

MINUTES OF THE House COMMITTEE ON Energy and Natural ResourcesThe meeting was called to order by Representative David J. Heinemann at
Chairperson3:30 ~~am~~/p.m. on January 26, 1983 in room 519-S of the Capitol.

All members were present except:

Committee staff present:

Ramon Powers, Research Department
Theresa Kiernan, Revisor of Statutes' Office
La Nelle Frey, Secretary to the Committee

Conferees appearing before the committee:

Representative Keith Farrar, Vice-chairman, House Energy and Natural
Resources Committee, Sponsor of HCR 5004.
Deb Miller, Governor's Legislative Aide.
Robert Stephan, Attorney General, State of Kansas.
Donald Schnacke, Kansas Independent Oil and Gas Association.
Tim Underwood, Kansas Association of Realtors.
Glenn Cogswell, Northwest Central Pipeline Corporation.
Ed Peterson, Assistant General Counsel, Kansas Corporation Commission.

HCR 5004 - A concurrent resolution memorializing the President of the
United States and the United States Congress to nullify
take-or-pay clauses and indefinite price escalator clauses
in natural gas purchase contracts.

Chairman Heinemann introduced Representative Keith Farrar, chief sponsor of
HCR 5004. Representative Farrar said he introduced this resolution as a
means of addressing the reasons we are faced today with higher prices for
natural gas that is presently in an oversupply situation, yet natural gas
consumers are not able to benefit from the availability of cheaper reserves
of natural gas that are being left in the ground. He stated that he believes
both the take-or-pay concept and the indefinite price escalator clauses
addressed in the resolution are at the heart of increased prices for natural
gas consumers. Additionally, he said they have caused reduced gas purchases
in the Hugoton field which has a depressing effect on the Kansas economy in
lost income as well as contributing to more unemployment for Kansas citizens.
Representative Farrar stated that Congress might not nullify these provisions,
but he noted that if enough pressure is applied, the percentage of takes from
high-priced natural gas could be reduced from approximately 90% to approxi-
mately 45%, thus allowing the pipelines to increase their purchases from
lower priced sources, such as the Hugoton field, and still provide needed
cash flow for the producers (see attachment 1).

Deb Miller, legislative aide to the Governor, said the Governor supports
HCR 5004. She stated that the Governor has been vitally concerned with
this issue over the last year and has focused specific attention on industry
practices such as take-or-pay and indefinite price escalator clauses (see
attachment 2).

Robert Stephan, Attorney General, appeared before the committee to voice
his support for HCR 5004. He said he hoped Congress would take the advice
of the resolution and nullify take-or-pay clauses and indefinite price
escalator clauses in natural gas purchase contracts (see attachment 3).

Donald Schnacke, Kansas Independent Oil and Gas Association, spoke in
opposition to HCR 5004. He stated that if the intent of HCR 5004 was
adopted, his organization would predict a curtailment of drilling and
shortages would once again occur. He said the solution to the problem is
not addressed in HCR 5004. Mr. Schnacke said that the problem of today's
price imbalance and conflicts in deliverability of natural gas still points
at the Congress. He stated that most experts believe a general overhaul of
the Natural Gas Policy Act (NGPA) of 1978, the Fuel Use Act and decontrol
of prices of natural gas would solve most, if not all, of the problems

CONTINUATION SHEET

MINUTES OF THE House COMMITTEE ON Energy and Natural Resources,
room 519-S Statehouse, at 3:30 ~~am~~/p.m. on January 26, 1983.

facing this industry, the consumer and issues contemplated in the future
(see attachment 4).

Tim Underwood, Kansas Association of Realtors, spoke in favor of HCR 5004. He said the realtors in Kansas are very concerned about the increasing natural gas prices in this state and the impact they have on the citizenry's ability to own their own homes. He said we have gone through a period of time when it has been very difficult for Kansans to own homes, and now with the increasing energy costs, it is just another factor that is going to impact on home ownership.

Glenn Cogswell, Northwest Central Pipeline Corporation, stated that Northwest Central understands that the purpose of the resolution is to call attention to the effect of take-or-pay clauses and indefinite price escalator clauses in natural gas purchase contracts and seek nullification of such clauses. He said Northwest Central endorses the purpose as stated in the resolution. Mr. Cogswell noted that it is true that take-or-pay and indefinite price escalator clauses have increased the price of natural gas to consumers. He said the sponsors of this resolution should be commended for their foresight in recognizing the problem and calling it to the attention of the President and the Congress of the United States.

Ed Peterson, Kansas Corporation Commission, distributed to committee members a copy of the Commission's notice of intervention before the Federal Energy Regulatory Commission regarding rate adjustments to Cities Service Gas Company's purchased gas adjustment. He also provided a brief overview of some of the gas suppliers take-or-pay contracts and the percentage of their gas reserves and delivered gas which are under take-or-pay contracts. He mentioned that some natural gas suppliers had experienced declines in their demand for natural gas, and if these declines in demand continue, he foresees the continuation of take-or-pay contracts. Mr. Peterson also said that several suppliers had requested special incentive rates because of the problems they currently face regarding their demand for natural gas.

Representative Ron Fox made a motion that the committee recommend to the House of Representatives that House Concurrent Resolution 5004 be adopted. Representative Farrar seconded the motion. The motion was unanimously passed.

Chairman Heinemann announced that the committee meeting scheduled for Thursday, January 27 had been cancelled.

There being no further business before the committee, the meeting adjourned at 5:00 p.m.

The next meeting of the committee will be held at 3:30 p.m. on February 1, 1983.

Rep. David J. Heinemann, Chairman

Date January 26, 1983

GUESTS

HOUSE ENERGY AND NATURAL RESOURCES COMMITTEE

NAME

ADDRESS

ORGANIZATION

no signees

*many in attendance -
sign-in sheet not circulated*

*26 in
attendance*

STATEMENT BY REP. KEITH FARRAR
BEFORE THE HOUSE ENERGY AND NATURAL RESOURCES COMMITTEE
WEDNESDAY, JANUARY 27
ON HCR 5004

Mr. Chairman and members of the committee, I appreciate the opportunity to appear before you today in support of HCR 5004.

As you are aware, one of the major items appearing in the news over the last few months, and especially now during the winter season, is the increasing cost to the consumer for natural gas. Included in the proposed Resolution are many of the reasons we are faced today with higher prices for a product that is presently in an over supply situation, yet we in Kansas and the United States are not able to benefit from the availability of cheaper reserves of natural gas that are being left in the ground. Something needs to be done. In a more normal supply and demand situation, the cost of natural gas would hold steady or decline because of less demand. As a farmer, I would like to see my income go up as I produce more, however we all know that agriculture is in financial trouble because of interference in the market place such as federal grain embargoes, or the threat of embargoes. No matter how good the intentions for protecting the consumer, we are again seeing the results of government interference in the market place.

To me, our present problems in pricing of natural gas can be traced back to the decision made many years ago by Congress and the Supreme Court to hold down the price of natural gas in relation to the price of other fossil fuels. The result was a reduction in exploration for natural gas and therefore a predictable shortage of natural gas developed for interstate markets. Again, Congress came to the rescue and passed the NGPA (Natural Gas Pricing Act) of 1978. Instead of

complete deregulation of the natural gas industry, Congress created more than 20 separate categories for pricing natural gas and allowing prices to escalate monthly until January 1, 1985 when they cease to exist, however, so-called old gas will not be completely deregulated.

Now back to the proposed Resolution. I will briefly try to explain my understanding of the "take-or-pay" clauses in many of the contracts negotiated by pipeline companies and natural gas producers in recent years.

The "take-or-pay" provisions require the purchaser to pay for all the gas contracted for (or a percentage of that amount) within a specified period of time whether or not the gas is taken. The contracts usually contain a provision for a make-up period during which the gas must be taken. As you can see, there are two parts to this provision. I would think the producers want the take provision to be sure of producing the well which results in creating the cash flow needed to continue developing oil and gas reserves.

The pay portion enables a pipeline company to know that they will have gas reserves for future sale. The actual effect of this clause in a contract during a decline in the market demand is the pipeline companies are faced with large payments associated with those take-or-pay provisions and may not be able to meet their make-up deadlines. In many instances, especially in the Hugoton field, pipeline companies are refusing to take from their normal supply of old, cheaper gas, thus creating higher prices to the consumer without letting the normal supply and demand forces affect the market place.

I am concerned, and satisfied in my own mind that some of the

contracts the pipeline companies claim they cannot cancel because they contain these "take-or-pay" provisions actually contain "market out" provisions or "unprofitability" provisions which allow the buyer to terminate the contract by notice to the seller. For instance, I will quote from a copy of a portion of a current pipeline contract - "Right to Terminate. It is specifically understood and agreed that if at any time in Buyer's sole opinion, the taking of gas hereunder from any well or wells become unprofitable, Buyer may terminate this Contract as to such well or wells upon sixty (60) days notice in writing to Seller."

