

BEFORE THE STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS

In the Matter of the Application of Kansas Gas)
Service, a Division of ONE Gas, Inc. for)
Approval of an Accounting Order to Track)
Expenses Associated with the Investigating,)
Testing, Monitoring, Remediating and Other)
Work Performed at the Manufactured Gas)
Plant Sites Managed by Kansas Gas Service.)

Docket No. 17-KGSG-455-ACT

TESTIMONY IN SUPPORT OF
UNANIMOUS SETTLEMENT AGREEMENT

OF DAVID SCALF

ON BEHALF OF

KANSAS GAS SERVICE, A DIVISION OF ONE GAS, INC.

1 **I. INTRODUCTION**

2 **Q. PLEASE STATE YOUR NAME.**

3 A. My name is David Scalf.

4 **Q. BY WHOM ARE YOU EMPLOYED AND WHAT IS YOUR BUSINESS ADDRESS?**

5 A. I am employed by ONE Gas, Inc., ("ONE Gas," "Kansas Gas Service" or "Company"). My
6 business address is 15 E. 5th Street, Tulsa, Oklahoma.

7 **Q. WHAT IS YOUR POSITION WITH ONE Gas?**

8 A. I am Vice President of Rates and Regulatory Affairs.

9 **Q. DID YOU FILE DIRECT AND REBUTTAL TESTIMONY ON BEHALF OF KANSAS**
10 **GAS SERVICE IN THIS CASE?**

11 A. I filed rebuttal testimony. I am also sponsoring and adopting the direct testimony filed by
12 David N. Dittmore in this case. Mr. Dittmore has recently left the Company.

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

14 A. I am providing testimony in support of the Unanimous Settlement Agreement ("Agreement")
15 between Kansas Gas Service, the Staff of the Kansas Corporation Commission ("Staff" and
16 "Commission," respectively), and the Citizens' Utility Ratepayer Board ("CURB")
17 (collectively, the "Parties"). I discuss the benefits of entering into a settlement in a case like
18 this one where the Parties had the benefit of a previous Commission decision dealing with the
19 regulatory treatment/policy of environmental costs incurred by a natural gas utility in the work
20 performed at a Manufactured Gas Plant ("MGP") site managed by the utility. I also provide
21 an overview of the terms of the Agreement entered into by the Parties in this case. Finally,
22 I apply the Commission standards for review of settlements to the Agreement in this case.

23 **Q. WHO ARE THE PARTIES TO THIS DOCKET?**

1 A. The Parties to this docket are Staff, CURB, and Kansas Gas Service.

2 **Q. ARE THERE ANY ISSUES NOT ADDRESSED IN THE AGREEMENT THAT ANY**
3 **OF THE PARTIES WISH TO LITIGATE?**

4 A. No, there are not. The Agreement addresses all issues between Staff, CURB, and Kansas Gas
5 Service.

6 **Q. WHO PARTICIPATED IN THE SETTLEMENT NEGOTIATIONS IN THIS**
7 **DOCKET?**

8 A. Representatives from Staff, CURB, and Kansas Gas Service participated in the settlement
9 negotiations in this docket. The Parties met at the Commission on September 28, 2017,
10 pursuant to the Commission's procedural order dated May 23, 2017, to collectively discuss the
11 issues in this docket and the possibility for settlement of some or all the issues. The Parties
12 continued their settlement discussions through October 12, 2017. A unanimous settlement of
13 all issues was reached by Staff, CURB and Kansas Gas Service resulting in the Agreement
14 filed with the Commission on October 12, 2017.

15 **II. BENEFITS OF ENTERING INTO A SETTLEMENT IN THIS TYPE OF DOCKET**

16 **Q. ARE SETTLEMENTS SUCH AS THE AGREEMENT FILED IN THIS CASE**
17 **BENEFICIAL?**

18 A. Yes. Settlements, like the Agreement filed in this docket, avoid adversarial litigation. They
19 save all parties (and the Commission) the time and cost of preparing for and participating in
20 an extensive evidentiary hearing. Settlements allow parties, who represent different interests
21 and who have different opinions on various issues, the ability to discuss and have an open
22 dialogue regarding their differences. This dialogue provides for "give and take" resulting in
23 an agreement that represents a compromise that considers, or balances, those varying interests

1 and opinions.

