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Issues: MKP/RPL Pipeline Adjustment
Witness: MICHAEL J. WALLIS
Sponsoring Party: MoPSC Staff
Type of Exhibit: Surrebuttal Testimony
Case No.: GR-96-450
Date Testimony Prepared: July 18, 2001

MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

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SURREBUTTAL TESTIMONY

OF

MICHAEL J. WALLIS

MISSOURI GAS ENERGY
a divison of
SOUTHERN UNION COMPANY

CASE NO. GR-96-450

Exhibit No. 13
Date 9/17/01 Case No. GR-96450
Reporter KRM

Jefferson City, Missouri
July, 2001

SURREBUTTAL TESTIMONY

OF

MICHAEL J. WALLIS

MISSOURI GAS ENERGY,

a division of

SOUTHERN UNION COMPANY

CASE NO. GR-96-450

Q. Are you the same Michael J. Wallis who filed direct and rebuttal testimony in this case?

A. Yes, I am.

Q. What is the purpose of your surrebuttal testimony?

A. The purpose of my surrebuttal testimony is to respond to the rebuttal testimony of Missouri Gas Energy (MGE or Company) witness Michael T. Langston and to respond to the rebuttal testimony of Mid-Kansas Partnership/Riverside Pipeline Company (MKP/RPC) witnesses John B. Adger, Jr., Dennis M. Langley, Howard E. Lubow, Wendell C. Putman, and Joan A. W. Schnepp.

Q. Do you agree with the position taken in rebuttal testimony by Mr. Langston (Page 5, Lines 7 to 22) and Mr. Adger (Page 29, Lines 13 to 14) that it is the Staff's position that MGE should have terminated (rather than renegotiated) the Mid-Kansas II contract and thus, should have severed its contractual obligation with MKP/RPC?

A. No. Termination of the Mid-Kansas II contract was only one of the alternatives available to MGE. The deposition of Staff witness Thomas A. Shaw

(Pages 23 and 24) indicates that the Staff does not believe that termination of the Mid-Kansas II contract was the only viable alternative available to MGE. Staff believes that MGE should have used its leverage with MKP/RPC to negotiate firm transportation rates (in the Mid-Kansas II contract) which were closely tied to Williams Natural Gas Company (WNG) firm transportation rates. Mr. Putman, on Page 10, Lines 4 to 21 of his rebuttal testimony, indicates that MGE had strong leverage with MKP/RPC when it negotiated the Mid-Kansas II contract because MGE had withheld $2.6 million in payments (over two months) from MKP/RPC. Mr. Putman further indicates that (1) the payments withheld by MGE created a serious cash flow shortage to MKP/RPC and (2) the resulting cash flow shortage caused MKP/RPC (within two months of the time period in which MGE withheld the payments) to agree to negotiate the Mid-Kansas II contract.

The Staff's MKP/RPC adjustment properly reflects Staff's position (MGE should have negotiated the Mid-Kansas II contract to reflect rates which were closely tied to WNG firm transportation rates) because it compares MKP/RPC firm transportation rates to WNG firm transportation rates and it gives MGE a multi-million dollar gas supply offset (which is applied against the excessive MKP/RPC transportation costs) in order to reflect the favorable pricing provision associated with the TransOK index during the 1996/1997 ACA period. Staff points out that the favorable pricing provision associated with the TransOK index disappears in June 1998. Staff's MKP/RPC adjustment calculation accurately reflects the total detriment to MGE's ratepayers as a result of MGE's failure to negotiate rates (in the Mid-Kansas II contract) which were closely tied to WNG firm transportation rates.

Q. Do you agree with the position taken in rebuttal testimony by Mr. Adger Page 19, Lines 1 to 9) that Staff's adjustment calculation ignores WNG fuel costs?

A. Yes. Staff agrees that WNG fuel costs were inadvertently omitted from the MKP/RPC adjustment calculation. Staff believes that WNG fuel costs in the amount of $1,042,366.79 should be added to the WNG gas supply component (the total revised WNG gas supply component is approximately $4.2 million) of Staff's MKP/RPC adjustment calculation in order to reflect the additional volumes which MGE would have needed to purchase from a supplier in order to comply with WNG's FERC tariff provisions related to fuel reimbursement (which is achieved by factoring up city-gate delivered volumes to account for pipeline fuel losses as reflected in WNG's FERC approved fuel percentages). As a result, the Staff's revised MKP/RPC adjustment is $3,490,082.81 ($4,532,449.60 minus $1,042,366.79). The Staff's revised MKP/RPC adjustment calculation is attached as Schedule 1 to my surrebuttal testimony.

