

Edgar Filing: ONE Gas, Inc. - Form 10-Q

ONE Gas, Inc.
Form 10-Q
October 29, 2015

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

X Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended September 30, 2015.

OR

___ Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from _____ to _____.

Commission file number 001-36108

ONE Gas, Inc.

(Exact name of registrant as specified in its charter)

Oklahoma

(State or other jurisdiction of
incorporation or organization)

46-3561936

(I.R.S. Employer Identification No.)

15 East Fifth Street, Tulsa, OK

(Address of principal executive offices)

74103

(Zip Code)

Registrant's telephone number, including area code (918) 947-7000

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X No ___

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes X No ___

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Edgar Filing: ONE Gas, Inc. - Form 10-Q

Large accelerated filer ☒ X
company___

Accelerated filer ___

Non-accelerated filer ___

Smaller reporting

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes ___ No ☒ X

On October 20, 2015, the Company had 52,154,655 shares of common stock outstanding.

This page intentionally left blank.

ONE Gas, Inc.

TABLE OF CONTENTS

<u>Part I.</u>	<u>Financial Information</u>	<u>Page No.</u>
<u>Item 1.</u>	<u>Financial Statements (Unaudited)</u>	<u>6</u>
	Statements of Income - Three and Nine Months Ended September 30, 2015 and 2014	<u>6</u>
	Statements of Comprehensive Income - Three and Nine Months Ended September 30, 2015 and 2014	<u>7</u>
	Balance Sheets - September 30, 2015 and December 31, 2014	<u>8</u>
	Statements of Cash Flows - Nine Months Ended September 30, 2015 and 2014	<u>11</u>
	Statement of Equity - Nine Months Ended September 30, 2015	<u>12</u>
	Notes to Financial Statements	<u>14</u>
<u>Item 2.</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>22</u>
<u>Item 3.</u>	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>32</u>
<u>Item 4.</u>	<u>Controls and Procedures</u>	<u>32</u>
<u>Part II.</u>	<u>Other Information</u>	<u>33</u>
<u>Item 1.</u>	<u>Legal Proceedings</u>	<u>33</u>
<u>Item 1A.</u>	<u>Risk Factors</u>	<u>33</u>
<u>Item 2.</u>	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>33</u>
<u>Item 3.</u>	<u>Defaults Upon Senior Securities</u>	<u>33</u>
<u>Item 4.</u>	<u>Mine Safety Disclosures</u>	<u>33</u>
<u>Item 5.</u>	<u>Other Information</u>	<u>33</u>
<u>Item 6.</u>	<u>Exhibits</u>	<u>33</u>
<u>Signature</u>		<u>35</u>

As used in this Quarterly Report, references to “we,” “our,” “us” or the “company” refer to ONE Gas, Inc., an Oklahoma corporation, and its predecessors and subsidiary, unless the context indicates otherwise.

The statements in this Quarterly Report that are not historical information, including statements concerning plans and objectives of management for future operations, economic performance or related assumptions, are forward-looking statements. Forward-looking statements may include words such as “anticipate,” “estimate,” “expect,” “project,” “intend,” “plan,” “believe,” “should,” “goal,” “forecast,” “guidance,” “could,” “may,” “continue,” “might,” “potential,” “scheduled” and other words of similar meaning. Although we believe that our expectations regarding future events are based on reasonable assumptions, we can give no assurance that such expectations or assumptions will be achieved. Important factors that could cause actual results to differ materially from those in the forward-looking statements are described under Part I, Item 2, Management’s Discussion and Analysis of Financial Condition and Results of Operations, “Forward-Looking Statements,” in this Quarterly Report and under Part I, Item 1A, “Risk Factors,” in our Annual Report.

INFORMATION AVAILABLE ON OUR WEBSITE

We make available, free of charge, on our website (www.onegas.com) copies of our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, amendments to those reports filed or furnished to the SEC pursuant to Section 13(a) or 15(d) of the Exchange Act and reports of holdings of our securities filed by our officers and directors under Section 16 of the Exchange Act as soon as reasonably practicable after filing such material electronically or otherwise furnishing it to the SEC. Copies of our Code of Business Conduct and Ethics, Corporate Governance Guidelines and Director Independence Guidelines are also available on our website, and we will provide copies of these documents upon request. Our website and any contents thereof are not incorporated by reference into this report.

We also make available on our website the Interactive Data Files required to be submitted and posted pursuant to Rule 405 of Regulation S-T.

GLOSSARY

The abbreviations, acronyms and industry terminology used in this Quarterly Report are defined as follows:

Annual Report	Annual Report on Form 10-K for the year ended December 31, 2014
Bcf	Billion cubic feet
CERCLA	Federal Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended
Clean Air Act	Federal Clean Air Act, as amended
Clean Water Act	Federal Water Pollution Control Amendments of 1972, as amended
CNG	Compressed natural gas
DOT	United States Department of Transportation
EPA	United States Environmental Protection Agency
EPARR	El Paso Annual Rate Review
EPS	Earnings per share
EPSA	El Paso Service Area
Exchange Act	Securities Exchange Act of 1934, as amended
GAAP	Accounting principles generally accepted in the United States of America
GRIP	Texas Gas Reliability Infrastructure Program
Heating Degree Day or HDD	A measure designed to reflect the demand for energy needed for heating based on the extent to which the daily average temperature falls below a reference temperature for which no heating is required, usually 65 degrees Fahrenheit
KCC	Kansas Corporation Commission
KDHE	Kansas Department of Health and Environment
LDCs	Local distribution companies
LIBOR	London Interbank Offered Rate
MMcf	Million cubic feet
Moody's	Moody's Investors Service, Inc.
NYSE	New York Stock Exchange
OCC	Oklahoma Corporation Commission
ONE Gas	ONE Gas, Inc.
ONE Gas Credit Agreement	ONE Gas' \$700 million revolving credit agreement, which expires January, 2019
ONE Gas Predecessor	ONE Gas' predecessor for accounting purposes that consists of the business attributable to ONEOK's natural gas distribution segment that was transferred to ONE Gas in connection with its separation from ONEOK
ONEOK	ONEOK, Inc. and its subsidiaries
PGA	Purchased Gas Adjustment Clause
PHMSA	United States Department of Transportation Pipeline and Hazardous Materials Safety Administration
Pipeline Safety, Regulatory Certainty and Job Creation Act	Pipeline Safety, Regulatory Certainty and Job Creation Act of 2011, as amended
Quarterly Report(s)	Quarterly Report(s) on Form 10-Q
RRC	Railroad Commission of Texas
S&P	Standard & Poor's Ratings Services
SEC	Securities and Exchange Commission
Securities Act	Securities Act of 1933, as amended
Separation and Distribution Agreement	

Separation and Distribution Agreement dated January 14, 2014, between
ONEOK
and ONE Gas
eXtensible Business Reporting Language

XBRL

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

ONE Gas, Inc.

STATEMENTS OF INCOME

(Unaudited)	Three Months Ended September 30,		Nine Months Ended September 30,		
	2015	2014	2015	2014	
(Thousands of dollars, except per share amounts)					
Revenues	\$225,226	\$241,522	\$1,158,543	\$1,304,538	
Cost of natural gas	54,724	75,070	548,226	701,757	
Net margin	170,502	166,452	610,317	602,781	
Operating expenses					
Operations and maintenance	98,698	101,829	304,681	309,154	
Depreciation and amortization	33,956	31,217	98,592	93,995	
General taxes	12,897	14,287	41,818	44,348	
Total operating expenses	145,551	147,333	445,091	447,497	
Operating income	24,951	19,119	165,226	155,284	
Other income	166	8	1,051	1,005	
Other expense	(1,884	) (652	) (2,840	) (1,829	)
Interest expense, net	(11,233	) (11,160	) (33,592	) (35,886	)
Income before income taxes	12,000	7,315	129,845	118,574	
Income taxes	(4,629	) (2,662	) (50,017	) (45,391	)
Net income	\$7,371	\$4,653	\$79,828	\$73,183	
Earnings per share					
Basic	\$0.14	\$0.09	\$1.52	\$1.40	
Diluted	\$0.14	\$0.09	\$1.50	\$1.38	
Average shares (thousands)					
Basic	52,408	52,361	52,627	52,353	
Diluted	53,072	53,014	53,315	52,848	
Dividends declared per share of stock	\$0.30	\$0.28	\$0.90	\$0.56	

See accompanying Notes to Financial Statements.

ONE Gas, Inc.

STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2015	2014	2015	2014
	(Thousands of dollars)			
Net income	\$7,371	\$4,653	\$79,828	\$73,183
Other comprehensive income (loss), net of tax				
Change in pension and other postretirement benefit plan liability, net of tax of \$(88), \$49, \$(264) and \$98, respectively	141	(78)	) 423	(156)
Total other comprehensive income (loss), net of tax	141	(78)	) 423	(156)
Comprehensive income	\$7,512	\$4,575	\$80,251	\$73,027
See accompanying Notes to Financial Statements.				