Now as to the reason of including in the proposed Resolution a request to nullify the indefinite price escalator clauses explained on page 2 starting on line 0063. "WHEREAS, The indefinite price escalator clauses in natural gas purchase contracts have caused the price of gas under those contracts to automatically become the ceiling price, thereby preventing the marketplace from determining the price of natural gas." Again, I will quote from a portion of a current natural gas contract - "Price - For all gas delivered to Buyer, Buyer shall pay Seller the ceiling prices, including all adjustments and escalations, applicable to the gas covered by this Agreement, as established by the Federal Energy Regulatory Commission or other federal or state governmental authority having jurisdiction, including but not limited to Acts of Congress. The price shall change to conform to all such adjustments and escalations on the date they become effective as to the gas covered hereby."

As you can see, I believe both the "take-or-pay" concept as well as the indefinite price escalator clauses are at the heart of increased prices for natural gas consumers. Additionally, they have caused

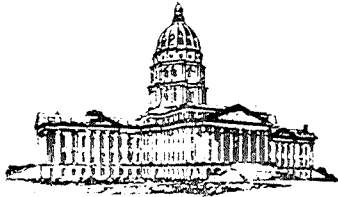
reduced gas purchases in the Hugoton field which has a depressing effect on the Kansas economy in lost income as well as contributing to more unemployment for Kansas citizens. I think it would be of benefit to point out the approximate underages in the takes of natural gas from the Hugoton field by some of the major companies since 1978 and what that means in dollar value of natural gas left in the ground. The total cumulative underages from the Hugoton field by December 1982 totaled 223.5 billion cubic feet of natural gas. Using an average well head price of 50 cents a thousand cubic feet, you come up with approximately one hundred twelve million dollars value at the well head. Conservatively the value to the consumer would be at least three times that amount. 1982 figures for the average well head price was 1.20 and 5.20 to 5.25 to the consumer.

Realistically I don't know if Congress will nullify these provisions, however if enough pressure is applied, the percentage of takes from high priced natural gas could be reduced from approximately 90% to approximately 45% thus allowing the pipelines to increase their purchases from lower priced sources, such as the Hugoton field, and still provide needed cash flow for the producers. As the committee looks at this Resolution, you may want to consider including within the Resolution a request of Congress to repeal the Power Plant and Industrial Fuels Act. To me, these restraints on use of natural gas prevent the best energy supply mix for industrial use, this restriction placed on the use of natural gas because it was thought we would not have enough natural gas for domestic consumption is no longer valid.

I will try to respond to questions.

STATE OF KANSAS

KEITH FARRAR
REPRESENTATIVE, 124TH DISTRICT
STEVENS, GRANT, STANTON,
MORTON, HASKELL COUNTIES
STAR ROUTE
HUGOTON, KANSAS 67951



TOPEKA

HOUSE OF
REPRESENTATIVES

COMMITTEE ASSIGNMENTS
MEMBER WAYS AND MEANS
JOINT COMMITTEE ON STATE BUILDING
CONSTRUCTION
INSURANCE

Information on Natural Gas Production

Some of this is part of the presentation to the K.C.C. September 23, 1982 on market demand hearings.

These exhibits point out the reduced production from the Hugoton field over the past few years, not that the Hugoton field couldn't produce more, but showing that the companies purchasing gas from the field are taking gas from other sources, usually at a higher price because of take or pay contracts the company has with other suppliers.

NATURAL GAS PRODUCTION

HUGOTON FIELD AND STATE TOTALS

(1)	(2) Hugoton Field Production (MCF)	(3) Total Kansas Production (MCF)
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1963	556,067,168	773,373,504
1964	567,981,458	810,069,686
1965	574,014,829	808,788,878
1966	608,766,800	856,421,989
1967	628,749,488	881,138,736
1968	595,454,070	848,380,950
1969	641,659,770	888,038,529
1970	652,062,194	909,413,281
1971	650,026,539	894,450,803
1972	652,773,807	898,618,234
1973	639,087,182	902,189,763
1974	640,672,818	894,307,867
1975	594,355,629	850,786,261
1976	565,998,996	836,205,709
1977	515,516,082	787,916,974
1978	556,952,720	862,099,086
1979	496,771,481	804,534,623
1980	417,699,964	741,272,555
1981	370,546,552	645,337,671
1982*	215,000,000	421,000,000

*Based upon 11 months actual production and estimated December production.

HUGOTON FIELD

	<u>Production 1981</u>	<u>Production 1982</u>	<u>Reduction</u>
SEPT	22,140,125	9,226,942	12,913,183
OCT	25,127,917	10,031,022	15,096,895
NOV	21,497,161	14,976,437	6,520,724
DEC	30,553,496	DEC data is not available	

PANOMA COUNCIL GROVE FIELD

		<u>Six-Month Figures</u>	<u>Total</u>
1979	First six months	80,889,082	137,286,275
	Second six months	56,397,193	
1980	First six months	76,250,866	110,306,899
	Second six months	34,056,033	
1981	First six months	47,453,859	78,031,437
	Second six months	30,577,578	
1982	First six months	48,238,759	60,013,697 (11 months)
	Last five months (excluding December)	11,774,938	

Hugoton Field, Kansas
 Nominations and Estimated Nominations By Purchaser
 For Six Month Periods October 1, 1980 Through September 30, 1983
 All Volumes In MMCF

Company	(1)	(2)	(3)	(4)	(5)
	<u>N O M I N A T I O N S</u>				
	10-1-80 to 3-31-81	4-1-81 to 9-30-81	10-1-81 to 3-31-82	4-1-82 to 9-30-82	10-1-82 to 3-31-83
Cities Service Gas	62,603.0	59,308.0	59,690.0	32,731.0	25,604.0 ¹⁰
Colorado Interstate	19,184.0	9,317.0	14,500.0	9,988.0	13,396.0
El Paso	5,360.0	5,433.3	5,403.7	5,433.3	5,403.7
Kansas-Nebraska	23,100.0	14,054.5	17,352.0	12,801.5	16,529.8
Mesa	17,701.0	11,803.0	15,281.0	8,962.0	11,600.0
Northern Natural	56,735.3	56,483.9	64,910.4	53,602.8	26,685.5 ^{57.9}
Panhandle Eastern	50,000.0	35,000.0	40,000.0	35,000.0	27,500.0 ^{9.3}
Others (APC, Peoples, Sunflower)	1,555.0	1,440.5	1,313.3	1,212.8	1,293.6
Total 6 months	236,238.3	192,840.2	218,450.4	159,731.4	128,012.6

Company	<u>E S T I M A T E D N O M I N A T I O N S</u>				
	4-1-81 to 9-30-81	10-1-81 to 3-31-82	4-1-82 to 9-30-82	10-1-82 to 3-31-83	4-1-83 to 9-30-83
Cities Service Gas	62,389.0	66,574.0	51,673.0	52,043.0	23,701.0
Colorado Interstate	12,244.0	15,798.0	13,391.0	13,885.0	9,874.0
El Paso	5,389.4	5,403.7	5,433.3	5,403.7	5,433.3
Kansas-Nebraska	15,500.0	22,082.0	11,959.0	16,788.0	12,834.0
Mesa	12,770.0	16,009.0	11,896.0	11,464.0	9,263.0
Northern Natural	56,955.6	69,951.2	55,163.9	63,443.7	25,620.0
Panhandle Eastern	35,000.0	50,000.0	30,000.0	40,000.0	22,500.0
Others (APC, Peoples, Sunflower)	1,580.0	1,710.0	1,455.0	1,352.0	1,387.0
Total 6 months	201,828.0	247,527.9	180,971.2	204,379.4	110,612.3

KANSAS HUGOTON FIELD

Comparison of Nominations, Production and Allowable
By Market Demand Periods
All Volumes in BCF

(1) <u>Market Demand Periods</u> (Winter)	(2) <u>Nominations</u>	(3) <u>Production</u>	(4) <u>% Prod./ Nom.</u> (3) ÷ (2)	(5) <u>Allowable</u>	(6) <u>% Prod./ Allow.</u> (3) ÷ (5)	(7) <u>% Allow./Nom.</u> (2) ÷ (5)
10-1-76 to 3-31-77	336.7	317.5	94.3	320.0	99.2	95.0
10-1-77 to 3-31-78	329.0	310.6	94.4	310.0	100.2	94.2
10-1-78 to 3-31-79	315.0	301.3	95.7	310.0	97.2	98.4
10-1-79 to 3-31-80	278.5	280.0	100.5	280.0	100.0	100.5
10-1-80 to 3-31-81	236.2	216.7	91.7	220.0	98.5	93.1
10-1-81 to 3-31-82	218.5	166.6	76.2	200.0	83.3	91.5
10-1-82 to 3-31-83	(128.0)					
Total six (6) periods	1,713.9	1,592.7	92.9	1,640.0	97.1	95.7
(Summer)						
4-1-77 to 9-30-77	292.4	214.4	73.3	295.0	72.7	100.9
4-1-78 to 9-30-78	261.4	247.7	94.8	290.0	85.4	110.9
4-1-79 to 9-30-79	253.5	211.6	83.5	250.0	84.6	98.6
4-1-80 to 9-30-80	200.6	182.3	90.9	175.0	104.2	87.2
4-1-81 to 9-30-81	192.8	174.3	90.4	175.0	99.6	90.8
4-1-82 to 9-30-82	159.7	84.0*	52.7	195.0	43.1	122.1
Total six (6) periods	1,360.4	1,114.3	81.9	1,380.0	80.7	101.4

*August and September production estimated.

