

BEFORE THE STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS

In the Matter of the Application of Black Hills/Kansas Gas Utility Company, LLC, d/b/a Black Hills Energy, for Approval of the Commission to Make Certain Changes in its Rate for natural Gas Service

Docket No.

14-BHCG-502-RTS

DIRECT TESTIMONY OF

RICHARD G. PETERSEN

FOR BLACK HILLS / KANSAS GAS UTILITY COMPANY, LLC

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2

I. NAME AND POSITION

3

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

4

A. My name is Richard G. Petersen. My business address is 1102 E First Street, Papillion, Nebraska.

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6

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

7

A. I am employed by Black Hills Utility Holdings, Inc. ("BHUH") as the Director of Regulatory Financial Services and Reporting. In this position, my responsibilities include financial reporting for BHUH's utilities, including Black Hills/Kansas Gas Utility Company, LLC, d/b/a Black Hills Energy ("Black Hills Kansas") and the preparation of financial exhibits and other information for rate case filings.

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II. BACKGROUND AND QUALIFICATION OF WITNESS

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Q. WILL YOU PLEASE STATE YOUR EDUCATIONAL BACKGROUND AND

15

BUSINESS EXPERIENCE?

1 A. I attended Dana College where I obtained a degree in Business Administration. I
2 began working for Northern Natural Gas Company and held various positions in
3 the Accounting and Regulatory Departments. In 1985, Aquila (previously known
4 as UtiliCorp United Inc.) purchased the Peoples Natural Gas Division ("Peoples")
5 from InterNorth, Inc. In 2008 Black Hills Corporation ("BHC") purchased the gas
6 and the Colorado electric properties from Aquila. I have held various positions in
7 the Accounting and Regulatory groups within Peoples, Aquila and BHUH.

8 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE ANY REGULATORY**
9 **BODIES?**

10 A. I have filed testimony before the Public Utilities Commission of Colorado, the
11 Iowa Utilities Board, the West Virginia Public Service Commission, the Michigan
12 Public Service Commission, the Nebraska Public Service Commission, the
13 Kansas Corporation Commission ("Commission") and the Missouri Public Service
14 Commission.

15

16 **III. PURPOSE OF TESTIMONY**

17 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

18 A. I am sponsoring the following accounting information on behalf of Black Hills
19 Kansas:

- 20 • Section 3 – Summary of rate base, operating income and rate of
21 return;
- 22 • Section 4 – Plant investments;
- 23 • Section 5 – Accumulated provision for depreciation and amortization;

- 1 • Section 6 – Working capital;
- 2 • Section 7 – Capitalization;
- 3 • Section 8 – Financial and operating data;
- 4 • Section 9 – Test year and pro forma income statements;
- 5 • Section 10 – Depreciation and amortization;
- 6 • Section 11 – Taxes;
- 7 • Section 12 – Allocation ratios;
- 8 • Section 13 – Annual report to BHC's stockholders and the Securities
9 and Exchange Commission.

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11 **IV. TESTIMONY**

12 **A. SECTION 3-SUMMARY OF RATE BASE, OPERATING INCOME AND**
13 **RATE OF RETURN**

14 **Q. PLEASE EXPLAIN THE SCHEDULES CONTAINED IN SECTION 3.**

15 A. Section 3 shows the computation of Black Hills Kansas rate base for natural gas
16 operations and the adjusted rate of return for the Company's Kansas natural gas
17 operations during the test year ended December 31, 2013. Schedule 1 is a
18 summary sheet which presents the various components of rate base and the
19 adjusted rate of return for Kansas. Rate base is shown as of the end of test
20 period, December 31, 2013. Line 16 of Schedule 1 shows the rate base as of
21 December 31, 2013 was \$131,193,233. Line 20 of Schedule 1 shows the rate of
22 return from present rates and rate base is 4.1682%. The proposed revenue

1 increase necessary to yield the requested 7.5220% rate of return is \$7,278,700
2 as shown on Schedule 1, Line 25.

3 **Q. PLEASE DESCRIBE SECTION 3, SCHEDULE 2, PAGE 1.**

4 A. This is a summary of the per-books test year rate base, related adjustments, and the
5 resulting test year rate base after these adjustments. The Adjusted Test Year rate base
6 is \$131,193,233. There are five adjustments to test year rate base. I will discuss the
7 adjustment for depreciation (RB-1); the depreciation product reassignment adjustment
8 (RB-3) and the adjustment for working capital (RB-5). Company Witness Jason Keil will
9 cover capital additions (RB-2). Company Witness Ann Stichler will address the
10 adjustment for the Gas Supply Management System (RB-4).

