In the Matter of the Application of Kansas Gas Service, a Division of ONE Gas, Inc. for Adjustment of its Natural Gas Rates in the State of Kansas.	))))	Docket No. 18-KGSG-560 - RTS

DIRECT TESTIMONY

OF

MARK W. SMITH

ON BEHALF OF KANSAS GAS SERVICE

A DIVISION OF ONE GAS, INC.

(REDACTED)

DIRECT TESTIMONY

OF

MARK W. SMITH

ON BEHALF OF KANSAS GAS SERVICE

A DIVISION OF ONE GAS, INC.

I. Position and Qualifications

Q. Please state your name and business address.

A. My name is Mark W. Smith. My business address is 15 East Fifth Street in Tulsa, Oklahoma.

Q. By whom and in what capacity are you employed?

A. I am Vice President, Treasury for ONE Gas, Inc., (hereinafter the "Company," "ONE Gas" or "Kansas Gas Service").

Q. Please describe your educational background and professional experience.

A. I have a Bachelor's of Science in Accounting from Oklahoma State University and a Master's in Business Administration from Phillips University. I am also a CPA. I have testified in cases before the Oklahoma Corporation Commission, the Kansas Corporation Commission ("Commission"), Railroad Commission of Texas, and FERC. I previously served on the Southern Gas Association Rate Committee where I taught a portion of its Regulatory 101 course. I have worked for ONE Gas or ONEOK, Inc., ("ONEOK"), for over 31 years in areas that include Rates and Regulatory, Corporate Accounting, Budgeting, Corporate Development and Treasury.

II. Executive Summary

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to: (1) provide background information relating to ONE Gas' funding of pension costs; (2) provide background information relating to ONE Gas' approach to funding its pension obligations; (3) request the sharing of the savings generated by excess pension funding between our customers and the Company (IS Adjustment 28); and (4) discuss the formation of the Utility Insurance Company ("UIC") and the reasonableness of the premiums paid by Kansas Gas Service and ONE Gas that are included in the cost of service filed with this application.

III. <u>Pension and OPEB Trackers</u>

Q. Please provide a review of the background on Kansas Gas Service's accounting trackers for Pension and OPEB expenses.

A. On September 11, 2009, the Commission issued an Order in the Docket No. 10-KGSG-130-ACT ("130 Docket") allowing Kansas Gas Service to implement two trackers: one to track Pension and OPEB expense; the other to track Pension and OPEB funding.

Under tracker 1, Kansas Gas Service established a regulatory asset or regulatory liability to record the differences between current-year Pension/OPEB expenses (as calculated by generally accepted accounting principles ("GAAP")), and Pension/OPEB expenses included in rates. These regulatory assets and liabilities are amortized in rates on a straight-line basis over a multiple year period beginning with each new rate proceeding.

Under tracker 2, Kansas Gas Service tracks funding to the Pension and OPEB trusts that differ from GAAP costs. Any funding shortage is recorded as a regulatory liability and any overage is recorded as a regulatory asset.

Q. What are the current balances and the projected December 31, 2018 balances in Tracker 1 and Tracker 2 for the Company's pension and OPEB plans?

A. The projected December 31, 2018 balance in Tracker 1 for the Pension is $6.6 million and for OPEB is negative $9.7 million. The projected December 31, 2018 balance in Tracker 2, for the

Pension is $35.0 million and for OPEB is $26.5 million. The balance for each tracker is shown below and projected for 2018.

