ONEOK INC /NEW/
Form 10-Q
April 29, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

# FORM 10-Q

X Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended March 31, 2010
OR
___ Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from __________ to __________.

Commission file number 001-13643

ONEOK, Inc.
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Oklahoma<br>(State or other jurisdiction of incorporation or organization) | 73-1520922<br>(I.R.S. Employer Identification No.) |
| 100 West Fifth Street, Tulsa, OK<br>(Address of principal executive offices) | 74103<br>(Zip Code) |

Registrant's telephone number, including area code (918) 588-7000

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days. Yes X No __

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every
Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes X No __

Indicate by checkmark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.
Large accelerated filer X Accelerated filer __ Non-accelerated filer __ Smaller reporting company__

Indicate by checkmark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes __ No X

On April 22, 2010, the Company had 106,295,263 shares of common stock outstanding.

ONEOK, Inc.
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As used in this Quarterly Report, references to "we," "our" or "us" refer to ONEOK, Inc., an Oklahoma corporation, and its predecessors and subsidiaries, unless the context indicates otherwise.

The statements in this Quarterly Report that are not historical information, including statements concerning plans and objectives of management for future operations, economic performance or related assumptions, are forward-looking statements. Forward-looking statements may include words such as "anticipate," "estimate," "expect," "project," "intend," "pl "believe," "should," "goal," "forecast," "guidance," "could," "may," "continue," "might," "potential," "scheduled" and other w of similar meaning. Although we believe that our expectations regarding future events are based on reasonable assumptions, we can give no assurance that such expectations and assumptions will be achieved. Important factors that could cause actual results to differ materially from those in the forward-looking statements are described under Part I, Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations, "Forward-Looking Statements" and Part II, Item 1A, "Risk Factors" in this Quarterly Report and under Part I, Item 1A, "Risk Factors," in our Annual Report.

INFORMATION AVAILABLE ON OUR WEB SITE

We make available on our Web site copies of our Annual Report, Quarterly Reports, Current Reports on Form 8-K, amendments to those reports filed or furnished to the SEC pursuant to Section 13(a) or 15(d) of the Exchange Act and reports of holdings of our securities filed by our officers and directors under Section 16 of the Exchange Act as soon as reasonably practicable after filing such material electronically or otherwise furnishing it to the SEC. Our Web site and any contents thereof are not incorporated by reference into this report.

We also make available on our Web site the Interactive Data Files required to be submitted and posted pursuant to Rule 405 of Regulation S-T. In accordance with Rule 402 of Regulation S-T, the Interactive Data Files shall not be deemed to be "filed" for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section, and shall not be incorporated by reference into any registration statement or other document filed under the Securities Act or the Exchange Act, except as shall be expressly set forth by specific reference in such filing.

GLOSSARY

The abbreviations, acronyms and industry terminology used in this Quarterly Report are defined as follows:

| | |
|---|---|
| AFUDC… | Allowance for funds used during construction |
| Annual Report | Annual Report on Form 10-K for the year ended December 31, 2009 |
| ASU | Accounting Standards Update |
| Bbl | Barrels, one barrel is equivalent to 42 United States gallons |
| Bbl/d | Barrels per day |
| BBtu/d | Billion British thermal units per day |
| Bcf | Billion cubic feet |
| Bcf/d | Billion cubic feet per day |
| Btu(s) | British thermal units, a measure of the amount of heat required to raise the temperature of one pound of water one degree Fahrenheit |
| Bushton Plant | Bushton Gas Processing Plant |
| Clean Air Act | Federal Clean Air Act, as amended |
| Clean Water Act | Federal Water Pollution Control Act Amendments of 1972, as amended |
| EBITDA | Earnings before interest, taxes, depreciation and amortization |
| EPA | United States Environmental Protection Agency |
| Exchange Act | Securities Exchange Act of 1934, as amended |
| FASB | Financial Accounting Standards Board |
| FERC | Federal Energy Regulatory Commission |
| GAAP | Accounting principles generally accepted in the United States of America |
| KCC | Kansas Corporation Commission |
| KDHE | Kansas Department of Health and Environment |
| LDCs | Local distribution companies |
| LIBOR | London Interbank Offered Rate |
| MBbl | Thousand barrels |
| MBbl/d | Thousand barrels per day |
| Mcf | Thousand cubic feet |
| MMBbl | Million barrels |
| MMBtu | Million British thermal units |
| MMBtu/d | Million British thermal units per day |
| MMcf | Million cubic feet |
| MMcf/d | Million cubic feet per day |
| Moody's | Moody's Investors Service, Inc. |
| NGL products | Marketable natural gas liquid purity products, such as ethane, ethane/propane mix, propane, iso-butane, normal butane and natural gasoline |
| NGL(s) | Natural gas liquid(s) |
| Northern Border Pipeline | Northern Border Pipeline Company |
| NYMEX | New York Mercantile Exchange |
| OBPI | ONEOK Bushton Processing Inc. |
| OCC | Oklahoma Corporation Commission |
| ONEOK | ONEOK, Inc. |
| ONEOK Credit Agreement | ONEOK's $1.2 billion Amended and Restated Credit Agreement dated July 14, 2006 |
| ONEOK Partners | ONEOK Partners, L.P. |

| | |
|---|---|
| ONEOK Partners Credit Agreement............. | ONEOK Partners' $1.0 billion Amended and Restated Revolving Credit Agreement dated March 30, 2007 |
| ONEOK Partners GP...................................... | ONEOK Partners GP, L.L.C., a wholly owned subsidiary of ONEOK and the sole general partner of ONEOK Partners |
| OPIS.................................................................. | Oil Price Information Service |
| Overland Pass Pipeline Company................ | Overland Pass Pipeline Company LLC |
| Quarterly Report(s)........................................ | Quarterly Report(s) on Form 10-Q |
| S&P.................................................................. | Standard & Poor's Rating Group |
| SEC.................................................................. | Securities and Exchange Commission |
| Securities Act................................................. | Securities Act of 1933, as amended |
| XBRL................................................................ | eXtensible Business Reporting Language |

