

**Comments by Texas Independent Energy, LP  
Regarding the Railroad Commission of Texas’  
Natural Gas Pipeline Competition Advisory Committee Report**

**Introduction**

Texas Independent Energy, LP, a Delaware limited partnership (TIE), appreciates this opportunity to submit comments on the Railroad Commission of Texas’ (RRC) Natural Gas Pipeline Competition Advisory Committee Report (Report). As reflected in the RRC’s rules that established the Advisory Committee, the Report was intended to “help the Commission review competition in the Texas intrastate pipeline industry, assess the effect of current statutes and rules on such competition, and develop recommendations for changes to statutes or rules that may be necessary.”

TIE is an indirect, wholly-owned subsidiary of Public Service Enterprise Group, Incorporated. TIE was formed in March 1999 to develop, construct, own and operate natural gas-fired electric generating facilities in the Electric Reliability Council of Texas, also known as ERCOT. TIE currently holds a 100% ownership interest in Guadalupe Power Partners, LP (GPP) and Odessa-Ector Power Partners, L.P. (OEPP). GPP owns a 1,000 MW natural gas-fired electric generating facility in Marion, Guadalupe County, Texas and OEPP owns a 1,000 MW natural gas-fired electric generating facility in Odessa, Ector County, Texas.

TIE participated in the RRC’s workshops organized to gather firsthand information from market participants on abusive discriminatory practices that impact fair competition on the Texas intrastate pipeline system. TIE understands that the Advisory Committee considered the information gathered at these workshops as it developed the various recommendations contained in the Report.

TIE’s comments reflected herein demonstrate that the Report:

1. did not address competitive concerns from “wellhead to burner tip”;
2. consistently refers to a competitive market while ignoring the reality that pipeline access is not competitive;
3. relegates “price transparency” solely to the complaint process;
4. recommends an Oklahoma market-based ratemaking process without recognizing that Oklahoma also requires open access on its intrastate pipelines; and
5. fails to respond fully to the Legislative charge to the RRC.

The Report, by avoiding the Legislative directive to examine non-competitive behavior on the Texas pipeline system, barriers to entry, and monopoly abuse, recommends less regulatory oversight for the pipelines. This conclusion is exactly the opposite of what is needed to foster competition in the Texas natural gas market.

Open access on the electric transmission system was key to advancing wholesale competition in the electric industry. Similarly, open access on the pipelines is key to a

competitive natural gas market in Texas. And because of the direct link between natural gas markets and natural gas-fired electric generation, improvements in the natural gas markets in Texas will have a positive impact on the competitive electric market in Texas.

### **Comments on the Legislative Charge to the RRC**

While TIE recognizes the effort that the Advisory Committee put into the Report, there are still a number of issues not addressed satisfactorily by the Advisory Committee. The Legislature, in its appropriations bill, required the RRC to conduct a study that:

1. examines and determines the extent to which viable competition exists in the Texas natural gas pipeline industry from wellhead to burner tip;
2. recommends solutions to bring market competition to any non-competitive segments of the industry;
3. includes an assessment of the effectiveness of current laws, regulations, enforcement and oversight in addressing any abuses of pipeline monopoly power and make recommendations for changes that may be necessary; and
4. includes a comparative review of competition in the Texas intrastate gathering and pipeline industry with open access transportation in the interstate pipeline industry administered by the Federal Energy Regulatory Commission (FERC).

### ***Determination Whether Viable Competition Exists***

In regards to the first charge, the recommendations of the Advisory Committee throughout the Report clearly reflect the proposition that it believes the intrastate pipeline system is broadly competitive, and that only small changes are necessary to the current system to resolve the occasional disagreement. This conclusion is implied without analysis or support. In fact, it is TIE's experience that the pipeline segment of the natural gas market is not competitive, and fundamental changes are necessary. Without open access, the pipelines become a bottleneck to competition in Texas. The first charge also directs the RRC to examine competition from wellhead to burner tip. It is well documented that different markets exist for different functions of the natural gas industry. The market characteristics of a gathering system are different from the market characteristics of a transmission pipeline which are different from the market characteristics of a distribution system. These functional markets (gathering, transmission, and distribution) are also well recognized cost functions as indicated by their functional separation required by the FERC Uniform System of Accounts. However, a review of the Report text finds that the one and only time the word "burner tip" appears in the Report is in the Executive Summary. The transportation concerns of a shipper such as TIE are completely absent from the Report. While the Report clearly focuses on natural gas producers and gas gathering, the concerns of the consumer or end user are never considered. End users are faced with unique transportation issues that must be addressed by the RRC to satisfy the concerns expressed by the Legislature.