	Pension		OPEB	
	Tracker 1 Balance	Tracker 2 Balance	Tracker 1 Balance	Tracker 2 Balance
2009	2,485,323	20,774,025	840,344	881,600
2010	5,312,183	47,167,581	(465,812)	2,731,248
2011	9,590,906	60,193,743	(2,028,404)	5,165,171
2012	14,988,978	80,841,391	(3,052,421)	7,294,005
2013	15,720,082	68,409,753	(5,863,947)	8,983,978
2014	14,320,813	61,108,489	(8,752,056)	11,504,635
2015	14,839,291	51,889,477	(11,933,767)	16,269,825
2016	13,626,633	44,401,602	(16,046,800)	21,836,535
2017	9,256,091	44,706,425	(11,899,598)	22,981,390
2018	6,626,600	34,966,412	(9,686,960)	26,489,613

IV. Background Relating to Pension Funding

Q. What is the financial accounting standard applicable to pension plan expense?

A. The expense associated with the Company's pension plan is determined in accordance with the Financial Accounting Standard Board ("FASB") Financial Accounting Standard No. 87 (now codified as FASB Accounting Standards Codification Topic 715, Compensation – Retirement Benefits ("ASC Topic 715")).

Q. Is FASB a government entity?

A. No. FASB is an independent and private not-for-profit organization which establishes financial accounting and reporting standards for public and private companies and not-for-profit organizations which follow GAAP. The U.S. Securities and Exchange Commission has designated FASB as entity which sets the accounting standard for public companies.[1]

[1] *See generally*, About the FASB, http://www.fasb.org/facts/index.shtml (5-7-2018).

Q. What federal regulation, if any, govern pension plans?

A. Pension funding is regulated by both the 1974 Employee Retirement Income Security Act ("ERISA") and the 2006 Pension Protection Act ("PPA").[2] The ERISA sets minimum standards for most voluntarily established pension and health plans in private industry to provide protection for individuals participating in these plans.[3] Similarly, the goal of the PPA was to establish rules that would protect retirement accounts and hold companies accountable for providing sufficient funding for pension accounts. Specifically, as it relates to this matter, the PPA set the rules that are used to determine the minimum required cash contribution and the maximum deductible cash contribution for each year.

Q. How were pensions typically funded under ERISA?

A. Generally, as it relates to pension plan years earlier than 2008, ERISA established minimum pension funding requirements, designed to eliminate any projected unfunded liability over a 10-15-year period, meaning that a typical plan would be fully funded after 10-15 years (assuming no change in relevant variables such as interest rates, investment return, or demographics).

Q. Did the PPA change funding requirements? If so, how?

A. Yes. The PPA, which became effective with the 2008 plan year, established new minimum funding requirements for nearly all pension plans. The PPA requires a pension plan sponsor to annually contribute an amount equal to: (1) the benefits estimated to be earned for the current plan year; plus (2) an amount sufficient to eliminate any underfunding in seven years (not taking any other changes into effect). Since the PPA decreased the period for amortizing any unfunded liability, it significantly accelerated the required contributions to satisfy the

[2] The Pension Protection Act is available at http://www.dol.gov/ebsa/pensionreform.html.

[3] *See generally*, Employee Retirement Income Security Act (ERISA), https://www.dol.gov/general/topick/retirement/erisa (5-7-2018).

funding rules. While PPA and ERISA changed the pension rules for certain years after 2008, neither act has repealed the previous guidance or requirements.

Q. How has pension expense typically been determined for rate making purposes?

A. For ratemaking purposes, the accrual methodology set forth in ASC Topic 715 is used to calculate pension expense. This is also the methodology that is required to be used for financial reporting purposes under GAAP. ASC Topic 715 requires companies to accrue pension costs over the working life of each qualified employee. An annual calculation is required to determine the amount of pension expense that must be recognized for financial reporting purposes. The calculation considers the accumulated amount that should have been accrued at the present time for each participant, and requires several assumptions to be made, including the age at which active employees are likely to retire, the expected future return on pension plan assets, future payroll levels, an appropriate discount rate, and other factors. In addition, certain gains and losses are amortized over a multi-year period. This amortization helps to mitigate significant fluctuations that can occur from year-to-year in pension plan investment earnings. Thus, the calculation of the pension expense is a snapshot at a point in time. The pension expense is impacted by what has happened in the past, as well as, what is expected to happen in the future. In addition, there is a gradual true-up of past estimates with actual results over time.

