

## MINUTES OF THE SENATE UTILITIES COMMITTEE

The meeting was called to order by Chairman Jay Emler at 9:30 A.M. on February 2, 2006 in Room 526-S of the Capitol.

Committee members absent:

Committee staff present: Athena Andaya, Kansas Legislative Research Department  
Raney Gilliland, Kansas Legislative Research Department  
Bruce Kinzie, Revisor of Statutes' Office  
Diana Lee, Revisor of Statutes' Office  
Ann McMorris, Committee Secretary  
Leann Hirschfeld, Intern

Conferees appearing before the committee:

Brad Dixon, president, Kansas Gas Service  
Richard C. Loomis, Aquila, Inc.  
Larry Berg, Midwest Energy, Inc.  
Ron Gaches, Atmos Energy  
David Springe, CURB  
Don Low, KCC

Others in attendance: See attached list.

Chairman Emler opened the hearing on

**SB 414 - Enacting the gas safety and reliability policy act.**

Proponents

Brad Dixon, President, Kansas Gas Service, spoke in favor of **SB 414** because it furthers the ability of natural gas utilities operating in Kansas to provide safe and reliable gas service. The provisions in this bill will enable natural gas public utilities to comply more effectively and efficiently with state and federal requirements. This bill provides a more streamlined approach to provide for non-revenue generating investments. (Attachment 1)

Richard C. Loomis, Aquila, Inc. favored this bill because it allows recovery of utility investment in non-revenue generating projects through a gas system replacement surcharge. (Attachment 2)

Larry Berg, Vice President of Corporate Relations, Midwest Energy, Inc., agreed with the reasons presented by Kansas Gas Service and Aquila and also noted the ability to pass through the cost of prudent safety and reliability investments in a timely manner is crucial to their on-going financial health and the customer base that remains. (Attachment 3)

Ron Gaches, Atmos Energy, urged passage of **SB 414** as this will encourage natural gas companies to increase the investment levels necessary to maximize the safety and reliability of their systems. (Attachment 4)

Questions from the committee regarding a cap and asking each company what their cost would be in a rate case. The responses on rate case cost ranged from \$250,000 to \$1.2 million, depending on the size of the company, not including KCC or CURB assessments.

Opponents

David Springe, consumer counsel, Citizens' Utility Ratepayer Board (CURB), spoke against **SB 414** saying that the bill is over-broad, ill-defined and one-sided in favor of the utilities and offers no protection for consumers. Without withdrawing or waiving CURB's outright opposition, CURB provided the Committee some suggested mark-up's to the bill to remove what CURB considers the most egregious language in the bill. (Attachment 5)

CONTINUATION SHEET

MINUTES OF THE Senate Utilities Committee at 9:30 A.M. on February 2, 2006 in Room 526-S of the Capitol.

Don Low, Director of the Utilities Division for the Kansas Corporation Commission, spoke in opposition of **SB 414** because it does not allow for a determination of the reasonableness of and need for a surcharge based on the individual circumstances of each natural gas utility. The KCC concern is that, without vesting discretion in the Commission to weigh the equities, circumstances could arise whereby the surcharge could result in customers paying unreasonable rates. (Attachment 6)

Due to the lack of time, the committee members were unable to complete their questioning and the Chairman scheduled the continuation of the hearing to February 9, 2006 at 9:30 a.m. in Room 235-S.

Approval of Minutes

Moved by Senator Reitz, seconded by Senator Lee, the minutes of the meetings of the Senate Utilities Committee held on January 31, 2006 and February 1, 2006 be approved. Motion carried.

Adjournment.

Respectfully submitted,

Ann McMorris, Secretary

Attachments - 6

# SENATE UTILITIES COMMITTEE GUEST LIST

DATE: FEBRUARY 2, 2006

Name	Representing
- Steve Johnson	Kansas Gas Service
Brad Dixon	Kansas Gas Service
LARRY BERG	MIDWEST ENERGY
Kimberly Deen	Agenda
Chuck Thomas	Agenda
Don Naches	Atmos Energy
Jim BARTLING	ATMOS
Tom Stephens	ATMOS
Whitney Samra	KS Gas Service
David Sprunx	Curb
David Rowe	Intern Sen Finncisco
Leann Hirschfeld	Intern Sen. Emler



## KANSAS GAS SERVICE

A DIVISION OF ONEOK

Before the Senate Utilities Committee

SB 414

Testimony of Brad Dixon, President

Kansas Gas Service

7421 W. 129<sup>th</sup> Street, Overland Park, Kansas

913-319-8600

February 2, 2006

Chairman Emler and Members of the Committee,

I appreciate the opportunity to testify in support of Senate Bill 414, which is known as the Gas Safety and Reliability Act. Kansas Gas Service, which provides natural gas service to over 650,000 customers in the State of Kansas, supports this bill because it furthers the ability of Kansas Gas Service and other natural gas utilities operating in the state to achieve the named purpose of the bill: that is to provide safe and reliable gas service.