ONE Gas, Inc.
BALANCE SHEETS

	September 30, 2015	December 31, 2014
(Unaudited)		
Assets		
Property, plant and equipment		
Property, plant and equipment	\$5,040,313	\$4,850,201
Accumulated depreciation and amortization	1,604,509	1,556,481
Net property, plant and equipment	3,435,804	3,293,720
Current assets		
Cash and cash equivalents	52,974	11,943
Accounts receivable, net	103,406	326,749
Materials and supplies	33,400	27,511
Income tax receivable	23,725	43,800
Natural gas in storage	159,912	185,300
Regulatory assets	31,703	50,193
Other current assets	12,227	22,005
Total current assets	417,347	667,501
Goodwill and other assets		
Regulatory assets	440,312	478,723
Goodwill	157,953	157,953
Other assets	54,905	51,313
Total goodwill and other assets	653,170	687,989
Total assets	\$4,506,321	\$4,649,210
See accompanying Notes to Financial Statements.		

ONE Gas, Inc.
BALANCE SHEETS
(Continued)

	September 30, 2015	December 31, 2014
(Unaudited)		
Equity and Liabilities		(Thousands of dollars)
Equity and long-term debt		
Common stock, \$0.01 par value:		
authorized 250,000,000 shares; issued 52,598,005 shares and outstanding 52,151,279 shares at	\$526	\$521
September 30, 2015; issued and outstanding 52,083,859 shares at December 31, 2014		
Paid-in capital	1,762,508	1,758,796
Retained earnings	71,746	39,894
Accumulated other comprehensive income (loss)	(4,751)	(5,174)
Treasury stock, at cost: 446,726 shares at September 30, 2015	(19,108)	—
Total equity	1,810,921	1,794,037
Long-term debt, excluding current maturities	1,201,306	1,201,311
Total equity and long-term debt	3,012,227	2,995,348
Current liabilities		
Current maturities of long-term debt	7	6
Notes payable	—	42,000
Accounts payable	57,240	159,064
Accrued interest	7,647	18,872
Accrued taxes other than income	40,429	44,742
Accrued liabilities	18,000	26,019
Customer deposits	58,331	60,003
Regulatory liabilities	41,337	32,467
Other current liabilities	10,478	9,260
Total current liabilities	233,469	392,433
Deferred credits and other liabilities		
Deferred income taxes	907,647	894,585
Employee benefit obligations	274,073	287,779
Other deferred credits	78,905	79,065
Total deferred credits and other liabilities	1,260,625	1,261,429
Commitments and contingencies		
Total liabilities and equity	\$4,506,321	\$4,649,210
See accompanying Notes to Financial Statements.		

This page intentionally left blank.

ONE Gas, Inc.
STATEMENTS OF CASH FLOWS

(Unaudited)	Nine Months Ended September 30,	
	2015	2014
	(Thousands of dollars)	
Operating activities		
Net income	\$79,828	\$73,183
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	98,592	93,995
Deferred income taxes	19,384	2,828
Share-based compensation expense	3,863	5,651
Provision for doubtful accounts	2,951	5,019
Changes in assets and liabilities:		
Accounts receivable	220,392	216,219
Materials and supplies	(5,889)	) 6,238
Income tax receivable	20,075	(4,862)
Natural gas in storage	25,388	(51,192)
Asset removal costs	(33,744)	) (34,963)
Accounts payable	(104,948)	) (70,063)
Accrued interest	(11,225)	) 7,521
Accrued taxes other than income	(4,313)	) 11,060
Accrued liabilities	(8,019)	) 15,977
Customer deposits	(1,672)	) (43)
Regulatory assets and liabilities	64,368	23,308
Other assets and liabilities	(15,493)	) (49,868)
Cash provided by operating activities	349,538	250,008
Investing activities		
Capital expenditures	(199,678)	) (224,619)
Cash used in investing activities	(199,678)	) (224,619)
Financing activities		
Repayments of notes payable	(42,000)	) —
Repurchase of common stock	(24,122)	) —
Issuance of debt, net of discounts	—	1,199,994
Long-term debt financing costs	—	(11,078)
Cash payment to ONEOK upon separation	—	(1,130,000)
Issuance of common stock	4,471	1,330
Dividends paid	(47,178)	) (29,121)
Cash provided by (used in) financing activities	(108,829)	) 31,125
Change in cash and cash equivalents	41,031	56,514
Cash and cash equivalents at beginning of period	11,943	3,171
Cash and cash equivalents at end of period	\$52,974	\$59,685
See accompanying Notes to Financial Statements.		

ONE Gas, Inc.
STATEMENT OF EQUITY

(Unaudited)

	Common Stock Issued (Shares)	Common Stock (Thousands of dollars)	Paid-in Capital (Thousands of dollars)
January 1, 2015	52,083,859	\$521	\$1,758,796
Net income	—	—	—
Other comprehensive income	—	—	—
Repurchase of common stock	—	—	—
Common stock issued and other	514,146	5	2,914
Common stock dividends - \$0.90 per share	—	—	798
September 30, 2015	52,598,005	\$526	\$1,762,508
See accompanying Notes to Financial Statements.			

ONE Gas, Inc.
 STATEMENT OF EQUITY
 (Continued)

(Unaudited)	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Total Equity
	(Thousands of dollars)			
January 1, 2015	\$39,894	\$—	\$(5,174	)\$1,794,037
Net income	79,828	—	—	79,828
Other comprehensive income	—	—	423	423
Repurchase of common stock	—	(24,122	)—	(24,122)
Common stock issued and other	—	5,014	—	7,933
Common stock dividends - \$0.90 per share	(47,976	)—	—	(47,178)
September 30, 2015	\$71,746	\$(19,108	)\$(4,751	)\$1,810,921
See accompanying Notes to Financial Statements.				

ONE Gas, Inc.

NOTES TO FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Our accompanying unaudited financial statements have been prepared pursuant to the rules and regulations of the SEC. These statements also have been prepared in accordance with GAAP and reflect all adjustments that, in our opinion, are necessary for a fair statement of the results for the interim periods presented. All such adjustments are of a normal recurring nature. The 2014 year-end balance sheet data was derived from audited financial statements, but does not include all disclosures required by GAAP. These unaudited financial statements should be read in conjunction with the audited financial statements and footnotes in our Annual Report. Due to the seasonal nature of our business, the results of operations for the three and nine months ended September 30, 2015, are not necessarily indicative of the results that may be expected for a 12-month period.

Separation - Prior to January 31, 2014, ONE Gas, Inc. was a wholly owned subsidiary of ONEOK and comprised its former natural gas distribution business. On January 31, 2014, we became an independent, publicly traded company as a result of a distribution by ONEOK of our common stock to ONEOK's shareholders. Our common stock began trading "regular-way" under the ticker symbol "OGS" on the NYSE on February 3, 2014.

We provide natural gas distribution services to more than 2 million customers in Oklahoma, Kansas and Texas through Oklahoma Natural Gas, Kansas Gas Service and Texas Gas Service, respectively. We serve residential, commercial, industrial and transportation customers in all three states. In addition, we also provide natural gas distribution services to wholesale and public authority customers.

Basis of Presentation - Prior to our separation from ONEOK, our financial statements were derived from ONEOK's financial statements, which included its natural gas distribution business as if we, for accounting purposes, had been a separate company for all periods presented. The financial statements for periods prior to the separation also include expense allocations for certain corporate functions historically performed by ONEOK, including allocations of general corporate expenses related to executive oversight, accounting, treasury, tax, legal, information technology and other services. We believe our assumptions underlying the financial statements, including the assumptions regarding the allocation of general corporate expenses from ONEOK, are reasonable. However, the financial statements may not include all of the actual expenses that would have been incurred by us and may not reflect our results of operations, financial position and cash flows had we been a separate publicly traded company during the periods presented prior to the separation.

All financial information presented after the separation represents the results of operations, financial position and cash flows of ONE Gas. Accordingly:

Our Statements of Income and Comprehensive Income for the three and nine months ended September 30, 2014, consist of the results of ONE Gas for the three and eight months ended September 30, 2014, and the results of ONE Gas Predecessor for the one month ended January 31, 2014.

Our Statement of Cash Flows for the nine months ended September 30, 2014, consists of the results of ONE Gas for the eight months ended September 30, 2014, and the results of ONE Gas Predecessor for the one month ended January 31, 2014.

Use of Estimates - The preparation of our financial statements and related disclosures in accordance with GAAP requires us to make estimates and assumptions with respect to values or conditions that cannot be known with certainty that affect the reported amount of assets and liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements. These estimates and assumptions also affect the reported amounts of revenue and expenses during the reporting period. Items that may be estimated include, but are not limited to, the economic useful life of assets, fair value of assets and liabilities, provision for doubtful accounts, unbilled revenues for natural

gas delivered but for which meters have not been read, natural gas purchased but for which no invoice has been received, provision for income taxes, including any deferred tax valuation allowances, the results of litigation and various other recorded or disclosed amounts.

We evaluate these estimates on an ongoing basis using historical experience and other methods we consider reasonable based on the particular circumstances. Nevertheless, actual results may differ significantly from the estimates. Any effects on our financial position or results of operations from revisions to these estimates are recorded in the period when the facts that give rise to the revision become known.

Related-Party Transactions - Prior to our separation from ONEOK on January 31, 2014, we had certain transactions with ONEOK, including, but not limited to, natural gas supply, allocated corporate services, employee benefits, cash management,

derivatives and long-term lines of credit. Following the separation, any services we receive from ONEOK are now third-party transactions. The remaining related-party transactions are not material.