V. <u>ONE Gas' Approach to Funding Its Pension Obligations</u>

Q. How does ONE Gas determine how much is required to be contributed annually to its pension plan?

A. ONE Gas relies on third-party actuaries to calculate the level of funding required under the PPA. ONE Gas generally contributes the amount required by the PPA, however, in some years it has been prudent to fund more than this amount. Once the plan becomes fully funded, the required contribution will simply be the benefits expected to be earned in the coming year.

Q. Does the Company have a targeted funding percentage and if so, what is the rationale behind the targeted funding percentage?

A. Yes, the Company has a targeted funding percentage. At a minimum, the Company targets the plan funding to ensure plan assets equal at least 80% of the plan's liability. This is a prudent approach because a failure to fund at least 80% of the plan's liability may result in benefit limitations, prohibition of lump sum payments, cessation of benefit accruals and restrictions on plan amendments. Specifically, under the PPA, a plan may become subject to various benefit limitations if its Adjusted Funding Target Attainment Percentage ("AFTAP") falls below certain thresholds. Consequently, certain financial and actuarial information (i.e., a "4010 filing") must be provided to the Pension Benefit Guarantee Committee ("PBGC") if the Funding Target Attainment Percentage ("FTAP") is less than 80% for any large plan in the contributing sponsor's controlled group.

Q. Please explain what "at risk" status means and the consequence of being deemed "at risk."

"At-Risk Status for Determining Minimum Required Contributions" is defined in the PPA. A plan is in At-Risk Status for the plan year under review, if the plan's FTAP for the preceding plan year was less than 80% of the plan's liabilities and when the plan's FTAP as measured using certain "at-risk assumptions" is found to be less than 70% of liabilities. Additionally, when a plan's status drops to At-Risk, its PBGC premiums are increased and the overall cost of the plan increases.

Q. How do the different funding requirements and targets lead to the creation of a prepaid asset for ONE Gas even when the pension plan is not fully funded?

A. While a plan may not be fully funded, it is still possible for a company to fund an amount more than what it has expensed. In ONE Gas' case, it has funded more than it has expensed.

The difference between total cumulative contributions made to the pension trust and the cumulative ASC Topic 715 expense as recognized at a specific point in time, equals either a prepaid pension asset or an accrued pension liability. Historically, ONE Gas contributions have exceeded ASC Topic 715 expense resulting in a prepaid pension asset.

In addition to ASC Topic 715 expense, ONE Gas accounts for the funded status of its pension plan and the amount of unrecognized pension expense on its financial statements. Over the life of a pension plan, the prepaid pension asset will naturally go to zero, so if at any point in time a prepaid pension asset exists, then it means that cash contributions to the plan exceeded ASC Topic 715 pension expense.

Additionally, IRS minimum required contributions (as spelled out by the PPA), and ASC Topic 715 expense are not the same and are not designed to be the same. ASC Topic 715 expense is leveled out over time. However, required minimum payments (i.e., contributions) to pension plan funds are often significantly different than the ASC Topic 715 expense in any given year.

Q. What actions are taken to ensure that the pension is not overfunded to the detriment of customers and that future volatility is reduced?

A. ONE Gas has undertaken a Liability Driven Investment Strategy ("LDIS") with a "glide path" to obtain a less volatile investment objective. The glide path simply moves more of the assets into fixed income with maturities that match plan liabilities as the plan becomes better funded, thus reducing risk to the plan. This strategy will result in the plan assets moving in tandem with the liability as interest rates go up and down, creating less volatility and fluctuation in the overall annual expense. The value of an LDIS is the assurance that assets are not over-exposed to equity markets that would require the Company and/or customers to make large future fundings.

Q. How was the prepaid pension asset originally funded?

A. The source of funding each year was initially cash on hand, which was replaced ultimately with long-term debt and equity.

Q. Do you believe it is prudent to fund pension obligations in a manner that may create a prepaid pension asset?

A. Yes. Funding the pension obligations in a manner that temporarily creates a prepaid pension asset is prudent because it avoids the negative (and costly) consequences of underfunding the plan and putting the plan into an At-Risk status, either intentionally or inadvertently through failure to build sufficient cushion into actuarially determined estimates. Moreover, the prefunding reduces future pension expense and costs such as the PBGC premium.