11 **Q. PLEASE EXPLAIN ADJUSTMENT RB-1.**

12 A. This adjustment reflects the impact on accumulated depreciation for the
13 depreciation annualization adjustment to the income statement (IS-16).

14 **Q. PLEASE EXPLAIN ADJUSTMENT RB-3.**

15 A. This adjustment reflects the impact on accumulated depreciation for the
16 depreciation product reassignment adjustment to the income statement (IS-17).

17 **Q. PLEASE EXPLAIN ADJUSTMENT RB-5.**

18 A. This adjustment to rate base reflects the impact of the working capital calculation.
19 The working capital calculation is shown in Section 6 and will be described later
20 in my testimony.

21 **Q. PLEASE EXPLAIN THE COMPONENTS OF TOTAL GAS PLANT BALANCES**
22 **WHICH ARE INCLUDED IN YOUR RATE BASE CALCULATIONS.**

1 A. The amounts shown for Total Gas Plant on Section 3, Schedule 2, Line 1
2 represent Black Hills Kansas Gas Plant in Service assigned to Kansas as of
3 December 31, 2013.

4 **Q. IS CONSTRUCTION WORK IN PROGRESS (CWIP) INCLUDED IN THE**
5 **TOTAL PLANT BALANCE OF DECEMBER 31, 2013?**

6 A. No. Black Hills Kansas has followed previous practices and has excluded CWIP
7 from the rate base calculation. However, Black Hills is seeking to recover CWIP
8 that is completed and placed in service by June 30, 2014 as noted in the
9 testimony of Witness Jason Keil.

10 **Q. WHAT IS INCLUDED IN THE MATERIALS AND SUPPLIES BALANCE**
11 **SHOWN ON SECTION 3, SCHEDULE 2, PAGE 1?**

12 A. Black Hills Kansas has prepared a thirteen-month average of Materials and
13 Supplies balances for use in its rate base calculation.

14 **Q. WHAT DOES GAS STORAGE REPRESENT ON SECTION 3, SCHEDULE 2,**
15 **PAGE 1?**

16 A. This represents a thirteen-month average of the gas inventory owned by Black
17 Hills Kansas and used for its Kansas operations.

18 **Q. WHAT IS INCLUDED IN PREPAYMENTS?**

19 A. Prepayments include advance payments for insurance, pension and gas
20 purchases.

21 **Q. WHAT IS INCLUDED IN WORKING CAPITAL?**

22 A. The calculation and explanation of the Working Capital component of rate base is
23 found in Section 6, Schedule 1, page 1.

1 **Q. PLEASE EXPLAIN SECTION 3, SCHEDULE 2, PAGES 2 THROUGH 29.**

2 A. Page 2 shows the Black Hills Kansas test year Income Statement for the test
3 year ended December 31, 2013. Page 3 reflects the total of all pro forma
4 adjustments. Page 4 indicates the income statement resulting after the inclusion
5 of the total of all pro forma adjustments. A calculation of each adjustment is
6 provided in Section 3, Schedule 2, Pages 5 through 29. A narrative explanation
7 of each adjustment is included in Section 9, Schedule 2, Pages 1 through 5.

8 **Q. PLEASE DESCRIBE SECTION 3, SCHEDULE 3.**

9 A. This schedule shows the computation of Black Hills Kansas revenue deficiency
10 based on the requested rate of return. The Revenue Deficiency is \$7,278,700.

11

12 **B. SECTION 4- PLANT INVESTMENTS**

13 **Q. PLEASE DESCRIBE SECTION 4.**

14 A. This section describes Black Hills Kansas Plant Investment for the State of
15 Kansas gas operations. Schedule 1 summarizes Gas Plant in Service. The
16 adjusted investment is \$241,734,776. Schedule 2 shows the gas plant in service
17 by primary account as of the end of the test year (December 31, 2013), at the
18 end of the prior twelve-month period (December 31, 2012), and at the end of the
19 three calendar years preceding the test year.

20

21 **C. SECTION 5 - ACCUMULATED PROVISION FOR DEPRECIATION AND**
22 **AMORITIZATION**

23 **Q. PLEASE EXPLAIN SECTION 5.**

1 A. This section presents Black Hills Kansas Accumulated Depreciation and
2 Amortization for Kansas gas operations. Schedule 1 shows the accumulated
3 depreciation and amortization by functional class and the corresponding
4 adjustments as of the dates shown in Section 4 relating to Plant Investment.

