In the Matter of the Application	)	
of Kansas Gas Service, A	)	
Division of ONE Gas, Inc. for	)	DOCKET NO. 16-KGSG-___-RTS
Adjustment of its Natural Gas	)	
Rates in the State of Kansas	)	

DIRECT TESTIMONY

OF

DAVID N. DITTEMORE

ON BEHALF OF

KANSAS GAS SERVICE

A DIVISION OF ONE GAS, INC

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DIRECT TESTIMONY

OF

DAVID N. DITTEMORE

KANSAS GAS SERVICE

DOCKET NO. 16-KGSG-___-RTS

I. INTRODUCTION

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is David N. Dittemore. My business address is 7421 West 129th Street, Overland Park, Kansas, 66213.

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

A. I am employed by Kansas Gas Service a Division of ONE Gas Inc. ("ONE Gas") (KGS or Company). I am the Director of Rates and Regulatory Affairs.

Q. PLEASE STATE YOUR EDUCATIONAL BACKGROUND AND BUSINESS EXPERIENCE.

A. I received a Bachelor of Science Degree in Business Administration with a major in Accounting from the University of Central Missouri. I am a Certified Public Accountant. I was previously employed by the Kansas Corporation Commission ("Commission" or "KCC") in various capacities including Managing Auditor, Chief Auditor and Director of Utilities. During my career I have been employed by WorldCom (telecommunications) and the Williams Companies (Williams Energy Marketing and Trading). From 2003 – 2007, I was self-employed providing regulatory consulting services on behalf of clients dealing with telecommunications, electric and natural gas regulatory issues. Since 2007, I have been employed by ONEOK/ONE Gas as a member of the Kansas Gas Service Regulatory Department.

Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THIS COMMISSION?

A. Yes. I have testified before the Commission on a number of occasions.

Q. COULD YOU PLEASE EXPLAIN THE SCOPE OF YOUR TESTIMONY?

A. Yes. The scope of my testimony includes:

1. I identify the amount of the proposed increase and the impact it will have on the average customer. My testimony includes a listing for each pro forma adjustment to Rate Base and Income Statement. (Section II);
2. I provide context for this rate increase proposal by presenting average residential bill information for the past ten years. I also provide an overview of the cost elements contained within the average customers' bill in 2015. (Section III);
3. I identify the requirements contained within the Commission's order in Docket No. 14- KGSG-100-MIS ("100 Docket") associated with the current rate case application. (Section IV);
4. I sponsor the majority of Schedules within the Minimum Filing Requirements (MFRs) pursuant to Kansas Administrative Regulations 82-1-231. (Section V);
5. I explain the pro forma adjustments to test period rate base, operating income and income tax expense that I am supporting. (Section VI); and,
6. I support the implementation of an annual Cost of Service Adjustment Mechanism. (Section VII).

Q. PLEASE PROVIDE AN EXECUTIVE SUMMARY OF YOUR TESTIMONY

A. The Company is seeking an overall base rate increase of $35.4 Million, and a net rate increase of $28 Million, with rates to be effective January 1, 2017. The most recent base rate increase approved for KGS became effective January 1, 2013. The proposed rate change will result in an increase to the average residential customer of $4.34 per month, net of the current Gas System Reliability Surcharge (GSRS) in effect of $0.76 per month. The GSRS will be reset to zero when the new base rates become effective, and the underlying costs supporting the surcharge are incorporated in this filing. Over the past four years KGS has experienced growth in its rate base and incurred increasing levels of Operating and Maintenance costs which have not been reflected in base rates. In addition, residential consumption has continued to decline, further reducing revenues.

The average KGS residential customer has seen significant cost reductions in their bill over the past three years as a result of the decline in the market cost of gas supplies. I compare the impact on the average customer bill of the proposed increase (assuming normal weather) with historic levels and conclude that the impact of the proposed increase should not pose a significant burden on the residential customer class.

I provide the context for the Company's rate change proposal by outlining the components of the average customer bill and conclude that 46% of the bill is comprised of KGS imposed costs (including ad valorem and income tax expense), while 48% relates to the cost of gas, including upstream transportation charges, and 6% relates to franchise fees, city and county taxes. The proposed increase confronting the Commission relates to the 46% of the average customer bill comprising those costs incurred by KGS to provide service.

My testimony includes a recommendation for a new annual mechanism, referred to as the Cost of Service Adjustment mechanism (COSA), which provides benefits for all stakeholders, and is necessary to provide KGS a reasonable opportunity to earn its authorized rate of return.

II. EXPLANATION OF PROPOSED INCREASE AND RESIDENTIAL CUSTOMER IMPACT AND IDENTIFICATION OF WITNESSES AND THEIR ADJUSTMENTS.

Q. WHAT IS THE AMOUNT OF THE REQUESTED INCREASE AND THE PROPOSED IMPACT ON RESIDENTIAL CUSTOMERS?

A. Kansas Gas Service is seeking an overall increase in base rates of $35.4 Million, resulting in a net increase in rates of $28 Million, net of $7.4 Million in GSRS revenues that are reclassified to base rates. A class cost of service study was conducted by Mr. Paul Raab, which indicates that the Residential class has the lowest realized return on common equity and therefore the proposed increase is assigned to this class. The proposed residential rate increase represents an increase in rates of 14.9%, net of the rebasing of the Gas System Reliability Surcharge (GSRS). The overall proposed residential increase on total customer bills, inclusive of the cost of gas is 7.2%, based upon the weighted average cost of gas during the test period. The impact on the average residential customer is an increase of $4.34 per month, or $52.08 per year. At the date new rates become effective the current residential GSRS rate of $.76, as well as the applicable GSRS rates charged to other customer classes will be reset to zero.

Q. COULD YOU PLEASE IDENTIFY THE TEST PERIOD PRO FORMA ADJUSTMENTS AND THE WITNESS WHO IS SPONSORING EACH ADJUSTMENT?

A. Yes. The list below contained in Table DND-1 identifies the pro forma adjustments and sponsoring witness.

TABLE DND-1

Adj. No.	Descriptions	Increase (Decrease) to Rate Base	Witness
PLT 1	CWIP	$ 13,048,927	Eaton
PLT 2	Asset Retirements	(2,281,551)	Eaton
PLT 3	Allocation of Corporate Assets	61,525,376	Turner
PLT 4	Plant Assets Not Used and Useful	(4,453,249)	Eaton

PLT 5	CNG Facility	$ (599,134)	Eaton
PLT 6	3rd Party Reimbursements	1,217,964	Eaton
ADA 1	Acc. Depreciation - Asset Retirements	2,281,551	Eaton
ADA 2	Acc. Depreciation - Corporate Assets	(16,693,239)	Turner
ADA 3	Acc. Depreciation - Plant Assets Not Used and Useful	3,164,425	Eaton
ADA 4	Acc. Depreciation - CNG Facility	58,444	Eaton
ADA 5	3rd Party Reimbursements	(1,217,964)	Eaton
WC 1	Pre-Payments - Corporate Assets	3,759,835	Turner
WC 2	Long Term Pre-Payments - Corporate Assets	618,099	Turner
WC 3	ADIT - Associated with Pension/OPEB	51,778,325	Dittemore
WC 4	ADIT - Reflect Test Year End Balance	(25,612,745)	Dittemore
WC 5	ADIT - Associated with COGR	5,274,550	Dittemore
WC 6	ADIT - Corporate	(7,916,831)	Dittemore

Adj. No.	Descriptions	Increase (Decrease) to Operating Income	Witness
IS 1	Eliminate Accrued and Unbilled Revenues	$ (238,752)	Eaton
IS 2	Eliminate Deferred WNA Revenues	(7,892,181)	Eaton
IS 3	Eliminate Cost of Gas Revenue and Expense	0	Eaton
IS 4	Eliminate Ad Valorem Surcharge Revenue and Expenses	1,401,626	Eaton
IS 5	Eliminate Gas System Reliability Surcharge Revenue	(5,171,257)	Eaton
IS 6	Test-year Revenue Adjustments (Flex)	(93,127)	Eaton
IS 7	Weather Normalization	10,146,344	Raab
IS 8	Revenue Annualization	501,372	Raab
IS 9	CNG Adjustment	(12,667)	Eaton
IS 10	Bad Debt Adjustment	(1,280,165)	Eaton
IS 11	Annualized Depreciation on Pro Forma Plant	(828,709)	Eaton
IS 12	Annualized Depreciation at Proposed Rates	(3,657,749)	Eaton
IS 13	Elimination of Royalty Fee	8,607,018	Eaton
IS 14	Transaction Credit	3,423,957	Eaton