Q. How have other jurisdictions treated prepaid pension assets?

A. Many utilities in several states such as in the District of Columbia, Michigan, New York, Ohio, Oklahoma, and Texas, have been allowed to earn a "return of" and a "return on" the prepaid pension asset. In an Oregon Public Utility Commission Pension Survey, 16 commissions reported that they recognize a "Prepaid Pension Asset/Liability" and allow "a return on amount invested in asset." An additional three commissions reported that they include cash contributions in "Working Capital," and six other commissions used a "Combination of Methods." Of those using multiple methods, several commissions mentioned including pension asset in rate base, or otherwise permitting the utility to earn a return on the asset.

For example, Texas has a tracker similar to that in place in Kansas and allows a return on the Prepaid Pension Asset.

VI. <u>Kansas Gas Service's Proposal to Share Savings Related to Pension Expenses Between Customers and the Company</u>

Q. What savings are the Kansas Gas Service customers realizing because of pension expenses being funded in excess of expense by the Company?

A. The customers are benefiting from lower pension and OPEB expense from the Company's prefunding. The prefunding of pension and OPEB expense was $67.7 million at the end of 2017 and is projected to be $61.5 million at the end of 2018. The expected savings for 2018 is $5.0 million, based on the December 2017 prefunded amount. The expected savings is calculated by multiplying the Tracker 2 Balance by the earnings rate:

Tracker 2 Balance	x	Earnings Rate	=	Expected Savings
$67,687,815	x	7.37%	=	$4,987,801

The cumulative savings since 2009 (inclusive of the 2018 projected prefunding amounts) has been $46.3 million for Kansas Gas Service customers. The benefit realized by the customers is detailed in the following illustration, by year:

	Tracker 2 Balance	Earnings Rate	Annual Benefit to Customers	
2009	21,655,625	8.50%	2010	$1,840,728
2010	49,898,828	8.50%	2011	$4,241,400
2011	65,358,914	8.50%	2012	$5,555,508
2012	88,135,397	8.50%	2013	$7,491,509
2013	77,393,732	8.00%	2014	$6,191,499
2014	72,613,125	7.75%	2015	$5,627,517
2015	68,159,303	7.75%	2016	$5,282,346
2016	66,238,138	7.75%	2017	$5,133,456
2017	67,687,815	7.37%	2018	$4,987,801

Q. Has the Company been formally precluded from recovering a return on the prepaid asset balance?

A. Yes, in Docket No. 10-KGSG-130-ACT, ("130 Docket") the Commission issued a ruling prohibiting the Company from recovering a return on investments in its pension plans. The purpose of the prohibition was to ensure the Company could not collect more from customers than it contributed to the pension plan. I am not sure that an overfunding scenario was ever considered at that time, because pension plans had lost billions of dollars in the market drop related to the financial crisis.

Q. Why are you now proposing a sharing of the savings between customers and the Company?

A. At the time the Order was issued in the 130 Docket, the idea of the pension plan being funded to the level that ONE Gas has funded in excess of ASC Topic 715 expense was not anticipated. Also, at the time, it was expected that the regulatory asset or liability would not have a cash impact. We now know that it has had a cash impact to the Company and that the savings generated have been a significant benefit to the customers. The Company has invested funds in the pension and OPEB in a manner which have resulted in a benefit to our customers. Because the benefit from the investments in the pension assets is similar in nature to the Company's investment in its pipelines, and because the benefit is calculable, the Company believes this request is reasonable.

Q. What is the level of sharing of the savings you are proposing?

A. Given the benefit customers have received thus far, I am proposing that the Company be allowed to share the savings with the customers, with two-thirds of the benefit going to the Company and one-third of the savings going to the customers. IS Adjustment 28 included in this filing increases pro forma expenses by $3,325,367 to reflect two-thirds of the savings generated by funding more than that required by the Commission.

