

United States of America
Before the
Federal Energy Regulatory Commission

Natural Gas Price Formation

Docket No. PL03-3

This filing is a response by Intelligence Press Inc., more generally known as *Natural Gas Intelligence* or *NGI*, to the Federal Energy Regulatory Commission's July 24, 2003 Policy Statement on Natural Gas and Electric Price Indices as it relates to price developers and to questions in a Dec. 19, 2003 letter from the Commission staff to *NGI*.

NGI also is taking this opportunity to report on the status of its price surveys today. The status report will be followed by Part I, which is *NGI's* revised code of conduct and methodology, updated this month. This is a much more detailed document than has been publicly provided in the past. It is aimed at giving increased transparency to our operations as part of the drive to restore confidence in the voluntary price surveys and encourage companies to contribute to the price surveys. Part II is in response to the Commission staff's questions that are not addressed in the conduct and methodology.

As a supplier of information to the gas industry and its customers for more than 20 years, *NGI* will continue to cooperate whenever possible to help restore the function, efficiency and confidence in the market and the price reports. The code of conduct and detailed methodology that follow, and our commitment to an audit, are evidence of our much more rigorous procedural approach to the price survey function. We are seeing similar reforms on the part of contributors to the survey, whose numbers are increasing.

We hope to see that same dedication and cooperation from all the companies that participate in the market and whose businesses are profoundly affected by market prices. We are sending out another round of letters this month and making calls to companies that currently are not participating in *NGI's* price survey, with the hope they may now be prepared to support this voluntary system.

Overall trading and reporting of trades has increased since the 2002 market low point. Changes have been made, and participation, particularly among major players, has increased as has the confidence level in the published prices.

The major participants in the natural gas market, particularly large producers and a handful of the very largest utilities have recognized the importance to their business of a robust price survey, and the potential for that survey to moderate volatility and aid in efficiently allocating resources. Also contributing to *NGI's* survey are some of the remaining large marketers that still engage in significant trading, and some of the new and growing marketers and smaller trading companies.

NGI believes it now has about two-thirds of the significant market participants reporting to its price survey, and our comfort level with the surveys has increased exponentially from a year ago. At this point we are focusing on gaining cooperation from nine other companies that do a large volume of trades and that have told FERC they do not report prices to price developers. We also are working on participation from two companies that have told the Commission in the recent round of filings in RM03-10 that they are reporting but are not reporting to *NGI*. While we are expending more effort on these larger traders, we also are continuing to solicit input from others.

Generally absent from the ranks of those reporting are the smaller LDCs and smaller producers, which likely deal only in very small volumes or do very little fixed price trading.

Many of the smaller LDCs, we believe, are choosing to index and stay with the market to avoid after-the-fact condemnations by local regulatory regimes. Smaller producers also tend to index because they do not have the in-house marketing expertise to do otherwise. These smaller participants believe their small amount of fixed-price trading has little impact on the market and it is not worth the operational adjustments, oversight and exposure connected with reporting.

We agree that those trading small volumes do not have a significant impact on the indices at the most heavily traded points. Their input is valuable, however, in three respects. One is for quotes for the more lightly traded points. The second is for market information, which helps us get a complete trading picture, and the third is for verification if questions arise. For these reasons we continue to encourage them to report. All information is valuable and is included.

Another category of companies not reporting is composed of those companies currently involved in investigations of past practices, whose legal departments are overworked and have advised them not to chance further price reporting complications. Also, some companies still have concerns about reliance on the safe harbor provisions issued by the Commission and the Commodity Futures Trading Commission. *NGI* lost one valuable contributor last month because that party said federal regulators were going over its data and nit-picking every rounding and transposition error. Constant requests for clarification were tying up too much staff time.

There is also the fact that every time the Commission or the CFTC or some assistant district attorney or congressional committee decides to "investigate" some portion of the gas market, it solidifies the resolve of those CEOs lurking on the sidelines. Because of the notoriety surrounding price reporting recently, the decision on participation is being made at the highest executive levels. The reaction of those executives is human nature and is the reason, we believe the Commission should allow an adequate amount of time for the investigations to be completed and the market to fully recover before making a final assessment of the voluntary system.

Achieving a robust market and reporting system is going to take time. We have come a long way from the chaotic nightmare of a market that characterized most of 2002. We

made major progress in 2003 and we believe that given the right environment we can make significant achievements in 2004.

