BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF NEBRASKA

IN THE MATTER OF THE APPLICATION OF	)	
SOURCEGAS DISTRIBUTION LLC FOR AN	)	
ORDER AUTHORIZING IT TO PUT INTO EFFECT	)	DOCKET NO. NG-0078
A SYSTEM SAFETY AND INTEGRITY RIDER	)	
TARIFF AND A SYSTEM SAFETY AND	)	
INTEGRITY RIDER CHARGE	)	

PREFILED DIRECT TESTIMONY AND EXHIBITS OF

CHARLES A. BAYLES

SECTION **PAGE**

I. INTRODUCTION

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Charles A. Bayles. My business address is 655 East Millsap Road, Fayetteville, Arkansas 72703.

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

A. I am employed by SourceGas LLC ("SourceGas") as Director, Engineering and Regulatory Operations. I am employed in that capacity for SourceGas Distribution LLC ("SourceGas Distribution" or the "Company"), SourceGas Arkansas Inc. and Rocky Mountain Natural Gas LLC.

Q. WHEN DID YOU BEGIN YOUR EMPLOYMENT WITH SOURCEGAS?

A. I began my employment with SourceGas in July 2008, when SourceGas purchased Arkansas Western Gas Company ("AWG"). Prior to that date, I had been employed by AWG since June 1988.

Q. PLEASE DESCRIBE YOUR RESPONSIBILITIES AS DIRECTOR, ENGINEERING AND REGULATORY OPERATIONS.

A. I am responsible for providing information, data, research and analysis and testimony from the Technical Services Group in connection with rates and regulatory filings, including rate cases, recovery mechanisms and certificate applications. In this position, I regularly interface with the Accounting, Regulatory and Legal departments.

Q. PLEASE STATE YOUR EDUCATIONAL BACKGROUND AND PROFESSIONAL EXPERIENCE.

A. I received an Associate of Science degree in Land Surveying from the University of Arkansas in 1983. In 1987, I received a Bachelor of Science degree in Civil

Engineering from the University of Arkansas. I am a registered professional engineer in the States of Nebraska, Arkansas, Colorado, Missouri and Wyoming.

Since joining AWG in 1988, I have held a number of positions for AWG and SourceGas prior to becoming Director, Engineering and Regulatory Operations. Those positions included: Computer Aided Design (CAD) Operator; Pipeline Inspector; Staff Engineer; Manager, Construction and Engineering; Manager, Project Management; Director, Transmission and Engineering; and Senior Director, Engineering and Strategic Planning.

Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE NEBRASKA PUBLIC SERVICE COMMISSION?

A. No. I have not previously testified before the Nebraska Public Service Commission (the "Commission").

I have prefiled testimony and testified before the Arkansas Public Service Commission in Docket No. 12-095-U, In the Matter of the Application of SourceGas Arkansas Inc. for a Certificate of Environmental Compatibility and Public Need to Construct and Operate Two Segments of Natural Gas Pipeline in Benton and Washington Counties, Arkansas.

I also have prefiled testimony and testified before the Wyoming Public Service Commission in Docket No. 30022-219-GA-13, Record No. 13646, In the Matter of the Application of SourceGas Distribution LLC for a Certificate of Public Convenience and Necessity for Major Facility Construction of the Chokecherry Compressor Station Located in Walcott, Wyoming, Approval of a Waiver of Section 249 of the Commission's Rules, Authority to Implement a Revenue Adjustment Mechanism and to Issue New Tariffs.

In addition I have prefiled testimony before the Arkansas Public Service

Commission in Docket No. 14-023-U, In the Matter of the Application of SourceGas Arkansas Inc. for a Certificate of Environmental Compatibility and Public Need to Construct and Operate a Natural Gas Pipeline in Mississippi County, Arkansas.

Q. ON WHOSE BEHALF ARE YOU TESTIFYING IN THIS DOCKET?

A. I am testifying in this docket on behalf of SourceGas Distribution.

Q. ARE YOU PRESENTING ANY EXHIBITS IN CONNECTION WITH YOUR TESTIMONY IN THIS PROCEEDING?

A. Yes. I will present the following 17 exhibits, which I prepared or compiled or caused to be prepared or compiled under my supervision:

Exhibit CAB-1 –	SourceGas Distribution's U.S. Department of Transportation ("DOT") Annual Report for Calendar Year 2013 (Transmission)
Exhibit CAB-2 –	SourceGas Distribution's DOT Annual Report for Calendar Year 2013 (Distribution - Nebraska)
Exhibit CAB-3 –	National Association of Regulatory Utility Commissioners ("NARUC") Statement, "NARUC Welcomes LaHood's Call to Action on Pipeline Safety," Dated February 14, 2011
Exhibit CAB-4 –	Letters by DOT Secretary Ray LaHood and the Pipeline and Hazardous Materials Safety Administration's ("PHMSA") Administrator Cynthia Quarterman to Governors, Commissioners, State Regulators and Industry Leaders, Dated March 28, 31, 31 and 18, 2011, Respectively
Exhibit CAB-5 –	DOT News Release of "Call to Action," Dated April 4, 2011
Exhibit CAB-6 –	DOT "Call to Action," Released April 4, 2011, Revised November 1, 2011
Exhibit CAB-7 –	Copy of Proceedings from National Pipeline Safety Forum, Held April 18, 2011
Exhibit CAB-8 –	Testimony of PHMSA Administrator Cynthia Quarterman before House of Representatives' Subcommittee on Energy and Power of the Committee on Energy and Commerce, Dated June 16, 2011

Exhibit CAB-9 – Letter from PHMSA Administrator Cynthia Quarterman to NARUC Chairman of the Board and President Tony Clark and Chair of NARUC Pipeline Safety Task Force Collette Honorable, Dated December 19, 2011

Exhibit CAB-10 – Letter from NARUC to PHMSA Administrator Cynthia Quarterman, Dated April 12, 2012

Exhibit CAB-11 – American Gas Association's ("AGA") Natural Gas Rate Round-Up, "Infrastructure Cost Recovery Update," Dated June 2012

Exhibit CAB-12 – American Gas Foundation ("AGF") Report Prepared by Yardley Associates, titled "Gas Distribution Infrastructure: Pipeline Replacement and Upgrades – Cost Recovery Issues and Approaches," Dated July 2012

Exhibit CAB-13 – AGA "Innovative Rates, Non-Volumetric Rates, and Tracking Mechanisms: Current List" (as of February 2014)

Exhibit CAB-14 – Official Summary of Pipeline Safety Act, Written by the Congressional Research Service (Undated)

Exhibit CAB-15 – "Pipeline Standards and Rulemaking Division: Current Rulemakings in Process" (Undated), Prepared for Meeting of PHMSA's Technical Advisory Committees, Held February 24-25, 2014

Exhibit CAB-16 – PHMSA's "Draft IVP Chart," dated September 10, 2013

Exhibit CAB-17 – "2014 Projects and Initiatives Reflected in the Proposed System Safety and Integrity Rider for SourceGas Distribution LLC in Nebraska," dated May 1, 2014

II. <u>TESTIMONY OVERVIEW</u>

Q. PLEASE SUMMARIZE YOUR TESTIMONY IN THIS DOCKET.

A. My testimony describes the System Safety and Integrity Rider ("SSIR") Tariff being proposed by SourceGas Distribution and explains why it should be approved by the Commission as being just and reasonable and in the public interest. The remainder of my testimony is divided into three sections. In Section III, I provide an overview of SourceGas Distribution's natural gas pipeline system in Nebraska based upon the latest annual reports that SourceGas has submitted to PHMSA. In Section IV, I describe the federal regulatory environment that causes the need for the proposed SSIR Tariff. In Section V, I describe the projects and initiatives that are to be covered under the proposed SSIR Tariff and quantify SourceGas's projected capital costs and operation and maintenance ("O&M") expenses for 2014 for those projects and initiatives.