Pursuant to this bill, natural gas public utilities operating in the state of Kansas will be able to more effectively and efficiently comply with state and federal requirements for natural gas safety. The legislation will also enable natural gas public utilities to comply with the requests of federal, state and local jurisdictions that request the utilities to relocate their facilities which may be located in streets and highways to facilitate street and highway improvement projects which occur throughout the state.

Kansas Gas Service and the other natural gas utilities operating in the state spend significant sums on an annual basis to provide safe reliable service. We also spend significant sums to relocate our facilities in streets and highways to facilitate highway and street improvement projects. For the years, 2003, 2004 and 2005, Kansas Gas Service spent approximately \$24 million per year on these groups of expenditures. This would equate to an annual charge of less than \$5.00.

These expenditures are not revenue enhancing to Kansas Gas Service and the natural gas utilities. The expenditures do not relate to providing service to new load. The expenditures are made to fulfill mandates required by governmental units. We do not contest the need for these mandates. They are appropriate. These mandates enhance safety, and promote the public well being through enhanced infrastructure in our local communities. These expenditures however, as I said, do not generate additional revenue for the natural gas utilities operating in the state.

Under Senate Bill 414, natural gas public utilities will be able to make timely recovery of these expenditures. The bill will enable natural gas utilities to make filings before the Kansas Corporation Commission showing how much money has been expended and the amount to be recovered. This bill has been modeled upon legislation passed in the state of Missouri in 2003.

Senate Utilities Committee  
February 2, 2006  
Attachment 1-1

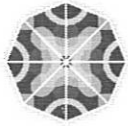
In addition to enhancing safety through more timely recovery of non-revenue enhancing safety expenditures, the legislation will assist in reducing regulatory expense and large rate increases. By allowing more timely recovery for safety related and infrastructure enhancement programs through the mechanism set forth in Senate Bill 414, there will be less frequent need for expensive contested rate case filings, the costs of which are passed on to customers. When such filings are made, the rate increases requested will also be less than they would otherwise be thereby reducing rate shock to customers at the time of their regular filings.

There are provisions to protect consumers against inappropriate expenditures. Utilities are limited in the number of filings they can make under this legislation. The filings will be subject to a review by the Kansas Corporation Commission. The legislation requires the utility to make a major rate case filing every five years. To the extent that the Commission determines in the major filing that any expenditures were inappropriate, they will be subject to disallowance and refund. The utilities are limited by the amount of revenues that they could request under this filing procedure to no more than 10% of their base revenues as determined in their last rate case. To the extent that there is any over collection of the surcharge, such over collection will be credited back to consumers on an annual basis.

You may question why do we need this legislation when you could simply file for a rate increase. It is our opinion that the traditional regulatory model does not efficiently fit the current financial environment for natural gas utilities in meeting their obligations to provide safe and reliable natural gas service. Kansas Gas Service and the other utilities operating in Kansas are continuously replacing aging infrastructure and relocating infrastructure to meet safety needs and infrastructure enhancements. These investments do not enhance revenues. The assets that they are replacing were initially installed at a significantly reduced cost compared to today and they were installed to meet a growing customer base. Today, we might replace a main line extension on a major thoroughfare that was initially installed more than 50 years ago. That line may have been installed at a cost of approximately \$1.00 per foot and today is replaced at a cost of approximately \$28.00 per foot. When the line was installed, it was there to meet the growing needs of a thriving community. Today, there is no additional load associated with that line, simply the same amount of consumption as was there before. We are past the days in the natural gas industry when an increasing customer load will offset the cost of infrastructure placements obviating the need for rate cases. We are past the time when a natural gas utility can make investments and make up for these investments through load growth or cost cutting. We are faced with a situation where we are in a constant need for additional capital to make necessary capital replacements.

To file for an annual increase to meet these increasing costs over which we have no control is inefficient and costly. Annual rate cases are time consuming and costly. This bill provides a more streamlined approach to provide for non-revenue generating investments. Customers will be protected under this bill against charges for imprudent investments. The customer will avoid the significant regulatory cost of annual rate filings which would be necessary to timely recover our investments to provide service to our customer.

Thank you for the opportunity to address you today and I will be available for questions.



