Approved: 2-6-02

MINUTES OF THE SENATE UTILITIES COMMITTEE.

The joint meeting of the House and Senate Utilities Committees was called to order by Chairman Senator Stan Clark at 9:30 a.m. on January 28, 2002 in Room 526-S of the Capitol.

All members were present except: Senator Karin Brownlee (excused)
Senator Susan Wagle (excused)

Committee staff present: Raney Gilliland, Legislative Research
Ann McMorris, Secretary

Conferees appearing before the committee:
Ron Hein, Pioneer Natural Resources
Steve M. Hanna, Utilicorp United Energy One
Ron Gaches, El Paso Corporation

Others attending: See attached list on House Utilities Committee minutes of same date

Updates on the Natural Gas & Oil Industry

Ron Hein, legislative counsel for Pioneer Natural Resources, provided information on the activities of Pioneer Natural Resources, USA, Inc., one of the largest independent exploration and production oil and gas companies in North America, with major natural gas production in the Hugoton field in southwest Kansas. He stressed that Kansas remains one the highest taxing states in the country on oil and gas production which may be one reason for companies looking at other states for capital expenditures. He also recommended study of long range solutions given the new technology and exploration and production techniques which offer hope that additional production can be achieved from Kansas reserves. (Attachment 1)

Steve M. Hanna, regional director Kansas, Colorado, Missouri- Gas Field Operations for Utilicorp United Energy One, provided background and 2001 operations highlights on three of their Kansas companies in his responsibility area. He reviewed the 2002 budgetary outlook for Kansas and the major approved projects. (Attachment 2)

Ron Gaches, of Gaches, Braden, Barbee & Association, presented information on the El Paso Corporation plan to strengthen its capital structure and enhance its liquidity. (Attachment 3)

Chair opened the floor for questions. The committee questions covered long range planning, equity financing, coal bed methane gas exploration, gas supply for irrigation, tax structure impact on exploration and long term liability.

The next meeting of the joint committees will be on January 29, 2002.

Adjournment.

Respectfully submitted,

Ann McMorris

Attachments - 3

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**Senate Utilities Committee**
**Testimony re: Natural Gas Industry**
**Presented by Ronald R. Hein**
**on behalf of**
**Pioneer Natural Resources U.S.A., Inc.**
**January 28, 2002**

Mr. Chairman, Members of the Committee:

I am Ron Hein, legislative counsel for Pioneer Natural Resources USA, Inc., one of the largest independent exploration and production oil and gas companies in North America, with major natural gas production in the Hugoton field in Southwest Kansas.

Pioneer Natural Resources USA, Inc. resulted from the merger of MESA and Parker and Parsley in 1997. Pioneer's core properties stand out as some of the best in the industry. Pioneer's long-lived assets provide a stable production base. It has an extensive inventory of development drilling locations and boasts an active rig program in the U.S., Argentina and Canada

With total proved reserves equivalent to 3.8 trillion cubic feet of natural gas or 628 million barrels of oil and with a reserves-to-production ratio of 14 years, Pioneer's production is among the industry's most stable. Contributing to this stability are Pioneer's three domestic core properties - the Hugoton and West Panhandle gas fields and the Spraberry oil and natural gas field. These fields represent 67% of the company's total reserve base and have a reserve to production life of 17 years.

During 2000, Pioneer added 437 billion cubic feet of natural gas equivalent reserves. Pioneer drilled 296 wells with 90% success worldwide, including 83 exploration and extension wells with 73% success.

Pioneer production in Kansas is based in the Hugoton & Panoma Gas Fields located in southwest Kansas. The Hugoton is one of the largest producing gas fields in the continental United States. Pioneer's Hugoton properties represent approximately 13% of the proved reserves in the field and are located on approximately 257,000 gross acres covering approximately 400 square miles.

Pioneer has working interests in approximately 1200 wells in the Hugoton field, 985 of which it operates. Pioneer also has royalty interests in approximately 500 wells.

Pioneer owns substantially all of the gathering and processing facilities, including the Satanta plant which services the company's production from the Hugoton.

Gross Operated Wellhead Production per year is approximately 39 billion cubic feet. Pioneer has 65-75 employees located in Kansas.

Kansas remains one of the highest taxing states in the country on oil and gas production with the combination of its severance tax and its *ad valorem* (property) tax. This is especially true given the declining nature and relative size of the production in Kansas.

Although I did not have an opportunity to verify these figures based upon the most recent data, the last information I had indicated that Pioneer's production in Kansas was taxed at an overall rate of approximately 10-12% when including the 4.3% severance tax (which is a gross receipts tax) and the *ad valorem* taxes, both state and local.

To give you an indication of how this affects capital expenditures and exploration in Kansas, Oklahoma imposes a 7% severance tax, but exempts production from *ad valorem* tax. As the Hugoton field continues to decline, this high rate of tax will continue to cause the premature closing and ultimate plugging of productive wells at a time when our society will need additional fossil fuels production. This is especially unfortunate given the fact that the United States continues to be reliant on foreign oil and gas.

It is important for our state policy makers to recognize the tremendous contribution that the Kansas oil and gas industry has made to our state. It is a simple economic development fact that states should always preserve and promote the industries they have before trying to attract new industries into the state.