COMPARISON OF TOTAL PURCHASES AND KANSAS HUGOTON PRODUCTION
 FIVE MAJOR INTERSTATE PIPE LINE COMPANIES
 1977 thru 1981
 ALL VOLUMES IN BCF

<u>Purchaser</u> <u>Year</u>	(1) Total Gas Purchases	(2) % Chg. Over 5 yr.	(3) Hugoton Production	(4) % Chg. Over 5 yr.	(5) Percent (%) Hugoton to Total Purchases (3) ÷ (1)
<u>Cities Service Gas</u>					
1977	457.7		172.9		37.8
1978	462.5		173.7		37.6
1979	456.6		150.5		33.0
1980	414.1		110.5		26.7
1981	393.4	-14.0%	102.3	-40.8%	26.0
1982 (6 mo.)			37.6		
<u>Colorado Interstate</u>					
1977	395.2		44.4		11.2
1978	397.7		46.8		11.8
1979	426.3		37.8		8.9
1980	402.5		29.2		7.3
1981	340.7	-13.8%	15.2	-65.6%	4.5
1982 (6 mo.)			10.4		
<u>Kansas-Nebraska</u>					
1977	131.2		41.2		31.4
1978	137.5		45.9		33.4
1979	130.5		36.8		28.2
1980	120.9		33.6		27.8
1981	107.9	-17.8	24.1	-22.4%	22.3
1982 (6 mo.)			12.9		
<u>Northern Natural</u>					
1977	759.7		130.4		17.2
1978	757.2		140.4		18.5
1979	801.0		135.7		16.9
1980	791.5		129.3		16.3
1981	826.8	+ 8.8%	114.3	-12.3%	13.8
1982 (6 mo.)			45.5		
<u>Panhandle Eastern</u>					
1977	637.8		76.9		12.1
1978	691.4		104.6		15.1
1979	738.1		94.9		12.9
1980	742.0		80.8		10.9
1981	745.2	+16.8%	84.8	+10.3%	11.4
1982 (6 mo.)			20.2		
<u>Total Five Companies</u>					
1977	2,381.6		465.8		19.6
1978	2,446.3		511.5		20.9
1979	2,552.5		455.6		17.8
1980	2,471.0		383.4		15.5
1981	2,414.0	+ 1.4%	340.7	-26.9%	14.1
1982 (6 mo.)			131.4		

STATE OF KANSAS



OFFICE OF THE GOVERNOR

State Capitol
Topeka 66612

John Carlin Governor

Testimony To
House Energy and Natural Resources

By

Deb Miller

Mr. Chairman and Members of the Committee:

It is a pleasure to appear before you today in support of House Concurrent Resolution 5004. The issue which you raise is one which the Governor has been vitally concerned with over the last year. He would be pleased to have the Kansas Legislature join him in this fight.

On February 19, 1982, the Governor first called on Congress to place a one year moratorium on gas price increases and thereby bring some stability to the market. He has since focused more specifically on industry practices such as take-or-pay and indefinite price escalator clauses which tend to artificially inflate prices.

By working with the National Governors' Association last summer, we were able to change the NGA policy to include language urging Congress to consider restrictions on take-or-pay and indefinite price escalator clauses.

Since that time the Governor has become increasingly concerned with take-or-pay clauses in natural gas contracts of some of the major pipelines serving Kansas.

The effect of these contracts has been to force pipelines to take expensive "new gas" and "deep gas" or pay for it. The result is that:

- 1) less expensive "old gas", such as the gas produced from the Hugoton field in southwest Kansas, is shut in although it could be delivered to natural gas consumers at a lower cost per unit;

- 2) as prices increase and consumption drops, consumers served by pipelines, such as Cities Service (now Northwest Central Energy Company), which has 70 percent of its supplies under take-or-pay contracts, may be forced to pay for gas they will never receive; and
- 3) as natural gas prices increase to the point where large industrial consumers switch to more economical alternative fuels, the fixed costs of the pipeline which they had carried are shifted to the remaining consumers.

The net effect of these individual impacts is the inverse of the law of supply and demand which was supposed to moderate natural gas prices in a deregulated market. In the perverse world of "take-or-pay" prices increase in the face of over supply and diminishing demand.

The impact of take-or-pay clauses on Kansas consumers served by the Cities Service (now Northwest Central Energy Company) has been a 53 percent increase in gas prices while purchases on the system have declined by 31 percent.

To alleviate this problem, the Governor is pursuing two separate but complementary courses: first of all, with the Attorney General as counsel, he has intervened in the Cities Service rate case before the Federal Energy Regulatory Commission urging them to disallow cost increases which have been caused by take-or-pay. The Governor has also directed the KCC to request the FERC to convene a "Joint Board", a forum composed of representatives of all states where Cities Service conducts business operations; this includes both producing and consuming states.

Moreover, the Governor is working with the National Governors' Association and our Kansas Congressional delegation to compel Congress to address the "take-or-pay" problem with legislation which will:

1. Insert in all current and future natural gas contracts, which contain "take-or-pay" or "indefinite price escalator" clauses, a "market out" clause which allows the purchaser to refuse to take gas supplies which cannot be marketed at the specified price without penalty and to renegotiate the contract; and
2. Amends Section 601 (c) of the NGPA to remove guaranteed pass-through of natural gas purchase costs and instead require the FERC to determine the purchased gas costs to be just and reason-

able expenses incurred through prudent management of the pipeline company. In this regard, the Governor suggests that as a measure of whether the gas costs are reasonable, the FERC should determine whether the company has purchased gas ratably from the fields and producers which comprise its total supply. This would prevent a company from taking a greater than proportionate share of expensive "new gas" or "deep gas" than "old gas" such as the supplies available from the Hugoton field.

Mr. Chairman, let me say again that the Governor welcomes and encourages the Legislature's support for HCR 5004. Though the issue of take-or-pay clauses is one which must ultimately be resolved at the Federal level, we have found that by aggressively advocating our concerns we can make a difference. The Governor is happy to have the additional voice of the Kansas Legislature on this issue which is of such extreme importance in Kansas to consumers, producers, and communities in Southwest Kansas.

NATURAL GAS

The total resource of domestic fossil fuels is finite, and the total annual production of energy from these sources is limited. Natural gas is the most environmentally acceptable, AND readily usable fuel. This has led to the rapid exploitation of available supplies.

Future natural gas curtailments are expected to cause increased distortion and dislocation in the economy. Even with stringent conservation, discovery of new gas fields will be needed to provide lead-time while alternate energy resources are developed.

Federal price policies historically undervalued interstate gas in relation to other fuels. This resulted in lowered incentives for exploration, an artificially high demand, and few incentives for conservation.

The National Governors' Association has supported the deregulation of new gas wellhead prices and recommends an excess profits tax on gas producers, with relief from such tax if excess earnings were plowed back into the exploration, and development of new natural gas supplies. In addition, a portion of the revenues from such a tax should be used for energy emergency impact assistance programs for individuals on fixed and low incomes.

