

BEFORE THE STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS

Before Commissioners: Jay Scott Emler, Chair
Shari Feist Albrecht
Pat Apple

In the Matter of the Complaint of Merit Energy) Docket No. 16-CONS-564-CINV
Company and Merit Hugoton, LP against ONEOK)
Field Services, LLC to establish just and) License No.: 32446
reasonable charges for gas gathering pursuant to)
K.A.R. 82-3-802)

PUBLIC VERSION

**PETITION FOR RECONSIDERATION OF MERIT ENERGY
COMPANY AND MERIT HUGOTON, LP**

COME NOW, the Complainants, Merit Energy Company and Merit Hugoton, LP (“Merit”), and pursuant to K.S.A. 77-529(a) petition the State Corporation Commission of the State of Kansas (“Commission”) for reconsideration of its Order dated February 28, 2017. This Petition for Reconsideration is for reconsideration of specific issues of fact or law involved in the initial hearing pursuant to K.A.R. 82-1-235. The Commission finding in Paragraph 94 that: “A gas gathering fee of \$0.68/MCF . . . is just, reasonable, not unjustly discriminatory and not unduly preferential” ignores the testimony of both Staff witness Bell and Merit witnesses Bower and Collins, all who testified to the reasoning behind the need for the use of averages in order to determine a range of reasonableness and recommended a fee of \$0.45/MCF (Merit) and \$0.44/MCF (Staff). The fee of \$0.68/MCF ordered by the Commission is either outside the range of reasonableness using average high and average low fees reported in the GG-1’s or approaches the upward range ignoring the evidence that Merit is a low cost causer and a low user of compression. At the very least, the Commission should have started with the \$[REDACTED]/MCF fee,

which represents the average fee under the 51 contracts, and then subtracted the \$[REDACTED]/MCF ONEOK pays to move gas across West Texas Gas to a plant, to yield a gathering fee of \$[REDACTED]/MCF as the fee to move Merit's gas from the wellhead to West Texas Gas. Therefore, Merit seeks reconsideration on the following specific grounds:

1. The Commission's findings in Paragraph 40 are unreasonable, arbitrary and capricious and not supported by evidence in the record and in fact ignore evidence that is in the record which supports the use of averages. In Paragraph 40 the Commission states: "The Commission finds no principled or logical basis in the record for using averages instead of the high and low fee range . . ." This finding ignores testimony in the record regarding using averages to eliminate the effect of outliers. There is in fact discussion in the record regarding using averages to eliminate outliers;

a. Witness Bower testified that: "If you have a number of agreements that have similar answers, then I think that gives you some confidence that similar agreements with similar answers are helpful to the answer that you are trying to get to. Because you can get an outlier agreement, one that is especially high or especially low, which might not be appropriate because they may have other situations that you don't know about. And we are never going to know what all of the circumstances are." (Tr. p. 142-143 lines 25-2) Such testimony, which outlines the risk of outlier agreements, lends itself to using the average of the weighted average fees or as witness Bell suggested using the average high and average low.

b. In the KCC Staff's post-hearing brief, Staff notes that in its GG-1 analysis of other gatherers besides ONEOK Field Services ("OFS"), the average low is

\$0.29/MCF, the average high is \$0.60/MCF and the average is \$0.40/MCF. The Staff indicates that because the \$[REDACTED]/MCF lies outside of this range it appears excessive. Staff used those averages to smooth out the outliers. (Post-Hearing Br. p. 4)

c. Witness Bell testified:

Q. "My point is, you are using averages to help smooth out the outliers?"

A. Yes.

Q. So to the extent we have some contract variations within those GG-1's the intent of the average is to help take account for those?