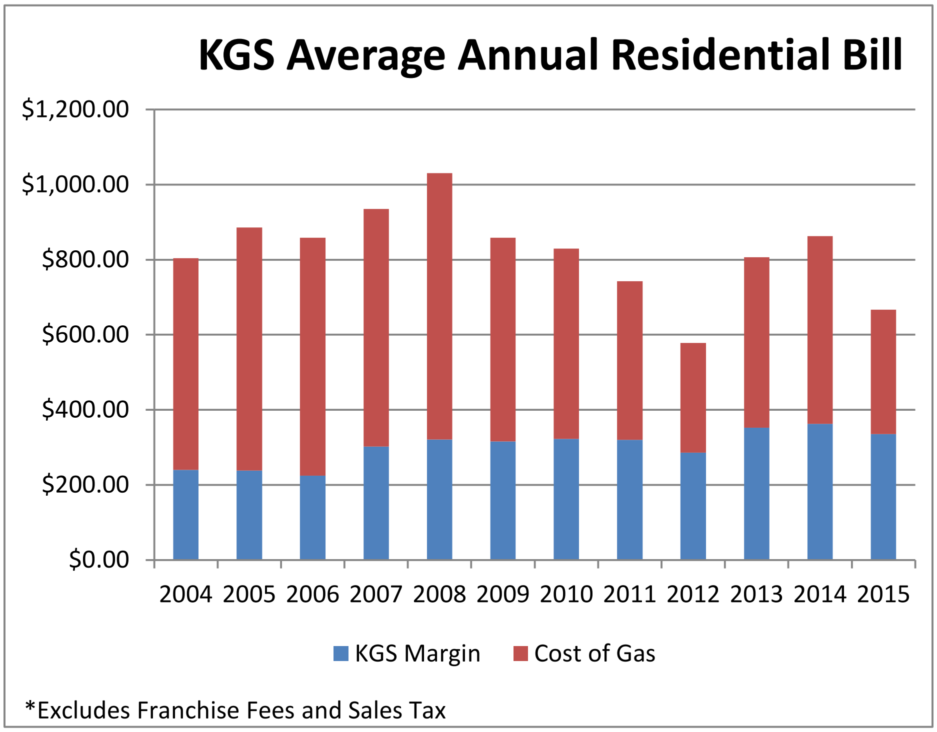
IS 15	Charitable Contributions and Excluded Costs	$ (13,314)	Eaton
IS 16	Shared Service Adjustment	(87,002)	Eaton
IS 17	Remove Certain O&M Expenses Related to unused Plant	45,989	Eaton
IS 18	Clearing Account Adjustment	(20,760)	Eaton
IS 19	Reclass Interest on Customer Deposits	(102,624)	Eaton
IS 20	GTI Expense	(314,868)	Eaton
IS 21	Insurance Adjustment	97,844	Eaton
IS 22	Workers Compensation	(250,531)	Eaton
IS 23	Payroll Adjustment for Union and Non Union KGS Employees	(2,364,771)	Eaton
IS 24	Adjustment to Employee Medical Reserve	(658,707)	Eaton
IS 25	Pension/OPEB Cost Adjustments	2,863,179	Eaton
IS 26	Pension/OPEB Amortization	3,168,966	Eaton
IS 27	Pension/OPEB Savings Sharing	(3,375,022)	Smith
IS 28	Annualized Corporate Depreciation	(412,670)	Turner
IS 29	Misc. Corporate Adjustments	267,310	Turner
IS 30	Distrigas % Adjustment	336,434	Turner
IS 31	Normalized Compensation (STI)	2,217,199	Turner
IS 32	Corporate Payroll Adjustment	(1,198,841)	Turner
IS 33	Corporate OPEB, Pension and Medical Benefits	15,054	Turner
IS 34	Rate Case Cost Amortization	(326,216)	Dittemore
IS 35	Income Tax Adjustment	(3,767,139)	Dittemore

III. RESIDENTIAL BILL HISTORY AND COMPONENTS

Q. PLEASE PROVIDE SOME BACKGROUND ON THE HISTORY OF THE AVERAGE RESIDENTIAL BILL OF A KGS CUSTOMER.

A. Table DND-2 sets forth the annual cost of the average residential customer bill for the period 2007 – 2015, based upon actual usage, as well as the average annual cost of gas. The annual cost of gas is simply the total costs KGS incurred for its purchase of natural gas to serve customers' demands, plus the costs of upstream storage and transportation from third-party pipeline companies.

Table DND-2



The annual total customer bill data shown in Table DND-2 is not adjusted for variations due to weather. However, when comparing the average annual bill with total annual cost of gas charges, it is clear that customers are enjoying a significant reduction in their bills associated with the decrease in the market cost of gas.

In 2015, the average residential customer bill declined $196 from 2014 levels. This reduction can be assigned to one of three categories:

a. Reduction in KGS volumetric charges associated with reduced usage - $35.

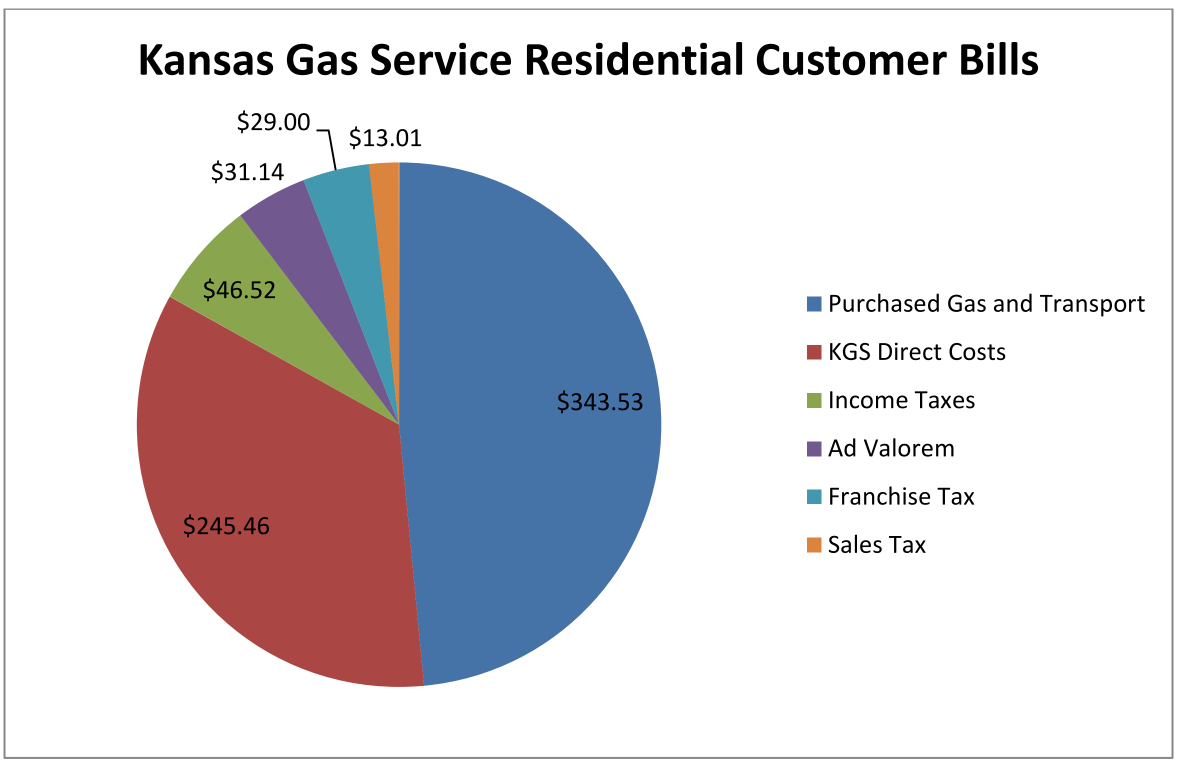
b. Reduction in COGR costs associated with reduced prices - $85.

c. Reduction in COGR costs associated with reduced usage - $76.

Q. PLEASE DISCUSS THE MAJOR COMPONENTS OF A RESIDENTIAL CUSTOMER'S BILL?

A. Table DND-3 splits out the primary components of the average 2015 residential customer's costs over the course of twelve months. In 2015, the average KGS residential customer incurred total costs of $708.66. Based upon the average actual usage of 68 MCF, approximately $344 or 48% of customer costs are associated with the cost of natural gas and related storage and transportation charges from third-party interstate pipeline companies. The base rates approved by the Commission are designed to recover not only KGS direct costs ($245.46), but also state and federal incomes taxes ($46.52) and ad valorem taxes ($31.14) that KGS incurs in providing service. The sum of these three totals $323.12, and represents 52% of the customer's bill.

Table DND-3



The issue in this proceeding is a proposed base rate increase that corresponds to the KGS direct costs, including a return on and a return of capital investments, as well as recovery of income and ad valorem taxes.

The average total of income taxes, ad valorem taxes, franchise fees and sales taxes levied on customers' bills in 2015 was $119.67. This total does not represent other taxes incurred in the provision of gas service, including payroll taxes as well as various taxes incurred by natural gas suppliers and interstate pipeline companies, which are incorporated into their pricing. The point of this information is to provide the Commission with some context for the proposed rate increase and its impact on total customer bills.