Q. Do you agree with the position taken in rebuttal testimony by Mr. Langley (Page 31, Lines 7 to 24 and Page 32, Lines 1 to 13); Mr. Langston (Page 14, Lines 1 to 18); Mr. Adger (Page 21, Lines 3 to 9); Mr. Putman (Page 15, Lines 15 to 18); and Ms. Schnepp (Page 12, Lines 5 to 7) that your use of a 4% premium to calculate the WNG gas supply component of Staff's adjustment is inappropriate when compared to the gas supply incentive plan sharing grid established by the Commission in its Order in MGE Case No. GO-94-318?

A. No. My use of a 4% premium to calculate the WNG gas supply component of Staff's adjustment is appropriate. The Commission, in its Order in Case No. GO-94-318, clearly designed MGE's gas supply incentive plan (GSIP) sharing grid so that MGE would be rewarded for purchasing gas supplies below the cumulative benchmark gas cost price (CBGCP) [the CBGCP is calculated, on a monthly basis, by multiplying the weighted average first of the month index price (published in Inside FERC's Gas Market Report) of 70% WNG and 30% Panhandle Eastern Pipeline Company (PEPL) by 1.04]. The Commission viewed that MGE should be rewarded (MGE is allowed to retain 50% of any gas supply savings which are between the CBGCP and 94% of the CBGCP) for any gas supplies which it purchased below 104% of the weighted average index price (the CBGCP). The Commission's Order clearly establishes that the 4% premium is the appropriate benchmark level to use to determine if MGE is procuring gas supplies for its customers in a reasonable, low cost manner.

The Staff, based on its review (during the 1996/1997 ACA period) of MGE's gas supply contracts, finds that [absent the Amoco and Oxy Tight Sands contracts which are not part of MGE's GSIP and the Oxy USA contract which Staff contested in Western Resources, Inc. (WRI) Case No. GR-94-228] the majority of MGE's gas supply contracts are (1) tied to an index plus a fixed number of cents and (2) have premiums which are below the 4% benchmark level.

The 14% premium level (110% of the CBGCP) advocated by Mr. Langley, Mr. Adger, Mr. Putman, and Ms. Schnepp is clearly excessive and is well above the Commission's benchmark premium level of 4%. Staff also points out that, with regard to MGE's GSIP sharing grid, a 14% premium level would require MGE to pay 50% of any gas supplies purchased between 104% (8 percent premium) of the CBGCP and 110% (14 percent premium) of the CBGCP. Clearly, the Commission does not regard a 14% premium level to be a good indication of gas purchasing practices.

Mr. Langston's use of Amoco and Oxy Tight Sands premiums as a possible substitute for the Staff's (and the Commission's) 4% premium level is inappropriate. The Amoco and Oxy Tight Sands demand charges are nearly 20%, and are not only above the Commission's benchmark premium level of 4% but are above the maximum premium allowed (above which MGE is subject to a prudence review) of 14% in MGE's GSIP. In fact, the Commission completely excluded the Amoco and Oxy Tight Sands contracts from MGE's GSIP. Staff also notes that (1) the Amoco and Oxy Tight Sands contracts (as well as the OXY USA contract) including the corresponding premiums were inherited by MGE when it purchased the WRI properties in early 1994 and (2) MGE, after acquiring the WRI properties, has not negotiated any gas supply contract with a premium even remotely close to the OXY USA premium levels and/or the Amoco and Oxy Tight Sands premium levels. In fact, the Staff, during its ACA audit reviews of MGE's gas supply contracts for the period of July 1, 1994 to June 30, 2000, discovered that the majority of the contracts negotiated by MGE have premiums below the Commission's benchmark premium level. Thus, Staff believes that the 4% premium level, which it used to calculate the WNG gas supply component of the MKP/RPC adjustment, is generous.

