125 FERC ¶ 61,082
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Suedeen G. Kelly, Marc Spitzer,
Philip D. Moeller, and Jon Wellinghoff.

Southern Star Central Gas Pipeline, Inc. Docket No. PA08-1-000

ORDER APPROVING AUDIT REPORT AND DIRECTING COMPLIANCE AND OTHER CORRECTIVE ACTIONS

(Issued October 22, 2008)

1. In this order, the Commission approves the attached Audit Report (Report) prepared by the Office of Enforcement's (OE) Division of Audits. The Report contains OE's findings and recommendations with respect to Southern Star Central Gas Pipeline, Inc.'s (Southern Star) compliance with the Commission's rules, regulations, and other requirements. We further direct Southern Star to implement the Report's corrective actions, including the procedures outlined below.

2. OE staff advised Southern Star of their findings and recommendations in a draft audit report, to which the company did not object. Accordingly, the OE Director could have acted on the Report under the authority delegated to her in 18 C.F.R. § 375.311 (2008). The Report's findings, however, implicated substantial non-compliance by the company.[1] Accordingly, the Commission has decided to take the unusual step of acting on this uncontested matter. Indeed, this was a close call, as the level of non-compliance and the seriousness of some of the violations was such that we seriously considered pursuing the imposition of penalties for the violations. On balance, after reviewing Southern Star's willingness to take corrective action, taking into account exemplary cooperation during the audit and considering the fact that Southern Star's predecessor was responsible for most of the serious violations discussed below, we decided to forego that remedy and instead address the company's violations in a Commission order to provide guidance to other companies similarly situated to Southern Star, an approach that

[1] In brief, during the audit, OE staff found that Southern Star (1) did not file with the Commission all contracts containing material deviations from the form of service agreement in its tariff, (2) did not file all the requisite information in its index of customers or post the index in the format required by the regulations, (3) did not post for bid capacity expiring under one contract, as required by its FERC-approved tariff, (4) did not comply with certain requirements when it filed its FERC Form No. 2 with the Commission, and (5) did not post its Transactional Report and Available Capacity Report in compliance with the requirements of the Commission's regulations.

falls outside the authority delegated to the OE Director. While the Commission is not penalizing Southern Star, the Commission may consider civil penalties in the future under similar circumstances.

Background

3. On October 4, 2007, OE staff issued a letter to Southern Star in this docket announcing commencement of an audit to determine whether, for the period from January 1, 2006 through May 30, 2008, Southern Star was in compliance with the Commission's accounting, reporting and transportation regulations contained in 18 C.F.R. Parts 201, 260, and 284; the North American Energy Standards Board (NAESB) standards; and Southern Star's FERC Gas Tariff. In the course of the audit, OE staff issued data requests, conducted site visits, and held meetings with Southern Star's officers and staff. On August 4, 2008, OE staff sent Southern Star a letter and draft audit report with their findings and recommendations. On September 2, 2008, Southern Star responded to OE staff's draft audit report, and stated the company's agreement with OE staff's findings and the recommended actions.

Audit Report

4. As noted, the Report finds that Southern Star did not fully comply with the requirements applicable to it and makes recommendations to correct the identified areas of non-compliance. The Report's principal findings are that Southern Star:

A. Failed to file with the Commission at least twenty-nine contracts containing material deviations from the *pro forma* service agreement in its tariff, in violation of 18 C.F.R. § 154.1(d) (2008).

B. Did not file all the requisite information in its index of customers, as required by 18 C.F.R. § 284.13(c) (2008), or post the index in the format required by 18 C.F.R. §§ 284.12 and 284.13(c) (2008).

C. Did not post for bid capacity expiring under one contract, as required by its FERC-approved tariff.

D. Did not comply with certain requirements when it filed its FERC Form No. 2 with the Commission.

E. Did not post its Transactional Report and Available Capacity Report in compliance with the requirements of 18 C.F.R. §§ 284.12 and 284.13 (2008).

5. The Report includes recommended remedies to address the identified instances of non-compliance and to help ensure Southern Star's future compliance with the requirements. The Report recommends that Southern Star:

A. Establish written policies and procedures to ensure that it files all contracts containing non-conforming terms and conditions with the Commission.

B. Submit to OE within 120 days of the issuance of the final audit report a master list of all currently effective agreements, indicating whether each agreement contains material non-conforming terms and conditions in the format described in the Report. For agreements that contain material non-conforming terms and conditions, Southern Star must indicate whether it filed the agreement with the Commission and provide the docket number under which it filed each agreement.

C. Submit to OE within 120 days of the issuance of the final audit report a matrix of unfiled agreements that contain material non-conforming terms and conditions in effect on the issuance date of the audit report.

D. Within 150 days of the issuance of the final audit report, file with the Commission all unfiled agreements that contain material non-conforming terms and conditions.

E. Submit to OE within 120 days of the issuance of the final audit report a statement signed by a member of Southern Star's senior management attesting to the accuracy of all information contained in the master list of effective agreements and the matrix listing all unfiled agreements that contain material non-conforming terms and conditions.

F. Establish written policies and procedures ensuring that Southern Star files and posts all indices of customers in compliance with the Commission's rules and regulations.

G. File corrected indices of customers for the period January 1, 2007 to January 1, 2008.

H. Archive corrected indices of customers for the period from January 1, 2007 to January 1, 2008, on Southern Star's web site.

I. Establish written policies and procedures that ensure that Southern Star performs capacity auctions in compliance with the Commission's rules and regulations and its tariff.

J. Review the quantities reported on its Gas Account pages for 2006 and 2007 to ensure that Southern Star reported the correct quantities in accordance with the instructions for that page of the FERC Form No. 2.

K. Establish and implement written policies and procedures that ensure accurate and complete reporting of fuel and lost and unaccounted-for gas on Southern Star's FERC Form No. 2.

L. Re-file the FERC Form No. 2 with corrected Gas Account pages for 2006 and 2007.

M. Establish and implement written policies and procedures that ensure Southern Star posts all web site postings in compliance with Commission rules and regulations and NAESB standards.

N. Review all web site postings for compliance with Commission and NAESB regulations and correct all inaccurate or incomplete postings.

Discussion

6. While the Commission faults Southern Star for not complying with our rules, regulations and other requirements as uncovered in OE staff's audit, we are especially troubled by the company's failure to file material deviations from the *pro forma* service agreement in its tariff, in violation of 18 C.F.R. § 154.1(d) (2008).[2] By way of background, section 4 of the Natural Gas Act requires natural gas companies to file with the Commission their rates and charges for any sale or transportation subject to the jurisdiction of the Commission.[3] Natural gas companies are also required to file all contracts that affect or relate to the rates, charges, classifications and services.[4] When the Commission accepts tariffs, the Commission considers that those tariffs are just and reasonable, except where the Commission explicitly directs modifications.[5]

[2] *See Alternatives to Traditional Cost-of-Service Ratemaking for Natural Gas Pipelines, Regulation of Negotiated Transportation Services, Statements of Policy and Comments*, 74 FERC ¶ 61,076, *order on clarification*, 74 FERC ¶ 61,194, *order on rehearing*, 75 FERC ¶ 61,024 (1996); *See also Natural Gas Pipeline Negotiated Rate Policies and Practices*, 104 FERC ¶ 61,134 (2003), *order on rehearing and clarification*, 114 FERC ¶ 61,042 (2006) (*2003 Policy Statement*).

[3] 15 U.S.C. § 717c (2006).

[4] *Id*.

[5] *Tennessee Gas Pipeline Company*, 65 FERC ¶ 61,356, at 62,907 (1993).

Correspondingly, service that is performed under a service agreement matching a *pro forma* agreement contained in the approved tariffs is, by definition, just and reasonable.[6]

7. The Commission must be able to review arrangements entered into by the parties that deviate from the *pro forma* service agreement to meet its obligations under the Natural Gas Act to assure that the agreement is just and reasonable. Pipelines' failure to file non-conforming agreements imperils the Commission's responsibility under the Natural Gas Act to ensure provisions are just and reasonable and are not unduly discriminatory or preferential. In 2001, the Commission clarified that a material deviation is any provision in a service agreement that: (1) goes beyond filling in the blank spaces with the appropriate information allowed by the tariff; and (2) affects the substantive rights of the parties.[7] Similarly, in the *2003 Policy Statement*, the Commission stated that "[s]ince there would appear to be no reason for the parties to use language different from that in the form of service agreement other than to affect the substantive right of the parties, this effectively means that all language that is different from the form of service agreement should be filed with the Commission."[8]

8. Prior to the Energy Policy Act of 2005,[9]we issued several audit reports containing findings that natural gas companies did not file contracts containing material deviations with the Commission.[10] The Commission also approved two settlement agreements relating to the failure to file with the Commission contracts that contain non-conforming

[6] *Id*.

