Exhibit No.:	
Issue:	*Put and Call Transactions*
Witness:	*Phil S. Lock*
Sponsoring Party:	*MoPSC Staff*
Type of Exhibit:	*Surrebuttal Testimony*
Case No.:	*GR-99-435*
Date Testimony Prepared:	*March 12, 2002*

MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

SURREBUTTAL TESTIMONY

OF

PHIL S. LOCK

UTILICORP UNITED INC.
d/b/a MISSOURI PUBLIC SERVICE

CASE NO. GR-99-435

Jefferson City, Missouri
March 2002

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d/b/a MISSOURI PUBLIC SERVICE

CASE NO. GR-99-435

Q. Please state your name and business address.

A. Phil S. Lock, 200 Madison Street, Jefferson City, MO 65101.

Q. By whom are you employed and what is your position?

A. I am a Regulatory Auditor III with the Missouri Public Service Commission (Commission).

Q. What is the purpose of your surrebuttal testimony?

A. To address Company witness Shawn Gillespie's rebuttal testimony in which he describes: 1) The methodology of quantifying price risk; and 2) The most equitable method of compensating regulated customers for price risk.

Q. On page 2, line 16 through page 3, line 2 of Mr. Gillespie's rebuttal testimony he explains why there is a difference between price risk methodology between the Southern System and the Northern and Eastern Systems. The Southern System is served by a monthly balanced pipeline and the Northern and Eastern Systems are served by a daily balanced pipeline. Does Staff agree that the difference in price risk methodology between the systems is attributed to monthly balancing on the Southern System compared to daily balancing on the Northern and Eastern Systems?

A. Yes, while this may be the criterion for the Company to determine if 50% or 100% of the gas is "put" to the customer, this explanation does not explain why they hypothetically chose 50% of the gas to be "put" to the customer for the Southern System. The Staff believes that imbalances are only one element that is considered by the Company when a put or call transaction is executed. When gas is not "put" to UtiliCorp 50% of the time, there are several options, in addition to imbalances, that must be considered to keep the gas supply portfolio in balance. In order to do this, the Company must also consider whether storage injections or withdrawals are required, whether additional gas needs to be bought or sold, or whether mid-month nominations are required. Different options may be executed depending on whether or not the Company needs the gas.

Q. On page 3, lines 4-7 of Mr. Gillespie's rebuttal testimony he indicated that Staff has not identified any scenarios that are contrary to the way Missouri Public Service (MPS) quantified price risk. Please describe the scenarios that Staff believes could be detrimental to the regulated customer.

A. In general, there are four ways that put and call transactions could be detrimental to the regulated customer. 1) Gas is "put" to UtiliCorp by the supplier when First-of-the-Month (FOM) prices are greater than the gas daily prices. 2) Gas is "not put" to UtiliCorp when FOM prices are less than gas daily prices. 3) Gas is "called" by the supplier when the FOM price is less than the gas daily price. 4) Gas can be recalled by UtiliCorp (called back) when FOM prices are less than gas daily prices. Each of these scenarios requires a separate analysis by the Company's Gas Supply Services Department.

In any of these circumstances, the supplier will have the flexibility in determining, on any given day, if it wants to "put" the gas to UtiliCorp or "call" the gas from UtiliCorp. In either case, the supplier pays a premium to UtiliCorp in return for the opportunity to "put" more expensive gas to UtiliCorp or "call" less expensive gas from UtiliCorp at a price that is advantageous to them.

The Staff believes that the supplier has **limited** risk because they have a predetermined premium that they pay UtiliCorp for the right to exercise put and call options. UtiliCorp, on the other hand, has **unlimited** risk because they are accepting the consequences of the higher price, between the FOM price and the gas daily price, when put and call options are exercised by the supplier. In this situation, the price difference between FOM and the gas daily price can be substantial. Any time a supplier exercises a put or a call option; this could have a detrimental effect on UtiliCorp's regulated customers.

Q. Why did the Staff quantify the adjustment by crediting back the premiums to gas costs?

A. The Company's method does not address all the conditions where the customer could have been harmed. The Company's gas suppliers had the economic incentive to exercise the put/call options to the detriment of the Company's customers. These transactions were meant to enhance the Company's earnings and should never have been linked to regulated gas supply contracts. If done as a separate unregulated business transaction, it is logical to assume that the Company would have structured the transactions so that put/call revenues would have at least covered the gas cost effect of the supplier exercising the option.

Another way to view the detriment is to identify how the Company's gas buyer decisions were affected by the existence of put and call provisions. This analysis would compare how the gas buyer "would have" purchased gas absent the presence of put and call provisions versus the uncertainty of gas buying decisions with the potential obligation of put and call gas.

The difficulty in reconstructing "hypotheticals" is the existence of alternatives, which the gas buyer had to choose from even without the burden of managing puts and calls. Absent the gas being "put" to the Company, the opportunity exists to obtain cheaper gas from storage. Other options may include the potential for nomination changes on another supply contract, managing an existing imbalance, or potential for entering the spot market for supply. These actions never took place because the gas buyer was constrained by the potential existence of puts and calls. This uncertainty can further be illustrated where a call and a put existed for a particular month. In planning for the upcoming month, the gas buyer might assume (for a put provision) that gas would be "put" to the Company while a separate but equal call package would be "called" away from the Company. Therefore, under the Company's philosophy, the two transactions would cancel out. However, this is unlikely, since a gas supplier will put or call the gas based upon whether or not the daily market is less than or greater than the FOM market. The Company has the regulatory requirement of obtaining the best gas costs while ensuring reliability to its customers. The put and call transactions were inconsistent with this responsibility and exposed captive customers of the Purchased Gas Adjustment clause to higher costs. In terms of price, there could be several potential markets for natural gas. Two of these markets include the daily market, with daily pricing, and the monthly market, with FOM pricing as an overall rule. Local Distribution Companies should minimize gas costs by optimizing the use of FOM and daily priced packages of gas (along with the appropriate use of hedging). It appears to Staff that the Company generally adopted a philosophy that FOM is acceptable and cheaper daily pricing is something that can be given up to the gas supplier.

Q. Mr. Gillespie indicated that quantifying price risk on the Northern and Eastern Systems was based on the difference between the daily gas price when gas was not put, but the option was exercised to call on the gas at the gas daily price, less the first of the month index (p. 2, ll. 8-12). Is this the only scenario that exists for put and call transactions for customers on the Northern and Eastern Systems?

A. The Staff is not certain. As described previously in my surrebuttal testimony, the Staff believes that several scenarios exist for the execution of put and call transactions.

Q. Mr. Gillespie indicated that under Staff's methodology, regulated customers may receive benefits, which offset the price risk (p. 3, ll. 15-16). Does Staff agree with this statement?

A. Staff believes that when various scenarios exist in any put or call transaction, it becomes increasingly difficult to quantify the price risk to the regulated customer. As Staff indicated in its rebuttal testimony, crediting back the premiums helps ensure that there is no price risk to Missouri-regulated customers. Staff's adjustment has the effect of offsetting price risk that may exist.

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 Public Service's Purchased Gas Adjustment Factors To Be Reviewed In Its 1998-1999 Actual Cost Adjustment	))))	Case No. GR-99-435

AFFIDAVIT OF PHIL S. LOCK

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

Phil S. Lock, being 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 5 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.

Phil S. Lock
Phil S. Lock

Subscribed and sworn to before me this 11th day of March 2002.

Toni M Charlton

TONI M. CHARLTON
NOTARY PUBLIC STATE OF MISSOURI
COUNTY OF COLE
My Commission Expires December 28, 2004