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State Corporation Commission
of Kansas

**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 an Extension of its Certificate of Convenience and Authority to Operate as a Natural Gas Public Utility in and Around the Area Heretofore Served by the City of Lebo, Kansas, a Municipally Owner Natural Gas Utility	)	Docket No. 24-KGSG-825-ACQ

CURB'S RESPONSE TO STAFF'S REPORT AND RECOMMENDATION

COMES NOW the Citizens' Utility Ratepayer Board ("CURB") and submits its Response to the *Staff's Report and Recommendation ("*R&R"), filed by Kansas Corporation Commission Staff ("Staff") with the Kansas Corporation Commission ("KCC" or "Commission") in the above-captioned docket on October 21, 2024.

BACKGROUND

1. On June 6, 2024, Kansas Gas Service ("KGS") filed an Application in this docket, requesting, pursuant to K.S.A. 66-131, that the Commission issue an extension of its Certificate of Convenience and Authority to operate as a natural gas public utility in and around the area heretofore served by the City of Lebo, Kansas ("Lebo").[1] This application was filed because KGS has entered into a purchase agreement with Lebo to purchase all of Lebo's properties and facilities used for the distribution of natural gas in Lebo for $1,000,000.00. KGS asserts that the purchase price is justified because Lebo's distribution system has been well maintained. However, desiring to take advantage of the Commission's municipal acquisition process established in Docket No. 08-ATMG-182-ACQ ("08-182 Docket"), KGS decided to limit the amount included in KGS's rate

[1] Application of Kansas Gas Service (June 6, 2024) (hereinafter, "Application").

base to the number of Lebo natural gas utility customers (302) multiplied by KGS's average embedded cost per customer of $3,022, for a total of $912,530. Applicant intends to pay cash for the acquisition.[2]

2. In these regards, CURB acknowledges that the Commission outlined a process for Commission approval of the acquisition of municipal natural gas utility systems by natural gas utilities regulated by the Commission in the 08-182 Docket. The process established in the 08-182 Docket includes provisions for determining a purchase price, voting procedures as required by K.S.A. 15-809, providing notice to affected customers of the proposed sale, and the assumption of supply and transportation contracts as appropriate.[3] The program also sets forth a separate set of regulatory terms and conditions that govern the recording of the transaction, rate-making procedures for any required system improvements, and provisions for the transfer of certificated territory.[4] It is Staff's view that this instant filing by KGS to acquire the gas distribution system facilities of Lebo comports in all material respects with the process established in the 08-182 Docket[5].

CURB'S RESPONSE

3. CURB has reviewed the application filed in this docket and has issued data requests ("DRs") to KGS. CURB is very appreciative of the efforts by KGS to respond to CURB's DRs. CURB also had an opportunity to discuss this application with Staff and appreciates the candid discussion as well as Staff's analysis. However, while CURB agrees with Staff that the application should be granted, CURB's analysis differs.

[2] Id.
[3] Docket No. 08-ATMG-182-ACQ, Order Approving Application (December 18, 2007) (hereinafter, "08-182 Docket, Order Approving Application").
[4] Id.
[5] Notice of Filing Staffs Report and Recommendation, p. 5., (October 21, 2024).

4. At the outset, CURB agrees with KGS and Staff that the process set forth in the 08-182 Docket governs this application. That process is described in paragraphs 11 and 12 of the Order Approving Application, as follows:

(11) The process [requested that] the Commission approve is as follows:

i. The gas utility and the Municipality agree on a purchase price and any necessary surcharge to make improvements to the system.
ii. The gas utility and the Municipality organize an election as required by K.S.A. 15-809, as well as any local ordinances.
iii. The gas utility will file the application for acquisition with the Commission.
iv. The gas utility will mail notice to each customer and allow 30 days for customers to submit comments to the KCC. This notice will contain a comparison of the municipality's rates and the gas utility' rates, and will include any applicable surcharge.
v. The gas utility will assume upstream transportation capacity contracts that will be consolidated with the gas utility existing contracts at the first available opportunity.
vi. The gas utility will assume any existing supply contracts that will be consolidated with the gas utility existing contracts at the first available opportunity.
vii. The Commission would authorize the gas utility to charge the current gas utility rates and other applicable charges listed in the current tariffs.