VII. Utility Insurance Company

Q. Has ONE Gas recently formed a wholly-owned subsidiary referred to as "Utility Insurance Company" to provide certain insurance coverage to KGS?

A. Yes. I will describe the ONE Gas risk management program and the services provided to KGS by Utility Insurance Company ("UIC"), ONE Gas' captive insurer. I will also explain why the insurance rates paid by KGS to UIC are reasonable and necessary. Also, I am sponsoring several exhibits. Exhibit MWS-1 summarizes the UIC insurance expense charged to KGS and the change in direct insurance cost inclusive of lower deductible limits. Exhibit MWS-2 is the UIC license approval from the Oklahoma Insurance Commission ("OIC"). Confidential Exhibits MWS-3, MWS-4, MWS-5, MWS-6 and MWS-7 are the policies issued by UIC to KGS. Exhibit MWS-8 is a study filed with the OIC.

Q. What is a captive insurance company?

A. A captive or captive insurance company is a company formed by a corporation to provide insurance to its divisions and subsidiaries. Captives are regulated insurance companies that must follow the insurance laws of the state in which they were incorporated and file annually with their respective insurance commissions.

Q. Why was UIC formed?

A. UIC was formed to provide ONE Gas' divisions in Kansas, Oklahoma and Texas and ONE Gas:

1) consistent and competitive insurance rates over the long-term;

2) continuity of insurance product offerings at a cost that is considerably lower than what ONE Gas could achieve if it sought insurance in the general marketplace;

3) insurance at lower deductible levels than can be purchased in the retail market; and

4) reinsurance in the wholesale market.

Q. Regarding item four above, why is it important that UIC can purchase reinsurance in the wholesale market?

A. The retail market will often not write insurance with low deductibles. In almost all the cases in the past, ONE Gas has had to obtain insurance containing a $2 million deductible. There have been several instances where the retail insurance market has pushed for a $5 million deductible. These high levels of deductibles result in the company and our customers being exposed to significant financial losses as the Company must incur large claims prior to deductibles being met. Additionally, buying in the wholesale market eliminates a premium tax which can be as much as $400,000 for ONE Gas in total.

Q. Does UIC have the potential to smooth out premium costs over the long term?

A. Yes, it does. In the general marketplace, rates fluctuate due to overall market conditions and events that are out of ONE Gas' control such as tornadoes, hurricanes, terrorist attacks or other companies inside or outside of our industry suffering significant liability events. In contrast, UIC will be able to look at premiums over a longer period and prevent spikes from happening in the short term.

Q. Please describe reinsurance and the reinsurance market.

A. The reinsurance market is a market that sells insurance to insurance companies or the retail market. In effect, it is the wholesale market for insurance and companies typically buy from the retail market. Because UIC is a regulated insurance company, UIC allows ONE Gas access to reinsurance markets directly versus going through the retail insurance markets where rates include profit, commissions, overhead, taxes and other transactional costs that can significantly increase premiums. By having the option to access the reinsurance markets directly, UIC can obtain lower rates, customize policy language, and secure additional insurance by either lowering the deductibles or raising insurance limits. This ensures competitive and consistent rates for KGS. Reinsurance markets are much more stable than retail markets and should result in more favorable rates over the long-term.

Q. Please briefly describe UIC and how it fits into ONE Gas' corporate structure.

A. UIC was chartered in Oklahoma on August 29, 2017, and was operational as of October 1, 2017. UIC is a wholly-owned subsidiary of ONE Gas and is incorporated under Oklahoma's laws and regulations. It is fully capitalized under the requirements of applicable Oklahoma law, as required by the OIC, and does not provide services to any entity other than ONE Gas and its divisions.

Q. How are the operations of UIC managed?

A. UIC is managed on a day-to-day basis by Aon Risk Solutions, ("Aon"), a third-party captive manager. Aon is one of the largest third-party risk management consulting firms in the world and has a team of individuals who specialize in the management, regulation, and uses for captive insurance companies and their owners. The main differentiator of a captive insurance company and a common insurance company is that a captive will write only the risks of its parent, namely ONE Gas. Captives can also write third party risks but currently UIC is responsible for the risks of ONE Gas and its operating divisions only.

