base.

Respectfully submitted,

COLUMBIA GAS TRANSMISSION CORPORATION

By /s/ Stephen J. Small
Stephen J. Small
Its Attorney

Post Office Box 1273
Charleston, West Virginia 25325

OF COUNSEL:

John M. Hill
Giles D. H. Snyder

Post Office Box 1273
Charleston, WV 25325

February 13, 1981

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the Restricted Service List compiled in this proceeding in accordance with the requirements of Section 1.17 of the Rules of Practice and Procedure.

Dated at Charleston, West Virginia, this 13th day of February, 1981.

/s/ Stephen J. Small

Stephen J. Small

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Alaskan Northwest Natural Gas Transportation Company	Docket No. CP80-435

COMMENTS OF THE COMMISSION STAFF

At the unrecorded prehearing conference of September 3 and 4, 1980, the presiding officer directed the applicants and requested any other interested party and the staff to submit comments on two issues related to the subproceeding established in the Commission Order of August 1, 1980. The two related issues concern identifying outstanding major design issues not resolved in the July 1, 1980, filing or subsequent to it, and whether or to what extent the Incentive Rate of Return (IROR) mechanism may be altered to allow the proceeding to progress under a situation not contemplated by Commission Orders creating the IROR. 1/ Pursuant to the request, the staff respectively submits the following comments.

The staff will first address the issue of the IROR mechanism and will be prepared to expand its comments at the conference to be held on October 7, 1980, to discuss IROR issues. Part two of these comments is comprised of a list of those major design issues which the staff believes have not, as yet, been resolved and should at this time be discussed.

I.

The staff believes a general recitation of how the mechanism, as ordered, would operate concerning the determination of the Certification Cost and Schedule Estimates (CCS) and Center Point (CP) values, is appropriate prior to detailing the options the staff believes may be available, should the Commission determine a need exists to amend the IROR mechanism.

A) The staff believes that a five step procedure was contemplated with regard to the CCSE and CP.

Step one would be the determination of final design criteria and parameters submitted by the applicants. These criteria

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1/ Order No. 17 issued December 1, 1978; Order No. 17A issued January 17, 1979; Order No. 31 issued June 8, 1979; Order No. 31B issued September 6, 1979; in Docket No. RM78-12.

would address normal and probable events as well as reasonably expected abnormal events. 2/

Following a fairly firm design being set, a Certification Cost Estimate is prepared. 3/ In this regard, the Commission has stated that "it is vital that the Commission have the most accurate and realistic set of cost estimates that can be obtained." (Order No. 31, mimeo at 46).

After the CCE is established, the Center Point should be determined based on the best current estimate of the actual costs of the project including overruns relative to the CCE. (Order No. 31, mimeo at 41). The determination of the CCE and CP should take place simultaneously at a point which appears to have been intended to be the time of final Commission certification.

Following certification, the Office of the Federal Inspector is to oversee the development of final design and construction plans. 4/ It is the staff's understanding that what is to be determined by OFI is the final engineering and construction plan based on the detailed criteria certificated by the Commission. Should design changes during construction be suggested, the Federal Inspector can increase the base CCE for the cost of such design change without impacting the Center Point. 5/ The changes to be treated in such a manner must be related to design changes and not involve matters such as increases in the prices of labor, material, or services not directly tied to an approved design change. (Order #31, Ordering Paragraph 9, mimeo at 244)

Any change to the final design submitted subsequent to approval of said design by the Federal Inspector, will not be added to the base CCE for rate of return purposes and will affect the Center Point determination unless it is approved subject to the Change in Scope mechanism. 6/ Such changes in scope would be generally applicable to changes caused by war, natural disaster, design changes ordered by state or Federal legislation or regulation, major routing changes ordered by state or Federal governments, and delay in

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2/ See Order No. 31, mimeo at 46, and Order No. 31B mimeo at 5.

3/ See Order No. 31, Ordering Paragraph 7, mimeo at 243.

4/ Reorganization Plan No. 1 of 1979.

5/ Order No. 31, mimeo at 123, 124.

