BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Natural Gas Price Formation Docket No. AD03-7

Supplemental Comments

This is to follow up on the Nov. 4, 2003 "Staff Workshop on Market Activity and Price Indicators," and supplement the testimony of Dexter Steis and Mark Curran for the *Natural Gas Intelligence* newsletters.

The number of transactions received by *NGI* for inclusion in its bidweek price survey has increased from 435 in November 2002 to 1,381 in November 2003. December 2003 remained about level with 1,387 transactions.

Volumes have gone from 3.9 Bcf for the November 2002 bidweek to 8.9 Bcf for November 2003. (Note that Steis mispoke during the conference, saying the 2002 figure was 2.6 Bcf. The latter figure was the total of physical gas transactions, but did not include the 1.3 Bcf of physical basis trades, which *NGI* began including in its bidweek price survey that month. The overall total thus is 3.9 Bcf.). December 2003 volumes stood at 9.0 Bcf.

The volume of daily trading has remained about the same at about 10 Bcf/d, although the number of trades has increased. The marked increase in the number of trades owes something to the fact that we believe a vast majority of price quotes we now receive represent individual transactions.

Nearly all the data *NGI* now receives is from a department other than the trading floor. *NGI* has steadily increased the number of companies participating in its survey and currently is negotiating with several others. As was noted in the conference, to get systems and agreements in place takes a lot of paperwork back and forth with legal, trading and IT departments, and in many cases must be approved at the highest executive levels.

NGI currently is working to comply with the Commission's policy statement on natural gas and electric price indices.

NGI would also like to comment on the overall question of the criteria for pipeline cash-out formulas based on our own experience with determining pricing points. A comment was made during the conference that all the pricing points were developed at the request of the readers of the newsletters. That is not exactly true. Because of its role as provider of market information and price discovery, *NGI* would begin listing a new pricing point when enough data was available. Sometimes this would coincide with traders' queries for a published index at a particular location and other times it would be unsolicited. In either case however, the decision was made based on the reliability and volume of the underlying data -- not the urging of the market.

When indexing began to become popular, *NGI* editors informally tried to steer market participants to tie their deals to the more actively traded pricing points and/or baskets of prices from different publications.

While some heeded this suggestion, others did not, electing instead to tie their contracts to the pricing point in closest proximity to their pipeline, plant, supply basin or delivery point. By doing this, the parties to the agreement chose to avoid geographical or basis risk rather than the liquidity risk inherent in a pricing point constructed from relatively low survey participation volume. We note here that market participants had many index options when looking to write a contract and most who are in the market are knowledgeable as to which points are heavily traded and which ones are not.

A FERC Staff member said at the conference that since the Staff is not actually in the market, it is hard for them to judge what the criteria for a point should be. *NGI* suggests it may not be just a question of volume of trades. Since the cashout provisions are part of a pipeline's tariff, which is open to challenge by customers of the pipeline, it would seem that those customers -- who are in the market -- would be the best judge as to the reliability of a pricing point, and would object to any they believed to be unreliable.

It is possible, as some suggested at the conference, that only the Tier 1 and Tier 2 points should be used for indexing. However, that would rule out the use of indexes published by index developers who do not endeavor to publish tiers. We note here that *NGI* always has appreciated sharing the price survey responsibility with other publications since it provides a check for those in the market and for us. We also would not like to see the number of competitors diminish since it makes it more difficult for survey participants to attempt to manipulate prices.

As a pipeline spokesman pointed out, there may be a good reason for pegging the cashout formula to a less-traded point, depending on the configuration and operation of a pipeline, to avoid incentives for manipulation. Here again the robustness of trading apparently is not the most important factor.

Possibly, the Commission should consider allowing the use of the pricing points selected by the pipelines in conjunction with their customers and simply require that a more heavily-traded point be added in as a safety net in case there is no quote for the chosen point. Also, the Commission could provide for reopening the tariff provision in the face of significant complaints.

Respectfully Submitted,

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