5

6 **D. SECTION 6- WORKING CAPITAL**

7 **Q. PLEASE EXPLAIN SECTION 6.**

8 A. Section 6 shows the computations of cash working capital for Black Hills Kansas
9 gas operations. Theoretically, cash working capital is the sum of cash that the
10 company must raise and have available for payment of normal operation and
11 maintenance expenses. This requirement is offset by cash that may be available
12 to the Company because a collection of cash has been made on behalf of a third
13 party, but not yet paid to the third party. An example would be the collection by
14 the Company of income taxes, which have not been paid to the state or federal
15 government. Another example would be the collection of interest that has not yet
16 been paid to the lender. In the calculation of a traditional lead/lag study, cash
17 collected for payment of taxes and interest would be an offset to the cash
18 required for working capital.

19 **Q. HOW WAS THE CASH WORKING CAPITAL REQUIREMENT CALCULATED**
20 **BY BLACK HILLS KANSAS GAS OPERATIONS?**

21 A. The amount of cash required for operating expenses was determined by
22 calculating one-eighth of annual O&M expenses for Kansas Gas Operations.
23 This calculation is shown in Section 6 on Schedule 1, page 1. This calculation,

1 used in past filings by various other utilities at the state and federal level,
2 approximates the cash required to operate a utility for 45 days. Forty-five days
3 generally allows a utility to manage through a complete cycle of monthly
4 customer billings and collections, as well as receipt and payment of invoices for
5 third party purchases and services, and employee payroll costs.

6 **Q. WERE THERE ANY OFFSETS TO THE WORKING CAPITAL CALCULATED**
7 **UNDER THIS METHOD?**

8 A. Yes. Reductions were made for accrued taxes and accrued interest.

9 **Q. WHAT IS THE AMOUNT OF WORKING CAPITAL REQUESTED TO BE**
10 **INCLUDED IN RATE BASE?**

11 A. The calculation in Section 6, Schedule 1, page 1, resulted in an allowance for
12 working capital of \$724,090.

13
14 **E. SECTION 7- CAPITALIZATION**

15 **Q. PLEASE DESCRIBE SECTION 7, SCHEDULES 1, 2 AND 3.**

16 A. This Section presents the capital structure and requested rate of return for Black
17 Hills Kansas gas operations for the twelve months ending December 31, 2013
18 and December 31, 2012. Schedule 1, Page 1 shows the requested rate of return
19 on total capital for the test year as 7.5220%. Schedule 2 shows a summary of
20 Black Hills Kansas long-term debt by month during the test year, the monthly
21 interest and the cost of each series of notes. Schedule 3 shows the interest
22 coverage calculation for Black Hills Kansas gas operations.

23 **Q. PLEASE DESCRIBE SECTION 7, SCHEDULE 4.**

1 A. Schedule 4 summarizes the Capital Structure for Black Hills Kansas at test year
2 end December 31, 2013 and for the year ended December 31, 2012.

3

4 **F. SECTION 8- FINANCIAL AND OPERATING DATA**

5 **Q. PLEASE DESCRIBE SECTION 8, SCHEDULE 1.**

6 A. Schedule 1 presents a balance sheet by primary account for Black Hills Kansas
7 total gas operations. The balance sheet includes the test year twelve months
8 ended December 31, 2013 and December 31, 2012, and each of the three
9 calendar years preceding the test year.

10 **Q. PLEASE EXPLAIN SECTION 8, SCHEDULES 2, 3, 4 AND 5.**

11 A. Schedules 2, 3, 4 and 5 of Section 8 all provide account detail corresponding to
12 the balance sheet and income statement data previously presented. Schedule
13 2A is an income statement by primary account for Black Hills Kansas gas
14 operations. Schedule 2B is an income statement and statement of retained
15 earnings by primary account for Black Hills Kansas' gas operations. Schedule 3
16 is a summary of Operating Revenues and Expenses by primary account for
17 Black Hills Kansas gas operations. Schedule 4 provides operating statistics by
18 rate schedule for the years 2010, 2011, 2012, twelve months ended December
19 31, 2012 and December 31, 2013. Schedule 5 shows annual payroll expense by
20 primary account for these same twelve month periods.