We hope the Commission will continue to encourage survey participation. We note that in its regular operations with regulated companies the Commission exerts pressure and makes every effort to have the parties achieve settlements that are in their own best interests. This type of approach has been working in the case of price surveys as well, and we hope the Commission will continue on this course.

We also believe that if the Commission were to attempt to install a mandatory system, they would lose many of the major participants in the current surveys which are the backbone of trading today. They are not jurisdictional companies and have strongly opposed a government-directed system. Even if, by rule or law, all market participants could be forced to participate in a government-sanctioned survey, given the sensitivity of the market to changes in this tight supply/demand situation, the transition would be likely to turn an already volatile market into chaos. We have very nearly been there. But we have emerged from the depths of 2002. Our progress has been encouraging. We cannot afford to go back.

We urge anyone who is interested in participating in the survey to contact us at the phone number or e-mail listed at the end of this document.

Part I

NGI's Code of Conduct and Price Index Methodology

(Updated January 2004)

Code of Conduct

Intelligence Press Inc., more generally known as *Natural Gas Intelligence* or *NGI*, operates under the journalism code of ethics, which requires that the personnel creating and compiling the content of our publications and management have no financial interest in the companies on which they report. *NGI* also warrants that its editorial and price survey employees and management do not trade in the natural gas commodity market, nor in any paper market relating to the natural gas commodity market.

Also, as journalists, *NGI* employees strive to maintain the highest standards of truth, accuracy, fairness and impartiality. This means double-checking facts, correcting errors as soon as possible, and striving to tell all sides of a story as equally as possible.

NGI also has a record of meeting deadlines and never failing over more than 20 years to publish a scheduled daily or weekly issue. In the real-time world, *NGI* strives to stay abreast of the news with timely reports over the Internet.

In its price surveys, *NGI* continuously works on soliciting the broadest possible participation from those who buy or sell natural gas. Our source base consists of participants from all sectors of the natural gas industry and its customers. By obtaining quotes from a large sampling of producers, marketers, intrastate pipelines, industrial end-users, and utilities, we increase the likelihood that the prices appearing in the newsletter more closely approach the true population average in an objective manner.

Confidentiality

In order to gain the broadest possible market participation and to protect our sources' competitive standing, *NGI* pledges not to reveal the confidential data that it receives, nor the source of any price information, nor will it reveal the parties involved in any transaction to any outside organization, except to the extent that it is legally required to do so (i) in response to any summons, subpoena, request of governmental or regulatory authority, or otherwise, or (ii) in order to comply with any applicable law, order or regulation, (hereafter, a "Required Disclosure"). *NGI*, before seeking to disclose Data in a Required Disclosure, shall to the extent legally permissible notify the Data Provider prior to making such disclosure in order to permit the Data Provider an opportunity to seek an appropriate protective order or grant a waiver of compliance with the provisions of this agreement.

Except for any Required Disclosure, without the prior written consent of the Data Provider, *NGI* will not disclose to any person either the fact that Data has been made available to it, that it has inspected any portion of the Data, the fact that discussions with

respect to the price index surveys are taking place with the Data Provider or other facts with respect to these discussions, including the status thereof; provided, however, that the Data Provider hereby consents to the public identification by *NGI* of Data Provider as providing information for use in *NGI's* publication of price index surveys.

Data sent to *NGI* price editors at the prices@intelligencepress.com e-mail address is archived and encrypted on a daily basis. Only the price survey staff and management have access to the confidential data submitted. Those personnel with access to the data are required to sign pledges of confidentiality restricting the use to purposes of evaluation, compilation, or editorial review of various price index surveys for publication (in aggregated form only and without disclosing the source thereof).

A copy of *NGI's* proposed Confidentiality Agreement is available at http://intelligencepress.com/features/ngi_confidentialityagreement.pdf

Price Index Methodology

What is Relevant Data and How Should It Be Submitted

"Data" shall include:

- All negotiated, fixed-price, non-affiliate transactions for both daily "incremental" and monthly (bid week) "baseload" delivery.
- Each transaction should be listed separately and should include transaction date negotiated, the flow date(s), location, volume, and price (\$/MMBtu or C\$/Gigajoule in Canada).
- Data Providers should submit all deals done during the relevant time frame.
- Data Providers should make all reasonable efforts to send price data to prices@intelligencepress.com or otherwise electronically submit data in a comma separated text file, an excel spreadsheet or other mutually agreed-upon format by 4:00 p.m. (EPT) on the business day before the first flow date of the data being submitted. Data submitted after 4:00 p.m. (EPT) will be included at the editor's discretion.
- Daily Data includes all fixed price deals done each business day (where a business day is any day Nymex is trading) before the 12:30 p.m. EPT pipeline nomination deadline for dry gas to flow the next day or over the weekend, as is the case Fridays.
- For the monthly market, Data includes transactions done on the last five business days of the month.
- Nymex physical basis deals done during bidweek should be denoted as such and included as "Data."