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PART I - FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS
ONEOK, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF INCOME

| | Three Months Ended March 31, | |
|---|---|---|
| (Unaudited) | 2010 | 2009 |
| | (Thousands of dollars, except per share amounts) | |
| Revenues | $ 3,923,967 | $ 2,789,827 |
| Cost of sales and fuel | 3,304,648 | 2,238,416 |
| Net margin | 619,319 | 551,411 |
| Operating expenses | | |
| Operations and maintenance | 180,272 | 161,719 |
| Depreciation and amortization | 77,856 | 72,126 |
| General taxes | 23,073 | 25,227 |
| Total operating expenses | 281,201 | 259,072 |
| Gain (loss) on sale of assets | (786) | 664 |
| Operating income | 337,332 | 293,003 |
| Equity earnings from investments (Note J) | 21,116 | 21,222 |
| Allowance for equity funds used during construction | 247 | 9,003 |
| Other income | 2,909 | 1,665 |
| Other expense | (1,053) | (3,944) |
| Interest expense | (76,520) | (77,961) |
| Income before income taxes | 284,031 | 242,988 |
| Income taxes | (97,311) | (79,439) |
| Net income | 186,720 | 163,549 |
| Less: Net income attributable to noncontrolling interests | 32,181 | 41,264 |
| Net income attributable to ONEOK | $ 154,539 | $ 122,285 |
| | | |
| Earnings per share of common stock (Note K) | | |
| Net earnings per share, basic | $ 1.46 | $ 1.16 |
| Net earnings per share, diluted | $ 1.44 | $ 1.16 |
| | | |
| Average shares of common stock (thousands) | | |
| Basic | 106,132 | 105,162 |
| Diluted | 107,410 | 105,733 |
| | | |
| Dividends declared per share of common stock | $ 0.44 | $ 0.40 |

See accompanying Notes to Consolidated Financial Statements.

ONEOK, Inc. and Subsidiaries
CONSOLIDATED BALANCE SHEETS

| (Unaudited) | March 31, 2010 | December 31, 2009 |
|---|---|---|
| Assets | (Thousands of dollars) | |
| Current assets | | |
| Cash and cash equivalents | $ 167,433 | $ 29,399 |
| Accounts receivable, net | 1,202,293 | 1,437,994 |
| Gas and natural gas liquids in storage | 397,254 | 583,127 |
| Commodity imbalances | 96,487 | 186,015 |
| Energy marketing and risk management assets (Notes B and C) | 156,086 | 113,039 |
| Other current assets | 89,175 | 238,890 |
| Total current assets | 2,108,728 | 2,588,464 |
| | | |
| Property, plant and equipment | | |
| Property, plant and equipment | 10,205,835 | 10,145,800 |
| Accumulated depreciation and amortization | 2,411,431 | 2,352,142 |
| Net property, plant and equipment | 7,794,404 | 7,793,658 |
| | | |
| Investments and other assets | | |
| Goodwill and intangible assets | 1,028,643 | 1,030,560 |
| Energy marketing and risk management assets (Notes B and C) | 22,547 | 23,125 |
| Investments in unconsolidated affiliates | 762,435 | 765,163 |
| Other assets | 612,435 | 626,713 |
| Total investments and other assets | 2,426,060 | 2,445,561 |
| Total assets | $ 12,329,192 | $ 12,827,683 |

See accompanying Notes to Consolidated Financial Statements.

ONEOK, Inc. and Subsidiaries
CONSOLIDATED BALANCE SHEETS

| (Unaudited) | March 31, 2010 | December 31, 2009 |
|---|---|---|
| Liabilities and shareholders' equity | (Thousands of dollars) | |
| Current liabilities | | |
| Current maturities of long-term debt | $493,220 | $268,215 |
| Notes payable (Note E) | 310,000 | 881,870 |
| Accounts payable | 965,015 | 1,240,207 |
| Commodity imbalances | 246,540 | 394,971 |
| Energy marketing and risk management liabilities (Notes B and C) | 75,119 | 65,162 |
| Other current liabilities | 581,622 | 488,487 |
| Total current liabilities | 2,671,516 | 3,338,912 |
| | | |
| Long-term debt, excluding current maturities | 4,103,333 | 4,334,204 |
| | | |
| Deferred credits and other liabilities | | |
| Deferred income taxes | 1,033,396 | 1,037,665 |
| Energy marketing and risk management liabilities (Notes B and C) | 13,115 | 8,926 |
| Other deferred credits | 628,191 | 662,514 |
| Total deferred credits and other liabilities | 1,674,702 | 1,709,105 |
| | | |
| Commitments and contingencies (Note H) | | |
| | | |
| Shareholders' equity (Note F) | | |
| ONEOK shareholders' equity: | | |
| Common stock, $0.01 par value: | | |
| authorized 300,000,000 shares; issued 122,545,085 shares and outstanding 106,283,759 shares at March 31, 2010; issued 122,394,015 shares and outstanding 105,906,776 shares at December 31, 2009 | 1,225 | 1,224 |
| Paid-in capital | 1,365,591 | 1,322,340 |
| Accumulated other comprehensive loss (Note D) | (105,564) | (118,613) |
| Retained earnings | 1,793,548 | 1,685,710 |
| Treasury stock, at cost: 16,261,326 shares at March 31, 2010 and 16,487,239 shares at December 31, 2009 | (674,103) | (683,467) |
| Total ONEOK shareholders' equity | 2,380,697 | 2,207,194 |
| | | |
| Noncontrolling interests in consolidated subsidiaries | 1,498,944 | 1,238,268 |
| | | |
| Total shareholders' equity | 3,879,641 | 3,445,462 |
| Total liabilities and shareholders' equity | $12,329,192 | $12,827,683 |

See accompanying Notes to Consolidated Financial Statements.

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ONEOK, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF CASH FLOWS

