

(iii) Any capacity (such as general partner of a limited partnership, managing member of a limited liability company or a comparable position for another type of pooled investment vehicle, or trustee of a trust) that gives you legal ownership of or access to client funds or securities.

(2) *Independent representative* means a person that:

(i) Acts as agent for limited partners of a limited partnership (or members of a limited liability company, or other beneficial owners of another type of pooled investment vehicle) and by law or contract is obliged to act in the best interest of the limited partners (or members, or other beneficial owners);

(ii) Does not control, is not controlled by, and is not under common control with you; and

(iii) Does not have, and has not had within the past two years, a material business relationship with you.

(3) *Qualified custodian* means:

(i) A bank as defined in section 202(a)(2) of the Advisers Act (15 U.S.C. 80b-2(a)(2));

(ii) A savings association as defined in section 3(b)(1) of the Federal Deposit Insurance Act (12 U.S.C. 1813(b)(1)) that has deposits insured by the Federal Deposit Insurance Corporation under the Federal Deposit Insurance Act (12 U.S.C. 1811);

(iii) A broker-dealer registered under section 15(b)(1) of the Securities Exchange Act of 1934 (15 U.S.C. 78o(b)(1)), holding the client assets in customer accounts;

(iv) A futures commission merchant registered under section 4f(a) of the Commodity Exchange Act (7 U.S.C. 6f(a)), holding the client assets in customer accounts; and

(v) With respect to securities for which the primary market is in a country other than the United States, and cash and cash equivalents reasonably necessary to effect transactions in those securities, a financial institution that customarily holds financial assets in that country and that holds the client assets in customer accounts segregated from its proprietary assets.

#### **PART 279—FORMS PRESCRIBED UNDER THE INVESTMENT ADVISERS ACT OF 1940**

3. The authority citation for Part 279 continues to read as follows:

**Authority:** The Investment Advisers Act of 1940, 15 U.S.C. 80b-1, *et seq.*, unless otherwise noted.

4. By amending Item 14 of Part II of Form ADV (referenced in § 279.1) by adding “(unless applicant is registered

or registering only with the Securities and Exchange Commission),” after the words “client funds or securities”.

Dated: July 18, 2002.

By the Commission.

**Margaret H. McFarland,**

*Deputy Secretary.*

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## **DEPARTMENT OF ENERGY**

### **Federal Energy Regulatory Commission**

#### **18 CFR Part 284**

**[Docket No. PL02-6-000]**

#### **Notice of Inquiry Concerning Natural Gas Pipeline Negotiated Rate Policies and Practices**

July 17, 2002.

**AGENCY:** Federal Energy Regulatory Commission.

**ACTION:** Notice of inquiry.

**SUMMARY:** The Federal Energy Regulatory Commission (Commission) is issuing this Notice of Inquiry to seek comments on its negotiated rate policies and practices, established in Alternatives to Traditional Cost-of-Service Ratemaking for Natural Gas Pipelines, Regulation of Negotiated Transportation Services of Natural Gas Pipelines, Statement of Policy and Request for Comments, 74 FERC ¶ 61,076 (1996). Specifically, the Commission is undertaking a review of the recourse rate as a viable alternative and safeguard against the exercise of market power of interstate gas pipelines, as well as the entire spectrum of issues related to its negotiated rate program, and welcomes comments on these issues.

**DATES:** Written comments must be received by the Commission by August 26, 2002. Reply comments must be received by the Commission 30 days after the filing date for initial comments.

**ADDRESSES:** Office of the Secretary, Federal Energy Regulatory Commission, 888 First Street, NE., Washington, DC 20426.

**FOR FURTHER INFORMATION CONTACT:** Michael G. Henry, Office of the General Counsel, Federal Energy Regulatory Commission, 888 First Street, NE., Washington, DC 20426 (202) 208-0532.