IV. COMPLIANCE WITH PROVISIONS OF THE STIPULATION AND AGREEMENT IN THE 100 DOCKET

Q. PLEASE ADDRESS THE CONDITIONS WITHIN THE STIPULATION AND AGREEMENT IN THE 100 DOCKET WHICH IMPACT THE CURRENT RATE CASE APPLICATION.

A. In the 100 Docket, the Commission approved the creation of ONE Gas from its former parent ONEOK. The transaction became effective in January, 2014. The relevant conditions identified in the Stipulation and Agreement in the 100 Docket, subsequently approved by the Commission, which impact the present application are as follows:

1. KGS is precluded from implementing base rate changes prior to January 1, 2017. KGS has adhered to this requirement and the proposed rates resulting from this application are requested to be effective as of January 1, 2017.

2. Elimination of regulatory asset associated with costs incurred in Docket No. 97-KGSG-486-MER.

As required in the Stipulation, these costs have been removed from the books of ONE Gas and are not included in this request.

3. KGS shall provide one-time rebates of $3,423,000 each April in the years, 2013 – 2015. The rebate shall take the form of a bill credit of $5.34.

Each of these required refunds have been made. Because these refunds are non-recurring, they have been eliminated from test year operations in Adjustment IS-14 as sponsored by KGS witness Ms. Lorna Eaton.

4. In conjunction with the refunds described above, KGS Pension Tracker 1 balances were reduced by $3,000,000.

The pension/OPEB costs deferred pursuant to Pension Tracker 1 are contained in Adjustment IS-26, sponsored by KGS witness Ms. Lorna Eaton.

5. The capital structure proposed in the next base rate case of ONE Gas shall be ONE Gas's actual capital structure; however, the equity component is not to exceed 55%.

KGS has adhered to this requirement by adjusting the actual capital structure in this filing to reflect a fifty-five percent equity component of ONE Gas's capital structure. This adjustment is shown in Section 7 of the minimum filing requirements.

Q. WHAT IS THE REVENUE REQUIREMENT IMPLICATION OF MODIFYING THE CAPITAL STRUCTURE TO REFLECT A 55% EQUITY RATIO?

A. This adjustment from the actual equity ratio of ONE Gas to 55 percent equates to a $6.3 million reduction in the revenue requirement. In other words, had the request been calculated on the actual equity level of ONE Gas, with everything else remaining unchanged, the overall request would be $6.3 million higher.

Q. SINCE THE REQUESTED 10.0% RETURN ON EQUITY IS PREMISED UPON THE EQUITY RATIO LIMITATION SET IN THE 100 DOCKET, WHAT WOULD BE THE EQUIVALENT ROE BASED UPON THE ACTUAL EQUITY LEVEL OF ONE GAS?

A. The equity ratio of ONE Gas is actually 60.5%. To put the impact of the reduction in the equity ratio from actual to 55% in perspective, note that a 10% ROE with a 55% equity ratio is equivalent to a 9.3% ROE with a 60.5% equity ratio.

V. COMPLIANCE WITH SCHEDULES REQUIRED BY K.A.R. 82-1-231.

Q. WHAT IS THE TEST YEAR FOR THIS FILING?

A. The test year is the twelve-month period ending December 31, 2015. Adjustments have been proposed for known and measurable changes to test year and to normalize operating results.

Q. HOW DOES KGS MAINTAIN ITS BOOKS AND RECORDS?

A. The Company maintains its books and records in accordance with the Federal Energy Regulatory Commission's (FERC) Uniform System of Accounts ("USOA") and Generally Accepted Accounting Principles (GAAP).

Q. WHICH SCHEDULES REQUIRED BY K.A.R. 82-1-231 ARE YOU SPONSORING IN THIS CASE?

A. I am sponsoring all of the schedules other than the schedules contained in Section 7, Schedules 12A and 12B in Section 12, and the Schedules in Section 18. The schedules included in Section 7 are sponsored by witness Mr. Mark Smith. Schedules 12 A and B, are sponsored by witness Ms. Crystal Turner and the schedules in Section 18 are sponsored by Mr. Justin Clements.

I am sponsoring schedules in the following sections of the MFRs:

Section 3	Summary of Pro Forma Rate Base, Revenues and Expenses supporting the Revenue Increase Requested
Section 4	Functional Classification of Plant in Service
Section 5	Functional Classification of Accumulated Depreciation and Amortization

Section 6	Working Capital Components
Section 8	Comparative Balance Sheets, Income Statements and Payroll Data
Section 9	Pro Forma Income Statement
Section 10	Pro Forma Depreciation and Amortization Expense
Section 11	Pro Forma Taxes
Section 12C	Labor Capitalization Ratio
Section 13	Annual Report
Section 14	Additional Information
Section 15	Additional Information
Section 16	Financial Statements
Section 17	Summary of Revenue by General Customer Classification

Q. PLEASE PROVIDE AN EXPLANATION OF SECTION 3 AND THE ACCOMPANYING SCHEDULES.

A. Section 3, Schedule 3-A, provides a summary of Pro Forma Rate Base, Pro Forma Revenues less Pro Forma Expenses to derive Operating Income at present rates. The Operating Income at present rates is divided by the rate base to calculate the rate of return earned under current rates.

Q. WHAT IS KGS'S CALCULATED RATE OF RETURN?

A. KGS's calculated rate of return under current rates is 4.9%.

Q. PLEASE EXPLAIN HOW THE REQUESTED REVENUE INCREASE WAS DETERMINED.

A. The required rate of return is applied to Pro Forma Rate Base to determine the additional Operating Income required. Because the additional Operating Income is after income taxes, this amount must be "grossed-up" to determine the revenue shortfall. Pro Forma Rate Base on line 5 is $902,967,733; Pro Forma Revenues on line 6 is

$287,931,412; less Pro Forma Total Expenses on Line 7 of $243,624,679 results in Pro Forma Operating Income at present rates of $44,306,733, as shown on line 8. As indicated, the Pro Forma Operating Income at present rates divided by Pro Forma Rate Base results in a rate of return of 4.9068% as shown on line 9. Line 11, the Operating Income Requirement of $65,734,245, is compared to the Operating Income at present rates to calculate the required Additional Operating Income of $21,427,512 as shown on Line 12. The Associated Income Tax on Line 13 is $14,019,158. The required overall revenue increase is $35,446,670 as shown on Line 14.

Schedule 3-B summarizes Rate Base, Revenues and Expenses in columnar format categorized as Amount Per Books, Pro Forma Adjustments and Pro Forma Adjusted Total. Schedule 3-C provides each Pro Forma adjustment used in the rate application.

Q. PLEASE DESCRIBE SECTION 4.

A. Section 4, Schedule 4-A, Functional Classification of Plant in Service, summarizes each plant in service detail account in functional categories under the headings of Amount Per Books, Pro Forma Adjustments and Pro Forma Adjusted Total. The Plant in Service Amount Per Books on Line 8 is $1,702,040,331; Pro Forma Adjustments reflect an increase of $68,458,332; the Pro Forma Adjusted Total is $1,770,498,663. Corporate allocated plant is included to identify the portion of ONE Gas plant in service allocated to KGS. The Pro Forma adjusted amounts are forwarded to Schedule 3-B and the total Pro Forma adjustment is forwarded to Schedule 3-A. The remaining pages in Schedule 4-A provide each account by the uniform FERC three-digit account in columnar format categorized as Amount Per Books, Pro Forma Adjustments and Pro Forma Adjusted Total.

Schedule 4-B continues the three-digit account format and is expanded by providing comparisons for the twelve months ended December 31, 2012, 2013, 2014, and 2015.

Schedule 4-C provides summary Pro Forma Adjustments to Plant in Service by functional classification.

Schedule 4-D provides an explanation of Pro Forma Adjustments and is further explained in testimony by witnesses identified in Table 1 of my testimony.

Q. PLEASE DESCRIBE SECTION 5.

A. Section 5, Schedule 5-A, Summary Functional Classification of Accumulated Provision of Depreciation and Amortization, summarizes each detail reserve account in functional categories in columnar format under the headings of Amount Per Books, Pro Forma Adjustments and Pro Forma Adjusted Total. Corporate allocated accumulated depreciation is included to identify the portion of ONE Gas' accumulated depreciation allocated to KGS. The Accumulated Provision of Depreciation and Amortization Amount Per Books on Line 9 is $591,732,290; Pro Forma Adjustment is an increase of $12,406,783; and Pro Forma Adjusted Total is $604,139,074. The Pro Forma adjusted amounts are forwarded to Schedule 3-B and the total Pro Forma adjustment is forwarded to Schedule 3-A.

Schedule 5-B, Detail Functional Classification of Accumulated Provision of Depreciation and Amortization, provides each reserve account by the uniform FERC three-digit account in columnar format under the headings of Amount Per Books, Pro Forma Adjustments and Pro Forma Adjusted Total. Sub-total amounts are forwarded to Schedule 5-A.