2 As I mentioned earlier in my testimony, the Parties had the advantage of the
3 Commission's decision in the KPS Case for guidance in this docket. Kansas Gas Service
4 relied upon the Commission's decision in the KPS Case regarding cost sharing and incentive
5 mechanisms in preparing its application in this docket. The Staff relied upon the
6 Commission's decision in the KPS Case as its starting point and then recommended certain
7 changes to the mechanisms to account for differences between the two cases. Kansas Gas
8 Service's rebuttal testimony challenged some of Staff's recommended changes to the
9 Commission approved KPS mechanisms. Many of the terms in the Agreement are based upon
10 the Commission's decision in the KPS Case, while some of the other terms in the Agreement
11 reflect the recommendations made by Staff and CURB.

12 **Q. WHAT ASSURANCE DOES THE COMMISSION HAVE THAT SETTLEMENTS**
13 **RESULT IN JUST AND REASONABLE RATES AND ARE IN THE PUBLIC**
14 **INTEREST?**

15 A. In some respect, settlements like the Agreement reached in this case, may produce a better
16 result than if the case were to be litigated. A settlement process allows parties to participate
17 in an open discussion of the different opinions the parties have regarding the disputed issues.
18 Through the open dialogue the parties respectfully debate the issues and discuss past
19 Commission precedent to reach a compromise position. The Commission has concluded on
20 many occasions that compromising and settling disputes, when such is done competently and
21 in good faith, should be favored, especially when the controversy involves complex issues that
22 may take considerable time and expense to litigate.

23 In this case, from my perspective, the individuals who participated in the settlement

1 negotiations for Staff and CURB vigorously presented their positions on the issues that were
2 in dispute in an intelligent and good faith manner. Their positions, as well as the
3 Commission's decision in the KPS Case, were not only considered in the compromise reached
4 by the Parties, but are reflected in the Agreement. Therefore, I am confident in recommending
5 to the Commission that the settlement, if approved, will result in just and reasonable rates and
6 is in the public interest.

7 **III. TERMS OF THE AGREEMENT**

8 **Q. ARE YOU FAMILIAR WITH THE TERMS OF THE AGREEMENT?**

9 A. Yes, I am. I was personally involved in the negotiations that led to the Agreement. The
10 Agreement contains two sections. The first section sets forth the procedural history of the
11 docket and the positions of the Parties on the issues. The last section sets forth the terms of
12 the settlement. The settlement terms contained in the Agreement address the following items:

- 13 (1) Accounting Authority Order ("AAO") (paragraph 8);
- 14 (2) Amortization Period (paragraph 9);
- 15 (3) CAP on AAO (paragraph 10);
- 16 (4) Regulatory Treatment of Insurance Proceeds (paragraph 11);
- 17 (5) Reporting Requirements (paragraph 12); and
- 18 (6) Miscellaneous Provisions (paragraph 13).

19 **Q. WOULD YOU EXPLAIN HOW EACH ONE OF THESE ITEMS WAS SETTLED BY**
20 **THE PARTIES?**

21 A. Yes, I can.

22 ACCOUNTING AUTHORITY ORDER: Under the Agreement, the Parties
23 recommend the Commission issue one AAO that will cover all MGP sites identified in the