### ***Solutions for Market Competition***

As to the second charge, the Report never offers solutions to bring market competition to non-competitive segments of the industry. At best, it attempts to publicize existing avenues to settle disputes case by case. Dispute resolution will not produce fair and reasonable results when one of the parties to the dispute dominates the gas delivery

process. While existing avenues for settling disputes may offer a useful means for bringing parties together, the lack of a level playing field between the parties limits the effectiveness of the process in obtaining results that would be achieved by the forces of a competitive market. If the system for addressing market competition issues does not work, then promoting greater reliance upon this same system will not produce a better result.

### ***Assessment of the Effectiveness of Current Regulation***

The third charge directs the RRC to assess the effectiveness of current regulations and recommend changes. However, the only changes the Advisory Committee identified in the Report were to pursue changes to the informal complaint process already initiated by the RRC, and to adopt market-based rate setting legislation. While the changes to the informal complaint process may enhance the effectiveness of the process, the complaint process, by its nature, only addresses situations after significant problems arise. It is a process that attempts to fix, after the fact, a market that does not work. Put another way, the Advisory Committee's response addresses the symptoms of the market issues, but not the root causes of the problem. The changes to the informal complaint process do nothing to correct the lack of competition that requires a shipper to use the process in the first place. Further, the second recommendation of the Advisory Committee, its proposed change in the rate setting process, will only exacerbate the problem of the lack of competition on the intrastate pipelines. The reasons for this are discussed later in these comments.

### ***Evaluation of Alternative Regulatory Models***

Finally, the fourth charge directs the RRC to compare the Texas transportation market with the open access interstate transportation market. However, this potentially valuable analysis is not addressed in the Report at all. Open access transportation on the interstate market is based on non-discriminatory access at just and reasonable rates, with information transparency as a fundamental component of the open access system. It is worth noting that the original charge by the Legislature directed the RRC to include in the Report "a comparative review of competition in the Texas intrastate gathering and pipeline industry with the open-access transportation in the interstate pipeline industry," but most of this language, including the term "open-access" was omitted from the Report.

### **Comments on the RRC's Charge to the Advisory Committee**

The RRC charged the Advisory Committee with six tasks related to: the informal complaint process, information transparency, scope of the policy changes, marginal gas well production, gas gathering and transportation fees and services, and how other states address discrimination issues in gas gathering and transportation. TIE will focus on the issues of information transparency and gas gathering and transportation fees and services in these comments.

### **Information Transparency**

A competitive market exhibits six well established characteristics: many buyers and sellers, products are interchangeable, buyers are not loyal to particular sellers, no barriers to market entry or exit exist, all sellers have equal access to resources, and *all*

*participants have complete price information.* Natural gas pipelines are monopolies under Texas law because the markets in which they operate generally do not have these characteristics. However, under certain conditions, pipelines and shippers can negotiate transportation agreements if neither party has an unfair advantage in the negotiations, if the rates charged are substantially the same as rates charged to other shippers for similar services, or if competition exists with another pipeline. The key condition which allows successful negotiations to take place is the availability of information to all parties. Without sufficient information on prices and services, a shipper will always be at a disadvantage to the pipeline offering the transportation service.

TIE, as an end user with variable load requirements, requires certain non-standard services in addition to standard firm and interruptible transportation service that only allow for uniform rates of flow. Therefore, such non-standard transportation service offerings such as swing service, balancing services and park and loan services that allow for non-uniform rates of flow and allow for variances in hourly takes are necessary to match gas supply deliveries to electric demand. However, the information that is required to be included in tariffs currently filed by the pipelines that provide these services is not complete or detailed enough to allow shippers to compare an offer for service with what has already been transacted and approved.