(12) Additionally, the terms of the acquisition would be as follows:

a) The gas utility will be allowed for accounting and ratemaking purposes to record the purchase price of the system assets as the gas utility's current distribution system average per customer embedded cost for meters, services, and mains on an original cost basis.
b) The actual price paid will not exceed the average embedded cost.
c) The gas utility shall make improvements to the system as may be necessary at its own expense until the purchase price and amount invested in improvements equals the current distribution system average cost per customer embedded cost.
d) Any improvements to the system that require investing more than the average embedded cost per customer for the gas utility will be recovered through a surcharge on the municipality customers that is agreed by the municipality prior to the system purchase by the gas utility.
e) The amount recovered under a surcharge will be recorded as customer-provided capital for ratemaking purposes.
f) Except for compliance with the terms of this docket, no separate accounting will be required from the gas utility when it files to extend its certificate for a municipal acquisition.
g) Application for extension of certificate will include a schedule showing the estimated costs of any necessary improvements, the calculation of any applicable surcharges, and the expected term of the surcharge.
h) The use of the gas utility standard asset purchase shall have a presumption of reasonableness.

i) Application for extension of certificate will include a schedule showing the comparison of the gas utility' rates and the municipality's rates.
j) Application for extension of certificate will include certified results from the election.
k) The gas utility will be required to file an executed copy of its asset purchase agreement as part of its application.
l) Any differences from the standard asset purchase agreement attached to the application as an exhibit will be identified and explained in the filing for an extension to the gas utility's certificate of convenience and authority. (Emphasis added.)[6]

5. With reference to this process, it is important to note that the purchase price paid by KGS for the Lebo utility system exceeds the distribution system average embedded cost per customer for meters, services, and mains on an original cost basis. As a result, KGS states that it seeks to recover only the embedded cost per customer ($3,022) multiplied by number of Lebo utility customers that KGS intends to serve (302) for a total of $912,530.[7] Thus, consistent with the process established in the 08-182 Docket, KGS concedes that the part of the purchase price of $1,000,000 that exceeds $912,530 will not be recovered by KGS in utility rates.[8]

6. However, in regard to the system improvements that require investing more than the average embedded cost per customer for KGS, CURB submitted discovery to KGS requesting a list of repairs, replacements and improvements that KGS expects to make to the acquired distribution assets during the first three years following the acquisition. KGS stated in its discovery response that it intends to make the following improvement to the Lebo system during the first year following the acquisition and to recover the costs of the same as follows:

> Upgrade the meters with Automated Meter Reading, which will cost approximately $316 per meter. KGS plans to charge this upgrade to a blanket capital project and include it in its next general rate case.

[6] 08-182 Docket, Order Approving Application, pp. 3-5.
[7] Application, p. 2.
[8] Id., p. 4.

> Upgrade the odorizer and regulation at the town border station. KGS predicts that this upgrade will cost between $100,000 to $125,000 and will be recovered via the Gas System Reliability Surcharge (GSRS).[9]

7. The plain reading of the pertinent regulatory terms and conditions established in the Order Approving Application in the 08-182 Docket requires that KGS makes any necessary improvements to the acquired system at its own expense until the total sum of the purchase price of the system and the investments in the improvements exceeds the current distribution system average embedded cost per customer.[10] Yet, in this docket, KGS has already met that ceiling. Thus, the terms set forth in that order provide that, in the event that the system improvements require investments that exceed the average embedded cost per customer, a surcharge must be established to enable KGS to recover the cost of these investments from the newly acquired customers.[11] Yet, KGS states that no such surcharge will be collected from Lebo customers.[12] Rather, KGS intends to socialize improvements to the Lebo border station through the GSRS. However, there is no exception stated in that order that plainly allows any improvements to the acquired municipal natural gas utility to be socialized among KGS's core customers.

