

MINUTES OF THE SENATE UTILITIES COMMITTEE.

The meeting was called to order by Chairperson Senator Stan Clark at 9:30 a.m. on February 21, 2002 in Room 231-N of the Capitol.

All members were present except:

Committee staff present: Raney Gilliland, Legislative Research
Emalene Correll, Legislative Research
Bruce Kinzie, Revisor of Statutes
Ann McMorris, Secretary

Conferees appearing before the committee:
Steve Johnson, Kansas Gas Service

Others attending: See attached list.

The chairman opened the hearing on:

S.B. 546 - Natural gas supplier, termination of franchises

Proponent:

Steve Johnson, Kansas Gas Service, spoke in support of the bill and noted this would give natural gas utility companies the same protection and authority provided to private retail electric suppliers and cities in K.S.A. 66-1,176(b) and (c). (Attachment 1)

Colin Hansen, Kansas Municipal Utilities, provided written testimony in support of **SB 546**. (Attachment 2)

The chair closed the hearing on **SB 546**.

The chairman opened for possible action on

SCR 1618 - Resolution urging Congress to open the Arctic National Wildlife Refuge (ANWR) to oil and gas exploration and production

Moved by Senator Tyson, seconded by Senator Emler, SCR 1618 be passed favorably. Motion carried.

Approval of minutes:

Moved by Senator Lee, seconded by Senator Emler, the minutes for Senate Utilities meetings held on February 6, 2002, February 11, 2002, February 12, 2002, February 13, 2002 and February 14, 2002 be approved. Motion carried.

The next meeting of the Senate Utilities Committee will be on February 22, 2002.

Adjournment.

Respectfully submitted,

Ann McMorris, Secretary

Attachments - 2



KANSAS GAS SERVICE

A DIVISION OF ONEOK

TESTIMONY

**TO: The Honorable Stan Clark, Chairman
And Members Of The
Senate Committee on Utilities**

**FROM: Steve Johnson
Executive Director for Corporate Relations
Kansas Gas Service**

**RE: SB 546 An Act Concerning Retail Natural Gas Suppliers;
Relating To Franchise Agreements**

DATE: February 21, 2002

Good Morning Mr. Chairman and Members of the Senate Committee on Utilities.

I am Steve Johnson, the Executive Director of Corporate Relations for Kansas Gas Service, a Kansas-based natural gas local distribution company headquartered in Overland Park. Kansas Gas Service (KGS) provides local natural gas service to over 640,000 customers in nearly 400 Kansas communities. KGS is a division of ONEOK, Inc., a Tulsa-based diversified energy company. With me today is Galen Biery, Assistant General Counsel for Kansas Gas Service and Whitney Damron, our Kansas lobbyist.

Mr. Biery deals with local franchise issues on a daily basis along with several KGS Community Relations Managers across the State and can discuss changes in current law vs. our proposed changes contained in SB 546 as well as answer questions on the bill following my testimony if you desire.

On behalf of Kansas Gas Service, I wish to thank you for holding hearings on SB 546 that would amend the statutes regarding compensation to a natural gas utility in the event their franchise agreement was either terminated during a period when a valid franchise is in effect or upon failure of a municipality to renew a franchise agreement at the end of a valid franchise agreement. SB 546 was modeled after current protections and authority provided to private retail electric suppliers and cities in K.S.A. 66-1,176 (b) and (c). Those statutes appear to have been enacted in 1987 and copies are included with my testimony so that you can see how this bill tracks with that section of law.

At the outset of my comments, I would say it is highly unlikely that we would ever seek to use the provisions of SB 546, as in most all cases, a franchise agreement is ultimately executed between a municipality and the local natural gas distribution company. However, there have been exceptions to this rule and there have been instances where a municipality has put a local distribution company on notice of intent not to renew a franchise agreement, and then changed their position prior to the expiration of the agreement.

KGS respectfully suggests it is appropriate for the Legislature to bring natural gas utilities to the same level as electric utilities in instances of acquisition by a city.