Schedule 5-C shows a Summary of Pro Forma Adjustments to Accumulated Provision of Depreciation and Amortization. This schedule summarizes by adjustment, each detail reserve account into functional categories in columnar format under the headings of Amount Per Books, Pro Forma Adjustments and Pro Forma Adjusted Total.

Schedule 5-D, Detail Functional Classification of Adjustments to Accumulated Depreciation and Amortization, shows each Pro Forma adjustment by the uniform FERC three-digit account in columnar format under the headings of Amount Per Books, Pro Forma Adjustments and Pro Forma Adjusted Total. Amounts are forwarded to Schedule 5-B and are summarized in Schedule 5-C.

Schedule 5-E continues the three-digit account format and is expanded by providing comparisons for the twelve months ended December 31, 2008, 2009, 2010, and 2011.

Schedule 5-F provides an explanation of Pro Forma Adjustments which are explained in the testimony of the witnesses identified in Table DND-1 of my testimony.

Q PLEASE DESCRIBE SECTION 6.

A. Section 6, Schedule 6-A, Summary of Working Capital, includes those items required to support the day-to-day business activities in rendering delivery service. Working capital items include materials and supplies, prepayments and gas storage inventory. This section also includes a reduction to rate base for such customer-provided capital items as accumulated deferred income tax liability (ADIT), customer deposits and customer advances.

Schedules 6-B and 6-C each present thirteen months of data by the uniform FERC account, since these types of costs fluctuate monthly, a thirteen-month average is utilized to normalize the embedded cost continually supplied or advanced by Company.

Schedule 6-D sets forth the total ADIT that represents an offset to rate base, including the allocable portion of ADIT that corresponds to corporate plant allocated to KGS in Section 4.

Q. PLEASE DESCRIBE SECTION 8.

A. Section 8, Schedule 8-A compares the Balance Sheet of KGS for the periods ended December 31, 2012, 2013, 2014 and 2015.

Schedule 8-B presents an Income Statement by FERC functional account and compares the twelve-month periods ended December 31, 2012, 2013, 2014 and 2015.

Schedule 8-C presents the Retained Earnings by FERC account and compares the twelve-month periods ended December 31, 2012, 2013, 2014 and 2015.

Schedule 8-D presents detailed Operating Revenues by FERC account and compares the twelve-month periods ended December 31, 2012, 2013, 2014 and 2015.

Schedule 8-E presents detailed Operating Expenses by FERC account and compares the twelve-month periods ended December 31, 2012, 2013, 2014 and 2015.

Schedule 8-F presents Usage, Revenues and Customer Data and compares the twelve-month periods ended December 31, 2012, 2013, 2014 and 2015.

Schedule 8-G presents KGS Operations Payroll Data by FERC account and compares the twelve-month periods ended December 31, 2012, 2013, 2014 and 2015.

Q. PLEASE DESCRIBE SECTION 9.

A. Section 9, Schedule 9-A, presents the Pro Forma Operating Income Statement. Revenues and expenses are summarized by the FERC functional categories to arrive at Operating Income under present rates in columnar format under the headings of Amount Per Books, Pro Forma Adjustments and Pro Forma Adjusted Total. Total Revenue on line 3, Amount Per Books, is $533,449,344; Pro Forma Adjustments to revenue are a decrease of $245,517,932 resulting in Pro Forma Revenue of $287,931,412. Total expenses on line 18, Amount Per Books, are $490,167,832; Pro Forma Adjustments to expenses are a decrease of $246,543,154 resulting in Pro Forma Expenses of $243,624,679. Operating income on line 19, Amount Per Books, is $43,281,512; Pro

Forma Adjustments to Operating Income is an increase of $1,025,222 resulting in Pro Forma Operating Income of $44,306,733.

Schedule 9-B is formatted similar to Schedule 9-A and is expanded to depict each Pro Forma adjustment proposed to normalize, to annualize, to include or exclude certain costs previously deferred pursuant to accounting authority orders and other adjustments. Schedule 9-C provides an explanation of Pro Forma Adjustments which are explained in the testimony of the witnesses identified in Table 1 of my testimony.

Q. PLEASE DESCRIBE SECTION 10.

A. Section 10, Schedule 10-A, presents Pro Forma Depreciation and Amortization Expense by the FERC functional categories in columnar format under the headings of Amount Per Books, Pro Forma Adjustments and Pro Forma Adjusted Total. Corporate allocated depreciation expense is included to identify the portion of ONE Gas' depreciation of plant in service allocated to KGS. Total Depreciation and Amortization Expense on line 15, Amount Per Books, is $44,264,296; Pro Forma Adjustments are an increase of $4,745,635 resulting in Pro Forma Adjusted Total of $49,009,931.

Schedule 10-B presents depreciation and amortization with amounts related to clearing accounts.

Schedule 10-C provides depreciation and amortization adjustments by FERC function. The total Pro Forma adjustment amounts are forwarded to Schedule 10-A.

Schedule 10-D depicts current depreciation rates and proposed depreciation rates resulting from a depreciation study performed and submitted as part of this application. Dr. Ronald E. White, who is testifying on behalf of the Company, sponsors the technical update to the depreciation study.

Schedule 10-E calculates the Pro Forma depreciation expense based on existing depreciation rates.

Schedule 10-F calculates the Pro Forma depreciation expense based on the proposed depreciation rates.

Q. PLEASE DESCRIBE SECTION 11

A. Section 11, Schedule 11-A presents Taxes other than Income Taxes and Income Taxes in columnar format under the headings of Amount Per Books, Pro Forma Adjustments and Pro Forma Adjusted Total. Total Taxes applicable to operations on line 9, Amount Per Books, are $42,479,230; Pro Forma Adjustments increase taxes $2,438,277 resulting in Pro Forma Adjusted Total of $44,917,507.

Schedule 11-B lists taxes other than income taxes such as components of payroll taxes, real estate and personal property taxes in columnar format under the headings of Amount Per Books, Pro Forma Adjustments and Pro Forma Adjusted Total.

Schedule 11-C, calculates taxable income and income taxes. In determining taxable income, the interest expense was synchronized by multiplying the weighted cost of debt in Section 7 by the rate base shown in Section 3. This schedule provides the necessary components to determine the appropriate taxable income based upon book revenues, expenses and all Pro Forma Adjustments to operations. These values are forwarded to Schedule 11-A.

Schedule 11-D provides a schedule of the taxable income.

Schedule 11-E shows Pro Forma Deferred income tax expense and investment tax credits.

Schedule 11-F describes the test period book/tax timing differences necessary to compute test period income tax expense.

Schedule 11-G shows the calculation of the tax gross-up ratio as well as providing the computation for the interest synchronization calculation.

Schedule 11-H provides the historical activity of the balance of the deferred investment tax credits and deferred income taxes.

Q. PLEASE DESCRIBE SECTION 12.

A. Schedules 12A and 12B address corporate allocation and are sponsored by company witness Crystal Turner. Schedule 12C, which I am sponsoring, contains a summary of the labor capitalization ratios used to determine the labor allocated to capital and expense.

Q. PLEASE DESCRIBE SECTION 13.

A. Section 13 contains the ONE Gas 2015 annual report to stockholders, which includes the FORM 10-K filed with the Securities and Exchange Commission.

Q. PLEASE DESCRIBE SECTIONS 14 AND 15.

A. Commission regulations provide that Sections 14 and 15 of the MFRs can be used to present additional evidence not provided elsewhere in the application. No additional evidence has been submitted.

Q. PLEASE DESCRIBE SECTION 16.

A. Financial statements required by Commission regulations to be included in Section 16 are provided in Section 13.

Q. PLEASE DESCRIBE SECTION 17.

A. Schedule 17-A presents a Summary of Revenue by General Customer Classification. Column 2 contains the Pro Forma Revenue from Existing Tariffs, column 3 has the Revenue Increase or decrease resulting from proposed tariffs, and column 4 shows the Pro Forma Revenue from the Proposed Tariffs.

Schedule 17-B shows Customers, Deliveries and Revenues for each existing individual tariff. The test year numbers are shown as “per books” and followed by Pro Forma Adjustments, and then Total Pro Forma Customers, Deliveries and Revenues.

Schedule 17-C contains Customers, Deliveries and Revenues for each proposed tariff. The revenue section shows Proposed Revenues, Pro Forma test year revenues and the increase resulting from the proposed tariffs. The percent of increase was calculated by dividing the additional proposed revenue by the sum of the COGR revenue and the Pro Forma test year revenue. The revenue per unit was calculated by the proposed revenue divided by the Pro Forma deliveries. The COGR revenue was determined by multiplying the test year Pro Forma deliveries by the weighted average cost of gas during the test year of $5.18.

Q. PLEASE DESCRIBE SECTION 18 AND WHICH WITNESS IS SPONSORING THAT SECTION?

A. Section 18 includes proposed changes to the Company's Rate Schedules and General Terms and Conditions. The section is sponsored by Company witness Justin Clements.

