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Before the Senate Utilities Committee
Comments by the
Staff of the Kansas Corporation Commission
March 9, 2006
Senate Bill 576

Thank you Mr. Chair and members of the Committee. I am Leo Haynos, Chief of Pipeline Safety for the Kansas Corporation Commission and I am appearing today on behalf of the KCC Staff. In my testimony today, I would like to address the fiscal impact of the proposed bill as well as provide some background of the current proceedings before the Commission directly related to this bill.

Under SB 576, The Commission would be given limited jurisdiction over gas transportation on a gathering system and limited jurisdiction over the right of access to interconnections on a gathering system. The jurisdiction conferred on the KCC would consist of the ability of the Commission to review any practices related to offering gas gathering services, transportation services, or access to the facilities and to determine if the practices are discriminatory or unduly preferential. Currently, the statute only gives the Commission authority to review gas gathering services. The fiscal impact of granting the Commission additional jurisdiction over transportation services, or questions of access to the gathering system is significant. It is difficult

to forecast the use of a complaint based system, However, the practical consequence of this bill would be the allowance of any interested party to petition the Commission regarding denial of access. A review of the operational concerns could be complicated given the dynamics of a gathering system and resolution of a complaint could be a lengthy process. While current law (K.S.A. 66-1502) allows utilities to be assessed costs for Commission investigations and K.S.A. 55-176 allows operators to be assessed costs for Commission investigations, there is no mechanism to assess costs to the individuals who bring a complaint under Chapter 55 who are not operators of wells or gathering systems.

At this time, the Commission has open a general investigation under docket number 06-GIMG-400-GIG that is examining the facts surrounding the operation of gas gathering systems, and the residential and agricultural consumption of gas delivered directly from gas gathering systems. In this docket, the Commission is requesting input from the affected parties on the obligations established under Kansas Law that affect the rights of the various parties. The laws in question are the Chapter 66 laws dealing with a public utility's obligation to provide sufficient and efficient service as well as the gas gathering laws listed in SB 576. To obtain this input, the Commission provided a list of specific questions that have been raised in previous gathering system complaints and in the discussions of the Southwest Kansas H₂S and Low Pressure Task Force.

On January 27, 2006, Staff filed its report and recommendation answering the questions posed by the docket. A copy of Staff's report and recommendation is attached to my testimony. At this time, the Commission has requested the remaining commenters to file a response to Staff's

report. Their response is due on March 14, and we expect a procedural schedule to be set shortly after the 14th for the Commission to hold a public hearing on this matter.

In our report and recommendation, Staff takes the position that many of the gathering systems in Southwest Kansas have a dual function. First, they provide gas gathering services by collecting gas from producers and moving it to transmission lines. Secondly, some of the gathering systems provide a transportation function by moving gas from a producer and selling it to an end use customer from an interconnect along the gathering system pipeline. It is Staff's opinion that the transportation function is not a gas gathering service and it is currently exempted from Commission jurisdiction by K.S.A. 66-105a. Other commenters have disagreed with this position, and they contend that the legislature intended to include the transportation function as a gathering service when the gas gathering statutes were written.

The present statute requires a gas gatherer to provide access to any producer that wants to connect to their system. Because most Kansas gathering systems have no capacity limits, adding volume does not usually create operational problems. In fact, it is our opinion that many of the Kansas systems have exactly the opposite problem. That is, gathering capacity far exceeds demand, and the gatherers have difficulty in maintaining minimum throughput rates needed to maintain an economic operation. The gas throughput volumes of a gathering system are dependent upon the depletion rate of wells, the transfer of wells to a different gathering system, the addition of wells to a system, or the reconfiguration of the system operations. Many of these variables may be unforeseen even by the operator of the gathering system. It is Staff's opinion that adding open access for retail customers through interconnections will significantly increase

the complexity of a gathering system's operation and inventory control. It can probably be done with the addition of electronic flow measurement and custody transfer equipment, but all of that technology comes with a cost for all parties. This would include the producers, the gathering system operator, any consumers presently connected to gathering systems, and those who might choose to exercise this new statutory right.