6/ Order No. 31, Ordering Paragraph 10, mimeo at 245, 246.

the issuance of government permits or certificates. (Order No. 31, mimeo at 120 to 121, and Order No. 31B, mimeo at 32 to 40). This mechanism is to protect the applicants from reduction in their rates due to events beyond their control.

B) As requested, the direction of these comments is to address, in part, the issue of the treatment of major design changes under the IROR. 7/ Such a discussion would be unnecessary if the filing of July 1, 1980, with which we now concern ourselves, had not been deficient and had conformed to the terms of the Commission's orders regarding the CCE, Center Point, and Incentive Rate of Return mechanism in general.

The staff believes, as the Commission has stated, that the IROR provides for "truly generous rates of return", and that special attention and expedited regulatory and administrative arrangements have been provided for this proceeding. (Order No. 31, mimeo at 20).

The IROR Orders provide for a final design with its costs, schedule, and risks being determined, prior to the issuance of a final Commission certificate. Risks and costs associated with truly abnormal occurences are to be covered by the Center Point. However, the application, for which this subproceeding was created, does not provide a complete initial design. It does not provide a basis for determining normal occurences, much less abnormal events. It has a minimum of fourteen (14) major design issues outstanding (See Part II, infra), some of which will not be addressed for some weeks. The filing also does not contain an accurate route corridor. Thus despite the sponsor's views as stated in their submission of September 29, 1980, to the contrary, the filing really isn't a valid basis for study at this time.

The IROR mechanism calls for a CCE and CP based on the best current estimate of the actual costs of the project including overruns relative to the CCE. The Commission felt that the CCE that would be filed would include "detailed planning and design that would resolve most of the inadequacies of the 1977 filed da (Order No. 31, mimeo at 41 to 46)

While the staff strongly opposed certain elements of the IROR mechanism, it believes that there is a required and logical nexus between the relevant parts. The staff believes that the IROR mechanism should not be altered due to failings in the application. The staff believes that while the Commission states 8/ that it does not know how to deal with the question of outstanding design issues at the time of approval of the CCE and CP, the orders creating the CCE, CP, and IROR, declare that there are to be no major outstanding

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7/ Notice of Technical Conference, issued September 23, 1980, in Docket No. CP80-435.

8/ Order of August 1, 1980, mimeo at 10.

design issues at that time. Therefore, the easy and correct answer is that the Commission should not attempt to set the CCE and CP until those major design issues are resolved and a generally accurate cost estimate and risk assessment can be developed.

(C) Should the Commission wish to consider setting a Certification Cost Estimate and Center Point based on such a paucity of necessary information as now exists, the staff believes that few reasonable options are available.

An example of one possibility previously offered, in part, to the Commission, is an analysis of the entire distribution of probable costs and potential overruns to establish a center point and a subsequent incentive rate of return. 9/

The use of several estimates or a probability analysis has severe pitfalls and has not, in the past, been deemed feasible. Under this theory, a series of hypothetical situations could be determined which would allow a center point to be developed based upon which situation which eventually occurs. The hypotheticals could contain minimum, maximum, and median cost estimates analyses based on the conservatism or liberalism of what is included in the various estimates. 10/

If a work breakdown structure (WBS) is used, each of several hundred cost elements would have to be supplied with a distribution for each. Each element could involve simple division or a complex mathematical formula to determine the various center points. This could result in the applicants having to prove the validity of three or more cost estimates and center points.

Should probability distributions or multiple estimates and Center Points be utilized, it could also increase the problem of potential abuse of the mechanism to maximize the outcome. 11/ The Commission has already expressed its concern over this possibility under the existing IROR mechanism. 12/

9/ James D. McCullough, Institute for Defense Analysis Study, Order 31, mimeo at 9, fn. 11.

10/ In this regard, it is important to note the Commission's inclination to avoid contingency and rely on inclusion of such risk in the center point. Order 31B, mimeo at 6, 7.

11/ McCullough Study, supra, fn. 9, mimeo at S-12 to S-13.

12/ See Order of August 1, 1980, mimeo at 10, 11, and fn. 15.