[7] *Columbia Gas Transmission Corp.*, 97 FERC ¶ 61,221, at 62,010 (2001). *See also ANR Pipeline Co.*, 98 FERC ¶ 61,247, at 62,002 (2002).

[8] *2003 Policy Statement*, 104 FERC at P 32.

[9] Energy Policy Act of 2005, Pub. L. No. 109-58, 119 Stat. 594 (2005) (EPAct 2005).

[10] *See Letter Order Issuing Final Audit Report for Gulf Stream Natural Gas System, LLC* in Docket No. PA04-16-000 (2004); *Letter Order Issuing Final Audit Report for Colorado Interstate Gas Company* in Docket No. PA04-9-000 (2004); *Letter Order Issuing Final Audit Report for East Tennessee Natural Gas, LLC* in Docket No. PA05-63-000 (2005); and *Letter Order Issuing Final Audit Report for Vector Pipeline, LP,* in Docket No. PA05-67-000 (2006).

material deviations.[11] At the time, however, the Commission did not have penalty authority under the Natural Gas Act, and as a consequence our remedies were limited.[12] That changed with the enactment of the EPAct 2005, which granted the Commission civil penalty authority for violations of the Natural Gas Act.[13]

9. The Southern Star audit is the first instance, following EPAct 2005, where Commission staff has identified material deviations in contracts that have not been filed with the Commission. As mentioned, the level of Southern Star's violations was such that we seriously considered penalties as a remedy because the failure to file contracts with material deviations has prevented us from ensuring that provisions are just and reasonable and are not unduly discriminatory or preferential under the NGA. However, at Southern Star, OE staff found that the majority of the contracts with material deviations were entered into by Southern Star's predecessor, which had made a statement, at the time of sale, that the pipeline was being operated in compliance with applicable regulatory requirements.[14] Additionally, Southern Star demonstrated exemplary cooperation during the audit and promptly implemented certain remedial actions as soon as OE staff identified them. On balance, we have decided to proceed here with a public order emphasizing our concern about the failure to file agreements with material deviations rather than impose a civil penalty on Southern Star. A public order provides similarly situated companies notice that the Commission treats these types of violations seriously.

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[11] *CenterPoint Energy Gas Transmission*, 104 FERC ¶ 61,280 (2004) (staff found that 76 of CenterPoint's 87 negotiated rate contracts contained material deviations and should have been filed with the Commission); *Texas Eastern Transmission, LP*, 110 FERC ¶ 61,188 (2005) (staff identified two contracts with material deviations that should have been filed with the Commission and Texas Eastern's follow-up review identified 49 additional contracts with material deviations that should have been filed with the Commission).

[12] *Revised Policy Statement on Enforcement*, 123 FERC ¶ 61,156, at P 41-49 (2008).

[13] Section 22(a) of the Natural Gas Act authorizes us to assess a civil penalty of up to $1,000,000 per violation for each day that it continues. 15 U.S.C. § 717t-1 (2006).

[14] In September 2002, Williams Gas Pipeline Company entered into an agreement to sell its pipeline assets to Southern Star Central Corporation and, stated that, to the best of its knowledge, "the operations … have been conducted in material compliance with all applicable laws, regulations, orders and other requirements of all Government Authorities having jurisdiction." Williams Companies Inc. 10K for December 31, 2002 obtained from www.sec.info.com/dsvrp.2424.q.htm (October 9, 2008).

10. While we have exercised our discretion in this case not to assess civil penalties for Southern Star's violations,[15] we want to point out to Southern Star and all other pipelines within our jurisdiction that we will not be inclined to be so lenient if we discover similar violations in the future. The rules regarding pipelines' tariffs that govern the provision of accessible and properly priced transportation service to their customers are too important to the efficient operation of the natural gas grid and markets for the Commission to do otherwise. Accordingly, the Commission will not hesitate to exercise the Natural Gas Act's penalty authority in appropriate circumstances in the future to deter such action.

11. The Audit Report also concluded that Southern Star did not have an effective regulatory compliance program. Indeed, in addition to the material deviations in the contracts not filed by Southern Star, Southern Star violated a host of other filing and posting violations as noted in paragraph 4 above. Accordingly, besides the recommendations included in the Audit Report, the Commission is encouraging Southern Star to implement a comprehensive regulatory compliance program consistent with the factors articulated in the Compliance Policy Statement.[16] Southern Star can also obtain guidance from two recent settlements whereby each company agreed to develop and implement a comprehensive regulatory compliance program.[17]

12. As a final matter, the Commission notes that our staff is available to answer questions about the Commission's requirements if Southern Star or other pipelines are

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[15] *See also Stingray Pipeline Company, L.L.C.*, 121 FERC ¶ 61,216 (2007) (following acquisition of Stingray, Enbridge, Inc, conducted an internal review and identified contracts with material deviations that should have previously been filed with the Commission). *CF PacifiCorp,* 125 FERC ¶ 61,034 (2008) *(*order accepting late-filed agreements of PacifiCorp, but reminding electric transmission providers to comply with filing requirements on a timely basis or face possible sanctions from the Commission).

[16] *Compliance with Statues, Regulations and Orders*, 125 FERC 61,058 at P 13-21 (2008) (*Compliance Policy Statement).*

[17] *See In re Edison Mission,* 123 FERC ¶ 61,170 (2008), *order denying motion to intervene and dismissing requests for clarification and rehearing of order approving stipulation and consent agreement,* 125 FERC ¶ 61,020 (2008) (as part of settlement, Mission agreed to implement a comprehensive compliance program at an approximate cost of $2,000,000 using an independent external consultant); *Duquesne Light Company*, 123 FERC ¶ 61,221 (2008) (as part of settlement, Duquesne agreed to implement a comprehensive compliance program at an approximate cost of $1,000,000 using an independent external consultant).

unsure how they apply to a particular situation.[18] We also remind pipelines that the Commission's enforcement policy favors self reporting by those who commit violations and that those whose violations are discovered by the Commission, in an audit or otherwise, may be treated less favorably than those who report their violations to the Division of Investigations of the Office of Enforcement.[19] Furthermore, as recently reinforced in our *Compliance Policy Statement*, the Commission intends to give significant credit to companies that have vigorous compliance programs.[20]

The Commission orders:

(A) The attached Report is approved in its entirety without modification.

(B) Southern Star is directed to implement the corrective actions recommended in the Report.

(C) Southern Star is directed to file a compliance plan outlining the steps it will take to implement the recommendations in the Report within 30 days of the issuance of this order.

(D) Southern Star must make quarterly filings in Docket No. PA08-01-000 detailing its progress in implementing the corrective actions until all the corrective actions are completed. The filings must be made not later than 30 days after the end of each calendar quarter, beginning with the first quarter after the filing of the compliance plan and continuing until Southern Star completes all the recommended corrective actions.

By the Commission.

(S E A L)

Kimberly D. Bose,
Secretary.

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[18] *Interpretive Order Modifying No-Action Letter Process and Reviewing Other Mechanisms for Obtaining Guidance*, 123 FERC ¶ 61,157 (2008).

[19] *Revised Policy Statement on Enforcement*, 123 FERC ¶ 61,156 at P 61-64 (2008).

[20] *Compliance Policy Statement* at P 21-26.

Federal Energy Regulatory Commission

Audit of Capacity Auctions, Fuel Retainage, Lost and Unaccounted for Gas Retainage, Contracts, Index of Customers Filings, FERC Form No. 11 Filings, Certain FERC Form No. 2 Information, Web Postings, Crediting of Penalty Collections, and Cash Management Arrangements at Southern Star Central Gas Pipeline, Inc.