Staff believes the practice of using a gathering system for deliveries to interconnected customers must necessarily remain secondary to the primary function for which these systems were constructed -- moving the gas from the producer to the transmission line. Open access for exit taps would eventually result in reconfiguration of the system that would be costly to the producer and ultimately lead to an early abandonment of the production reservoir which will directly impact producers and royalty owners. Excessive exit taps would also diminish the amount of gas that is delivered to gas plants for processing. When turndown limits of a plant are met, the plant must shutdown, reconfigure its operation, or deliver the gas to another source. This would obviously be an additional cost required from the gatherer and the producer in order to continue delivering gas to markets other than exit taps.

We would also like to point out that the proposed language in Section 6 and Section 8 appear to be contradictory. The changes in Section 6 require a public utility to obtain Commission approval prior to abandoning a customer. This is consistent with Commission practice and we feel we currently have the obligation to review proposed abandonments by public utilities under K.S.A. 66-117. The changes in Section 8 of the bill, however, indicate to us that Commission review of a proposed abandonment would only be required if the customer files a complaint. It

is our understanding that the intention of Section 8 in the current statute is to provide gas consumers served by a public utility advance notice of an impending abandonment. As we note in our report and recommendation, it is often difficult or nearly impossible for the public utility to be able to forecast gas availability on a gathering system. A more appropriate change may be a requirement for both the gathering system operator and the public utility to provide notice of an anticipated abandonment. Once notice is served, the KCC would have the obligation under 66-117 or under the proposed change in Section 6 of the bill to review the abandonment. I also think you should be aware that many of the consumers connected to gathering systems are not served by public utilities. Rather they are served under private contracts between the gathering system operator or an independent gas marketer.

This concludes my testimony, and I would be happy to answer any questions you may have.

KCC STAFF TESTIMONY
ATTACHMENT 1

MEMORANDUM

To: Brian J. Moline, Chair
Michael C. Moffet, Commissioner
Robert E. Krehbiel, Commissioner

From: Leo Haynos

Date: January 24, 2006

Re: Docket No. 06-GIMG-400-GIG
Report and Recommendation in Response to Request for Comments

Introduction

Expansive gas gathering systems are present in and around the southwest Kansas gas fields. These systems are primarily used to collect gas from numerous wells and deliver it to one or more points for transportation on intrastate and interstate pipelines to markets and end users. Many Kansas residents and businesses use the gas from the fields by tapping directly into the many miles of gathering system pipe throughout the region. These customers take unprocessed gas from points along the gathering systems referred to as "exit taps" prior to the final delivery point of the system. The final delivery point of the gathering system is the physical end of the gathering pipeline, usually a processing plant or point of sale to another pipeline.

In the order opening this docket, the Commission requested Staff and interested parties to respond to a series of questions. The following paragraphs provide Staff's analysis of the issues involved in this investigation, and they provide specific answers to each question listed in the

opening order. In addition to our analysis, Staff has listed 7 recommendations for the Commission's consideration.

Background

The gas gathering systems in southwest Kansas consist primarily of a piping network that was installed by vertically integrated interstate natural gas transmission companies. The transmission companies owned the gathering/transmission pipeline network as well as the natural gas in the system. Many of the consumers currently connected to the gathering system were originally customers of the interstate transmission company. The transmission companies provided gas service to exit taps as part of right-of-way contracts and for commercial sales. At least two of the transmission companies applied for and received certificates of convenience from the Kansas Corporation Commission to serve customers adjacent to their gathering systems. Before 1992, these interstate companies provided bundled sales and transportation service at federally regulated rates and the Kansas tariffs mirrored the federal rates.

The bundled services of sales, transportation, and storage were discontinued in 1993 for most customers by the Federal Energy Regulatory Commission (FERC) Order 636. After the passage of Order 636, the various functions of the gathering systems were sold or transferred to a variety of entities. The gathering systems belonging to interstate transmission companies were spun down to become intrastate gathering companies in order to compete with other intrastate gatherers. Because Order 636 prohibited the interstate companies from continuing gas sales, the Kansas certificated territory and retail direct sales customers were sold or transferred to gas public utilities with Commission approval.

Under the present operating scenario, many of the gathering systems in southwest Kansas transport gas to exit taps, serve customers through exit taps AND move gas from production lines to transmission lines. In some cases, the rights to serve consumers connected to exit taps are owned by public utilities that are certificated in the area to provide retail gas sales. In many cases, retail gas sales from gathering lines are conducted by companies that are not certificated public utilities. Staff's research indicates the gas providers that are not public utilities typically are third party gas marketers that are transporting gas on the gathering system, or the gas is provided for retail sale by an affiliate of the gas gatherer. These retail sales typically are subject to private contracts between the consumer and the gas provider.