Without getting into details, new technology and exploration and production techniques offer hope that additional production can be achieved from Kansas reserves. At least the state should make the effort to stop the rate of decline in the Hugoton and other fields. Unfortunately, given the state of Kansas fiscal picture, now is not the time to discuss long range solutions to the natural gas industry in Kansas.

This committee has introduced and approved legislation in the past which indicates an understanding of the need to help promote the Kansas oil and gas industry, and that such promotion can also create economic development and, commensurately, additional tax revenues for the state and local government. This committee reviewing the state of the natural gas industry in these hearings is another indication of a willingness to take action today to insure the long-range success of our state in general and of southwest Kansas specifically.

Thank you very much for permitting me to testify, and I will be happy to yield to questions.

**Utilicorp United Energy One**

**Legislative Presentation - January 28, 2002**

**Regional Director Kansas, Colorado, Missouri – Gas Field Operations**
**Steve M. Hanna**
**Regional Office – 15055 Bethel Road, Platte City, Mo. 64079**
**816-737-7777 Extension 5202**

**Kansas Regional Responsibility Area – Lawrence, Wichita, & SW Kansas**

**Background and 2001 Operations Highlights**

- **Kansas demographics**

  - Kansas Public Service – Lawrence, Kansas
  - Chuck Hoag, District Director, 110 E. 9th, Lawrence, Kansas
    - Serves 29,000 Customers
    - 28 Full Time Employees
    - New Customer Additions 750
    - New Main Installation – 40,000 feet
    - Major Customers
      - University of Kansas
      - Haskell Indian Nations University
      - Hallmark Cards
      - Heinz Pet Foods
    - 2001 Capital Expenditures
      - Growth $692,000
      - Integrity $331,000
    - Gas Supply – Williams Natural Gas

  - Peoples Natural Gas – Wichita & Wichita Territory Pipeline System (WTPL)
  - Randy Lee, District Director, 3845 W. Harry Street, Wichita, Kansas
    - Serves 30,000 Customers
    - 41 Full Time Employees
    - New Customer Additions 750
    - New Main Installation 73,920 feet
    - WTPL system incorporates approximately 400 gas wells from Attica to Sterling
    - Major Customers
      - Learjet, Wichita
      - North American Salt, Lyons
      - Cargil Salt, Hutchinson
    - 2001 Expenditures
      - Growth $900.000
      - Integrity $2,100,000
    - Gas Supply – Reliant Energy, Williams Natural Gas, WTPL System

- Peoples Natural Gas – SW Kansas - Garden City, Dodge City, Liberal, and Numerous Surrounding Agricultural Communities
- District Director, Gary Wise, 2303 West Frontview, Dodge City, Kansas
    - Serves 39,000 Customers
    - 63 Full Time Employees
    - New Customer Additions 450
    - New Main Installation 48,846
    - Major Customers
        - Meat Processing Plants
        - Cattle Empire
        - Community Colleges
        - Irrigation Customers (Billing Agent for the Gathering & Transmission Operators)
    - 2001 Expenditures
        - Growth & Integrity $1,249,414
    - Gas Supply – Williams Natural Gas, Anadarko, OneOk, Duke, and Enron

- Compliance & Safety - Satisfactory Kansas Corporation Commission Compliance Safety Inspections Throughout the Responsibility Area.

## 2002 Outlook, Opportunities, & Challenges

- Budgetary Outlook
    - State of Kansas Growth & Integrity Budget $4,566,600
        - Major Approved Projects

| | |
|---|---|
| Replace the Willowbrook Infrastructure | $250,000 |
| Enhance the Sublette Irrigation System | $250,000 |
| Replace Feeder Line to Cimarron | $110,000 |
| Replace PVC Main in Lazy Acres Trailer Park | $60,000 |
| General Main & Service Replacement | $1,176,600 |
| Specific Growth Projects | $504,600 |
| General Growth Blanket Projects | $1,752,200 |
| System Integrity & Upgrade Projects | $198,700 |

- Internal Employee and Organizational Focus Opportunities & Challenges
    - "Customer Centric" Employee Launch in 1st Quarter
    - Assure Compliance to New Department of Transportation Rule Part 192 Subpart N "Operator Qualification"

# Gaches, Braden, Barbee & Associates

Comments of El Paso Corporation
Presented to Joint Meeting of
Kansas House and Senate Utilities Committees
Monday, January 28, 2002
Presented by Ron Gaches

El Paso Corporation announced on Friday, January 25th that it has initiated a plan to strengthen its capital structure and enhance its liquidity in response to recent changes in market conditions precipitated by Enron's bankruptcy. It has become clear in the last month that the market now expects energy companies to maintain lower leverage and more simplified balance sheets. El Paso's strong cash flow and large asset base enable the company to meet these changed expectations both efficiently and expediently.

The key elements of this plan are to:

- Generate approximately $2.25 billion in cash from asset sales
- Reduce capital spending to approximately $3.1 billion and generate free cash flow in excess of $1.5 billion in 2002
- Increase common equity by at least $1.3 billion through a combination of retained earnings and equity financings
- Eliminate or renegotiate the rating triggers in certain El Paso financings

This plan ensures that El Paso will remain one of the strongest and most stable competitors in the industry.