| (Unaudited) | Three Months Ended March 31, 2010 | 2009 |
|---|---|---|
| | (Thousands of dollars) | |
| Operating activities | | |
| Net income | $186,720 | $163,549 |
| Depreciation and amortization | 77,856 | 72,126 |
| Allowance for equity funds used during construction | (247) | (9,003) |
| Loss (gain) on sale of assets | 786 | (664) |
| Equity earnings from investments | (21,116) | (21,222) |
| Distributions received from unconsolidated affiliates | 21,998 | 25,187 |
| Deferred income taxes | 19,542 | 23,624 |
| Share-based compensation expense | 4,566 | 4,173 |
| Allowance for doubtful accounts | (221) | (822) |
| Changes in assets and liabilities: | | |
| Accounts receivable | 235,922 | 251,980 |
| Gas and natural gas liquids in storage | 177,305 | 404,416 |
| Accounts payable | (268,987) | (311,252) |
| Commodity imbalances, net | (58,903) | (51,317) |
| Unrecovered purchased gas costs | 98,783 | 42,445 |
| Accrued interest | 43,133 | 38,623 |
| Energy marketing and risk management assets and liabilities | 24,522 | (32,921) |
| Fair value of firm commitments | (23,023) | 153,391 |
| Other assets and liabilities | 40,081 | 38,545 |
| Cash provided by operating activities | 558,717 | 790,858 |
| Investing activities | | |
| Changes in investments in unconsolidated affiliates | 1,334 | 3,362 |
| Capital expenditures (less allowance for equity funds used during construction) | (68,273) | (243,027) |
| Proceeds from sale of assets | 563 | 1,083 |
| Cash used in investing activities | (66,376) | (238,582) |
| Financing activities | | |
| Repayment of notes payable, net | (571,870) | (813,300) |
| Repayment of notes payable with maturities over 90 days | - | (470,000) |
| Issuance of debt, net of discounts | - | 498,325 |
| Long-term debt financing costs | - | (4,000) |
| Repayment of debt | (3,333) | (104,037) |
| Repurchase of common stock | (5) | (247) |
| Issuance of common stock | 4,663 | 2,509 |
| Issuance of common units of ONEOK Partners, net of discounts | 322,721 | - |
| Dividends paid | (46,701) | (42,080) |
| Distributions to noncontrolling interests | (59,782) | (52,751) |
| Cash used in financing activities | (354,307) | (985,581) |
| Change in cash and cash equivalents | 138,034 | (433,305) |
| Cash and cash equivalents at beginning of period | 29,399 | 510,058 |
| Cash and cash equivalents at end of period | $167,433 | $76,753 |

See accompanying Notes to Consolidated Financial Statements.

ONEOK, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

| | ONEOK Shareholders' Equity | | | |
|---|---|---|---|---|
| (Unaudited) | Common Stock Issued (Shares) | Common Stock (Thousands of dollars) | Paid-in Capital | Accumulated Other Comprehensive Income (Loss) |
| December 31, 2009 | 122,394,015 | $1,224 | $1,322,340 | $ (118,613 ) |
| Net income | - | - | - | - |
| Other comprehensive income | - | - | - | 13,049 |
| Repurchase of common stock | - | - | - | - |
| Common stock issued | 151,070 | 1 | (7,480 ) | - |
| Common stock dividends - | | | | |
| $0.44 per share | - | - | - | - |
| Issuance of common units of ONEOK Partners | - | - | 50,731 | - |
| Distributions to noncontrolling interests | - | - | - | - |
| March 31, 2010 | 122,545,085 | $1,225 | $1,365,591 | $ (105,564 ) |

See accompanying Notes to Consolidated Financial Statements.

ONEOK, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(Continued)

| (Unaudited) | ONEOK Shareholders' Equity | | | |
|---|---|---|---|---|
| | Retained Earnings | Treasury Stock | Noncontrolling Interests in Consolidated Subsidiaries | Total Shareholders' Equity |
| | (Thousands of dollars) | | | |
| December 31, 2009 | $1,685,710 | $(683,467) | $ 1,238,268 | $ 3,445,462 |
| Net income | 154,539 | - | 32,181 | 186,720 |
| Other comprehensive income | - | - | 16,287 | 29,336 |
| Repurchase of common stock | - | (5) | - | (5) |
| Common stock issued | - | 9,369 | - | 1,890 |
| Common stock dividends - $0.44 per share | (46,701) | - | - | (46,701) |
| Issuance of common units of ONEOK Partners | - | - | 271,990 | 322,721 |
| Distributions to noncontrolling interests | - | - | (59,782) | (59,782) |
| March 31, 2010 | $1,793,548 | $(674,103) | $ 1,498,944 | $ 3,879,641 |

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ONEOK, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

| (Unaudited) | Three Months Ended March 31, 2010 | Three Months Ended March 31, 2009 |
|---|---|---|
| | (Thousands of dollars) | |
| Net income | $186,720 | $163,549 |
| Other comprehensive income (loss), net of tax | | |
| Unrealized gains on energy marketing and risk management assets/liabilities, net of tax of $(18,839) and $(38,232), respectively | 43,489 | 60,497 |
| Realized gains in net income, net of tax of $8,022 and $27,678, respectively | (10,058) | (53,919) |
| Unrealized holding gains (losses) on available-for-sale securities, net of tax of $62 and $(118), respectively | (97) | 188 |
| Change in pension and postretirement benefit plan liability, net of tax of $2,533 and $1,599, respectively | (4,016) | (2,534) |
| Other, net of tax of $(11) and $(51), respectively | 18 | 190 |
| Total other comprehensive income, net of tax | 29,336 | 4,422 |
| Comprehensive income | 216,056 | 167,971 |
| Less: Comprehensive income attributable to noncontrolling interests | 48,468 | 31,222 |
| Comprehensive income attributable to ONEOK | $167,588 | $136,749 |

See accompanying Notes to Consolidated Financial Statements.

ONEOK, Inc. and Subsidiaries
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

## A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Our accompanying unaudited consolidated financial statements have been prepared in accordance with GAAP and reflect all adjustments that, in our opinion, are necessary for a fair presentation of the results for the interim periods presented. All such adjustments are of a normal recurring nature. The 2009 year-end consolidated balance sheet data was derived from audited financial statements but does not include all disclosures required by GAAP. These unaudited consolidated financial statements should be read in conjunction with our audited consolidated financial statements in our Annual Report. Due to the seasonal nature of our business, the results of operations for the three months ended March 31, 2010, are not necessarily indicative of the results that may be expected for a 12-month period.

Our significant accounting policies are consistent with those disclosed in Note A of the Notes to Consolidated Financial Statements in our Annual Report.

Recently Issued Accounting Updates

The following recently issued accounting standards updates affect our consolidated financial statements and related disclosures:

Fair Value Measurements and Disclosures - In January 2010, the FASB issued ASU 2010-06, "Improving Disclosures about Fair Value Measurements," which established new disclosure requirements and clarified existing requirements for disclosures of fair value measurements. ASU 2010-06 required us to add two new disclosures, when applicable: (i) transfers in and out of Level 1 and 2 fair value measurements including the reasons for the transfers, and (ii) a gross presentation of activity within the reconciliation of Level 3 fair value measurements. Except for separate disclosure of purchases, sales, issuances and settlements in the reconciliation of our Level 3 fair value measurements, we applied this guidance to our disclosures beginning with this Quarterly Report. The separate disclosure of purchases, sales, issuances and settlements in the reconciliation of our Level 3 fair value measurements will be required beginning with our March 31, 2011, Quarterly Report, and we do not expect the impact to be material. ASU 2010-06 requires prospective application in the period of adoption, and we have not recast our prior-year disclosures. See Note B for more discussion of our fair value measurements.