Analysis

Kansas statutes K.S.A. 55-1,101 et seq. (gas gathering statutes) recognize gathering systems are a natural monopoly. The statutes require the Commission to provide regulatory oversight to allow producers or gas marketers access to the system and to prevent discriminatory gathering practices. The term gas gathering services included in the statute is defined as gathering or preparation of gas for transportation. That is to say, gas gathering services is a function of moving gas FROM production TO transmission. Under this scenario, the gathering function includes any processing that is done to prepare the gas for transmission. Therefore, it follows that while gathering can have many points of entry or access to the system, there is only one exit point. In Staff's opinion, this definition only recognizes the connection to the transmission line as an exit point from a gathering system. Although not defined in statute, the definition of a transmission line is typically the next segment of the gas delivery system. Transmission may be defined as moving or transporting gas from a point of receipt or entry on the line to an exit point. At the transmission exit point, the function of the piping system becomes distribution. Gas

distribution could be the immediate sales to a customer, e.g. a pipeline tap, or it could be wholesale sales to a retail provider like a public utility distribution network.

The definitions included in the gas gathering statutes indicate to Staff that the Kansas legislature recognized the above described pipeline functions, (gathering, transmission and distribution) could coexist on a gas gathering system. This fact is demonstrated by the inclusion of the word "primarily" in K.S.A. 55-150(d) to define a gas gathering system¹. Other examples of this intent are found in K.S.A. 55-1,107 and 55-1,109 which distinguish between a public utility selling gas at retail from a gas gathering system and a person offering gas gathering services. The phrase from K.S.A. 55-1,107, " ... A person purchasing natural gas OR gas gathering services from a person offering gas gathering services in a retail natural gas service area...", (emphasis added) clearly indicates that sale of natural gas for retail was not considered to be a subset of gas gathering services. Although the gas gathering statutes recognize the multi-functionality of a gas gathering system, the prescriptive language of the statutes only addresses the gas gathering function. It is Staff's opinion that the gas gathering statutes never contemplated regulatory control over service to exit taps because no requirements were placed on the transmission or distribution functions that coexist on gathering lines in southwest Kansas.

It is Staff's contention that the gathering systems of concern have the dual functionality of gas gathering systems and transmission systems. Staff believes that at the point custody for the gas transfers to a certificated public utility, the piping and facilities become a public utility under the definition of K.S.A. 66-104. Examples of this scenario would be those consumers served by

¹ K.S.A. 55-150(d): "Gas gathering system" means a natural gas pipeline system used primarily for transporting natural gas from a wellhead, or a metering point for natural gas produced by one or more wells, to a point of entry into a main transmission line...

Midwest and Aquila from facilities connected to the gathering system. Although the infrastructure delivering the gas to these customers is exempt from being considered a public utility function, the public utility function begins at the point of custody transfer to the public utility or to the gas provider. It is Staff's understanding that many of the companies that provide retail gas sales to consumers from gas gathering systems are not certificated public utilities.

Staff believes the function of delivering gas from production to an exit tap should be considered a transportation function rather than a gathering function. Although transporting gas by intrastate pipeline meets the definition of a public utility under K.S.A. 66-104, K.S.A. 66-105a clearly states that gas gathering systems whose primary function is delivering gas from production to transmission can not be considered as public utilities or common carriers in Kansas. Under the Natural Gas Act, the Federal Energy Regulatory Commission (FERC) was given jurisdiction over companies engaged in interstate transportation or sale of natural gas. Because the gas in question is produced and consumed prior to entering interstate transportation, this type of sales transaction is also not subject to FERC jurisdiction.

Policy Considerations

Based on the above analysis, Staff has reviewed each question listed in the docket and provided answers specific to each question. Furthermore, Staff has reviewed the comments received from other intervenors in this docket. Based on our analysis and review of intervenors' comments, Staff offers the following recommendations for the Commission's consideration:

1. The provision of exit taps on a gathering system should be left to the discretion of the gathering system operator. Commission involvement should be limited to the effect an exit tap may have on gas gathering services. Staff believes gas gathering services do not include delivery of gas to end use customers and the practice of using the system for this purpose must necessarily remain secondary to the primary function of gathering gas i.e. moving the gas from the producer to the transmission line. Open access for exit taps would eventually result in reconfiguration of the system that would be costly to the producer and ultimately lead to an early abandonment of the production reservoir. Excessive exit taps would also diminish the amount of gas that is delivered to gas plants for processing. When turndown limits of a plant are met, the plant must shutdown, reconfigure its operation, or deliver the gas to another source. This would obviously be an additional cost required from the gatherer and the producer in order to continue delivering gas to markets other than exit taps.
2. Any gas gathering system that provides gas to an exit tap under a contract other than a right-of-way (ROW) agreement is providing gas transportation rather than a gas gathering service. Regulation of intrastate transportation of natural gas has historically fallen within the purview of the Commission; however, current legislation exempts this function from Commission jurisdiction if it occurs on a gathering system. Staff

recommends the Commission rule on Staff's interpretation that the different functions of the gas gathering system may have different regulatory oversight.

3. Gas delivered by gas gathering system operators to exit taps as part of ROW agreements should be considered as incidental to the operation of a gas gathering system. Those agreements should be considered as private contractual matters outside the jurisdiction of the Commission except as provided for in K.S.A. 66-105a (b)-(d).
4. Gas sold to exit tap customers that are not under ROW or leasehold agreements is considered by Staff to be a distribution function of natural gas. As such, we believe this function may fall under the definition of a public utility in K.S.A. 66-104 or the definition of a gas provider in K.S.A. 66-2101(f). If the Commission agrees with this interpretation, the entities providing retail gas sales that meet the definition of a public utility should be required to apply for a certificate of convenience and necessity in order to continue serving customers. The terms and conditions of the certificate should reflect the unique operating conditions of providing distribution service from gas gathering systems.
5. Staff recommends that the Commission, as part of this proceeding, request comments with technical justification from the industry on what level of H₂S contamination should be allowed residential consumers connected to exit taps.
6. If abandonment of service to a public utility customer becomes necessary, Staff believes some amount of compensation for the conversion to an alternative fuel source is appropriate for residential consumers. Staff agrees with the comments of Midwest Energy (See Written Comments of Midwest Energy answer to question B4) that the amount of reimbursement for each case of abandonment should be reviewed using an established set of principles that provides guidelines for the amount of reimbursement.

Therefore, Staff recommends the Commission direct Staff and the parties to this investigation to compile a specific set of principles dealing with reimbursement for conversion to alternative energy for review and approval as part of this proceeding.

7. In fulfilling the requirements of K.S.A. 55-1,109, Staff recommends that utilities providing notice of insufficient gas supply be required to establish a close working relationship with the company providing transportation service to the exit tap customer. We believe this communication to be a condition of providing sufficient and efficient service. More robust and timely communications between the utility and operator of the gathering system should result in a more dependable forecast of future supplies.

ANSWERS TO QUESTIONS IN OPENING ORDER

A. Exit Taps and Gas Gatherers

- (1) **Under K.S.A. 2004 Supp. 55-1,103 is there a requirement that gas gathering systems provide “exit taps” to persons requesting such taps? In other words, are exit taps within the scope of "gathering services" and the obligation to provide "access to any person seeking such services or facilities [essential to provision of such services]?"**

The requirement for access can not be taken out of context of the phrase essential to the provision of such services. Staff does not believe exit taps are within the scope of 55-1,103

- (2) **If some exit taps are provided, is it unjustly discriminatory or unduly preferential under K.S.A. 2004 Supp. 55-1,103 to deny new exit taps or to curtail some but not all existing taps?**

Under K.S.A. 66-105a, a gas gathering system can not be considered a public utility. However, Staff contends the taps in question are a distribution function of the pipeline that extends beyond the gas gathering system. As such, those taps that provide retail sales of gas for residential and commercial consumers meet the definition of K.S.A. 66-104 and should be considered public utilities. Adding or denying new taps on the gas gathering system would not fall under the jurisdiction of the Commission because of the exemption provided in K.S.A. 66-105a.

- (3) **Do any other statutes impose a requirement on gas gathering systems to provide exit taps or other services to end use customers?**

Staff maintains the definition of gas gathering systems only applies to the piping function of delivering gas from production facilities to a transmission line. Under this definition, exit taps as defined in the order opening this docket are something other than a part of a gas gathering system. Gas gathering systems providing distribution or transportation service are exempt from KCC oversight. Other than the potential application of 66-104 to some of the existing taps, there are no requirements.