1 application, testimony and exhibits filed by Kansas Gas Service and all cash expenditures
2 made by Kansas Gas Service after January 1, 2017, relating to all MGP Costs. MGP Costs
3 are defined as actual and prudent external costs incurred after January 1, 2017, and which are
4 necessary for the investigation and remediation work at MGP sites approved by the Kansas
5 Department of Health and Environment ("KDHE"). MGP Costs would also include regulatory
6 costs (except internal labor costs) incurred related to MGP site oversight by the KDHE, as
7 well as costs (except internal labor costs) incurred in this Commission docket and any
8 compliance docket. Further, MGP Costs would include those actual and prudent costs
9 incurred in the pursuit of insurance recoveries to reimburse Kansas Gas Service for MGP
10 Costs (except internal labor costs). Additionally, MGP Costs would not include costs incurred
11 by Kansas Gas Service relating to a cause of action or third-party claims relating to the MGP
12 sites, including but not limited to claims for third-party damages, claims for injunctive relief,
13 declaratory judgements, claims pertaining to nuisance and/or claims formed under the
14 common law ("Non MGP Costs"). Kansas Gas Service shall be allowed to accumulate in
15 account 182.3 and seek approval to recover in subsequent rate cases, the actual and prudent
16 MGP Costs it incurs beginning on January 1, 2017, at the twelve (12) former MGP sites
17 currently managed by Kansas Gas Service, which are identified in this docket.

18 AMORTIZATION PERIOD: Under the terms of the Agreement, Kansas Gas Service
19 will be allowed to defer and seek recovery of 100% of the MGP Costs. For the first rate case
20 in which Kansas Gas Service seeks recovery of MGP Costs that it has deferred, Kansas Gas
21 Service shall use a 15-year amortization period. Kansas Gas Service shall be allowed to
22 continue to defer and seek recovery of 100% of MGP Costs as defined in this agreement in
23 subsequent rate cases. Each respective set of MGP Costs Kansas Gas Service seeks recovery

1 of shall be considered a separate tranche. Excluding the first tranche, which shall be assigned
2 a 15-year amortization period, Kansas Gas Service shall be allowed to seek an amortization
3 period for each separate tranche of MGP Costs provided the amortization period cannot result
4 in ratepayers paying greater than the net present value of 60% of MGP Costs. Parties, other
5 than Kansas Gas Service, reserve the right to argue a different amortization period should
6 apply as necessary to effectuate any and all degrees of ratepayer/shareholder cost recovery.
7 Kansas Gas Service reserves the right to rebut the positions of other Parties in the event other
8 Parties recommend an amortization period that would result in ratepayers paying less than the
9 net present value of 60% of MGP Costs. Any unamortized MGP Costs shall not be included
10 in rate base in rate cases or accumulate carrying charges outside of a rate case. Once a MGP
11 Cost tranche's amortization period has been approved by the Commission, no Party shall be
12 allowed to recommend the MGP Cost tranche's amortization period should be altered.

13 CAP ON AAO: Under the terms of the Agreement, the expenditures relating to the
14 MGP Costs covered by the AAO shall be limited to \$15 million net of insurance recoveries.
15 If future MGP Costs (net of insurance recoveries) are expected to exceed \$15 million, then
16 Kansas Gas Service will be required to file an application in this docket for approval to
17 increase the \$15 million cap established in the AAO. Staff and CURB reserve their respective
18 rights to challenge a future request by Kansas Gas Service to increase the \$15 million cap and
19 did not waive their unequivocal right to reassert any argument posed in this docket with
20 respect to any such requested future increase above \$15 million. Likewise, Kansas Gas
21 Service reserved its right to reassert any rebuttal argument posed in this docket should Staff
22 or CURB reassert any argument posed in this docket.

23 REGULATORY TREATMENT OF INSURANCE PROCEEDS: Under the terms of

1 the Agreement, one hundred percent (100%) of the proceeds paid by insurance companies to
2 reimburse Kansas Gas Service for MGP Costs (as defined in the Agreement) shall be applied
3 by Kansas Gas Service to reduce the gross MGP Costs. To the extent possible, Kansas Gas
4 Service shall track and match up proceeds received from insurance with the cost paid and the
5 site to which it is related. The Parties understand and agree that other general liability claims
6 could be made against the insurance policies for recovery of Non MGP Costs, but neither the
7 costs related to those claims or any insurance proceeds relating to those claims shall be
8 covered under this AAO and this Agreement.