**Aquila**

**Testimony in Support of Senate Bill 414**

**Remarks of Richard C. Loomis**

**Aquila, Inc.**

**Vice President, Kansas and Colorado Gas**

**Good morning Mr. Chairman and Members of the Senate Utilities Committee.**

**Thank you for the opportunity to present testimony this morning. My name is Chuck Loomis, Vice President of Kansas and Colorado Gas Operations for Aquila, Inc. I am based in Lawrence, Kansas which serves as the headquarters for Aquila's Kansas Gas Operations.**

**Aquila's natural gas operations in Kansas serve approximately 105,000 customers in over 40 communities across the state, including Lawrence, parts of Wichita, Dodge City, Garden City, Liberal and Goodland.**

**Aquila stands in support of Senate Bill 414. It is fair to say that replacing and improving infrastructure is a challenge for many. State highways, city streets, sewer systems, water systems all serve as examples of infrastructure that must be replaced and improved over time. Typically, gas utility franchises allow gas lines to be installed in public right of way. When a city or the state undertakes an infrastructure improvement project, the gas utility may be required to move its gas lines in the public right of way. Senate Bill 414 allows gas utilities to recover the cost of these relocation projects in a more timely manner. Aquila's investment in**

Senate Utilities Committee  
February 2, 2006  
Attachment 2-1

relocation of gas mains has averaged approximately \$400,000 annually in the past three years.

Aging gas utility infrastructure is a challenge for gas utilities as well. Original installation of natural gas mains and service lines occurred many years ago, and due to age, corrosion, and other factors have led to deterioration over time. To ensure a safe, reliable gas distribution system, Aquila invests \$2 - \$3 million annually for gas main, service line and other facility replacements. Senate Bill 414 helps to address a challenge faced by gas utilities relating to recovering the cost of investing in safety related pipeline replacement projects in a more timely manner than occurs in the historical regulatory process.

As a utility invests capital in pipeline relocation and replacement projects, there is a lag in cost recovery from the time the investment is made until such investment is included in the utility's rate base, typically through a rate case filing. This lag is often referred to as regulatory lag. Generally, these types of investments are not controversial issues, but are a regular part of maintaining integrity throughout the gas systems. This bill allows recovery of utility investment in these non-revenue generating projects through a gas system replacement surcharge, while maintaining the necessary and appropriate checks and balances in the regulatory system to ensure utility investments are prudent.

Aquila also recognizes another potential benefit from passage of this bill. During 2005, nearly 100 rural customers in Southwest Kansas were disconnected from natural gas service due to potentially unsafe levels of hydrogen sulfide in the gas supply. Most of the customers were converted to propane. Under this bill, Aquila

may be able to extend service to customers to allow continued provision of safe, reliable natural gas service.

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Aquila believes that implementation of a Gas System Replacement Surcharge as envisioned in this bill will result in a more efficient and effective regulatory process. We remain committed to discussing and resolving concerns that the Kansas Corporation Commission or other parties may have. I appreciate the opportunity to present remarks to you this morning and am happy to stand for questions at the appropriate time. Thank you.



Before the Senate Utilities Committee  
SB 414  
Testimony of Larry Berg, Vice President of Corporate Relations  
Midwest Energy, Inc.  
1330 Canterbury Road, Hays, Kansas  
785-623-8148 (cell)  
February 2, 2006

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Chairman Emler and Members of the Committee,

I appreciate the opportunity to testify in support of Senate Bill 414, the Gas Safety and Reliability Act. Midwest Energy is a customer-owned utility that provides natural gas service to nearly 42,000 customers in small towns and rural areas of Western Kansas. This legislation would help us to continue the provision of safe and reliable natural gas service.

For the sake of brevity, I will not repeat the supporting reasons already presented by representatives from Kansas Gas Service and Aquila. We are in agreement.

In addition to those comments, Midwest Energy faces unique challenges. The demographic trends in Western Kansas are no secret. Midwest Energy does not enjoy the load growth present in more populated areas. Most of our towns are losing population. Therefore, in addition to the usual inflationary pressures, we have fewer customers using natural gas. In the last three years, we have lost three percent of our customer base.

Compounding that problem is the low customer density of our service area. Midwest Energy only serves about 14 customers per mile of gas pipe. Compare that to the number of homes or business that might be served by a single block of pipe in an urban setting.

The ability to pass through the cost of prudent safety and reliability investments in a timely manner is crucial to our on-going financial health and the customer base that remains. Although rate cases are necessary from time to time, we believe any measure that helps delay the costs of preparing, filing and litigating rate cases is good for our customers.

Midwest Energy is open to proposals that would address concerns of the Kansas Corporation Commission. I appreciate this opportunity and will take questions at the appropriate time. Thank you.

Senate Utilities Committee  
February 2, 2006  
Attachment 3-1

**Senate Utilities Committee**  
**Regarding SB 414 – The Gas Safety and Reliability Act**  
**Testimony of Atmos Energy**  
**Presented by Ron Gaches**  
**February 2, 2006**

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Thank you Chairman Emler for this opportunity to comment in support of Senate Bill 414, the Gas Safety and Reliability Act. I am Ron Gaches appearing on behalf of Atmos Energy.