Staff notes that MGE, during each of the three years of its original GSIP, purchased its gas supplies (exclusive of the Amoco and Oxy Tight Sands contracts) at approximately 95%, 94%, and 95% respectively, of the CBGCP. Thus, MGE's actual premium levels (for the non-tight sands portion of its total gas supply portfolio) for its three most recent audited ACA periods are well below the 4% premium level which Staff used to calculate the WNG gas supply component of the MKP/RPC adjustment.

Q. Do you agree with the position taken in rebuttal testimony by Ms. Schnepp (Page 3, Line 8 to Page 9, Line 13) and Mr. Langston (Page 15, Lines 3 to 18) that your use of a 4% premium to calculate the WNG gas supply component of the Staff's adjustment ignores various non-price factors contained in the Mid-Kansas II contract, such as warranty of supply, daily and hourly load following capability, peaking capability, and no-notice and balancing provisions?

A. No. The various non-price provisions mentioned by Ms. Schnepp and Mr. Langston are not unique and can be obtained from other gas suppliers besides MKP/RPC. MGE did not perform any type of bidding process or RFP (Request for Proposal) to ascertain if it could have purchased the MKP/RPC volumes (under the same terms as contained in the Mid-Kansas II contract) from another gas supplier. MGE chose to retain MKP/RPC as its supplier for the 46,332 mmbtu maximum daily quantity (MDQ) of gas supply when it negotiated the Mid-Kansas II contract in February 1995. Thus, it is impossible to speculate on what might have happened if MGE had made the decision to use a different supplier for the 46,332 mmbtu per day of gas supply.

In addition, Staff disagrees with Mr. Langston's and Ms. Schnepp's classification of the Mid-Kansas II contract as a peaking contract. Staff points out that (1) during the winter months of December 1996 to February 1997 MGE purchased 100% of the 46,332 mmbtu MDQ of gas supply which it is allowed to purchase under the Mid-Kansas II contract and (2) during the months of November 1996 and March 1997 to June 1997 MGE purchased 50% of the MDQ of 46,332 mmbtu of gas supply which it is allowed to purchase under the Mid-Kansas II contract. The load factors of 100% (for three months) and 50% (for 5 months), which MGE experienced during the 1996/1997 ACA period, with regard to the Mid-Kansas II contract, are typical of baseload contracts (which command a relatively low premium) not peaking contracts. Staff also points out that the MKP/RPC pipeline does not have any storage facilities and thus, does not allow MGE to utilize storage withdrawal volumes in order to meet a peak day. Thus, MKP/RPC was forced (in order to compete with WNG who owns storage facilities with large amounts of storage capacity) to provide MGE with a baseload type contract which has swing capability (the Mid-Kansas II contract can swing from zero to 46,332 mmbtu per day).

Staff points out that the 46,332 mmbtu MDQ of gas supply which MGE received from MKP/RPC, during the 1996/1997 ACA period, is only a small percentage of its total gas supply peak day needs. MGE receives the vast majority of its peak day gas supplies from WNG under a variety of contractual provisions (including the types of non-price provisions mentioned by Ms. Schnepp) which typically contain fixed premiums. The Commission clearly indicated, in its Order in Case No. GO-94-318, that a 4% premium is an appropriate benchmark for MGE's entire gas supply portfolio (with the exclusion of the Amoco and Oxy Tight Sands contracts), including the Mid-Kansas II contract. The Staff appropriately used a 4% premium to calculate the WNG gas supply component of the MKP/RPC adjustment. The Staff also recognized the favorable pricing provision associated with the TransOk index and included (in its adjustment) a gas supply offset (which was applied against the excessive MKP/RPC transportation charges) of approximately $4.2 million.

Q. Do you agree with the position taken in rebuttal testimony by Mr. Langley (Page 30, Line 7 to Page 31, Line 5); Mr. Adger (Page 19, Lines 1 to 9); Mr. Putman (Page 14, Lines 17 to 19); and Mr. Langston (Page 17, Lines 12 to 22) that Staff's adjustment calculation is inappropriate because it does not reflect, as part of the WNG total costs, any of the GSR transition costs and take-or-pay charges which are typically incurred by WNG's customers?