It is apparent that under an approach such as generally described above, an enormous additional workload will result beyond that expected for a single accurate and detailed cost estimate and potential overruns. The inherent inaccuracies of a probability approach is recognized. Studies have indicated that in the Defense industry, which is quite sophisticated with such analyses, a "perfect" cost estimate is still subject to at least a variance of + 20 percent. 13/ This would create a center point of between 0.8 to 1.2 in the best of circumstances.

The staff believes that if any recommendations were made to the Commission concerning changes in the IROR to include additional elements of ignorance and risk in the Commission's certificate, three changes must be specified and ordered (listed below).

The Commission has shown a willingness to reward the applicants for design changes that reduce costs, to set a Center Point at a minimum of 1, and to not allow changes in scope to be submitted by parties other than applicants even if such changes could result in a net reduction of the cost of the project. The order allowing this treatment indicates that the intent was to encourage a reduction in construction costs in the belief that it would result in a net benefit to consumers. Such instances were believed to arise rarely.

On three separate occasions, the Commission has recognized that there is a potential for abuse. 14/ The concern was that design and resulting cost estimate changes would not be submitted until after Commission certification. If the changes were delayed, the cost estimate and the Center Point would not reflect actual costs but could encourage inflated estimates. If the inflated estimates were accepted, design changes that resulted in a reduction in the CCE would not be reflected and would not impact the center point and therefore result in an unforseen and unacceptable increase in the actual rate of return.

Should the Commission decide to adopt a CCSE and CP with major design issues outstanding, it could create the situation it most fears. As the intent of IROR was, in greatest part, to protect the consumers, the Commission must order:

(1) Design changes requested or ordered by OFI that would result in a reduction of the CCE will reduce the CCE to the extent of its savings, 2) the Center Point may be less than or equal to one

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13/ McCullough Study, supra, fn. 9, mimeo at 48.

14/ See Order of August 1, 1980, mimeo at 10, 11, in Docket No. CP80-435; Order of April 28, 1980, mimeo at 100-101, fn. 121, and Order of June 20, 1980, mimeo at 23-25, both in Docket Nos. CP78-123, et. al.

and 3) provide that changes in scope can be submitted by anyone and approved if they result in a net reduction of project costs.

II.

As the staff stated, at the conference of September 3, supra, 1980, the presiding officer detailed four major unresolved design issues and directed the applicant and requested other parties and the staff to submit any additional possibilities.

The four listed issues were generally; 1) re-alignments necessitated by the Department of the Interior Grant of Right-Of-Way, 2) trench over or tunnel through Atigun Pass, 3) use of snow pads and snow roads, and 4) use of any different design mode particularly above-ground or bermed pipeline.

In addition, the staff believes the following ten major design change possibilities should be considered.

1. A decrease in the design pressure of the pipeline from 1260 psig to 1000 psig or less allowed by removal of all natural gas liquid components at Prudhoe Bay for use as petrochemical feedstock.

2. The requirement for a thermal workpad over the Alyeska fuel gas pipeline.

3. The requirement for a thermal workpad adjacent to the haul road to prevent thaw degredation.

4. The elimination of workpads in major portions of Spreads 5 and 6.

5. A buried or aerial crossing of the Yukon River, or a possible trade-off with Alyeska of Atigun tunnel space for Yukon River bridge space.

6. A less conservative frost heave mitigative design based on frost heave test results.

7. A change to an ambient temperature pipeline in Spreads 5 and 6.

8. An increase of one year in the construction schedule because of a delay in the Sales Gas Conditioning Facility until July, 1986.

9. A Communications System design based on specific equipment as opposed to the present performance criteria-scope design.

10. The use of new construction camps instead of refurbished Alyeska camps.

Respectfully submitted,

John P. Roddy

David L. Huard

Thomas J. Burgess
Commission Staff Counsel

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the official restricted service list compiled by the Secretary in Docket No. CP80-435, in accordance with the requirements of Section 1.17 of the Rules of Practice and Procedure.

Dated at Washington, D.C. this 3rd day of October, 1980.