21

22 **G. SECTION 9- TEST YEAR AND PRO FORMA INCOME STATEMENTS**

23 **Q. PLEASE BRIEFLY SUMMARIZE SECTION 9, SCHEDULE 1.**

1 A. This section presents the Income Statement and all pro forma adjustments to the
2 test year. Column 1 provides the per-book income statement with revenues
3 annualized, Column 2 is the sum of the pro forma adjustments and Column 3 is
4 the Income Statement after all adjustments. Schedule 1 shows that the net
5 effect of all pro forma adjustments is to reduce Utility Operating Income by
6 \$(3,720,773).

7 **Q. PLEASE EXPLAIN SECTION 9, SCHEDULE 2.**

8 A. Section 9, Schedule 2 is an explanation of all pro forma adjustments that affect
9 the income statement.

10 **Q. WHY WERE THESE ADJUSTMENTS MADE?**

11 A. The adjustments were made to the test year to remove possible non-recurring
12 events in the test year that were caused by weather fluctuations or other unusual
13 circumstances. Adjustments also reflect known and measurable changes that
14 have occurred, or are expected to occur within a short time period subsequent to
15 end of the test year. When all adjustments are considered, the data for the fully-
16 adjusted test year will reflect the Company's performance under "normal"
17 operating circumstances.

18 **Q. HAVE THESE ADJUSTMENTS BEEN REFLECTED IN PRIOR RATE CASE**
19 **FILINGS WITH THE COMMISSION?**

20 A. Yes. Most of the adjustments have been used in previous rate cases, and were
21 accepted by the Commission.

22 **Q. WHO WILL PROVIDE SUPPORT FOR THESE ADJUSTMENTS?**

1 A. Tom Sullivan, a Company consultant, will support weather and irrigation
2 normalization adjustments (Adjustment Nos. IS- 1 and IS- 2).

3

4 The adjustments supported by Company Witness Ann Stichler are the impact of
5 the Black Hills Kansas Weather Normalization Adjustment program (Adjustment
6 No.IS-3); an Ad Valorem tax adjustment (Adjustment No.IS- 4); the payroll
7 annualization adjustment (Adjustment No.IS- 6); the impact of a new Gas
8 Management System (Adjustment No. IS-13); two adjustments related to the
9 acquisition of Anadarko properties (Adjustment Nos. IS-5 and IS-12); an
10 adjustment for the “Future Track” employee program (IS-15); and a property tax
11 adjustment (Adjustment No.IS-20).

12

13 Company Witness Jason Keil will support the adjustments for advertising costs
14 (Adjustment No. IS-8); contributions and dues (Adjustment No.IS- 9); rate case
15 expenses (Adjustment No. IS-11); bad debts (Adjustment No. IS-14) and
16 depreciation expense relating to capital additions (Adjustment No. IS-18).

17

18 I will support the remaining pro forma adjustments—employee severance
19 expense (Adjustment No.IS-7); workers’ compensation (Adjustment No.IS-10);
20 depreciation expense annualization (Adjustment No. IS-16); a product
21 reassignment for depreciation expenses (Adjustment No.IS-17) and a
22 commission assessment expense adjustment (Adjustment No. IS-19).

23

1 The depreciation adjustments include the results of depreciation studies
2 prepared by Company Consultant John Spanos. His testimony will address the
3 determination of new depreciation rates for Black Hills Kansas direct operations,
4 Black Hills Service Company, and BHUH.

5
6 **H. SEVERANCE EXPENSE ADJUSTMENT (ADJUSTMENT NO. 1S-7)**

7 **Q. PLEASE EXPLAIN ADJUSTMENT NO. IS-7 RELATING TO SEVERANCE**
8 **COSTS.**

9 A. The elimination of \$40,280 of expense reflects one time employee severance
10 payments. The charges applicable to Kansas were \$11,018 for direct Kansas
11 operations, \$4,648 allocated to Kansas from Black Hills Service Company
12 (“BHSC”) and \$24,614 allocated to Kansas from BHUH.

13
14 **I. WORKERS COMPENSATION ADJUSTMENT (ADJUSTMENT NO. 1S-10)**

15 **Q. PLEASE EXPLAIN THE ADJUSTMENT FOR WORKER’S COMPENSATION**
16 **(ADJUSTMENT NO. IS-10).**

17 A. A one-time reduction in expense of \$144,119 was made in November 2013 to the
18 Workers’ Compensation accrual account. This one-time adjustment has been
19 reversed in the case and also increased by \$12,832 to reflect the normal monthly
20 accrual for 2013. The total pro forma adjustment (Adjustment No. IS-10) is
21 \$156,951.