A. No. As I previously indicated, Staff believes that MGE should have used its leverage with MKP/RPC to negotiate firm transportation rates (in the Mid-Kansas II contract) which were closely tied to WNG's firm transportation rates. As a result, it would be improper for the Staff to include WNG GSR transition costs and take-or-pay charges in its MKP/RPC adjustment calculation since Staff is not advocating that MGE should have switched to WNG in order to transport an additional 46,332 mmbtu MDQ of gas supply. In addition, MGE witness Mr. Langston indicates on Page 18, Lines 1 and 2 of his rebuttal testimony that the annual impact to MGE's ratepayers, if MGE had actually transported the 46,332 mmbtu per day of gas supply over the WNG pipeline, would have amounted to only $110,000 for the 1996/1997 ACA period.

Q. Do you agree with the position taken in rebuttal testimony by Mr. Langston (Page 3, Line 6 to 10 and Page 16, Line 20 to Page 17, Line 2) that Staff's adjustment calculation is inappropriate because it does not reflect the MKP/RPC Kansas Corporation Commission (KCC) rate reductions, effective August 1997 and October 1997, as well as approximately $3.3 million in actual refunds associated with MKP/RPC transportation rates charged during the 1996/1997 ACA period?

A. No. The August 1997 and October 1997 KCC rate reductions went into effect after MGE's 1996/1997 ACA period (July 1, 1996 to June 30, 1997) had ended and as a result, should not be considered in Staff's adjustment calculation. In addition, Mr. Langston fails to mention that WNG was ordered to reduce its FTS transportation rates from $10.2703 to $9.011 per mmbtu (effective March 1, 1997). Staff would point out that while it is true that MKP/RPC transportation rates are subject to periodic rate reductions (and rate increases) and refund provisions, it is equally true that WNG transportation rates are subject to periodic rate reductions and refund provisions. Due to the on-going nature of these rate reductions and refund provisions and the difficulty in assigning refunds to specific periods, the Staff, in calculating its MKP/RPC adjustment, has made an appropriate apples-to-apples comparison of the actual tariffed transportation rates charged by both MKP/RPC and WNG during the 1996/1997 ACA period.

Q. Do you agree with the position taken in rebuttal testimony by Mr. Langston (Page 16, Lines 8 to 18) that it would have been appropriate for Staff to have used a comparison of PEPL rates to MKP/RPC rates, to calculate the MKP/RPC adjustment, rather than the Staff's actual comparison of MKP/RPC rates to WNG's rates?

A. No. MGE transports approximately 25,000 mmbtu per day of firm peak day gas supply over PEPL as opposed to transporting nearly 800,000 mmbtu per day of firm peak day gas supply over WNG. Clearly, WNG (not PEPL) is the major pipeline supplier in the Kansas City, Missouri area. Staff's adjustment calculation properly compares the MKP/RPC rates to the pipeline rates (WNG pipeline rates) which were predominate in the Kansas City market.

Q. Do you agree with the position taken in rebuttal testimony by Mr. Adger (Page 18, Lines 1 to 9) that Staff's adjustment calculation ignores WNG market rates, WNG variable transportation charges, and MKP/RPC reservation charges?

A. No. The Staff's adjustment calculation clearly includes each of the items mentioned by Mr. Adger. A cursory review of MGE's response to Staff Data Request

No. 23 and Staff's adjustment workpaper clearly shows that all of the relevant components of gas supply and transportation are included in the Staff's MKP/RPC adjustment calculation.

Staff's MKP/RPC adjustment calculation does ignore WNG capacity release credits because capacity release was not an option available to MGE during the 1996/1997 ACA period with regard to MKP/RPC. As a result, Staff's adjustment calculation is actually conservative (smaller) considering that Staff did not reduce the WNG fixed reservation charge component of its adjustment in order to reflect capacity release credits which would have been subtracted from the fixed transportation charges on the WNG invoice to MGE.

Q. Do you agree with the position taken in rebuttal testimony by Mr. Lubow (Page 20, Lines 1 to 17) that Staff failed to consider the Mid-Kansas II contract in the context of MGE's total gas supply portfolio?