VI. EXPLANATION OF ADJUSTMENTS

Q. MR. DITTEMORE, YOU SPONSOR FOUR DIFFERENT ADJUSTMENTS TO THE ACCUMULATED DEFERRED INCOME TAX ("ADIT") LIABILITY. PLEASE BEGIN BY DEFINING ADIT.

A. ADIT records the cumulative differences between Income Tax Expense recorded pursuant to GAAP for financial reporting purposes and actual income taxes paid to taxing authorities. While there are a number of contributing factors impacting the ADIT balance, typically the ADIT is a net liability rather than an asset. Significant activity in this account is driven by accelerated tax depreciation contrasted with more conservative book depreciation. These differences in depreciation rates create a difference between 'book income' and 'taxable income' which, when applied to the effective tax rate, results in an entry to the ADIT account, usually creating a liability. The difference between book and tax depreciation rates turns around over time (i.e., tax depreciation is initially higher than book but then this trend reverses itself as the asset becomes fully depreciated for both book and tax purposes. and thus is an example of what is termed a temporary difference. As an asset becomes fully depreciated for tax purposes, the book depreciation continues and the difference between the two cumulative depreciation balances is reduced until it is eventually eliminated, resulting in the elimination of the ADIT balance for that particular asset. Temporary differences affect the timing of the payment of income taxes contrasted with the recognition of Income Tax Expense per GAAP. Over time, however, these temporary differences are eliminated. During the period of time when the annual tax depreciation is greater than the annual book depreciation of an asset, the taxable income will be lower and thus taxes paid will be lower than the related book income tax expense, creating a deferred tax liability. When the turn-around occurs, the book depreciation will be higher than the tax depreciation, thus producing lower book income, resulting in lower income tax expense compared with taxes paid, which reduces the deferred tax liability.

Q. PLEASE EXPLAIN HOW THE ADIT ACCOUNT IS TREATED FOR RATEMAKING PURPOSES?

A. The typical regulatory treatment of the net ADIT balance is to reflect it as an offset to Rate Base. This treatment is appropriate because the net ADIT liability represents a source of financing to the utility. The application of the net ADIT balance as a Rate Base offset is generally not a source of contention in rate proceedings. As shown in Schedule 6-D of the Application, KGS has recorded a net ADIT Liability of ($304,289,937) as of 12/31/15. The pro forma balance of ($272,849,807) is treated as an offset to Rate Base, consistent with traditional regulatory treatment.

Q. PLEASE NOW TURN TO ADJUSTMENT WC 3 AND EXPLAIN WHY THIS ADJUSTMENT IS NECESSARY.

A. Adjustment WC 3 reduces the ADIT Liability (thus increasing Rate Base) $51,778,325. This adjustment is necessary to eliminate the impact of pension and Other Post Employment Benefit (OPEB) funding on KGS ADIT balance and is consistent with the Stipulation and Agreement in Docket No. 10-KGSG-130-ACT ("130 Docket").

Q. PLEASE BEGIN BY PROVIDING AN OVERVIEW OF THE 130 DOCKET.

A. The 130 Docket dealt with fairly complex accounting/funding issues related to utility pension and OPEB costs. Essentially, OPEB costs are those costs accrued to provide retiree benefits such as medical and dental coverage. The Order permitted KGS to defer, as a regulatory asset or liability, differences between current year GAAP Pension/OPEB expense and those corresponding expense levels included in each utility's revenue requirement determined in its most recent rate case[1]. The other major element of the approved Order was that the utilities were required to make contributions to an external trust fund. KGS has greatly exceeded the funding requirements set forth in the Order.

Q. WHAT IS THE IMPLICATION OF THIS OVER-FUNDING ON THE BALANCE OF ADIT?

A. The cumulative pension/OPEB funding in excess of that recorded as a book expense has resulted in an increase in the ADIT balance of $51,778,325. The reason is that the funding is deductible for tax purposes, while the lower book expense is used within the calculation of the deferred tax expense. This difference between the funding level and the book expense creates a deferred tax liability.

Q. DO CUSTOMERS BENEFIT FROM FUNDING IN EXCESS OF THAT REQUIRED IN THE 130 DOCKET?

A. Yes. Mr. Mark Smith addresses this issue within his testimony.

Q. DOES THIS EXCESS FUNDING RESULT IN AN ASSET THAT IS INCLUDED IN RATE BASE?

A. No. The Order in the 130 Docket provided there would be no rate base recognition for any excess contributions beyond the pension/OPEB funding requirements. KGS has not

[1] The amortization of this balance is presented as adjustment IS 26.

included a rate base additive for its level of funding in this application. The pertinent language from the KCC's order in the 130 Docket is:

> B. KGS's application with respect to Tracker 2, to establish a regulatory asset/liability account to accumulate the difference between the current year pension/OPEB contribution to its established trusts and current year GAAP pension/OPEB costs, not as a component of rate base as set forth by Staff's recommendation is hereby approved.

As indicated by Mr. Smith's testimony we are not requesting rate base recognition in this filing,

Q. HOW DOES THIS LANGUAGE SUPPORT YOUR ADJUSTMENT TO ELIMINATE THE ADIT LIABILITY ASSOCIATED WITH THIS EXCESS FUNDING?

A. Absent this adjustment, KGS would be penalized for its excess funding through a reduction in rate base. The excess funding has benefited customers and KGS should not be faced with a reduction to its rate base, through its ADIT account, as a direct result of its level of funding. The language in the Order indicates there should be no rate base recognition of the excess funding as an additive to rate base. To be consistent with the intent of the Order, rate base should not be reduced for the tax liability generated as a result of the funding.

Q. PLEASE IDENTIFY ADJUSTMENT WC 4 TO RATE BASE?

A. Adjustment WC 4 reduces rate base $25,612,745 by reducing the Net Operating Loss (NOL) balance within the deferred tax liability associated with excess pension and OPEB funding as discussed in Adjustment WC 3. The justification for Adjustment WC 4 is identical to that of Adjustment WC 3. Identical adjustments were proposed and accepted in the last KGS base rate case Docket No. 12-KGSG-835-RTS ("835 Docket").

Q. PLEASE CONTINUE WITH AN EXPLANATION OF ADJUSTMENT WC 5.

A. Adjustment WC 5 reduces the ADIT Liability $5,274,550 and is necessary to remove the impacts associated with KGS's Cost of Gas Rider. At any point in time, customers have either under or over funded the cost of gas, transportation and storage costs KGS incurs to deliver natural gas to consumers. KGS monitors the status of the over/under account and reports monthly to the KCC Staff. This difference is either taxable or tax deductible depending upon the balance. Since there is an equal likelihood of a positive or negative balance in this account going forward, I recommend that the impact of the balance at the end of the test period be removed for purposes of establishing the appropriate ADIT Liability balance used as a rate base deduction. There is no income statement impact from this issue, thus an adjustment to pro forma revenues or expenses is unnecessary.

Q. PLEASE EXPLAIN ADJUSTMENT WC 6

A. Adjustment WC 6 reduces rate base $7,916,831 and is necessary to attribute a portion of ADIT Liability to KGS associated with the allocation of corporate plant as described by Company witness Crystal Turner in Adjustment PLT 3. As discussed in her testimony, these assets are used in the provision of utility service and because they are not recorded on the books of KGS, they must be allocated. Similarly, the ADIT liability associated with these assets is not recorded on the books of KGS and thus, an adjustment is necessary to properly allocate this customer provided capital to KGS.

Q. PLEASE CONTINUE WITH AN EXPLANATION OF ADJUSTMENT IS 34.

A. Adjustment IS 34 increases pro forma operating expenses $326,216. This adjustment incorporates the estimated costs of this rate case plus the unamortized rate case costs from the 835 Docket, amortized over a three-year period. The adjustment is netted against test year rate case amortization costs, resulting in a net increase in operating expenses. The actual costs of the rate proceeding shall be incorporated into the final adjustment at the conclusion of this docket.

Q. PLEASE CONTINUE WITH AN EXPLANATION OF ADJUSTMENT IS 35.

A. Adjustment IS 35 calculates the pro forma income tax expense $3,767,139. This adjustment is based upon pro forma operating income which incorporates all pro forma adjustments contained within this filing, and is necessary to properly match pro-forma income tax expense with pro forma taxable income.

VII. COST OF SERVICE ADJUSTMENT MECHANISM

Q. WHY IS THE COMPANY PROPOSING AN ANNUAL COST OF SERVICE ADJUSTMENT ("COSA") MECHANISM AT THIS TIME?

A. As the Commission knows, ONE Gas is a pure-play natural gas utility, focused on providing safe, reliable, natural gas service at a reasonable cost. In order to provide high quality service that our customers and the Commission expect, it is imperative that the Company has a reasonable opportunity to earn its Commission authorized return on equity. The proposed COSA mechanism will provide a reasonable opportunity to earn our authorized return, which is not currently available in the existing regulatory framework.

As is discuss later in my testimony, the proposed mechanism also offers benefits to KGS customers.

