



# AMERICAN PUBLIC GAS ASSOCIATION

April 22, 2009

The Honorable Lisa Murkowski  
Ranking Member  
Energy and Natural Resources Committee  
United States Senate  
Washington, D.C. 20510

Dear Senator Murkowski:

The American Public Gas Association (APGA) is one of 20 major associations that supports amendment of Natural Gas Act (NGA) Section 5 to provide the Federal Energy Regulatory Commission (FERC) with authority to set a refund-effective date in complaint proceedings so that, in the appropriate circumstances, the FERC can order refunds at the conclusion of a complaint proceeding against an interstate pipeline. This important amendment of NGA Section 5 is contained in S. 672 introduced by Senator Cantwell and, of course, is not "retroactive ratemaking," as mislabeled by the pipelines, since the refunds, if any, are prospective from the refund-effective date, which may not precede the date the complaint is filed.

The Interstate Natural Gas Association of America (INGAA), the lobbying arm of the pipeline industry, has sent you a letter dated April 2 asking that you oppose the NGA Section 5 reform provided for in S. 672. The purpose of this letter is to address what we believe are inaccurate and misleading arguments made in the INGAA letter in regard to the impact this legislation would have on infrastructure.

It is highly significant that INGAA does not address (much less deny) that many pipelines are over-recovering in the hundreds of millions of dollars in excess of the just and reasonable rate level. The most recent (March 2009) study of the Natural Gas Supply Association (an annual study based on financial data filed by interstate pipelines with the FERC) stated that "[O]ur analysis of thirty-two pipeline companies shows that over a five-year period pipelines earned roughly \$3.7 billion more than they would have collected on an average 12 percent allowed return on equity." NGSAA concluded as follows: "While pipelines have clearly performed effectively for their shareholders, it is just as clear that returns are at a point where FERC oversight is necessary."

Rather than deny that its member-pipelines are over-charging with impunity, INGAA in effect argues that Congress should look the other way because unless pipelines are permitted to keep the excess revenues, they will be unable to continue to finance infrastructure construction. This argument is flawed on multiple fronts, a few of which are discussed below. First, pipeline rates are required to be just and reasonable under the NGA, which means that they provide for recovery of all prudently incurred costs plus a fair rate of return; and as the Supreme Court made

clear in the famous *Hope Natural Gas* case, a fair rate of return must be sufficient to permit pipelines to raise capital at reasonable rates in the market place.<sup>1</sup> Thus, the notion that pipelines must be allowed to charge rates in excess of the just and reasonable standard in order to finance capital expenditure for infrastructure runs counter to fundamental and well-established ratemaking principles embedded in the NGA and longstanding judicial precedent.

Not only is there no theoretical basis for the “infrastructure” argument made by INGAA, but it is also belied by the facts. The facts show no correlation between over-recovering pipelines and pipelines building infrastructure or between over-recovering pipelines and bond ratings. For example, the largest pipeline company in the country is El Paso Corporation, owning 25% of the total interstate throughput. El Paso is not an over-earner (see attached NGSA table reflecting that El Paso’s five-year average weighted equity return has been 10.9% - 23<sup>rd</sup> on the list of 32 pipelines), and yet it is one of the largest active participants in the construction of new infrastructure. Furthermore, El Paso has been an active participant in building infrastructure despite having a bond rating of BB – a bond rating that results not from its steady (if not glamorous) pipeline income but from its volatile exploration and production business (in 2007 and 2008, El Paso’s EBIT from the pipeline group was approximately \$1.3 billion, whereas the E&P group showed losses of \$1.4 billion in 2008 and marginal gains in 2007).