A. No. The Staff, in its MKP/RPC adjustment calculation, gave MGE a gas supply offset of approximately $4.2 million in order to reflect the favorable pricing provision in the Mid-Kansas II contract, with regard to the TransOk index, by using a 4% benchmark premium level (which was recommended by the Commission in its evaluation of MGE's total gas supply portfolio). The key point with regard to MGE's contract with MKP/RPC is that the MKP/RPC firm transportation reservation rates are more than double the WNG firm transportation reservation rates and are clearly detrimental to MGE's customers. This fact must be carefully weighed against any perceived benefits to be derived by MGE as a result of competition, reliability, and supply diversity.

Q. Do you agree with the position taken in rebuttal testimony by Mr. Lubow (Page 23, Lines 21 to 23) that Staff failed to recommend a disallowance given the fact that PEPL's firm transportation reservation rates were higher than WNG's firm transportation reservation rates?

A. No. Staff clearly indicated in its response to MKP/RPC Data Request No. 26 that it did not propose an adjustment with regard to PEPL's firm transportation reservation rates because they were only slightly higher than WNG's firm transportation reservation rates. MKP/RPC's firm transportation reservation rates, however, are more than double WNG's firm transportation reservation rates.

Q. Please summarize your surrebuttal testimony.

A. Staff believes that its revised MKP/RPC adjustment calculation is appropriate because it (1) reflects an appropriate 4% premium, (2) takes into consideration relevant non-price provisions, (3) properly reflects GSR transition costs and take-or-pay charges, (4) properly reflects MKP/RPC and WNG rate reductions and refunds, and (5) properly reflects the Staff's position that MGE should have used its leverage with MKP/RPC to negotiate firm transportation rates (in the Mid-Kansas II contract) which were closely tied to WNG's firm transportation rates.

Q. Does this conclude your surrebuttal testimony?

A. Yes, it does.

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of	)	
Missouri Gas Energy's	)	Case No. GR-96-450
Gas Cost Adjustment Tariff Revisions to be	)	
reviewed in its 1996-1997 Annual	)	
Reconciliation Adjustment Account.	)	

AFFIDAVIT OF MICHAEL J. WALLIS

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

Michael J. Wallis, of lawful age, on his oath states: that he has participated in the preparation of the foregoing Surrebuttal Testimony in question and answer form, consisting of 11 pages to be presented in the above case; that the answers in the foregoing Surrebuttal Testimony were given by him; that he has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of his knowledge and belief.

Michael J. Wallis

Michael J. Wallis

Subscribed and sworn to before me this 17th day of July, 2001.

D Suzie Mankin

D SUZIE MANKIN
NOTARY PUBLIC STATE OF MISSOURI
COLE COUNTY
MY COMMISSION EXP. JUNE 21,2004

Case No. GR-96-450
KPOC Adjustment
Source: DR No. 23

Gas Cost Component	Total Actual KPOC Gas Costs	Total Estimated WNG Gas Costs	Staff Adjustment
Fixed Transportation	11,955,046.17	5,476,757.44	6,478,288.73
Variable Transportation	1,478,112.36	257,641.02	1,220,471.34
Gas Supply	21,507,075.94	25,715,753.20	(4,208,677.26)
Total Costs	34,940,234.47	31,450,151.66	3,490,082.81

Calculation Of WNG Gas Supply Costs:

Month	Volumes	WNG IFGMR Index Price	Incentive Plan Benchmark Premium at 4%	Total WNG Gas Supply Price	Gas Supply Costs
July, 1996	316,159	2.18	0.09	2.27	716,795.68
August, 1996	165,099	2.14	0.09	2.23	367,444.33
September, 1996	0	1.67	0.07	1.74	0.00
October, 1996	152,491	1.68	0.07	1.75	266,432.28
November, 1996	828,145	2.50	0.10	2.60	2,153,177.00
December, 1996	1,503,796	3.68	0.15	3.83	5,755,328.05
January, 1997	1,508,894	4.30	0.17	4.47	6,747,773.97
February, 1997	1,347,803	2.81	0.11	2.92	3,938,819.49
March, 1997	741,205	1.63	0.07	1.70	1,256,490.72
April, 1997	749,876	1.70	0.07	1.77	1,325,780.77
May, 1997	771,203	1.92	0.08	2.00	1,539,938.15
June, 1997	750,899	2.11	0.08	2.19	1,647,772.77
Total Gas Supply Costs	8,835,570				25,715,753.20