(4) If exit taps are not covered by K.S.A. 2004 Supp. 55-1,103, what jurisdiction does the Commission have with regard to provision of such exit taps, in addition to that provided under House Bill 2263, e.g is the provision of such service a public utility service subject to Chapter 66 regulation?

Staff believes the gas gathering piping network serves three purposes: Those are: 1. providing gas gathering services; 2. providing intrastate transportation service to exit tap customers; and, 3. downstream of the tap, providing distribution gas service to the consumer. This question addresses only the distribution aspect which is an extension to the gas gathering piping. As stated in the response to Question 2(A), Staff believes the Commission has jurisdiction over existing exit taps that provide service to residential and commercial consumers. Taps that provide service for agricultural purposes may be exempt from the K.S.A. 66-104 definition under the provisions of the Rural Self Help Gas Act, (see response to question A-7).

(5) Do the answers to the previous questions differ if a public utility owns the meter or other facilities between the exit tap and customer?

If the customer is currently served under established tariffs by a public utility certificated to serve in that territory, Staff would expect the public utility to continue that obligation.

(6) How does the fact that some exit tap customers may be entitled to service from the gathering systems due to right-of-way agreements affect the answers to the previous questions?

If gas service is being provided as an incidental cost to operating the gas gathering system, it is conceivable that a right-of-way customer could be considered to be part of the gathering system and thereby exempt from public utility regulation as per the terms of 66-105a. However, if the gas is being provided to the right-of-way customer by a third party at market prices, the answer to Question 4(A) would apply.

(7) Does K.S.A. 66-2101 et seq., the Self Help Act, affect the obligations of gas gathering services operators with regard to exit taps?

The Self Help Act² allows certain exit tap customers open access to a source of gas supply; however, it does not grant the rural gas user open access to gas piping networks. Staff believes exit taps are a distribution function attached to the gas gathering pipeline. As such, any agreements between the gathering system operator and the customer that deal with exit taps are not gas gathering services. Access to the physical pipeline tap appears to be the result of ROW agreements or private agreements between the gathering system operator and the end use customer. In Staff's opinion, those exit taps that are not the result of ROW agreements appear to be the a condition of a gas transportation agreement with the gathering system operator. The Commission does not have jurisdiction over transportation agreements on gas gathering systems because of the exemptions in K.S.A. 66-105a.

²The Rural Kansas Self Help Gas Act, (K.S.A. 66-2101 et. seq.) provides customers using gas for agricultural purposes the ability to bypass certificated public utilities if the utility does not have gas distribution infrastructure in place to serve the customer. Under this act, the rural gas user may contract with any entity to supply natural gas and the provider of such service is exempt from being considered a public utility.

B. Abandonment of Service by Gas Gathering System Operators

- (1) If a person offering gas gathering service asserts that it can no longer adequately or safely provide gas to exit tap customers what type of showing should be required pursuant to House Bill 2263? What standard or minimum showing should be required to demonstrate that the supply of gas is inadequate? What is the minimum showing with regard to safety aspects of the presence of H₂S?**

House Bill 2263 requires the Commission to determine the reasonableness of any health or safety related curtailment. In order to perform this function, Staff believes it is necessary for the operator to provide gas sampling data or system operations records that demonstrate the need for a curtailment. Furthermore, Staff is unwilling to make a "reasonableness" determination based on anecdotal records. The amount of data supplied should be of sufficient quantity and quality to make a convincing argument regarding the notice of curtailment. With regards to curtailments that result from H₂S contamination, Staff believes the Hugoton Field H₂S and Low Pressure Task Force report will provide guidelines on the level of H₂S that should be considered by the operator when recommending curtailment. Staff notes the task force's guidelines do not establish a clear threshold of the amount of H₂S in the gas that should result in curtailment to consumers. However, we recognize that it would be beneficial to the industry for the Commission to establish the maximum amount of H₂S in the gas stream at which curtailment would be mandatory for certain classes of customers. In Docket 05-CONS-222-CMSC, Staff has recommended a level of 15 parts per million (ppm) of H₂S in the gas stream as the level at which service to residential customers should be curtailed. Staff recommends that the Commission, as

part of this proceeding, request comments with technical justification from the industry on what level of H₂S contamination should be allowed residential consumers connected to exit taps.

(2) If gas quality is poor or a potential safety risk, but the exit tap customer still wishes to purchase the gas, is the gas gathering service required to continue furnishing the gas?