A. Yes."

(Tr., p. 337, lines 12-18)

d. One example of an outlier is what the Commission uses to establish the upward boundary in the so called "range reasonableness": Anadarko's \$1.35/MCF fee. The Commission noted that Merit's GG-1 analysis shows the highest fee to be \$1.35 (Anadarko) and the lowest to be \$0.02 (DCP-Stanton). (Paragraph No. 46) One Dollar and 35/100 (\$1.35) is not a comparable fee to ONEOK's system as the Anadarko system is significantly more robust than ONEOK's, providing vacuum service at the wellhead and then compressing the gas to 500 psig into a plant (Collins Rebuttal Testimony, p.9, lines 17-23). This vacuum service (negative pressure on the wellhead) leads to better well performance and higher production because the gas is being pulled out of the ground by the gathering system. In comparison, ONEOK's average system pressure is about six (6) psig (Pearson Direct Testimony, p.6, lines 8-9), which means that the gas flowing out of the ground must penetrate a pressure gradient in order for it to produce. This curtails the potential production of a well. Taking the gas from vacuum pressure up to 500 psig

requires significantly more work than what ONEOK is doing, 6 psig wellhead pressure to 30 psig to WTG (Tr. p. 97, lines 20-25). Comparing a fee reported for Anadarko's system to a fee charged on ONEOK's system is not equating fees for comparable services. Using the \$1.35 ignores the Commission's own finding: "The Commission agrees with Staff's articulation of the principle that the cost causer should be the cost payer." (Paragraph 45)

e. In fact, Staff notes on Page 4 of Post-Hearing Brief that in regards to non-OFS GG-1's "It is safe to assume that a very high percentage of the fee charged by these other gathering companies is for shipping gas all of the way to the processing plant which would require greater compression services than ONEOK is providing Merit." (Staff Post-Hearing Brief, p. 4). Therefore, just using the highest reported GG-1 fee as the upward boundary of a range of reasonableness is not appropriate.

2. In the testimony above, the range of high and low fees is so broad and so wide, \$0.02 to \$1.35, that you cannot use that range to establish a "range of reasonableness." The use of averages or weighted averages is necessary in order to establish a range of reasonableness rather than a range of high and low fees. Using a range of high and low fees gives the Commission unbridled discretion to take any number it wants without any accountability and is arbitrary and capricious. A more appropriate "range of reasonableness" is the average low and high for OFS systems and the average low and high for non-OFS systems as testified to by Merit and the Commission Staff and as presented to the Commission in the post-hearing briefs. By all measures, \$[REDACTED]/MCF is outside the range of reasonableness and should not be used to calculate a reasonable gathering fee even when it is reduced by \$[REDACTED]/MCF. The resulting \$[REDACTED]/MCF is also outside the "range of reasonableness" or at least at the highest end as demonstrated below.

a. Using Merit's GG-1 analysis, the range of reasonableness using average high and low fees would be somewhere between:

i. Non-OFS - \$0.29/MCF and \$0.59/MCF excluding compression and \$0.30/MCF and \$0.61/MCF including compression.

ii. OFS - \$0.37/MCF and \$0.61/MCF excluding compression and including compression - \$0.44/MCF and \$0.71/MCF.

b. Using KCC Staff's GG-1 analysis, the range using average high and low fees would be somewhere between:

i. Non-OFS - \$0.29/MCF and \$0.60/MCF.

ii. OFS - \$0.38/MCF and \$0.62/MCF

c. Even ONEOK's GG-1 analysis using average high and low fees yields:

i. Non-OFS - \$0.29/MCF and \$0.60/MCF excluding compression and \$0.31/MCF and \$0.62/MCF including compression.

ii. OFS - \$0.37/MCF and \$0.58/MCF excluding compression and \$0.46/MCF and \$0.71/MCF including compression.