Docket No. PA08-1-000
October 21, 2008

Office of Enforcement
Division of Audits

Table of Contents

I. Executive Summary

A. Overview

The Division of Audits (DA) within the Office of Enforcement (OE) has completed an audit of Southern Star Central Gas Pipeline, Inc. (Southern Star or Company). The audit was initiated to evaluate the Company's compliance with certain of the Federal Energy Regulatory Commission's (FERC or the Commission) accounting, reporting, and transportation regulations contained in 18 C.F.R. Part 201,[1] 18 C.F.R. Part 260,[2] 18 C.F.R. Part 284,[3] North American Energy Standards Board (NAESB) standards,[4] and Southern Star's FERC Gas Tariff.[5] Specifically, we reviewed Southern Star's: (1) capacity auctions under 18 C.F.R. §§ 284.8 and 284.221(d); (2) fuel retainage under 18 C.F.R. § 154.403 and Southern Star's FERC Gas Tariff; (3) lost and unaccounted for gas retainage under 18 C.F.R. § 154.403 and Southern Star's FERC Gas Tariff; (4) service agreements under 18 C.F.R. § 154.112 and Southern Star's FERC Gas Tariff; (5) index of customers (Index) filings under 18 C.F.R. § 284.13(c); (6) FERC Form No. 11 (Form 11) filings under 18 C.F.R. § 260.3; (7) certain FERC Form No. 2 (Form 2) information under 18 C.F.R. § 260.1; (8) web site postings under 18 C.F.R. §§ 284.13(b), 284.13(c), 284.13(d) and the NAESB Standards; (9) crediting of penalty collections under 18 C.F.R. § 154.501 and Southern Star's FERC Gas Tariff; and (10) cash management arrangements under 18 C.F.R. § 260.400. The audit covered the period from January 1, 2006 through May 30, 2008.

B. Southern Star Central Gas Pipeline, Inc.

Southern Star (formerly Williams Gas Pipelines Central, Inc.) is an indirect, wholly-owned subsidiary of GE Energy Financial Services, Inc. (GE Energy), a subsidiary of General Electric, and Caisse de depot et placement du Quebec (CDP).[6] GE

[1] 18 C.F.R. Part 201 (2007).

[2] 18 C.F.R. Part 260 (2007).

[3] 18 C.F.R. Part 284 (2007).

[4] 18 C.F.R. § 284.12 (2007).

[5] FERC Gas Tariff, Original Volume No. 1.

[6] In 2002, Williams Gas Pipeline Company sold the assets of Williams Gas Pipelines Central to Southern Star Central Corp., a subsidiary of AIG Highstar Capital, L.P. In 2003, GE Energy acquired two percent of Southern Star. In 2005, GE acquired an additional 58% of Southern Star and CDP acquired 40% of Southern Star. Southern Star has been managed and operated out of Owensboro, Kentucky since 2002.

Energy has 60% indirect ownership and CDP has 40% indirect ownership, with each having 50% of the voting rights.

Southern Star is an interstate natural gas transmission company that owns and operates a natural gas pipeline system that includes facilities for natural gas transmission and storage. The pipeline system is 6,000 miles long and operates in Colorado, Kansas, Missouri, Nebraska, Oklahoma, Texas, and Wyoming. Southern Star's storage facilities include eight underground fields. Together, the storage fields have approximately 43 Bcf of working gas capacity and approximately 1.2 Bcf of storage delivery capacity.

Southern Star did not have service agreements with its affiliates, nor did affiliates conduct business on the Southern Star system through the capacity release program during the audit period.

C. Summary of Compliance Findings

Audit staff's review identified the following five compliance issues:

- *Filing Non-Conforming Contracts with the Commission:* Southern Star did not file all contracts containing material deviations with the Commission as required by 18 C.F.R § 154.1(d) (2007).

- *Index of Customers Filings and Web site Postings:* Southern Star did not file its Index in compliance with the Commission's electronic filing instructions. Additionally, Southern Star did not post its Index in the format required by the Commission's electronic filing instructions and the NAESB business practice and electronic communications standards as required by 18 C.F.R §§ 284.12 and 284.13 (2007).

- *Capacity Auctions:* Southern Star did not post for bid expiring capacity under one contract as required by its FERC-approved tariff.

- *Fuel and Lost and Unaccounted for Gas Reporting:* Southern Star failed to report gas received from shippers for fuel separately from gas received for lost and unaccounted for gas in its Form 2. Additionally, Southern Star did not report storage system losses on its Form 2 as required by the Commission's Form 2 instructions.

- *Other Web site Postings:* Southern Star did not post the transactional report (TR) and the available capacity report (ACR) postings in compliance with Commission regulations and NAESB business practice and electronic communications standards as required by 18 C.F.R §§ 284.12 and 284.13 (2007).

D. Summary of Recommendations

We recommend that Southern Star:

- Establish, implement, and then update as needed, written policies and procedures to ensure Southern Star:

  - Files all contracts containing non-conforming terms and conditions with the Commission.
  - Files and posts all Indices in compliance with Commission rules and regulations.
  - Performs capacity auctions in compliance with its tariff and Commission rules and regulations.
  - Reports accurate and complete data for fuel and lost and unaccounted for gas on Southern Star's Form 2.
  - Posts all web site postings in compliance with Commission rules and regulations.

- Within 120 days following the issuance of the final audit report in this docket, Southern Star will submit to the DA, a master list of all currently effective agreements indicating whether each agreement contains material non-conforming terms and conditions. For agreements that contain material non-conforming terms and conditions, Southern Star will indicate whether it filed the agreements with the Commission.

- Within 120 days following the issuance of the final audit report in this docket, Southern Star will submit to the DA, a matrix similar to the format filed in Docket No. RP07-120-000, eLibrary Accession No. 20070103-0062, of unfiled agreements that contain material non-conforming terms and conditions in effect on the issuance date of the audit report. To determine what agreements contain material deviations, Southern Star will apply the definition of material deviation contained in the Negotiated Rate Policy Statement.[7] DA may then request a copy of any or all listed contracts.

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[7] *Natural Gas Pipeline Negotiated Rate Policies and Practices*, 104 FERC ¶ 61,134 (2003), *order on reh'g and clarification*, 114 FERC ¶ 61,042 at P 27 (2006) (Negotiated Rate Policy).

- Within 120 days following the issuance of the final audit report in this docket, Southern Star will submit a statement to the DA, signed by a member of Southern Star's senior management, attesting to the accuracy of all information contained in both the master list of effective agreements and the matrix listing all unfiled agreements that contain material non-conforming terms and conditions.

- Within 150 days of the issuance of the final audit report, file with the Commission under section 154.1(d) of the Commission's regulations all unfiled agreements that contain material non-conforming terms and conditions.

- Re-file and archive corrected Indices for the period January 1, 2007 to January 1, 2008.

- Re-file Form 2 with corrected Gas Account pages for 2006 and 2007.

- Review all transactional and available capacity web site postings for compliance with the Commission's regulations and NAESB's standards and correct all inaccurate or incomplete postings.

E. Compliance and Implementation of Recommendations

Audit staff further recommends that Southern Star:

- Submit for audit staff's review Southern Star's plans for implementing audit staff's recommendations. The Company should provide these plans to audit staff within 30 days of the issuance of the Final Audit Report in this docket.

- Submit quarterly reports to OE describing the Company's progress in completing each corrective action recommended in the Final Audit Report in this docket. The Company should make the quarterly filings no later than 30 days after the end of each calendar quarter, beginning with the first quarter after the Final Audit Report in this docket is issued, and continuing until the Company completes all the recommended corrective actions.

- Submit copies of any written policies and procedures developed in response to the recommendations in the Final Audit Report. The Company should submit these policies and procedures for audit staff's review in the first quarterly filing after the Company completes these products.

II. Introduction

A. Objective

The objectives of the audit were to determine how and whether Southern Star complied with selected accounting, reporting, and transportation regulations as enumerated above. To accomplish the objectives, audit staff reviewed data and evaluated actions taken by the Company before and during the period of the audit, i.e. January 1, 2006 through May 30, 2008. Actions taken by the Company subsequent to the close of the audit period are noted in this audit report.

B. Scope and Methodology

The steps audit staff employed to evaluate the Company's compliance included the following:

- Reviewing a large number of publicly-available materials prior to commencement of the audit on October 1, 2007, including the Company's filings to the FERC, select filings to the Securities and Exchange Commission, national and local news clippings and trade press articles, the Company's FERC approved gas tariff, and all public information available on the Company's web site.