Our policy for calculating transfers between levels of the fair value hierarchy recognizes the transfer as of the end of each reporting period. Prior to January 1, 2010, our policy of calculating transfers recognized transfers in at the end of the reporting period and transfers out at the beginning of the reporting period. Therefore, transfers into and out of Level 3 and included in earnings may not be comparable with prior periods.

Embedded Credit Derivatives - In March 2010, the FASB issued ASU 2010-11, "Scope Exception Related to Embedded Credit Derivatives," which clarified that disclosures required for credit derivatives do not apply to an embedded derivative's feature related to the transfer of credit risk that is only in the form of subordination of one financial instrument to another. This guidance will be effective for our September 30, 2010, Quarterly Report and will be applied prospectively. We are currently reviewing the applicability of ASU 2010-11 to our consolidated financial statement and related disclosures.

## B. FAIR VALUE MEASUREMENTS

Determining Fair Value - We define fair value as the price that would be received from the sale of an asset or the transfer of a liability in an orderly transaction between market participants at the measurement date. We use the market and income approaches to determine the fair value of our assets and liabilities and consider the markets in which the transactions are executed. While many of the contracts in our portfolio are executed in liquid markets where price transparency exists, some contracts are executed in markets for which market prices may exist but the market may be relatively inactive. This results in limited price transparency that requires management's judgment and assumptions to estimate fair values. Inputs into our fair value estimates include commodity exchange prices, over-the-counter quotes, volatility, historical correlations of pricing data and LIBOR and other liquid money market instrument rates. We also utilize internally developed basis curves that incorporate observable and unobservable market data. We validate our valuation inputs with third-party information and settlement prices from other sources, where available. In addition, as prescribed by the income approach, we compute the fair value of our derivative portfolio by discounting the projected future cash flows from our derivative assets and liabilities to present value using interest rate yields to calculate present-value discount factors derived from LIBOR, Eurodollar futures and U.S. Treasury swaps. We also take into consideration the potential impact on market prices of liquidating positions in an orderly manner over a reasonable period of time under current market conditions. We consider current market data in evaluating counterparties', as well as our own, nonperformance risk, net of collateral, by using specific and sector bond yields and also monitoring the credit default swap markets. Although we use our best estimates to determine the fair value of the derivative contracts we have executed, the ultimate market prices realized could differ from our estimates, and the differences could be material.

Recurring Fair Value Measurements - The following tables set forth our recurring fair value measurements for the periods indicated:

| | March 31, 2010 | | | | |
|---|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Netting | Total |
| | (Thousands of dollars) | | | | |
| Assets | | | | | |
| Derivatives (a) | | | | | |
| Commodity Contracts | | | | | |
| Exchange-traded contracts | $ 134,991 | $ - | $ - | $ - | $ 134,991 |
| Over-the-counter financial contracts | - | 62,962 | 518,619 | - | 581,581 |
| Physical contracts | - | 12,734 | 52,007 | - | 64,741 |
| Foreign Exchange Contracts | 73 | - | - | - | 73 |
| Netting | - | - | - | (602,753 ) | (602,753 ) |
| Total derivatives | 135,064 | 75,696 | 570,626 | (602,753 ) | 178,633 |
| Trading securities (b) | 7,458 | - | - | - | 7,458 |
| Available-for-sale investment securities (c) | 2,529 | - | - | - | 2,529 |
| Total assets | $ 145,051 | $ 75,696 | $ 570,626 | $ (602,753 ) | $ 188,620 |
| | | | | | |
| Liabilities | | | | | |
| Derivatives (a) | | | | | |
| Commodity Contracts | | | | | |
| Exchange-traded contracts | $ (140,926 ) | $ - | $ - | $ - | $ (140,926 ) |
| Over-the-counter financial contracts | - | (56,685 ) | (401,329 ) | - | (458,014 ) |
| Physical contracts | - | (4,423 ) | (21,724 ) | - | (26,147 ) |
| Netting | - | - | - | 536,853 | 536,853 |
| Total derivatives | (140,926 ) | (61,108 ) | (423,053 ) | 536,853 | (88,234 ) |
| Fair value of firm commitments (d) | - | - | (111,597 ) | - | (111,597 ) |
| Total liabilities | $ (140,926 ) | $ (61,108 ) | $ (534,650 ) | $ 536,853 | $ (199,831 ) |

(a) - Our derivative assets and liabilities are presented in our Consolidated Balance Sheets as energy marketing and risk management assets and liabilities on a net basis. We net derivative assets and liabilities, including cash collateral, when a legally enforceable master-netting arrangement exists between the counterparty to a derivative contract and us. At March 31, 2010, we held $70.5 million of cash collateral and had posted $4.6 million of cash collateral with various counterparties.
(b) - Our trading securities are presented in our Consolidated Balance Sheets as other current assets.
(c) - Our available-for-sale investment securities are presented in our Consolidated Balance Sheets as other assets.
(d) - Our fair value of firm commitments are presented in our Consolidated Balance Sheets as other current liabilities and other deferred credits.

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| | December 31, 2009 | | | | |
|---|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Netting | Total |
| | (Thousands of dollars) | | | | |
| Assets | | | | | |
| Derivatives (a) | $149,034 | $4,898 | $672,631 | $(690,399 ) | $136,164 |
| Trading securities (b) | 7,927 | - | - | - | 7,927 |
| Available-for-sale investment securities (c) | 2,688 | - | - | - | 2,688 |
| Total assets | $159,649 | $4,898 | $672,631 | $(690,399 ) | $146,779 |
| | | | | | |
| Liabilities | | | | | |
| Derivatives (a) | $(109,713 ) | $(8,481 ) | $(535,937 ) | $580,043 | $(74,088 ) |
| Fair value of firm commitments (d) | - | - | (134,620 ) | - | (134,620 ) |
| Total liabilities | $(109,713 ) | $(8,481 ) | $(670,557 ) | $580,043 | $(208,708 ) |

(a) - Our derivative assets and liabilities are presented in our Consolidated Balance Sheets as energy marketing and risk management assets and liabilities on a net basis. We net derivative assets and liabilities, including cash collateral, when a legally enforceable master-netting arrangement exists between the counterparty to a derivative contract and us. At December 31, 2009, we held $136.5 million of cash collateral and had posted $26.1 million of cash collateral with various counterparties.
(b) - Our trading securities are presented in our Consolidated Balance Sheets as other current assets.
(c) - Our available-for-sale investment securities are presented in our Consolidated Balance Sheets as other assets.
(d) - Our fair value of firm commitments are presented in our Consolidated Balance Sheets as other current liabilities and other deferred credits.