Passage of SB 414 will encourage natural gas companies to increase the investment levels necessary to maximize the safety and reliability of their systems. In some cases these investments are mandated by federal or state agencies and in other instances there is some level of discretion associated with the scheduling and timing of those investments.

Under current Kansas law and regulatory practice, investments made to replace gas system infrastructure may not be recovered until the investment is in the ground, the investment is deemed “used and required to be used” prudent in a regulatory rate case before the Kansas Corporation Commission. The current system produces a significant regulatory lag time between when the dollars are spent for infrastructure replacement and when the company begins to recover these expenditures in the rates.

Because the current system allows recovery of such expenses only following approval in a rate case, there is often a multi-year delay in beginning the recovery of such expenditures. Rate cases are slow and expensive. The only alternative available under our current regulatory system is to file a rate case each year, an unnecessarily expensive proposition for the utility and ultimately our ratepayers.

SB 414 will allow a gas utility to apply a surcharge to customers’ bills and start to recover costs expended to replace infrastructure in a timely manner. This will reduce the costs associated with filing rate cases and reduce the regulatory lag associated with recovery of such funds, thereby making available additional funds for investment in the integrity of our system.

- The industry proposal contains several safeguards:

- Capital dollars must be expended and the new pipe in the ground before any investment can be recovered.
- The surcharge is capped at 10 percent of their base revenues.
- The KCC would review all expenditures before they are allowed to be recovered in customer rates, and the Commission is not bound until costs are reviewed as part of a reconciliation or general rate proceeding.
- Surcharges are subject to refund after annual reconciliations conducted by the KCC.
- Eligible capital projects must be non-revenue producing and the costs must not be already be part of the utility's base rates.
- A utility can apply for a GSRS adjustment no more than twice per 12-month period.
- Full rate cases will be required at least every five years with the KCC and any overcharges would be subject to refund and true-up.

The environment in which utilities make investment decisions has changed over time, while the manner in which costs for infrastructure investments has not changed for many years. This proposal has been adopted in several states with great success. It will produce significant benefits in terms of assurance of safety and reliability of our systems and we encourage your support.

Atmos Energy is a regional natural gas company serving approximately 3.2 million customers in 12 states. Our Kansas service territory provides natural gas service to approximately 125,000 customers through 111 communities in 33 counties of Kansas. Our Kansas regional office is located in Olathe and our national headquarters is in Dallas, Texas.

# Citizens' Utility Ratepayer Board

## Board Members:

Gene Merry, Chair  
A.W. Dirks, Vice-Chair  
Carol I. Faucher, Member  
Laura L. McClure, Member  
Douglas R. Brown, Member



State of Kansas

*Kathleen Sebelius, Governor*

David Sprunge, Consumer Counsel  
1500 S.W. Arrowhead Road  
Topeka, Kansas 66604-4027  
Phone: (785) 271-3200  
Fax: (785) 271-3116  
<http://curb.kcc.state.ks.us/>

## SENATE UTILITIES COMMITTEE S.B. 414

Testimony on Behalf of the Citizens' Utility Ratepayer Board  
By David Sprunge, Consumer Counsel  
February 2, 2006

Chairman Emler and members of the committee:

Thank you for this opportunity to offer testimony on S.B. 414. The Citizens' Utility Ratepayer Board is opposed to this bill for the following reasons:

First, CURB does not support codifying in statute the type of mechanism in statute. While CURB would likely oppose before the Commission the implementation of an unnecessarily broad and one sided mechanism, as is proposed in this bill, codifying this type of mechanism in statute removes the Commission's flexibility to design a fair and balanced approach to capital recovery. Further, CURB believes that this type of mechanism is unnecessary. The utilities throughout history have had to deal with unexpected extraordinary capital expenditures. The Commission has historically granted accounting orders for extraordinary capital expenditures that are outside of the utility's normal operating parameters, or are outside of a utility test year. There is simply no reason to create this type annual surcharge. In fact, through the flexibility of the regulatory process, we did in fact place a small surcharge on Aquila bills in Aquila's last gas rate case to pay for a specific right of way project (21<sup>st</sup> street in Wichita). CURB would note that this was limited, specific, and the product of an agreement of all parties, meaning that customers also received other benefits within the agreement. It was a balance approach to a specific issue that benefited all parties, unlike the current bill.