John P. Roddy
Commission Staff Counsel

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UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Alaskan Northwest Natural Gas Transportation Company	)	Docket No. CP80-435

COMMISSION STAFF COMMENTS

FILI
PRC

I) On July 1, 1980, Alaskan Northwest Natural Gas Transportation Company (NWA or Applicant) filed a partial application for a final certificate of public convenience and necessity to construct and operate a natural gas pipeline across Alaska as part of the Alaska Natural Gas Transportation System (ANGTS). The incomplete application requested that two issues be addressed at this time, a Certification Cost and Schedule Estimate (CCE or CCSE) and Center Point (CP) determination.

On August 1, 1980, the Commission established a limited "subproceeding" to address the possible resolution of the CCE and CP. The object of the subproceeding is to aid the presiding officers, through a series of technical conferences, in the preparation of a report to the Commission. The report is directed to set out, to the extent possible, the areas of agreement among the parties if any, the areas on which the parties disagree, and to make substantive and procedural recommendations for Commission resolution of all issues within the subproceeding.

The Commission trial staff has actively participated in the technical conferences as well as served data requests and formal Interrogatories. 1/

II) One element mentioned as a concern of the Commission in its Order of August 1, 1980, is the existence of known, yet unresolved, design alternatives at the point of Commission determination of the CCE and CP. The ordering paragraph creating the subproceeding states:

> "... (T)he final report shall be based on the pipeline design that is current as of the date of the final conference, including all major

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1/ While the present proceeding is a "subproceeding", the Commission has not in any way limited the trial staff from performing its traditional role. Therefore, the staff has actively investigated the issues within the subproceeding as well as the many areas that must be addressed before final certification can issue.

> design alternatives under consideration by the project sponsors, whether or not such design alternatives are identified in the application." (Ordering Paragraph C, mimeo at 12).

At the request of the presiding officers, the staff has previously provided: 1) A list of outstanding, unresolved design alternatives; in addition to the four mentioned in the right-of-way grant material and the interim report of the presiding officers dated September 26, 1980; 2) Comments of how or whether such outstanding design issues may be handled in determining the CCE and CP consistent with Commission Orders 31 and 31B. (Comments filed October 3, 1980).

III) At the technical conference of October 23, 1980, (Tr 37, 38), the presiding officer requested that trial staff provide by November 7, 1980, a summary document concerning the various outstanding design issues. Each such issue was to be discussed delineating the staff's understanding of the potential for resolution of the issue by stipulation or more formal proceedings such as cross-examination of witnesses where information is deficient.

The staff agreed to provide such a document on the understanding that it be deemed a preliminary statment of the staff's position. (Tr. 40). The lack of requested information and time to review that which was provided on the design issues, renders certain the need for revision should long-sought and essential information be provided in the future conferences or as answers to Interrogatories.

The staff believes that its outstanding design issues fall roughly into three categories: 1) Those issues where sufficient information has been received for adequate analysis and where an atmosphere exists for some formal stipulation to be entered into by the parties when a proper vehicle for entering such stipulation presents itself; 2) Those substantial issues where sufficient information exists to presume the need for full hearing or other formal inquiry by the Commission prior to addressing the granting of final certification; 3) Those issues where essential information is still lacking to such an extent as to preclude a determination by the staff as to which approach to resolution is appropriate.

The staff's tentative positions on those matters are listed below (see VI infra).

IV) The technical conferences to date have addressed many elements of the CCE and CP. At times, certain areas were discussed through question and answer in great detail. However, the staff has not taken a position, even tentatively, on the many areas discussed and no opportunity to do so has appeared.

Therefore, for the purposes of a complete record as well as informing the presiding officers and all parties, the staff has in-

cluded its tentative position on as many additional areas of disagreement herein as time would allow.

Staff has two major concerns with the Certification Cost Estimate (CCE) of $8.79 billion filed by Alaskan Northwest Natural Gas Transportation Co. (NWA) on July 1, 1980, and amended to $9.1 billion on October 27, 1980. The first concern is with the methodology of the estimates, the embedded contingencies, and the appropriate contingency and Center Point given the estimate content. The second concern is with major design changes identified by the parties and the appropriate treatment of these changes. The potential cost impact of the staff concerns with sufficient information to estimate costs amount to an aggregate reduction in the CCE of $929 million and/or to an aggregate increase in excess of $846 million excluding contingency and finance charge. The Staff finds the methodology of engineering and design to be conservation and a minimum risk approach. The Staff will explore the appropriate contingency and Center Point values in the final technical conference in the subproceeding on November 10-20, 1980.