8. In CURB's view, the upgrade of the odorizer and regulation at the Lebo border station is an improvement to the Lebo utility system contemplated by the process set forth in the 08-182 Docket. It is a system improvement. Improvements to the Lebo border station clearly benefit the residents of Lebo solely. It appears to CURB that a border station is integral to the Lebo utility system. CURB has trouble perceiving that improvements to an integral part of a municipal

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[9] While KGS plans to upgrade the odorizer and regulation equipment and flow these upgrades into the GSRS surcharge, the City of Lebo's customers will be charged for other GSRS investments that occur on other infrastructure investments in the KGS system.
[10] 08-182 Docket, Order Approving Application, p. 3.
[11] Id.
[12] Application, p. 3.

natural gas utility system is not contemplated as an improvement subject to the cap set forth in the Order Approving Application in the 08-182 Docket.

9. Indeed, CURB believes that the intent of the process outlined in the 08-182 Docket is to place a limit on the total amount of costs that utility customers will bear in the acquisition of a municipal utility. Here, adding the costs of KGS's upgrade of the odorizer and regulation at the Lebo border station requires KGS core customers to bear total costs beyond the average embedded cost per customer. Essentially, it eliminates the cap on the cost of acquiring a municipal natural gas utility system that will be borne by core customers.

10. KGS may argue that, consistent with its line extension policy found in GT8 tariff, socializing the cost of KGS's upgrade of the odorizer and regulation at the Lebo border station should be allowed. Accordingly, CURB believes that KGS may point to the following provision:

> Ordinary Extensions: A project that is reasonably expected to provide the Company with 10 year revenues equal to or greater than the estimated cost of construction shall be considered an Ordinary Extension for the purpose of determining required contribution amounts and/or whether there is a potential for refunds. (a) Company will make ordinary extensions of its distribution mains as and when necessary to serve prospective customers and located within the corporate limits of a city or suburban area adjacent thereto, or within unincorporated communities. (b) The Ordinary Extension Allowance shall be the length of the extension but no greater than 100 feet per customer served. (c) The Ordinary Extension Value shall be the Ordinary Extension Allowance times the per foot cost of the distribution main project, not including extraordinary costs due to unusual construction conditions or barriers or of special equipment or facilities.[13]

Yet, line extension policies are not mentioned or inferred as an exception in the conditions set forth in the 08-182 Docket. Nor is there language in the conditions set forth in the 08-182 Docket allowing ordinary costs of system improvements to be an exception to the surcharge requirement. There is no language in the surcharge requirement in the 08-182 Docket that provides for an exception if the acquiring utility has a tariff that allows certain utility costs to be socialized among

[13] KGS Tariff Schedule GTC8, Section 8.01.03(2), (January 1, 2017).

all ratepayers. Clearly, these exceptions could have been specifically set out in the process, or the Commission could have provided some leeway, such as stating that "unless otherwise determined by the Commission" or similar language.

11. Rather, the plain language used in the process established by the Commission in the 08-182 Docket is straightforward. To reiterate, it states:

> "***<u>Any</u>*** improvements to the system that require investing more than the average embedded cost per customer for the gas utility will be recovered through a surcharge on the municipal customers. (Emphasis Added)[14]

CURB has trouble getting past that plain language. Moreover, the effect of the process outlined in the 08-182 Docket already provides an allowance for system improvements to a municipal natural gas utility to be acquired pursuant to that docket. That allowance is the full amount of the pertinent utility's "current distribution system average costs per customer imbedded costs for meters, service and mains on an original cost basis" which remain after deducting the amount of those imbedded costs that are allocated to the purchase price[15] Essentially, KGS proposes to increase that allowance.