Based on current commodity prices, El Paso expects to meet earnings expectations of $3.30 per share this year and to achieve earnings per share in the range of $3.40 to $3.55 in 2002.

Senate Utilities Committee
January 28, 2002
Attachment 3-1

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"The credit requirements in our industry have changed and we have decided to implement a plan to respond proactively to that change," explained William A. Wise, president, chairman and chief executive officer of El Paso Corporation.

"El Paso Corporation has always been and will continue to be an asset and cash flow-rich company," said Wise. "Our asset portfolio is one of the most diverse and well-managed in the industry. El Paso was built on a solid foundation of assets that have generated a stream of consistent, high-quality cash flow, totaling $4.0 billion in net operating cash flow year-to-date. Our strategy continues to be centered around owning and operating quality assets, as evidenced by our ongoing investments in infrastructure across the energy value chain from pipeline expansions to power generation facilities."

El Paso's assets include 58,000 miles of interstate pipeline and associated storage facilities, 24,000 miles of gathering and intrastate pipelines, and 35 processing and treating plants. Domestically, the company generates 6,974 megawatts of power. El Paso has over 6 trillion cubic feet equivalent of natural gas reserves, is the fourth largest producer of natural gas in the country, and has one of the lowest finding costs in the industry.

El Paso continues development of an interstate pipeline project from Southeast Wyoming into Kansas, terminating in Greensburg. The formal FERC certification process will begin when El Paso has established there is sufficient producer interest to make the project viable.

"Deregulation Is Working"

By Spencer Abraham
Monday, January 14, 2002; Page A17
The Washington Post

In 2001 the nation's largest power trader, Enron, declared bankruptcy. The largest electricity distribution company, PG & E, went bankrupt. The largest independent power producer, Calpine, lost $2 billion in market capitalization in the space of a month. And the nation's largest state, California, went through a series of rolling blackouts.

These events have many people calling for a return to centrally controlled regulation in the electricity markets and for new regulations in the energy-derivative markets. But like the scientist who cut off all the legs of a frog, yelled at it to jump and, when it remained motionless, recorded in his lab book, "A frog with no legs goes deaf," we should be careful about the lessons drawn from these events.

Consider what did not happen in 2001. Gasoline prices did not surge; they dropped. Electricity prices did not continue climbing; they dropped. Natural gas prices did not increase; they dropped. In the face of Enron's collapse, the largest bankruptcy in U.S. history, there were no price spikes, no trading panics, no electricity outages and no gas shortages. On the contrary, we've added some 51,000 megawatts of electricity this year and some 99,000 are scheduled to come on line in 2002. That's more power added to our economy than at any time in history.

The lesson California can draw from the events of 2001 is not the one I've heard recently: "Deregulation is to blame." The lesson is simpler and more classic: Prices respond to scarcity. The state averted electricity outages this summer largely by reducing demand, much of that associated with a declining economy, passing on price increases to consumers and mild weather. But we can't count on the weather, and we need California's economy to grow. What's more, the state still faces a problem: Not enough new power generation has been built, and new generation still is not being encouraged.

Those who see an answer to today's challenges in re-regulation seem to have forgotten the abuses of the past: utilities that engaged in massive building programs unrelated to customer needs; billions of dollars of "stranded" costs (investments that served no useful purpose) imposed on rate payers; bloated budgets and inaction in the face of need.

State planning is no substitute for transparent and competitive markets; just ask Californians who will be paying long-term above-market prices for energy that the state bought at the height of the crisis.

There seems to be an unseemly amount of glee in some circles over Enron's collapse. This is a disservice to the human dimension of Enron's failure. Thousands have lost their jobs, and longtime employees have seen their retirement savings evaporate.

So far, there is no indication that the energy side of Enron's business was the cause of its collapse. The trading functions that Enron performed played a central role in providing market liquidity and risk allocation. Enron was a pioneer in this market, a market that has grown from almost nothing in 1994 to nearly 900 billion kilowatt hours now. Part of the reason the markets adjusted so smoothly to the Enron collapse was the liquidity and risk allocation provided by the wholesale markets Enron had helped create.

None of this is to excuse the actions of Enron management that caused the collapse. There will and should be comprehensive investigations of Enron. We need to send a message to the market that abuses will not be tolerated. But we need to send an equally clear message that we are moving forward with open and competitive electricity markets.

Reacting to the uncertainty created by this year's events, the power generation sector has been hit hard by the markets. Investors are wondering if we are going to continue on the path to open markets or are going to turn back the clock.

Electricity is too important to our economy to suffer through a return to central planning or extended indecision. We need more power plants; we need to upgrade our transmission systems; we need to invest in the new technologies that will move us toward a future of even more clean and efficient generation capacity, with diverse fuels from coal to natural gas to renewables.

The President's National Energy Plan proposes these steps and more. There exists significant bipartisan support for reform. Congress now has the opportunity to ensure we benefit the American consumer and our economy by fostering a more competitive and reliable electricity market.