Q. PLEASE IDENTIFY SOURCEGAS DISTRIBUTION'S OTHER WITNESS WHO IS PROVIDING PREFILED DIRECT TESTIMONY IN THIS DOCKET CONCERNING THE PROPOSED SSIR TARIFF.

A. SourceGas Distribution is presenting the testimony of one other witness. Mr. Jerrad S. Hammer, Director – Rates and Regulatory, presents a Jurisdictional revenue deficiency analysis that reflects the impact of this Application and the Company's pending applications in Docket Nos. NG-0072.1 and NG-0079, supports the proposed SSIR Tariff from a policy perspective, describes the mechanics of the proposed SSIR Tariff, calculates the proposed System Safety and Integrity Rider Charges and describes the derivation of those charges.

III. SOURCEGAS DISTRIBUTION'S NATURAL GAS PIPELINE SYSTEM IN NEBRASKA

Q. PLEASE PROVIDE AN OVERVIEW OF SOURCEGAS DISTRIBUTION'S NATURAL GAS PIPELINE SYSTEM IN NEBRASKA.

A. SourceGas Distribution provides natural gas retail distribution and transportation services to customers in nearly 200 communities across the predominantly rural western two-thirds of Nebraska through its approximately 5,970 miles of natural gas pipeline in the State. Copies of SourceGas Distribution's DOT Annual Reports for

Calendar Year 2013 are attached to my testimony as Exhibits CAB-1 (Transmission) and CAB-2 (Distribution – Nebraska).

Q. PLEASE DESCRIBE EXHIBIT CAB-1.

A. Exhibit CAB-1 shows on page 13 that SourceGas Distribution's reported 1,206.822 miles of natural gas transmission system in Nebraska have nominal pipe sizes ranging from four (4) inches or less to eight (8) inches. Page 17 of Exhibit CAB-1 shows that all 1,206.822 miles of SourceGas Distribution's natural gas transmission system in Nebraska are cathodically protected steel pipe, of which 1,077.062 miles are coated and 129.76 miles are bare.

Q. PLEASE DESCRIBE EXHIBIT CAB-2.

A. Exhibit CAB-2 shows on page 1 that of SourceGas Distribution's reported 4,762.996 miles of natural gas distribution mains in Nebraska, 1,400.332 miles are plastic pipe, 2,597.015 miles are cathodically protected coated steel pipe, and 755.843 miles are cathodically protected bare steel pipe. Page 2 shows that 2,588.404 miles of the 4,762.996 miles of distribution mains in Nebraska are two (2) inches or less, with almost the entire remaining pipe ranging from two (2) inches to eight (8) inches. On page 3 of Exhibit CAB-2, SourceGas Distribution reported 238 leaks on its distribution system mains and services in Nebraska in 2012, 137 of which required immediate repair as they were designated as "hazardous." In 2013, SourceGas Distribution installed 792 excess flow valves ("EFVs") on single family residential services in Nebraska, bringing the total number of EFVs installed on these services in Nebraska to 2,139.

IV. <u>FEDERAL REGULATION OF PIPELINE SYSTEM SAFETY AND INTEGRITY</u>

Q. WHAT IS THE RELEVANCE OF FEDERAL REGULATION OF PIPELINE SYSTEM SAFETY AND INTEGRITY TO NATURAL GAS UTILITIES IN NEBRASKA?

A. In addition to being subject to the Minimum Safety Standards for Pipelines in Rule 002 of the Commission's Natural Gas and Pipeline Rules and Regulations, natural gas utilities in Nebraska also are subject to PHMSA's pipeline system safety and integrity regulations. PHMSA's regulations include Code of Federal Regulations ("CFR") Title 49 (Transportation), Part 192 (Transportation of Natural Gas and Other Gas by Pipeline: Minimum Federal Safety Standards). See Commission Rule 002.01 (incorporating by reference CFR Title 49, Part 192). Through certification by PHMSA's Office of Pipeline Safety, the Pipeline Safety Section of the Fuels Safety Division of the Nebraska State Fire Marshal (the "State Fire Marshal") enforces PHMSA's regulations including Part 192. *See* Nebraska Natural Gas Pipeline Safety Act of 1969, Neb. Rev. Stat. §§ 81-542 to 81-550 and 81-552; Regulations Pursuant to the Nebraska Natural Gas Pipeline Safety Act of 1969, Title 155 (State Fire Marshal), Chapter 1.

Section 192.1 states that Part 192 "prescribes minimum safety requirements for pipeline facilities and the transportation of gas, including pipeline facilities and the transportation of gas within the limits of the outer continental shelf." Section 192.3 defines "pipeline facilities" as "new and existing pipelines, rights-of-way, and any equipment, facility, or building used in the transportation of gas or in the treatment of gas during the course of transportation." That same section defines the term "transportation of gas" as "the gathering, transmission, or distribution of gas by pipeline or the storage of gas, in or affecting interstate or foreign commerce." An "operator," as defined in Section 192.3, is an entity that "engages in the transportation of gas." SourceGas Distribution is an "operator" under Part 192 of PHMSA's regulations.

Q. WHAT EVENTS HAVE SHAPED THE FEDERAL REGULATION OF PIPELINE SYSTEM SAFETY AND INTEGRITY SINCE THE TURN OF THE 21^ST CENTURY?

A. Following closely in time to a deadly gasoline pipeline rupture, explosion and fire near Bellingham, Washington, in June 1999, a natural gas transmission pipeline rupture, explosion and fire in August 2000 near Carlsbad, New Mexico, killed 12 members of a family camping in the area. The investigation following the Carlsbad accident demonstrated that more had to be done than traditional methods of ensuring pipeline system safety and integrity.

Q. DID THOSE EVENTS INFLUENCE FEDERAL LEGISLATIVE AND REGULATORY ACTIVITY IMPACTING NATURAL GAS UTILITIES?

A. Yes. The Bellingham and Carlsbad accidents triggered a wave of federal legislative and regulatory activity. Congress passed and the President signed into law the Pipeline Safety Improvement Act of 2002 (the "PSIA of 2002"). As required by the PSIA of 2002, in December 2003, PHMSA published the Gas Transmission Integrity Management Rule (49 CFR Part 192, Subpart O), commonly referred to as the "TIMP Rule." The TIMP Rule, which changed the traditional ways of ensuring pipeline system safety and integrity, specifies how pipeline operators must identify, prioritize, assess, evaluate, repair and validate the safety and integrity of gas transmission pipelines that could, in the event of a leak or failure, affect High Consequence Areas ("HCAs") within the United States. In general, HCAs are areas where highly populated buildings or outdoor areas of population exist. The TIMP

Rule also requires operators to apply to their pipelines in non-HCAs what they learn about their pipelines in HCAs.

As required by the TIMP Rule, SourceGas implemented and continues to employ a written pipeline system safety and integrity management program, called SourceGas's "TIMP." The TIMP Rule and SourceGas's TIMP also refer to HCAs and non-HCAs as "covered segments" and "non-covered segments," respectively. As shown on page 15 of Exhibit CAB-1, the TIMP Rule and SourceGas's TIMP covers the 1,206.822 miles of SourceGas Distribution's natural gas transmission system in Nebraska. Of that mileage, 1.288 miles of SourceGas Distribution's natural gas pipeline system in Nebraska are located in HCAs. *See* Exhibit CAB-1, page 16. The TIMP is a dynamic and evolving program and thus is continually undergoing modifications and revisions. These modifications reflect operating and industry experience and conclusions drawn from the transmission integrity management process and incorporate tools and techniques as they become available.