Second, providing this type of one sided cost recovery mechanism favors the utility by shifting further risk onto ratepayers. Natural gas utilities already pass 100% of the gas costs directly to consumers each month. Of the total annual revenues that the utility needs to collect to pay its operating costs and profits for shareholders, the monthly customer charge provides accounts for over 40%. The monthly customer charge revenues are safe and risk free and non-volatile sources of capital recovery for the utility. Strategically every utility attempts to increase the customer charge to higher levels in each ratecase to "front load" costs into higher customer charges to reduce financial risk exposure. The remaining 50%-60% of annual revenues due a natural gas utility are collected through volumetric charges collected when customer uses the natural gas. However, through agreements with each gas utility, we have created a Weather Normalization Adjustment, that guarantees that the utility will collect its annual revenue requirement, regardless of whether it is colder or warmer than normal. This is a

Senate Utilities Committee  
February 2, 2006  
Attachment 5-1

mechanism that removes financial risk of changing weather from the utility. (CURB would note that the WNA mechanisms are a balanced risk reduction, benefiting consumers when weather is colder than normal) The Commission passes property tax changes through to consumers annually. And recently the Commission changed 30 years of policy and is now allowing natural gas utilities to recover the gas portion of uncollectible bills every year through the PGA mechanism. It is clear that in the broadest sense, natural gas utility rates, and policies implemented by the Commission, have served to minimize the financial risk that Kansas natural gas utilities face.

It is within this broad context that this bill must be understood. What this bill proposes to do is take one of the few remaining financial risks to the utility, that is timing difference between when the utility expends capital and when it can begin recovering capital in a rate case (regulatory lag), and create a mechanism to move that risk directly onto consumer bills. This bill will allow the utilities to increase rates twice a year as they spend money, without having the Commission or CURB examine the utility's other costs. From an accounting standpoint, the depreciation expense that is already in consumer rates should be adequate to fund the capital expenditures necessary to replace worn out or unsafe facilities. Using the depreciation expense to fund new capital expenditure replaces depreciated utility ratebase with new utility ratebase. (For example, assume a utility has a rate case every year, and has \$10 million in depreciation expense and \$10 million in new capital expenditures. Consumers should be held harmless, since rates would go down as rate base decreased by \$10 million through depreciation, but that ratebase is replaced by the new \$10 million capital expenditure, causing the consumer rates to go back up to the level they started. Under this bill, consumer rates would go up to account for the \$10 million spent by the utility, but rates would not be allowed to reflect the reduction for the \$10 million of depreciated rate base. Consumers pay higher rates, but don't get the benefit of any offsetting reductions.)

Third, while the utilities suggest that this bill, and the surcharge it creates will apply narrowly to a small subset of capital expenditures (safety and right of way), as drafted, the language in the bill will allow a natural gas utility to place almost all of its annual capital expenditures into this surcharge. For example, to be an "eligible infrastructure system replacement" and therefore eligible for the surcharge, the capital expenditure can be to "replace or extend the useful life of an existing infrastructure". (Section 2(d)(4) at page 1, line 35) With the exception of new lines placed in service to supply brand new developments, this language is broad enough to make every capital expenditure made by a utility on plant replacement or upgrade in every year an eligible infrastructure system replacement.

Also, the "natural gas utility plant projects", the cost of which will be placed in the surcharge are "mains, valves, service lines regulator stations vaults and other pipeline system components installed to comply with state or federal safety requirements as replacements for existing facilities that have worn out or are in deteriorating condition" (Section 2(f)(1) at page 1, line 41) Given that every utility has an ongoing obligation to operate a safe and reliable system, and must replace "worn out and deteriorating" facilities to maintain safety levels, again, every capital expenditure would fall within this

category and be eligible for inclusion in the surcharge. This bill is not narrow or specifically tailored.

Under the bill, utilities can avoid a rate review for up to 60 months, or longer, while increasing rates to consumers through the surcharge up to twice a year. (Section 3(b)-(c) and Section 4(c)) The bill only allows staff to review whether the “underlying costs are in accordance with the provisions” of the act and to “confirm the proper calculation”, and specifically states that “no other revenue requirement or ratemaking issues may be examined” in consideration of the petition. (Section 4(b)(2)) These provision are remarkably one sided and unfair to consumers. The bill goes on to state specifically what the Commission “shall only” consider in determining the “appropriate pretax revenue” to be generated by the surcharge. (Section 4(d)) Designating these categories as the only things that the Commission can consider specifically precludes CURB or the staff of the Commission from bringing forth evidence that may result in offsetting cost savings to the proposed rate increases. In fact, in calculating some of the costs, the bill specifically excludes any input from CURB. For example, if the utility’s last case was settled in a “black box” (a number is negotiated, but the specific adjustments are not specified) then to calculate the surcharge the bill requires the use of the average of the Staff and Company recommendations from the last case. (Section 4(d)(9)). Using only staff and the company completely ignores CURB’s recommendations in the last case, and will tend to bias upwards what consumers pay under the surcharge. Again, this provides protection and benefit to the utility, but provides nothing to the consumers that have to pay the costs.

This bill is clearly over-broad, ill-defined and one-sided in favor of the utilities. Nothing in this bill benefits, aids or provides protection and balance for consumers. The bill is clearly designed to create a regulatory system that simply reimburses the gas utilities for nearly everything they expend in an immediate and risk free fashion. As such CURB recommends that the Committee protect consumers and not pass this bill.