Segments - We operate in one reportable business segment: regulated public utilities that deliver natural gas to residential, commercial, industrial, wholesale, public authority and transportation customers. The accounting policies for our segment are the same as described in Note 1 of our Notes to Financial Statements in our Annual Report. We evaluate our financial performance principally on operating income. For the three and nine months ended September 30, 2015, and 2014, we had no single external customer from which we received 10 percent or more of our gross revenues.

Goodwill Impairment Test - We assess our goodwill for impairment at least annually as of July 1. At July 1, 2015, we assessed qualitative factors to determine whether it was more likely than not that the fair value of our reporting unit was less than its carrying amount. After assessing qualitative factors (including macroeconomic conditions, industry and market considerations, cost factors and overall financial performance), we determined that no further testing was necessary.

Recently Issued Accounting Standards Update - In August 2015, the FASB issued ASU 2015-15, "Interest-Imputation of Interest (Subtopic 835-30)," which specifically addresses the presentation and subsequent measurement of debt issuance costs associated with line of credit arrangements. We do not expect this issued guidance, which will be adopted concurrently with ASU 2015-03, to have a material impact on our financial statements.

In April 2015, the FASB issued ASU 2015-03, "Interest-Imputation of Interest," which requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability. We do not expect this issued guidance, which is required to be adopted for our interim and annual reports for periods beginning after December 15, 2015, to have a material impact on our financial statements.

In April 2015, the FASB issued ASU 2015-05, "Intangibles-Goodwill and Other-Internal-Use Software," which helps entities evaluate the accounting for fees paid by a customer in a cloud computing arrangement. We are evaluating the impact of this issued guidance, which is required to be adopted for our interim and annual reports for periods beginning after December 15, 2015.

In May 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers," which clarifies and converges the revenue recognition principles under GAAP and International Financial Reporting Standards. In July 2015, FASB delayed the effective date for one year. We are evaluating the impact of this issued guidance, which is required to be adopted for our interim and annual reports beginning with the first quarter 2018.

2. REGULATORY ASSETS AND LIABILITIES

The tables below present a summary of regulatory assets, net of amortization, and liabilities for the periods indicated:

	September 30, 2015		
	Current	Noncurrent	Total
	(Thousands of dollars)		
Under-recovered purchased-gas costs	\$10,354	\$—	\$10,354
Pension and postretirement benefit costs (see Note 8)	19,445	429,346	448,791
Reacquired debt costs	812	9,122	9,934
Other	1,092	1,844	2,936
Total regulatory assets, net of amortization	31,703	440,312	472,015
Accumulated removal costs (a)	—	(11,846)	(11,846)
Weather normalization	(5,821)	—	(5,821)
Over-recovered purchased-gas costs	(33,363)	—	(33,363)

Edgar Filing: ONE Gas, Inc. - Form 10-Q

Ad valorem tax	(2,153)	—	(2,153)
Total regulatory liabilities	(41,337)	(11,846)	(53,183)
Net regulatory assets (liabilities)	\$(9,634)	\$428,466	\$418,832

(a) Included in other deferred credits in our Balance Sheets.

15

	December 31, 2014		
	Current	Noncurrent	Total
	(Thousands of dollars)		
Under-recovered purchased-gas costs	\$28,712	\$—	\$28,712
Pension and postretirement benefit costs	18,108	466,684	484,792
Reacquired debt costs	812	9,730	10,542
Other	2,561	2,309	4,870
Total regulatory assets, net of amortization	50,193	478,723	528,916
Accumulated removal costs (a)	—	(15,451)	(15,451)
Weather normalization	(16,516)	—	(16,516)
Over-recovered purchased-gas costs	(13,055)	—	(13,055)
Ad valorem tax	(2,896)	—	(2,896)
Total regulatory liabilities	(32,467)	(15,451)	(47,918)
Net regulatory assets (liabilities)	\$17,726	\$463,272	\$480,998
(a) Included in other deferred credits in our Balance Sheets.			

Regulatory assets on our Balance Sheets, as authorized by various regulatory authorities, are probable of recovery. Base rates are designed to provide a recovery of costs during the period rates are in effect, but do not generally provide for a return on investment for amounts we have deferred as regulatory assets. All of our regulatory assets are subject to review by the respective regulatory authorities during future regulatory proceedings. We are not aware of any evidence that these costs will not be recoverable through either riders or base rates, and we believe that we will be able to recover such costs, consistent with our historical recoveries.

Purchased-gas costs include the costs that have been over- or under-recovered from customers through the purchased-gas cost adjustment mechanisms and also include natural gas utilized in our operations, premiums paid and any cash settlements received from our purchased natural gas call options.

3. CREDIT FACILITY AND SHORT-TERM NOTES PAYABLE

ONE Gas Credit Agreement - The ONE Gas Credit Agreement contains certain financial, operational and legal covenants. Among other things, these covenants include maintaining ONE Gas' debt-to-capital ratio of no more than 70 percent at the end of any calendar quarter. The ONE Gas Credit Agreement also contains customary affirmative and negative covenants, including covenants relating to liens, indebtedness of subsidiaries, investments, changes in the nature of business, fundamental changes, transactions with affiliates, burdensome agreements and use of proceeds. In the event of a breach of certain covenants by ONE Gas, amounts outstanding under the ONE Gas Credit Agreement may become due and payable immediately. At September 30, 2015, our debt-to-capital ratio was 40 percent and we were in compliance with all covenants under the ONE Gas Credit Agreement.

The ONE Gas Credit Agreement includes a \$50 million sublimit for the issuance of standby letters of credit and also features an option to request an increase in the size of the facility to an aggregate of \$1.2 billion from \$700 million upon satisfaction of customary conditions, including receipt of commitments from new lenders or increased commitments from existing lenders. Borrowings made under the facility are available for general corporate purposes. The ONE Gas Credit Agreement contains provisions for an applicable margin rate and an annual facility fee, both of which adjust with changes in our credit rating. Based on our current credit ratings, borrowings, if any, will accrue interest at LIBOR plus 79.5 basis points, and the annual facility fee is 8 basis points.

We have a commercial paper program under which we may issue unsecured commercial paper up to a maximum amount of \$700 million to fund short-term borrowing needs. The maturities of the commercial paper notes may vary but may not exceed 270 days from the date of issue. The commercial paper notes are generally sold at par less a discount representing an interest factor.

The ONE Gas Credit Agreement is available to repay the commercial paper notes, if necessary. Amounts outstanding under the commercial paper program reduce the borrowing capacity under the ONE Gas Credit Agreement. At September 30, 2015, we had no short-term borrowings, \$1.0 million in letters of credit issued under the ONE Gas Credit Agreement and \$699.0 million of remaining credit available under the ONE Gas Credit Agreement.

4. LONG-TERM DEBT

Senior Notes - We have senior notes, consisting of \$300 million of 2.07 percent senior notes due in 2019, \$300 million of 3.61 percent senior notes due in 2024 and \$600 million of 4.658 percent senior notes due in 2044 (collectively, our "Senior Notes"). The indenture governing our Senior Notes includes an event of default upon the acceleration of other indebtedness of \$100 million or more. Such events of default would entitle the trustee or the holders of 25 percent in aggregate principal amount of the outstanding Senior Notes to declare those Senior Notes immediately due and payable in full.

5. EQUITY

Dividends - In October 2015, a dividend of \$0.30 per share (\$1.20 per share on an annualized basis) was declared for shareholders of record on November 13, 2015, payable December 1, 2015.

6. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

The following table sets forth the effect of reclassifications from accumulated other comprehensive income (loss) in our Statements of Income for the periods indicated:

	Three Months Ended		Nine Months Ended		
Details about Accumulated Other Comprehensive Income (Loss) Components	September 30,		September 30,		Affected Line Item in the
	2015	2014	2015	2014	Statements of Income
	(Thousands of dollars)				
Pension and other postretirement benefit plan obligations (a)					
Amortization of net loss	\$12,564	\$8,542	\$37,694	\$25,625	
Amortization of unrecognized prior service cost	(374	)(303	)(1,120	)(909	)
	12,190	8,239	36,574	24,716	
Regulatory adjustments (b)	(11,961	)(8,366	)(35,887	)(24,970	)
	229	(127	) 687	(254	)
	(88	)49	(264	)98	
Total reclassifications for the period	\$141	\$(78	) \$423	\$(156	)
					Income before income taxes
					Income tax expense
					Net income

(a) These components of accumulated other comprehensive income (loss) are included in the computation of net periodic benefit cost. See Note 8 for additional detail of our net periodic benefit cost.

(b) Regulatory adjustments represent pension and other postretirement benefit costs expected to be recovered through rates and are deferred as part of our regulatory assets. See Note 2 for additional disclosures of regulatory assets and liabilities.

7. EARNINGS PER SHARE

Basic EPS is based on net income and is calculated based upon the daily weighted-average number of common shares outstanding during the periods presented. Also, this calculation includes fully vested stock awards that have not yet been issued as common stock. Diluted EPS includes basic EPS, plus unvested stock awards granted under our compensation plans, but only to the extent these instruments dilute earnings per share.