NGA urges Congress to consider restrictions on industry practices which tend to inflate prices artificially by undermining market forces which would otherwise be at work, such as take-or-pay and indefinite price escalator clauses in natural gas purchase contracts. CONGRESSIONAL ACTION IS NEEDED TO RESTORE ORDER TO NATURAL GAS MARKETS, TO INCREASE COMPETITION, AND TO EQUALIZE AND REDUCE NATURAL GAS PRICES. SPECIFICALLY, THE GOVERNORS RECOMMENDED THAT CONGRESS ENACT LEGISLATION TO:

1. INCLUDE IN ALL EXISTING AND FUTURE NATURAL GAS CONTRACTS WHICH CONTAIN TAKE-OR-PAY OR INDEFINITE PRICE ESCALATOR CLAUSES A MARKET-OUT CLAUSE ALLOWING THE PURCHASER TO REFUSE TO TAKE GAS SUPPLIES WITHOUT INCURRING ANY PENALTY AND TO RENEGOTIATE THE CONTRACT.
2. AMEND SECTION 601(c) OF THE NGPA TO REMOVE THE GUARANTEED PASS-THROUGH OF NATURAL GAS PURCHASE COST AND INSTEAD REQUIRE THE FERC TO DETERMINE WHETHER THE PURCHASE GAS COSTS ARE JUST AND REASONABLE EXPENSES INCURRED THROUGH PRUDENT MANAGEMENT AND OPERATION OF THE COMPANY.
3. REQUIRE THE FERC TO HOLD AT LEAST FIVE REGIONAL HEARINGS WITHIN 12 MONTHS OF ENACTMENT TO EXAMINE AND SUBSEQUENTLY ADOPT METHODS TO ENSURE THE LOWEST POSSIBLE CONSUMER GAS PRICES CONSISTENT WITH THE MAINTENANCE OF A HEALTHY DOMESTIC NATURAL GAS INDUSTRY.

In addition, the administration and the Congress should consider measures to assure equal access to all natural gas supplies to both interstate and intrastate natural gas pipelines.

Development of legislation and executive commitments to determine national priorities for use of natural gas, specific programs designed to promote natural gas conservation, and a major effort to convert and phase-out as rapidly as possible those existing natural gas facilities that do not represent the wisest and best use of natural gas under current circumstances would prevent accelerated depletion of remaining supplies of natural gas, which could result from deregulation.

There is evidence of vertical and horizontal integration and interlocking relationships among natural gas producers and purchasing pipelines. There is also evidence of integrated and interlocking relationships among natural gas, petroleum, coal and uranium mining firms.

These conditions may result in an anticompetitive aspect of the energy industry which could cause an artificial inflation of the price of natural gas and other energy supplies.

Developments in the energy industry should be closely monitored to determine whether the letter and spirit of national antitrust laws are respected fully.

The administration and Congress should take prompt action to facilitate the earliest availability of natural gas from the Arctic slope to markets in the Midwest, East, Middle South and Pacific Coast states. This resource, essential to the health of these sections of the United States, must not be withheld because of delays in administrative agency approval or unnecessarily extended court proceedings.

Adopted July 1976; revised August 1980 and August 1982.

TESTIMONY OF
ATTORNEY GENERAL ROBERT T. STEPHAN
House Energy & Natural Resources Committee
Wednesday, January 26, 1983
Room 519-S, Capitol Building
3:30 p.m.

I appreciate the opportunity to appear before you in support of House Concurrent Resolution No. 5004. This is a measure I am very interested in seeing passed. The more I learn about the contracts Cities Service Pipeline Company, now called Northwest Central, entered into with producers of new high-priced natural gas, the more dismayed I am that this situation was allowed to develop. Indeed, I hope Congress will take the advice of House Concurrent Resolution No. 5004 and nullify portions of these contracts which are contrary to public policy and defy all logic and good sense. I believe your resolution would put additional pressure to bear on Congress, and I hope you will approve it.

Of course, the interest of Kansas in this issue is two-fold. Take-or-pay clauses and indefinite price escalators have a double effect on our state. We are having to pay exorbitant prices for gas, and the very lives of many unable to pay those prices are threatened. But additionally, the Kansas economy has suffered because billions of cubic feet of our own less expensive, old natural gas are going unproduced and unused. As long as take-or-pay contracts remain in effect and the pipelines are allowed to pass their costs on, gas prices will not stabilize, and little lower-priced Kansas gas will be used.

Take-or-pay simply means that the pipeline has guaranteed it will pay for a particular amount of gas from a producer, whether it uses that gas or not. Northwest Central, a major supplier of gas to Kansas, has entered into take-or-pay contracts for a great deal of high-priced new gas. In fact, beginning last November, Northwest Central reached the point where it was required by take-or-pay contracts to pay for more gas than it had demand for. In other words, it paid for gas it did not use. This is being called a take-or-pay deficit or penalty. In November and December Northwest Central's take-or-pay deficit amounted to \$12 million. The company itself estimates it will have take-or-pay deficits in 1983 of \$80 million. For the next four years it estimates its take-or-pay deficits could reach \$373 million or even more. I wish we could get the grain companies to contract for Kansas wheat on a take-or-pay basis.

This is a spiral which will continue until government takes action to stop it. Northwest Central has contracted to take or pay for more and more gas each year. As the price to the consumer escalates, demand will become less and less. That in turn increases the take-or-pay deficits, which if Northwest Central has its way, will be passed on to consumers, raising prices further, and demand again will decrease and deficits will increase.

Before the Federal Energy Regulatory Commission, we, of course, oppose the passing on of any costs of take-or-pay

deficits to consumers. We oppose the passing on of any take-or-pay costs at all to consumers. Northwest Central made bad business judgments in entering into these contracts and no one else should have to pay for those mistakes but Northwest Central. Because we believe take-or-pay contracts are contrary to public policy, we are further calling for refunds to consumers for costs of the high-priced gas we have been sold recently, where lower-priced gas would have been used had it not been for take-or-pay contracts. It will take several months and several hearings in Washington before we know the Federal Energy Regulatory Commission's decision.

It certainly is my preference that Congress decide this issue for us immediately by declaring these contracts void in violation of public policy. I encourage you to voice support for such action by approving House Concurrent Resolution No. 5004.

I will be happy to answer any questions.



KANSAS INDEPENDENT OIL & GAS ASSOCIATION

500 BROADWAY PLAZA • WICHITA, KANSAS 67202 • (316) 263-7297

ATTACHMENT 4

January 26, 1983

TO: House Energy and Natural Resources Committee

RE: HCR 5004.

Despite the present popular attitude contained in HCR 5004, we shall offer the following comments before you act.

It is correct in assuming the issue of contracting relating to natural gas pricing is a matter that primarily confronts the Congress. However, natural gas contracts have, are, and will be entered into in Kansas in the future, between producers, pipelines and consumers that may or may not contain escalator clauses or take-or-pay clauses.

We find there is much misunderstanding about "take-or-pay" and "indefinite price escalator" clauses. Many do not understand them.

If instead of "take-or-pay", which many believe has the connotation of holding a gun to the head of the pipeline forcing them to take gas they can't use, --if we referred to these clauses as "minimum production sales", or "natural gas ~~shortage~~ ^{Storage} charges", we wonder if the public would be as much offended.

These clauses were simply put into contracts to assure a normal flow of dollars to the bank to service debt of risk takers who drill the wells and assure the production and deliverability of the gas. In Kansas, I doubt if many of these contract provisions are activated. The more expensive wells found in Oklahoma and Wyoming where the cost of the drilling of a well below 15,000 feet can exceed \$20 million, dictate these provisions.

The important thing for you to consider is that the pipeline buys the gas, whether it takes it currently or at a later date through make-up provisions contained in the take-or-pay clauses.

Indefinite price escalator clauses in contracts are placed in natural gas contracts in an attempt to keep wellhead prices of gas at or close to market prices. Normally, these contracts are for many years or for the life of the well and these clauses attempt to avoid short-term contracts that, in today's market, might otherwise have to be renegotiated on a year to year basis.

ATTACHMENT 4

Use of indefinite price escalator clauses are limited by existing law. To nullify them completely would further distort market value versus prices received for natural gas.

If the intent of HCR 5004 were finally adopted, we would predict a curtailment of drilling and shortages would once again occur. Nullifying these contract provisions will result in premature abandonment of Kansas wells resulting in shortages and increased prices in the long run to consumers. Without strong incentive prices and assurances of a steady cash flow, producers will not take the risk to drill the wells. People that advance money for building pipelines to hook up these wells want to be assured of a steady flow of money.

The solution to the problem is not addressed in HCR 5004. The problem of today's price imbalance and conflicts in deliverability of natural gas still points at the Congress.

The NGPA of 1978 sets prices at a ceiling that have no relationship to the marketplace. Old gas, much of which is in Kansas is locked in at low prices indefinitely. We have gas below 20¢/mcf in Kansas when the national average for this type of gas is \$1.35/mcf.

Additionally the Federal Industrial Fuel Use Act enacted in 1978 continues to severely restrict the use of natural gas in America. IOCC addressed this subject in New Orleans, with Governor Carlin present. We agree.

Most experts believe a general overhaul of the NGPA of 1978, the Fuel Use Act and decontrol of prices of natural gas would solve much if not all of the problems facing this industry, the consumer and issues contemplated in the future.