As a matter of course, any gas supply that can be demonstrated to be a potential safety risk should be curtailed regardless of the wishes of the customer. As noted earlier, Staff does not believe a gas gathering service is being offered to exit tap customers. In some cases, however, the supply of natural gas to exit taps falls under the authority of 66-104. For those taps that are considered to be public utilities, (see responses to questions 2(A)-4(A) above), the public utility would be required to provide sufficient and efficient service to its customers, (See K.S.A. 66-1,202). Staff considers providing gas of poor quality or of a potential safety risk to be an indication that the public utility is not providing sufficient and efficient service. Therefore, Staff would recommend the public utility be required to provide proper service to the customer or abandon the service. However, Staff notes the gas supplied to exit tap customers by definition is not comparable to the quality of gas supplied to the typical distribution consumer. For exit tap customers, the subjective phrase "sufficient and efficient" has to be considered within the context of the supply available.

(3) If termination of service is allowed, what authority does the Commission have to require the person providing gas gathering service (or its marketing affiliate) to provide for costs of an alternative fuel source such as propane in cases where:

- (a) The customer is directly served by the gas gathering system;**
- (b) A utility acquires the gas from the gas gathering system operator (or its affiliate)?**

In those cases where the exit tap falls under the authority of K.S.A. 66-104, the Commission has a long track record of requiring the public utility to provide an alternative fuel source for residential consumers. This practice has been justified as being part of the utility's obligation to provide efficient and sufficient service. By virtue of the utility's certificate and tariff, it holds itself out as a reliable supplier of energy to its customer. If the service is not sufficient or efficient it has breached its contract with its customer and Staff believes some amount of compensation is appropriate. Staff is unaware of any previous Commission order to provide an alternative fuel source for irrigators or commercial customers. We note, however, that exit tap customers for agricultural purposes have the right to seek alternative supplies under the Kansas Rural Self Help Gas Act.

- (4) What are the reasonable costs that should be reimbursed to customers who are abandoned or curtailed? Should this vary by the type of customer; i.e. residential, business or irrigation? Specifically, if use of the alternative fuel requires conversion of appliance and machinery, which appliances and machinery, such as irrigation equipment, should be covered? What should be the amount of reimbursement with regard to the alternative fuel itself; e.g. one tank of propane?**

In our answer to the previous question, Staff stated our opinion that some compensation to customers of public utilities is justified. In the abandonment cases that have been brought before the Commission there is no standard for the amount of compensation. Typically, Staff recommends the residential consumer be reimbursed an amount equivalent to

converting/replacing all household appliances (including domestic outbuilding appliances) for propane service, supplying the equivalent of a 500 gallon tank for propane storage, and supplying the differential in the cost of propane and natural gas for a one year supply of energy. Staff suggests the amount of compensation should take into account the culpability of the utility that brings about the service termination. For example, a utility that has failed to procure sufficient supply contracts or operating agreements to continue service may be required to offer more compensation to abandoned customers than a utility that is required to abandon service through circumstances beyond their control such as pressure depletion of supply or contamination of supply.

C. Natural Gas Public Utilities

- (1) What responsibilities do utilities have when a person offering gas gathering service determines that it can no longer supply gas to exit tap customers served by the utility? With regard to K.S.A. 55-1,109, is a general customer notice that service may be insufficient for the coming year appropriate notice or should utilities be required to provide more detailed information?**

It is Staff's position that the utility in this scenario is not using a gas gathering service. Rather, it is executing a supply contract for its customers in the same way that gas supplies are procured for all utility customers. Recognizing that gas gathering systems may be used for gas gathering and transportation, the legislature required public utilities to provide advance notice to its customers should they determine the supply may be limited for the coming year. It has been Staff's experience that utilities providing service to exit tap customers have no firm forecast of future supply availability. The inaccurate forecast may be the result of a poorly written supply contract, but more likely it is the result

of the dynamics of being supplied from a gathering system. The operation of the gathering system is dependent upon the depletion rate of wells, the transfer of wells to a different gathering system, the addition of wells to a system, or the reconfiguration of the system operations. Many of these variables may be unforeseen even by the operator of the gathering system. However, as part of providing sufficient and efficient service, Staff suggests that utilities be required to establish a close working relationship with the company providing transportation service to the exit tap customer. More robust and timely communications between the utility and operator of the gathering system should result in a more dependable forecast of future supplies.

(2) In reference to questions B(2) (3) and (4) above, what obligation does the utility have to continue service or convert the customer to an alternate source of energy?