9 Additionally, at the time the Parties mutually agree that this docket or compliance
10 docket can be closed and there are insurance proceeds remaining in excess of the MGP Costs
11 Kansas Gas Service has asked its customers to pay, then Kansas Gas Service shall be allowed
12 to retain those excess insurance proceeds at the time the Commission closes out the docket.
13 Upon closure of the docket, Kansas Gas Service will not be permitted to seek recovery from
14 Kansas ratepayers any future MGP Costs related to Kansas Gas Service's Kansas MGP sites,
15 regardless of whether or not such MPG Costs are known or unknown, definite or contingent,
16 or arise from MGP sites covered by this Agreement, or otherwise.

17 REPORTING REQUIREMENTS: The Agreement also includes several reporting
18 requirements. Kansas Gas Service shall comply with the following reporting requirements
19 under the AAO:

20 a. Kansas Gas Service shall file an annual report on or before April 1 of each year
21 in a compliance docket that shall include: (1) all reports provided to KDHE during the
22 preceding calendar year; (2) a description of the MGP work conducted in the preceding
23 calendar year along with a summary of the associated MGP Costs incurred; (3) a description

1 of the work scheduled to be conducted in the subsequent calendar year as well as a cost
2 estimate for such work; and (4) the amount of insurance proceeds received, if any, associated
3 with MGP Costs in the preceding year;

4 b. Kansas Gas Service shall also (to the extent possible), include in the annual
5 report: (i) MGP Costs (and invoices reflecting those MGP Costs) broken down by MGP site
6 and (ii) proceeds paid by the insurance company to reimburse KGS for MGP Costs matched
7 up to MGP cost invoices and broken down by MGP site (if possible); and

8 c. In addition to the above mentioned reporting requirements, if Kansas Gas
9 Service becomes aware of additional remediation projects that are reasonably expected to
10 exceed \$1 million, it shall meet with the Staff and CURB to provide them the scope of the
11 work to be performed under the project that has been approved by KDHE. During this
12 meeting, Kansas Gas Service will provide the estimated cost for the work to be performed, an
13 explanation with support of how the work will be performed, an explanation of the
14 reasonableness of the work to be performed, an explanation as to what other options Kansas
15 Gas Service evaluated, and an explanation as to why the option chosen by Kansas Gas Service
16 and approved by the KDHE was selected over the other options.

17 MISCELLANEOUS PROVISIONS: The Agreement includes several procedural
18 miscellaneous provisions:

19 a. The Agreement indicated it fully resolves issues specifically addressed in the
20 Agreement and that the terms contained in the Agreement constitute a fair and reasonable
21 resolution of the issues addressed in the Agreement;

22 b. The Agreement states it resulted from extensive negotiations among the Parties
23 and are interdependent. In the event the Commission does not approve and adopt the terms

1 of the Agreement in total, any Party has the option to terminate the Agreement and, if so
2 terminated, none of the Parties shall be bound, prejudiced, or in any way affected by any of
3 the terms contained in the Agreement, unless otherwise provided herein. If this Agreement
4 is terminated under this provision, then the Parties agree to seek the first available hearing date
5 on the Commission's calendar for an evidentiary hearing on the merits of the issues raised in
6 this docket;

7 c. The Agreement also states that it is the Parties' intent to pre file testimony in
8 support of the Agreement and to present those witnesses in support of the Agreement at a
9 hearing before the Commission. The Parties agreed to move for the admission of all pre filed
10 testimony and exhibits and to waive cross examination of all witnesses. The Parties reserved
11 the right to ask witnesses questions relating to any questions posed by the Commission at the
12 hearing on the Agreement;

13 d. The Agreement provided that unless (and only to the extent) otherwise
14 specified in the Agreement, the Parties shall not be prejudiced, bound, or affected in any way
15 by the terms of the Agreement in: (1) any future Commission or court proceeding; (2) any
16 proceeding currently pending under a separate docket; and/or (3) in this proceeding, if the
17 Commission decides not to approve the Agreement in total or in any way conditions its
18 approval of the same; and

19 e. The Agreement does not prejudice or waive any Party's rights, positions,
20 claims, assertions, or arguments in any proceeding in this docket, or any other proceedings
21 before this Commission or in any court.