Donald P. Schnacke



Natural Gas • Crude Oil
Exploration & Production

McCOY PETROLEUM CORPORATION

John Roger McCoy
President

Harvey H. McCoy
Vice-President

One Main Place / Suite 410 Wichita, Kansas 67202

316-265-9697

January 21, 1983

Mr. Don Schnacke
KIOGA
718 Merchants National Bank Building
Topeka, Kansas 66612

Re: House Concurrent Resolution #5004

Dear Don:

House Concurrent Resolution #5004 urges the President and Congress to nullify "take-or-pay" clauses and indefinite price escalator clauses in natural gas purchase contracts. This Resolution, while probably well intended, is based on several false premises and if the subject contract clauses were nullified, as asked for in the Resolution, the end result would be disastrous for the very consumers the Resolution is intended to help.

The Resolution states "The national average wellhead value of natural gas increased from \$.22 per MCF in 1973 to approximately \$2.40 per MCF in July, 1982, and ---". Both of these prices are, for the most part, based on government controlled price ceilings and have little to do with the true value of the gas. The true value of the gas would be the price it would receive if it were competing in the marketplace with other fuels. Both of these prices are below the competitive value of the gas.

The Resolution states "The indefinite price escalator clauses in natural gas purchase contracts have caused the price of gas under those contracts to automatically become the ceiling price, thereby preventing the marketplace from determining the price of natural gas". This is not true in Kansas and several other states, as the "Kansas Natural Gas Price Protection Act" and similar laws in other states limit the use of the indefinite price escalator clauses in contracts covering gas under state jurisdiction. The contract price for gas at the wellhead under most contracts has little relation to the price "at the marketplace" after several years. The indefinite price escalator clauses are an attempt to keep the wellhead price of the gas more near to the current price "at the marketplace". Use of the clauses is limited by existing laws and to nullify them completely would further distort the relationship between the value and price received for gas at the wellhead.

The Resolution states "The pipeline companies were required by producers seeking new gas supplies to take the gas contracted for or pay for the gas whether or not they can market it". Gas purchase contracts are executed as the result of arms length negotiation between the purchasers and the producers. A producer can not require a purchaser to do something that it did not agree to do at the time the contract was negotiated. The purchaser agreed to the "take-or-pay" provision as part of the consideration. Nothing is mentioned in the Resolution about make-up provisions. Most take-or-pay provisions in contracts also carry a make-up provision that any gas paid for and not produced can later be produced and not paid for, or "made-up".

The Resolution states "The dramatic decline in the taking of natural gas from Kansas has had a devastating impact on royalty owners, producers, and industry employees". This statement leaves the impression that the decline comes solely as the result of indefinite price escalator clauses and "take-or-pay" clauses in gas purchase contracts. This is at best a gross exaggeration. The decline in takes of Kansas gas is influenced to a large part by the decline in demand for gas and the increased supply of gas that was made available as the result of more favorable economics for gas drilling that was made possible by the very contract clauses this Resolution seeks to destroy.

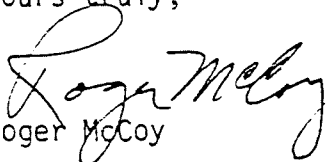
House Concurrent Resolution # 5004 should not be passed. If the indefinite price escalator clauses and "take-or-pay" clauses were to be nullified as asked for in the Resolution, a minimal short term relief would soon give way to long term agony as drilling would be curtailed, the short oversupply would be used up and we would again be in a shortage situation. The next shortage situation will be much more serious with regard to the price paid by the consumer for gas since much of the old low cost gas will be depleted and will not be available to cushion the cost of the new expensive gas.

Curtailed drilling is not a threat by the producers, it is simply a response. Much of the present adequate supply (deliverability) of natural gas comes as a direct result of the gas supply available from the deep expensive wells made feasible to drill only because of the relatively high wellhead price and the assurance of adequate cash flow for a reasonable pay out made possible by the "take-or-pay" provisions in the contracts. Without the present price and take factors, most of these wells are simply not economic to drill. If the producers do not have a chance to make a profit, the wells simply will not be drilled.

The nullifying of indefinite price escalator clauses in contracts would cause the premature abandonment of many Kansas wells currently producing gas on a commercial basis as a result of price increases dictated by the contracts' indefinite price escalator clauses.

I am sure the negative end result of passage of this Resolution and subsequent action by the Federal Government would be far different than that envisioned by most of the Resolution's sponsors.

Yours truly,


Roger McCoy

It's time to totally decontrol natural gas

Despite overwhelming opinion to the contrary, the time has come to completely decontrol the natural gas market. In fact, the time has never been better and logic and reason fairly cry for such a move.

This winter has been milder than anticipated so far and most consumers have had lower heating bills than were expected. The combination of warmer-than-usual weather and higher gas prices also has kept demand moderated and supplies plentiful.

With usage down and supplies up, these factors would serve to mitigate any sudden price jump created by total decontrol of prices. Moreover, deregulation in the last half of this heating season would allow the market plenty of time to adjust to the temporary shock of decontrol between now and the advent of the 1983-84 heating season.

Anyone who is skeptical of this line of reasoning should try one last argument on for size: Regulation simply is not doing the job it was intended to do, which is to keep prices down.

Despite all efforts by Congress to protect consumers from price increases, natural gas lives an inflationary life all its own during a time of otherwise dramatic disinflation.

On the face of it, this alone makes a strong case for freeing the market.

A thorough review of the history of natural gas controls doesn't weaken the argument, either.



Jerry Honster
The Star's business & financial editor

Natural gas has been regulated since 1938, when rates were fixed for those transporting and selling gas in interstate markets. In 1954, regulation of interstate business was extended to producers at the wellhead. The end result of legislating prices that were lower than the product's value was the disaster that befell consumers during the winter of 1976-77, when states dependent on the interstate market suffered two months of dangerous shortages that on occasion created potential life-threatening situations for residential consumers.

In an effort to encourage production, Congress went through an exercise in pseudo-deregulation that for all practical purposes made the problem worse by enlarging what was already a crazy-quilt price structure.

All this regulation has brought America from a situation where gas was cheap but increasingly

hard to get to a situation where it's plentiful but difficult to afford. The next step, given regulation's result to date and political pressure for added controls, is gas that will be both expensive and in short supply—or the worst of all possible worlds.

Looked at another way, natural gas remains the only commodity under government controls and, wonder of wonders, it is the most confused and inefficient market in the American economy today.

All of which seems to argue persuasively for decontrol because as it stands now the U.S. marketplace hasn't the slightest idea of what the supply and demand factors are or what the true market clearing price is.

Until consumers, suppliers and producers know these factors with some degree of certainty, nobody can make any rational decisions as to whether being part of the natural gas market makes good sense as either a buyer or seller.

Most, however, seem to reject deregulation proposals because they are absolutely convinced that it will mean even higher prices.

But this seems a rather irrational view, considering what has happened when other markets have been deregulated—the most recent best example being the oil market. Since oil was deregulated two years ago, the price trend for all petroleum products has been a steadily downward one.

This has been the case even

though oil price deregulation was opposed for years on the belief that decontrol would send prices through the roof.

The popular counter to that case in point, though, is to say the gas business is a much different animal than the oil business and thus more insulated from free market forces.

Well, of course it is. But that's not the same thing as saying natural gas is totally exempt from the law of supply and demand once everyone knows what the clearing price is and what the traffic will bear.

But a simple truth is fairly plain at this point: While consumers may not know what will happen to gas prices in the wake of decontrol, they do know the consequences of what happens with controls.

Working out from the knowledge of what control has wrought in the real world seems to acknowledge that controls aren't serving the consumer very well and haven't for more 45 years.

If reasonable minds accept such realities for what they are, it seems overwhelmingly logical to accept the notion that another approach to the natural gas market is at least worth a try.

This leaves only a totally free market because it's about the only thing that hasn't been tried yet. And the timing couldn't be better for such an experiment.

RESOLUTION ON SURPLUS
DELIVERABILITY OF NATURAL GAS

WHEREAS, the United States continues to import foreign fuels at high levels; and

WHEREAS, these imports are largely composed of oil which is being used in the nation's industrial sector because of the prohibition in the Fuel Use Act against the use of natural gas as industrial fuel; and

WHEREAS, there now exists a substantial surplus of deliverable domestic natural gas; and

WHEREAS, the Fuel Use Act's said prohibition is contributing significantly to this domestic gas deliverability surplus; and

WHEREAS, such surplus has caused both severe curtailment of production from existing wells and the inability of some new wells to obtain any market at all; and

WHEREAS, this situation threatens to cause premature abandonment of gas wells and their reserves, thereby resulting in physical waste, and it restrains the exploration for and development of new reserves; and

WHEREAS, use of natural gas for industrial purposes in lieu of other fuels has a positive advantage in terms of preserving environmental quality.