Thank you.

Without withdrawing or waiving CURB’s outright opposition to this bill, CURB is providing the Committee some suggested mark-up’s to the bill to remove what CURB considers some of the most egregious language in the bill. While CURB does not recommend the Committee pass this bill, if the Committee does decide to move forward with a bill of this nature, CURB request that the Committee make the following changes, at minimum, to bring some level o balance and protection back into the bill.

An Act concerning public utilities; relating to natural gas.

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

New Sec. 1 **Citation of act.** This act may be cited as the Gas Safety and Reliability Policy Act.

New Sec. 2 **Definitions.** For the purposes of this act.

(a) "GSRS" means gas system reliability surcharge.

(b) "Appropriate pretax revenues", means the revenues necessary to produce net operating income equal to:

(1) The natural gas public utility's weighted cost of capital multiplied by the net original cost of eligible infrastructure system replacements, including recognition of accumulated deferred income taxes and accumulated depreciation associated with eligible infrastructure system replacements which are included in a currently effective GSRS; and

(2) Recover state, federal, and local income or excise taxes applicable to such income; and

(3) Recover depreciation expenses.

(c) "Commission" means the state corporation commission.

(d) "Eligible infrastructure system replacement" means natural gas public utility plant projects that:

(1) Do not increase revenues by directly connecting the infrastructure replacement to new customers;

(2) Are in service and used and required to be used;

(3) Were not included in the natural gas public utility's rate base in its most recent general rate case; and

(4) ~~Replace or extend the useful life of an existing infrastructure;~~

(e) "Natural Gas Public Utility" shall have the same meaning respectively ascribed thereto by K.S.A. 66-1,200(a).

(f) "Natural Gas Utility Plant Projects" may consist only of the following:

(1) Mains, valves, service lines, regulator stations, vaults, and other pipeline system components installed pursuant to Commission approval to comply with new or extraordinary state or federal safety requirements as replacements for existing facilities that have worn out or are in deteriorated condition; that were not in effect at the time of the utility's last rate hearing;

~~(2) Main relining projects, service line insertion projects, joint encapsulation projects, and other similar projects extending the useful life or enhancing the integrity of pipeline system components undertaken to comply with state or federal safety requirements; and~~

(3) ~~(2)~~ Facilities, Facility relocations required due to construction or improvement of a highway, road, street, public way, or other public work by or on behalf of the United States, this state, a political subdivision of this state, or another entity having the power of eminent domain provided that the costs related to such projects have not been reimbursed to the natural gas public utility.

(g) "GSRS revenues", means revenues produced through a GSRS exclusive of revenues from all other rates and charges.

**New Section 3. Rate schedules, procedures to establish or change.**

(a) Notwithstanding any provisions of K.S.A. 66-117, and this chapter to the contrary, beginning July 1, 2006, a natural gas public utility ~~providing gas service~~ may file a petition ~~and proposed rate schedules~~ with the commission to establish ~~or change a~~ GSRS ~~rate schedules~~ that will allow for the adjustment of the natural gas public utility's rates and charges to provide for the recovery of costs for eligible infrastructure system replacements. ~~The commission may not approve an GSRS to the extent it would produce total annualized GSRS revenues below the lesser of one million dollars or one-half of one percent of the natural gas public utility's base revenue level approved by the commission in the natural gas public utility's most recent general rate proceeding. The commission may not approve a GSRS to the extent it would produce total annualized GSRS revenues exceeding ten percent of the natural gas public utility's base revenue level approved by the commission in the natural gas public utility's most recent general rate proceeding. A GSRS and any future changes thereto shall be calculated and implemented in accordance with the provisions of New Sections 2 through 4. GSRS revenues shall be subject to a refund based upon a finding and order of the commission to the extent provided in subsections (e) and (h) of New Section 4.~~

(b) The commission shall not approve a GSRS for any natural gas public utility that has not had a general rate proceeding decided or dismissed by issuance of a commission order within the past 60 months, unless the natural gas public utility has filed for or is the subject of a new general rate proceeding.

(c) In no event shall a natural gas public utility collect a GSRS for a period exceeding sixty months unless the natural gas public utility has filed for or is the subject of a new general rate proceeding; provided that the GSRS may be collected until the effective date of new rate schedules established as a result of the new general rate proceeding, or until the subject general rate proceeding is otherwise decided or dismissed by issuance of a commission order without new rates being established.