In addition to providing management services for the daily operations of UIC, Aon provides the Company with consultation services regarding insurable risks, coverage, and other related services. However, the direction and philosophy of UIC is determined by UIC's board and the ONE Gas risk management group, which reports to me. Importantly, the OIC has oversight and governs the rates and capitalization of UIC. Attached as Exhibit MSW-2 is a document approving UIC's original rates and approving UIC as an insurance company. UIC's initial annual filing is now under review by the OIC.

Q. Do the premiums charged to KGS include insurance coverage for corporate assets of ONE Gas?

A. No, not directly. Corporate is charged its own appropriate premium based on its assets and risks. This Corporate insurance expense is allocated through Distrigas to each division, including KGS, as described by Ms. Davidson.

Q. What types of insurance coverage does UIC provide for ONE Gas' KGS division?

A. UIC provides the following insurance coverages for KGS:

1) property, plant, and equipment, including business interruption;

2) general liability and employment practices;

3) workers' compensation and employers' liability; and

4) automobile liability.

Copies of these policies are attached as Exhibit MWS-3 through Exhibit MWS-7.

Q. Can you describe the nature of the coverage provided by UIC to KGS.

A. Yes. KGS receives insurance coverage for an amount that is equal to or in excess of $25 million per event, as well as at least $25 million in terrorism coverage, with a $250,000 deductible per occurrence for each type of policy listed above. This deductible is much lower than what is available in the retail insurance markets for companies the size of ONE Gas and is offered at rates based on each division's loss history. As an example, liability insurance could not be purchased in the retail marketplace with a deductible below $1 million.

Q. You stated that UIC provides insurance coverage that is not commercially available at the UIC deductible level and UIC pricing. What do you rely on to support this statement?

A. As insurance risks are renewed for an annual term, ONE Gas has attempted to obtain lower deductibles. For example, in the case of liability insurance, insurers would only provide quotes down to a $1 million deductible level, and in some cases, would not provide a quote for a deductible lower than $2 million. In some cases, insurers have pushed for a higher deductible. In one instance, to lower the liability deductible to $1 million from $2 million, the annual premium would increase by $1.2 million. Similar circumstances have occurred in the areas of property and auto insurance. We recently asked our lead property insurance carrier to provide a quote with a $250,000 deductible, and they refused to do so.

Q. Explain how the cost of obtaining the insurance coverage for KGS and its peer divisions through UIC is determined.

A. UIC bases premiums on a long-term time horizon, consistent with the industry-accepted approach for captives. This approach recognizes that there will be periods when losses are less than forecasted and periods when losses are greater than forecasted. The price paid to UIC by KGS and its peer divisions (Oklahoma Natural Gas, Texas Gas Service, ONE Gas Corporate) is determined using several factors and based upon the advice and actuarial services of Aon. These factors are:

1) administrative fees;

2) cost of reinsurance premiums;

3) reserve requirements;

4) loss history; and

5) projected losses for all the various policies.

The administrative fees and cost of reinsurance premiums are paid by UIC directly to non-affiliated third parties and are included within the overall premium charged to KGS by UIC at cost without mark-up.

Q. What are some of the major drivers in setting the costs of the premiums?

A. The major drivers for the cost of premiums are for:

1) property insurance is the replacement value of the assets being insured and the potential business interruption or net margins of the division;

2) workers' compensation insurance is the salary and number of employees in a division;

3) automotive insurance is the number of vehicles that each division is operating; and

4) liability insurance is net margins, the number of customers, the value of the assets deployed, the age of the assets used, and the number of employees.