NOW, THEREFORE, BE IT RESOLVED by the IOCC that the Fuel Use Act should be amended to allow use of natural gas as an industrial fuel.

UNITED STATES OF AMERICA
BEFORE THE FEDERAL ENERGY REGULATORY COMMISSION

Handout
1-26-83
energy + natural
gas
ccs
HC. 04

Cities Service Gas Company) Docket No. TA83-1-43-000

NOTICE OF INTERVENTION
OF THE KANSAS STATE
CORPORATION COMMISSION

Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. 385.214, the State Corporation Commission (Kansas Commission) files its notice of intervention in the above-captioned proceeding.

The Kansas Commission is a regulatory body which is charged by Kansas law with jurisdiction to regulate rates and charges for the sale of electric energy and natural gas to consumers within the State of Kansas.

The Kansas Commission submits that good cause exists to permit its intervention and that no delay to these proceedings will be caused by its intervention. The Kansas Commission further requests that copies of all documents and correspondence be sent to:

Richard C. (Pete) Loux, Chairman
State Corporation Commission
of the State of Kansas
4th Floor, State Office Building
Topeka, Kansas 66612

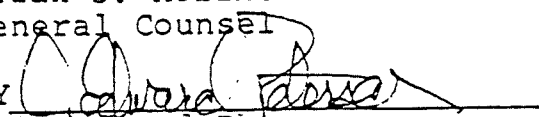
and

C. Edward Peterson
Assistant General Counsel
State Corporation Commission
of the State of Kansas
4th Floor, State Office Building
Topeka, Kansas 66612

Respectfully submitted,

STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS

Brian J. Moline
General Counsel

BY 
C. Edward Peterson
Assistant General Counsel
State Corporation Commission
4th Floor, State Office Building
Topeka, Kansas 66612
(913) 296-2543

September 30, 1982

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Cities Service Gas Company,) Docket No. TA83-1-43-000

PROTEST AND REQUEST FOR SUSPENSION
OF KANSAS STATE CORPORATION COMMISSION

The Kansas State Corporation Commission, pursuant to Rule 211 of the Commission's Rules of Practice and Procedure, 18CFR 385.211, hereby protests the increase in rates filed for in this proceeding, and requests that the increased rates be suspended for the maximum period allowed by law. In support hereof, the Kansas State Corporation Commission states as follows:

2. On September 22, 1982, Cities Service Gas Company (Cities Service) tendered for filing revised tariff sheets which, inter alia, reflect rate adjustments to Cities Services' PGA for increases in the current cost of gas, deferred purchased gas costs, and a special 12-month surcharge to recover retroactive payments to producer suppliers pursuant to Commission Order Nos. 93 and 93-A. The total increase proposed is 82.16 cents per Mcf. This filing, if accepted, would increase rates to Kansas ratepayers by approximately 66 million dollars over the proposed effective period.

3. The Kansas State Corporation Commission is very concerned about the effect of this large increase at this time. The increase proposed in this docket follows two increases approved already this year by the FERC. A purchased gas adjustment was approved by the FERC effective April 23, 1982, which increased rates by 38 cents per Mcf. In addition, the FERC approved subject to refund an increase in the Cities Service rate case filed in Docket No. RP82-114 which allows a 19 cents per Mcf increase to take effect on December 23, 1982. If the filing in this docket is approved, the rates of Cities Service Company will have increased an estimated 35% in less than one year. An increase of this proportion is unduly burdensome to ratepayers, and therefore is unjust, unreasonable, and not in the public interest.

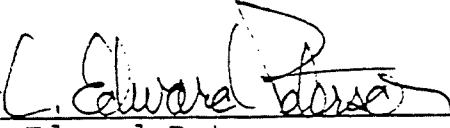
4. The requested increase also should be prohibited on grounds that it constitutes fraud and abuse as contained in Section 601(c) of the Natural Gas Policy Act of 1978, 15 U.S.C. §3431(c). The FERC policy is that fraud, abuse, or other grounds of protesting PGA filings are to be equated with

misrepresentation. The filing in this docket contains such a misrepresentation. The majority of the requested increase is attributed to "increases in Cities Services' natural gas supplier rates." However, the requested increase in this docket is well in excess of an increase that would be necessary to provide adequate service to Cities Services' customers. While it may be true that the rates of natural gas suppliers have increased generally, it is also true that Cities Service has chosen to decrease its takes of lower cost gas under contract in the Hugoton Field. This decrease in take in the Hugoton Field has been in excess of 40% during the past five years. At the same time, Cities Service has reduced its minimum take requirements for newer and higher cost gas in other fields by only 14%. The result is that average prices to the customer have been needlessly increased. To allege an increase of the magnitude contained in this filing as necessary to meet natural gas supplier rates is to misrepresent the position of the Cities Service system. Cities Service has justified this proposed increase with misrepresented and concealed facts. The proposed tariffs therefore should be suspended for the maximum period allowed by law and set for hearing.

WHEREFORE, the Petitioner, Kansas State Corporation Commission respectfully requests that the increase proposed by the filing of tariffs in this docket be suspended until March 23, 1983, and set for hearing.

Respectfully submitted,

Brian J. Moline
General Counsel

BY 
C. Edward Peterson
Assistant General Counsel
Kansas State Corporation
Commission
Topeka, Kansas 66612

UNITED STATES OF AMERICA
BEFORE THE FEDERAL REGULATORY COMMISSION

Cities Service Gas Company) Docket No. RP82-114-000

Cities Service Gas Company) Docket No. TA83-1-43

MOTION OF KANSAS STATE CORPORATION COMMISSION
TO CONSOLIDATE PROCEEDINGS

The Kansas State Corporation Commission (KCC), pursuant to Rule 212 of the Commission's Rules of Practice and Procedure, and 18 C.F.R. 385.212, hereby moves that the above-captioned proceedings be consolidated for purposes of hearing and decision, and in support thereof, states as follows:

1. On September 22, 1982, Cities Service tendered for filing revised tariff sheets which, inter alia, reflect rate adjustments to Cities Services' P.G.A. for increases in natural gas supply rates, a surcharge adjustment to amortize the deferred purchase gas cost account balance, and a special 12-month surcharge to recover estimated retroactive payments to producer suppliers pursuant to Commission Order Nos. 93 and 93-A. By petitions of even date, the Kansas State Corporation Commission is seeking intervention, and requesting a five month suspension and hearing concerning these tariff sheets. The filing indicates anomalies in purchase patterns which may rise to the level of fraud or abuse recognized under Section 601(c) of the Natural Gas Policy Act of 1978, 15 U.S.C. §3431(c).


2. The Kansas State Corporation Commission recognizes the narrow definition of fraud and abuse as determined by the Commission, but the KCC believes this filing clearly falls within that narrow definition. Should the Commission find an absence of fraud or abuse, the State Corporation Commission argues in the alternative that this filing indicates imprudent management which is resulting in unreasonable natural gas costs to consumers of the Cities Service Gas Company. The Commission has stated that challenges to a pipeline's internal management and contracting practices concerning the practice of natural gas are more properly considered in a Section 4 proceeding. United Gas Pipe Line Company, Docket No. TA82-2-11-000 (Order issued June 30, 1982). Consequently, the Kansas State Corporation Commission requests that this docket be consolidated with the pending rate case of Cities Service Gas Company in Docket No. RP82-114-000.

3. The issue of fraud and abuse in natural gas acquisition costs and the issue of management imprudence involve common questions of law and fact which warrant a consolidation. Consolidation would eliminate the potential for duplication in discovery, presentation of testimony and evidence, and hearing.

WHEREFORE, for the foregoing reasons, Docket Nos. RP82-114-000 and TA83-1-43-000 should be consolidated for purposes of hearing and decision.

Respectfully submitted,

Brian J. Moline
General Counsel

BY 
C. Edward Peterson
Assistant General Counsel
Kansas State Corporation
Commission
Topeka, Kansas 66612

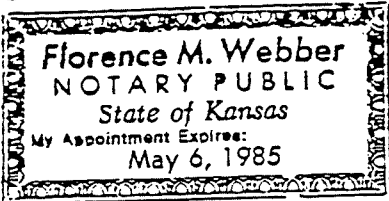
VERIFICATION

STATE OF KANSAS)
) SS
COUNTY OF SHAWNEE)

C. Edward Peterson, being first duly sworn upon oath deposes and says that he has read the foregoing document and knows the contents thereof, that he has been authorized to present the same on behalf of the State Corporation Commission of the State of Kansas, and that the facts therein stated are true and correct as he verily believes.

C. Edward Peterson
C. Edward Peterson

Subscribed and sworn to before me this 30th day of September, 1982.