In the interests of receiving data from the broadest selection of Data Providers in the near term, *NGI* currently is not requiring that counterparty or buy/sell information be included in data, but it appreciates the companies that provide this useful information.

Consistent with the FERC's policy statement, *NGI* is asking that data be submitted by personnel other than traders. However, in the interest of receiving data from the broadest

scope of market participants, *NGI* may make special arrangements -- for an interim period -- to allow certain data providers time to transition to procedures where data comes directly from a mid- or back-office.

How Data is Used to Set Indexes

As described above, data is received by *NGI* from a variety of sources. These data submissions are first separated into their component parts or trades and initial determinations are made as to which, if any, of the pricing locations *NGI* publishes each component applies to. Also an initial determination is made of whether each component meets our requirements for applicable trade date and flow date(s) for the survey and a cursory check is made on the reasonableness of the report (to ferret out typos and obvious mistakes of transcription). Individual components or entire submissions may be dropped from our survey at this stage or they may be flagged for further investigation. Also components may be flagged because of questions as to the appropriateness of the component or provenance of the data.

Once data from all or nearly all submissions has been initially processed *NGI* is left with a set of data for each location we publish. Each of these sets are then taken individually and determinations are made about outliers within the set and determinations are made to identify any irregular data.

Irregular data may be either price or volume levels that are not confirmed by more than one source. When there is a sufficient number of reports in a given set, then statistical measures are often used to help make these determinations, such as reports that are more than three (3) standard deviations from the mean and are unconfirmed by other companies. In addition reports that are between 2.5 and 3 standard deviations from the mean may be excluded if they are not confirmed and similar trading was not observed by other sources at related locations, at the discretion of the editor.

When irregular data is observed it is often because *NGI* has made errors in the initial determination of appropriate pricing location or applicable trade or flow date - these are then corrected, either by moving the report to the appropriate location or removing it from our survey. Occasionally the source of an irregularity can not be explained and *NGI* may exclude a report, at the discretion of the editor. Reports that were flagged in the initial processing of the data are reviewed for their appropriateness, applicability, and reasonableness and may be excluded at the discretion of the editor. Reports may also be excluded because of extremely low volume (less than 1,000 MMBtu/d) or if there is an indication that there were special provisions tied to the transaction or if the transaction was not conducted at arms length, again at the discretion of the editor.

If *NGI* notices a pattern of persistent irregular reporting, *NGI* may contact the company involved. If the problem is not resolved, *NGI* may decide to exclude all of the information submitted by that Data Provider, but will take that step only after a formal complaint has been sent to the Data Provider's directors.

Setting the Prices

Once irregular, inappropriate or non-applicable reports have been excluded and outliers

removed, then *NGI* is left with a set data set at each location from which a low, high, and average price can be published. A volumetric weighted average is calculated using the volumetric weighted average method, which is expressed by the following formula:

$$A = \frac{\sum P \cdot V}{TV}$$

where A = average price, P = price per individual transaction, V = volume of each individual transaction, P*V= cumulative total of each transaction multiplied by its volume, TV = total volume.

Example:

Price	Volume	Factor (P*V)
\$1.22	25	30.50
\$1.25	5	6.25
\$1.27	10	12.70
\$1.19	7.5	8.93
	TV=47.5	P*V = 58.38

$$A = 58.38 / 47.5 = \$1.229$$

A rounds to \$1.23

There is one caveat: If the total volume of reports at a given location for the bidweek survey is below 25,000 MMBtu/d and *NGI* determines, given other available market information, that the resulting weighted average is an inadequate representation of market activity then an assessment is made using that other available market information. These locations are published marked with an asterisk (*) and a footnote explains that such an assessment was made. If the totality of information is inadequate, *NGI* does not publish an index.