We categorize derivatives for which fair value is determined using multiple inputs within a single level, based on the lowest level input that is significant to the fair value measurement in its entirety.

Our Level 1 fair value measurements are based on NYMEX-settled prices, actively quoted prices for equity securities and foreign currency forward exchange rates.  These balances are predominantly comprised of exchange-traded derivative contracts, including futures and certain options for natural gas and crude oil, which are valued based on unadjusted quoted prices in active markets.  Also included in Level 1 are equity securities and foreign currency forwards.

Our Level 2 fair value inputs are based on NYMEX-settled prices for natural gas and crude oil that are utilized to determine the fair value of certain non-exchange traded financial instruments, including natural gas and crude oil swaps, as well as physical forwards.

For the three months ended March 31, 2010, there were no transfers between levels 1 and 2.

Our Level 3 inputs include internally developed basis curves incorporating observable and unobservable market data, NGL price curves from a pricing service, historical correlations of NGL product prices to published NYMEX crude oil prices, market volatilities derived from the most recent NYMEX close spot prices and forward LIBOR curves, and adjustments for the credit risk of our counterparties.  We corroborate the data on which our fair value estimates are based using our market knowledge of recent transactions, analysis of historical correlations and validation with independent broker quotes or a pricing service.  The derivatives categorized as Level 3 include natural gas basis swaps, swing swaps, options and physical forward contracts, NGL swaps and interest-rate swaps.  Also included in Level 3 are the fair values of firm commitments and long-term debt that have been hedged.  We do not believe that our Level 3 fair value estimates have a material impact on our results of operations, as the majority of our derivatives are accounted for as hedges for which ineffectiveness is not material.

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The following tables set forth the reconciliation of our Level 3 fair value measurements for the periods indicated:

| | Derivative Assets (Liabilities) | Fair Value of Firm Commitments | Total |
|---|---|---|---|
| | (Thousands of dollars) | | |
| January 1, 2010 | $136,694 | $ (134,620 ) | $2,074 |
| Total realized/unrealized gains (losses): | | | |
| Included in earnings (a) | (4,496 ) | 23,023 | 18,527 |
| Included in other comprehensive income (loss) | 13,222 | - | 13,222 |
| Transfers into Level 3 | 1,468 | - | 1,468 |
| Transfers out of Level 3 | 685 | - | 685 |
| March 31, 2010 | $147,573 | $ (111,597 ) | $35,976 |
| Total gains (losses) for the period included in earnings attributable to the change in unrealized gains (losses) relating to assets and liabilities still held as of March 31, 2010 (a) | $18,458 | $ (7,046 ) | $11,412 |

(a) - Reported in revenues and cost of sales and fuel in our Consolidated Statements of Income.

| | Derivative Assets (Liabilities) | Fair Value of Firm Commitments | Long-Term Debt | Total |
|---|---|---|---|---|
| | | (Thousands of dollars) | | |
| January 1, 2009 | $ 42,355 | $ 42,179 | $ (171,455 ) | $ (86,921 ) |
| Total realized/unrealized gains (losses): | | | | |
| Included in earnings | 110,002 (a) | (153,391 ) (a) | 1,455 (b) | (41,934 ) |
| Included in other comprehensive income (loss) | (7,730 ) | - | - | (7,730 ) |
| Maturities | - | - | 100,000 | 100,000 |
| Terminations prior to maturity | - | - | 70,000 | 70,000 |
| Transfers in and/or out of Level 3 | 25,611 | - | - | 25,611 |
| March 31, 2009 | $ 170,238 | $ (111,212 ) | $ - | $ 59,026 |
| Total gains (losses) for the period included in earnings attributable to the change in unrealized gains (losses) relating to assets and liabilities still held as of March 31, 2009 (a) | $ 136,563 | $ (138,637 ) | $ - | $ (2,074 ) |

(a) - Reported in revenues and cost of sales and fuel in our Consolidated Statements of Income.

(b) - Reported in interest expense in our Consolidated Statements of Income.

Realized/unrealized gains (losses) include the realization of our derivative contracts through maturity and changes in fair value of our hedged firm commitments and fixed-rate debt swapped to a floating rate. Maturities represent the long-term debt associated with an interest-rate swap that matured during the period. Terminations prior to maturity represent the long-term debt associated with an interest-rate swap that was terminated during the period. Transfers into Level 3 represent existing assets or liabilities that were previously categorized at a higher level for which the unobservable inputs became a more significant portion of the fair value estimates. Transfers out of Level 3 represent existing assets and liabilities that were previously classified as Level 3 for which the observable inputs became a more significant portion of the fair value estimates.

Other Financial Instruments - The approximate fair value of cash and cash equivalents, accounts receivable and accounts payable is equal to book value, due to the short-term nature of these items. The fair value of notes payable approximates the carrying value since the interest rates, prescribed by each borrowing's respective credit agreement, are periodically adjusted to reflect current market conditions.

The estimated fair value of long-term debt, including current maturities, was $4.9 billion at March 31, 2010, and $4.8 billion at December 31, 2009. The book value of long-term debt, including current maturities, was $4.6 billion at March 31, 2010, and $4.6 billion at December 31, 2009. The estimated fair value of long-term debt has been determined using quoted market prices of the same or similar issues with similar terms and maturities.

## C. RISK MANAGEMENT AND HEDGING ACTIVITIES USING DERIVATIVES

Our Energy Services and ONEOK Partners segments are exposed to various risks that we manage by periodically entering into derivative instruments. These risks include the following:

- Commodity price risk - We are exposed to the risk of loss in cash flows and future earnings arising from adverse changes in the price of natural gas, NGLs and crude oil. We use commodity derivative instruments such as futures, physical forward contracts, swaps and options to mitigate the commodity price risk associated with a portion of the forecasted purchases and sales of commodities and natural gas and natural gas liquids in storage;
- Basis risk - We are exposed to the risk of loss in cash flows and future earnings arising from adverse changes in the price differentials between pipeline receipt and delivery locations. Our firm transportation capacity allows us to purchase gas at a pipeline receipt point and sell gas at a pipeline delivery point. Our Energy Services segment periodically enters into basis swaps between the transportation receipt and delivery points in order to protect the fair value of these location price differentials related to our firm commitments; and
- Currency exchange rate risk - As a result of our Energy Services segment's activities in Canada, we are exposed to the risk of loss in cash flows and future earnings from adverse changes in currency exchange rates on our commodity purchases and sales primarily related to our firm transportation and storage contracts that are transacted in a currency other than our functional currency, the U.S. dollar. To reduce our exposure to exchange-rate fluctuations, we use physical forward transactions, which result in an actual two-way flow of currency on the settlement date in which we exchange U.S. dollars for Canadian dollars with another party.