12. Indeed, CURB is concerned with KGS's interpretation of the terms required under the Order Approving Application in the 08-182 Docket. First, there is absolutely no mention in those terms of measuring 10 years of revenue versus 10 years of expenses relative to whether municipal customers should bear the cost of system improvements to their own system. Rather, the terms set a cap for the purchase price combined with any system improvements at the average embedded cost per customer, regardless of whether the cap results in a revenue gain or loss. Secondly, most Kansas gas utilities have a line extension policy similar to GT8. To allow KGS to socialize the cost of KGS's upgrade of the odorizer and regulation at the Lebo border station by

[14] 08-182 Docket, Order Approving Application, p. 4.
[15] Id.

analogy to a line extension policy will alter the clear limitation of the amount of the purchase price and improvements that will be borne by KGS's core customers. In addition, line extensions are limited in the services provided and pertain to individual customers on a case-by-case basis. KGS's upgrade of the odorizer and regulation at the Lebo border station is a large system improvement. In short, CURB sees that this interpretation effectively results in a new standard than clearly established in the 08-182 Docket.

13. Furthermore, the terms established in the 08-182 Docket require:

> Any improvements to the system that require investing more than the average embedded cost per customer for the gas utility will be recovered through a surcharge on the municipality customers that is agreed by the municipality prior to the system purchase by the gas utility.[16]

In this docket, KGS does not appear to comply with this provision as the surcharge is not addressed in the Asset Purchase Agreement ("APA") between Lebo and KGS, and the APA recites that it constitutes the whole agreement between the parties. Moreover, it does not appear that KGS provided notice to Lebo customers that by voting for approval of the acquisition of the Lebo utility system by KGS could result in a surcharge for needed system improvements.

14. KGS could have deducted the costs of improvements from the acquisition price. CURB is reasonably assured that KGS performed a due diligence analysis of the Lebo utility system it intended to purchase. Being aware of the plain provisions established in the Order Approving Application in the 08-182 Docket, KGS would have been aware that these charges could be determined to be justly collected through a surcharge on the Lebo customers to whom the improvements directly benefit. Yet, KGS chose to discount that possibility in its contract with Lebo and in its application.

[16] Id.

15. CURB recognizes that the Commission is free to interpret its own orders or to revise its orders when necessary to meet the public interests, and CURB is respectful of that prerogative and the Commission's decision. In these regards, CURB has researched several dockets that have followed the process set forth in the 08-182 Docket, CURB could not locate any dockets that allow system improvements to municipal utility systems that exceed the cap established in the 08-182 Docket to be borne by a utility's core customers. In fact, CURB cannot find a docket where revenues and expenses for any period of time is discussed as pertinent to the acquisition of a municipal natural gas utility, If there is such precedent, CURB genuinely would appreciate being enlightened and would certainly acknowledge the same. CURB notes that there is no citation to any such precedent in the Application or Staff's R&R. Such a precedent would greatly affect CURB's analysis of the issue in this docket, although, as stated below, CURB has no objection to granting KGS's application for other reasons.

16. CURB also wants to indicate its respect for the analysis that Staff has performed in this docket. Staff's position is as follows:

> Staff initially questioned KGS's decision to recover the upgrade costs through separate cost-recovery mechanisms (e.g., blanket capital project, GSRS) rather than an additional surcharge on the acquired customers. In order to ascertain the necessity of a surcharge, Staff relied on the conditions established in KGS's line extension policy found in Schedule GTC8 of the Company's tariff. This policy, as approved by the Commission, allows KGS to designate a project as economic or "ordinary" on the condition that ten years of projected revenue generated by the project would be sufficient to cover the estimated costs of the investment. Staff submitted discovery to KGS requesting a forecast of the expected revenue contribution from the acquired customers over the next ten years. KGS estimated that it will generate $1,396,319 of revenue over the next decade from these customers. Staff compared KGS's estimated ten-year revenues with its forecasted expenditures according to information that is currently quantifiable.[17]

CURB understands the appeal of this "do no harm" criterion for approving acquisitions of municipal natural gas utilities. While Staff's position may be commendable from a practical

[17] Notice of Filing Staff's Report and Recommendation, p. 4. (October 21, 2024)

standpoint, given the advantages of potential economies of scale that derive from acquisitions, CURB feels constrained to point out the plain language involved in the process established in the 08-182 Docket. Further, as noted earlier, while CURB respects the Commission's ability to interpret its own orders as well as the Commission's authority to revise its orders, CURB believes there is also a benefit to consistently maintaining the plain language limitations set forth in the 08-182 Docket that utilities have complied with for over 15 years.

