

202-up

Exhibit No.:  
Issues: Hedging Gains and Losses  
Witness: Dana E. Eaves  
Sponsoring Party: MoPSC Staff  
Type of Exhibit: Rebuttal Testimony  
Case No.: EO-2017-0065  
Date Testimony Prepared: June 22, 2017

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# MISSOURI PUBLIC SERVICE COMMISSION

## COMMISSION STAFF DIVISION

### ENERGY RESOURCES DEPARTMENT

#### REBUTTAL TESTIMONY

OF

DANA E. EAVES

Staff Exhibit No. 202-up  
Date 8-24-17 Reporter AE  
File No. EO-2017-0065

THE EMPIRE DISTRICT ELECTRIC COMPANY

CASE NO. EO-2017-0065

Jefferson City, Missouri  
June 2017

\*\* Denotes Highly Confidential Information \*\*

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Rebuttal Testimony of  
Dana E. Eaves

1 Q. Does Mr. Hyneman in his direct testimony discuss your position in Kansas  
2 City Power and Light Greater Missouri Operations Company ("GMO") recent general rate  
3 case, Case No. ER-2016-0156, related to GMO's natural gas hedging activities?

4 A. Yes he does.

5 Q. Would you please put into context what your position was in Case No.  
6 ER-2016-0156?

7 A. Yes. During Staff's GMO Fuel Adjustment Clause ("FAC") Prudence Review  
8 in Case No. EO-2011-0390, Staff became aware that GMO used the practice of  
9 cross-hedging.<sup>1</sup> Staff took a position that the NYMEX<sup>2</sup> natural gas futures and spot energy  
10 prices were not sufficiently linked and by not contractually sharing the energy price risk with  
11 a third party supplier any gains or losses associated with cross-hedging should not be allowed  
12 for recovery through GMO's FAC. The Commission rejected Staff's position and found:

13 The Commission's Staff has failed to provide substantial controverting  
14 evidence to rebut the presumption of the prudence of GMO's hedging  
15 practices. The Commission's Staff has failed to meet its burden, by a  
16 preponderance of the evidence, of proving that GMO was imprudent  
17 with its hedging practices during the prudence review period of June 1,  
18 2009 through November 30, 2010.

19 Staff continued to have concerns related to GMO's cross-hedging practices and during  
20 GMO's most recent general rate case, Case No. ER-2016-0156, recommended that GMO  
21 suspend its cross-hedging activities. To be clear, Staff recommended GMO only suspend its  
22 cross-hedging practice. However, GMO personnel claimed the cross-hedging and natural gas  
23 fuel hedging were so intertwined it would be impossible to separate them. Based upon  
24 GMO's position that cross-hedging and natural gas fuel hedging were intertwined, Staff  
25 recommended GMO suspend, but not eliminate, its natural gas hedging activities and

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<sup>1</sup> The practice of linking natural gas future contracts to on-peak purchases of power.

<sup>2</sup> NYMEX is a commodity futures exchange owned and operated by CME Group of Chicago.

Rebuttal Testimony of  
Dana E. Eaves

1 maintain the appropriate language in its FAC tariff to provide GMO an easy path to resume its  
2 natural gas fuel hedging practices if market forces should change significantly. If it were not  
3 for GMO's flawed cross-hedging practices, Staff would not have recommended a suspension  
4 of GMO's natural gas fuel hedging.

5 Q. How is Mr. Hyneman's reference to Staff's position on hedging in the GMO  
6 rate case relevant to Empire's FAC prudence review?

7 A. It is not relevant to Empire.

8 Q. Does Empire cross-hedge?

9 A. No. Empire's natural gas hedging practices do not use NYMEX natural gas  
10 futures contracts to price hedge against on-peak purchased power. Empire's hedging  
11 activities only consists of the purchase of NYMEX natural gas futures contracts as a price  
12 hedge of natural gas used for fuel in the generation of electricity. Staff has evaluated these  
13 practices and determined them to be prudent.

14 Q. Has Staff analyzed Empire's historical financial natural gas hedging results  
15 based upon Empire's approved Risk Management Plan (RMP)?

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23 *continued on next page*

## Rebuttal Testimony of Dana E. Eaves

1           A.     Yes, and the high level results of Staff's analysis are included in the following  
2     Highly Confidential Table 1.