The following tables set forth the computation of basic and diluted EPS from continuing operations for the periods indicated:

Three Months Ended September 30, 2015

Edgar Filing: ONE Gas, Inc. - Form 10-Q

	Income	Shares	Per Share Amount
	(Thousands, except per share amounts)		
Basic EPS Calculation			
Net income available for common stock	\$7,371	52,408	\$0.14
Diluted EPS Calculation			
Effect of dilutive securities	—	664	
Net income available for common stock and common stock equivalents	\$7,371	53,072	\$0.14

	Three Months Ended September 30, 2014		
	Income	Shares	Per Share Amount
	(Thousands, except per share amounts)		
Basic EPS Calculation			
Net income available for common stock	\$4,653	52,361	\$0.09
Diluted EPS Calculation			
Effect of dilutive securities	—	653	
Net income available for common stock and common stock equivalents	\$4,653	53,014	\$0.09

	Nine Months Ended September 30, 2015		
	Income	Shares	Per Share Amount
	(Thousands, except per share amounts)		
Basic EPS Calculation			
Net income available for common stock	\$79,828	52,627	\$1.52
Diluted EPS Calculation			
Effect of dilutive securities	—	688	
Net income available for common stock and common stock equivalents	\$79,828	53,315	\$1.50

	Nine Months Ended September 30, 2014		
	Income	Shares	Per Share Amount
	(Thousands, except per share amounts)		
Basic EPS Calculation			
Net income available for common stock	\$73,183	52,353	\$1.40
Diluted EPS Calculation			
Effect of dilutive securities	—	495	
Net income available for common stock and common stock equivalents	\$73,183	52,848	\$1.38

On January 31, 2014, 51,941,236 shares of our common stock were distributed to ONEOK shareholders in conjunction with the separation. For comparative purposes, and to provide a more meaningful calculation of weighted-average shares outstanding, we have assumed this amount and any shares associated with fully vested stock awards that have not been issued to be outstanding as of the beginning of each period prior to the separation presented in the calculation of weighted-average shares.

8.EMPLOYEE BENEFIT PLANS

The following tables set forth the components of net periodic benefit cost for our pension and other postretirement benefit plans for the periods indicated:

	Pension Benefits			
	Three Months Ended		Nine Months Ended	
	September 30, 2015	September 30, 2014	September 30, 2015	September 30, 2014
	(Thousands of dollars)			
Components of net periodic benefit cost				
Service cost	\$3,497	\$3,554	\$10,518	\$9,227
Interest cost	10,652	10,948	31,956	32,844
Expected return on assets	(15,363)	(14,965)	(46,087)	(44,895)
Amortization of unrecognized prior service cost	66	137	200	411

Edgar Filing: ONE Gas, Inc. - Form 10-Q

Amortization of net loss	11,054	7,550	33,164	22,649
Net periodic benefit cost	\$9,906	\$7,224	\$29,751	\$20,236

	Other Postretirement Benefits			
	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2015	2014	2015	2014
	(Thousands of dollars)			
Components of net periodic benefit cost				
Service cost	\$849	\$867	\$2,547	\$2,908
Interest cost	2,665	2,901	7,997	8,703
Expected return on assets	(2,908)	)(2,848	)(8,724	)(8,544
Amortization of unrecognized prior service cost	(440)	)(440	)(1,320	)(1,320
Amortization of net loss	1,510	992	4,530	2,976
Net periodic benefit cost	\$1,676	\$1,472	\$5,030	\$4,723

We recover qualified pension benefit plan and other postretirement benefit plan costs through rates charged to our customers. Certain utility commissions require that the recovery of these costs be based on specific guidelines. The difference between these regulatory-based amounts and the periodic benefit cost calculated pursuant to GAAP is deferred as a regulatory asset or liability and amortized to expense over periods in which this difference will be recovered in rates, as authorized by the applicable utility commission.

Measurement - In October 2015, plan amendments were approved to merge our frozen cash-balance defined benefit pension plan covering certain Texas Gas Service employees with our defined benefit pension plan covering nonbargaining unit employees and certain bargaining unit employees. In addition, we announced to certain pre-65 participants in our postretirement medical plans a change from a self-insured postretirement medical plan to a plan providing participants an annual benefit that will allow them to select coverage on a healthcare exchange. As a result, we will remeasure the respective plan assets and benefit obligations in the fourth quarter 2015.

9.COMMITMENTS AND CONTINGENCIES

Environmental Matters - We are subject to multiple historical, wildlife preservation and environmental laws and/or regulations which affect many aspects of our present and future operations. Regulated activities include, but are not limited to, those involving air emissions, storm water and wastewater discharges, handling and disposal of solid and hazardous wastes, wetland preservation, hazardous materials transportation, and pipeline and facility construction. These laws and regulations require us to obtain and/or comply with a wide variety of environmental clearances, registrations, licenses, permits and other approvals. Failure to comply with these laws, regulations, licenses and permits may expose us to fines, penalties and/or interruptions in our operations that could be material to our results of operations. In addition, emission controls and/or other regulatory or permitting mandates under the Clean Air Act and other similar federal and state laws could require unexpected capital expenditures. We cannot assure that existing environmental statutes and regulations will not be revised or that new regulations will not be adopted or become applicable to us. Revised or additional statutes or regulations that result in increased compliance costs or additional operating restrictions could have a material adverse effect on our business, financial condition, results of operations and cash flows.

We own or retain legal responsibility for the environmental conditions at 12 former manufactured natural gas sites in Kansas. These sites contain potentially harmful materials that are subject to control or remediation under various environmental laws and regulations. A consent agreement with the KDHE governs all work at these sites. The terms of the consent agreement allow us to investigate these sites and set remediation activities based upon the results of the investigations and risk analysis. Remediation typically involves the management of contaminated soils and may involve removal of structures and monitoring and/or remediation of groundwater.

We have completed or addressed removal of the source of soil contamination at 11 of the 12 sites according to plans approved by the KDHE. Regulatory closure has been achieved at three of the sites. We have begun site assessment at the remaining site where no active remediation has occurred.

Our expenditures for environmental evaluation, mitigation, remediation and compliance to date have not been significant in relation to our financial position, results of operations or cash flows, and our expenditures related to environmental matters had no material effects on earnings or cash flows during the nine months ended September 30, 2015 and 2014. We do not expect expenditures for these matters to have a material adverse affect on our financial condition, results of operations or cash flows.

Pipeline Safety - We are subject to PHMSA regulations, including integrity-management regulations. PHMSA regulations require pipeline companies operating high-pressure transmission pipelines to perform integrity assessments on pipeline segments that pass through densely populated areas or near specifically designated high-consequence areas. In January 2012, the Pipeline Safety, Regulatory Certainty and Job Creation Act was signed into law. The law increased maximum penalties for violating federal pipeline safety regulations and directs the DOT and the Secretary of Transportation to conduct further review or studies on issues that may or may not be material to us. These issues include, but are not limited to, the following:

- an evaluation of whether natural gas pipeline integrity-management requirements should be expanded beyond current high-consequence areas;
- a verification of records for pipelines in class 3 and 4 locations and high-consequence areas to confirm maximum allowable operating pressures; and
- a requirement to test previously untested pipelines operating above 30 percent yield strength in high-consequence areas.

The potential capital and operating expenditures related to this legislation, the associated regulations or other new pipeline safety regulations are unknown.

Legal Proceedings - We are a party to various litigation matters and claims that have arisen in the normal course of our operations. While the results of litigation and claims cannot be predicted with certainty, we believe the reasonably possible losses from such matters, individually and in the aggregate, are not material. Additionally, we believe the probable final outcome of such matters will not have a material adverse effect on our results of operations, financial position or cash flows.

10. DERIVATIVE FINANCIAL INSTRUMENTS AND FAIR VALUE MEASUREMENTS

Accounting Treatment - We record all derivative instruments at fair value, with the exception of normal purchases and normal sales that are expected to result in physical delivery. The accounting for changes in the fair value of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship and, if so, the reason for holding it, or if regulatory rulings require a different accounting treatment.

If certain conditions are met, we may elect to designate a derivative instrument as a hedge to mitigate the risk of exposure to changes in fair values or cash flows.

The table below summarizes the various ways in which we account for our derivative instruments and the impact on our financial statements:

Accounting Treatment	Recognition and Measurement	
	Balance Sheet	Income Statement
Normal purchases and normal sales	- Recorded at historical cost	- Change in fair value not recognized in earnings
Mark-to-market	- Recorded at fair value	- Change in fair value recognized in, and recoverable through, the purchased-gas cost adjustment mechanisms

We have not elected to designate any of our derivative instruments as hedges. Premiums paid and any cash settlements received associated with the commodity derivative instruments entered into by us are included in, and recoverable through, the purchased-gas cost adjustment mechanisms.

Determining Fair Value - We define fair value as the price that would be received from the sale of an asset or the transfer of a liability in an orderly transaction between market participants at the measurement date. We use the market and income approaches to determine the fair value of our assets and liabilities and consider the markets in

which the transactions are executed. We measure the fair value of a group of financial assets and liabilities consistent with how a market participant would price the net risk exposure at the measurement date.

Fair Value Hierarchy - At each balance sheet date, we utilize a fair value hierarchy to classify fair value amounts recognized or disclosed in our financial statements based on the observability of inputs used to estimate such fair value. The levels of the hierarchy are described below:

Level 1 - Unadjusted quoted prices in active markets for identical assets or liabilities;

Level 2 - Significant observable pricing inputs other than quoted prices included within Level 1 that are, either directly or indirectly, observable as of the reporting date. Essentially, this represents inputs that are derived principally from or corroborated by observable market data; and

Level 3 - May include one or more unobservable inputs that are significant in establishing a fair value estimate. These unobservable inputs are developed based on the best information available and may include our own internal data.