Error Corrections

Because we understand that the market relies on the certainty provided by *NGI* indices and that trading decisions are being made based on these indices the moment they are published, *NGI* will only correct errors within two business days of the posting of the original index. And although the ultimate decision will be made after taking into account factors such as the nature of the error and who was responsible, it would be unlikely that *NGI* would issue a correction unless the error results in an index that diverges by at least 1% from the originally published index posting.

Indications of Volume of Trading

In July 2003 *NGI* instituted a Tier system for its bidweek survey to illustrate levels of trading at each location. Points with volumes of trades reported of 100,000 MMBtu/d or greater are designated as Tier 1; points with volumes between 25,000 MMBtu/d and 100,000 are designated as Tier 2; and points with volumes reported less than 25,000 MMBtu/d are Tier 3. As data volumes increase *NGI* looks to graduate to a system of publishing the actual volumes reported at each trading location.

Part II

Auditing

NGI is working to get systems in place that will allow a meaningful audit to be performed. At the current time *NGI's* processing of the data is accomplished using software directed toward speed and deadline requirements. It does not create an auditable paper trail, showing every operation that went into creating the final result. At this point, *NGI* can attest that it is following its methodology. It is not possible at this time, however, for *NGI* to track intermediate steps, such as moving or eliminating quotes, as described in our methodology.

NGI's technical staff currently is in the process of revamping internal data handling procedures. As the time of this writing additional procedures that insure that data submitted to *NGI* are maintained in an archive have been implemented, and the focus is on the procedures for tracking decisions made in the disposition of outliers. Once this process is complete *NGI* will be in a position to solicit bids from auditing companies to see if we can have an outside audit performed that will fit within our budget. Since Intelligence Press is a small company the extra effort on the part of our staff takes time, and expense is a serious consideration. *NGI* expects that it will be able to solicit bids from auditing companies in the second quarter of 2004.

Information Availability

NGI's price indices are available on a daily or weekly basis to anyone who subscribes and pays a subscription price to *NGI's Daily Gas Price Index* or *NGI's Weekly Gas Price Index*. The publications may be accessed on the web at <http://intelligencepress.com> or by fax. Subscribers to the weekly also may access the bidweek prices on the website after 4 p.m. EPT on the first business day of the month. *NGI* also sells historical data sets of published indices.

Responding to the Commission staff's questions about accessibility for the Commission to relevant data in the event of suspected bad faith reporting or potential manipulation, *NGI* notes that the confidentiality terms stated above and in the sample confidentiality agreement attached (see Exhibit A) provide that *NGI* will not disclose commercially sensitive data provided by survey participants "except to the extent that it is legally required to do so (i) in response to any summons, subpoena, request of governmental or regulatory authority, or otherwise, or (ii) in order to comply with any applicable law, order or regulation. The terms stipulate that if legally permissible *NGI* will notify the data provider before responding to a government subpoena.

Most of the agreements *NGI* has signed in the last year include the "legally required" exception and *NGI* will seek to include that exception in all new confidentiality agreements. We still, however, have a few older agreements which do not contain that clause, which we are attempting to amend, and verbal agreements which we are attempting to replace with our standard agreement -- without losing any survey participants.

Also, in the event of a Commission request for confidential data where there is evidence of false information being supplied, where appropriate, *NGI* will seek a waiver of the confidentiality agreement with the parties involved.

Also, as it has in the past, *NGI* will continue to provide non-confidential reports to the Commission and respond to questions seeking non-confidential information.

Finally, we note that in addition to the reform measures already put in place by the Commission, the data providers, and the price developers, the best defense against manipulation of the market is an abundance of data, which is where the major part of *NGI's* efforts currently are directed.

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Exhibit A

Date:

Company:
Attn:
Address
City, State

Re: Confidentiality Agreement protecting _____ proprietary information

Ladies and Gentlemen:

_____ (the "Disclosing Party") may from time to time furnish Natural Gas Intelligence (including editors at Intelligence Press owned publications such as *NGI's Weekly Gas Price Index* and *NGI's Daily Gas Price Index*, hereafter "NGI") with gas related pricing and other information in connection with compilation of various price index surveys, which information is confidential or otherwise generally not available to the public. Confidential information shall not, with respect to *NGI*, include information (a) that is or may become generally available to the public other than as a direct or indirect result of any breach of this agreement, or (b) that is known to *NGI* at the time of disclosure or is thereafter acquired at any time from a source other than the Disclosing Party and was not reasonably believed by *NGI* to be prohibited from making disclosure.