- Identifying the standards and criteria audit staff would use to evaluate the Company's compliance with each of the ten objectives within the scope of the audit. These standards and criteria included rules, regulations, and other requirements related to capacity auctions, fuel retainage, lost and unaccounted for gas retainage, service agreements, Index filings, Form 11 filings, certain Form 2 information, web postings, crediting of penalty collections, and cash management arrangements.

- Conducting two site visits to the Company's headquarters in Owensboro, KY. The site visits facilitated audit staff's ability to:

    - pose clarifying questions about the Company's operations, processes, and procedures;
    - interview Company personnel, particularly those engaged in activities that relate to the ten objectives under audit;
    - test the controls employed by the Company to ensure compliance with FERC's requirements; and

  - test the service agreements and the web site postings to ensure accuracy, completeness, and compliance with FERC's requirements.

- Conducting qualitative and quantitative tests on data provided by the Company (e.g. to ensure web site postings were complete, accurate, and in the format required by FERC) to determine whether such data were consistent with data filing requirements, web site posting requirements, and other requirements associated with the scope of the audit.

- Holding discussions with Company personnel, primarily to clarify questions about the Company's responses to data requests and preliminary observations made by the audit staff during the site visits.

- Conferring with other FERC staff on various compliance issues to ensure that audit findings would be wholly consistent with FERC precedent and policy. For example, audit staff conferred with the Office of General Counsel and the Office of Energy Market Regulation regarding the non-conforming terms and conditions contained in the Company's service agreements.

Audit staff also performed a number of specific actions to evaluate the Company's compliance with all relevant requirements of the ten objectives within the scope of this audit. A description of these actions follows.

In order to evaluate compliance with capacity auction requirements, audit staff reviewed the Company's FERC-approved gas tariff to determine the process FERC approved for Southern Star's capacity auctions. Audit staff interviewed Southern Star's employees to determine what process they used to conduct the capacity auctions. Audit staff compared the two processes to determine if the employee's processes adhered to the FERC-approved tariff.

Audit staff obtained a list of expiring contracts from the Company and from the Company's secure web site. Audit staff evaluated four expiring contracts to determine if Southern Star complied with the Company's requirements for expiring contracts as outlined in its tariff. The tests included verifying that Southern Star posted the available capacity, accepted bids, determined the best bid, and notified the existing capacity holder of the best bid or otherwise extended the contract in accordance with its FERC-approved tariff.

With respect to the fuel and loss retainage, audit staff reviewed the Company's tariff to determine Southern Star's process for recovery of gas used for fuel and gas lost due to pipeline operations. Audit staff interviewed the Regulatory Staff Analyst, Manager of Rates and Strategic Planning, and Manager of Scheduling and Billing to determine how Southern Star recovered gas used for fuel and operation of the pipeline.

Audit staff then compared the tariff-approved process to actual practice to determine if the employee's processes adhered to the tariff.

Audit staff verified Southern Star's fuel used and natural gas losses (F&L) tied to its books and records, discounted fuel in accordance with its tariff, and reported F&L in accordance with the Form 2 filing instructions.

To evaluate whether Southern Star had processes in place to ensure it filed service agreements containing non-conforming terms and conditions in conformance with the regulations,[8] audit staff interviewed Southern Star's employees who processed service agreements. To determine if Southern Star filed all service agreements containing non-conforming terms and conditions, audit staff tested a random sample of transportation contracts and associated agreements. The sample represented contracts of each rate schedule type for both firm and interruptible services. Audit staff selected a sample of (1) 53 firm transportation (FT) contracts out of 210 FT contracts, or 25% of the total number of FT contracts (2) 69 interruptible transportation (IT) contracts, or 20% of the total population of 345 IT contracts (3) 60 facility construction, ownership, and operations (COO) contracts, or 12% of the total population of 504 COO contracts, and (4) 74 capacity release contracts from a total population of 208 capacity release contracts, or 36% of the population. The audit tests involved comparing the service agreements; COO agreements; capacity release contracts; letter agreements; discount agreements; and other documentation in the files, to the various tariff requirements and *pro forma* service agreements (PFSA) contained in Southern Star's tariff over the last 16 years.

With respect to the Index filing and posting requirements, audit staff reviewed the July 2006 and July 2007 Indices filed with FERC and the July and October 2007 Indices posted on Southern Star's web site. Audit staff performed a number of tests to ensure the accuracy and completeness of Southern Star's Index filings and postings. The tests audit staff performed to determine whether Southern Star filed and posted accurate Indices included verifying the Company had identified all affiliates, firm rate schedules, and bundled services on the Indices. In addition, audit staff compared the Index filed July 2007 to the Index filed July 2006 to determine if the Company reported its contract information consistently. Audit staff followed up all inconsistencies. Furthermore, audit staff tested the accuracy and completeness of the Indices. Audit staff compared the contents of the contracts in the sample to the information contained in the Index filings and postings to verify the Company reported accurate and complete information for the service agreements in the sample. The sample contained 25% of all firm service agreements, or 53 firm service agreements out of a population of 210 firm service

[8] A contract provision is non-conforming if the provision in the contract or service agreement deviates in any material aspect from the form of service agreement in the tariff (18 C.F.R. § 154.1(d)).

agreements. In addition, audit staff tested the Index posted on the Company's web site for compliance with FERC's regulations and the NAESB standards.

For the Form 11 analysis, audit staff reviewed each Form 11 filed during the period January 2006 through September 2007. Audit staff compared the Company's Form 11s filed on November 13, 2006 and August 10, 2007 to the FERC's electronic filing instructions for compliance. Furthermore, audit staff tested the November 2006 and August 2007 filings for accuracy and completeness. To accomplish this, audit staff reviewed Southern Star's trial balance and billing records to verify the quantities and dollars Southern Star reported in each Form 11 were accurate.

After discussions between audit staff and Southern Star personnel during the audit, Southern Star filed a request for waiver to depart from the instructions for filing Form 11 and Form 2. The requested waiver was granted by the Chief Accountant.[9] In its request for a waiver, Southern Star argued the proposed departures from the filing instructions would enhance market transparency. Specifically, Southern Star requested waiver to report the components of a bundled service separately. For example, Southern Star requested waiver to report the transportation revenues and quantities as transportation and the storage revenues and quantities as storage.

In order to evaluate compliance with FERC's TR posting requirements, audit staff interviewed a Scheduling Representative and a Contract and Customer Service Representative to determine the procedures and control processes the Company relied on to produce accurate, complete, and timely reports. Audit staff tested a sample of 135 service agreement files to determine if Southern Star posted all pertinent data accurately and completely. Additionally, to ensure the report postings complied with the FERC-approved NAESB standards, audit staff compared the transactional report postings to the NAESB standards.

Audit staff evaluated Southern Star's ACR against the requirements of the Commission's regulations and the FERC-approved NAESB standards related to the ACR. Additionally, audit staff interviewed a Contract Representative and Customer Services employee, as well as a Scheduling Representative to determine if the Company's procedures and control processes were sufficient to ensure compliance with FERC's regulations and orders. Audit staff compared the ACR postings to the NAESB standards to ensure the ACRs conformed to the posting requirements.

To ensure accurate and complete ACR postings, audit staff tested a sample of 96 receipt and delivery points in the unsubscribed capacity reports, 15% of the total population of 645 receipt and delivery points, and 194 points, 30% of the total

[9] *Southern Star Central Gas Pipeline, Inc.*, Docket No. AC08-120-000 (August 5, 2008) (unpublished letter order).

population, reported in the operationally available capacity report. These tests included comparing the design capacity from the Location Details report posted on Southern Star's web site to the design capacity reported in the ACR. In addition, audit staff verified the accuracy of the unsubscribed capacity reported on the ACR by calculating the unsubscribed capacity and comparing that calculation to the unsubscribed capacity reported on the ACR. For the calculation, audit staff subtracted the subscribed capacity, which was the total capacity reported on the Index for each point, from the design capacity reported on the Location Details report.