V) Two additional items should be stressed at this time:

First, the application of July 1, 1980, was substantially amended on or about October 27, 1980, reflecting the rerouting of the proposed pipeline consistent with the terms of the right-of-way grant issued by the Department of the Interior. In addition to the change in location, the amendment reflects the additional costs associated with the changes. The material is some 10 volumes in length and effects nearly half the proposed route.

Second, at the conference of October 7, 1980, the staff made an offer of settlement to NWA potentially to resolve part of the list of outstanding design issues. (Tr. 59-61). In sum, the offer addressed those outstanding design issues known prior to certification but as to which NWA either does not wish to or cannot provide design, cost, and risk which will result in a net reduction in project costs. The staff suggested that if such design alternatives are later adopted, NWA would request a reduciton of its CCE to the extent of the savings. The staff continues to believe that major design alternatives known prior to certification should be analyzed for design, cost, and center point effect prior to the determination of the CCE and CP.

VI) TENTATIVE STAFF POSITIONS

1. PROJECT DIRECTORATE ESTIMATE ISSUES

The issues involved in third party monitoring costs were discussed by the parties in the technical conference of October 27-29, 1980. Only $75.2 million of the $278.6 million estimated for third party monitoring are required by Federal and Alaska statutes. Staff notes that the Federal statute, the Mineral Leasing Act, is

being challenged in court by Pacific Gas Transmission Co. and Northern Border Pipeline Co., and as a result $53.6 million of the $75.2 million at least has a possibility of not being expended.

The remaining $203.4 million in costs to the State of Alaska is not required by statute and may be more properly supported with tax and royalty revenues from the project. These costs appear to be related to financing participation by Alaska which is not presently at issue or filed with the Commission in this subproceeding.

NWA has requested that third party monitoring costs not be included in the project Cost Performance Ratio since they are not under the control of NWA. Staff could possibly agree to such a position provided that costs caused by fault or non-performance on the part of NWA not passed through, a procedure to which NWA has given preliminary consent.

Project Directorate costs include pre-certification costs for which approval is pending before the Commissionin Docket No. CP78-123, et al. Staff believes that CP78-123, et al., is the appropriate forum for approval of pre-certification costs and that the CCE should be adjusted accordingly.

The parties have noted the absence of costs for a minority training program and an EEO compliance program in the CCE. All parties agreed to the immediate requirement for these programs. Accordingly, the staff believes that costs should be immediately included in the CCE for such programs.

All remaining Project Directorate costs will be examined in the Technical Conference of November 10-20, 1980.

2. DOI REROUTE

NWA filed an amended design and CCE on October 27, 1980, for the reroute mandated by the DOI right of way grant. The increase in cost of $200 million in pipeline, of $402.2 million in temporary facilities, and of $12.3 million in project directorate will be examined during the technical conference of November 10-20, 1980.

3. EMBANKMENT CONSTRUCTION MODE

NWA was to provide cost estimates to the parties by November 7, 1980, for alternative embankment construction modes.

4. SNOW PAD - SNOW ROAD CONSTRUCTION

NWA was to provide cost estimates to the parties by November 7, 1980, for snow pad and snow road construction.

5. ATIGUN PASS TUNNEL

NWA was to provide a cost estimate for the 22,000 foot Atigun Pass Tunnell alternative to the parties by October 27, 1980. NWA declined to develop this information by letter dated October 28, 1980. Staff independently estimates that a tunnel to carry a road

and four pipelines, but excluding the costs of constructing the road and the pipeline, at a range of $100 million to $700 million. Any split of costs proposed between Alaska, Alyeska, and NWA is unknown. At the very least, all costs associated with Atigun Pass should be deleted from the CCE until the tunnel option is decided.

6. THERMAL WORKPAD

Staff believes that concerns of Alyeska and of the State of Alaska relating to thaw degradation of the Prudhoe Bay haul road and of the soil surrounding the Alyeska Fuel Gas Pipeline will force NWA to use a thermal workpad adjacent to the haul road. NWA has proposed only a structural workpad.