These potential risk factors are updated annually, along with loss histories for each type of coverage, and Aon provides actuarial services to determine the rates just as any insurance company would do for its clients. These rates and actuarial study are then filed with the OIC for their review and approval. I have attached Confidential Exhibit MWS-7, which is the feasibility study included in the original application filed with the OIC. Any amount of reinsurance that UIC purchases is allocated at cost based on the annual premiums being charged for that type of coverage.

Q. Does the long-term forecast method of determining premium costs benefit KGS and its customers?

A. Yes. Over the long-term, these forecasts provide KGS with more consistency in the premium cost to be incurred. Insurance costs are a necessary part of providing natural gas service. To the extent the costs significantly vary from year to year, based on an annual review of the actual losses incurred, the rates charged to customers would experience more variance in the general market. For example, there were large Texas property losses caused by hurricanes last year. Premiums based solely on those losses from that year would be markedly higher than premiums based on a longer time horizon. In addition to cost variances, after major catastrophic events, there can be contraction in insurance availability. Through UIC, KGS and its customers are assured of the availability of the same level of insurance coverage at relatively consistent premium costs without being subjected to the inevitable insurance cycles. Further, having a relatively stable premium rate allows the utility to plan with greater certainty the investment necessary to ensure a safe and reliable system.

Q. How are the charges to KGS from UIC determined?

A. The actual amount of the premium charged is based on different factors such as property replacement values, employee count, net margins, the number of autos, and loss history for each division, and will vary depending on the type of coverage. UIC uses actuarial services of Aon to develop risk based premiums as previously explained. If a division's property replacement values are greater than that of another utility division, then the division with the greater amount will bear more of the total premium cost charged by UIC. This is also the case for losses. If the loss history is greater in one division, that division will bear a larger premium. We think this is important as it prevents one division from subsidizing another division which may have higher losses. If we just used plant values, for example, there would be no premium incentive for the divisions to take actions to avoid losses. Specifically, Aon provides a quantification of the potential exposure under the various risks by producing a forecast for the upcoming policy year. The analysis is based on ONE Gas and its divisions' own loss experience with actuarial adjustments to account for the nature of the claims, the development of claims, the underlying loss cost trends and changes in exposure. This risk-based approach more appropriately allocates the cost to each of ONE Gas' divisions and corporate office than a simple rate multiplied by an employee count or rate multiplied by an asset value.

Q. Is the price charged to KGS by UIC higher than the price charged by UIC to other divisions, affiliates or third parties for the same item or class of items?

A. No. On a risk-adjusted basis, the price charged by UIC to KGS is no higher than what is charged to ONE Gas' other divisions. The same types of underlying costs and methodology are employed in calculating each division's premium.

Q. Does UIC provide insurance coverage to any third parties?

A. No, UIC only insures ONE Gas and its divisions. In the future, UIC may add risks such as medical stop loss, employee life insurance, and employee medical insurance, but only for our employees. There are no plans to insure third parties outside of ONE Gas, it's divisions and subsidiaries and their dependents/families.

Q. Are the UIC costs paid by KGS reasonable and necessary?

A. Yes, buying appropriate levels of insurance is a necessary expense to prevent catastrophic events from negatively impacting the Company and to make sure that expenses are consistent and do not spike and dip from year to year. This is true for both KGS assets that are insured through UIC for which UIC charges KGS a premium and for UIC's coverage of ONE Gas corporate assets. Ms. Davidson and Mr. Goad sponsor the schedule that shows the amount of corporate costs for ONE Gas assets that KGS is seeking to recover through rates.

Q. Does this conclude your direct testimony?

A. Yes, it does.

VERIFICATION

STATE OF OKLAHOMA)
) ss.
COUNTY OF TULSA)

Mark W. Smith, being duly sworn upon his oath, deposes and states that he is Vice President Treasury for 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.

Mark W. Smith

Mark W. Smith

Subscribed and sworn to before me this 1 day of June 2018.