22 Finally, if the Commission approves the Agreement in its entirety and incorporates the
23 same into its final order in this docket, the Parties intend to be bound by its terms and the

Commission's order incorporating its terms as to all issues addressed herein, and will not appeal the Commission's order.

IV. COMMISSION STANDARDS FOR REVIEW OF AGREEMENT

Q. ARE YOU FAMILIAR WITH THE FACTORS THE COMMISSION CONSIDERS WHEN REVIEWING A PROPOSED SETTLEMENT AGREEMENT?

A. Yes, I am.

Q. CAN YOU IDENTIFY THOSE FIVE FACTORS?

A. The five factors the Commission considers when reviewing proposed settlement agreements are as follows:

(1) Whether there was an opportunity for the opposing party to be heard on their reasons for opposition to the Agreement;

(2) Whether the Agreement is supported by substantial competent evidence;

(3) Whether the Agreement conforms with applicable law;

(4) Whether the Agreement results in just and reasonable rates; and

(5) Whether the results of the Agreement are in the public interest.

Q. DID ALL PARTIES TO THIS CASE HAVE AN OPPORTUNITY TO BE HEARD WITH RESPECT TO THE TERMS OF THE AGREEMENT?

A. Yes, they did.

Q. IS THE SETTLEMENT AGREEMENT AMONG THE PARTIES IN CONFORMITY WITH THE FACTORS THE COMMISSION CONSIDERS IN REVIEWING SETTLEMENTS?

A. Yes. Although the factors established by the Commission have a legal application, it is my understanding all the Parties agree the established standards have been met. Settlement

1 negotiations were comprehensive and as expected, the Parties had differing positions on
2 certain items. However, the Parties were able to negotiate a compromise that satisfied each
3 party in all respects. This was done, in part, by relying upon the ratemaking/policy treatment
4 and cost-sharing recovery/incentive mechanisms approved by the Commission in the KPS
5 Case and adjusting those based on factors unique to this case raised by Staff and CURB with
6 respect to the Commission's decision in the KPS Case.

7 **Q. IS THE AGREEMENT A REASONABLE COMPROMISE OF THE PARTIES'**
8 **POSITIONS IN THIS CASE?**

9 A. Yes, it is. The provisions of the Agreement were negotiated by the Parties in conjunction with
10 the acknowledgment that it is unlikely the Commission would accept all of any one, of the
11 Parties' prefiled positions. Kansas Gas Service carefully considered the issues before the
12 Commission and used its best judgment and knowledge of Commission precedent in the KPS
13 Case to determine where compromise was warranted and appropriate. Based upon its
14 observations of Staff and CURB during the settlement discussions, Kansas Gas Service
15 believes Staff and CURB used a similar method of evaluating the issues and assessing
16 litigation risk based upon the Commission precedent in the KPS Case and made their
17 decisions in an intelligent and good faith manner. Kansas Gas Service submits there is ample
18 evidence in the record in this docket to demonstrate the provisions of the Agreement will
19 establish just and reasonable rates and are in the public interest.

20 **Q. HOW DO CUSTOMERS BENEFIT FROM THE AGREEMENT?**

21 A. There are many benefits to customers under the Agreement. First, the Agreement establishes
22 a cap on the AAO and requires Kansas Gas Service to seek additional accounting authority
23 if it plans on extending that cap. Second, the proposal would result in an amortized cost to be

1 recovered from customers that is known, measurable and consistent. In the absence of the
2 accounting order and regulatory treatment proposed under the Agreement, there would likely
3 be a question of whether test period costs represented a normalized level of ongoing MGP
4 Costs to be included in Kansas Gas Service's revenue requirement. Because MGP Costs will
5 vary year-to-year, it would be a challenge to determine an appropriate level to include in base
6 rates. The provisions in the Agreement require that the MGP Costs be amortized over a
7 lengthy period, i.e., in the first rate case over a 15-year period, thus establishing a
8 straight-forward, consistent approach to annual cost recovery. As indicated earlier in my
9 testimony, the 15-year amortization period used for the first deferred amount is five years
10 longer than the 10-year amortization period approved by the Commission in the KPS Case.