In December 2006, Congress passed and the President signed into law the Pipeline Inspection, Protection, Enforcement and Safety Act (the "PIPES Act"). The PIPES Act reauthorized pipeline system safety and integrity programs, and strengthens PHMSA's regulatory and enforcement authority. The PIPES Act mandates that PHMSA prescribe minimum standards for pipeline system safety and integrity management programs for distribution pipelines to ensure fitness for service. The law provides for PHMSA to require operators of distribution pipelines to continually identify and assess risks on their distribution lines, to remediate conditions that present a potential threat to pipeline system safety and integrity, and to monitor program effectiveness. The PIPES Act also requires that companies engaging in excavation and construction activity must utilize the “811” one-call notification system in states with such systems to locate underground pipelines and facilities before starting projects.

As mandated by the PIPES Act, in December 2009, PHMSA published the Integrity Management Program for Gas Distribution Pipelines Rule (49 CFR Part 192, Subpart P), commonly referred to as the “DIMP Rule.” The DIMP Rule requires each operator to develop, write and implement a distribution pipeline system safety and integrity management program. A key component of the DIMP Rule, Section 192.1007(f), states as follows:

> “*Periodic Evaluation and Improvement*. An operator must re-evaluate threats and risks on its entire pipeline and consider the relevance of threats in one location to other areas. Each operator must determine the appropriate period for conducting complete program evaluations based on the complexity of its system and changes in factors affecting the risk of failure. An operator must conduct a complete program re-evaluation at least every five years. The operator must consider the results of the performance monitoring in these evaluations.”

As required by the DIMP Rule, SourceGas implemented its written distribution pipeline system safety and integrity management program as of August 2, 2011, called SourceGas’s “DIMP.” SourceGas’s DIMP covers its natural gas pipeline regulated by DOT as distribution pipeline, which measured nearly 4,763 miles in SourceGas’s latest DOT Annual Report (see Exhibit CAB-2, page 1). The DIMP is a dynamic and evolving program and thus is continually undergoing modifications and revisions. These modifications reflect operating and industry experience and conclusions drawn from the distribution integrity management process and incorporate tools and techniques as they become available. The DIMP uses performance measures to determine the program effectiveness and to initiate modifications or additions as necessary.

Q. HAVE SUBSEQUENT EVENTS TRIGGERED ANOTHER WAVE OF FEDERAL LEGISLATIVE AND REGULATORY ACTIVITY IMPACTING NATURAL GAS UTILITIES?

A. Yes. The tragic and high profile events involving natural gas pipelines in San Bruno, California (September 2010), Wayne, Michigan (December 2010), Philadelphia, Pennsylvania (January 2011), Allentown, Pennsylvania (February 2011), and Hanoverton, Ohio (February 2011), among other incidents, have triggered another wave of legislative and regulatory activity impacting natural gas utilities.

Q. DID PHMSA TAKE ACTION IN RESPONSE TO THOSE TRAGIC EVENTS?

A. Yes. Three days after the incident in Hanoverton, Ohio, on February 14, 2011, DOT Secretary Ray LaHood made an appearance at the NARUC 2011 Winter Meeting. He announced at that meeting that the DOT was convening a series of meetings with state regulators, gas pipeline inspectors and other interested parties to improve the safety and integrity of the nation's gas pipeline systems. In response, NARUC Chairman of the Board and President Tony Clark of North Dakota (now Commissioner of the Federal Energy Regulatory Commission) and Committee on Gas Chair Timothy Alan Simon of California issued the following statement on February 14, 2011:

> "On behalf of the nation's State public utility commissioners, we thank Secretary LaHood for meeting with us today. State regulators fully understand the importance of assuring the safety of our nation's pipeline system. We take these responsibilities seriously and personally. We truly appreciate the Secretary offering an invitation to us to speak about these issues on a bigger scale. The nation must be assured that its gas pipeline system is safe and reliable, and that responsibility falls on all of us. We welcome Secretary LaHood's call for action and we look forward to working with him, [PHMSA] Administrator Cynthia Quarterman, and whomever else the Secretary includes."

A copy of the complete NARUC statement, titled "NARUC Welcomes LaHood's Call to Action on Pipeline Safety," is attached to my testimony as Exhibit CAB-3.

In March 2011, DOT Secretary Ray LaHood and PHMSA Administrator Cynthia Quarterman sent letters to Governors, Commissioners, state regulators, industry leaders and others, advising them that the above-referenced tragedies "highlight the need to take a hard look at the integrity of the Nation's pipelines" and "underscore the need to develop a comprehensive solution that will prevent accidents like these from recurring." Copies of those letters are attached collectively as Exhibit CAB-4.

The DOT Secretary and PHMSA Administrator invited the recipients of those letters to attend a National Pipeline Safety Forum in April 2011, "with the goal of *accelerating* the rehabilitation, repair, and replacement of critical pipeline infrastructure with known integrity risks." (Emphasis added). More directly, in the letters to the Governors, Secretary LaHood "urge[d] [each Governor's] staff to encourage companies *and the State utility commission to accelerate pipeline repair, rehabilitation, and replacement programs* for systems whose integrity cannot be positively confirmed." (Emphasis added).

On April 4, 2011, Secretary LaHood announced a "Call to Action" by which the DOT "launched a national pipeline safety initiative to repair and replace aging pipelines to prevent potentially catastrophic incidents." The news release of the "Call to Action" states that the DOT's "pipeline safety plan will address immediate concerns in pipeline safety, such as ensuring pipeline operators know the age and condition of their pipelines; proposing new regulations to strengthen reporting and inspection requirements; and making information about pipelines and the safety record of pipeline operators easily accessible to the public." The "Call to Action" explains that the "[i]nvestments that are made now will ensure the safety of the American people and the integrity of the pipeline infrastructure for future generations." Copies of the news release and the "Call to Action" are attached to my testimony as Exhibit CAB-5 and Exhibit CAB-6, respectively.

Q. DID PHMSA HOLD THE NATIONAL PIPELINE SAFETY FORUM?

A. Yes. A copy of the proceedings from the National Pipeline Safety Forum, held on April 18, 2011, is attached to my testimony as Exhibit CAB-7. The second of three panel discussions addressed, among other topics, "rate-setting and cost recovery issues." (Exhibit CAB-7, p. 6 of 61). As part of that panel discussion, participants indicated that "[m]any states are working on infrastructure recovery but the mechanism can vary from state to state. One state may have an accelerated replacement program, another state may have an incentive for replacement, and a third state may have timely recovery which allows operators to recover costs in the year the pipelines are replaced." (Exhibit CAB-7, p. 16 of 61).

Q. DID PHMSA TESTIFY BEFORE CONGRESS ABOUT SECRETARY LAHOOD'S "CALL TO ACTION"?

A. Yes. On June 16, 2011, before the House of Representatives' Subcommittee on Energy and Power of the Committee on Energy and Commerce, PHMSA Administrator Quarterman provided testimony about PHMSA's safety and integrity oversight of the country's more than 2.5 million miles of pipelines and Secretary LaHood's "Call to Action." The Administrator testified, in part:

> "In the wake of several recent serious pipeline incidents, PHMSA is taking a hard look at the nation's pipelines. The pipeline infrastructure—like our roads, bridges, ports, and rail infrastructure—needs more attention. Investments now will ensure the safety of the American people and the integrity of the pipeline infrastructure to deliver energy for future generations. We are issuing a call to action for all pipeline stakeholders, including the public, the pipeline industry and our State partners. Together, we need to chart a course to accelerate the identification, repair, rehabilitation and replacement of high risk pipeline infrastructure before it becomes a risk to people or the environment. *PHMSA is specifically calling on State Public Utility Commissions to establish cost*

> *recovery mechanisms that effectively address infrastructure replacement costs.*" (Exhibit CAB-8, p. 1 of 5; Emphasis added).