Current law provides a means for a city to acquire the control of a utility through a resolution at the end of a valid franchise agreement. In such instances, the city, the utility and the judge with jurisdiction over the case each select a commissioner to “appraise and ascertain the fair cash value of said plant and the appurtenances thereto...” (K.S.A. 21-811). The parties may employ experts in the field for valuation purposes and cross-examination of experts is provided for under this procedure. However, the process is highly subjective and, in the opinion of KGS, provides little guidance to the parties as to what is appropriate to be valued, particularly in regards to current and future contracts with customers, future revenues, transition costs, tax consequences, depreciation schedules and other such considerations. These issues will necessarily impact those customers who remain on the natural gas utilities system and should be considered when determining compensation rates to the natural gas utility. These items are specifically delineated in the event of a termination of service rights for a retail electric supplier as noted earlier in my comments.

Cities may also acquire natural gas service assets through eminent domain and condemnation procedures during the time a valid franchise agreement is in place. In addition, most franchise agreements would provide a city with the ability to terminate a franchise agreement in case of failure to perform under the agreement by the franchisee.

We believe natural gas and electric distribution companies are similarly situated to such an extent they should be similarly treated in rare instances of the failure to renew or the termination of a valid franchise agreement by a city. Significant investments are made by natural gas utilities in order to provide safe and reliable service to the citizens of Kansas and this investment made on behalf of the utility’s customers should be fairly and accurately compensated for in the event a city seeks to acquire the infrastructure and facilities of its current natural gas supplier.

We do not stand before you seeking changes to these statutes for the benefit of only Kansas Gas Service, but for our customers as well. In the event a city does terminate an agreement or fails to renew a franchise agreement, the amount of consideration in question will not simply be the value of hard assets transferred to the city, but may include a broad spectrum of additional costs that will then be born by ratepayers that are still on a gas company's system, but perhaps not by those that remain with the city that takes over a gas property. Accordingly, we propose this change in order to protect all customers of natural gas utilities and not just those who are removed from the system by a city through the their failure to renew a franchise agreement or termination of an existing agreement.

Finally, to our knowledge, no one has argued the acquisition costs and considerations for a city to acquire the operations of a local electric service provider are unfair, as this issue has been in the news in recent years. Accordingly, we believe comparable considerations should be provided to natural gas utilities and their customers.

On behalf of Kansas Gas Service, I thank you for your consideration of this legislation. I would be pleased to stand for questions at the appropriate time.

SENATE BILL No. 546

By Committee on Utilities

2-8

9 AN ACT concerning retail natural gas suppliers; relating to franchise
10 agreements; compensation.

11

12 *Be it enacted by the Legislature of the State of Kansas:*

13 Section 1. (a) When the service rights of a retail natural gas supplier
14 are terminated by a city during the period in which a valid franchise is in
15 effect and the service rights are assumed by the terminating city, or an
16 entity acting on behalf of or as an agent for the city, the governing body
17 of the city shall acquire from the terminated supplier the parts of the
18 local natural gas distribution system necessary to serve all customers
19 within the previously franchised area and the terminated supplier shall
20 sell the system to the governing body of such city for which it shall be
21 fairly compensated. Such compensation shall be an amount mutually
22 agreed upon by the affected parties or an amount determined by the
23 following formula:

24 (1) The depreciated replacement cost for the gas utility facilities in
25 the territory in which the service rights have been terminated. As used
26 in this paragraph, "depreciated replacement cost" means the original in-
27 stalled cost of the facilities, adjusted to present value by utilizing a na-
28 tionally recognized index of utility construction costs, less accumulated
29 depreciation based on the book depreciation rates of the selling utility,
30 as filed with and approved by the state corporation commission, which
31 are in effect at the time of acquisition;

32 (2) the depreciated replacement costs of the remaining proportion of
33 any take or pay contracts or participation agreements;

34 (3) the depreciated replacement cost for the gas utility facilities out-
35 side the affected territory used in providing service to the formerly fran-
36 chised area. Such facilities shall include all compression, regulating or
37 transmission facilities throughout the terminated utility's integrated sys-
38 tem, the value of which shall be determined by the depreciated replace-
39 ment cost formula in paragraph (1) multiplied by the percentage of the
40 terminated utility's total retail sales to customers in the affected area
41 during the 12 months next preceding the effective date of the sale;