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4 \*\*\*

5 Q. What does Table 1 show in regards to Empire's natural gas hedging practices?

6 A. It shows that over a longer period of time, fifteen and a half years, Empire's  
7 hedging practices have incurred \$ \*\* \_\_\_\_\_ \*\* in losses.

8 Q. Mr. Hyneman states on page 11 of his direct testimony "Starting in 2009  
9 the natural gas market changed from a market characterized by high prices and high volatility  
10 to one that consistently reflects low prices and low volatility." Do you agree with  
11 that statement?

Rebuttal Testimony of  
Dana E. Eaves

A. While I have not seen forecasts that predict upward swings in natural gas prices from the pre-2009 levels in natural gas market, volatility still remains because market forces are always at play. Table 2 illustrates price volatility for the first six months of 2017 which reflects a 22% change in price in just the first six months of 2017.

Table 2



Q. Is it Staff's position that Empire should do away with its natural gas hedging practices?

A. No, Staff is concerned that leaving Empire's customers exposed to price volatility in the natural gas market is not a prudent action. Staff recommends that Empire leave its risk management policies in place and continue natural gas fuel hedging.

Rebuttal Testimony of  
Dana E. Eaves

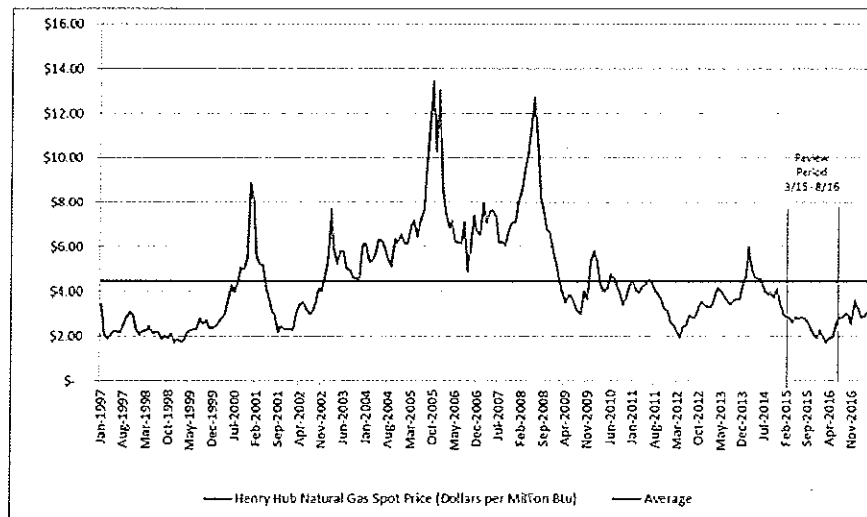
Q. Have you analyzed historical natural gas spot prices?

A. Yes and I have provided Table 2 detailing monthly natural gas spot prices from January 1997 to April 2017 at Henry Hub<sup>3</sup> and Chart 1 that graphs the same data.

Table 2

Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
1997	3.45	2.15	1.69	2.03	2.25	2.20	2.19	2.49	2.68	3.07	3.01	2.35
1998	2.09	2.23	2.24	2.43	2.14	2.17	2.17	1.85	2.02	1.91	2.12	1.72
1999	1.85	1.77	1.79	2.15	2.26	2.30	2.31	2.80	2.55	2.73	2.37	2.36
2000	2.42	2.66	2.79	3.04	3.59	4.29	3.99	4.43	5.06	5.02	5.52	8.90
2001	8.17	5.61	5.23	5.19	4.19	3.72	3.11	2.97	2.19	2.46	2.34	2.30
2002	2.32	2.32	3.03	3.43	3.5	3.26	2.99	3.09	3.55	4.13	4.04	4.74
2003	5.43	7.71	5.93	5.26	5.81	5.82	5.03	4.99	4.62	4.63	4.47	6.13
2004	6.14	5.37	5.39	5.71	6.33	6.27	5.93	5.41	5.15	6.35	6.17	6.58
2005	6.15	6.14	6.96	7.16	6.47	7.18	7.63	9.53	11.75	13.42	10.3	13.05
2006	8.69	7.54	6.89	7.16	6.25	6.21	6.17	7.14	4.9	5.85	7.41	6.73
2007	6.55	8	7.11	7.6	7.64	7.35	6.22	6.22	6.08	6.74	7.1	7.11
2008	7.99	8.54	9.41	10.18	11.27	12.69	11.09	8.26	7.67	6.74	6.68	5.82
2009	5.24	4.52	3.96	3.5	3.83	3.8	3.38	3.14	2.99	4.01	3.66	5.35
2010	5.83	5.32	4.29	4.03	4.14	4.8	4.63	4.32	3.89	3.43	3.71	4.25
2011	4.49	4.09	3.97	4.24	4.31	4.54	4.42	4.06	3.9	3.57	3.24	3.17
2012	2.67	2.51	2.17	1.95	2.43	2.46	2.95	2.84	2.85	3.32	3.54	3.34
2013	3.33	3.33	3.81	4.17	4.04	3.83	3.62	3.43	3.62	3.68	3.64	4.24
2014	4.71	6	4.9	4.66	4.58	4.59	4.05	3.91	3.92	3.78	4.12	3.48
2015	2.99	2.87	2.83	2.61	2.85	2.78	2.84	2.77	2.66	2.34	2.09	1.93
2016	2.28	1.99	1.73	1.92	1.92	2.59	2.82	2.82	2.99	2.98	2.55	3.69
2017	3.30	2.85	2.68	3.10								