Q. HAS KGS HAD A HISTORY OF FREQUENT BASE RATE FILINGS?

A. No. Since being acquired by ONEOK in 1997, Kansas Gas Service has filed three rate cases. This filing represents its fourth such filing in 20 years. The last base rate case application occurred four years ago, in May, 2012.

Q IN YOUR OPINION, DOES KGS HAVE A REALISTIC OPPORTUNITY TO EARN ITS AUTHORIZED RETURN ON EQUITY?

A. No. One of the objectives of utility regulation is that the rates approved by regulatory agencies should provide the utility with the opportunity (but not a guarantee), to earn its authorized return on equity. "The (utility) rates should be high enough to provide the utility with a reasonable opportunity to recover the total costs of providing service and to sustain its financial integrity."[2]

Unlike electric utilities with a history of growing load, gas utilities face continual declines in residential consumption, delayed recovery of depreciation and return on a good portion of its capital investments as well as recovery of increasing Operating and Maintenance expenses. Currently, the only opportunity to recover these increasing costs (other than GSRS qualifying investment) is through a full base rate case, which is expensive and time-consuming to both prepare and process, and as discussed below, results in considerable regulatory lag.

Q. HAS KGS EARNED ITS AUTHORIZED RETURN ON EQUITY SINCE ITS LAST RATE PROCEEDING?

A. No. Under any measure KGS's actual return on equity earned each year, has fallen far short of the ROEs proposed by any of the parties in its last rate proceeding.

Q. WHAT CAUSES THE ACTUAL RETURN ON EQUITY TO BE BELOW THE ALLOWED RETURN ON EQUITY APPROVED IN A RATE PROCEEDING?

A. In my opinion, the causes can be summarized as follows:

1. Increases in cost compared to the allowed cost recovery in a rate review,
2. Increase in net plant compared to the allowed net plant in a rate review, including approved GSRS plant,
3. Decreases in consumption by residential customers, and
4. The outcome of the company's most recent base rate case.

Q. WILL THE COMPANY BE ABLE TO REPLICATE ITS HISTORIC PATTERN OF INFREQUENT RATE FILINGS IN THE FUTURE?

A. No. The company cannot sustain the level of under-earnings experienced in the past three years over an extended time period in the future.

[2] Accounting for Public Utilities §3.01(3), Release November, 2010.

Q. EARLIER YOU MENTIONED THE PROPOSED MECHANISM WOULD PROVIDE BENEFITS TO KGS CUSTOMERS. PLEASE IDENTIFY SUCH BENEFITS.

A. The customer benefits resulting from implementation of an annual review mechanism include:

1. Increased transparency of KGS's operations due to the annual review process, translating to less controversial ratemaking procedures, balancing the needs of our customers, the Commission, its Staff as well as the Company;
2. Rate Increases, while likely more frequent, will be smaller and reduce the possibility of rate shock;
3. Reduction in the number of applicable riders;
4. All operating efficiencies obtained by KGS are promptly flowed back to customers through the annual mechanism; and
5. A significant reduction in rate case costs which otherwise would be incurred in fully litigated rate cases.

Q. EXPLAIN HOW CUSTOMERS WILL BENEFIT FROM INCREASED TRANSPARENCY OF KGS's OPERATIONS UNDER THE PROPOSED COSA MECHANISM.

A. The proposed mechanism will require an annual filing by KGS that will be subject to review by the KCC Staff, CURB and other interested parties. The annual review by regulators will allow for greater familiarity with and knowledge of KGS operations.

Q. PLEASE EXPLAIN HOW THE INCREASED LEVEL OF TRANSPARENCY WILL TRANSLATE TO LESS CONTROVERSIAL AND PROTRACTED RATEMAKING PROCEDURES.

A. Once the process of annual filings occurs, we would expect Staff and CURB to greatly increase their familiarity and comfort level with both the filing itself and the annual process. For example, with each GSRS filing that was made, Staff and KGS became more comfortable with the process and there has been little controversy between the parties since inception of the mechanism. I believe the annual review mechanism would work in a similar fashion.

Q. WHY DO YOU BELIEVE OVER TIME THE FILINGS WOULD BECOME LESS CONTROVERSIAL?

A. It's been my experience that the most consistently controversial items within natural gas utility rate filings are the following:

a. Return on Equity

b. Depreciation Rates

c. Incentive Compensation

d. Class Cost of Service

e. Rate Design

As discussed below, these items will be incorporated into the annual mechanism consistent with the Commission's findings in this proceeding, thus eliminating controversy surrounding these traditional ratemaking issues. Since the artificial cap on equity was limited to the first general rate case filed after the separation with ONEOK under the settlement approved by the Commission in the 100 Docket, the 55% equity cap should not apply to the COSA filings. Instead, KGS should be allowed to use its actual equity ratio, not to exceed 60%, in those COSA filings. The cost of debt and cost of equity determined in this rate case would still apply to the COSA filings and would be applied to ONE Gas' actual capital structure, subject to the limitation above.

Q. HOW WILL THE ANNUAL REVIEW REDUCE THE POTENTIAL FOR CUSTOMER RATE SHOCK?

A. The annual review mechanism may result in more frequent rate increases than is the case under the traditional rate case methodology; however, such annual reviews will produce smaller rate increases and will provide additional opportunities for decreases than is the case with rate filings that are years apart. As a direct consequence of the significant time between rate filings in the traditional model, the utility bears the compounding impact of multi-year cost increases, until such time as it is able or permitted to submit a comprehensive base rate application. This result generally translates to much larger, albeit less frequent rate increases. Further, there is an important consumer protection feature of our proposal which provides added assurance that significant increases will not occur. I will discuss that feature later in my testimony in a discussion of the details of the mechanism.

Q. HOW WOULD THE ANNUAL COSA MECHANISM REDUCE THE NUMBER OF KGS RIDERS?

A. If the Commission authorizes this annual review mechanism, KGS will no longer file for the Gas System Reliability Surcharge (GSRS) and would eliminate the Ad Valorem Tax Surcharge (AVTS).

Q. IF THE COMMISSION DESIRES THE RETENTION OF THE GSRS SURCHARGE, DOES KGS OBJECT TO RETAINING THAT MECHANISM?

A. No. If the Commission desires to retain focus on KGS's GSRS investment, we do not have any objection to retaining that mechanism and such investments could easily be incorporated in the annual COSA mechanism as is done today with a base rate increase.

Q. EARLIER YOU INDICATED THAT THE MECHANISM WOULD HAVE CUSTOMER PROTECTION FEATURES THAT BALANCE THE INTERESTS OF CUSTOMERS AND SHAREHOLDERS. PLEASE IDENTIFY WHAT SPECIFIC FEATURES YOU ARE REFERENCING.

A. The COSA mechanism proposed by KGS is somewhat similar to the annual review mechanism that was proposed by Atmos in Docket No. 16-ATMG-079-RTS (079

Docket), in that both propose to incorporate an annual review mechanism[3]. However, the KGS COSA mechanism differs from that proposed by Atmos in that it caps the eligible annual Operating and Maintenance (O&M) cost increases year over year at four percent. In other words, for purposes of calculating the O&M expense portion of the annual revenue requirement, the increase is limited to a four percent annual increase compared with the O&M expense levels adopted by the Commission in this proceeding. The proposed capping of O&M increases eligible for recovery in this annual mechanism, renders moot the argument some may raise that an annual review mechanism reduces or eliminates the incentive a utility has to control its costs.

In addition to the O&M expense cap, another important feature of the mechanism is the provision that KGS will be required to submit pre-filed testimony accompanying the annual review mechanism. The testimony will provide an overview of the filing as well as a description of all pro forma adjustments. An additional aspect of the proposed mechanism is that in the event the Commission is unable to render a decision in the 135 day process envisioned in the tariff, the rates implemented on September 1 will be considered "interim rates" subject to refund. Therefore, if some unique regulatory issues arise that the parties are unable to resolve, requiring modification to the streamlined process, the refund provision provides customers with protection pending ultimate resolution of the litigated issue(s). I do not envision protracted litigation surrounding the COSA, given that the more controversial rate case components will be effectively resolved based up on determinations made as part of this general rate case docket.

Another important consumer protection feature of the annual review mechanism is that it is designed to be a three-year pilot program. At the end of the initial three-year program, the Commission will be in a position to evaluate the public policy implications of the pilot program. Thus, the Commission is not burdened in this docket with the task

[3] The Commission has also previously approved formula rates in Docket No. 13-MKEE-452-MIS (2013)

of addressing a proposed change in the method of establishing base rates, which would have an impact for an indefinite period of time. Instead, after review of the trial period, the Commission could reauthorize the annual filings for an additional period of time based on the success of the pilot program and the level of confidence Staff, CURB and KGS have in it to provide just and reasonable rates.

Q. CONTINUE WITH AN EXPLANATION OF HOW OPERATING EFFICIENCIES ACHIEVED BY KGS WILL BE FLOWED BACK TO CUSTOMERS.

A. Operating efficiencies achieved by KGS would be captured for the benefit of customers in the form of reduced operating expenses. Since the mechanism incorporates an annual review, these efficiency gains would be reflected in the operational results that factor into whether a change in rates is warranted.