With respect to the crediting of penalty collections, audit staff reviewed Southern Star's FERC-approved gas tariff as it relates to penalty collections, reviewed the Company's policies and procedures, and interviewed personnel involved in the collection, reporting, and refunding of penalty collections. In addition, audit staff reviewed the 2007 Annual Operational Flow Order Report and the 2007 Annual Cash-Out Refund Report that Southern Star filed with FERC for accuracy. After reviewing all invoices for a three-month period, audit staff selected a sample of 24 invoices. The sample was comprised of invoices for three consecutive months for eight shippers, which were all of the shippers that met the requirements in Southern Star's FERC-approved gas tariff for cash-out penalties. Audit staff verified Southern Star calculated the amount of cash-out payments and Operation Flow Order (OFO) penalties in accordance with its tariff. Audit staff verified Southern Star applied the appropriate tolerance levels and rates in calculating imbalance and cash-out penalties.

In order to evaluate Southern Star's compliance with FERC's cash management program, audit staff reviewed Southern Star's cash management filing made with FERC, its 2006 Form 2, and the cash management agreement. Audit staff interviewed management and non-management employees involved in the cash management program. In addition, audit staff performed tests to determine if Southern Star filed the cash management agreement and any changes to the agreement within the appropriate period; computed its proprietary capital ratios accurately; and maintained supporting documentation for all deposits into the cash management program, borrowings from the cash management program, and interest income and expense associated with the cash management program, as required by the Uniform System of Accounts.[10]

[10] 18 C.F.R. Part 201, Account No. 146, Accounts Receivable from Associated Companies (2007).

III. Compliance Findings and Recommendations

1. Filing Non-Conforming Contracts with the Commission

Southern Star did not file at least twenty-nine contracts containing material deviations with the Commission.

Pertinent Guidance

The Commission's regulations at 18 C.F.R. § 154.1(d) (2007) requires that any contract or executed service agreement that deviates in any material aspect from the form of service agreement in the tariff is subject to the filing requirements of Part 154. In its Negotiated Rate Policy Statement,[11] the Commission, citing *Columbia*,[12] defined a material deviation as any provision of a service agreement that (1) goes beyond the filling-in of the spaces in the form of service agreement with the appropriate information provided for in the tariff and (2) that affects the substantive rights of the parties. In *Columbia*, the Commission stated that a pipeline must file any contract containing a material deviation from the form of service agreement as a non-conforming agreement.[13]

Additionally, in *Tennessee Gas Pipeline Company and East Tennessee Natural Gas Company*,[14] the Commission stated it allows parties to negotiate additional "mutually" agreeable differences; however, these negotiated differences cannot substantially alter the approved form of service agreement in the tariff.[15] Furthermore, the Commission stated, "neither the pipeline nor the customer can insist on any changes to the form of service agreement accepted by the Commission."[16]

[11] *Negotiated Rate Policy*, 104 FERC ¶ 61,134, at FN 3 (2003), *order on reh'g and clarification*, 114 FERC ¶ 61,042 (2006).

[12] *Columbia Gas Transmission Corp.*, 97 FERC ¶ 61,221 at 62,002 (2001) (*Columbia*).

[13] *Id.* at 62,001.

[14] *Tennessee Gas Pipeline Company and East Tennessee Natural Gas Company*, 65 FERC ¶ 61,356 (1993).

[15] *Id.* at 62,907.

[16] *Id.* at 62,907.

Background

Audit staff reviewed 272 individual contracts or agreements of the total population of 1267 Southern Star firm and interruptible transportation and storage agreements, pooling services agreements, park and loan agreements and COO agreements. To determine whether there were any contracts that contained non-conforming material deviations. Audit Staff compared the agreements and related documents to the PFSA in effect at the time the parties signed the agreement and the currently effective PFSA in Southern Star's tariff. Specifically, Audit staff analyzed 53 of Southern Star's 210 firm transportation agreements (FTS) and identified 25 with material non-conforming deviations. Of the 25 contracts with material non-conforming deviations, five were executed or amended by Southern Star and the remainder had been executed by Southern Star's predecessor. Audit staff also reviewed 69 interruptible transportation agreements and identified four with non-conforming deviations[17] to the PFSA in Southern Star's tariff.

Examples of the non-conforming terms and conditions audit staff identified during the review include, but are not limited to:

- A letter agreement stating the Company will include $4 million in its capital program for October 1, 1996 through September 30, 2001 to upgrade the mainline to maintain or enhance service to the Shipper. Additionally, the Shipper can designate potential projects for such capital expenditures through September 2000.
- Two FT contracts transferred to another shipper without going through capacity release.
- A letter agreement stating, due to competitive offers, the Company will pay the Shipper $2.5 million in contribution in aid of construction to replace 9 miles of the 10 existing miles of the Shipper's pipe due to the shipper's competitive transportation alternatives, and the Shipper will support Southern Star's efforts to recover the $2.5 million through the Company's rates.
- A letter agreement stating the Company will pay a third party $210,000 to upgrade the third party's system to deliver gas to the shipper while the Company performed Department of Transportation testing and disrupted the shipper's service. In exchange, the third party would commit to a five-year FTS contract at 3,300 Dth at maximum rate and the Shipper will exercise its rights to extend the contract an additional two years.

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[17] Although the deviations are considered material because they go beyond "filling in the blank" (they do not accurately reflect which state's contract law would govern a dispute), one deviation occurred before Southern Star took control and three occurred shortly after Southern Star took over operations of the pipeline.

- A Trans-Storage Service (TSS) contract containing an adverse action early out clause, alternative dispute clause, qualified offer early out clause, and Account 191 early out clause.
- Contracts indicating a state different from the state listed in the PFSA as the state whose laws will control.

Commission precedent, as noted above, defines a material deviation as any provision of a service agreement that (1) goes beyond the filling-in of the spaces in the PFSA with the appropriate information provided for in the tariff and (2) that affects the substantive rights of the parties. The provisions audit staff identified were not in the PFSA, go beyond filling in the spaces of the PFSA, and affect the substantive rights of at least one of the parties. Therefore, these provisions contain material deviations from the PFSA.

Audit staff's interviews of Southern Star employees and review of Southern Star's internal documents also revealed that Southern Star had no written policies or procedures to ensure compliance with FERC requirements or a FERC regulatory compliance program.

Recommendations

We recommend Southern Star:

1. Establish, implement, and then update as needed, written policies and procedures to ensure Southern Star files all contracts containing non-conforming terms and conditions with the Commission.

2. Within 120 days following the issuance of the final audit report in this docket, Southern Star will submit to the DA a master list of all currently effective agreements indicating whether each agreement contains material non-conforming terms and conditions. For agreements that contain material non-conforming terms and conditions, Southern Star will indicate whether it filed the agreements with the Commission and provide the docket number under which Southern Star filed each agreement.

3. Within 120 days following the issuance of the final audit report in this docket, Southern Star will submit to the DA, a matrix similar to the format filed in Docket No. RP07-120-000, eLibrary Accession No. 20070103-0062, of unfiled agreements that contain material non-conforming terms and conditions in effect on the issuance date of the audit report. To determine what agreements contain material deviations, Southern Star will apply the definition of material deviation contained in the Negotiated Rate

Policy Statement at P 27. DA may then request a copy of any or all listed contracts. DA reserves the right to take further action it deems appropriate after its review of the information provided by Southern Star.

4. Within 120 days following the issuance of the final audit report in this docket, Southern Star will submit a statement to the DA, signed by a member of Southern Star's senior management, attesting to the accuracy of all information contained in both the master list of effective agreements and the matrix listing all unfiled agreements that contain material non-conforming terms and conditions.

5. Within 150 days of the issuance of the final audit report, file with the Commission all unfiled agreements that contain material non-conforming terms and conditions.

2. Index of Customers Filings and Web site Postings

Southern Star did not file its Index in compliance with the Commission's electronic filing instructions. Additionally, Southern Star did not post its Index in the format required by the Commission's electronic filing instructions and the NAESB business practice and electronic communications standards.

Pertinent Guidance

The Commission's regulations at 18 C.F.R. § 284.13(c) (2007) require, on the first business day of each calendar quarter, an interstate pipeline to file with the Commission an Index of all its firm transportation and storage shippers that complies with the requirements set forth by the Commission. In addition, an interstate pipeline must post the Index on its internet web site, in accordance with § 284.12 and the information must remain available until the next quarterly posting. The following information, in part, is required for each shipper receiving firm transportation services or storage services from the pipeline company: the full legal name and identification number, the effective and expiration dates of the contract, the maximum daily contract quantity for transportation service, and the maximum storage quantity for storage service.