**New Section 4 Documentation to be submitted—notice to be published—examination of proposal—authorization by commission, when—pretax revenues, factors to be considered—revised rate schedule, filed when—rulemaking authority.**

(a) At the time that a natural gas public utility files a petition with the commission seeking to establish or change a GSRS, it shall submit proposed GSRS rate schedules and its supporting documentation regarding the calculation of the proposed GSRS with the petition, and shall serve a copy of said petition upon the Commission Staff and the Citizens Utility Ratepayer Board. ~~with a copy of its petition, its proposed rate schedules, and its supporting documentation.~~

(b) (1) When a petition, ~~along with any associated proposed rate schedules~~, is filed ~~pursuant to the provisions of New Sections 2 through 4~~, the commission shall ~~conduct an examination of the proposed GSRS.~~

(2) The staff of the commission ~~may examine information of the Natural gas public utility to confirm that the underlying costs are in accordance with the provisions of New Sections 2 through 4 and to confirm proper calculation of the proposed~~



charge, and may shall submit a report regarding its examination to the commission not later than sixty days after the petition is filed. ~~No other revenue requirement or ratemaking issues may be examined in consideration of the petition or associated proposed rate schedules filed pursuant to the provisions of New sections 2 through 4.~~

3) (2) The commission may hold a hearing on the petition and any associated rate schedules and shall issue an order to become effective not later than one hundred twenty days after the petition is filed.

~~(4)~~ (3) If the Commission finds that a petition complies with the requirements of New Sections 2 through 4, the commission shall enter an order authorizing the natural gas public utility to impose a GSRS that is sufficient to recover appropriate pretax revenue, as determined by the commission pursuant to the provisions of New sections 2 through 4.

(c) A natural gas utility may effectuate a change in its rate pursuant to the provisions of this section no more often than ~~two times~~ once every twelve months.

(d) In determining the appropriate pretax revenue, the commission shall consider ~~only~~ the following factors:

(1) The net original cost of eligible infrastructure system replacements. The net original cost shall be defined as the original cost of eligible infrastructure system replacements less associated retirements of existing infrastructure;

(2) The accumulated deferred income taxes associated with the eligible infrastructure system replacements;

(3) The accumulated depreciation associated with the eligible infrastructure system replacements;

(4) The current state, federal, and local income tax or excise rates;

(5) The natural gas public utility's actual regulatory capital structure as determined during the most recent general rate proceeding of the natural gas public utility;

(6) The actual cost rates for the natural gas public utility's debt and preferred stock as determined during the most recent general rate proceeding of the natural gas public utility.

(7) The natural gas public utility's cost of common equity as determined during the most recent general rate proceeding of the natural gas public utility.

(8) The current depreciation rates applicable to the eligible infrastructure system replacements; and

(9) In the event information pursuant to subdivisions (5), (6), and (7) of this subsection is unavailable and the commission is not provided with such information on an agreed-upon basis, the Commission shall utilize the ~~average of the recommendations contained in the testimony submitted by the natural gas public utility, and~~ Commission staff during the most recent general rate proceeding of the natural gas public utility to determine the capital structure, recommended cost rates for debt and preferred stock, and recommended cost of common equity to determine the average weighted cost of capital.

(e) (1) The monthly GSRS charge shall be allocated among the natural gas public utility's classes of customers in the same manner as costs for the same type of facilities was allocated among classes of customers in the natural gas public utility's most recent general rate proceeding. If that allocation is not available or determinable, the

Commission shall utilize ~~the average of~~ the recommendations contained in the testimony submitted by the ~~natural gas public utility and the~~ commission staff during the most recent general rate proceeding of the natural gas public utility regarding class allocation of costs.

(2) At the end of each twelve-month calendar period the GSRS is in effect, the natural gas public utility shall reconcile the differences between the revenues resulting from a GSRS and the appropriate pretax revenues as found by the commission for that period and shall submit the reconciliation and a proposed GSRS adjustment to the commission for approval to recover or refund the difference, as appropriate, through adjustments of the GSRS charge.

(f) (1) A natural gas public utility that has implemented an GSRS pursuant to the provisions of New Sections 2 through 4 shall file revised rate schedules to reset the GSRS to zero when new base rates and charges become effective for the natural gas public utility following a commission order establishing customer rates in a general rate proceeding that incorporates in the utility's base rates, subject to subsections (h) and (i) of this section, eligible costs previously reflected in the currently effective GSRS.

(2) Upon the inclusion in a natural gas public utility's base rates subject to subsections (h) and (i) of this section of eligible costs previously reflected in a GSRS, the natural gas public utility shall immediately thereafter reconcile any previously unreconciled GSRS revenues as necessary to ensure that revenues resulting from the GSRS match as closely as possible the appropriate pretax revenues as found by the commission for that period.