A copy of the PHMSA Administrator's testimony is attached to my testimony as Exhibit CAB-8.

Q. HOW HAS PHMSA CALLED ON STATE PUBLIC UTILITY COMMISSIONS TO ESTABLISH COST RECOVERY MECHANISMS THAT EFFECTIVELY ADDRESS INFRASTRUCTURE REPLACEMENT COSTS?

A. PHMSA Administrator Quarterman called on state public utility commissioners to establish cost recovery mechanisms that effectively address infrastructure replacement costs through her letter, dated December 19, 2011, to Mr. Clark and Ms. Collette Honorable, Chair of NARUC's Pipeline Safety Task Force. A copy of the letter is attached to my testimony as Exhibit CAB-9.

In her letter, the Administrator expresses PHMSA's "appreciat[ion of] the NARUC's continued diligence in promoting rate mechanisms that will encourage and will enable pipeline operators to take reasonable measures to repair, rehabilitate or replace high-risk gas pipeline infrastructure." The letter states that "[m]any State public utility commissions have encouraged the timely repair, rehabilitation, and replacement of high-risk gas pipeline infrastructure through special rate mechanisms."

In support of this statement, the Administrator attached to her letter "a white paper on state pipeline infrastructure replacement programs in the hope that you will share it with your members as a resource for encouraging more States to adopt alternative or more flexible rate mechanisms that will facilitate the replacement or repair of high-risk pipelines." The white paper concludes (at Exhibit CAB-9, p. 21 of 34) that "[n]early 30 State public utility commissions have established pipeline infrastructure replacement programs as part of the ratemaking process. These programs play a vital role in protecting the public by ensuring the prompt rehabilitation, repair, or replacement of high-risk gas distribution infrastructure." A copy of the white paper is included as part of Exhibit CAB-9.

Q. DID NARUC RESPOND TO THE LETTER FROM PHMSA ADMINISTRATOR QUARTERMAN?

A. Yes. NARUC responded by letter dated April 12, 2012, a copy of which is attached to my testimony as Exhibit CAB-10. Referencing the Pipeline Safety, Regulatory Certainty, and Job Creation Act of 2011 that Congress passed in December 2011 and the President signed into law on January 3, 2012 (the "Pipeline Safety Act"), the letter states that NARUC "look[s] forward to working with you as we begin the implementation of the *many* rulemaking proceedings this important law requires." (Emphasis added). NARUC also comments in the letter that its "members and our colleagues at State legislatures are leading the way in the adoption of innovative rate mechanisms that encourage timely pipeline system replacement." Along that line, NARUC also says the following in the letter:

> "*The pipeline owners know their needs and requirements better than any of us, and we would note that they can come to us at anytime to propose replacement and safety improvements to their systems.* They do not need our permission to file a fair proposal for accelerated cost recovery for new pipeline infrastructure. The regulatory paradigm puts the onus on the industry to demonstrate the needs of their systems in an open and fact-based process before a commission with the requisite stakeholders or interveners participating. *If the utility can demonstrate its proposal is fair, balanced, and advances the goal of pipeline safety in such a process, it will receive an appropriate rate structure.*" (Emphasis added).

Q. HAVE MANY STATE UTILITY COMMISSIONS GRANTED SUCH ACCELERATED COST RECOVERY MECHANISMS?

A. Yes. In June 2012, the AGA published its Natural Gas Rate Round-Up titled "Infrastructure Cost Recovery Update" (the "AGA Rate Round-Up"). A copy of the

AGA Rate Round-Up is attached to my testimony as Exhibit CAB-11. The AGA states therein (at Exhibit CAB-11, pp. 1 and 5 of 20):

> "In 2007, when AGA published its first report on infrastructure cost recovery methods, 15 natural gas utilities in 11 states serving 8 million residential natural gas customers were using innovative rate structures that allowed them to modify tariffs and recover the costs of investments in utility replacement incurred between rate cases. Since that time, the use of these advanced regulatory mechanisms has tripled. Today, 47 utilities in 22 states serving 24 million residential natural gas customers are using full or limited special rate mechanisms to recover their replacement infrastructure investments, and 5 utilities have mechanisms pending in another state and the District of Columbia. Ten states have enacted legislation or issued generic regulations that give utilities in three additional states the authority to implement these mechanisms. A further 14 utilities in 7 states are recovering these investments using rate stabilized tariffs. Together, these regulatory programs are helping natural gas utilities maintain safe and reliable service to more than 30 million of the nation's 65 million residential natural gas customers."

> "Congress, the U.S. Department of Transportation, and state commissions are devoting greater attention to the need for additional investment in the infrastructure required to maintain and improve the safety and reliability of the distribution network. More than half of the states now allow utilities to recover the costs incurred between rate cases associated with replacing aging infrastructure, and ten states have implemented legislation or state-wide regulatory programs to comprehensively address infrastructure issues."

Q. WERE THE AGA'S FINDINGS ADDRESSED IN AN INDEPENDENT REPORT ON PIPELINE INFRASTRUCTURE REPLACEMENT AND COST RECOVERY?

A. Yes. In July 2012, the AGF released a report prepared for it by Yardley & Associates, titled "Gas Distribution Infrastructure: Pipeline Replacement and Upgrades – Cost Recovery Issues and Approaches" (the "AGF Report"). Founded in 1989, the AGF is a 501(c)(3) organization focused on being an independent source of information research and programs on energy and environmental issues that affect public policy, with a particular emphasis on natural gas. Yardley & Associates provides advisory services, expert testimony and litigation support to natural gas industry participants. A copy of the AGF Report is attached to my testimony as Exhibit CAB-12.

Referencing the mechanisms identified in the AGA Rate Round-Up, the AGF Report explains on Exhibit CAB-12, page 6 of 37, that:

> "Each mechanism accommodates LDC [*i.e.*, local distribution company] - specific circumstances and the particular statutory guidance, policies, and precedent of the respective jurisdiction. These ratemaking approaches support the increased capital requirements of replacing and enhancing leak-prone infrastructure, while preserving the fundamental elements of the traditional regulatory compact. The approval of these cost recovery mechanisms reflects the heightened focus on pipeline safety, the contribution of pipeline replacement efforts to improved safety and reliability, and the challenges to timely cost recovery attributable to large-scale investments in non-revenue producing facilities."

Q. DID THE AGF REPORT ALSO DISCUSS THESE MECHANISMS FROM THE PERSPECTIVE OF REGULATORS?

A. Yes. On Exhibit CAB-12, page 6 of 37, the AGF Report states that:

> "The implementation of infrastructure cost recovery mechanisms *enhances the regulatory oversight of LDC infrastructure replacement and enhancement initiatives* by facilitating stakeholder understanding of efforts to improve the safety and reliability of the LDC networks serving the public. *These reviews allow commissions and other stakeholders to focus on pipeline safety and integrity to a greater degree than is usually possible in rate case proceedings.* Commissions are able to concentrate their review on unique LDC circumstances, the extent of the challenges, the prioritization of investments, and potential bill impacts, all of which influence the pace of the replacement efforts." (Emphasis added).

Q. HAS THE AGA RECENTLY UPDATED ITS 2012 FINDINGS ON THE NUMBER OF STATE UTILITY COMMISSIONS THAT HAVE GRANTED SUCH ACCELERATED COST RECOVERY MECHANISMS?

A. Yes. As of February 2014, the AGA reports that 75 utilities in 34 states and the District of Columbia are using full or limited special rate mechanisms to recover their replacement infrastructure investments, and 7 utilities have mechanisms pending. These figures do not include the utilities in four other states, including, in Nebraska, SourceGas Distribution and Black Hills/Nebraska Gas Utility Company, LLC, d/b/a Black Hills Energy, Omaha ("Black Hills"), that have authority under statute or generic rules to implement these mechanisms. A copy of the relevant portion of AGA's update is attached to my testimony as Exhibit CAB-13.

