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Kansas Corporation Commission
Patrice Peterson-Klein

BEFORE THE CORPORATION COMMISSION

OF THE STATE OF KANSAS

OCT 26 2012

by
State Corporation Commission
of Kansas

IN THE MATTER OF THE APPLICATION]
OF KANSAS GAS SERVICE, A DIVISION]
OF ONEOK, INC., FOR ADJUSTMENT]
OF ITS NATURAL GAS RATES IN THE]
STATE OF KANSAS]

KCC Docket No. 12-KGSG-835-RTS

TESTIMONY IN SUPPORT OF SETTLEMENT

ANDREA C. CRANE

ON BEHALF OF

THE CITIZENS' UTILITY RATEPAYER BOARD

October 26, 2012

1 **Q. Please state your name and business address.**

2 A. My name is Andrea C. Crane and my business address is 90 Grove Street, Suite 211
3 Ridgefield, Connecticut 06877. (Mailing address: P.O. Box 820, Georgetown, CT
4 06829).

5
6 **Q. Did you previously file testimony in this case?**

7 A. Yes, on September 24, 2012, I filed Direct Testimony on revenue requirement and certain
8 policy issues on behalf of the Citizens' Utility Ratepayer Board ("CURB"). In that
9 testimony, I recommended that the Kansas Corporation Commission ("KCC") approve a
10 rate increase of \$14,253,365 for Kansas Gas Service ("KGS" or "Company"). In
11 addition, I recommended that the KCC reject the Company's request to implement a
12 Revenue Normalization Adjustment ("RNA") rider. Testimony on behalf of CURB was
13 also filed by Dr. J. Randall Woolridge and by Brian Kalcic. Dr. Woolridge's Direct
14 Testimony addressed cost of capital and capital structure issues. Mr. Kalcic's Direct
15 Testimony addressed class cost of service and rate design issues.

16

17 **Q. Since your Direct Testimony was filed, have the parties engaged in settlement**
18 **discussions?**

19 A. Yes, the parties to this case have engaged in subsequent settlement discussions. As a
20 result, the parties filed a Joint Motion on October 26, 2012, requesting approval of a
21 Stipulation and Agreement ("S&A") to resolve the issues in this case.

22

1 **Q. Can you please summarize the terms of the S&A?**

2 A. The S&A provides for a base rate increase of \$28.0 million, \$6.4 million of which will be
3 collected from non-residential customers. While the parties did not agree upon a specific
4 authorized return on equity, the S&A states that a pre-tax overall return of 10.6% will be
5 used for purposes of quantifying the Company's Gas Service Reliability Surcharge
6 ("GSRS") rider. The S&A includes a five-year amortization period for deferred pension
7 and other post-employment benefit ("OPEB") costs, as well as a five-year amortization
8 period for rate case costs. Pursuant to the S&A, the Company will utilize the
9 depreciation rates proposed by Staff witness William Dunkel, although the Company has
10 not agreed to the principles underlying those rates and is free to raise issues with regard
11 to depreciation methodologies in future cases.

12 The S&A identifies the base levels of pension and OPEB expenses that will be
13 used as the basis for future deferrals. In addition, the S&A identifies the base level of ad
14 valorem taxes that will be used as the basis for future Ad Valorem Tax Surcharges. The
15 S&A also provides that the RNA will not be implemented. Other provisions of the S&A
16 include some revisions to the methodology used to calculate the Weather Normalization
17 Adjustment ("WNA").

18 Finally, the S&A includes the specific tariff rates that will implemented if the
19 S&A is approved by the KCC, including a monthly service charge for residential
20 customers of \$15.35 per month.

21

22

1 **Q. Are you familiar with the standards used by the KCC to evaluate a settlement that**
2 **is proposed to the Commission?**

3 A. Yes, I am. The KCC has adopted five guidelines for use in evaluating settlement
4 agreements. These include: (1) Has each party had an opportunity to be heard on its
5 reasons for opposing the settlement? (2) Is the agreement supported by substantial
6 evidence in the record as a whole? (3) Does the agreement conform to applicable law? (4)
7 Will the agreement result in just and reasonable rates? (5) Are the results of the
8 agreement in the public interest, including the interests of customers represented by any
9 party not consenting to the agreement?

10 I understand that CURB counsel will address item 3, i.e., does the agreement
11 conform to applicable law, in her opening statement at the upcoming hearing. Since I am
12 not an attorney, it is more appropriate for CURB counsel to address this issue than for me
13 to address it. However, I will discuss the remaining four guidelines.

14
15 **Q. Has each party had an opportunity to be heard on its reasons for opposing the**
16 **settlement?**

17 A. I participated personally in settlement negotiations in this case and each party had a full
18 and complete opportunity to be heard. Constellation opted not to participate. The parties
19 discussed issues, resolved certain numerical discrepancies, and negotiated aggressively.
20 At this time, I am not aware of any party to the case who opposes the settlement.