The Commission's requirements for the Index are set forth in the "Instruction Manual for Electronic Filing of the Index" (Instructions) (June 2000). These instructions require the web site posting date and the filing date to be the first business day of each calendar quarter. Further, the instructions require the gas pipeline to enter one Header record per filing, one Details record for each combination of shipper/rate schedule/contract, as many Agent or Asset Manager records as needed per contract, as many Points records as needed per contract, and one footnote record per contract.

The Commission's regulations at 18 C.F.R. § 284.12 (2007) require interstate pipelines to abide by NAESB business practice and electronic communication standards. Standard 4.3.16 of the NAESB Wholesale Gas Quadrant (WGQ) Business Practice Standards, Book 1 of 2, version 1.7 (Standards) requires companies to post their Index and make a version available in a tab-delimited downloadable file. Further, Standard 4.3.35 of the NAESB WGQ Standards requires companies to display the column headings for the Index posted on the web site in the same order as in the Index filed with the Commission.

Additionally, the Commission's regulations at 18 C.F.R. § 284.12(b)(3) (2007) require interstate pipelines to provide the Index on the public web site, directly downloadable without the need for users to first view the Index on the web site, and the Index must provide the same content for all information regardless of the electronic format in which it is provided.

Background

Audit staff reviewed the July 1, 2007 Index Southern Star electronically filed with the Commission and the version posted to its internet web site to determine if Southern Star filed and posted a complete and accurate Index. Audit staff determined Southern Star filed and posted its July 1, 2007 Index, but it did not file or post it accurately or completely. Southern Star did not file the Index in the format required by the electronic filing instructions. The instructions require one Detail record, and as many Points records as needed, per contract; however, Southern Star reported multiple Detail records for several contracts and no Point records for other contracts.

Additionally, Southern Star did not report all of the required information accurately in either the filed or posted version of the July 1, 2007 Index. The Index did not report all shipper identification numbers, did not report accurate contract expiration dates, incorrectly reported daily maximum injection quantities in the maximum daily transportation column for certain storage contacts, and inaccurately reported certain contracts as negotiated rate contracts, when in fact, the contracts were discounted rate contracts. In addition, Southern Star posted the October 1, 2007 Index in September 2007; therefore, Southern Star did not keep the information from the July 1, 2007 Index posted for the required period.

Audit staff reviewed Southern Star's internet web site to determine whether it made available for download the July 1, 2007 Index in the format required by the Commission and NAESB. Southern Star posted an HTML version of its July 1, 2007 Index, but it did not make it available for download without first viewing it, nor did Southern Star make available the required tab-delimited downloadable version.

Audit staff compared the July 1, 2007 electronically filed Index to the July 1, 2006 electronically filed Index. As a result of the comparison, audit staff determined Southern Star filed an incomplete July 1, 2007 Index and an incomplete July 1, 2006 Index with the Commission. Both Indices were missing contracts in effect at the time of the filing. The July 1, 2007 Index was missing seven contracts and the July 1, 2006 Index was missing one contract.

After discussions held between audit staff and Southern Star personnel, Southern Star decided to perform an audit of its January 1, 2008 Index, testing the accuracy and completeness of every contract listed on the Index. To test the accuracy of the Southern Star audit, audit staff selected a sample of 19 contracts, or 10% of the population of 190 contracts. Audit staff compared the contract information in Southern Star's work papers with the supporting documentation in the contract files. Audit staff's tests confirmed Southern Star's results. Southern Star's review identified contracts listed in the Index that contained inaccurate information.

Recommendations

We recommend Southern Star:

6. Establish, implement, and then update as needed, written policies and procedures to ensure Southern Star files and posts all Indices in compliance with Commission rules and regulations.

7. Re-file corrected Indices for the period of January 1, 2007 to January 1, 2008.

8. Archive corrected Indices for the period of January 1, 2007 to January 1, 2008 on Southern Star's web site.

3. Capacity Auction

Southern Star did not post for bid expiring capacity under one contract as required by its FERC-approved tariff.

Pertinent Guidance

Section 6.2 of Southern Star's General Terms and Conditions in its FERC-approved tariff states Southern Star will post the availability of capacity under an expiring or terminating service agreement on its electronic bulletin board together with all applicable terms (including quantity and maximum rate) six months prior to the expiration or termination of any such service agreement. If the termination notice period under a service agreement is less than six months, Southern Star shall post the availability of such capacity after either party provides the other with a notice of termination.

Under section 6.1 of Southern Star's General Terms and Conditions, prior to the expiration of the term of an existing service agreement and prior to Southern Star's posting the available capacity, Southern Star and the existing capacity holder may mutually agree to an extension of the term of the service agreement with respect to all or part of the underlying capacity.

Background

Audit staff reviewed contracts nearing their termination dates to assess compliance with section 6 of Southern Star's General Terms and Conditions. In most cases, the contracts continued under evergreen provisions. In one case, Southern Star posted the capacity for bid. In some cases, existing capacity holders negotiated an extension of the term of the contract for all or a part of the underlying capacity before the required posting period, six months prior to the expiration of the contract.

Southern Star failed to post a portion of the expiring capacity for one of the contracts audit staff reviewed. Southern Star notified the existing capacity holder seven months prior to the expiration of the contract to allow the existing capacity holder the opportunity to extend the contract before the required posting of the capacity. The existing capacity holder elected to extend the contract for the portion of the capacity in one zone, but not for the capacity in the other zone. Southern Star provided no evidence to audit staff that it posted for bid the expiring capacity the existing capacity holder elected not to extend. Southern Star should have posted the capacity that the existing capacity holder elected not to extend in conformance with section 6 of the General Terms and Conditions of its tariff.

Recommendations

We recommend Southern Star:

9. Establish, implement, and then update as needed, written policies and procedures to ensure Southern Star performs capacity auctions in compliance with Commission rules and regulations and its tariff.

4. Fuel and Lost and Unaccounted for Gas Reporting

Southern Star failed to report gas received from shippers for fuel separately from gas received for lost and unaccounted for gas in its Form 2. Additionally, Southern Star did not report storage system losses in its Form 2.

Pertinent Guidance

Page 520 of Form 2 entitled Gas Account – Natural Gas includes separate lines for reporting Gas Received from Shippers as Compressor Station Fuel, Gas Received from Shippers as Lost and Unaccounted for, Transmission System Losses, and Storage System Losses. Interstate pipelines must report the respective information on the appropriate line.

Background

Natural Gas Received from Shippers as Lost and Unaccounted and Fuel Used

Audit staff reviewed page 520 of Southern Star's 2006 and 2007 Form 2 filings. Southern Star reported 7,428,753 Dth and 6,912,605 Dth, for 2006 and 2007 respectively, on line 13, Gas Received from Shippers as Lost and Unaccounted for and nothing on line 12, Gas Received from Shippers as Compressor Station Fuel. Audit staff questioned Southern Star about the reporting. Southern Star replied in a written response that:

> Southern Star reports all of the gas received from shippers, both gas received from shippers for compressor fuel and gas received from shippers for lost and unaccounted for, on line 13 of page 520 of the Form 2. The reason for this is that, while Southern Star does calculate a separate fuel rate and loss rate in its annual fuel filing, it charges shippers a total fuel reimbursement rate (both fuel and loss) and does not separately track or account for how much of the reimbursement is for fuel versus how much is for lost and unaccounted for gas.

Southern Star's tariff at section 13 of the General Terms and Conditions requires that Southern Star state a separate fuel and loss reimbursement percentage for the production area (transmission), the market area (transmission), and for storage. Southern Star lists its fuel reimbursement percentages on Sheet No. 12 of its FERC-approved tariff.

Section 13 also requires Southern Star to file revised fuel and loss reimbursement percentages each year based on actual experience for the preceding 12-month period ended September 30. Southern Star's annual fuel filing breaks down the fuel reimbursement percentages by storage and transmission. The total storage fuel reimbursement percentage is comprised of a storage fuel percentage, a storage loss percentage, a storage fuel surcharge percentage, and a storage loss surcharge percentage. The storage fuel percentage and the storage loss percentage are designed to permit Southern Star to recover storage fuel and storage losses in kind, respectively, in the upcoming period. The storage fuel surcharge percentage recovers the difference between actual storage fuel used and the quantity retained in kind for fuel used during the prior 12-month period. The storage loss surcharge percentage recovers the difference between actual storage losses and the quantity retained in kind for such losses during the prior 12-month period.