Other pipeline companies active in building infrastructure are the Williams Companies (its largest pipeline being Transco, which is 20<sup>th</sup> on the NGSA list with a five-year average return of 12.1%) and Loews Corp (whose largest pipelines are Gulf South – 21<sup>st</sup> on the NGSA list at 11.5% - and Texas Gas – which is not on the NGSA list). Again, the significant points are that (i) these companies are active in constructing infrastructure despite not being over-earners and (ii) their bond ratings (BBB for Williams and A for Loews) do not depend on whether their rates are maintained at just and reasonable levels. For Williams, income from its pipelines accounted for less than 24% of total income in 2008; for Loews, annual revenues from pipelines accounted for 6.4% of total revenues in 2008. The bond ratings of these companies are obviously a function primarily of their non-regulated activities.

The most consistently egregious pipeline over-earner, Natural Gas Pipeline Company of America, which during the most recent five years for which data is available has averaged in excess of a 34% return on equity (with a high of over 40%), is not investing in significant infrastructure; in fact it was 80% sold in early 2008 to Babcock & Brown, a company that collects high earning assets around the world (predominantly in Australia) in order to provide generous returns to its owners. In other words, NGPL is not underwriting new infrastructure investment in the United States with its excess earnings – rather, it was spun off by Kinder-Morgan for some \$5.26 billion as a result of its demonstrated ability to earn far in excess of a fair return on equity – excess returns underwritten by its gas customers.

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<sup>1</sup> The Supreme Court observed as follows in oft-cited *Hope* case affirming the Commission’s equity return allowance: “From the investor or company point of view, it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business. These include service on debt and dividends on the stock. By that standard the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital..” *Federal Power Comm’n v. Hope Natural Gas Co.*, 320 U.S. 591 at 603 (1944)(citations omitted).


In short, pipelines provide steady income for all of these large, integrated companies, but to suggest that NGA Section 5 reform would “slow the development of energy infrastructure” is without basis in theory or in fact. The fact of the matter is that companies, most of them large integrated entities with some income from pipeline operations, invest in infrastructure projects in the billions of dollars *because* they are profitable – yielding around 13% on equity with virtually no risk of under-recovery because the rates they charge include all fixed costs (plus profit) in a reservation charge that is collected without regard to throughput.

In addition, the FERC commissioners, each of whom is dedicated to enhancing energy infrastructure, understand there is no nexus between NGA Section 5 reform and development of new infrastructure, as evidenced by the fact that both the past FERC Chairman (and his predecessor) and the newly appointed FERC Chairman, as well as all sitting commissioners, support NGA Section 5 reform.

INGAA also has made the assertion that since the transportation component of the blended natural gas rate is relatively small, Congress should not address this issue. APGA maintains that the billions of dollars of overcharges by a handful of pipelines, dollars which should be in the pockets of consumers and not shareholders, demand congressional action.

The pipelines appear to want Congress to forget that the overriding mandate of the Natural Gas Act is that consumers pay just and reasonable rates. In the current financial crisis, it is more important than ever that consumers pay only what is cost-justified (versus what they can get away with under a flawed NGA Section 5). I thank you in advance of your consideration of this important consumer protection issue and welcome any questions.

Sincerely,

A handwritten signature in black ink, appearing to read "Bert Kalisch". The signature is fluid and cursive, with a prominent initial "B" and a long, sweeping underline.