Staff estimates a cost increase of $73 million for installing 1.5 inches of insulating board in the workpad on Sections 1 through 4.

7. AERIAL CROSSING OF YUKON RIVER

Alyeska presently holds the rights to use the vacant easterly Yukon River Bridge pipeline crossing carriage. NWA's estimate is based on obtaining the rights to use this existing crossing. If NWA fails to obtain those rights, an aerial crossing of the Yukon River would be required. The staff estimates the cost of this crossing at $18.5 million. A reduction of $10 million in crossing royalty cost would give a net cost estimate increase of $8.5 million for the crossing excluding reroute costs.

8. REDUCTION OR ELIMINATION OF WORKPAD IN SPREADS 5 & 6

The staff has designed a minimum workpad in Spreads 5 and 6 based on considerations of equipment movement and the proprietary geotechnical data of the sponsors. The staff design would result in a cost reduction of $1 million. The staff notes that NWA has reduced the average workpad thickness from 42 inches to 36 inches for these spreads in the amended CCE "filing" of October 27, 1980.

9. AMBIENT TEMPERATURE PIPELINE IN SPREADS 5 & 6

The staff has studied the proprietary data provided by NWA that indicates the existence of a thaw bulb along the Haines Pipeline right of way, and delineates the soil types encountered. The staff notes the thaw bulb is so extensive that NWA is studying moving the chilled gas pipeline 12 to 15 feet off the stripped right of way in order to reach non-thawed soil.

Based on the proprietary data, the staff believes that an ambient temperature pipeline extending from the discharge of Compressor Station 13 to the Canadian Border is technically feasible. Two alternate pipeline designs are feasible depending on the

assumptions:

1. Convential buried pipeline assuming that any thaw settlement has already occurred along the Haines right-of-way. This option would result in a cost savings of $221 million.

2. Conventional buried pipeline alternating with gravel embankment construction over permafrost soils containing greater than 7 percent silt and greater than 50 percent passing 200 mesh. The embankment made of construction material should mitigate thaw settlement in the permafrost soils. This option would result in a cost savings of $171 million.

Operating (fuel) costs would decrease by 40 percent for a non-chilled pipeline in that an increase in compression horsepower is more than offset by elimination of refrigeration horsepower.

10. LESS CONSERVATIVE FROST HEAVE MITIGATION

NWA expects that insulation thickness may be reduced from the CCE design based on test results from the frost heave test facilities. It is probably impossible to quantify these savings without data from the facilities. It may be possible to prove that any reduction in rate base from cost savings in this area would be of more benefit to the ratepayer than any gain in the rate of return on equity.

11. INCREASE OF ONE YEAR IN CONSTRUCTION SCHEDULE

NWA takes the position that the pipeline and conditioning plant will be available for service on schedule despite some indications to the contrary. Presumably NWA is willing to accept the risk of a 6 month to 1 year delay in the conditioning plant, and a mechanism could be crafted to allocate the risk properly.

12. COMMUNICATIONS SYSTEM DESIGN

As previously stated, the communications system design is based on two alternate scopes and is not equipment specific. Presumably a less expensive system or a more expensive, but more reliable, system may emerge in final design.

13. NEW CONSTRUCTION CAMPS

Staff has been unable to obtain the cost of new construction camps from NWA in order to compare with purchase, renovation, and relocation of Alyeska camps.

14. PIPELINE LAY RATE

The pipeline lay rate of 3200 feet (40 joints) per day for bare pipe and 2800 feet per day for insulated pipe forms the basis of the entire estimate. This lay rate was determined by a panel of experienced Execution Contractors (EC's) and represents their collective best judgement based on Alaskan and worldwide experience with pipeline construction. However, this lay rate of 3200 ft. (40

joints) contrasts with the March, 1977, estimate of 4000 feet or 50 joints per day, with the projected Foothills lay rate of 3600 feet or 54 joints per day, and with a Williams Brothers estimated lay rate of 4000 feet or 50 joints per day. Thus, the filed lay rate contains some embedded contingency for Alaskan experience which must be accounted for in establishing the values of contingency and Center Point.