In order to induce the Disclosing Party to furnish confidential information to *NGI*, the parties agree as follows:

1. *NGI* will not disclose the confidential information furnished to it pursuant to this agreement without the prior written consent of the Disclosing Party, other than to directors, officers and employees of *NGI* who need to receive such confidential information solely for the purposes of evaluation, compilation or editorial review of various price index surveys for publication (in aggregated form only and without identifying the source thereof) in *Natural Gas Intelligence*, *NGI's Weekly Gas Price Index* and *NGI's Daily Gas Price Index* (those individuals who are directly or indirectly furnished confidential information by the Disclosing Party or *NGI* are collectively referred to herein as the "Representatives"), and that *NGI* will advise its Representatives of the confidential nature of the information and shall be responsible for such Representatives' compliance with the terms of this agreement.
2. *NGI* may also disclose the confidential information to the extent that it is legally required to do so (i) in response to any summons, subpoena, request of governmental or regulatory authority, or otherwise, or (ii) in order to comply with any applicable law, order or regulation, (hereafter, a "Required Disclosure"). *NGI*, before seeking to disclose confidential information in a Required Disclosure, shall to the extent legally permissible notify the Disclosing Party prior to making such disclosure in order to permit the Disclosing Party an opportunity to seek an appropriate protective order or grant a waiver of compliance with the provisions of this Agreement.
3. Except for any Required Disclosure, without the prior written consent of the Disclosing Party, *NGI* will not, and will direct its Representatives not to, disclose to any person either the fact that the confidential information has been made available to it, that it has inspected any portion of the confidential information, the fact that discussions with respect to the price index surveys are taking place with the Disclosing Party or other facts with respect to these discussions, including the status thereof; provided, however, that the Disclosing Party hereby consents to the public identification by *NGI* of

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Disclosing Party as providing information for use in *NGI's* publication of price index surveys that adheres to *NGI's* publicly disclosed requirements.

4. Except as otherwise provided herein, *NGI* and its Representatives will not use the confidential information other than solely for the purpose of evaluation, compilation or editorial review of various price index surveys for publication (in aggregated form only and without identifying the source thereof) in *Natural Gas Intelligence*, *NGI's Weekly Gas Price Index* and *NGI's Daily Gas Price Index*.
5. Each party understands and agrees that monetary damages would not be an adequate remedy for breach of this agreement. In the event of a breach or threatened breach of this agreement, the other party shall be entitled to injunctive and other equitable relief and such remedies shall be in addition to all other remedies available to it at law or in equity. Both parties hereby expressly waive (i) their right to trial by jury in respect of any suit, action or proceeding relating to this agreement and (ii) their right, if any, to claim or recover punitive or exemplary damages in connection with any alleged or actual breach of this agreement. The Disclosing Party shall also be entitled to recover its reasonable legal fees and expenses and costs in enforcing this agreement or recovering damages for any breach hereof.
6. This agreement shall be governed by and construed in accordance with the laws of the Commonwealth of Virginia without regard to the principles of conflicts of laws of thereof.
7. The parties hereto agree that no employment, agency, joint venture, partnership or fiduciary relationship shall be deemed to exist or arise between them with respect to this agreement or the proposed reporting of price index surveys.
8. Disclosing Party hereby certifies that it will provide gas and/or power transaction and related pricing and other information to *NGI* with the good faith belief that such information: (i) accurately represents transactions consummated by the Disclosing Party at the stated price and contains accurate information about the components of each reported transaction; (ii) represents a complete set of transactions for the stated product; and (iii) is provided by a back office or other non-commercial point or person within the Disclosing Party's organization who is responsible for the accuracy and completeness of all reported transactional data. Disclosing Party understands that if *NGI* poses questions to it concerning the accuracy and/or completeness of information that the Disclosing Party has previously submitted, it will respond in a timely manner and in good faith to resolve those questions. In the event of any errors or omissions, Disclosing Party will make reasonable efforts to inform *NGI* and, as necessary, modify its internal processes to eliminate or minimize the likelihood of future errors or omissions in its data submissions.
9. The provisions of this Agreement shall terminate on the date two years from the date of the last disclosure of confidential information made pursuant to this letter.

Very truly yours,

Intelligence Press, Inc.

By: _____

Name: _____

Title: _____

ACCEPTED AND AGREED:

By: _____

Name: _____

Title: _____