17. CURB does have some additional concerns with this proposal. What if the estimated revenue contribution generated by the City of Lebo is not as high as these estimates suggest? How will this be addressed, if at all, after 10 years? Will KGS socialize these costs and will all customers system-wide be responsible for these costs? Would Lebo be solely responsible? Will KGS and its shareholders be responsible? If the amount placed into the Lebo system should change over the course of 10 years, it would not take much over a 10-year period of time for adjustments to occur which would cause the $263,357 overage to disappear. It is CURB's opinion that should this occur, KGS and its shareholders should be responsible for any revenue shortfall and should have to absorb these costs and not have them socialized among ratepayers. Since no surcharge to Lebo customers has been agreed to in this purchase as CURB believes it should have been under paragraph 12 iv of the Order Approving Application in the 08-182 Docket, it seems only fair to all parties, at the very least, that KGS would be responsible for these costs should they occur.

18. Those concerns aside, CURB does believe that Lebo customers will benefit from the acquisition by KGS. These municipal customers will benefit from KGS gas supplies and expertise. Therefore, it does not appear to CURB to be in the public interest to deny this application away at this point in time despite the issues with system improvements. Certainly, one cannot place

blame on Lebo residents on the manner in which this docket proceeded. CURB will represent the residents and small businesses of Lebo just the same as it represents KGS's residential and small business core customers. CURB recognizes that a surcharge equating to the costs of KGS's upgrade of the odorizer and regulation at the Lebo border station on a mere 300 Lebo customers could have a substantial rate impact on some Lebo citizens.

19. While CURB believes that it is reasonable for KGS to absorb the costs of improvements made to the Lebo border station as good will, it does not believe that this will occur; and it may be contrary to the public interest to thwart the decision of the majority of Lebo citizens to be acquired by KGS, under the exigencies here present. Indeed, in order to obtain gas supplies to serve Lebo residents, time is of the essence ahead of the winter season. Winters have been severe in Kansas at times during the past few years. Adequate preparation is imperative. Due to these time limitations, it may do significant harm to the citizens of Lebo to deny the application at this late date.

20. In short, while CURB does have some disagreement with KGS regarding the interpretation of certain regulatory provisions governing the application, CURB does see some advantages for Lebo stemming from KGS's acquisition of its municipal natural gas utility. KGS is a reliable gas provider and good steward of its system. Therefore, CURB does not object to granting the application, but hopes that the Commission will limit the exception to the particular exigencies and facts of this case, preserving the cap on the amount of the improvements to municipal natural gas utility systems that will be absorbed by a utility's core customers in all future municipal natural gas utility acquisition cases.

WHEREFORE, CURB does not object to the application.

Respectfully submitted,

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VERIFICATION

STATE OF KANSAS)
) ss:
COUNTY OF SHAWNEE)

I, Todd E. Love, of lawful age and being first duly sworn upon my oath, state that I am an attorney for the Citizens' Utility Ratepayer Board; that I have read and am familiar with the above and foregoing document and attest that the statements therein are true and correct to the best of my knowledge, information, and belief.

Todd E. Love

SUBSCRIBED AND SWORN to before me this 29th day of October, 2024.

DELLA J. SMITH
Notary Public - State of Kansas
My Appt. Expires January 26, 2025

Notary Public

My Commission expires: 01-26-2025.

CERTIFICATE OF SERVICE

24-KGSG-825-ACQ

I, the undersigned, hereby certify that a true and correct copy of the above and foregoing document was served by electronic service on this 29th day of October, 2024, to the following:

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