Florence M. Webber
Notary Public

My Commission Expires:
May 6, 1985

CERTIFICATE OF SERVICE

This is to certify that the foregoing document has been served this 30th day of September, 1982, upon each person designated on the official list compiled by the Secretary in this proceeding in accordance with Section 210 of the Commission's Rules of Practice and Procedure.

C. Edward Peterson
C. Edward Peterson
Assistant General Counsel

Service emphatically denies that the quoted statement in the Company's filing is in any way a misrepresentation or that Cities Service has otherwise misrepresented the facts in its filing.

2. At the outset, it is important to emphasize that the "misrepresentation" which KSCC alleges is not of the type contemplated by Section 601(c) of the Natural Gas Policy Act (NGPA). Section 601(c) speaks in terms of the "amount paid" to producers being excessive due to fraud, abuse, or similar grounds. KSCC has not alleged, nor could it, that Cities Service has improperly paid to any producer any amount in excess of that allowable under the NGPA and applicable Commission regulations. 2/ Nor has KSCC alleged, nor could it, that this PGA filing reflects the impact of substantial volumes of gas purchases at unregulated prices under Section 107 of NGPA, as has been the case in the PGA filings of numerous other pipelines recently considered by the Commission. Thus, KSCC has not even alleged, much less demonstrated, an instance of "fraud or abuse" within the meaning of Section 601(c).

3. As to the general allegation of a "misrepresentation" in Cities Service's PGA filing, the Company's filing in fact reflects exactly what is stated therein -- increases in the Company's natural gas supplier rates -- and such increases are reflected in the filing strictly in accord with the Commission's PGA regulations and the PGA provision in the Company's FERC Gas Tariff.

2/ Nor has KSCC alleged that Cities Service has been imprudent under the NGA in the prices it has paid to individual producers.

4. KSCC's complaint as to the Company's pattern of takes from producers is totally misleading and misinformed; this pattern is not in any sense arbitrary or unjust to the consumers, as suggested by KSCC. As set forth in the testimony in Cities Service's most recent general rate increase filing in Docket No. RP82-114 (Statement P, Prepared Direct Testimony of R. Thomas Widney, pp. 6-7), Cities Service's system demands for gas are now far exceeded by the gas supplies currently available, and the Company allocates its purchases among producers based upon various factors, including, inter alia, customer demand, contractual obligations, availability of gas, capacity of pipeline facilities, and state proration orders. KSCC has focused solely upon price to the complete exclusion of all of these other clearly pertinent factors.

Of particular significance, KSCC ignores totally the take-or-pay provisions in Cities Service's contracts with producers. When Cities Service's purchases under many of its contracts fall below certain levels, these take-or-pay provisions are triggered and Cities Service is faced with payments for gas not taken. These payments, which are expected to be very substantial, would be added to Cities Service's rate base, with Cities Service's customers paying very significant additional costs for return and related taxes on that increased rate base. Cities Service's pattern of gas purchases is necessary to avoid or minimize such payments and the related increases in Cities Service's cost of service and thus serves the interests of Cities Service's customers. With specific regard to the reduced takes in the Kansas-Hugoton Field referred to by KSCC (Protest, p. 2), the undisputed fact is that "that field provides Cities

Service the most flexibility and greatest possibility of making "take-or-pay volumes in the future" (see pp. 3-4 of Prepared Direct Testimony of Robert E. Berney, Statement P, Docket No. RP82-114).

That these increasing take-or-pay payments are of extreme importance to Cities Service and its customers, and cannot be so blithely ignored as the KSCC assumes, is apparent from the expected magnitude of these payments. As shown in the Prepared Direct Testimony of Mr. Robert E. Berney in Docket No. RP82-114 at pages 4-5, Cities Service has estimated take-or-pay deficiencies of \$149 million in 1983 alone with a total projected deficiency of \$360 million for the four-year period 1982-86, based on pro-rata purchases by deliverability from all producers.

3/

The potential magnitude of these payments is so great that it is clearly reasonable and prudent in the best interests of its customers for Cities Service to attempt to ameliorate the amount of take-or-pay payments by increasing the proportion of the total take-or-pay gas from the Kansas-Hugoton and other lower-priced fields and thus reducing the level of its current purchases from the lower-priced fields. Indeed, the magnitude of these potential take-or-pay deficiencies based on pro rata gas purchases is so great that it is very doubtful that Cities Service would be able to borrow enough money to make the payments incurred even during just the first year. 4/

3/ These take-or-pay deficiencies would be reduced to \$170 million for the four-year period if Cities Service's proposed off-system sale pending in Docket No. CP82-302 should ultimately be authorized.

4/ The potential take-or-pay penalties of \$149 million for 1983 and \$360 million for 1983-86 can be put in perspective by comparing those amounts with Cities Service's total presently outstanding debt of \$165 million (Docket RP82-114, Statement F(3), page 1) and its total rate base of \$356 million (Docket RP82-114, Statement B).

In addition, insufficient demand for gas relative to minimum take-or-pay volumes is expected to continue for many years into the future on the Cities Service system. The effect of this is that within the next few years gas paid for but not taken could not be made up. This would require the immediate expensing of the very substantial payments involved, further increasing very substantially Cities Service's rates to its customers. 5/ Thus, the average prices to Cities Service's customers have not been "needlessly increased" (Protest, p. 2), and KSCC's statement that "the requested increase in this docket is well in excess of the increase that would be necessary to provide adequate service to Cities Service's customers" (Protest, p. 2) is grossly in error.

5. KSCC further states that "should the Commission find an absence of fraud or abuse, [KSCC] argues in the alternative that [the PGA] filing indicates imprudent management which is resulting in unreasonable natural gas costs to consumers of the Cities Service Gas Company" (Motion, p. 1), and seeks to consolidate Cities Service's PGA Docket No. TA83-1-43 with Cities Service's general rate proceeding in Docket No. RP82-114-000. For the reasons Cities Service has shown above, the Company's pattern of purchases is reasonable and indeed necessary and could not constitute "imprudence" under the Natural Gas Act. Thus, there is not even a prima facie showing for KSCC's charges of imprudence; nor is there any reason to entangle and impede Cities Service's PGA filing by consolidating it with the Company's general rate increase proceeding, which may have numerous potential issues totally unrelated to the Company's purchased gas costs.

5/ Mississippi River Transmission Corp., Docket No. RP82-48-000, order issued March 31, 1982.

6. The five-month suspension for the "maximum period allowed law as requested by KSCC (Protest, p. 1) is clearly contrary to the public interest and unjustified. First, such suspension would require Cities Service to finance approximately \$110 million in revenues it would have otherwise received from its jurisdictional customers if the PGA filing were effective during the five-month suspension period. Financing of this magnitude would be difficult if not impossible to arrange, would be expensive, would seriously impair Cities Service's financial position and would jeopardize its credit standing. Second, the suspension would mean that the deferred revenues would be collected in the subsequent summer PGA period, with carrying charges, and spread over a smaller summer sales volume, in addition to the normal PGA increase to be filed to be effective in April for the summer period. All of the foregoing would seriously prejudice Cities Service and its customers and is clearly inimical to the public interest.

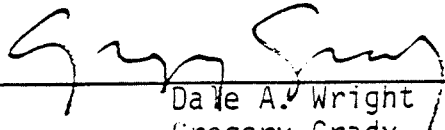
7. Midwest urges that Cities Service's PGA be suspended for "at least one day, subject to refund, and set down for hearing" (Motion, p. 3). However, there is no basis specifically articulated for such requested relief. Midwest cites an alleged "potential adverse impact of the proposed filing on many customers" and states that "a preliminary examination thereof indicates that the proposed increases may be unjust and unreasonable. . ." (Motion, p. 2). Cities Service is not aware of any aspect of its filing which could be construed as rendering the rates therein "unjust and unreasonable," and Midwest has cited none. The Commission is not empowered arbitrarily, totally without reason, to suspend such rates, as apparently proposed by Midwest.

WHEREFORE, for the foregoing reasons, the Commission should deny the requests for suspension made by KSCC and Midwest and the request for consolidation by KSCC.

Respectfully submitted,

LITTMAN, RICHTER, WRIGHT
& TALISMAN, P.C.

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Attorneys for
Cities Service Gas Company

October 8, 1982

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the official service list compiled by the Secretary in this proceeding.

Dated at Washington, D.C. this 8th day of October, 1982.

/s/ 
Gregory Grady

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& Talisman, P.C.
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Of Counsel for
Cities Service Gas Company

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

In the matter of CITIES SERVICE)
GAS COMPANY.) Docket No. TA83-1-43-000

MOTION OF KANSAS STATE CORPORATION COMMISSON
FOR LEAVE TO FILE RESPONSE
TO ANSWER OF CITIES SERVICE GAS COMPANY

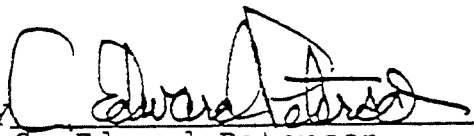
Pursuant to Rule 212 of the Commission's Rules of Practice and Procedure, 18 C.F.R. 385.212, the Kansas State Corporation Commission (KCC) hereby respectfully requests permission to respond to the Answer filed by the Cities Service Gas Company (Cities Service) in this docket.