Q. HOW WILL THE ANNUAL MECHANISM REDUCE REGULATORY EXPENSE?

A. Absent an unusual change in operating environment, the annual mechanism should reduce the need for traditional - fully litigated base rate proceedings, which are costly to produce and process for all parties. Instead, for the purposes of the COSA, the decisions regarding most of the significant and controversial rate case issues will be based upon the Commission's determinations of those issues in this proceeding. The ability to merely incorporate the results of this case into the annual filings, translates to avoided rate case costs.

Q. ARE YOU FAMILIAR WITH STAFF TESTIMONY IN OPPOSITION TO THE ANNUAL RATE MECHANISM (ARM) PROPOSED BY ATMOS IN THE 079 DOCKET?

A. Yes, I am.

Q. CAN YOU SUMMARIZE THE CRITICISM CONTAINED IN STAFF TESTIMONY CONCERNING THE ARM.

A. Staff testimony levied the following concerns with the ARM proposal[4]:

1. The mechanism cut the statutory review time in half from 240 days to 120 days.
2. The burden of proof involving the ARM was shifted to Staff and Atmos was not required to submit testimony.
3. The ARM tariff was not presented as a pilot or experimental program.
4. The ARM tariff did not appear to contemplate a situation where disagreement could arise between Atmos and Staff or another intervenor.
5. The ARM tariff addressed a problem largely of Atmos' own making.
6. The reduction of regulatory lag benefited only shareholders, and not ratepayers.

Q. PLEASE DISCUSS EACH OF THESE POINTS INCLUDING HOW THE COSA MECHANISM ADDRESSES THESE ISSUES OR WHY THE POINTS ARE NOT RELEVANT.

A. Under the KGS COSA mechanism, rates would become effective on the one-hundred thirty fifth day after filing, subject to refund, if the Commission has not issued an order regarding the application. This proposed COSA permits an additional fifteen days of review beyond that contemplated in the Atmos ARM. However, despite the reduced time frame for review from a standard fully litigated rate proceeding, the full time frame allotted for a base rate proceeding should not be necessary under the COSA mechanism. As discussed earlier, the most controversial issues usually debated in traditional rate cases will be incorporated into the COSA filing consistent with findings in this present case; thus, reducing the need for the level of review incurred in base rate proceedings. Further, the annual review will enhance Staff and CURB's familiarity with KGS's operations and financial records which will allow for a shorter more focused review.

[4] Testimony of Justin Grady, 079 Docket, pgs 23-24

KGS recognizes it has the burden of proof to demonstrate that its request produces just and reasonable rates and has specifically included such a reference within the tariff. Moreover, as discussed above, all stakeholders benefit from the COSA mechanism.

Q. IS THE KGS COSA PROPOSAL PRESENTED AS A PILOT PROGRAM?

A. Yes. Staff's criticism that the Atmos ARM was not presented as a pilot program is not relevant in this situation as KGS has clearly identified its proposal as a pilot program subject to review at the end of its three-year implementation period in 2019. At that time, the Commission will have an opportunity to evaluate the mechanism and its results on all stakeholders.

Q. WHAT PROVISIONS ARE ASSUMED IF PARTIES TO THE APPLICATION DO NOT REACH AGREEMENT?

A. First, I wish to reiterate that I don't believe that scenario is likely. However, in the event it does occur, KGS recommends presenting oral arguments before the Commission by each intervenor's technical staff. This process would provide the Commission with the opportunity to hear from each party's technical experts in a straightforward and simple process where the information could be quickly provided by each party, permitting the Commission the necessary background information to render a decision.

Q. CONTINUE WITH A DISCUSSION OF STAFF'S CONCERN THAT THE ISSUES GIVING RISE TO ATMOS ARM PROPOSAL WAS LARGELY OF ATMOS' MAKING.

A. I disagree with the assertion that the ARM proposal was largely due to Atmos' own making.

Q. HOW DO YOU RESPOND TO STAFF'S POSITION THAT THE REDUCTION OF REGULATORY LAG BENEFITS SHAREHOLDERS, BUT NOT CUSTOMERS?

A. Utilities should be given a reasonable opportunity to earn the rate of return authorized by the Commission. The reduction of regulatory lag is consistent with this objective. The proposed COSA mechanism and the protections built into it are a benefit to customers, as I further elaborate below.

Q. WILL REGULATORY LAG BE ELIMINATED UNDER THE KGS COSA PROPOSAL?

A. No. For example, capital investment that becomes used and useful in January of a given year will, under the proposed mechanism, not be reflected in customers' rates until September of the following year. KGS will continue to have the same incentives it has today to control costs.

Q. IF THE COSA MECHANISM IS ADOPTED, WHY WOULD KGS RETAIN THE INCENTIVE TO CONTROL COSTS?

A. Public natural gas utilities have a responsibility to all stakeholders to first ensure they provide safe and reliable natural gas service in compliance with all laws and regulations. These companies also have a responsibility to their shareholders to maximize shareholder return. The COSA mechanism does not protect utility shareholders from bearing the financial burden of increased operating costs. There is no deferral mechanism within the COSA to shift increasing O&M costs to future periods and further, the proposed mechanism caps increases in O&M costs at four percent, year-over-year. Therefore, utility managers retain the incentive to control costs in order to maximize earnings with or without the COSA mechanism.

Q. PROVIDE AN OVERVIEW OF THE PRIMARY ELEMENTS OF THE MECHANISM.

A. Each year KGS will prepare a revenue requirement calculation setting forth the actual test year data, adjusted for known and measurable changes and to annualize the data for known income statement impacts. The application, will be filed by April 15th and shall include pre-filed testimony supporting the calculation of the revenue requirement as well as an explanation of each test period adjustment. The adjustments to test period operations are designed to reflect an annualized level of O&M expense relying upon the same ratemaking methodologies used by the Commission today to define revenue requirements in fully litigated base rate proceedings. Likewise, adjustments to rate base will be those typically made in existing base rate proceedings. Any resulting changes to the existing approved revenue requirement shall be allocated to customer classes in the same proportion as the allocation of revenue requirement by class approved in this docket. The revised rates would apply to all customers other than special contract customers, who are served at existing competitive rates.

The information provided in the application would include test year data and otherwise conform to the information provided in current base rate case filings. However, historic data would not be included within the application, as the Commission will already be in possession of this information within this base rate filing as well as subsequent COSA filings. The COSA tariff requires that KGS submit its work papers to the KCC Staff and CURB simultaneously with the Application so that complete information is available for review at the time of the filing.

Staff, CURB and any other intervenor would have 60 days from the date the application and work papers are submitted to identify issues. The tariff requires that all parties work in good faith to resolve any disputes. Within 75 days of the filing Staff and any other interested interveners will submit its report and recommendation to the Commission. KGS will submit its response to the Staff report and other reports, if any, within ten days after those reports are submitted. At this point, the parties would submit a joint recommendation to the Commission on whether a brief technical hearing is necessary or whether the Commission could reach a decision based upon the written positions of the parties. The objective is for the Commission to issue an order on or before September 1st. If the Commission were unable to reach a decision by that time, the proposed rates would be placed in effect, subject to refund for any subsequent determination by the Commission that modifies the interim rates.

As mentioned earlier, the COSA mechanism is drafted as a pilot program that would be in effect for test periods 2017 – 2019, with corresponding rates in effect under the program for a three-year period beginning September 2018. Absent reauthorization as noted above, or a rate case or show cause proceeding being filed, it is expected that a new base rate case would be submitted in late 2020 or early 2021, at which time all parties would be able to address whether the pilot program shall be continued on a permanent basis, modified, or discontinued.

Q. HOW WILL THE COSA MECHANISM INCORPORATE A RETURN ON EQUITY INTO THE REVENUE REQUIREMENT CALCULATION?

A. The Authorized Return on Equity (AROE) adopted in this proceeding will be the AROE on which the COSA calculations are based. The Earned Return on Equity (EROE) shall be determined based upon actual test year operating results adjusted for known and measurable changes. The resulting EROE is then compared with the AROE to determine the revenue deficiency or excess.

Q. ARE YOU PROPOSING A LIMITATION ON THE ANNUAL LEVEL OF INCREASE IN OPERATING AND MAINTENANCE COSTS?

A. Yes. The limitation or cap on O&M costs, which excludes Depreciation Expense and taxes, is set at an annual increase not to exceed four percent applied per annum from December 31, 2015. If the Commission approves a revenue requirement in this proceeding which includes total O&M costs of $245 Million annually, then the cap limitation that would apply to the first COSA calculation for rates to be effective in September, 2018, would be ($150M*1.04*1.04) $164.4M. Thus, KGS is assuming the risk that its costs may exceed the four percent threshold per year and thus not fully recover its costs.