Kathleen Hill

NOTARY PUBLIC

My appointment Expires:

01/13/22

KATHLEEN HILL
NOTARY
14000359
EXP. 01/13/22
PUBLIC
STATE OF OKLAHOMA

Kansas Gas Service
Exhibit MWS-1
Summary of direct Insurance cost

Type of Insurance	Annual Premiums Paid to UIC	Deductible	Coverage
Property, plant, and equipment, which includes business interruption	$ 517,336	$ 250,000	> $25 million
General liability and employment practices	$ 1,510,107	$ 250,000	> $25 million
Workers' compensation and employers' liability	$ 133,509	$ 250,000	Statutory
Automobile liability	$ 2,622	$ 250,000	> $2 million
Total	$ 2,163,574		

GOVERNOR
MARY FALLIN

INSURANCE COMMISSIONER
JOHN D. DOAK

OKLAHOMA INSURANCE DEPARTMENT
STATE OF OKLAHOMA

October 26, 2017

BILL MOURELATOS
76 ST PAUL ST STE 500
BURLINGTON, VT 05401

Re: Approved License
Utility Insurance Company, Inc., OK License #502253624

Dear Mr. Mourelatos:

My staff and I welcome the above referenced company into the State of Oklahoma. Enclosed please find the company's Certificate of Authority as an authorized Pure Captive.

If you are ever in Oklahoma City, we invite you to come into our offices to get acquainted.

Sincerely,

John D. Doak

John D. Doak
Insurance Commissioner

Oklahoma License #: 502253624

NAIC #:

State of Oklahoma

Oklahoma Insurance
3625 NW 56th Street, Suite 100
Oklahoma City, Oklahoma 73112

Whereas, the **UTILITY INSURANCE COMPANY, INC.**, a company organized under the laws of **Oklahoma** and located at 15 E FIFTH ST, TULSA, OK, 74103, having complied with the applicable laws of Oklahoma, is hereby licensed and authorized to transact the business of:

Casualty (including vehicle)

Property

This Certificate of Authority shall be perpetual and automatically renewed as of March 1st of every year, unless the company fails to qualify for renewal pursuant to the requirements of Title 36 of the Oklahoma Insurance Code.

IN TESTIMONY WHEREOF, I have hereunto set my Hand and affixed the Official Seal of the Insurance Commissioner at the City of Oklahoma City, State of Oklahoma, this 24th day of October, 2017.

John D. Doak
Insurance Commissioner
State of Oklahoma Insurance Department

In the Matter of the Application of Kansas Gas Service, a Division of ONE Gas, Inc. for Adjustment of its Natural Gas Rates in the State of Kansas.	))))	Docket No. 18-KGSG-____ - RTS

CONFIDENTIAL

EXHIBIT MWS-3

REDACTED

In the Matter of the Application of Kansas Gas Service, a Division of ONE Gas, Inc. for Adjustment of its Natural Gas Rates in the State of Kansas.	))))	Docket No. 18-KGSG-____ - RTS

CONFIDENTIAL

EXHIBIT MWS-4

REDACTED

In the Matter of the Application of Kansas Gas Service, a Division of ONE Gas, Inc. for Adjustment of its Natural Gas Rates in the State of Kansas.	))))	Docket No. 18-KGSG-____ - RTS

CONFIDENTIAL

EXHIBIT MWS-5

<u>REDACTED</u>

In the Matter of the Application of Kansas Gas Service, a Division of ONE Gas, Inc. for Adjustment of its Natural Gas Rates in the State of Kansas.	))))	Docket No. 18-KGSG-____ - RTS

CONFIDENTIAL

EXHIBIT MWS-6

REDACTED

In the Matter of the Application of Kansas Gas Service, a Division of ONE Gas, Inc. for Adjustment of its Natural Gas Rates in the State of Kansas.	))))	Docket No. 18-KGSG-____ - RTS

CONFIDENTIAL

EXHIBIT MWS-7

<u>REDACTED</u>

In the Matter of the Application of Kansas Gas Service, a Division of ONE Gas, Inc. for Adjustment of its Natural Gas Rates in the State of Kansas.	))))	Docket No. 18-KGSG-____ - RTS

CONFIDENTIAL

EXHIBIT MWS-8

REDACTED