Q. IS NEBRASKA ONE OF THE STATES THAT NOW ALLOW GAS UTILITIES TO RECOVER THE COSTS INCURRED BETWEEN RATE CASES ASSOCIATED WITH REPLACING AGING INFRASTRUCTURE?

A. Yes. Sections 66-1865 and 66-1866 of the State Natural Gas Regulation Act (the "Act") state that natural gas utilities in Nebraska may file with the Commission, beginning on January 1, 2010, an application and proposed rate schedules to establish or change infrastructure system replacement cost recovery charge rate schedules that will allow for the adjustment of the utility's rates and charges to provide for the recovery of costs for eligible infrastructure system replacements. The Commission has approved infrastructure system replacement recovery charges for SourceGas Distribution (Docket No. NG-0072, Order entered June 25, 2013) and Black Hills (Docket No. NG-0074, Order entered November 25, 2013).

Q. WHY IS SOURCEGAS DISTRIBUTION PROPOSING TO IMPLEMENT A SYSTEM SAFETY AND INTEGRITY RIDER WHEN IT ALREADY HAS AN APPROVED INFRASTRUCTURE SYSTEM REPLACEMENT RECOVERY CHARGE AND MAY SEEK TO ADJUST SUCH CHARGE UNDER THE ACT?

A. Mr. Hammer addresses this question in his Direct Testimony from a rate making perspective. The federal directives that I have discussed and ongoing public concern have led to a fundamental change of direction in the way the natural gas industry is regulated, and that change has increased costs and made them more difficult to plan for and predict. Based upon the scope of present legislative mandates and regulatory initiatives, and other signals from regulators, the current flurry of regulatory activity appears to be just the tip of the iceberg. It may take several years before the natural gas industry can extrapolate if and when this fundamental change of direction may settle into a more predictable routine. This fundamental change in direction places greater burdens on pipeline operators such as SourceGas Distribution to implement the requirements of ever-changing federal regulations and requires that the costs of compliance be recovered on a concurrent basis as the costs are incurred.

Q. PLEASE DESCRIBE THE PRESENT LEGISLATIVE MANDATES AND REGULATORY INITIATIVES.

A. In its letter dated April 12, 2012 (Exhibit CAB-10), NARUC correctly characterizes the Pipeline Safety Act as requiring "*many* rulemaking proceedings." (Emphasis added). A copy of the official summary of the Pipeline Safety Act, written by the Congressional Research Service, is attached to my testimony as Exhibit CAB-14.

The official summary of the Pipeline Safety Act, among other things, identifies rulemaking initiatives relevant to, and other requirements imposed on, pipeline operators such as SourceGas Distribution. Those rulemaking initiatives and other requirements include the following:

- <u>Pipeline Safety Act, Section 4</u>: This section requires a study to discuss the ability of transmission pipeline facility operators to respond to a natural gas release from a pipeline segment located in an HCA. This section also directs PHMSA, after consideration of the results of the study presented in the report and if appropriate, to require by regulation the use of automatic or remote-controlled shut-off valves, or equivalent technology, where economically, technically, and operationally feasible, on new or entirely replaced transmission pipeline facilities.
- <u>Pipeline Safety Act, Section 5</u>: This section directs PHMSA to evaluate whether safety and integrity management system requirements should be expanded beyond HCAs. The results of the evaluation must be presented in a report. This section also directs PHMSA, depending upon the results of the evaluation presented in the report, to issue regulations effective not later

than January 3, 2015 that expand safety and integrity management system requirements, or elements of them, beyond HCAs.

- Pipeline Safety Act, Section 8: This section requires PHMSA to report to Congress on leak detection systems utilized by operators of transportation-related flow lines.

- Pipeline Safety Act, Section 22: This section directs PHMSA, if appropriate and after issuing a final report on the evaluation of the National Transportation Safety Board's ("NTSB's") recommendation on excess flow valves in applications other than service lines serving one single family residence, to issue regulations that require the use of excess flow valves, or equivalent technology, where economically, technically, and operationally feasible on new or entirely replaced distribution branch services, multi-family facilities, and small commercial facilities.

- Pipeline Safety Act, Section 23: This section directs PHMSA to require each gas pipeline operator or owner to verify records for all interstate and intrastate gas transmission pipelines in Class 3 and Class 4 locations and Class 1 and Class 2 HCAs to ensure they reflect accurately the pipeline's physical and operational characteristics and confirm their established maximum allowable operating pressures ("MAOP"). This section also directs each gas pipeline operator to submit to PHMSA documentation relating to each pipeline segment for which records are insufficient to confirm the established MAOP of the segment. In addition, this section requires PHMSA to issue regulations for conducting tests to confirm the material strength of previously untested natural gas transmission pipelines located in HCAs and operating at a pressure greater than 30% of specified minimum yield strength ("SMYS").

Q. YOUR SUMMARY OF SECTION 23 OF THE PIPELINE SAFETY ACT MENTIONS THE TERMS "CLASS" LOCATIONS, "MAOP" AND "SMYS." PLEASE EXPLAIN THE MEANING OF THESE TERMS.

A. A "Class" location unit is an onshore area that extends 220 yards on either side of the centerline of any continuous one-mile length of pipeline in accordance with CFR Title 49, Part 192, Section 192.5, which defines each numbered Class location unit. Class location units along a transmission pipeline are determined by the count of buildings intended for human occupancy and/or qualifying outdoor areas within the class location unit. That count increases along the progression of Classes from "1" to "4." As shown on page 16 of Exhibit CAB-1, although SourceGas Distribution does not operate in any Class 4 locations in Nebraska, it does operate 23.17 miles of pipe in Class 3 locations in addition to 66.448 miles of pipe in Class 2 locations and 1,117.204 miles of pipe in Class 1 locations.

"MAOP" verification plays a vital role in the integrity management program because the Potential Impact Radius calculation used to determine whether an area is an HCA depends upon the MAOP of the line. The MAOP is calculated using factors of class location, pipe grade and wall thickness of the pipe, among other variables.

"SMYS" is the minimum yield strength of steel pipe manufactured in accordance with a listed specification.

As I discuss in detail later in my Direct Testimony, Section 23, along with Section 5, of the Pipeline Safety Act forms the basis for many of PHMSA's rulemaking proceedings, regulations and advisory bulletins mandating MAOP verification, transmission pipeline system integrity management assessments ("assessments") and system knowledge.

Q. WHAT IS THE STATUS OF PHMSA'S RULEMAKING ACTIVITIES?

A. PHMSA's Technical Pipeline Safety Standards Committee and Technical Hazardous Liquid Pipeline Safety Standards Committee (together, the Technical Advisory Committees, or "TAC") met in a joint session on February 25-26, 2014. PHMSA's website posted documents prepared for that meeting. One of the documents is titled "Pipeline Standards and Rulemaking Division: Current Rulemakings in Process" (undated). A copy of that document is attached to my testimony as Exhibit CAB-15. Exhibit CAB-15 identifies the following pending PHMSA rulemaking activities applicable to pipeline operators:

- <u>Pipeline Safety: Safety of Gas Transmission Pipelines, Docket No. PHMSA-2011-0023</u>: Through this rulemaking, PHMSA is considering whether changes are needed to the regulations governing the safety and integrity of gas transmission pipelines. In particular, PHMSA is considering whether the

TIMP Rule requirements should be changed, including adding more prescriptive language in some areas, and whether other issues related to system safety and integrity should be addressed by expanding TIMP Rule requirements to non-TIMP areas. Specific issues being investigated include: whether the definition of an HCA should be revised, whether additional restrictions should be placed on the use of specific pipeline assessment methods, whether revised requirements are needed on new construction or existing pipelines concerning mainline valves (including valve spacing and installation of remotely operated or automatically operated valves), whether requirements for corrosion control of steel pipelines should be strengthened, and whether new regulations are needed to govern the safety and integrity of gathering lines and underground gas storage facilities. The comment period on the Advance Notice of Proposed Rulemaking ("ANPRM") ended January 20, 2012. The AGA filed comments on behalf of its members, including SourceGas Distribution.[1] A Notice of Proposed Rulemaking ("NPRM") currently is "under development within PHMSA." *See* Exhibit CAB-15, page 4.