~~(g) A natural gas public utility's filing of a petition or change to an GSRS pursuant to the provisions of New Sections 2 through 4 shall not be deemed to be a rate increase for purposes of K.S.A. 66-117.~~

~~(h) (g)~~ Commission approval of a petition, and any associated rate schedules, to establish or change a GSRS pursuant to the provisions of New Sections 2 through 4 shall in no way be binding upon the commission in determining the ratemaking treatment to be applied to eligible infrastructure system replacements during a subsequent general rate proceeding when the commission may undertake to review the reasonableness and prudence of such costs. In the event the commission disallows, during a subsequent general rate proceeding, recovery of costs associated with eligible infrastructure system replacements previously included in a GSRS, the natural gas public utility shall offset its GSRS in the future as necessary to recognize and account for any such over collections.

~~(i) (h)~~ Nothing in this section shall be construed as limiting the authority of the commission to review and consider infrastructure system replacement costs along with other costs during any general rate proceeding of any natural gas public utility.

New Section 5: Notwithstanding the above sections, the Commission shall retain the option of expensing directly on consumer bills, the cost of eligible infrastructure system replacement costs for natural gas utility projects, rather than calculating and imposing the GSRS in a manner that recovers the appropriate pretax revenues as defined in the bill.

New Section 6 ~~5~~. **Effective Date.** This act shall take effect and be in force from and after its publication in the statute book.



# KANSAS

CORPORATION COMMISSION

KATHLEEN SEBELIUS, GOVERNOR  
BRIAN J. MOLINE, CHAIR  
ROBERT E. KREHBIEL, COMMISSIONER  
MICHAEL C. MOFFET, COMMISSIONER

BEFORE THE SENATE UTILITIES COMMITTEE  
PRESENTATION OF THE  
KANSAS CORPORATION COMMISSION  
February 2, 2006

SB 414

Thank you, Chairman and members of the Committee. I am Don Low, Director of the Utilities Division for the Kansas Corporation Commission. I appreciate the opportunity to testify on SB 414 on behalf of the Commission. The Commission opposes this legislation because it does not allow for a determination of the reasonableness of and need for a surcharge based on the individual circumstances of each natural gas utility.

Surcharges such as the proposed GSRS represent what is known as "single issue ratemaking." Single issue ratemaking occurs when customer rates are changed based on only a single aspect of the numerous factors that normally go into determining the revenue requirements for a traditionally regulated company. Single issue ratemaking is a departure from the normal practice of determining appropriate rates by looking at all the expenses, investment, cost of capital and revenues of a utility in a test period. The concern that must be addressed in evaluating single issue rates is that changing rates based on only one factor necessarily ignores potential offsetting changes in other factors. For example, increases in some costs may be offset by decreases in other costs or by increased revenues. If there are such offsetting changes, the rates resulting from the examination of only one factor might not accurately reflect the real financial needs of the company.

This is not to say that such a ratemaking approach is never justified. Indeed, the KCC and other state commissions generally allow for "single issue ratemaking" when there is enough justification to override the general concern that resulting rates might be unreasonable.

Senate Utilities Committee  
February 2, 2006  
Attachment 6-1

The Kansas legislature has provided specific authorization for single issue ratemaking in two situations. K.S.A. 66-117(f) provides for a surcharge by electric and natural gas utilities to reflect changes in the utility's ad valorem tax expenses. K.S.A. 6-1230 *et seq* provided for a similar surcharge for right-of-way fees imposed by cities but it was limited to costs incurred during a short period in 2002 and 2003. In addition, K.S.A. 66-1237 provides for the unbundling of transmission costs and subsequent changes in rates. Although the transmission rate changes are dependent on approval by FERC, they might be viewed as a form of single issue ratemaking.

The KCC has also exercised its discretion under existing law to allow specific surcharges or pass-through mechanisms. The Purchased Gas Adjustment (PGA) and Energy Cost Adjustment (ECA) mechanisms first were allowed in the late 1970's when natural gas and energy costs were volatile and largely beyond the control of the utilities. The ECA was eliminated for some electric companies in the early 90's when energy costs were more stable but has recently been reinstated. The Commission also recently approved of an Environmental Cost Recovery Rider to allow for quicker recovery of Westar's expected investments in pollution control facilities. That ECRR is expected to reduce the overall final costs to ratepayers of the equipments.

In deciding to allow these mechanisms, the Commission has carefully considered whether there was good reason to override the general concerns about single-issue ratemaking. Our concern with SB 414 is that it would not let the KCC undertake that balancing with regard to the specific circumstances of each company. Under subsection 4(b)(4) of the bill, the KCC is required to allow a GSRS for the company if the costs involved meet the bill's criteria. Thus, even if the company were experiencing declines in other expenses or investment that more than offset the costs addressed in the GSRS, the KCC would not have the ability to deny a surcharge. We recognize that there are limitations on the size and duration of the GSRS imposed by the bill. Nonetheless, the concern is that, without vesting discretion in the Commission to weigh the equities, circumstances could arise whereby the surcharge could result in customers paying unreasonable rates. Consequently, the Commission opposes the mandatory nature of this bill.