42 (4) all reasonable and prudent costs of detaching the gas system fa-
43 cilities to be sold, including the reasonable costs of studies and inventories

1-4

1 made to determine the facility's value and all reasonable and prudent
2 costs of reintegrating the remaining gas system facilities of the retail gas
3 supplier whose service rights are terminated;

4 (5) an amount equal to the net revenues received during the 12
5 months next preceding the date of termination of the service rights from
6 the customers within the affected area of the retail gas supplier whose
7 service rights are terminated. As used in this paragraph, "net revenues"
8 means the total revenues received by the terminated utility for gas service
9 within the affected area less franchise and sales taxes collected; the cost
10 of gas recovered in the revenues; and labor, maintenance, administration
11 and insurance. This number shall be multiplied by the number of years
12 remaining in any franchise contract; and

13 (6) an amount equal to the state and federal tax liability created by
14 the taxable income pursuant to the provisions of this paragraph and par-
15 agraphs (1), (2), (3), (4) and (5) by the retail gas supplier whose service
16 rights are terminated, calculated, without regard to any tax deductions or
17 benefits not related to the sale of assets covered herein.

18 (b) If the parties are unable to agree upon the amount of compen-
19 sation to be paid pursuant to this act after 60 days following the date of
20 termination of service rights, either party may apply to the district court
21 having jurisdiction where any portion of the facilities are located for de-
22 termination of compensation. Such determination shall be made by the
23 court sitting without a jury.

24 Sec. 2. In addition to the fair cash value of any plant and appurte-
25 nance thereto determined pursuant to K.S.A. 12-811, and amendments
26 thereto, a retail natural gas supplier whose service rights have expired by
27 reason of failure of the renewal of a valid franchise shall be entitled to
28 compensation for all reasonable and prudent costs of detaching the gas
29 system facilities to be sold and all reasonable and prudent costs of rein-
30 tegrating the remaining gas system facilities of such retail gas supplies
31 less the value of all gas system facilities replaced by the new facilities
32 required for the reintegration of the remaining gas system facilities, plus
33 an amount equal to the gross revenues received from the customers
34 within the affected area during the 12 months next preceding the date of
35 expiration of the most recent valid franchise, less taxes.

36 Sec. 3. This act shall take effect and be in force from and after its
37 publication in the statute book.

66-1,176b. Termination of service rights during period when a valid franchise is in effect; facilities to be acquired; compensation; formula. (a) When the service rights of a retail electric supplier are terminated by a city during the period in which a valid franchise is in effect and the service rights are assumed by the terminating city, the governing body of the city shall acquire from the terminated supplier

the parts of the local electric distribution system necessary to serve all customers within the previously franchised area and the terminated supplier shall sell the system to the governing body of such city for which it shall be fairly compensated. Such compensation shall be an amount mutually agreed upon by the affected parties or an amount determined by the following formula:

(1) The depreciated replacement cost for the electric utility facilities in the territory in which the service rights have been terminated. As used in this paragraph, "depreciated replacement cost" means the original installed cost of the facilities, adjusted to present value by utilizing a nationally recognized index of utility construction costs, less accumulated depreciation based on the book depreciation rates of the selling utility, as filed with and approved by the state corporation commission, which are in effect at the time of acquisition;

(2) the depreciated replacement costs of the remaining proportion of any take or pay power contracts or participation power agreements;

(3) the depreciated replacement cost for the electric utility facilities outside the affected territory used in providing service to the formerly franchised area. Such facilities shall include all generation facilities and all transmission facilities throughout the terminated utility's integrated system, the value of which shall be determined by the depreciated replacement cost formula in paragraph (1) multiplied by the percentage of the terminated utility's total retail kilowatt-hour sales to customers in the affected area during the 12 months next preceding the effective date of the sale;

(4) all reasonable and prudent costs of detaching the electric system facilities to be sold, including the reasonable costs of studies and inventories made to determine the facility's value and all reasonable and prudent costs of reintegrating the remaining electric system facilities of the retail electric supplier whose service rights are terminated;

(5) an amount equal to the net revenues received during the 12 months next preceding the date of termination of the service rights from the customers within the affected area of the retail electric supplier whose service rights are terminated. As used in this paragraph, "net revenues" means the total revenues received by the terminated utility for electric service within the affected area less franchise and sales taxes collected; the cost of fuel or purchased power recovered in the revenues; and labor,

maintenance, administration and insurance. This number shall be multiplied by the number of years remaining in any franchise contract; and

(6) an amount equal to the state and federal tax liability created by the taxable income pursuant to the provisions of this paragraph and paragraphs (1), (2), (3), (4) and (5) by the retail electric supplier whose service rights are terminated, calculated without regard to any tax deductions or benefits not related to the sale of assets covered herein.

