

100 FERC ¶ 61, 143
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
William L. Massey, Linda Breathitt,
and Nora Mead Brownell.

In Re Investigation of Certain Financial Data Docket No. IN02-6-000

ORDER TO RESPOND

(Issued August 1, 2002)

Issued to:
Northern Natural Gas Company
Transwestern Pipeline Company

1. Pursuant to sections 5, 7, and 16 of the Natural Gas Act (NGA), 15 U.S.C. §§ 717d, 717f, and 717o, this Order to Respond (Order) directs Transwestern Pipeline Company (Transwestern) and Northern Natural Gas Company (Northern), which are or were jurisdictional interstate pipeline subsidiaries of the Enron Corporation (Enron),¹ to state why they have not violated the Commission's Uniform System of Accounts for natural gas companies,² and why the costs and indebtedness associated with loans totaling approximately \$1 billion made by the pipelines with Citicorp North America, Inc. (Citicorp) and JP Morgan Chase Bank (JP Morgan) within two weeks of Enron filing for Chapter 11 reorganization under the Federal Bankruptcy Code were not imprudently incurred and therefore unrecoverable by the pipelines in any future rate proceedings before this Commission.

¹Northern was purchased by Dynegy, Inc. in February, 2002. On July 29, 2002, MidAmerican Energy Holdings Company announced that it intended to purchase Northern from Dynegy.

²Part 201 Uniform System of Accounts Prescribed for Natural Gas Companies Subject to Provisions of the Natural Gas Act, 18 C.F.R. Part 201 (2002).

Procedural Background

2. In November 2001, the Chief Accountant, concerned over the financial control exerted by parent companies over the assets of their jurisdictional subsidiary companies, began a review of transactions between parent companies and their jurisdictional subsidiaries. Specifically, the balances in the cash account and accounts related to associated companies, reported in the FERC Forms 1, 2, and 6, were reviewed for the years 1997 through 2001. This review revealed that certain companies had significant balances in gas and electric Account 146 - Accounts Receivable from Associated Companies, and oil Account 13 - Receivables from Affiliated Companies, and that the balances in these accounts had significantly increased over the period under review. These accounts are used to record receivables for items such as revenue for services rendered, material furnished, rent, interest and dividends, advances and notes. Company personnel interviewed stated that the account balances were increasing due to participation in cash management or money pool programs with their parent companies.

3. An audit was initiated for selected natural gas and oil pipelines and public utilities in January 2002, to determine compliance with the Commission's accounting and reporting requirements for the years 2000 through 2001.

4. On March 1, 2002, the Commission instituted a non-public investigation regarding financial data related to transactions, activities and accounting practices that may have impaired the financial condition of entities subject to the Commission's jurisdiction for the benefit of corporate parents or other affiliates or associated entities of jurisdictional companies.

Loan Agreements of Transwestern and Northern

5. Transwestern and Northern did not have written cash management agreements with Enron.

6. In November 2001, Transwestern and Northern, at the request of their parent, Enron, entered into revolving credit agreements for \$550 million and \$450 million, respectively, with Citicorp and JP Morgan. Both pipelines pledged their pipeline assets as collateral under the respective loan agreements. Subsequent to these transactions, Enron entered into agreements with Transwestern and Northern for the same funds.

7. Specifically, on November 13, 2001, Enron Corporation entered into two subordinated promissory notes with Transwestern for \$137.5 million and \$412.5 million (totaling \$550 million). The notes state that they are subordinated to prior payment of all

senior indebtedness upon dissolution, liquidation, or reorganization for the benefit of creditors of Enron. Interviews with Transwestern's Manager of Financial Accounting and Reporting revealed that the \$137.5 million was used to pay off a portion of a \$250 million unsecured loan outstanding by Enron North America, another Enron subsidiary, to Citibank (a member of Citicorp). The remainder of the funds (\$412.5 million less \$10 million held by Transwestern for operating capital) was swept to Enron under a cash management program in exchange for the second subordinated note. As of June 14, 2002, Enron has made no payments on the subordinated notes. Transwestern has written these notes off as unrecoverable.

8. Notes to Transwestern's FERC Form 2 for 2001 provide additional information. On December 31, 2001, Transwestern was in default of the debt covenants requiring the company to maintain a net worth of no less than \$750 million. Due to Enron's bankruptcy, Transwestern reserved the balance in Account 146 (\$785 million) which reduced the company's net worth. On April 30, 2002, the Citicorp debt agreement was amended to reduce the tangible net worth test to \$400 million and the default was waived.