3. Even the Commission noted the "\$[REDACTED]/MCF gathering fee does not fall within the range of high and low fees OFS charges other producers." (Paragraph No. 86)

4. Using the Commission's own cost causer – cost payer analysis stated in Paragraph 45 of the Order, Merit's gathering fees should be well below the high end of the range of reasonableness because it was clearly established Merit is a low user of compression. The

Commission Staff witness Bell stated: “Merit though, is in my investigation, a very low compression user.” (Tr. p. 26, lines 6-7) Further, it was testified on numerous occasions that ONEOK generally delivers Merit’s gas to WTG at normally 30 psig. (Tr. p. 97, lines 20-25) Even ONEOK’s witness Kyle Pearson’s prefiled testimony established that portions of ONEOK’s system deliver up to 102 psig. (Pearson Prefiled Testimony, p. 9, lines 14-19) Yet, ONEOK only delivers Merit’s gas to 30 psig. Again, ONEOK witness Pearson stated in his prefiled testimony that: “The largest operating maintenance costs on ONEOK’s system are compressor maintenance and operations.” As a low user of compression, Merit is a low “cost causer” of compression expenses and the gathering fee charged Merit should be commiserate: well below the upper bound of the “range of reasonableness.”

5. The Commission’s Order is also unlawful and contrary to the evidence and thereby arbitrary and capricious where it finds that: “Commission finds that the gathering fees in the existing contracts between Merit and OFS do not add much that is new for consideration beyond Factors 1 and 2 above. Subtracting the \$[REDACTED]/MCF from the offered fee of \$[REDACTED]/MCF or the average of \$[REDACTED] on OFS’ 51 renegotiated 2015 contracts with fees of \$0.68 and \$[REDACTED] respectively. These are very near the \$[REDACTED]/MCF currently in place with the 2007 OXY contract and \$[REDACTED]/MCF fee offered to Merit prior to this complaint proceeding.” (Paragraph 70) This finding illustrates the Commission’s fundamental misunderstanding as to the impact a few cents in gathering fees can have.

6. Contract No. 732769 (the contract in this docket) has approximately 5,000/MCF/d under it. (Collins Prefiled Testimony, p. 4, line 19) The \$[REDACTED]/MCF difference between \$0.68/MCF and \$[REDACTED]/MCF is equal to \$[REDACTED] in annual revenue. The \$0.13/MCF difference between \$[REDACTED]/MCF and ONEOK’s average fee of \$0.55/MCF according to their GG-

1's is \$237,250.00 in revenue annually. The \$0.23/MCF difference between \$0.68/MCF and the KCC Staff and Merit's suggestion of an appropriate rate of approximately \$0.45/MCF (Staff Post-Hearing Brief, p. 8; Merit Post-Hearing Brief, p. 29) is \$419,750.00 in revenue annually.

7. The findings in Paragraph 70 also ignore the impact these findings could have on Contract 432278, Merit's large gathering agreement which terminates on June 30, 2017, which has about [REDACTED]/MCF/d under it. (Collins Prefiled Testimony, p. 4, line 14.) The \$[REDACTED]/MCF difference between \$0.68/MCF and \$[REDACTED]/MCF is equal to \$[REDACTED] in annual revenue. The \$0.13/MCF difference between \$0.68/MCF and ONEOK's average fee of \$0.55/MCF according to their GG-1's is more than \$[REDACTED] in revenue annually. The \$0.23/MCF difference between \$0.68/MCF and KCC Staff and Merit's suggestion of an appropriate rate of approximately \$0.45/MCF is over \$[REDACTED] in revenue annually. The difference in pennies adds up to millions of dollars over the life of these contracts. Therefore, it is erroneous and contrary to the evidence to state: "These (\$0.68/MCF and \$[REDACTED]/MCF) are very near the \$[REDACTED]/MCF fee currently in place for the 2007 OXY contract and the \$[REDACTED]/MCF fee offered to Merit prior to this Complaint proceeding." (Paragraph No. 70)

8. The Commission's findings in Paragraph 33 are also unlawful, arbitrary and capricious. The Commission found that: "Merit produced no evidence that these Kansas producers were unable or unwilling to file complaints if they thought it necessary." The evidence before the Commission was that these agreements were not the result of negotiations in a competitive market as noted by both Merit (Merit Post-Hearing Brief, p. 5) and Staff witness Bell (Tr, Vol. 2, pp. 326-327, lines 22-3). Cross Exhibit No. 1 easily demonstrated that of the [REDACTED] contracts recently renegotiated by ONEOK, only [REDACTED] of the contracts besides Merit's had an average meter count of over [REDACTED]. Generally the contracts were for very small volumes with [REDACTED]