The following derivative instruments are used to manage our exposure to these risks:

- Futures contracts - Standardized exchange-traded contracts to purchase or sell natural gas or crude oil at a specified price, requiring delivery on or settlement through the sale or purchase of an offsetting contract by a specified future date under the provisions of exchange regulations;
- Forward contracts - Commitments to purchase or sell natural gas, crude oil or NGLs for delivery at some specified time in the future. We also use currency forward contracts to manage our currency exchange rate risk. Forward contracts are different from futures in that forwards are customized and non-exchange traded;
- Swaps - Financial trades involving the exchange of payments based on two different pricing structures for a commodity. In a typical commodity swap, parties exchange payments based on changes in the price of a commodity or a market index, while fixing the price they effectively pay or receive for the physical commodity. As a result, one party assumes the risks and benefits of movements in market prices, while the other party assumes the risks and benefits of a fixed price for the commodity; and
- Options - Contractual agreements that give the holder the right, but not the obligation, to buy or sell a fixed quantity of a commodity, at a fixed price, within a specified period of time. Options may either be standardized and exchange traded or customized and non-exchange traded.

Our objectives for entering into such contracts include, but are not limited to:

- reducing the variability of cash flows by locking in the price for all or a portion of anticipated index-based physical purchases and sales, transportation fuel requirements, asset management transactions and customer-related business activities;
- locking in a price differential to protect the fair value between transportation receipt and delivery points and to protect the fair value of natural gas or NGLs that are purchased in one month and sold in a later month; and
- reducing our exposure to fluctuations in foreign currency exchange rates.

Our Energy Services segment also enters into derivative contracts for financial trading purposes primarily to capitalize on opportunities created by market volatility, weather-related events, supply-demand imbalances and market liquidity inefficiency, which allows us to capture additional margin. Financial trading activities are executed generally using financially settled derivatives and are normally short term in nature.

With respect to the net open positions that exist within our marketing and financial trading operations, fluctuating commodity prices can impact our financial position and results of operations. The net open positions are actively managed, and the impact of the changing prices on our financial condition at a point in time is not necessarily indicative of the impact of price movements throughout the year.

Our Distribution segment also uses derivative instruments to hedge the cost of anticipated natural gas purchases during the winter heating months to protect our customers from upward volatility in the market price of natural gas. The use of these derivative instruments and the associated recovery of these costs have been approved by the OCC, KCC and regulatory authorities in most of our Texas jurisdictions.

We are also subject to fluctuation in interest rates. We manage interest-rate risk through the use of fixed-rate debt, floating-rate debt and interest-rate swaps. Interest-rate swaps are agreements to exchange an interest payment at some future point based on the differential between two interest rates.

Accounting Treatment

We record derivative instruments at fair value, with the exception of normal purchases and normal sales that are expected to result in physical delivery. The accounting for changes in the fair value of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship and, if so, the reason for holding it.

If certain conditions are met, we may elect to designate a derivative instrument as a hedge of exposure to changes in fair values, cash flows or foreign currency. Certain non-trading derivative transactions, which are economic hedges of our accrual transactions, such as our storage and transportation contracts, do not qualify for hedge accounting treatment.

The table below summarizes the various ways in which we account for our derivative instruments and the impact on our consolidated financial statements:

| | | Recognition and Measurement | | |
|---|---|---|---|---|
| Accounting Treatment | | Balance Sheet | | Income Statement |
| Normal purchases and normal sales | - | Fair value not recorded | - | Change in fair value not recognized in earnings |
| Mark-to-market | - | Recorded at fair value | - | Change in fair value recognized in earnings |
| Cash flow hedge | - | Recorded at fair value | - | Ineffective portion of the gain or loss on the derivative instrument is recognized in earnings |
| | - | Effective portion of the gain or loss on the derivative instrument is reported initially as a component of accumulated other comprehensive income (loss) | - | Effective portion of the gain or loss on the derivative instrument is reclassified out of accumulated other comprehensive income (loss) into earnings when the forecasted transaction affects earnings |
| Fair value hedge | - | Recorded at fair value | - | The gain or loss on the derivative instrument is recognized in earnings |
| | - | Change in fair value of the hedged item is recorded as an adjustment to book value | - | Change in fair value of the hedged item is recognized in earnings |

Gains or losses associated with the fair value of derivative instruments entered into by our Distribution segment are included in, and recoverable through, the monthly purchased-gas cost mechanism.

We formally document all relationships between hedging instruments and hedged items, as well as risk management objectives, strategies for undertaking various hedge transactions and methods for assessing and testing correlation and hedge ineffectiveness. We specifically identify the asset, liability, firm commitment or forecasted transaction that has been designated as the hedged item. We assess the effectiveness of hedging relationships quarterly by performing a regression analysis on our cash flow and fair value hedging relationships to determine whether the hedge relationships are highly effective on a retrospective and prospective basis. We also document our normal purchases and normal sales transactions that we expect to result in physical delivery and which we elect to exempt from derivative accounting treatment.

The presentation of settled derivative instruments on either a gross or net basis in our Consolidated Statements of Income is dependent on the relevant facts and circumstances of our different types of activities rather than based solely on the terms of the individual contracts. All financially settled derivative instruments, as well as derivative instruments considered held for trading purposes that result in physical delivery, are reported on a net basis in revenues in our Consolidated Statements of Income. The realized revenues and purchase costs of derivative instruments that are not considered held for trading purposes and non-derivative contracts are reported on a gross basis. Derivatives that qualify as normal purchases or normal sales that are expected to result in physical delivery are also reported on a gross basis.

Revenues in our Consolidated Statements of Income include financial trading margins, as well as certain physical natural gas transactions with our trading counterparties. Revenues and cost of sales and fuel from such physical transactions are reported on a net basis.