Chart 1



<sup>3</sup> A natural gas pipeline located in Erath, Louisiana that serves as the official delivery location for futures contracts on the NYMEX.

Rebuttal Testimony of  
Dana E. Eaves

1           Q.     What conclusions do you draw from your analyses of historical natural gas  
2 spot prices over this nearly 20 year time period at the Henry Hub?

3           A.     The recent 20 year history of natural gas prices show volatility and cannot be  
4 predicted with any certainty. During the period of this prudence review, natural gas  
5 commodity price levels are lower than any 18 month period since 2000. It would be highly  
6 speculative and likely imprudent to believe that such historically low gas prices as seen during  
7 the prudence review period can be sustained going forward.

8           Q.     Does this conclude your rebuttal testimony?

9           A.     Yes it does.



BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MISSOURI

In the Matter of the Sixth Prudence Review of )  
Costs Subject to the Commission-Approved )  
Fuel Adjustment Clause of The Empire District )  
Electric Company )

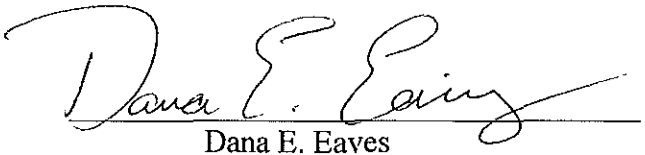
Case No. EO-2017-0065

AFFIDAVIT OF DANA E. EAVES

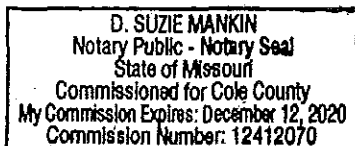
STATE OF MISSOURI )  
 ) ss  
COUNTY OF COLE )

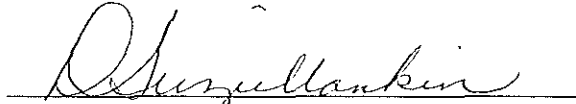
**COMES NOW**, Dana E. Eaves and on his oath declares that he is of sound mind and lawful age; that he contributed to the foregoing Rebuttal Testimony; and that the same is true and correct according to his best knowledge and belief.

Further the Affiant sayeth not.

  
Dana E. Eaves

Subscribed and sworn to be this 21<sup>st</sup> day of June, 2017.



  
Notary Public

**CASE PROCEEDING PARTICIPATION**

**DANA E. EAVES**

<b>PARTICIPATION</b>		<b>TESTIMONY</b>
<b>COMPANY</b>	<b>CASE NO.</b>	<b>ISSUES</b>
Ameren Missouri	ER-2016-0179	Fuel Adjustment Clause
KCP&L GMO	ER-2016-0156	Fuel Adjustment Clause
KCP&L	EO-2016-0183	MEEIA Prudence Review
KCPL GMO	EO-2015-0180	MEEIA Prudence Review Program costs and TD-NSB Share, Software system costs, Contractors, Interest Costs
Ameren Missouri	EO-2015-0029	MEEIA Prudence Review Program costs and TD-NSB Share, Software system costs, Contractors, Interest Costs
Empire District Electric Company	EO-2014-0057	FAC Prudence Review Risk Management
AmerenUE	EO-2013-0407	FAC Prudence Review Risk Management
KCP&L Greater Missouri Operations (GMO)	EO-2013-0325	FAC Prudence Review Purchased Power Agreements & Costs, Hourly weighted Transfer Pricing, Off- system sales revenue
Empire District Electric Company	EO-2013-0114	FAC Prudence Review Financial Hedges, Off-system sales revenue
Ameren Missouri	EO-2012-0074	FAC Prudence Review Direct/Rebuttal Requirements Contracts
KCP&L Greater Missouri Operations (GMO)	EO-2011-0390	FAC Prudence Review Direct/Rebuttal Hedging Purchased Power
Empire District Electric Company	EO-2011-0285	FAC Prudence Review FAC Components