- Pipeline Safety: Expansion of Excess Flow Valves in Gas Distribution Systems to Applications Other Than Single-Family Residences, Docket No. PHMSA-2011-0009: Through this rulemaking, PHMSA seeks to address the NTSB safety recommendation to PHMSA that excess flow valves be installed in all new and renewed gas service lines, for structures other than single family dwellings, when the operating conditions are compatible with readily available valves. The comment period on the ANPRM ended on March 19, 2012. In a related proceeding, Docket No. PHMSA-2012-0086 (Pipeline Safety: Information Collection Activities, Excess Flow Valve Census), the AGA filed comments on behalf of its members, including SourceGas Distribution.[2] This rulemaking now is in the "NPRM stage." *See* Exhibit CAB-15, page 8.

- Pipeline Safety: Public Comment on Leak and Valve Studies Mandated by the Pipeline Safety Act, Docket No. PHMSA-2012-0021: As required by Sections 4 and 8 of the Pipeline Safety Act, respectively, PHMSA is required to complete reports on the use of automatic/remote-controlled shut-off valves and leak detection systems. On September 28, 2012, PHMSA released a draft report titled "Leak Detection Study," conducted by Dr. David Shaw and others (DTPH56-11-D-000001).[3] On October 4, 2012, PHMSA released a draft report titled "Studies for the Requirements of Automatic and Remotely Controlled Shutoff Valves on Hazardous Liquids and Natural Gas Pipelines with Respect to Public and Environmental Safety," conducted by the Oak

1 http://www.aga.org/our-issues/safety/pipleinesafety/AGAcomment/2012/Documents/AGA_comments_A_thru_O_App_FINAL.pdf; http://www.aga.org/our-issues/safety/pipleinesafety/AGAcomment/2012/Documents/AGA%20section%20K_FINAL.pdf

2 http://www.aga.org/our-issues/safety/pipleinesafety/AGAcomment/2012/Documents/AGA%20Final%20Comments%20to%20EFV%20Census_071611.pdf

3 http://primis.phmsa.dot.gov/meetings/FilGet.mtg?fil=397.

Ridge National Laboratory (ORNL/TM-2012/411).[4] PHMSA currently is developing a NPRM that would require, for gas transmission pipelines in HCAs and Class 3 and Class 4 locations, mandatory installation of automatic shutoff valves, remote controlled valves, or equivalent technology and establish performance based meaningful metrics for rupture detection for gas pipelines. *See* Exhibit CAB-15, page 12 (unnumbered).

- Pipeline Safety: Class Location Requirements, Docket No. PHMSA-2013-0161: Through this rulemaking, PHMSA is considering whether applying the TIMP requirements, or elements of TIMP, to areas beyond current HCAs would mitigate the need for class location requirements for gas transmission pipelines. According to the NPRM, if the use of class location designation were to be eliminated or merged, many regulatory sections will need to be reevaluated. The AGA filed comments on behalf of its members, including SourceGas Distribution.[5]

- Pipeline Safety: Issues Related to the Use of Plastic Pipe in Gas Pipeline Industry: PHMSA is developing a NPRM to "address the following plastic pipe topics: focus on gas lines, authorized use of PA12 at higher pressures, AGA petition to raise D.F. [design factor] from 0.32 to 0.40 for PE [polyethylene] pipe, enhanced tracking and traceability, miscellaneous revisions for PE and PA11 pipelines, [and] additional provisions for fittings used on plastic pipe." *See* Exhibit CAB-15, page 11.

Q. IN ADDITION TO CONDUCTING RULEMAKING PROCEEDINGS, HAS PHMSA ISSUED ANY STATEMENTS ABOUT MAOP VERIFICATION, ASSESSMENTS AND SYSTEM KNOWLEDGE?

A. Yes. PHMSA has issued Advisory Bulletins about MAOP verification, assessments and system knowledge. For example, Advisory Bulletin ADB-11-01 states that:

> "An operator must diligently search, review and scrutinize documents and records, including but not limited to, all as-built drawings, alignment sheets, and specifications, and all design, construction, inspection, testing, maintenance, manufacturer, and other related records. These records shall be traceable, verifiable, and complete. If such a document and records search, review, and verification cannot be satisfactorily completed, the operator cannot rely on this method for calculating MAOP."[6]

Advisory Bulletin ADB-11-01 further states that:

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4 https://primis.phmsa.dot.gov/meetings/FilGet.mtg?fil=396.

5 http://www.aga.org/our-issues/safety/pipleinesafety/AGAcomment/2013/Documents/AGA%20Comments_ClassLocationRequirements_PHMSA-2013-0161_FINAL_110113.pdf .

6 76 Fed. Reg. 1504, 1506 (January 10, 2011).

> "These records should be traceable, verifiable, and complete to meet [PHMSA regulation] §§ 192.619…. If such a document and records search, review, and verification cannot be satisfactorily completed, the operator may need to conduct other activities such as in-situ examination, pressure testing, and nondestructive testing or otherwise verify the characteristics of the pipeline when identifying and assessing threats or risks."[7]

Another example is Advisory Bulletin ADB-2012-06, which "informs gas operators of anticipated changes in annual reporting requirements to document the confirmation of MAOP, how they will be required to report total mileage and mileage with adequate records, when they must report, and what PHMSA considers an adequate record."[8] Advisory Bulletin ADB-2012-06 contains the following statements:

> "As directed in the Act, PHMSA will require each owner or operator of a gas transmission pipeline and associated facilities to verify that their records confirm MAOP of their pipelines within Class 3 and Class 4 locations and in Class 1 and Class 2 locations in HCAs.
>
> * * * *
>
> PHMSA plans to use information from the 2013 Gas Transmission and Gathering Pipeline Systems Annual Report to develop potential rulemaking for cases in which the records of the owner or operator are insufficient to confirm the established MAOP of a pipeline segment within Class 3 and Class 4 locations and in Class 1 and Class 2 locations in HCAs. Owners and operators should consider the guidance in this advisory for all pipeline segments and take action as appropriate to assure that all MAOP and MOP [maximum operating pressure] are supported by records that are traceable, verifiable and complete.
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> * * * *
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> Finally, PHMSA notes that on September 26, 2011, NTSB issued Recommendation P-11-14: Eliminating Grandfather Clause. Section 192.619(a)(3) allows gas transmission operators to establish MAOP of pipe installed before July 1, 1970, by use of records noting the highest actual operating pressure to which the segment was subjected during the five years preceding July 1, 1970. NTSB Recommendation P–11–14 requests that PHMSA delete § 192.619(a)(3), also known as the 'grandfather clause,'

[7] 76 Fed. Reg. 1504, 1507 (January 10, 2011).
[8] 77 Fed. Reg. 26822 (May 7, 2012).