Cash flows from futures, forwards, options and swaps that are accounted for as hedges are included in the same Consolidated Statements of Cash Flows category as the cash flows from the related hedged items.

Fair Values of Derivative Instruments

See Note B for a discussion of the inputs associated with our fair value measurements.

The following table sets forth the fair values of our derivative instruments for the periods indicated:

| | March 31, 2010 | | | December 31, 2009 | | |
|---|---|---|---|---|---|---|
| | Fair Values of Derivatives (a) | | | Fair Values of Derivatives (a) | | |
| | Assets | | (Liabilities) | Assets | | (Liabilities) |
| | (Thousands of dollars) | | | | | |
| Derivatives designated as hedging instruments | | | | | | |
| Energy Services - fair value hedges | $ 156,762 | | $ (45,178 ) | $ 197,037 | | $ (59,731 ) |
| Energy Services - cash flow hedges | 68,437 | (b) | (40,377 ) | 115,215 | (c) | (53,265 ) |
| ONEOK Partners - cash flow hedges | 21,483 | | (10,198 ) | 459 | | (18,772 ) |
| Total derivatives designated as hedging instruments | 246,682 | | (95,753 ) | 312,711 | | (131,768 ) |
| Derivatives not designated as hedging instruments | | | | | | |
| Commodity contracts | | | | | | |
| Non-trading instruments | | | | | | |
| Natural gas | | | | | | |
| Exchange-traded contracts | 2,586 | | (24,183 ) | 24,692 | | (20,657 ) |
| Over-the-counter financial contracts | 368,439 | | (382,695 ) | 382,783 | | (427,057 ) |
| Physical contracts | 63,713 | | (25,868 ) | 46,598 | | (16,234 ) |
| Trading instruments | | | | | | |
| Natural gas | | | | | | |
| Exchange-traded contracts | 26,953 | | (16,447 ) | 15,151 | | (16,153 ) |
| Over-the-counter financial contracts | 72,940 | | (80,141 ) | 44,600 | | (42,181 ) |
| Total commodity contracts | 534,631 | | (529,334 ) | 513,824 | | (522,282 ) |
| Energy Services - foreign exchange contracts | 73 | | - | 28 | | (81 ) |
| Total derivatives not designated as hedging instruments | 534,704 | | (529,334 ) | 513,852 | | (522,363 ) |
| Total derivatives | $ 781,386 | | $ (625,087 ) | $ 826,563 | | $ (654,131 ) |

(a) - Included on a net basis in energy marketing and risk management assets and liabilities on our Consolidated Balance Sheets.
(b) - Includes $11.3 million of derivative assets associated with cash flow hedges of inventory that were adjusted to reflect the lower of cost or market value. The deferred gains associated with these assets have been reclassified from accumulated other comprehensive loss.
(c) - Includes $37.7 million of derivative assets associated with cash flow hedges of inventory that were adjusted to reflect the lower of cost or market value. The deferred gains associated with these assets have been reclassified from accumulated other comprehensive loss.

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Notional Quantities for Derivative Instruments

The following table sets forth the notional quantities for derivative instruments held for the periods indicated:

| | Contract Type | March 31, 2010 Purchased/ Payor | March 31, 2010 Sold/ Receiver | December 31, 2009 Purchased/ Payor | December 31, 2009 Sold/ Receiver |
|---|---|---|---|---|---|
| Derivatives designated as hedging instruments: | | | | | |
| Cash flow hedges | | | | | |
| Fixed price | | | | | |
| - Natural gas (Bcf) | Exchange futures | 2.8 | (9.6) | 6.4 | (20.7) |
| | Swaps | 14.5 | (49.5) | 18.1 | (80.7) |
| - Crude oil and NGLs (MMBbl) | Swaps | - | (2.4) | - | (2.4) |
| Basis | | | | | |
| - Natural gas (Bcf) | Forwards and swaps | 16.3 | (55.3) | 23.7 | (99.6) |
| Fair value hedges | | | | | |
| Basis | | | | | |
| - Natural gas (Bcf) | Forwards and swaps | 166.8 | (166.8) | 210.4 | (210.4) |
| | | | | | |
| Derivatives not designated as hedging instruments: | | | | | |
| Fixed price | | | | | |
| - Natural gas (Bcf) | Exchange futures | 27.3 | (20.9) | 38.8 | (22.7) |
| | Forwards and swaps | 96.0 | (106.9) | 100.6 | (117.4) |
| | Options | 67.5 | (44.2) | 102.6 | (80.6) |
| - Foreign currency (Millions of dollars) | Swaps | $2.6 | $- | $4.6 | $- |
| Basis | | | | | |
| - Natural gas (Bcf) | Forwards and swaps | 868.8 | (869.8) | 940.7 | (947.1) |
| Index | | | | | |
| - Natural gas (Bcf) | Forwards and swaps | 63.7 | (13.6) | 66.4 | (33.1) |

These notional amounts are used to summarize the volume of financial instruments. However, they do not reflect the extent to which the positions offset one another and consequently do not reflect our actual exposure to market or credit risk.

Cash Flow Hedges - Our Energy Services and ONEOK Partners segments use derivative instruments to hedge the cash flows associated with anticipated purchases and sales of natural gas, NGLs and condensate and cost of fuel used in the transportation of natural gas. Accumulated other comprehensive income (loss) at March 31, 2010, includes gains of approximately $13.2 million, net of tax, related to these hedges that will be realized within the next 21 months as the forecasted transactions affect earnings. If prices remain at current levels, we will recognize $11.6 million in net gains over the next 12 months, and we will recognize net gains of $1.6 million thereafter.

For the three months ended March 31, 2010 and 2009, cost of sales and fuel in our Consolidated Statements of Income includes $11.3 million in each period, reflecting an adjustment to inventory at the lower of cost or market value. In each period, we reclassified $11.3 million of deferred gains, before income taxes, on associated cash flow hedges from accumulated other comprehensive income (loss) into earnings.