15. PIPELINE CONSTRUCTION CONTINGENCY FOR WEATHER AND DELAY

The cost estimate for pipeline construction is based on a ten percent factor for weather and a two and one half percent factor for delay. This is applied to the Line Up/Hot Pass welders and all other pipeline operations are coordinated and staffed to this central function. This twelve and one half percent factor is further stated in the workpapers supplied for "Haul and String" and for "Haul and String Weights". Although NWA claims that this is a standard estimating practice, the staff maintains that it represents, rather, a contingency for weather embedded in the estimate that must be taken into account when setting values for contingency and Center Point.

16. DITCH GRAVEL QUANTITY ERROR

The estimated gravel requirements for ditch backfill in the amended cost estimate is approximately three times the ditch volume available to be backfilled. Correcting this error for material site stripping, crushing, hauling, and indirect costs results in approximately a $200 million reduction in the amended estimate. Although NWA stated that this error in the original estimate would be corrected, the staff notes that an incomplete correction was made in NWA's submission of October 27, 1980.

17. LINE PIPE SPECIFICATIONS AND PRICE

The staff has requested the exact specification provided to the line pipe manufacturers as a basis of bid quotation, but NWA has not provided this information to date. A general statement is made that one half the pipe will have a Charpy Impact specification of 70 ft.-lb. and one half will have a specification of 105 ft.-lb. and that these two toughness levels will be randomly placed in the pipeline for crack propagation resistance. The staff believes that such a random placement would not be realistic, and that costs for planned placement logisitics and control should be added to the estimate. At this time the staff has insufficient information to estimate the costs of planned-versus-random placement.

NWA has also stated that a lower toughness specification and the use of crack mechanical arrestors is still under active study. the staff, again, has insufficient information to evaluate the cost impact of such a design change. The staff understands that the cost of the higher toughness pipe is substantial and any approval of the CCE should stipulate that the associated costs should be lowered should the arrestor approach be eventually chosen.

Finally, the line pipe price in the estimate is based on an average of prices from six suppliers, five foreign and one domestic. This procedure presumes that equal amounts of pipe will be purchased from each supplier, whereas freight is estimated (temporary facilities) on the basis of 75 percent foreign and 25 percent

domestic. A further complication is the inability of the domestic manufacturer to meet the toughness specification at present although NWA, without demonstrated justification estimated on the basis that adequate toughness spcifications could be met at the future time of purchase.

Purchase of the pipe from the low bidder rather than the average price would result in a cost savings of $133 million. Purchase of 75 percent of the pipe from the low bidder and 25 percent domestic would result in a cost savings of $84 million. Should a strong "Buy American Act" be legislated, assuming that the domestic manufacturer can meet the delivery and specifications, costs would increase by $64.7 million.

18. MISCELLANEOUS UNSPECIFIED MATERIALS

Pipeline materials segment of the estimate contains a line item for miscellaneous unspecified material equal to 25 percent of all specified miscellaneous materials. This line item, stated to be based on current estimating practice, may contain some inherent contingency.

19. COMPRESSOR AND METERING STATION ESTIMATE CONCERNS

The refrigeration capacity requirement calculated by the FERC-AGPO computer model is 40 percent of the refrigeration capacity specified by NWA. The staff is continuing to investigate this anomaly and its potential for a cost estimate reduction of $70 million as well as substantial operating cost savings.

It should be noted that the NWA specified refrigeration capacity increased by 25 percent from the March, 1977, Estimate to the current CCE and is based on bare pipe heat transfer whereas much of the pipe will be insulated. Taking a credit for the insulation should reduce costs further.

The material price for compressors and turbine drivers was established by averaging four of ten quotations received. The staff has requested, but has not received, a quotation summary for all ten quotations. Staff also requested the quotation for the refrigeration equipment used for the $20 million estimate for testing equipment; the same has not been received. In addition, the NWA estimate included certain allowances in the material takeoffs. The staff believe the $20 million and the material takeoff allowances and definite factors in the consideration in the consideration of contingency and should be discussed at the November conference.

The staff has also requested information concerning Fluor's cost overrun experience in constructing the TAPS pump stations but has not yet received the information although the Morrison-Knudsen study would indicate that it is available. This information would be very helpful in analyzing the validity of NWA's contingency estimates for the compressor and metering stations.