> and require gas transmission pipeline operators to reestablish MAOP using hydrostatic pressure testing. PHMSA reminds operators that this recommendation will be acted upon following the collection of data, including information from the 2013 Gas Transmission and Gathering Pipeline Systems Annual Report, which will allow PHMSA to determine the impact of the requested change on the public and industry in conformance with our statutory obligations."[9]

Q. ARE OPERATORS SUCH AS SOURCEGAS DISTRIBUTION REQUIRED TO COMPLY WITH THESE PHMSA ADVISORY BULLETINS?

A. Yes.

Q. HAVE THERE BEEN ANY SIGNIFICANT RECENT DEVELOPMENTS REGARDING PHMSA'S RULEMAKING PROCEEDINGS, REGULATIONS AND ADVISORY BULLETINS MANDATING MAOP VERIFICATION, ASSESSMENTS AND SYSTEM KNOWLEDGE?

A. Yes. On May 28, 2013, PHMSA issued a notice announcing a public workshop to be held on the concept of ''Integrity Verification Process ("IVP").[10] The IVP is a multiple step process that includes sections on the "grandfather clause" and MAOP records, testing and failure history, location risk (including a new term, Moderate Consequence Areas or "MCAs," that applies to pipelines where the potential impact radius includes one or more homes/structures intended for human occupancy), low stress review for pipe below a certain percentage SMYS, material documentation review, assessment and analysis review, implementation and deadlines. PHMSA has released two versions of its "Draft IVP Chart": the first in July 2013 and the second in September 2013. PHMSA held the public workshop on August 7, 2013.

[9] 77 Fed. Reg. 26822, 26823-24 (May 7, 2012). In its DOT Annual Report for Calendar Year 2013, SourceGas Distribution reported incomplete MAOP records for 0.21 miles within Class 3 locations (in HCA) in Nebraska. See Exhibit CAB-1, page 18.

[10] 78 Fed. Reg. 32010 (May 28, 2013).

PHMSA has stated that this regulatory initiative is intended to address "specific Congressional mandates and [NTSB] recommendations related to recent accidents that have occurred on pipelines with previously undetected integrity issues associated with original material manufacturing, construction, installation, testing, or records."[11] Key drivers are Section 23 of the Pipeline Safety Act and NTSB's Recommendation P-11-14 and other NTSB Recommendations. These mandates and recommendations call for the removal of the existing "grandfather clause," new pressure testing requirements, integrity verification plans for pipeline segments that do not have complete records establishing their maximum operating pressures, and the conversion of all gas transmission pipelines to accommodate inspection by inline inspection ("ILI") technology. According to PHMSA, "the definition for MCAs [is] to be established in future regulations."[12]

Q. WHY IS PHMSA'S IVP SUCH A SIGNIFICANT RECENT DEVELOPMENT?

A. PHMSA's IVP is such a significant recent development for several reasons. From a procedural viewpoint, PHMSA's IVP represents a sea change departure from how PHMSA previously has promulgated its regulations. In essence, the IVP represents what the industry is calling a "mega rule" that seeks to address, *jointly*, MAOP verification requirements required by Section 5 of the Pipeline Safety Act *and* the expansion of integrity management program requirements, associated with assessments and system knowledge, called for by Section 23 of the Pipeline Safety Act. It is by far the largest single rulemaking that the pipeline industry has ever considered.

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[11] PHMSA's Pipeline Integrity Verification Process Workshop, "Event Summary Report" (dated August 7, 2013), p. 1. A copy of this document is available at http://primis.phmsa.dot.gov/meetings/FilGet.mtg?fil=552.

[12] *Id.* at p. 7. PHMSA's "Draft IVP Chart" dated September 10, 2013, which is being provided as Exhibit CAB-16, states that an MCA "means non-HCA pipe in Class 4, 3, or 2 locations, & Class 1 locations with 1 house/occupied site in PIR [Potential Impact Radius]."

From a substantive standpoint, the industry expects that the IVP will change the way pipeline operators run their business on a daily basis. In comments filed with PHMSA on October 9, 2013, the AGA stated:

> "[E]stablishing requirements to test previously untested transmission pipelines outside of HCAs or below 30% SMYS would immediately bring thousands of miles of lower risk and lower consequence pipelines into this enhanced regulatory process, dramatically increasing the cost to customers, impact to operators and timeline to implement…. Operators have explained that it will take 10 to 15 years to complete MAOP verification testing in HCAs."[13]

> "[T]he revised PHMSA draft IVP represents 75 percent of the total transmission mileage operated by LDCs [local distribution companies], which is a 600 percent increase over the mileage covered by the current HCA definition being applied by industry. AGA members have approximately 55,000 miles of transmission pipelines, of which approximately 45,000 miles of pipeline will be impacted by the revised draft PHMSA IVP process and only 10,000 miles would continue to operate under existing 49 CFR 192 regulations."[14]

Q. WHAT DOES PHMSA'S IVP MEAN FOR THE STATUS OF THE FEDERAL REGULATORY ENVIRONMENT OF PIPELINE SYSTEM SAFETY AND INTEGRITY?

A. PHMSA's IVP validates my earlier statements that it is not clear if or when the fundamental change of direction in the way that the natural gas industry is regulated will settle into a more predictable routine, and that it may take several years before the natural gas industry can extrapolate if and when this fundamental change of direction may settle into a more predictable routine. This fundamental change in direction places greater burdens on pipeline operators such as SourceGas Distribution to implement the requirements of ever-changing federal regulations and

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[13] Docket No. PHMSA-2013-0119, Pipeline Safety: Public Workshop on the Integrity Verification Process, "The Third Set of Comments of the American Gas Association on the Revised PHMSA Draft Integrity Verification Process" (filed October 9, 2013), p. 5. AGA's Third Set of Comments is available at http://www.regulations.gov/ #!documentDetail;D=PHMSA-2013-0119-0083.

[14] *Id.* at p. 8.

requires that the costs of compliance be recovered on a concurrent basis as the costs are incurred.

V. PROJECTS AND INITIATIVES REFLECTED IN THE PROPOSED SYSTEM SAFETY AND INTEGRITY RIDER

Q. HAVE YOU REVIEWED THE DIRECT TESTIMONY OF JERRAD S. HAMMER PREFILED IN THIS DOCKET?

A. Yes. Mr. Hammer's Direct Testimony describes and justifies the System Safety and Integrity Rider, or SSIR, that SourceGas Distribution is proposing in this docket. Section V of Mr. Hammer's Direct Testimony explains the mechanics of the Company's proposed SSIR Tariff, which is designed to collect Eligible System Safety and Integrity Costs.

Q. WHAT ARE "ELIGIBLE SYSTEM SAFETY AND INTEGRITY COSTS?"

A. Mr. Hammer provides a detailed definition of this term in his Direct Testimony, but, generally speaking, Eligible System Safety and Integrity Costs are eligible capital costs and O&M expenses related to System Safety and Integrity Projects.

Q. WHAT ARE "SYSTEM SAFETY AND INTEGRITY PROJECTS?"

A. Mr. Hammer's Direct Testimony states that the proposed SSIR Tariff defines System Safety and Integrity Projects to mean one of the following four types of "Projects":

1. Projects to comply with the TIMP Rule, including projects in accordance with SourceGas's TIMP and projects in accordance with State enforcement of the TIMP Rule and SourceGas's TIMP;
2. Projects to comply with the DIMP Rule, including projects in accordance with SourceGas's DIMP and projects in accordance with State enforcement of the DIMP Rule and SourceGas's DIMP;

3. Projects to comply with PHMSA's final rules and regulations that become effective on or after the filing date of the Application requesting approval of the SSIR; and

4. Facility relocation projects with a per-project total cost of $20,000 or more, exclusive of all costs that have been, are being, or will be reimbursed otherwise, required due to construction or improvement of a highway, road, street, public way or other public work by or on behalf of the United States, the State of Nebraska, a political subdivision of the State of Nebraska or another entity having the power of eminent domain.