See answer to B(3) and B(4).

(3) How do utility obligations related to rates and quality of service for exit tap customers differ from its traditional customers served by distribution systems owned by the utility?

In previous responses, we have suggested that service to exit tap customers can not be directly compared to traditional customer served by distribution systems. In addition to a continuous supply of high quality gas, distribution systems typically have a higher density of customers per mile of pipe. Staff would expect this arrangement to result in relatively lower operating costs because of the efficiencies gained from operating a system with consistent gas quality and a high density of customers. On the other hand, servicing exit tap customers typically requires a disproportionate amount of travel or staffing to respond to service calls because of the relatively few customers spread over many miles. The fact that gas quality and pressure can vary at any given time increases the need to provide individual service

which increases the cost of servicing this type of customer. K.S.A. 66-1,202 requires the utility to provide sufficient and efficient service. Given the dynamics of a gathering system operation, Staff recognizes the cost to provide sufficient and efficient service for exit tap customers will be slightly higher. Staff suggests the utility considered these variables when they applied for certification and held themselves out as a supplier of energy for exit tap customers. Although more service outages and longer response time to service calls may be inevitable for exit tap customers, the utility still has the obligation to provide service to this customer. The fact that the utilities have little if any investment in the infrastructure that serves this customer more than compensates them for the higher cost of service. In Staff's opinion, the quality of service to exit tap customers should not be significantly different than the quality of service provided to customers served by distribution networks.

(4) What role should quality of gas and continuity of supply play in establishing tariff prices for public utility customers?

For public utilities certificated in southwest Kansas, the established tariff price for natural gas is provided through a purchased gas adjustment. This price is set using a weighted average of the cost of gas throughout the utility's operation. A comparison of cost of gas from gathering systems to that of transmission line purchases shows no appreciable difference in the purchase price. Because the price of gas is simply passed through from the utility to the customer and the gas purchase prices from transmission or gathering are roughly equal, Staff sees no need to establish different tariff prices for the various classes of customer a utility may have.

(5) How has the unbundling of retail service, gas gathering facilities, and transportation facilities by former gathering system operators affected the ability of the current

public utility to provide service to exit tap customers in its certified service territory?

Before unbundling occurred, vertically integrated interstate transmission companies provided gas gathering services, transportation services, and retail distribution sales of natural gas from gas gathering systems. Recognizing the distribution sales were a public utility function, at least three of the interstate companies applied for and received certificates of convenience to serve retail customers. At that time, the only pipe in the area of these franchises was the gathering system. Therefore, the interstate companies recognized the use of the gathering system as the means of transporting gas to their retail customers and the certificate of convenience allowed them to be the only company that could serve a given area. With the passage of Federal Energy Regulatory Commission Order 636, the interstate companies were required to stop providing retail sales and become strictly a transportation company. Subsequently, the gathering systems, which were never under FERC regulation, became an unattractive operation for the transmission companies who could no longer own the gas on their system. At this point, it is Staff's understanding that the gathering systems were sold off or "spun down" to affiliate companies. At approximately the same time as the sale of the gathering system, the certificated area and its customers were divested to local distribution companies (LDCs). The LDCs applied for and received a transfer of the certificates to serve these exit tap customers. In reviewing the transfer of the certificates, it is apparent to Staff that the Commission order approving the acquisition of the certificated area surrounding the gas gathering system placed no requirement on the LDC's to secure access to the pipe that serves their customers or to secure long term gas supply for the customers. The subsequent action of the legislature in exempting gas transportation on a gas gathering pipe system from Commission jurisdiction in K.S.A. 66-105a effectively removed any requirements

that the gas gathering system operator negotiate supply arrangements for LDC customers. Although service to LDC customers is currently being provided, this set of circumstances places the LDC at an obvious disadvantage in meeting their obligation to provide sufficient and efficient service.

D. Effect of Negotiated Contracts

- (1) If the obligation to provide gas from the gathering system is addressed in a contract between the gathering system operator (or its affiliate) and the utility, what jurisdiction does the Commission have over the contract? Specifically, to what extent does the Commission have jurisdiction to enforce, interpret, or invalidate contract terms with regard to service, rates and liabilities?**

Staff believes the contract described would be a transportation contract. With the exemption found in K.S.A. 66-105a, the Commission would have no authority over transportation contracts offered on gas gathering systems.