The total transmission fuel reimbursement percentage, for both the production area and the market area, consists of a separate transmission fuel percentage and a transmission loss percentage to recover both fuel used and natural gas lost, respectively, in the upcoming period. Southern Star calculates a single transmission surcharge percentage to recover the difference between actual fuel used and natural gas lost and the quantity retained in kind for fuel used and natural gas lost during the prior period.

Since, in its annual fuel filing, Southern Star calculates a storage fuel percentage, a storage fuel surcharge percentage, and a transmission fuel percentage, Southern Star could calculate the amount to report on line 12, Gas Received from Shippers as Compressor Station Fuel by multiplying the appropriate actual quantities received, either transmission or storage, by the respective fuel percentages. Similarly, Southern Star could report the correct amount on line 13, Gas Received from Shippers as Lost and Unaccounted For, by multiplying the storage loss percentage, storage loss surcharge percentage, and transmission loss percentage by the appropriate quantities stored or transported. Audit staff, however, acknowledges that because Southern Star does not calculate a separate surcharge percentage for transmission losses and transmission fuel used, Southern Star cannot divide and apply the transmission surcharge percentage to quantities transported to calculate accurately the portion attributable to lost and unaccounted for gas, and the portion attributable to fuel used.

After further discussions regarding the reporting of gas received for fuel and losses, Southern Star volunteered to improve its reporting of fuel used, and lost and unaccounted for volumes. It will report fuel quantities based on amounts received through the storage fuel percentage, storage fuel surcharge percentage, and transmission fuel percentage. It will report lost quantities based on the storage loss percentage, storage loss surcharge percentage, and transmission loss percentage. Southern Star will include the total transmission surcharge receipts on either line 12 or 13, and include a footnote breaking out the portion of the reported number attributable to the transmission surcharge percentage estimating how much it received for fuel and how much it received for lost and unaccounted for gas.

Storage and Transmission System Losses

Form 2 requires separate reporting for transmission and storage system losses on lines 32 and 34 of page 520, respectively. Southern Star reported Transmission System Losses of 939,449 Dth and 1,322,421 Dth in the 2006 and 2007 Form 2 filings, respectively. However, Southern Star reported no Storage System Losses on the 2006 and 2007 Form 2 filings.

Audit staff reviewed Southern Star's annual fuel filing submitted in Docket No. RP07-96-000 filed on December 1, 2006 as part of this audit. In that filing, Southern Star reported actual storage losses of 2,110,215 Dth for the twelve-month period ending September 30, 2006. Southern Star should have reported its actual storage losses in its Form 2 since according to its annual fuel filing it had such losses. Southern Star should have reported actual storage loss quantities on the Gas Account page as instructed.

Recommendations

We recommend Southern Star:

10. Review the quantities reported on the Gas Account pages for 2006 and 2007 to ensure Southern Star reports the correct quantities in accordance with the instructions for that page of the Form 2.

11. Establish, implement, and then update as needed, written policies and procedures to ensure accurate and complete reporting of fuel and lost and unaccounted for gas on Southern Star's Form 2.

12. Re-file the Form 2 with corrected Gas Account pages for 2006 and 2007.

5. Other Web site Postings

Southern Star did not post the TR and the ACR postings (collectively, web site postings) in compliance with Commission regulations and NAESB business practice and electronic communications standards.

Pertinent Guidance

The Commission's regulations at 18 C.F.R § 284.12(b)(3) (2007) require that all electronic information provided and electronic transactions conducted by a pipeline be provided on the public internet. For documents posted on the web site, users must be able to search the entire document, copy selected portions of the document, and download the document without the need to first view it. Finally, pipelines must maintain posted documents for three years.

The Commission's regulations at 18 C.F.R. § 284.13(b) (2007) require interstate pipelines to post on the internet reports on firm transportation and interruptible transportation services in conformity with 18 C.F.R. § 284.12 and maintain access to the reports for 90 days. Section 284.13(b)(1) requires pipelines to post the reports for the original contract and each revision of the contract.

The Commission's regulations at 18 C.F.R. § 284.12 (2007) require interstate pipelines to abide by the NAESB business practice and electronic communication standards. The Technical Implementation of Business Process for Transactional Reporting, of NAESB's WGQ Capacity Release Related Standards, version 1.7 establishes the required format for the web site postings of the TRs and ACRs.

Background

Audit staff reviewed Southern Star's web site to determine whether it posted and made available for download the firm transportation TRs, interruptible transportation TRs, capacity release TRs, and ACRs in the format required by the Commission and NAESB. In addition, audit staff reviewed Southern Star's web site postings to determine if it posted all of the required information and maintained the postings for the required three years.

Transactional Reports

Southern Star did not reflect changes to its discount agreements in the TRs. While on site, audit staff held a discussion with the Manager of Contract Administration regarding Southern Star's discount agreements. Section 284.13(b)(1)(iii) requires pipelines to report the rate charged under the contract in its TRs. Section 284.13(b)(1) also requires the reporting of the rate charged when the pipeline revises the contract. The Manager of Contract Administration informed audit staff that Southern Star did not consider rate changes to be changes that warranted a posting in the TRs. Shortly after the discussion, Southern Star informed audit staff that it would reflect the rate changes in the TRs. Southern Star changed provisions not involving the rate charged in eight of the 135 contracts audit staff tested; however, audit staff was not able to locate the posting of the changes.

Southern Star did not post all of the information required by the NAESB standards nor did it label all of the columns correctly in the TR. Some of the information Southern Star did not include in the TR includes, but is not limited to, the posting time, rate ID or description, report level, surcharge ID, surcharge indicator, and the transportation service provider DUNS numbers.

While on site, audit staff met with Southern Star's contract and information technology employees regarding the TRs. Southern Star has made the necessary changes to the TR. The TR now includes the required information and the columns are labeled correctly.

Available Capacity Reports

The ACRs consist of two types of reports, the unsubscribed capacity report (UCR) and the operationally available capacity report (OACR). Audit staff tested Southern Star's UCRs for completeness and accuracy. Audit staff's calculation of the unsubscribed capacity differed from the reported unsubscribed capacity for 65 of the 96 points tested, or 47%. Audit staff calculated the unsubscribed capacity for each point by subtracting the subscribed capacity from the design capacity. Audit staff determined the subscribed capacity from the data reported on the Index. Southern Star's secure web site contains a report query for each point. This report includes the design capacity for each point. Southern Star confirmed that audit staff calculated unsubscribed capacity correctly.

Because of the audit staff's findings, Southern Star reviewed all of the point information and updated the totals reported on the UCR. Southern Star informed audit staff that it entered its design capacity manually. Its review confirmed some of the information was incorrect. Audit staff tested all 96 points again. During the second test, audit staff documented that Southern Star had changed the design capacity for 13 points since audit staff's first test. After audit staff's second test, three of the 96 points tested, reported a different total for unsubscribed capacity than the total calculated by audit staff.

Southern Star's UCR did not contain all of the NAESB required information. The required data missing from Southern Star's UCR includes, but is not limited to, the location quantity type indicator, and the transportation service provider DUNS number.

Audit staff tested Southern Star's operationally available capacity report (OACR) for completeness by testing a sample of 97 points, 15% of the total population of points.

During the initial testing of Southern Star's OACRs, audit staff noticed the design capacity data on the October 16, 2007 report was different from the design capacity data on the October 11, 2007 report for certain locations. Audit staff interviewed Southern Star's Gas Control Manager; he informed us that Southern Star formatted the report so it would show the full design capacity unless the operational capacity was less than the design capacity. In that case, the report would replace the design capacity with the operational capacity. Because of this discussion, Southern Star updated the report so that it reported design capacity for all locations.

Audit staff tested the OACRs for completeness and accuracy after Southern Star made the correction for the reporting of design capacity. Southern Star's OACR did not contain all of the information required by NAESB. The missing information includes, but is not limited to, the location quantity type indicator and the transportation service provider DUNS number. The OACR did report the IT indicator; however, Southern Star was not reporting the information correctly.

According to NAESB, the transmission service provider must mark the IT indicator column if the pipeline had no operationally available capacity at a point and IT service was being used. Southern Star marked the IT indicator column if there was operationally available capacity at a point and IT service was available. Audit staff held discussions with Southern Star concerning the IT indicator; because of these discussions, Southern Star is now using the IT indicator as required.