Q. IN THE PREVIOUS SECTION OF YOUR DIRECT TESTIMONY, YOU ADDRESS THE FIRST THREE TYPES OF SYSTEM SAFETY AND INTEGRITY PROJECTS. HOW DOES THE FOURTH TYPE OF PROJECT, FACILITY RELOCATION PROJECTS, PROMOTE PIPELINE SYSTEM SAFETY AND INTEGRITY?

A. From time to time, the State of Nebraska or a municipality in which SourceGas Distribution provides service, for example, will undertake projects, such as change of grade, new construction, installation or repair of sewers, storm sewers, drainages, waterlines, power lines, communication systems, right-of-ways or other public works. Some of these projects require SourceGas Distribution to change the position of its natural gas mains, service connections or other aspects of its natural gas system. In such cases, relocation of SourceGas Distribution's system away from the affected public works enables the State or municipality to continue to provide, or enhance or expand, public services, and the Company to continue to provide natural gas services, in a manner that does not jeopardize the health, safety or welfare of residents and businesses.

Q. DOES THE SYSTEM SAFETY AND INTEGRITY RIDER APPROVED BY THE COLORADO PUBLIC UTILITIES COMMISSION ("PUC") FOR ROCKY MOUNTAIN INCLUDE FACILITY RELOCATION PROJECTS IN THE DEFINITION OF SYSTEM SAFETY AND INTEGRITY PROJECTS?

A. No, it does not. In its application requesting Colorado PUC approval of its System Safety and Integrity Rider, Rocky Mountain did include facility relocation projects in the definition of System Safety and Integrity Projects. Ultimately, Rocky Mountain agreed to remove facility relocation projects from the definition of System Safety and Integrity Projects as part of a comprehensive stipulation and settlement among all parties in its consolidated Rocky Mountain rate case and SSIR case (Proceeding Nos. 13A-0046G *et al.*).

Q. PLEASE EXPLAIN WHY SOURCEGAS DISTRIBUTION IS PROPOSING IN THIS APPLICATION TO INCLUDE FACILITY RELOCATION PROJECTS IN THE DEFINITION OF SYSTEM SAFETY AND INTEGRITY PROJECTS.

A. Facility relocation projects are directly related to pipeline safety and integrity activities. Such projects are an integral step in the overall safety and integrity process. The relocation costs requested by the Company are projects over which the Company does not have control; these projects are required by government entities to enhance the public welfare, including safety.

Further, if the Company were not to relocate facilities to accommodate these government-mandated projects, then safety and integrity issues are likely to result because the pipeline either will be located in an unsafe or inaccessible location or will be in the way of other construction activities that could result in an unsafe work environment and/or compromise the integrity of the pipeline.

It also is important to note that the State of Nebraska already has authorized jurisdictional utilities to recover costs associated with facility relocation projects under Sections 66-1865 and 66-1866 of the Act. Section 1802(14)(c) of the Act defines the term “jurisdictional utility plant projects” for the purpose of determining an infrastructure system replacement cost recovery charge under Sections 66-1865 and 66-1866 of the Act to mean: “Facility relocations required due to construction or improvement of a highway, road, street, public way, or other public work by or on behalf of the United States, this state, a political subdivision on this state, or another entity having the power of eminent domain, if the costs related to such relocations have not been reimbursed to the jurisdictional utility.” The Company is requesting the same authority under its proposed SSIR Tariff.

Q. WHY IS SOURCEGAS DISTRIBUTION PROPOSING A PER FACILITY RELOCATION PROJECT TOTAL COST OF $20,000 OR MORE FOR ELIGIBILITY AS A SYSTEM SAFETY AND INTEGRITY PROJECT?

A. Utilities work daily with the United States, the State of Nebraska, municipalities and other entities having the power of eminent domain to coordinate public works projects, natural gas projects, and the location of public works and natural gas facilities. Simply to reduce significantly the sheer number of non-reimbursable facility relocation projects eligible for recovery as a Project, SourceGas Distribution decided to place a $20,000 per project minimum requirement on eligibility under the proposed SSIR Tariff.

Q. HAVE YOU PREPARED A DOCUMENT DESCRIBING THE SYSTEM SAFETY AND INTEGRITY PROJECTS AND INITIATIVES THAT SOURCEGAS DISTRIBUTION IS UNDERTAKING IN 2014?

A. Yes. Exhibit CAB-17 is a document that I prepared titled "2014 Projects and Initiatives Reflected in the Proposed System Safety and Integrity Rider for SourceGas Distribution LLC in Nebraska," and dated May 1, 2014. Attachment 1 to Exhibit CAB-17 is a one-page Excel workbook that summarizes and itemizes SourceGas Distribution's projected capital costs and O&M expenses for 2014 for projects and initiatives covered by the proposed System Safety and Integrity Rider in Nebraska.

Q. PLEASE DESCRIBE EXHIBIT CAB-17.

A. Exhibit CAB-17 contains two primary sections. Section I is an "Introduction" of the SSIR. Section II identifies and describes SourceGas Distribution's "2014 Projects and Initiatives" reflected in the proposed SSIR.

Q. PLEASE DESCRIBE SECTION II OF EXHIBIT CAB-17.

A. Section II of Exhibit CAB-17 groups SourceGas Distribution's 2014 SSIR projects and initiatives into nine categories that are presented in the following lettered subsections:

A. Replacement of Bare Steel Distribution Main
B. Replacement of Transmission Pipeline
C. Barricades
D. Cathodic Protection and Corrosion Prevention
E. Span Replacements
F. Town Border Stations
G. Top of Ground (TOG) Replacement
H. Centerline Surveys
I. MAOP Verification

Each of the nine subsections includes a "Background" discussion (paragraph numbered 1), the "SSIR Project Classification" (paragraph numbered 2) that identifies the Project "Classification Under the SSIR Tariff" and the "Objective Criteria Analyzed" by the Company, a "Project Description" (paragraph numbered 3) and a discussion of each of the "Specific Projects" (paragraph numbered 4).

Q. WHAT COSTS DOES SOURCEGAS DISTRIBUTION EXPECT TO INCUR FOR THE 2014 SSIR PROJECTS AND INITIATIVES IDENTIFIED IN EXHIBIT CAB-17?

A. Attachment 1 to Exhibit CAB-17 itemizes SourceGas Distribution's projected 2014 capital costs and O&M expenses for projects and initiatives to be covered under the proposed SSIR Tariff. In total, SourceGas Distribution's projected capital expenditures for SSIR projects and initiatives in 2014 total $11,627,216 and its projected O&M expenses for SSIR projects and initiatives in 2014 total $65,312. I have provided Attachment 1 to Exhibit CAB-17 to Mr. Hammer to develop the revenue requirement associated with the 2014 SSIR projects and initiatives and to develop the proposed System Safety and Integrity Rider Charges.

Q. WILL SOURCEGAS DISTRIBUTION TRACK ACTUAL ELIGIBLE SYSTEM SAFETY AND INTEGRITY COSTS RELATED TO SYSTEM SAFETY AND INTEGRITY PROJECTS AND INITIATIVES?

A. Yes. The dollar amounts identified above and itemized in Attachment 1 of Exhibit CAB-17 are projected capital costs and projected O&M expenses for specified projects and initiatives covered by the proposed SSIR Tariff. SourceGas Distribution will track actual capital costs and actual O&M expenses related to those projects and initiatives. Mr. Hammer's Direct Testimony addresses how the Company proposes to reconcile projected Eligible System Safety and Integrity Costs with actual Eligible System Safety and Integrity Costs.

Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

A. Yes. I respectfully request that the Commission approve the SSIR Tariff being proposed by SourceGas Distribution as being just and reasonable and in the public interest. I will conclude by offering into evidence Exhibits CAB-1 through CAB-17.