██████████ wells giving the producers no economic choice but to accept ONEOK's terms. (Tr. p. 175, lines 23-25) Further, the operators had no other option than to have their gas gathered on ONEOK's system. (Tr. p. 176, lines 7-8) It was further demonstrated that ONEOK's presentations highlighted their corporate strategy to increase fees and that that was one of their key goals. (See Exhibits 1, 2 and 5 of Collins Prefiled Testimony)

CONCLUSION

The Commission by picking a gathering fee of \$██████/MCF as the starting point for its analysis ignores that there is no basis in the record for that \$██████/MCF other than it lies between \$0.02/MCF and \$1.35/MCF. It further ignores the fact that \$██████/MCF is not even within the range of what OFS charges others. The Commission further failed to understand the significance even a few cents per MCF made on the operators and in doing so failed to set a fee within a range of reasonableness. At the very least, the Commission should have started with the \$██████/MCF, which represents the average fee under the 51 contracts, and then subtracted \$██████/MCF to yield \$██████/MCF as the fee to move Merit's gas from the wellhead to WTG (Merit Post-Hearing Brief, Paragraph 56).

For the Commission to outright dismiss the testimony as to the need for and the rationale for using averages to arrive at a range of reasonableness in which to determine a reasonable gathering fee is unlawful. Witnesses Bower, Collins and Bell all testified to the reasoning behind and the need for the use of averages in order to determine a range of reasonableness. The Commission further dismissed evidence that Merit is a low user of compression and hence a lower "cost causer," indicating the fee charged to Merit should be on the low end of the range of reasonableness. Based thereon, Merit felt that a reasonable gathering fee would be \$0.45/MCF

(Merit Post-Hearing Brief, Paragraph 81) and Staff Witness Bell felt a reasonable gathering fee would be \$0.44/MCF (Post-Hearing Brief of Commission Staff, p. 8); that was their recommendation in the record.

The fees recommended by Merit (\$0.45/MCF) and Staff (\$0.44/MCF) and even the \$[REDACTED]/MCF that ONEOK is charging other producers under the 51 agreements all generally fall within a range of reasonableness using GG-1 average high and average low fees to determine the upper and lower bounds. The fee of \$0.68/MCF ordered by the Commission is either outside of a range of reasonableness using average high and average low fees reported in the GG-1s, or approaches the upward boundary of the range, which ignores the evidence that Merit is a low cost causer, as a low user of compression.

WHEREFORE, Merit respectfully requests the Commission reconsider its Order of February 28, 2017, as to the specific issues of fact and law set forth herein.

Respectfully submitted,

MARTIN, PRINGLE, OLIVER,
WALLACE & BAUER, L.L.P.

By: /s/ Stanford J. Smith, Jr.
Jeff Kennedy, #12099
Stanford J. Smith, Jr., #11353
100 North Broadway, Suite 500
Wichita, KS 67202
Telephone: (316) 265-9311
Facsimile: (316) 265-2955
jkennedy@martinpringle.com
sjssmith@martinpringle.com
*Attorneys for Merit Energy Company and
Merit Hugoton, LP*

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing document was electronically filed with the Kansas Corporation Commission and e-mailed on this 15th day of March, 2017, to:

John G. McCannon, Esq.
Litigation Counsel
Kansas Corporation Commission
266 North Main, Suite 220
Wichita KS 67202
j.mccannon@kcc.ks.gov

David E. Bengtson, Esq.
STINSON LEONARD STREET LLP
1625 North Waterfront Parkway, Suite 300
Wichita, KS 67206-6620
david.bengtson@stinsonleonard.com

/s/ Stanford J. Smith, Jr.
Stanford J. Smith, Jr.