We recognize transfers into and out of the levels as of the end of each reporting period.

Determining the appropriate classification of our fair value measurements within the fair value hierarchy requires management's judgment regarding the degree to which market data is observable or corroborated by observable market data. We categorize derivatives for which fair value is determined using multiple inputs within a single level, based on the lowest level input that is significant to the fair value measurement in its entirety.

Derivative Instruments - At September 30, 2015, we held purchased natural gas call options for the heating season ending March 2016, with total notional amounts of 38.1 Bcf, for which we paid premiums of \$11.6 million, and had a fair value of \$4.4 million. At December 31, 2014, we held purchased natural gas call options for the heating season ended March 2015, with total notional amounts of 16.0 Bcf, for which we paid premiums of \$6.4 million, and had a fair value of \$0.1 million. The premiums paid and any cash settlements received are recorded as part of our unrecovered purchased-gas costs in current regulatory assets as these contracts are included in, and recoverable through, the purchased-gas cost adjustment mechanisms. Additionally, changes in fair value associated with these contracts are deferred as part of our unrecovered purchased-gas costs in our Balance Sheets. Our natural gas call options are classified as Level 1 as fair value amounts are based on unadjusted quoted prices in active markets including NYMEX-settled prices. There were no transfers between levels for the three and nine months ended September 30, 2015 and 2014.

Other Financial Instruments - The approximate fair value of cash and cash equivalents, accounts receivable and accounts payable is equal to book value, due to the short-term nature of these items. Our cash and cash equivalents are comprised of bank deposits and money market accounts, and are classified as Level 1.

Short-term notes payable and commercial paper are due upon demand and, therefore, the carrying amounts approximate fair value and are classified as Level 1. The book value of our long-term debt, including current maturities, was \$1.2 billion at both September 30, 2015 and December 31, 2014. The estimated fair value of our long-term debt, including current maturities, was \$1.2 billion and \$1.3 billion at September 30, 2015 and December 31, 2014, respectively. The estimated fair value of our Senior Notes at September 30, 2015 and December 31, 2014, was determined using quoted market prices, and are considered Level 2.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis should be read in conjunction with our unaudited financial statements and the Notes to Financial Statements in this Quarterly Report, as well as our Annual Report. Due to the seasonal nature of our business, the results of operations for the three and nine months ended September 30, 2015, are not necessarily indicative of the results that may be expected for a 12-month period.

RECENT DEVELOPMENTS

Dividend - In October 2015, a dividend of \$0.30 per share (\$1.20 per share on an annualized basis) was declared for shareholders of record on November 13, 2015, payable December 1, 2015.

Regulatory Activities - Oklahoma - In July 2015, Oklahoma Natural Gas filed a request with the OCC for an increase in base rates, reflecting system investments and operating costs necessary to maintain the safety and reliability of its natural gas distribution system. Oklahoma Natural Gas' request, if approved, represents an increase of \$50.4 million in base rates and is based on a 10.5 percent return on equity, unchanged from the previous general rate case filed in 2009. This filing also requests the continuation, with certain modifications, of the Performance Based Rate Change plan that was established in 2009. Additionally, the common equity ratio requested is 60.5 percent based on ONE Gas' actual equity ratio as of March 31, 2015, with debt costs of 3.95 percent. The filing represents a rate base of approximately \$1.2 billion. The hearing on the merits on Oklahoma Natural Gas' request will occur in November 2015. In accordance with Oklahoma law, the OCC has 180 days to consider Oklahoma Natural Gas' proposed rate changes.

In March 2015, Oklahoma Natural Gas filed its energy-efficiency program true-up application for its 2014 program year, requesting a utility incentive of \$1.2 million. In July 2015, the Public Utility Division of the OCC and all other parties entered into a joint stipulation approving the filing. A hearing on the merits was held in July 2015, with the Administrative Law Judge recommending the approval of the joint stipulation. The matter is now before the OCC who may accept, reject or modify the Administrative Law Judge's recommendation.

In December 2014, the Public Utility Division of the OCC filed an application to close the remaining items associated with Oklahoma Natural Gas' take-or-pay rider. The OCC's final audit of the take-or-pay rider and related items included a review of the over-recovery of \$1.1 million and adopted Oklahoma Natural Gas' recommendation to refund this over-recovery to customers through its PGA mechanism. The pass-through of the over-recovery through the PGA has no impact on operating income.

Kansas - Kansas Gas Service is expected to file a rate case in 2016 based on a 2015 test year, with new rates effective January 2017.

In August 2015, Kansas Gas Service submitted an application to the KCC requesting an increase in customers' bills totaling approximately \$2.4 million related to its Gas System Reliability Surcharge. The KCC has 120 days to render a decision on the request.

In March 2015, the KCC issued an order opening an investigation regarding accelerated replacement of obsolete pipeline materials. This order was issued after several open meetings were hosted by the KCC in the fourth quarter of 2014, discussing the status of natural gas infrastructure replacement in Kansas. In June 2015, the KCC issued an order agreeing with Kansas Gas Service and other LDCs, as well as the KCC Staff, that the KCC has jurisdiction to approve alternative pipeline replacement programs with alternative rate mechanisms. In July 2015, the Citizen's Utility Ratepayer Board (CURB) submitted a petition for reconsideration of the KCC's order. In August 2015, the KCC issued an order rejecting CURB's petition for reconsideration. Kansas Gas Service and other LDCs filed testimony in October

2015, and the KCC will review testimony to determine what, if any, changes should occur. A procedural schedule setting forth the major actions and timelines associated with the investigation is pending before the KCC.

Texas - In March 2014, Texas Gas Service and the City of El Paso agreed to enter into an annual rate review mechanism called the EPARR. The EPARR provides for a streamlined review of Texas Gas Service's revenue requirement on an annual basis, and is in lieu of a filing under the GRIP statute. Texas Gas Service continued to file under the GRIP statute for other incorporated cities in the El Paso service area until early 2015, when the other incorporated cities in the El Paso service area adopted the EPARR mechanism. GRIP is a capital-recovery mechanism that allows for a rate adjustment providing recovery of and a return on incremental capital investments made between rate cases.

In March 2015, Texas Gas Service filed under the EPARR, requesting an increase in revenues of \$9.4 million in the City of El Paso and surrounding incorporated cities in the EPSA. The filing included a request to include a payroll adjustment which would increase revenues by an additional \$1.8 million, for a total increase in revenues of \$11.2 million. In August 2015, Texas Gas Service and the incorporated cities in the EPSA reached an agreement on a rate increase of \$8.0 million to take effect in August 2015. In April 2015, Texas Gas Service filed with the RRC under the GRIP statute, requesting an increase of \$0.4 million in revenues for the unincorporated areas of the El Paso service area. The RRC approved the filing in July 2015.

Texas Gas Service received approval for rate relief under the GRIP statute with the City of Austin, Texas, and surrounding communities in May 2015, for approximately \$3.7 million. The new rates became effective in June 2015.

In the normal course of business, we have received approval for increases totaling \$4.7 million in 2015 for rate relief under the GRIP and cost-of-service adjustments in other Texas jurisdictions to address investments in rate base and changes in cost of service.

FINANCIAL RESULTS AND OPERATING INFORMATION

Selected Financial Results - The following table sets forth certain selected financial results for our operations for the periods indicated:

Financial Results	Three Months Ended		Nine Months Ended		Three Months			Nine Months		
	September 30,		September 30,		2015 vs. 2014			2015 vs. 2014		
	2015	2014	2015	2014	Increase (Decrease)			Increase (Decrease)		
	(Millions of dollars, except percentages)									
Natural gas sales	\$197.9	\$213.4	\$1,063.7	\$1,203.2	\$(15.5)	(7)%	\$(139.5)	(12)%		
Transportation revenues	20.9	20.2	72.9	74.9	0.7	3 %	(2.0)	(3)%		
Cost of natural gas	54.7	75.1	548.2	701.8	(20.4)	(27)%	(153.6)	(22)%		
Net margin, excluding other revenues	164.1	158.5	588.4	576.3	5.6	4 %	12.1	2 %		
Other revenues	6.4	8.0	21.9	26.5	(1.6)	(20)%	(4.6)	(17)%		
Net margin	170.5	166.5	610.3	602.8	4.0	2 %	7.5	1 %		
Operating costs	111.6	116.2	346.5	353.5	(4.6)	(4)%	(7.0)	(2)%		
Depreciation and amortization	34.0	31.2	98.6	94.0	2.8	9 %	4.6	5 %		
Operating income	\$24.9	\$19.1	\$165.2	\$155.3	\$5.8	30 %	\$9.9	6 %		
Capital expenditures	\$74.3	\$76.0	\$199.7	\$224.6	\$(1.7)	(2)%	\$(24.9)	(11)%		

The following table sets forth our net margin, excluding other revenues, by type of customer, for the periods indicated:

	Three Months Ended		Nine Months Ended		Three Months			Nine Months		
Net Margin, Excluding Other Revenues	September 30,		September 30,		2015 vs. 2014			2015 vs. 2014		
	2015	2014	2015	2014	Increase (Decrease)			Increase (Decrease)		
Natural gas sales	(Millions of dollars, except percentages)									
Residential	\$118.9	\$115.1	\$425.8	\$413.4	\$3.8	3	%	\$12.4	3	%
Commercial and industrial	23.3	22.3	85.4	84.2	1.0	4	%	1.2	1	%
Wholesale and public authority	1.0	0.9	4.3	3.8	0.1	11	%	0.5	13	%
Net margin on natural gas sales	143.2	138.3	515.5	501.4	4.9	4	%	14.1	3	%
Transportation revenues	20.9	20.2	72.9	74.9	0.7	3	%	(2.0	) (3	)%
Net margin, excluding other revenues	\$164.1	\$158.5	\$588.4	\$576.3	\$5.6	4	%	\$12.1	2	%

Our net margin on natural gas sales is comprised of two components, fixed and variable margin. Fixed margin reflects the portion of our net margin attributable to the monthly fixed customer charge component of our rates, which does not fluctuate based on customer usage in each period. Variable margin reflects the portion of our net margin that fluctuates with the volumes delivered and billed. We believe that the combination of the significant residential component of our customer base, the fixed charge component of our sales margin and our regulatory rate mechanisms that we have in place result in a stable cash flow profile. The following table sets forth our net margin on natural gas sales by revenue type for the periods indicated:

Edgar Filing: ONE Gas, Inc. - Form 10-Q

	Three Months Ended		Nine Months Ended		Three Months			Nine Months		
	September 30,		September 30,		2015 vs. 2014			2015 vs. 2014		
Net Margin on Natural Gas Sales	2015	2014	2015	2014	Increase (Decrease)			Increase (Decrease)		
Net margin on natural gas sales	(Millions of dollars, except percentages)									
Fixed margin	\$128.0	\$123.3	\$387.8	\$367.2	\$4.7	4	%	\$20.6	6	%
Variable margin	15.2	15.0	127.7	134.2	0.2	1	%	(6.5	) (5	)%
Net margin on natural gas sales	\$143.2	\$138.3	\$515.5	\$501.4	\$4.9	4	%	\$14.1	3	%

Net margin increased \$4.0 million for the three months ended September 30, 2015, compared with the same period last year, due primarily to an increase of \$4.6 million from new rates primarily in Oklahoma and Texas, offset partially by other revenues.

Net margin increased \$7.5 million for the nine months ended September 30, 2015, compared with the same period last year, due primarily to the following:

- an increase of \$19.4 million from new rates primarily in Oklahoma and Texas; and
- an increase of \$3.7 million in residential sales due primarily to customer growth in Oklahoma; offset partially by a decrease of \$5.6 million due to lower sales volumes, net of weather normalization, primarily from warmer weather for the nine months ended September 30, 2015, compared with the same period last year;
- a decrease of \$5.1 million due to lower line extension revenue, from commercial and industrial customers, and other revenues;
- a decrease of \$3.2 million in rider and surcharge recoveries due to a lower ad valorem surcharge in Kansas and the expiration of the rider associated with the recovery of take-or-pay settlements in Oklahoma, both of which are offset by lower regulatory amortization in depreciation and amortization expense; and
- a decrease of \$1.9 million due primarily to lower transportation volumes from weather-sensitive customers primarily in Kansas.

Operating costs decreased \$4.6 million for the three months ended September 30, 2015, compared with the same period last year, due primarily to the following:

- a decrease of \$3.9 million in information technology costs, which includes \$3.3 million of costs associated with our separation from ONEOK in the prior year;
- a decrease of \$1.6 million in outside services and other costs associated with pipeline maintenance activities;
- a decrease of \$1.1 million in ad valorem taxes;
- a decrease of \$0.6 million in fleet-related expenses; and
- a decrease of \$0.5 million in bad debt expense due primarily to warmer weather in Kansas; offset partially by
- an increase of \$3.7 million in employee-related costs due primarily to increases of \$2.9 million in higher labor costs and \$0.8 million in benefit costs.

Operating costs decreased \$7.0 million for the nine months ended September 30, 2015, compared with the same period last year, due primarily to the following:

- a decrease of \$3.5 million in information technology costs, which includes \$5.9 million of costs associated with our separation from ONEOK in the prior year, offset partially by higher costs for maintenance agreements;
- a decrease of \$3.5 million in outside service costs associated with pipeline maintenance activities;
- a decrease of \$3.0 million in legal and workers' compensation expense;
- a decrease of \$2.6 million in ad valorem taxes; and
- a decrease of \$2.1 million in bad debt expense due primarily to warmer weather in Kansas; offset partially by
-

an increase of \$8.1 million in employee-related costs due primarily to increases of \$4.8 million in higher labor costs and \$3.2 million in benefit costs.

Depreciation and amortization expense increased \$2.8 million for the three months ended September 30, 2015, compared with the same period last year, due to an increase in depreciation of \$3.3 million from our capital expenditures being placed in service, offset partially by a decrease in the amortization associated with the ad valorem surcharge rider in Kansas. Depreciation and amortization expense increased \$4.6 million for the nine months ended September 30, 2015, compared with the same period last year, due to an increase in depreciation of \$8.3 million from our capital expenditures being placed in service, offset partially by a decrease in the amortization of the ad valorem surcharge rider in Kansas and take-or-pay rider in Oklahoma of \$2.9 million.

Capital Expenditures - Our capital expenditures program includes expenditures for pipeline integrity, extending service to new areas, modifications to customer service lines, increasing system capabilities, pipeline replacements, fleet, facilities and information technology assets. It is our practice to maintain and upgrade our infrastructure, facilities and systems to ensure safe, reliable and efficient operations.

Capital expenditures decreased \$1.7 million for the three months ended September 30, 2015, and decreased \$24.9 million for the nine months ended September 30, 2015, compared with the same respective periods last year, due primarily to information technology hardware and software assets acquired in 2014 due to our separation from ONEOK.

Selected Operating Information - The following tables set forth certain selected operating information for the periods indicated:

(in thousands)	Three Months Ended September 30,								Variances 2015 vs. 2014			
	2015				2014				Increase (Decrease)			
Average Number of Customers	OK	KS	TX	Total	OK	KS	TX	Total	OK	KS	TX	Total
Residential	776	573	606	1,955	769	569	601	1,939	7	4	5	16
Commercial and industrial	71	50	33	154	71	50	33	154	—	—	—	—
Wholesale and public authority	—	—	3	3	—	—	3	3	—	—	—	—
Transportation	6	6	1	13	5	6	1	12	1	—	—	1
Total customers	853	629	643	2,125	845	625	638	2,108	8	4	5	17

(in thousands)	Nine Months Ended September 30,								Variances 2015 vs. 2014			
	2015				2014				Increase (Decrease)			
Average Number of Customers	OK	KS	TX	Total	OK	KS	TX	Total	OK	KS	TX	Total
Residential	783	580	607	1,970	776	579	602	1,957	7	1	5	13
Commercial and industrial	73	50	34	157	73	50	34	157	—	—	—	—
Wholesale and public authority	—	—	3	3	—	—	3	3	—	—	—	—
Transportation	5	6	1	12	5	6	1	12	—	—	—	—
Total customers	861	636	645	2,142	854	635	640	2,129	7	1	5	13

Volumes (MMcf)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Natural gas sales				
Residential	7,476	7,845	78,987	84,809
Commercial and industrial	3,676	3,810	25,460	26,853
Wholesale and public authority	247	287	1,719	1,518
Total volumes sold	11,399	11,942	106,166	113,180
Transportation	43,056	43,653	150,611	159,002
Total volumes delivered	54,455	55,595	256,777	272,182

Total volumes delivered decreased for the three and nine months ended September 30, 2015, compared with the same periods last year, due primarily to warmer temperatures in 2015. The impact on residential and commercial margins was mitigated significantly by weather-normalization mechanisms.

Wholesale sales represent contracted natural gas volumes that exceed the needs of our residential, commercial and industrial customer base and are available for sale to other parties. The impact to net margin from changes in volumes

associated with these customers is minimal.

	Three Months Ended September 30,				2015 vs 2014					
	2015		2014		Actual Variance		2015		2014	
	Actual	Normal	Actual	Normal			Actual as a percent of Normal			
Heating Degree Days										
Oklahoma	—	14	11	14	(100)	)%	—	%	79	%
Kansas	9	52	43	52	(79)	)%	17	%	83	%
Texas	—	1	1	1	(100)	)%	—	%	100	%
	Nine Months Ended September 30,				2015 vs 2014					
	2015		2014		Actual Variance		2015		2014	
	Actual	Normal	Actual	Normal			Actual as a percent of Normal			
Heating Degree Days										
Oklahoma	2,067	2,012	2,381	2,012	(13)	)%	103	%	118	%
Kansas	2,824	2,965	3,331	2,965	(15)	)%	95	%	112	%
Texas	1,117	1,023	1,034	1,025	8	%	109	%	101	%

Normal HDDs are established through rate proceedings in each of our rate jurisdictions for use primarily in weather normalization billing calculations. See further discussion on weather normalization in our Regulatory Overview section in Part 1, Item 1, “Business,” of our Annual Report. Normal HDDs disclosed above are based on:

- 10-year weighted average HDDs as of December 31, 2008, for years 1999-2008, as calculated using 11 weather stations across Oklahoma and weighted on average customer count for Oklahoma;
- 30-year average for years 1981-2010 published by the National Oceanic and Atmospheric Administration, as calculated using 13 weather stations across Kansas and weighted on HDDs by weather station and customers for Kansas; and
- a rolling 10-year average of actual natural gas distribution sales volumes by service area for Texas.