The following table sets forth the effect of cash flow hedges recognized in other comprehensive income (loss) for the periods indicated:

| Derivatives in Cash Flow Hedging Relationships | Three Months Ended March 31, 2010 | 2009 |
| --- | --- | --- |
| | (Thousands of dollars) | |
| Commodity contracts | $ 62,328 | $ 98,608 |
| Interest rate contracts | - | 121 |
| Total gain recognized in other comprehensive income (loss) on derivatives (effective portion) | $ 62,328 | $ 98,729 |

The following tables set forth the effect of cash flow hedges on our Consolidated Statements of Income for the periods indicated:

| Derivatives in Cash Flow Hedging Relationships | Location of Gain (Loss) Reclassified from Accumulated Other Comprehensive Income (Loss) into Net Income (Effective Portion) | Three Months Ended March 31, 2010 | 2009 |
|---|---|---|---|
| | | (Thousands of dollars) | |
| Commodity contracts | Revenues | $29,956 | $82,715 |
| Commodity contracts | Cost of sales and fuel | (12,097 ) | (1,554 ) |
| Interest rate contracts | Interest expense | 221 | 436 |
| Total gain (loss) reclassified from accumulated other comprehensive income (loss) into net income on derivatives (effective portion) | | $18,080 | $81,597 |

| Derivatives in Cash Flow Hedging Relationships | Location of Gain (Loss) Recognized in Income on Derivatives (Ineffective Portion and Amount Excluded from Effectiveness Testing) | Three Months Ended March 31, 2010 | 2009 |
|---|---|---|---|
| | | (Thousands of dollars) | |
| Commodity contracts | Revenues | $1,016 | $3,048 |
| Commodity contracts | Cost of sales and fuel | (877 ) | (530 ) |
| Total gain (loss) recognized in income on derivatives (ineffective portion and amount excluded from effectiveness testing) | | $139 | $2,518 |

In the event that it becomes probable that a forecasted transaction will not occur, we will discontinue cash flow hedge treatment, which will affect earnings. For the three months ended March 31, 2010 and 2009, there were no gains or losses due to the discontinuance of cash flow hedge treatment since the underlying transactions were no longer probable.

Other Derivative Instruments - The following table sets forth the effect of our derivative instruments that are not part of a hedging relationship on our Consolidated Statements of Income for the periods indicated:

| Derivatives Not Designated as Hedging Instruments | Location of Gain | Three Months Ended March 31, 2010 | 2009 |
|---|---|---|---|
| | | (Thousands of dollars) | |
| Commodity contracts - trading | Revenues | $ 2,028 | $ 3,305 |
| Commodity contracts - non-trading (a) | Cost of gas and fuel | (41 ) | (539 ) |
| Foreign exchange contracts | Revenues | 59 | (262 ) |
| Total gain recognized in income on derivatives | | $ 2,046 | $ 2,504 |

(a) - For the three months ended March 31, 2010 and 2009, we recognized $3.9 million and $2.1 million, respectively, of losses associated with the fair value of derivative instruments entered into by our Distribution segment that were deferred as they are included in, and recoverable through, the monthly purchased-gas cost mechanism.

Fair Value Hedges - In prior years, we terminated various interest-rate swap agreements. The net savings from the termination of these swaps is being recognized in interest expense over the terms of the debt instruments originally hedged. Interest expense savings from the amortization of terminated swaps for the three months ended March 31, 2010 and 2009, were $2.5 million and $2.6 million, respectively. The remaining amortization of terminated swaps will be recognized over the following periods:

| | ONEOK | ONEOK Partners | Total |
|---|---|---|---|
| | (Millions of dollars) | | |
| Remainder of 2010 | $ 4.8 | $ 2.8 | $ 7.6 |
| 2011 | $ 3.4 | $ 0.9 | $ 4.3 |
| 2012 | $ 1.7 | $ - | $ 1.7 |
| 2013 | $ 1.7 | $ - | $ 1.7 |
| 2014 | $ 1.7 | $ - | $ 1.7 |
| Thereafter | $ 23.6 | $ - | $ 23.6 |

ONEOK and ONEOK Partners had no interest-rate swap agreements at March 31, 2010.

Our Energy Services segment uses basis swaps to hedge the fair value of location price differentials related to certain firm transportation commitments. Net gains or losses from the fair value hedges and ineffectiveness are recorded to cost of sales and fuel. The ineffectiveness related to these hedges included gains of $1.3 million and losses of $0.8 million for the three months ended March 31, 2010 and 2009, respectively.

For the three months ended March 31, 2010, cost of sales and fuel in our Consolidated Statements of Income includes gains of $10.8 million related to the change in fair value of derivatives declared as fair value hedges. Revenues include losses of $9.6 million for the three months ended March 31, 2010, to recognize the change in fair value of the hedged firm commitments.

Credit Risk - We monitor the creditworthiness of our counterparties and compliance with management’s risk tolerance as determined by our Risk Oversight and Strategy Committee. We maintain credit policies with regard to our counterparties that we believe minimize overall credit risk. These policies include an evaluation of potential counterparties’ financial condition (including credit ratings, bond yields and credit default swap rates), collateral requirements under certain circumstances and the use of standardized master-netting agreements that allow us to net the positive and negative exposures associated with a single counterparty. We have counterparties whose credit is not rated, and for those customers we use internally developed credit ratings.

Some of our derivative instruments contain provisions that require us to maintain an investment grade credit rating from S&P and/or Moody’s. If our credit ratings on senior unsecured long-term debt were to decline below investment grade, we would be in violation of these provisions, and the counterparties to the derivative instruments could request collateralization on derivative instruments in net liability positions. The aggregate fair value of all financial derivative instruments with contingent features related to credit risk that were in a net liability position as of March 31, 2010, was $14.0 million for which we have posted collateral of $4.6 million in the normal course of business. If the contingent features underlying these agreements were triggered on March 31, 2010, we would have been required to post an additional $9.4 million of collateral to our counterparties.

The counterparties to our derivative contracts consist primarily of major energy companies, LDCs, electric utilities, financial institutions and commercial and industrial end-users. This concentration of counterparties may impact our overall exposure to credit risk, either positively or negatively, in that the counterparties may be similarly affected by changes in economic, regulatory or other conditions. Based on our policies, exposures, credit and other reserves, we do not anticipate a material adverse effect on our financial position or results of operations as a result of counterparty nonperformance.

The following table sets forth the net credit exposure from our derivative assets for the period indicated:

| | March 31, 2010 | | | | December 31, 2009 | | | |
|---|---|---|---|---|---|---|---|---|
| | Investment Grade | Non-investment Grade | Not Rated | Total | Investment Grade | Non-investment Grade | Not Rated | Total |
| Counterparty sector | (Thousands of dollars) | | | | | | | |
| Gas and electric utilities | $ 49,961 | $ 2,803 | $ 3,142 | $ 55,906 | $ 26,964 | $ 2,668 | $ 7,972 | $ 37,604 |
| Oil and gas | 62,115 | - | 1,825 | 63,940 | 54,578 | 224 | | |