9. On November 19, 2001, Enron entered into an assignment and assumption agreement with Northern for \$112.5 million. This amount was used to pay off the remainder of the Enron North America unsecured loan discussed above. Northern also entered into an agreement with MCTJ Holding Company (MCTJ), a limited liability company, set up between Enron and Northern. This agreement consisted of a note for \$307.5 million, the remainder of the \$450 million loan less \$30 million held by Northern in a bank account for operating capital. Northern personnel stated that MCTJ then distributed the \$307.5 million to another Enron subsidiary, CGNN Holdings Company, Inc., MCTJ's parent, which in turn loaned the funds to Enron.

10. Additionally, Northern received \$1.5 billion from Dynegy, Inc., in return for Series A Preferred 6% stock issued in November. At the same time, Northern loaned the proceeds to MCTJ, which in turn distributed the funds to Enron. Northern has recorded the \$1.5 billion in Account 145 - Notes Receivable from Associated Companies.

11. During staff's audit in early March 2002, the Director of Financial Accounting and Reporting for Transwestern and Northern indicated that Enron had the pipelines take out the November 2001 loans to try to hold off a declaration of bankruptcy. He also indicated that neither company expected to receive any repayment of these loans due to Enron's bankruptcy. The pipelines are still liable for the entire \$550 million and \$450 million.

Discussion

12. The Uniform System of Accounts requires that jurisdictional entities keep their " books of account, and all other books, records, and memoranda which support the entries in such books of account so as to be able to furnish readily full information as to any item included in any account. Each entry shall be supported by such detailed information as will permit ready identification, analysis, and verification of all facts relevant thereto." ³

13. It appears that due to the failure to maintain written cash management agreements with Enron, neither Transwestern nor Northern were able to support entries in Account 146 of the Uniform System of Accounts.

14. Therefore, the Commission is directing Transwestern and Northern each to provide written responses stating why the Commission should not find that each of them has violated the General Instructions-Records under Part 201 of the Uniform System of Accounts by failing to maintain written cash management agreements with Enron.

15. Under sections 4, 5 and 7 of the NGA: (1) the rates, charges and services of natural gas companies must be just and reasonable and not unduly discriminatory; (2) the Commission may, after a hearing on its own motion, find that the rates, charges, or services of a natural gas company are unjust, unreasonable or unduly discriminatory and accordingly modify such rates, charges, or services by order; and (3) the jurisdictional services provided by natural gas companies may be authorized on the basis of a finding that such services are in the public interest.

16. It appears that the loans made by Transwestern and Northern described above were imprudent. It further appears that Transwestern and Northern will experience an increased credit risk as a result of the loans and will have a significantly higher cost of capital.

17. Therefore, the Commission is directing Transwestern and Northern each to provide written responses stating why the Commission should not find that the November 2001 loans described above were imprudently incurred, and why the costs

³See General Instructions-Records under Part 201 of the Commission's Uniform System of Accounts for Natural Gas Companies Subject to the Provisions of the Natural Gas Act.

Docket No. IN02-6-000

arising from such loans and arrangements should be passed on to ratepayers after the settlement rates now in effect expire.⁴

The Commission orders:

(A) Transwestern and Northern are each hereby ordered, within thirty days of the date of this order, to provide written responses stating why the Commission should not find that each of them has violated the General Instructions-Records under Part 201 of the Uniform System of Accounts by failing to maintain written cash management agreements with Enron.

(B) Transwestern and Northern are each hereby ordered, within thirty days of the date of this order, to provide written responses stating why the Commission should not find that the November 2001 loans as described above were imprudently incurred, and why the costs arising from such loans and arrangements should be passed on to ratepayers after the settlement rates now in effect expire.

By the Commission

(S E A L)

Magalie R. Salas,
Secretary.

⁴Under the settlement reached in Northern's last general rate case in Docket , No. RP98-203-000, Northern may not file a general rate increase before November 1, 2003, but must file a general rate case not later than May 1, 2004. Under the settlement reached in Transwestern's last general rate case in Docket Nos. RP95-271-000, et al., Transwestern's negotiated settlement rates expire in 2006.