11 Next, under the terms in the Agreement, our customers will not incur the total
12 economic cost associated with MGP expenditures because the Company is foregoing a request
13 for carrying charges and rate base recognition of the unamortized MGP Costs. This is
14 consistent with the Commission's decision in the KPS Case. Therefore, the Company's
15 shareholders, who thus far have absorbed all the MGP Costs incurred between November 1,
16 1997, and December 31, 2016, would continue to absorb a significant portion of those costs
17 going forward under the terms of the Agreement.

18 Finally, terms in the Agreement would provide for annual monitoring of MGP Costs.
19 Staff, CURB and the Commission will have access to the annual reports and will have an
20 opportunity to review the information provided outside of, and prior to, a rate case proceeding.

21 **Q. HOW WILL THE PROVISIONS IN THE AGREEMENT RESULT IN THE**
22 **ESTABLISHMENT OF JUST AND REASONABLE RATES?**

23 **A.** There are several provisions within the Agreement that assure future changes in rates which

1 account for MGP Costs will be just and reasonable. As in the KPS Case, the amortization
2 period agreed to by the Parties will effectively place the Company and its shareholders at risk
3 for more than 40% of the MGP Costs and will provide Kansas Gas Service not only an
4 incentive to efficiently and effectively manage investigative and remediation work and costs
5 at the MGP sites, but will also provide Kansas Gas Service an incentive to aggressively pursue
6 the recovery of those costs from insurance companies. In addition, the reporting requirements
7 contained in the Agreement will allow Staff, CURB and the Commission to track the work
8 being conducted at the MGP sites, the actual and estimated costs relating to that work, and
9 Kansas Gas Service's efforts to recover those costs from insurance companies. Finally, the
10 Staff, CURB and the Commission will have the opportunity to review and approve the MGP
11 Costs in subsequent rate cases before the MGP Costs are placed in rates for recovery.

12 **Q. HOW WILL THE TERMS IN THE AGREEMENT PROMOTE THE PUBLIC**
13 **INTEREST?**

14 A. In its Order approving the sale of Western Resources, Inc.'s gas utility system to ONE Gas'
15 predecessor in 1997, the Commission specifically identified environmental investigation and
16 remediation of the MGP sites as an important public interest matter and ordered ONE Gas'
17 predecessor to continue the work at the MGP sites under the current order issued by KDHE.
18 Approval of the Agreement provides a balanced approach in the adoption of a
19 regulatory/policy cost-sharing and incentive mechanism to fund the further investigation and
20 remediation of the MGP sites. This will benefit customers and the public interest in Kansas
21 through clean air and water.

22 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

A. Yes, it does.

VERIFICATION

STATE OF OKLAHOMA)
) ss:
COUNTY OF TULSA)

David Scalf, being duly sworn upon his oath, deposes and states that he is Vice President of Rates and Regulatory Affairs for ONE Gas, Inc.; that he has read and is familiar with the foregoing Testimony in Support of Unanimous Settlement Agreement filed herewith; and that the statements made therein are true to the best of his knowledge, information, and belief.

David Scalf
David Scalf

SUBSCRIBED AND SWORN to before me this 12th day of October, 2017.



Commission/Appointment Expires:

October 25, 2021

Joanne C Davis
Notary Public

CERTIFICATE OF SERVICE

I hereby certify that a copy of the above and foregoing Testimony in Support of Unanimous Settlement Agreement of David Scalf was sent via U.S. Mail, postage prepaid, hand-delivery, or electronically, this 12th day of October, 2017, addressed to:

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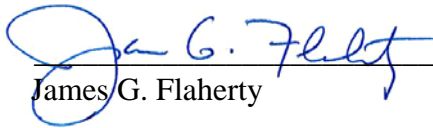
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