Recommendations

We recommend Southern Star:

13. Establish, implement, and then update as needed, written policies and procedures to ensure Southern Star posts all web site postings in compliance with Commission rules and regulations and NAESB standards.

14. Review all web site postings for compliance with the Commission and NAESB regulations and correct all inaccurate or incomplete postings.

SOUTHERN STAR
CENTRAL GAS PIPELINE

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LEGAL DEPARTMENT

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September 2, 2008

Bryan K. Craig, Director
Division of Audits
Federal Energy Regulatory Commission
888 First Street, N.E.
Room 51-37
Washington, D.C. 20426

Re: Southern Star Central Gas Pipeline, Inc.
Office of Enforcement
Docket No. PA08-1-000
Letter Dated August 20, 2008

Dear Mr. Craig:

The Division of Audits within the Office of Enforcement has completed an audit of Southern Star Central Gas Pipeline, Inc. (Southern Star) for the period January 1, 2005 through May 30, 2008. This letter is intended to respond to the draft audit letter (Letter) dated August 20, 2008, referred to above wherein the Division of Audits recommended corrective action on the five findings of non-compliance addressed in this letter below. The Letter requested that Southern Star respond, in writing, to the audit findings and recommendations within 15 days, indicating its agreement or disagreement with the audit findings, the corrective action planned, or taken, or if Southern Star disagrees with any conclusion, an explanation of why and a description of an alternative action. Southern Star responds as follows:

I. **Filing Non-Conforming Contracts With the Commission**

Southern Star agrees with the audit staff's finding that it did not file all contracts containing material deviations with the Commission as required by 18 CFR §154.1(d)(2007). Southern Star agrees as recommended by the audit staff to:

1. Within 30 days of the issuance of the Final Audit Report, file its plans to implement the audit staff recommendations regarding establishment, and implementation and updating of written policies regarding the filing of all contracts with non-conforming terms and conditions with the Commission;

2. Submit a master list of all currently effective transportation service agreements, discount agreements and construction and operating agreements (Agreements) indicating whether each Agreement contains material non-conforming terms and conditions, and if so, if the

Agreement was ever filed with the Commission for that purpose and for those that were filed, the docket number;

3. Submit a matrix similar to the format filed in Docket No. RP07-120-000, e-Library Accession No. 20070103-00052, of non-filed Agreements that contain material non-conforming terms and conditions as defined in the Negotiated Rate Policy Statement in effect on the issuance date of the audit report[1]; and

4. Submit a statement, signed by a member of Southern Star's Senior Staff, attesting to the accuracy of all information contained in both the master list of effective Agreements and the matrix listing all non-filed Agreements that contain material non-conforming terms and conditions.

With respect to the last three recommendations above, Southern Star fully understands that it must complete a thorough review sufficient to satisfy the Commission's concerns and to satisfy its senior management of the accuracy and completeness of the information to be filed with the Commission. To do so, it must review in detail every currently effective transportation service agreement, all effective discount agreements and every effective construction and operating agreement for existing facilities on its system. Because of the magnitude of this level of review of over 1,000 Agreements Southern Star believes that a 120 day time period would lead to a more thorough and useable result and avoid the necessity of requesting an extension.

Although Southern Star has already started its contract review as a result of concerns and questions from the audit staff, it has limited the number of people conducting this review to two employees, a Staff Attorney and the Manager of Contract Administration, in order to ensure accuracy and consistency. Southern Star believes that it is primarily these two employees who need to be involved in the creation of the master list and matrix in order to ensure the highest level of accuracy and consistency. Southern Star is committed to allow these two employees to devote the vast majority of all their time to this task and will shift these employee's day to day responsibilities to other employees to the maximum extent possible.

Therefore, Southern Star requests that the deadline for such filings be extended from the current deadline of 90 days following the issuance of the final audit report, to 120 days from that date.

II. Index of Customer Filings and Website Postings

Southern Star agrees that it did not file its Index of Customers (Index) in compliance with the Commission's electronic filing instructions, nor post its Index in the format required by the Commission's electronic filing instructions and the NAESB business practice and electronic communications standards as required by 18 CFR §284.12 and 284.13(2007). Southern Star already has corrected, as of March 1, 2008, the issues pointed out by the audit staff with the filing of its Index and the posting of the same, and is currently in compliance with the Commission's instructions and the NAESB standards, as instructed by the audit staff. Southern Star agrees to:

1. Within 30 days of the issuance of a Final Audit Report, file its plan to implement the audit staff's recommendations regarding the establishment, implementation and updating of written policies regarding the filing and posting of all Indices in compliance with Commission's rules and regulations.

[1] *Natural Gas Pipeline Negotiated Rate Policies and Practices*, 104 FERC ¶61,134 (2003), *order on reh'g and clarification*, 114 FERC ¶61,042 at P 27 (2006).

2. Within 30 days of the issuance of a Final Audit Report, re-file corrected indices for each quarter for the period of January 1, 2007 to January 1, 2008.

3. Within 30 days of the issuance of a Final Audit Report, archive corrected indices for the period of January 1, 2007 to January 1, 2008 on its website.

III. **Capacity Auctions**

Southern Star agrees that it did not post for bid expiring capacity under one contract as required by its FERC tariff.

Southern Star agrees that within 30 days of the issuance of a Final Audit Report, it will file its plan to implement the audit staff's recommendations regarding the establishment, implementation and updating of written policies and procedures to ensure Southern Star performs capacity auctions in compliance with Commission rules and regulations and its tariff.

IV. **Fuel and Lost and Unaccounted for Gas Reportings**

Southern Star agrees that it failed to report gas received from shippers for fuel separately from gas received for lost and unaccounted for gas in its Form 2 for the reasons discussed in the draft audit report, nor did it report storage system losses in its Form 2.

Southern Star agrees to:

1. Within 30 days of the issuance of the Final Audit Report, file its plans to implement the audit staff recommendations regarding establishment, implementation and updating of written policies and procedures to ensure accurate and complete reporting of fuel and lost and unaccounted for gas on Southern Star's Form 2.

2. Within 90 days of the issuance of the Final Audit Report, review the quantities reported on the Gas Account pages for 2006 and 2007 to ensure Southern Star reports the correct quantities in accordance with the instructions for that page of the Form 2 as agreed with the audit staff, and file the Form 2 with corrected pages for 2006 and 2007.

V. **Other Website Postings**

Southern Star agrees it did not post the TR and the ACR postings in compliance with Commission regulations and NAESB business practice and electronic communication standards.

Southern Star has already corrected, as of March 1, 2008, the issues pointed out by the audit staff in regards to the TR and the ACR and the posting of the same, and is currently in compliance with the Commission's instructions and the NAESB Standards, as instructed by the audit staff.

Southern Star agrees to:

1. Within 30 days of the issuance of the Final Audit Report, file its plans to implement the audit staff's recommendations regarding establishment, implementation and updating of written policies and procedures to ensure Southern Star posts all required website postings in compliance with Commission rules and regulations and NAESB standards.

2. Within 120 days of the issuance of the Final Audit report, review all required website postings for compliance with Commission and NAESB regulations and correct all inaccurate or uncompleted postings.

VI. **Additional Recommendations**

Southern Star also agrees that within 30 days of the issuance of the Final Audit Report to submit more detailed plans to audit staff for implementing audit staff's recommendations.

Southern Star further agrees to submit quarterly reports to the Office of Enforcement describing its progress in completing the corrective actions recommended in the Final Audit Report, beginning no later than 30 days after the end of the first quarter after the Final Audit report is issued and continuing within 30 days after the end of each calendar quarter thereafter, until Southern Star completes all the recommended corrective actions.

Southern Star will submit copies of all written policies and procedures developed in response to the recommendations in the Final Audit Report in the first quarterly report after those documents are completed.

Southern Star appreciates the opportunity to respond to the audit staff's findings and the opportunity it had to work with the audit staff during its onsite visits. Southern Star welcomes the chance to work with the audit staff in the future, in order to bring Southern Star's practices in the areas covered by the audit into compliance with the Commission's regulations and policies.

Very truly yours,

Beverly H. Griffith

Beverly H. Griffith
Senior Vice President and General Counsel

Document Content(s)