**CASE PROCEEDING PARTICIPATION**

**DANA E. EAVES**

<b>PARTICIPATION</b>		<b>TESTIMONY</b>
<b>COMPANY</b>	<b>CASE NO.</b>	<b>ISSUES</b>
AmerenUE	EO-2010-0255	FAC Prudence Review Direct/Rebuttal Requirements Contracts
Empire District Electric Company	EO-2010-0084	FAC Prudence Review Fuel Cost, Off-System Sales, Interest Cost
Missouri American Water Company	WR-2008-0311	Surrebuttal; Pension and Other Post-Retirement Employee Benefits Costs, Annual Incentive Plan Pay-out Based Upon Meeting Financial Goals and Customer Satisfaction Survey, Labor and Labor-Related Expenses, Rate Case Expenses, Insurance Other than Group, and Waste Disposal Expense
Empire District Electric Company	ER-2008-0093	Fuel and Purchased Power, Fuel Inventories, FAS 87 (pension), FAS 106 (OPEBS), Expenses and Regulatory Assets, Off System Sales, Transmission Revenue, SO2 Allowances, Maintenance Expense
Laclede Gas Company	GR-2007-0208	Accounting Schedules Reconciliation
Aquila, Inc., d/b/a Aquila Networks-MPS & L&P	ER-2007-0004	Payroll Expense, Payroll Taxes and Employee Benefits
Empire District Electric Company	ER-2006-0315	Direct - Jurisdictional Allocations Factors, Revenue, Uncollectible Expense, Pensions, Prepaid Pension Asset, Other Post-Employment Benefits  Rebuttal - Updated: Pension Expense, Updated Prepaid Pension Asset, OPEB's Tracker, Minimum Pension Liability
Missouri Gas Energy (Gas)	GR-2004-0209	Direct - Cash Working Capital, Payroll, Payroll Taxes, Incentive Compensation, Bonuses, Materials and Supplies, Customer Deposits and Interest, Customer Advances and Employee Benefits  Surrebuttal - Incentive Compensation

**CASE PROCEEDING PARTICIPATION**

**DANA E. EAVES**

<b>PARTICIPATION</b>		<b>TESTIMONY</b>
<b>COMPANY</b>	<b>CASE NO.</b>	<b>ISSUES</b>
Aquila, Inc. d/b/a Aquila Networks-MPS & L&P (Natural Gas)	GR-2004-0072	Direct - Payroll Expense, Employee Benefits, Payroll Taxes  Rebuttal – Payroll Expense, Incentive Compensation, Employer Health, Dental and Vision Expense
Aquila, Inc., d/b/a Aquila Networks-MPS (Electric)	ER-2004-0034	Direct - Payroll Expense, Employee Benefits, Payroll Taxes  Rebuttal – Payroll Expense, Incentive Compensation, Employer Health, Dental and Vision Expense
Aquila, Inc., d/b/a Aquila Networks-L&P (Electric & Steam)	HR-2004-0024	Direct - Payroll Expense, Employee Benefits, Payroll Taxes
Osage Water Company	ST-2003-0562 WT-2003-0563	Direct - Plant Adjustment, Operating & Maintenance Expense Adjustments
Empire District Electric Company	ER-2002-0424	Direct - Cash Working Capital, Property Tax, Tree Trimming, Injuries and Damages, Outside Services, Misc. Adjustments
Citizens Electric Corporation	ER-2002-0297	Direct - Depreciation Expense, Accumulated Depreciation, Customer Deposits, Material & Supplies, Prepayments, Property Tax, Plant in Service, Customer Advances in Aid of Construction
UtiliCorp United Inc, d/b/a Missouri Public Service	ER-2001-672	Direct - Advertising, Customer Advances, Customer Deposits, Customer Deposit Interest Expense, Dues and Donations, Material and Supply, Prepayments, PSC Assessment, Rate Case Expense