Bert Kalisch  
President & CEO

Natural Gas Supply Association  
Actual Pipeline Rate of Return on Equity

NGSA Analysis - 32 Pipelines

Pipeline Name	Year Ended	Year Ended	Year Ended	Year Ended	Year Ended	5-year Average Weighted by Equity Ratebase
	2003	2004	2005	2006	2007	
1 Natural Gas Pipeline Company of America 1/	28.0%	29.6%	34.3%	40.1%	38.9%	34.4%
2 Kinder Morgan Interstate Gas Trans. LLC	24.1%	23.6%	25.6%	40.7%	44.3%	31.2%
3 Panhandle Eastern Pipe Line Company, LP	25.2%	27.7%	35.0%	35.6%	23.6%	28.9%
4 Dominion Transmission, Inc. (formerly CNG Trans.)	21.6%	24.1%	23.6%	19.1%	21.4%	21.8%
5 Mojave Pipeline Company 2/	16.8%	20.0%	21.9%	28.9%	17.2%	20.6%
6 Great Lakes Gas Transmission Ltd. Partnership	17.7%	20.8%	20.8%	22.6%	21.3%	20.5%
7 Transwestern Pipeline Company, LLC 3/	21.9%	19.7%	23.1%	19.6%	17.4%	20.1%
8 National Fuel Gas Supply Corporation	22.8%	19.4%	20.0%	18.2%	16.2%	19.2%
9 Northern Border Pipeline Company	22.0%	19.9%	17.4%	17.2%	18.5%	18.9%
10 CenterPoint Energy Gas Trans. (formerly Reliant)	21.5%	22.0%	22.3%	15.7%	12.3%	17.2%
11 Colorado Interstate Gas Company	16.5%	14.9%	12.5%	20.1%	19.5%	16.5%
12 Florida Gas Transmission Company, LLC	12.1%	12.7%	14.0%	17.5%	17.1%	14.6%
13 Kern River Gas Transmission Co.	10.5%	11.6%	9.7%	15.8%	24.5%	14.3%
14 Texas Eastern Transmission, LP	13.9%	15.2%	13.6%	12.3%	15.5%	14.1%
15 Northern Natural Gas Company	7.6%	12.0%	13.1%	17.9%	18.9%	14.1%
16 Tennessee Gas Pipeline Company	16.7%	14.6%	13.3%	12.2%	12.0%	13.6%
17 ANR Pipeline Company	14.4%	10.1%	17.0%	13.1%	12.2%	13.4%
18 Questar Pipeline Company	14.5%	12.7%	11.1%	15.0%	11.1%	12.7%
19 Gas Transmission Northwest Corp. (formerly PG&E) 4/	14.1%	11.5%	12.1%	10.4%	14.6%	12.5%
20 Transcontinental Gas Pipe Line Corp.	13.6%	13.8%	12.6%	9.3%	11.8%	12.1%
21 Gulf South Pipeline Co., LP (formerly Koch Gateway) 5/	-1.6%	12.9%	17.0%	24.0%	8.2%	11.5%
22 Southern Natural Gas Company	12.7%	13.0%	10.8%	10.8%	10.5%	11.4%
23 El Paso Natural Gas Company	13.7%	10.9%	7.9%	12.3%	10.0%	10.9%
24 Columbia Gulf Transmission Company	14.0%	12.7%	9.5%	7.1%	8.5%	10.0%
25 Columbia Gas Transmission Corporation	12.5%	11.8%	7.6%	7.3%	9.6%	10.0%
26 Trunkline Gas Company, LLC	10.6%	9.2%	8.5%	9.6%	10.4%	9.7%
27 Northwest Pipeline GP	5.9%	11.0%	10.7%	12.5%	10.7%	9.1%
28 Southern Star Central Gas Pipeline, Inc. (formerly Williams)	18.7%	13.8%	5.8%	4.4%	5.5%	8.6%
29 CenterPoint Energy Mississippi River Transmission	6.6%	9.6%	6.8%	7.7%	9.4%	8.1%
30 East Tennessee Natural Gas, LLC	4.8%	4.5%	7.0%	11.7%	5.9%	6.5%
31 Equitrans, LP	-5.0%	-9.2%	-19.0%	-2.8%	-6.1%	-7.4%
32 Sea Robin Pipeline Company, LLC 6/						
Simple Average	14.5%	14.5%	14.2%	16.0%	15.0%	14.6%
Weighted Average by Equity Ratebase	14.7%	14.7%	14.2%	14.5%	14.7%	14.6%

Pipelines NGSA's analysis determined do not have a fuel tracking mechanism to true-up their fuel costs at the end of the five-year analysis period.

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