Actual HDDs are based on the quarter-to-date and year-to-date, weighted average of:

- 11 weather stations and customers by month for Oklahoma;
- 13 weather stations and customers by month for Kansas; and
- 9 weather stations and natural gas distribution sales volumes by service area for Texas.

CONTINGENCIES

Legal Proceedings - We are a party to various litigation matters and claims that have arisen in the normal course of our operations. While the results of litigation and claims cannot be predicted with certainty, we believe the reasonably possible losses from such matters, individually and in the aggregate, are not material. Additionally, we believe the probable final outcome of such matters will not have a material adverse effect on our results of operations, financial position or cash flows.

LIQUIDITY AND CAPITAL RESOURCES

General - We have relied primarily on operating cash flow, commercial paper and the ONE Gas Credit Agreement for our liquidity and capital resource requirements. We fund operating expenses, working capital requirements, including purchases of natural gas, and capital expenditures primarily with cash from operations, commercial paper and bank

credit facilities.

We believe that the combination of the significant residential component of our customer base, the fixed-charge component of our natural gas sales net margin and our regulatory rate mechanisms that we have in place result in a stable cash flow profile. Because the energy consumption of residential customers is less volatile compared with commercial and industrial customers, our business historically has generated stable and predictable net margin and cash flows. Additionally, we have several

26

regulatory rate mechanisms in place to reduce the lag in earning a return on our capital expenditures. We anticipate that our cash flow generated from operations and our expected short- and long-term financing arrangements will enable us to maintain our current and planned level of operations and provide us flexibility to finance our infrastructure investments.

Our ability to access capital markets for debt and equity financing under reasonable terms depends on market conditions and our financial condition and credit ratings. We believe that stronger credit ratings will provide a significant advantage to our business. By maintaining a conservative financial profile and stable revenue base, we believe that we will be able to maintain an investment-grade credit rating, which we believe will provide us access to diverse sources of capital at favorable rates in order to finance our infrastructure investments. Credit rating agencies perform independent analyses when assigning credit ratings.

Short-term Financing - The ONE Gas Credit Agreement contains certain financial, operational and legal covenants. Among other things, these covenants include maintaining a debt-to-capital ratio of no more than 70 percent at the end of any calendar quarter. The ONE Gas Credit Agreement also contains customary affirmative and negative covenants, including covenants relating to liens, indebtedness of subsidiaries, investments, changes in the nature of business, fundamental changes, transactions with affiliates, burdensome agreements, and use of proceeds. In the event of a breach of certain covenants by us, amounts outstanding under the ONE Gas Credit Agreement may become due and payable immediately. At September 30, 2015, our debt-to-capital ratio was 40 percent, and we were in compliance with all covenants under the ONE Gas Credit Agreement.

The ONE Gas Credit Agreement includes a \$50 million sublimit for the issuance of standby letters of credit and also features an option to request an increase in the size of the facility to an aggregate of \$1.2 billion from \$700 million, upon satisfaction of customary conditions, including receipt of commitments from new lenders or increased commitments from existing lenders. Borrowings made under the facility are available for general corporate purposes. The ONE Gas Credit Agreement contains provisions for an applicable margin rate and an annual facility fee, both of which adjust with changes in our credit rating. Based on our current credit ratings, borrowings, if any, will accrue interest at LIBOR plus 79.5 basis points, and the annual facility fee is 8 basis points. The total amount of short-term borrowings authorized by ONE Gas' Board of Directors is \$1.2 billion.

We have a commercial paper program under which we may issue unsecured commercial paper up to a maximum amount of \$700 million to fund short-term borrowing needs. The maturities of the commercial paper notes may vary but may not exceed 270 days from the date of issue. The commercial paper notes are generally sold at par less a discount representing an interest factor.

The ONE Gas Credit Agreement is available to repay the commercial paper notes, if necessary. Amounts outstanding under the commercial paper program reduce the borrowing capacity under the ONE Gas Credit Agreement. At September 30, 2015, we had no short-term borrowings and \$1.0 million in letters of credit issued under the ONE Gas Credit Agreement. At September 30, 2015, we had approximately \$53.0 million of cash and cash equivalents and \$699.0 million of remaining credit available under the ONE Gas Credit Agreement.

Long-Term Debt - We have senior notes, consisting of \$300 million of 2.07 percent senior notes due 2019, \$300 million of 3.61 percent senior notes due 2024 and \$600 million of 4.658 percent senior notes due 2044 (collectively, our "Senior Notes"). The indenture governing our Senior Notes includes an event of default upon the acceleration of other indebtedness of \$100 million or more. Such events of default would entitle the trustee or the holders of 25 percent in aggregate principal amount of the outstanding Senior Notes to declare those Senior Notes immediately due and payable in full.

Credit Ratings - Our credit ratings as of September 30, 2015, were:

Rating Agency	Rating	Outlook
---------------	--------	---------

Edgar Filing: ONE Gas, Inc. - Form 10-Q

Moody's	A2	Stable
S&P	A-	Stable

Our commercial paper is currently rated Prime-1 by Moody's and A-2 by S&P. We intend to maintain strong credit metrics while we pursue a balanced approach to capital investment and a return of capital to shareholders via a dividend that we believe will be competitive with our peer group.

Capitalization structure - As of September 30, 2015, our total capitalization structure is 40 percent debt to 60 percent equity.

Pension and Other Postretirement Benefit Plans - Information about our pension and other postretirement benefits plans, including anticipated contributions, is included under Note 12 of the ONE Gas Notes to Financial Statements in our Annual Report. See Note 8 of the Notes to Financial Statements in this Quarterly Report for additional information.

CASH FLOW ANALYSIS

We use the indirect method to prepare our Statements of Cash Flows. Under this method, we reconcile net income to cash flows provided by operating activities by adjusting net income for those items that impact net income but may not result in actual cash receipts or payments and changes in our assets and liabilities not classified as investing or financing activities during the period. Items that impact net income but may not result in actual cash receipts or payments include, but are not limited to, depreciation and amortization, deferred income taxes, share-based compensation expense and provision for doubtful accounts.

The following table sets forth the changes in cash flows by operating, investing and financing activities for the periods indicated:

	Nine Months Ended September 30,		Variances 2015 vs. 2014 Increase (Decrease)
	2015	2014	
	(Millions of dollars)		
Total cash provided by (used in):			
Operating activities	\$349.5	\$250.0	\$99.5
Investing activities	(199.6)	(224.6)	25.0
Financing activities	(108.8)	31.1	(139.9)
Change in cash and cash equivalents	41.1	56.5	(15.4)
Cash and cash equivalents at beginning of period	11.9	3.2	8.7
Cash and cash equivalents at end of period	\$53.0	\$59.7	\$(6.7)

Operating Cash Flows - Operating cash flows are affected by earnings from our business activities. Changes in natural gas prices and demand for our services or natural gas, whether because of general economic or weather conditions, changes in supply or increased competition from other service providers, could affect our earnings and operating cash flows. Typically, our cash flows from operations are greater in the first half of the year compared with the second half of the year.

Cash flows from operating activities, before changes in operating assets and liabilities, increased for the nine months ended September 30, 2015, compared with the same period in 2014. The increase was due primarily to changes in net margin and operating expenses discussed in Financial Results and Operating Information.

The net increase in cash flows from operating assets and liabilities was due primarily to the collection of trade and income tax receivables, changes in natural gas in storage, payment of trade payables and the recovery of natural gas purchase costs through our purchased-gas cost mechanisms. The timing of cash collections from customers and payments to vendors and suppliers varies from period to period in the normal course of business and directly impacts our cash flows from operations.

Investing Cash Flows - Cash used in investing activities decreased for the nine months ended September 30, 2015, compared with the prior period due primarily to capital expenditures for information technology assets associated with our separation from ONEOK.

Financing Cash Flows - The changes in cash flows from financing activities are primarily the result of our \$1.19 billion debt issuance and \$1.13 billion cash payment to ONEOK for the nine months ended September 30, 2014, in connection with our separation from ONEOK, compared with repayments of commercial paper, dividends paid to shareholders and repurchases of common stock for the nine months ended September 30, 2015.

ENVIRONMENTAL, SAFETY AND REGULATORY MATTERS

Environmental Matters - We are subject to multiple historical, wildlife preservation and environmental laws and/or regulations, which affect many aspects of our present and future operations. Regulated activities include, but are not limited to, those involving air emissions, storm water and wastewater discharges, handling and disposal of solid and hazardous wastes, wetland preservation, hazardous materials transportation, and pipeline and facility construction. These laws and regulations

require us to obtain and/or comply with a wide variety of environmental clearances, registrations, licenses, permits and other approvals. Failure to comply with these laws, regulations, licenses and permits may expose us to fines, penalties and/or interruptions in our operations that could be material to our results of operations. In addition, emission controls and/or other regulatory or permitting mandates under the Clean Air Act and other similar federal and state laws could require unexpected capital expenditures at our facilities. We cannot assure that existing environmental statutes and regulations will not be revised or that new regulations will not be adopted or become applicable to us. Revised or additional statutes or regulations that result in increased compliance costs or additional operating restrictions could have a material adverse effect on our business, financial condition, results of operations and cash flows.