Q. IF THE COSA CALCULATION DETERMINES THAT A RATE CHANGE IS REQUIRED, HOW WILL SUCH INCREASE/DECREASE BE ALLOCATED TO CUSTOMERS?

A. The Commission's determination made in this case, regarding the appropriate assignment of the revenue requirement by rate class shall be the basis to assign any revenue deficiencies/excess arising from the COSA. Therefore, there should be no new controversy associated with this issue. The resulting rate design shall be based upon the relative ratio of customer charge and volumetric charges that are adopted within this proceeding.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.

VERIFICATION

STATE OF KANSAS)
) ss.
COUNTY OF JOHNSON)

David Dittemore, being duly sworn upon his oath, deposes and states that he is Director of Rates and Regulatory Affairs for Kansas Gas Service, a Division of ONE Gas, Inc.; that he has read and is familiar with the foregoing Direct Testimony filed herewith; and that the statements made therein are true to the best of his knowledge, information, and belief.

David Dittemore
NAME

Subscribed and sworn to before me this 27 day of April 2016.

STATE OF KANSAS NOTARY PUBLIC
JILL TENNANT
My Appointment Expires
June 21, 2018

Jill Tennant
NOTARY PUBLIC

My appointment Expires:
June 21, 2018

Cost of Service Adjustment (COSA) Plan

1. **Applicability**

1.01 The rider is applicable to all sales and transportation rate schedules except where not permitted under a separately negotiated customer contract.

1.02 The rate adjustments implemented under this mechanism will reflect annual changes in the Company's cost to provide natural gas distribution service.

2. **Purpose**

The purpose of this mechanism is to provide an annual earnings review in order to adjust rates to reflect the most recent historic costs necessary in the provision of natural gas utility service.

3. **Application**

Each annual application submitted by Kansas Gas Service (Company or KGS) shall calculate the revenue requirement of the company consistent with standard ratemaking principles adopted by the Kansas Corporation Commission (KCC or Commission). No provision contained within this tariff will limit the Company's ability to file a general rate change application, or the Commission's authority to file a show-cause proceeding. Kansas Gas Service shall have the burden of proof to demonstrate the reasonableness of its application and resulting rates.

The Company shall file an Application for a Commission determination pursuant to this COSA Rate Schedule for calendar years 2017, 2018 and 2019, with each filing to be submitted by the following April 15th. The Application shall include pre-filed testimony in support of the test period financial information as well as each pro-forma test period adjustment. During this three-year period, the COSA shall be considered a pilot program. Any subsequent Applications made pursuant to terms outlined in this tariff would require the approval of the KCC.

3.01 The Company shall, on or before April 15, file an application with the KCC and provide copies to Staff of the KCC, and the Citizens Utility Ratepayer Board (CURB). Historic information prior to the test period need not be provided. Where applicable, the data provided below shall include the test period actual data, listing of individual adjustments to test period data by FERC account and the as-adjusted balance. The filing shall include information consistent with the requirements of sections of K.A.R. 82-1-231 listed below:

Section 1: Application, letter of transmittal and authorization
Section 2: General Public Notification
Section 3: Summary of Rate Base, Operating Income and Rate of Return,
Section 4: Plant in Service
Section 5: Accumulated Provision for Depreciation and Amortization
Section 6: Working Capital
Section 7: Capital and Cost of Money
Section 9: Test Period and pro forma Income Statements

Issued: __________ Effective: __________ By: __________ David N. Dittemore, Director – Regulatory Affairs	

Cost of Service Adjustment (COSA) Plan

Section 10: Depreciation and Amortization
Section 11: Taxes
Section 12: Allocation Ratios
Section 18: Allocation of revenue requirement to customer classes, development of proposed rate design, proof of revenues and proposed tariffs

3.02 The filing shall be accompanied by work papers provided to the KCC Staff and CURB supporting each of the pro-forma adjustments.

3.03 The pro-forma adjusted operating expenses, excluding depreciation expense and all taxes, shall not exceed 104% of the previous year's as adjusted operating and maintenance (O&M) expenses, excluding depreciation expense and all taxes. The initial 4% O&M limitation shall be calculated on a per annum basis as of December 31, 2015. This provision shall represent a limit by which operating expenses may not increase for purposes of calculating the Earned Return on Equity (EROE) as discussed below. The KCC's authorized operating expenses within the KGS base rate proceeding shall be used as a baseline upon which subsequent operating expense limits would be determined. Any costs incurred as a result of new governmental mandates subsequent to December 31, 2015, shall not be included for purposes of calculating the O&M limitation.

3.04 An expedited processing schedule shall be established to provide notice and due process to all interested parties, including customers. Any calculations disputed by the parties shall be identified to the Company prior to June 15. The parties shall work in good faith to resolve all disputes prior to June 15. The KCC Staff report and recommendation will be provided to the KCC by June 30 and the Company's response to Staff's report and recommendation shall be filed with the Commission within seven business days following the filing of Staff's report and recommendation.

3.05 Unless disputed by the parties, any rate schedules incorporating the COSA Plan by reference will become effective by Order of the Commission with the first billing cycle in September. If the parties have not resolved the disputed issues, the issues will be set for hearing before the Commission. If the Commission has not issued an order by September 1 following the date of an application, then the rate schedules may be placed into effect and collected on an interim basis, subject to refund.

3.06 The revenue requirement increase or decrease as identified within Sections 3 and 18 listed above shall be determined pursuant to the return on equity parameters identified in Section 4 below.

Cost of Service Adjustment (COSA) Plan

4. **Application of the COSA Plan**

4.01 The Company's Allowed Return on Equity (AROE) is that set pursuant to the order of the Commission contained within the 2016 KGS base rate filing. This AROE shall be the effective AROE until modified by Commission order. Such modification shall be applied prospectively.

4.02 The Earned Return on Equity (EROE) shall be recalculated annually under this Plan, for use in determining any rate change adjustments that become effective during subsequent years. Except as otherwise provided in other sections of this tariff, the calculation shall be performed using the same methodology used to calculate the EROE pursuant to KGS' 2016 base rate filing.

4.03 The Company will submit revised rate schedules to the Commission each time the rates are adjusted pursuant to this Rate Schedule.

5. **Term**

This Rate Schedule shall become effective upon issuance of a Commission order and terminate at the end of the pilot program period approved by the Commission, or as the result of a final order being issued in a general rate case or show cause proceeding.

6. **Force Majeure Provision**

If any cause beyond the reasonable control of the Company, including, but not limited to, natural disaster, orders or acts of civil or military authority, terrorist attacks, or government mandates, which results in a deficiency in the revenues which are not readily capable of being addressed in a timely manner under this Rate Schedule, the Company may file for rate relief.

7. **Application of COSA Calculation Procedure**

7.01 For each 12-month period ending December 31, the Company shall file an Application for a Commission determination pursuant to this COSA Rate Schedule to determine whether the Company's jurisdictional non-fuel revenues should be increased, decreased, or left unchanged. If it is determined that the jurisdictional non-fuel revenues should be increased or decreased, the Company's rate schedules will be adjusted in the manner set forth in this Rate Schedule. Any revenue modifications will be allocated to the Company's customers based upon the customer class cost of service allocation approved by the KCC in the KGS 2016 base rate case filing. The revised rate schedules will become effective by Order of the Commission for the September cycle one bills and will remain in effect until changed under the provisions set forth in this Rate Schedule and by order of the Commission.

7.02 Rates applicable to each class shall be split between Customer Charge and Commodity Charge in the same proportion to total revenue as the underlying rates approved by the KCC in the most recent KGS base rate proceeding.

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Cost of Service Adjustment (COSA) Plan

8. **Annual COSA Plan Calculation**

8.01 The calendar year shall be the test year.

8.02 Rate Base and cost of service shall be computed in the same manner as approved by the Commission in KGS 2016 base rate case. This section does not prohibit the parties from requesting certain modifications to these rate change adjustments.

8.03 The Company's actual capitalization ratio as of the end of the test period shall be used to calculate the revenue requirement, except that the equity component shall not exceed 60%. The Company's weighted cost of debt at December 31 of test period shall be used to calculate the overall rate of return.

8.04 Actual year operating Revenues shall be modified consistent with the Commissions' findings in KGS' 2016 base rate case. The as adjusted Operating Revenues shall include, but not necessarily limited to test period weather normalization accruals and shall be determined based upon weather coefficients as determined in the KGS 2016 base rate case.

8.05 Actual test year operating Expenses shall also be modified consistent with the Commissions' findings in KGS 2016 base rate case based upon annualized December 31 year-end data for the following:

a. Depreciation expense calculated based upon December 31 balances multiplied by Commission authorized depreciation rates.

b. Labor costs based upon employees' compensation levels and employment levels as of December 31.

c. Actual test year expenses will be adjusted consistent with Commission findings on appropriate items to include/exclude in the revenue requirement pursuant to its order in the 2016 KGS base rate case.

d. The cost impacts of tax changes or governmental mandates shall be annualized.

e. Other adjustments as appropriate.

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