#### **SUPPLEMENTARY INFORMATION:**

#### **Natural Gas Pipeline Negotiated Rates Policies and Practices**

1. In this notice of inquiry (NOI), the Federal Energy Regulatory Commission

(Commission) presents an opportunity for comments regarding its Negotiated Rates Policies and Practices, established in Alternatives to Traditional Cost-of-Service Ratemaking for Natural Gas Pipelines, Regulation of Negotiated Transportation Services of Natural Gas Pipelines, Statement of Policy and Request for Comments, 74 FERC ¶ 61,076 (1996). Specifically, the Commission is undertaking a review of the recourse rate as a viable alternative and safeguard against the exercise of market power of interstate gas pipelines, as well as the entire spectrum of issues related to its negotiated rate program, and welcomes comments on these issues.

#### **Background**

2. Since 1996 pipelines have had the option to use negotiated rates as an alternative to cost-of-service ratemaking. The Commission introduced negotiated rates to allow pipelines choosing not to seek market base rates by establishing a lack of market power or to undertake an incentive rate program, to adopt another alternative to traditional cost-of-service regulation. The original program was developed at a time when there was a great deal of concern about capacity “turnback” as a result of Order Nos. 436 and 636, and other factors.<sup>1</sup> Because the industry was shifting from traditional supply sources to other sources, many existing pipeline shippers no longer needed the same amount of firm capacity from their traditional pipeline’s supply regions, and as a result sought to “turn back” transmission capacity when their transportation contracts expired. The negotiated rates program was thus developed to help pipelines market that turned-back capacity to new shippers, such as electric generators, as well as to help retain local distribution customers whose existing contracts were expiring.

3. Under the negotiated rates program, instead of cost-of-service regulation, the pipeline and a shipper may negotiate rates that vary from the pipeline’s otherwise applicable tariff. A recourse rate that is on file in the pipeline’s tariff is always available for those shippers preferring traditional cost-of-service rates. The Commission recognized, however, that potential problems could occur if capacity became constrained, as for example, if shippers that were willing to pay more than the maximum rate through a negotiated rate were bidding against shippers that were bidding the maximum recourse rate. The Commission required that, in those situations, customers bidding more than the maximum rate would be treated as

<sup>1</sup> See, e.g., 74 FERC ¶ 61,079 at 61,225-26 (1996).

if they were bidding the recourse rate, and capacity was to be allocated *pro rata* among the negotiated rate bidder and recourse rate bidders. This, it was thought, would remove an incentive for negotiated rate shippers to bid more than the maximum recourse rates when capacity is constrained, because the shipper would have known it was paying more than was necessary to get the capacity.<sup>2</sup> In the last several years, there has been a significant increase in the reliance on negotiated rates to price natural gas transportation service. More recently, negotiated rate transactions based on price-index differentials have developed. These types of transactions, in particular, have raised serious concerns regarding the breadth and direction of the Commission's negotiated rate program.<sup>3</sup>

4. When the Commission introduced negotiated rates, at the suggestion of certain industry participants, it expected that negotiated rates would help achieve flexible, efficient pricing when market-based rates are not appropriate. Negotiated rates offered greater rate flexibility while limiting market power through the availability of the recourse rate.<sup>4</sup> The recourse rate option, the Commission explained, "would prevent pipelines from exercising market power by assuring that the customer can fall back to cost-based, traditional service if the pipeline unilaterally demands excessive prices or withholds service."<sup>5</sup>

5. So important was the availability of the recourse rate option that, as the Commission explained, the success of the negotiated rate policy relied upon the recourse rate "remain[ing] a viable alternative to negotiated service."<sup>6</sup> The failure of the recourse rate option to remain viable was an "impermissible" result.

6. Accordingly, the Commission finds that it is an appropriate time to assess the value and viability of its negotiated rate program. The Commission is seeking comments from all segments of the industry on these matters.

### Questions for Response

7. The Commission seeks responses to the following questions:

(A) Has the negotiated rate program been generally successful or unsuccessful in granting pipelines needed flexibility to serve new natural gas markets and retain existing markets? (Please support position taken with concrete specifics as much as possible.)

(B) Should the Commission modify its negotiated rate program?

(C) Do the negotiated rate filing requirements provide sufficient information for necessary transparency of the transactions? Should the Commission require pipelines to file negotiated rates on thirty days notice before such rates are implemented?