The KCC has protested the requested increase in this docket. The Answer of Cities Service suggests that the arguments of KCC failed to acknowledge certain factors. The principal factor relied upon by Cities Service is the existence of take-or-pay provisions in its gas purchase contracts. Rather than justifying the proposed increase in this docket, Cities Service's arguments based upon take-or-pay provisions merely serve to underscore the need for investigation and hearing on this matter. The KCC seeks permission to illustrate the faults within the Answer of Cities Service.

WHEREFORE, the KCC respectfully requests that the Commission accept for filing the response of the KCC to the Answer of Cities Service Company in this matter.


Respectfully submitted,

BRIAN J. MOLINE
General Counsel

By 
C. Edward Peterson
Assistant General Counsel
State Corporation Commission
Legal Division
Fourth Floor
State Office Building
Topeka, Kansas 66612
(913) 296-2543

CERTIFICATE OF SERVICE

I hereby certify that on this 15th day of October, 1982, I mailed a true and correct copy of the above and foregoing Motion For Leave to File Response to Answer of Cities Service Gas Company in the U.S. Mail, to the Federal Energy Regulatory Commission.

BY 
C. Edward Peterson
Assistant General Counsel
State Corporation Commission
Legal Division
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State Office Building
Topeka, Kansas 66612
(913) 296-2543

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

In the matter of CITIES SERVICE) Docket No. TA83-1-43-000
GAS COMPANY.) Docket No. RP82-114-000

RESPONSE OF KANSAS STATE CORPORATION COMMISSION

Pursuant to Rule 213 of the Commission's Rules of Practice and Procedure, 18 C.F.R. 385.213, the Kansas State Corporation Commission (KCC) hereby responds to the Answer of Cities Service Gas Company (hereinafter "Answer"). The KCC states as follows:

1. By Motion of equal date, the KCC has requested permission to file this Response to Answer of Cities Service Gas Company.

2. The position of the KCC in its protest to the proposed increase in PGA tariffs is straightforward. The KCC is aware of the surplus supply of gas on the Cities Service system. (Prepared direct testimony of Robert E. Berney, Docket No. RP82-114-000, Page 3-4.) In the face of this surplus supply, Cities Service appears to have chosen to purchase from relatively expensive sources and to reduce purchases from relatively inexpensive sources. This practice results in a needless increase in the price of gas to the ultimate consumers. The KCC bases its conclusions on the following facts. During the years 1977 through 1981, Cities Service has reduced its production in the Kansas-Hugoton Field from 172.9 BCF per year to 102.3 BCF per year, or a decrease of 40.8 percent. During the same time period Cities Service reduced its total purchases from other fields by only 14%.¹/ As a consequence, the relatively expensive gas is constituting greater

1./ Exhibit No. 4 prepared by Ron Cook, Consulting Engineer. In the matter of Establishing Rules and Regulations Relating to the Production, Sales and Conservation of Natural Gas in the Hugoton Field, KCC Docket No. 134,551-C (C-20,129).

proportions of the total gas supply. Of even more concern are the changes occurring in Cities Service minimum take requirements. During the period 1979 through 1981 the proportion of total purchases of Cities Service which were purchased from take-or-pay sources of supply rose from 53.7% to 68.8%.^{2/} The increase in minimum takes was also changing relative to each source of supply as indicated by the following table:^{3/}

MINIMUM TAKE REQUIREMENTS BY SOURCE OF CITIES SERVICE GAS CO.

(Volumes in Mmcf)

<u>Source</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>6-Months 1982</u>
Oklahoma	97 094	111 113	107 904	57 118
Texas	30 460	11 108	12 141	10 671
Colorado		1 108	2 279	2 106
Wyoming	8 644	28 750	49 266	27 271
Missouri	26 446	33 143	34 440	18 047
Kansas-Hugoton	37 922	34 888	36 608	20 118
Panoma Council Grove	28 696	23 962	22 451	8 146
Total Minimum Takes	229 262	244 072	265 089	143 477

2./ Response of Cities Service Gas Company to KCC Data Request, Question 2(a), Docket No.134,551-C (C-20,129).

3./ Response of Cities Service Gas Company to KCC Data Request, Question 2(b), Docket No. 134,551-C (C020,129).

It should be noted that the most dramatic increase in minimum takes occurs from the Wyoming source of supply where most if not all gas resources are relatively expensive. The result of these practices is clearly an increased average price to consumers, which the KCC asserts may rise to the level of an unjust and unreasonable price.

3. In its Answer Cities Service raises the "defense" of take-or-pay provisions in its contracts with producers. (Answer, Page 3.) Cities argues that its purchasing patterns are for the most part dictated by the need to maintain minimum takes required under take-or-pay provisions in order to avoid payments for gas not taken. Cities also argues that these purchasing practices which result in higher average cost to consumers are actually in the consumers' best interest. (Answer, Page 4.) However, the negative effect of take-or-pay provisions upon the company and its consumers is further indication of the need for an investigation into the purchasing practices of the Cities Service Gas Company in this docket.

4. Cities Service has argued that its behavior in accordance with take-or-pay requirements constitutes prudent management. (Answer, Page 5.) Cities Service has negotiated itself into a position where it faces estimated take-or-pay deficiencies of \$149 million and \$360 million for the four-year period ending in 1986. Furthermore, it appears that Cities Service is continuing to increase take-or-pay requirements. As shown in the table appearing in Paragraph No. 2, the Minimum Take Requirements are increasing in most areas with a particularly dramatic increase in Minimum Take Requirements appearing from the Wyoming sources. In spite of Cities Service's concern over the impact of take-or-pay requirements, Cities Service apparently has continued incurring additional sources subject to take-or-pay provisions at the expense of cheaper sources of supply. Indeed, in its Answer Cities Service admits that the take-or-pay requirements have resulted in lowering current purchases from lower priced fields. (Answer, Page 4.)


5. The KCC is concerned that these practices are resulting in prices for natural gas which are unfair and unreasonable to the customers of Cities Service. Of particular concern to the KCC is the trend of increasing Minimum Take Requirements under take-or-pay provisions. Rather than ignore the importance of increasing take-or-pay payments, the KCC has protested the PGA filing and requested the Commission to study all of Cities Service's purchasing pattern. The practice of Cities Service of entering into take-or-pay contracts appears to have been particularly damaging. Take-or-pay provisions have been damaging to the company by placing it into the position of

facing serious take-or-pay deficiencies for at least the next four years. Take-or-pay contracts have been damaging to consumers by creating prices that are higher than necessary to provide service. Contractual provisions which place the pipeline and its consumers in such a disadvantaged position are at best of only questionable value to the public interest. The existence of these contractual provisions and the burden they impose on Cities Service and its consumers are not a defense in support of the PGA filing of Cities Service. Rather, the existence of the burdens posed by these contracts suggests the need for an investigation into whether Cities Service has acted prudently and reasonably during its purchasing of natural gas supplies.

WHEREFORE, the Kansas State Corporation Commission respectfully renews its request that the increase proposed by the filing of the tariffs in this docket be suspended and set for hearing.

Respectfully submitted,

BRIAN J. MOLINE
GENERAL COUNSEL

By 
C. Edward Peterson
Assistant General Counsel
State Corporation Commission
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Topeka, Kansas 66612
(913) 296-2543

VERIFICATION

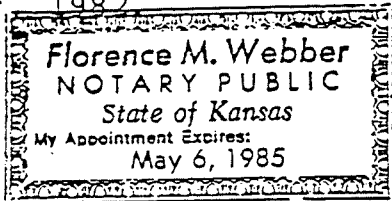
STATE OF KANSAS)
) SS
COUNTY OF SHAWNEE)

C. Edward Peterson, being first duly sworn upon oath deposes and says that he has read the foregoing document and knows the contents thereof, that he has been authorized to present the same on behalf of the State Corporation Commission of the State of Kansas, and that the facts therein stated are true and correct as he verily believes.



C. Edward Peterson

Subscribed and sworn to before me this 15th day of October, 1982




Notary Public

My Commission Expires:

CERTIFICATE OF SERVICE

This is to certify that the foregoing document has been served this _____ day of October, 1982, upon each person designated on the official list compiled by the Secretary in this proceeding in accordance with Section 210 of the Commission's Rules of Practice and Procedure.



C. Edward Peterson
Assistant General Counsel