(b) If the parties are unable to agree upon the amount of compensation to be paid pursuant to this act after 60 days following the date of termination of service rights, either party may apply to the district court having jurisdiction where any portion of the facilities is located for determination of compensation. Such determination shall be made by the court sitting without a jury.

History: L. 1987, ch. 255, § 1; April 23.

66-1,176c. Compensation of private retail electric supplier for certain electric system facilities acquired by city. In addition to the fair cash value of any plant and appurtenance thereto determined pursuant to K.S.A. 12-811, a retail electric supplier whose service rights have expired by reason of failure of the renewal of a valid franchise shall be entitled to compensation for all reasonable and prudent costs of detaching the electric system facilities to be sold and all reasonable and prudent costs of reintegrating the remaining electric system facilities of such retail electric supplier less the value of all electric system facilities replaced by new facilities required for the reintegration of the remaining electric system facilities.

History: L. 1987, ch. 255, § 2; April 23.

66-1,176c

PUBLIC UTILITIES

RETAIL ELECTRIC SUPPLIERS

66-1,176b



kansas municipal utilities

Submitted Testimony Provided the

Senate Utilities Committee

February 21, 2002

*Colin Hansen
Executive Director
Kansas Municipal Utilities*

Senate Bill 546 – Natural Gas Annexation Compensation

Thank you for the opportunity to provide this written testimony regarding SB 546. Municipal Utilities (KMU) is the statewide association representing 154 municipal electric, natural gas and water utilities. Formed in 1928, KMU members currently provide utility services to over one million Kansans. I serve as the Executive Director of the association with offices located in McPherson.

In Kansas, 67 cities provide natural gas distribution services to their citizens. The vast majority of these municipal gas systems operate in small rural towns. With the exception of Winfield, Chanute and Iola, all of the municipal gas systems operate in communities less than 5,000 in population. The majority serve towns of less than 1,000 in population and are typically surrounded by rural land in which no gas utility provides service.

Since last summer, KMU has worked with stakeholders in the electric industry to address several reasonable and valid annexation concerns voiced by the rural electric cooperatives. The result was SB 480 which, while requiring a significant sacrifice on the part of municipal electric utilities, continues to be supported by KMU as just and fair compromise legislation.

KMU remains uncertain whether the same annexation concerns are reasonable and valid for natural gas service territory. Investor-owned utilities have not yet demonstrated to our membership the necessity for such legislation. In fact, municipal gas members have reported that they believe the negotiations for disputed gas customers with private gas utilities have been fair and equitable on both sides.

Cities with municipal gas systems rarely take over customers in the service territory of another gas utility. However, in the rare instances in which this has happened the city and utility have commonly negotiated to secure transfer of the gas customers.

For example, the city of Iola worked with Kansas Gas Service in 1999 to “purchase” 126 KGS gas customers that were located within the city limits. The city of Winfield, conversely, attempted to negotiate the transfer of eight Peoples Natural Gas customers

(again located within the city boundaries) to the municipal gas system in 1993. At the \$1,100 per meter cost the company demanded, the city was forced to abandon the prospect of serving those citizens. In both situations, the private utility had ample ability to recoup reasonable value for their investment in these customers.

I again thank the committee for the opportunity to provide written testimony. Should you have any questions, comments or concerns about the testimony, please feel free to contact me at the postal address, phone number or email address below.

Colin Hansen
Executive Director
Kansas Municipal Utilities
421 North Main, Ste. 3
McPherson, Kansas 67460
pb 620/241-1423
fx 620/241-7829
email chansen@kmunet.org
web www.kmunet.org