20. TEMPORARY FACILITIES AND SERVICES ESTIMATE CONCERNS

The purchase of compressor station construction camps from Alyeska is a confused issue with NWA claiming during the sub-proceeding that it plans to purchase eight pump station camps whereas the workpapers in support of the estimate show the purchase of nine

pump station camps. The additional camp in question has already been sold to ARCO by Alyeska, but it remains in the CCE at an average cost of $10.8 million to purchase, relocate and refurbish. If NWA requires eight pump station camps, the $10.8 presently shown for the ninth camp million should be removed from the estimate. If NWA requires nine camps, the cost of constructing a new station camp should be included in the estimate.

The staff has requested NWA to supply information on the cost of new camps, but NWA has refused to do so until negotiations with Alyeska are completed. NWA has stated that negotiation should be concluded by Mid-November and information will then be promptly provided to the staff. The cost of new camps is required to compare with purchase, relocation, and renovation of the 24 or 25 camps to be obtained from Alyeska. These costs are also required to evaluate the appropriate values for contingency and Center Point in the event that purchase negotations with Alyeska are not successful.

NWA has estimated that 40 percent of the camp sewage treatment facilities must be replaced and 60 percent can be renovated. The latest NWA consultant study on the treatment facilities cannot be made available to the staff until December, 1980. The staff observation of some of the facilities indicates a requirement for 100 percent replacement.

The cost for restoring and revegetating the Alyeska camp sites after purchase and relocation of the camps is included in the NWA estimate. The staff believes that this cost properly should remain the responsibility of Alyeska or that a transfer of the responsibility to NWA should reduce the purchase price of the camps.

Finally, the staff notes that an office space leasing figure of $2.10 per square foot per month for the Fairbanks area has been utilized in the temporary facilities and in the communications system estimates. This cost compares to a Fairbanks average of $1.36/sq. ft./month and a lowest rate of $.75. Although the total amount of money is not worth argument, this rate is an additional and cogent example of the conservative approach in the estimate.

21. COMMUNICATIONS AND SUPERVISORY SYSTEM ESTIMATE

The estimate filed by NWA is based on an average of two quotations for a microwave-based, terrestial system and two quotations for a satellite-based system. These systems were quoted to satisfy performance specifications, and do not provide quantities or prices of materials from which the Office of the Federal Inspector would be able to track design changes. The quoted facilities do not include costs for an interface with the Foothills facility at the Canadian border.

A Support Service line item for $236 thousand is for an undefinable consulting service if required. This amount certainly appears to fit the category of contingency. The Staff believes the design basis to be overly conservative; any approval of the CCE should stipulate the associated costs should be lowered should the existing system be utilized.

22. ENVIRONMENTAL CONCERNS

At present there are three areas of concern to the staff. First is the the roughly 300 miles of rerouting around the Fairbanks area. No environmental baseline material has been provided for this segment nor has there been any discussion of access to this area. Secondly, the staff remains concerned about the increasing quantities of gravel estimated to be needed. To what extent will new material sites be required? What is the magnitude of the anticipated extensions to existing sites over and above the original proposal? What environmental baseline data is available for the new sites and/or what efforts are being taken to obtain such information? Lastly, the Atigun Pass tunnel is also of concern. The primary items of interest are the locations and extent of the adit points and construction work areas, the quantity of excavated material and the method and locations of disposal or use of this large volume of material, and disruption of the environment by disposal of excavated material and by blasting at the adits.

The currently proposed pipeline design involves many modifications in mile-by-mile design and routing which are markedly different from the design and routing contemplated in the original proposal. Many of these modifications go beyond the scope of the environmental impact statements prepared for the project. The staff believes that there must be an assessment of the environmental significance of the filed modifications as well as future major modifications to avoid delays based on environmental considerations.

Respectfully submitted,

John P. Roddy

David L. Huard

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Commission Staff Counsel

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 Docket No. CP80-435, in accordance with the requirements of Section 1.17 of the Rules of Practice and Procedure.

Dated at Washington, D.C. this 7th day of November, 1980.

John P. Roddy
Commission Staff Counsel