In the Report, the Advisory Committee offers three recommendations regarding the problem of lack of information transparency. First, it proposes enhancements to the RRC's existing informal complaint process. Second, it encourages the RRC and trade associations to publicize the availability of existing information. And third, it recommends that the Legislature give producers the option of not including a confidentiality provision in future contracts.

Unfortunately, none of these recommendations solves the central problem of anti-competitive behavior. The only way to increase competition on natural gas pipelines is to provide sufficient market information on prices and services so that both the shipper and pipeline can negotiate on a level playing field. Making this information available can dramatically reduce or even eliminate the need for an informal complaint process. Why give a mediator access to contract information to determine a fair and reasonable rate when the parties can do the same thing with the same information. This recommendation only provides access to information after there is a problem. Publicizing existing information might be helpful to some shippers, but the examples noted in the Report are all directed at producer information, not end users like TIE. And as aptly concluded in the Report, publicly available information seldom provides the level of detail needed to negotiate effectively a rate. Finally, giving producers the option to make contract information public falls far short of the goal that all market participants have complete price information. Producers believing they have a favorable agreement may not give up that confidentiality, so the available market information is skewed. And a producer's contract terms will provide limited help to an end user with different transportation needs.

TIE suggests that a more fundamental approach to making information more available and more useful to all parties is to enhance the RRC's tariff filing requirements to require

sufficient information from pipelines to compare adequately services. It is the pipelines – not the shippers – that hold the information necessary to assure fair negotiations. While individual shippers’ names can remain confidential if required by the shipper, details such as receipt and delivery points, summary terms and conditions, rates and specific service descriptions are among the additional information needed to ensure a competitive service offer. The RRC already maintains an electronic tariff system, so the additional information can be filed and made available quite readily at little, if any, increased cost to participants.

### **Gas Gathering and Transportation Fees**

In addressing gas gathering and transportation fees and services, the Advisory Committee concluded that the RRC should not move to an open access transportation system because the current “lightly regulated” market is more responsive to the specific needs of the parties. The Advisory Committee even recommends that the RRC move away from cost based ratemaking and be given the ability to use either a cost-of-service based or a market based method to set rates in a formal rate proceeding. The Advisory Committee cites a portion of Sec. 24.5 (D) of Title 52 of the Oklahoma Statutes as a model for a market-based methodology. Using a ratemaking method based on the Oklahoma statute would allow the RRC to consider other negotiated rates when setting a disputed rate. However, a more complete look at the Oklahoma statute reveals that gatherers must first offer *open access* natural gas transportation, subject to certain conditions, under the Oklahoma statute (see Sec. 24.5 (B) and (C)). Access to information and provision of non-discriminatory services are integral features of the open access system, but this system has been explicitly rejected by the Advisory Committee in the Report. The Oklahoma statute referenced by the Advisory Committee states that the Oklahoma Corporation Commission (the rate setting authority) shall determine a fee or terms and conditions of service “which would result from arms-length bargaining in good faith in a competitive market between persons of equal bargaining power”. Until relevant, detailed and complete information is available from the pipelines, an arms-length negotiation between persons with equal bargaining power cannot occur and, therefore, cannot be the basis for rate setting in Texas.

The Report mentions two other issues related to rate making that are untrue or misleading. First, it suggests that pipelines do not keep their books with cost-of service regulation in mind. Of course, regulated utilities are required by law to maintain their books in accordance with the FERC system of accounts, so this a compliance issue and not a competition issue. Second, the Report argues that rate cases are expensive and should be avoided. In situations where true competition exists, this may be advisable. But this statement ignores all other situations when competition does not exist and the regulatory authority has an obligation to set rates based on the cost of service. For a pipeline utility that has total revenues in the hundreds of millions of dollars, even rates that are one percent too high will cost shippers millions of dollars. In this case, the \$300,000 in rate case expenses mentioned in the Report becomes money well spent.

**Conclusion**

As discussed in detail in these filed comments, TIE has reviewed the response to the Legislative charge to the RRC contained in the Report, and has concluded that the Report does not address adequately the problem of anti-competitive practices on the Texas intrastate pipeline system. TIE urges the Commission to consider the observations contained in these comments and initiate additional investigations into further changes that will help assure fair access to natural gas transportation for all shippers in Texas.