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Drafting and Interpreting Sensitive Gas Purchase Contract Provisions

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DRAFTING AND INTERPRETING
SENSITIVE GAS PURCHASE
CONTRACT PROVISIONS

by

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for the

NATURAL GAS SYMPOSIUM: CONTRACT
SOLUTIONS FOR THE FUTURE
REGULATORY ENVIRONMENT

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University of Colorado School of Law
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DRAFTING AND INTERPRETING
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William D. Watson
Holme Roberts & Owen
March 24, 1983

I. INTRODUCTION

A. Personal Bias

B. Gas Purchase Contract Characteristics

1. Contract/regulation confusion
2. Contract or option
3. Precision and ambiguity
 - a. complexity
 - b. weasel words

II. INDEFINITE PRICING

A. Escalators

1. Area rate clause
 - a. FPC area rate
 - b. any regulated price
2. Redetermination
 - a. timing
 - i. what triggers
 - ii. notice required
 - iii. frequency
 - b. favored nations
 - i. two or three party

- ii. average prices
- iii. other limitations
- c. alternate fuel
 - i. specific fuel
 - ii. general reference
 - iii. transportation
- d. market price
- e. renegotiation
 - i. standard
 - ii. termination
- f. arbitration
 - i. timing
 - ii. standard

B. Caps

1. Types

- a. regulatory passthrough
 - i. gas
 - ii. "fraud or abuse" NGPA § 601(b)&(c)
 - A. new statute
 - B. intrastate purchaser
 - iii. facilities
 - iv. take or pay
- b. marketability
 - i. standard
 - ii. discretion

- c. competing fuel
 - i. specific fuel
 - ii. general reference
- 2. Operation
 - a. prospective or retroactive
 - b. automatic or optional
 - c. cancellation mechanics
 - i. buyer if refused by seller
 - ii. seller if claimed by buyer
 - d. notice mechanics

III. TAKE OR PAY

A. Objectives

- 1. Producer
 - a. cash flow
 - b. present value
- 2. Pipeline
 - a. commitment
 - b. flexibility
 - c. ambiguity

B. TERMS

- 1. General - agree to take, a minimum quantity, or pay for the part not taken
- 2. Obligation Basis
 - a. deliverability
 - i. determination
 - A. testing
 - B. calculation

- C. pressure
 - D. unrestricted flow
 - E. notice mechanics
 - F. arbitration
 - i. preconnection
 - A. determination
 - B. arbitrary standard
 - b. reserves
 - i. determination
 - ii. ratio
 - c. agreed amount
 - d. ceiling
3. Commencement
- a. fixed date
 - b. connection
 - c. first delivery
 - d. agreement on basis
 - e. indefinite extensions
 - i. certificates
 - ii. force majeure
 - iii. indefinite obligation
4. Calculation Period
5. Pricing
- a. Gas
 - i. end of period

ii. weighted average

iii. when not taken

b. Adjustments

i. taxes

ii. Btu

C. Makeup

1. Credit calculation

a. gas or money

b. price changes

2. Time limit

a. fixed

b. term of contract

c. term extension

d. early termination

i. contract

ii. single well

3. Cash payback

a. general requirement

b. special circumstances

D. Special Provisions

1. Deliverability cap

2. Seller billing or demand

a. records

b. routine procedures

c. risk

3. Requirement for agreement
 4. Carry-forward
 5. Force majeure
- E. Enforcement
1. Payment
 2. Cancellation
- F. Regulation
1. Direct
 - a. prepayments distinguished
 - b. unrecovered advance
 - c. NGA 5 year makeup requirement
 2. Indirect
 - a. FERC Statement of Policy - December 16, 1982
 - i. 18 C.F.R. § 2.103
 - ii. deny interstate pipelines cost pass-through for take or pay in excess of 75% of deliverability in contracts after December 23, 1982
 - b. Columbia Gas Transmission Corporation rate case
 - i. FERC docket nos. TA81-1-21-001 and TA81-2-21-001
 - ii. ALJ denial of take or pay passthrough
 3. Proposed Regulation
 - a. Senate Resolution 515
 - i. passed December 14, 1982 (90 to 3)
 - ii. encourages FERC to review administrative actions to prevent gas

price increases, including modification of take or pay clauses

iii. encourages producers and pipelines to renegotiate to recognize changed conditions

b. Proposed legislation

c. FERC

IV. BUYER OUTS

A. Pricing

B. Disconnection

1. right to cancel
2. uneconomic connection

C. Regulation

1. direct
2. indirect

D. Force Majeure

1. detailed performance
2. basic performance

E. Brute Force