21
22 **Q. Is the agreement supported by substantial evidence in the record as a whole?**

1 A. Yes, it is. As noted in the S&A, the Company requested a rate increase of \$50,707,852,
2 which was revised to \$48,806,972 in its Rebuttal Testimony. CURB recommended a rate
3 increase of \$14,253,377 and Staff recommended a rate increase of \$14,469,378.
4 Therefore, the negotiated rate increase of \$28.0 million represents a substantial reduction
5 from the amount requested in KGS's original filing. While the proposed increase is
6 higher than the amounts recommended by Staff and CURB, all parties had litigation risk
7 that was taken into account as the S&A was negotiated.

8 The direct testimonies of the parties in this case included a wide range of capital
9 structures, ranging from the Company's claim of 58.85% equity to Staff's recommended
10 equity ratio of 45.59%. In addition, the return on equity recommendations ranged from
11 the Company's claim of 10.75% to CURB's recommended 8.5%. Given the fact that the
12 return on equity has a greater impact as the percentage of equity in the capital structure
13 increases, there was a very wide range of outcomes possible if the case had been fully
14 litigated. The parties were not able to agree on a stated return on equity, but they were
15 able to agree on a pre-tax cost of capital of 10.6% to be used for purposes of establishing
16 the next GSRS. It is impossible to impute a cost of equity to this pre-tax cost of capital
17 without knowing the underlying capital structure. For illustrative purposes, if one
18 utilized CURB's recommended capital structure consisting of 50% debt and 50% equity,
19 a pre-tax cost of capital of 10.6% would imply a cost of equity of just under 9.6%, well
20 below the Company's requested 10.75%. Moreover, the pre-tax cost of capital utilized in
21 the Company's current GSRS rate is 11.87%. Thus, the S&A will result in a significant
22 reduction in the pre-tax cost of capital used in the GSRS and CURB therefore believes

1 that the pre-tax cost of capital identified in the S&A is reasonable for purposes of
2 establishing a new GSRS.

3 After cost of capital and capital structure issues, the most significant accounting
4 adjustment in CURB's testimony related to incentive compensation costs. Staff had also
5 recommended a significant adjustment relating to incentive compensation in its
6 testimony. While the S&A does not identify the resolution of any specific accounting
7 issues, other than amortizations that are required to be specified by the Company's
8 auditors, CURB believes that the issue of incentive compensation has been reasonably
9 addressed in the proposed \$28 million increase. Moreover, the S&A reflects the five-
10 year amortization of deferred pension and OPEB costs recommended by both Staff and
11 CURB. The S&A also includes the withdrawal of the RNA, as proposed by CURB. As
12 stated in my Direct Testimony, CURB's position is that the RNA is unnecessary and
13 would transfer risk from shareholders to ratepayers without any commensurate ratepayer
14 benefit. Therefore, CURB views withdrawal of the RNA as a major provision of the
15 S&A.

16 Given that the proposed increase is between the amount requested by the
17 Company and the amounts recommended by Staff and CURB, given the range of possible
18 outcomes depending upon the capital structure and cost of equity issues, and given the
19 elimination of the RNA, the proposed increase of \$28.0 million represents a reasonable
20 compromise based on the evidence in the record in this case.

21
22 **Q. Will the agreement result in just and reasonable rates?**

1 A. Yes, I believe that the S&A will result in just and reasonable rates. As discussed above,
2 the revenue increase included in the S&A is substantially less than the amount requested
3 by KGS. In addition, the settlement rates allocate a portion of that increase to non-
4 residential customers, so the rate increase will be spread among a larger base than
5 originally proposed by KGS. Moreover, approximately \$10.9 million of the increase
6 reflects a transfer of costs that are currently being collected through the GSRS, so that
7 portion of the increase will be revenue neutral since there will be an immediate offsetting
8 decrease in the GSRS. Finally, the S&A results in a customer charge for residential
9 customers of \$15.35 per month, significantly less than the \$19.25 charge requested by
10 KGS in its filing. Given these factors, I believe that the settlement will result in just and
11 reasonable rates.

12

13 **Q. Are the results of the agreement in the public interest, including the interests of**
14 **customers represented by any party not consenting to the agreement?**

15 A. As noted above, all parties to this proceeding support the S&A. Therefore, the interests
16 of customers represented by all parties to this proceeding have been considered. This
17 agreement is in the public interest. It results in a revenue increase that is approximately
18 55.2% of the increase requested by KGS. It significantly reduces the carrying costs that
19 will be charged to ratepayers through the Company's GSRS. And it preserves the
20 integrity of the regulatory process by eliminating the Company's proposed RNA.
21 Approval of the S&A will also reduce rate case costs, which would otherwise be passed
22 on to ratepayers.

1

2 **Q. What do you recommend?**

3 A. I recommend that the KCC find that the S&A is supported by substantial evidence in the
4 record, will result in just and reasonable rates, and is in the public interest. Therefore, I
5 recommend that the KCC approve the S&A as filed.

6

7 **Q. Does this conclude your testimony?**

8 A. Yes, it does.

CERTIFICATE OF SERVICE

12-KGSG-835-RTS

I, the undersigned, hereby certify that a true and correct copy of the above and foregoing document was served by electronic service on this 26th day of October, 2012, to the following parties who have waived receipt of follow-up hard copies:

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