(D) Does the recourse rate option effectively mitigate pipeline market power? Are further mitigation measures necessary? And if so, which measures?

(E) Should the Commission disallow negotiated rates above the maximum recourse rate? Should the negotiated rate be limited to a certain multiple of the maximum recourse rate? Should the negotiated rate be limited to adjusting the levels of the reservations demand and commodity rate components, but the total revenue responsibility over the term of the contract remain equal the revenue responsibility under the recourse rate?

(F) Should the Commission disallow negotiated transportation rate deals based on price differentials of delivered gas between hubs?

(G) If such index price differential rates continue to be allowed, should some limits or restraints be placed on them? If so, what limits might be useful or appropriate?

### Public Comment Procedure

8. The Commission invites interested persons to submit written comments on the matters and issues raised in this notice, including any related matters or alternative proposals that commenters may wish to discuss. Upon evaluation of those comments, the Commission will determine what further action, if any, will be appropriate. Comments are due August 26, 2002. Comments must refer to Docket No. PL02-6-000, and may be filed either in electronic or paper format. Those filing electronically do not need to make a paper filing.

9. Documents filed electronically via the Internet can be prepared in a variety of formats, including WordPerfect, MS Word, Portable Document Format, Real Text Format, or ASCII format, as listed on the Commission's Web site at <http://ferc.gov>, under the e-filing link. The e-filing link provides instructions

for how to Login and complete an electronic filing. First time users will have to establish a user name and password. The Commission will send an automatic acknowledgment to the sender's e-mail address upon receipt of comments. User assistance for electronic filing is available at 202-208-0258 or by e-mail to [efiling@ferc.gov](mailto:efiling@ferc.gov). Comments should not be submitted to the e-mail address.

10. For paper filings, the original and 14 copies of such comments should be submitted to the Office of the Secretary, Federal Energy Regulatory Commission, 888 First Street, NE., Washington DC 20426.

11. All comments will be placed in the Commission's public files and will be available for inspection in the Commission's Public Reference Room at 888 First Street, NE., Washington DC 20426, during regular business hours. Additionally, all comments may be viewed, printed, or downloaded remotely via the Internet through FERC's home page using the FERRIS link.

### Document Availability

12. In addition to publishing the full text of this document in the **Federal Register**, the Commission provides all interested persons an opportunity to view and/or print the contents of this document via the Internet through FERC's home page (<http://www.ferc.gov>) and in FERC's Public Reference Room during normal business hours (8:30 a.m. to 5 p.m. Eastern time) at 888 First Street, NE., Room 2A, Washington, DC 20426.

13. From FERC's home page on the Internet, this information is available in the Federal Energy Regulatory Records Information System (FERRIS). The full text of this document is available on FERRIS in PDF and WordPerfect format for viewing, printing, and/or downloading. To access this document in FERRIS, type the docket number excluding the last three digits of this document in the docket number field.

14. User assistance is available for FERRIS and the FERC's Web site during normal business hours from our Help line at (202) 208-2222 or the Public Reference Room at (202) 208-1371 Press 0, TTY (202) 208-1659. E-Mail the Public Reference Room at [public.referenceroom@ferc.gov](mailto:public.referenceroom@ferc.gov).

By direction of the Commission.

**Linwood A. Watson, Jr.,**  
Deputy Secretary.

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<sup>2</sup> *Id.* at 61,241.

<sup>3</sup> See, e.g., Transwestern Pipeline Co., 94 FERC ¶ 61,233 (2001), *order to show cause*, 94 FERC ¶ 61,337 (2001), 95 FERC ¶ 61,143 (2001), and PG&E Gas Transmission, Northwest Corp., *order establishing hearing procedures*, 96 FERC ¶ 61,276 (2001).

<sup>4</sup> Alternatives to Traditional Cost-of-Service Ratemaking for Natural Gas Pipelines, Statement of Policy and Request for Comments, 74 FERC ¶ 61,076 at 61,240, *order on clarification*, 74 FERC ¶ 61,194, *reh'g denied*, 75 FERC ¶ 61,024 (1996).

<sup>5</sup> *Id.*

<sup>6</sup> *Id.*