1 **J. DEPRECIATION ANNUALIZATION (ADJUSTMENT NO. IS-16)**

2 **Q. ADJUSTMENT NO. IS- 16 ANNUALIZES DEPRECIATION EXPENSE. PLEASE**
3 **EXPLAIN.**

4 This adjustment annualizes depreciation expenses based on twelve months
5 ended December 31, 2013 plant balances. The adjustment is the difference
6 between the actual expense for the twelve months ended December 31, 2013
7 and the annualized year-end amount, and recognizes changes in the annual
8 level of expense associated with plant additions and retirements occurring during
9 the test year. The adjustment is also reflected in the accumulated provision for
10 depreciation.

11
12 Additionally, depreciation studies for BHSC assets, BHUH assets and Black Hills
13 Kansas gas assets were completed by outside consultant John Spanos. The
14 results of his studies are also reflected in the depreciation annualization
15 adjustment. Mr. Spanos will cover the calculation of the three depreciation
16 studies in his direct testimony.

17
18 **K. DEPRECIATION EXPENSE PRODUCT REASSIGNMENT**
19 **(ADJUSTMENT NO. IS-17)**

20 **Q. PLEASE EXPLAIN ADJUSTMENT NO. IS-17 WHICH REFLECTS A PRODUCT**
21 **REASSIGNMENT FOR DEPRECIATION EXPENSE.**

22 A. A review of the common general plant assignment between regulated and non-
23 regulated operations is performed every year. As a result of this review, it was

1 determined that an adjustment should be made to plant and accumulated
2 depreciation by general plant account to ensure that no subsidization exists
3 between regulated and non-regulated operations.
4

5 **L. COMMISSION ASSESSMENTS (ADJUSTMENT NO. IS-19)**

6 **Q. PLEASE EXPLAIN THE ADJUSTMENT FOR COMMISSION ASSESSMENT**
7 **ACCRUALS (ADJUSTMENT NO. IS-19).**

8 A. In 2013, an entry was made to Account 408 (taxes other than income) to reduce
9 Commission assessment expenses based on revenue. This one-time adjustment
10 for past periods should be reversed so that assessment amounts accrued
11 properly reflect the annual cost of Commission assessments. The pro forma
12 adjustment increased expense by \$224,321.
13

14 **M. SECTION 10- DEPRECIATION AND AMORITIZATION**

15 **Q. PLEASE EXPLAIN SECTION 10.**

16 A. Section 10 shows the per-book annual Depreciation and Amortization expenses
17 by functional class.
18

19 **N. SECTION 11- TAXES**

20 **Q. PLEASE DESCRIBE SECTION 11.**

21 A. Section 11 shows the impact of all Adjustments on Income Taxes. Schedules 2
22 and 3 show the Computation of Taxable Income before and after all Pro Forma
23 Adjustments. Schedule 4 shows the Computation of Income Taxes before and

1 after all Pro Forma Adjustments. Schedule 5 reflects Deferred Taxes Relating to
2 ITC. Schedule 6 shows the Deferred Income Tax balances arising from
3 Accelerated Depreciation.

4
5 **O. SECTION 12- ALLOCATION RATIOS**

6 **Q. PLEASE EXPLAIN SECTION 12.**

7 A. Section 12 describes the various allocation bases used to assign corporate
8 support costs to Kansas gas operations.

9
10 **P. ANNUAL REPORT**

11 **Q. PLEASE EXPLAIN SECTION 13.**

12 A. Section 13 includes BHC'S 2013 Annual Report and Form 10-K, as filed with the
13 Securities and Exchange Commission.

14
15 **V. CONCLUSION**

16 **Q. MR. PETERSEN, DOES THIS CONCLUDE YOUR PRE-FILED DIRECT**
17 **TESTIMONY IN THIS PROCEEDING?**

18 A. Yes.

State of Nebraska)
) ss
County of Douglas)

AFFIDAVIT OF RICHARD G. PETERSEN

I, Richard G. Petersen, being first duly sworn on oath, depose and state that I am the same Richard G. Petersen identified in the foregoing Direct Testimony; that I have caused the foregoing Direct Testimony to be prepared and am familiar with the contents thereof, and that the foregoing Direct Testimony as identified therein is true and correct to the best of my knowledge, information, and belief as of the date of this Affidavit.



Richard G. Petersen

Subscribed and sworn to before me,
A Notary Public, in and for said County
and State, this 11th day of April.



Notary Public

My Commission expires: _____