We own or retain legal responsibility for the environmental conditions at 12 former manufactured natural gas sites in Kansas. These sites contain potentially harmful materials that are subject to control or remediation under various environmental laws and regulations. A consent agreement with the KDHE governs all work at these sites. The terms of the consent agreement allow us to investigate these sites and set remediation activities based upon the results of the investigations and risk analysis. Remediation typically involves the management of contaminated soils and may involve removal of structures and monitoring and/or remediation of groundwater.

We have completed or addressed removal of the source of soil contamination at 11 of the 12 sites according to plans approved by the KDHE. Regulatory closure has been achieved at three of the sites. We have begun site assessment at the remaining site where no active remediation has occurred.

Our expenditures for environmental evaluation, mitigation, remediation and compliance to date have not been significant in relation to our financial position, results of operations or cash flows, and our expenditures related to environmental matters had no material effects on earnings or cash flows during the nine months ended September 30, 2015 and 2014. We do not expect expenditures for these matters to have a material adverse affect on our financial condition, results of operations or cash flows.

Pipeline Safety - We are subject to PHMSA regulations, including integrity-management regulations. PHMSA regulations require pipeline companies operating high-pressure transmission pipelines to perform integrity assessments on pipeline segments that pass through densely populated areas or near specifically designated high-consequence areas. In January 2012, the Pipeline Safety, Regulatory Certainty and Job Creation Act was signed into law. The new law increased maximum penalties for violating federal pipeline safety regulations and directs the DOT and the Secretary of Transportation to conduct further review or studies on issues that may or may not be material to us. These issues include, but are not limited to, the following:

- an evaluation of whether natural gas pipeline integrity-management requirements should be expanded beyond current high-consequence areas;
- a verification of records for pipelines in class 3 and 4 locations and high-consequence areas to confirm maximum allowable operating pressures; and
- a requirement to test previously untested pipelines operating above 30 percent yield strength in high-consequence areas.

The potential capital and operating expenditures related to this legislation, the associated regulations or other new pipeline safety regulations are unknown.

Air and Water Emissions - The Clean Air Act, the Clean Water Act, analogous state laws and/or regulations promulgated thereunder, impose restrictions and controls regarding the discharge of pollutants into the air and water in the United States. Under the Clean Air Act, a federally enforceable operating permit is required for sources of significant air emissions. We may be required to incur certain capital expenditures for air-pollution-control equipment in connection with obtaining or maintaining permits and approvals for sources of air emissions. We do not expect that these expenditures will have a material impact on our respective results of operations, financial position or cash flows.

The Clean Water Act imposes substantial potential liability for the removal of pollutants discharged to waters of the United States and remediation of waters affected by such discharge.

Federal, state and regional initiatives to measure and regulate greenhouse gas emissions are underway. We monitor relevant federal and state legislation to assess the potential impact on our operations. The EPA's Mandatory Greenhouse Gas Reporting Rule requires annual greenhouse gas emissions reporting as carbon dioxide equivalents from affected facilities and for the natural gas delivered by us to our natural gas distribution customers who are not otherwise required to report their own emissions. The additional cost to gather and report this emission data did not have, and we do not expect it to have, a material impact on our results of operations, financial position or cash flows. In addition, Congress has considered, and may consider in the future, legislation to reduce greenhouse gas emissions, including carbon dioxide and methane. Likewise, the EPA may

institute additional regulatory rulemaking associated with greenhouse gas emissions. At this time, no rule or legislation has been enacted that assesses any costs, fees or expenses on any of these emissions.

CERCLA - The federal CERCLA, also commonly known as Superfund, imposes strict, joint and several liability, without regard to fault or the legality of the original act, on certain classes of “persons” (defined under CERCLA) that caused and/or contributed to the release of a hazardous substance into the environment. These persons include but are not limited to the owner or operator of a facility where the release occurred and/or companies that disposed or arranged for the disposal of the hazardous substances found at the facility. Under CERCLA, these persons may be liable for the costs of cleaning up the hazardous substances released into the environment, damages to natural resources and the costs of certain health studies. We do not expect that our responsibilities under CERCLA will have a material impact on our respective results of operations, financial position or cash flows.

Pipeline Security - The United States Department of Homeland Security’s Transportation Security Administration issued updated pipeline security guidelines in April 2012. Our pipeline facilities have been reviewed according to the current guidelines and no material changes have been required to date.

Environmental Footprint - Our environmental and climate change strategy focuses on taking steps to minimize the impact of our operations on the environment. These strategies include: (1) developing and maintaining an accurate greenhouse gas emissions inventory according to current rules issued by the EPA; (2) improving the efficiency of our various pipelines; (3) following developing technologies for emission control; and (4) utilizing practices to reduce the loss of methane from our facilities.

We participate in the EPA’s Natural Gas STAR Program to voluntarily reduce methane emissions. We continue to focus on maintaining low rates of lost-and-unaccounted-for natural gas through expanded implementation of best practices to limit the release of natural gas during pipeline and facility maintenance and operations.

Regulatory - Several regulatory initiatives impacted the earnings and future earnings potential of our business. See discussion of our regulatory initiatives in Management’s Discussion and Analysis of Financial Condition and Results of Operations.

IMPACT OF NEW ACCOUNTING STANDARDS

Information about the impact of new accounting standards, if any, is included in Note 1 of the Notes to Financial Statements in this Quarterly Report.

ESTIMATES AND CRITICAL ACCOUNTING POLICIES

The preparation of our financial statements and related disclosures in accordance with GAAP requires us to make estimates and assumptions with respect to values or conditions that cannot be known with certainty that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements. These estimates and assumptions also affect the reported amounts of revenue and expenses during the reporting period. Although we believe these estimates and assumptions are reasonable, actual results could differ from our estimates.

Information about our estimates and critical accounting policies is included under Item 7, Management’s Discussion and Analysis of Financial Condition and Results of Operations, “Estimates and Critical Accounting Policies,” in our Annual Report.

FORWARD-LOOKING STATEMENTS

Some of the statements contained and incorporated in this Quarterly Report are forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act. The forward-looking statements relate to our anticipated financial performance, liquidity, management's plans and objectives for our future operations, our business prospects, the outcome of regulatory and legal proceedings, market conditions and other matters. We make these forward-looking statements in reliance on the safe harbor protections provided under the Private Securities Litigation Reform Act of 1995. The following discussion is intended to identify important factors that could cause future outcomes to differ materially from those set forth in the forward-looking statements.

Forward-looking statements include the items identified in the preceding paragraph, the information concerning possible or assumed future results of our operations and other statements contained or incorporated in this Quarterly Report identified by words such as "anticipate," "estimate," "expect," "project," "intend," "plan," "believe," "should," "goal," "guidance," "could," "may," "continue," "might," "potential," "scheduled," and other words and terms of similar meaning.

One should not place undue reliance on forward-looking statements, which are applicable only as of the date of this Quarterly Report. Known and unknown risks, uncertainties and other factors may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by forward-looking statements. Those factors may affect our operations, markets, products, services and prices. In addition to any assumptions and other factors referred to specifically in connection with the forward-looking statements, factors that could cause our actual results to differ materially from those contemplated in any forward-looking statement include, among others, the following:

- our ability to recover operating costs and amounts equivalent to income taxes, costs of property, plant and equipment and regulatory assets in our regulated rates;
- our ability to manage our operations and maintenance costs;
- changes in regulation, including the application of market rates by state and local agencies;
- the economic climate and, particularly, its effect on the natural gas requirements of our residential and commercial industrial customers;
- competition from alternative forms of energy, including, but not limited to, solar power, wind power, geothermal energy and biofuels;
- variations in weather, including seasonal effects on demand, the occurrence of storms and disasters, and climate change;
- indebtedness could make us more vulnerable to general adverse economic and industry conditions, limit our ability to borrow additional funds and/or place us at competitive disadvantage compared with competitors;
- our ability to secure reliable, competitively priced and flexible natural gas supply;
- the mechanical integrity of facilities operated;
- operational hazards and unforeseen operational interruptions;
- adverse labor relations;
- the effectiveness of our strategies to reduce earnings lag, margin protection strategies and risk mitigation strategies;
- our ability to generate sufficient cash flows to meet all our cash needs;
- changes in the financial markets during the periods covered by the forward-looking statements, particularly those affecting the availability of capital and our ability to refinance existing debt and fund investments and acquisitions;
- actions of rating agencies, including the ratings of debt, general corporate ratings and changes in the rating agencies' ratings criteria;
- changes in inflation and interest rates;
- our ability to purchase and sell assets at attractive prices and on other attractive terms;
- our ability to recover the costs of natural gas purchased for our customers;
- impact of potential impairment charges;
- volatility and changes in markets for natural gas;
- possible loss of LDC franchises or other adverse effects caused by the actions of municipalities;
- payment and performance by counterparties and customers as contracted and when due;
- changes in regulation of natural gas distribution services, particularly those in Oklahoma, Kansas and Texas;
- changes in law resulting from new federal or state energy legislation;
- changes in environmental, safety, tax and other laws to which we and our subsidiaries are subject;
- advances in technology;
- population growth rates and changes in the demographic patterns of the markets we serve;
- acts of nature and the potential effects of threatened or actual terrorism, including cyber attacks, and war;
- the sufficiency of insurance coverage to cover losses;
- the effects of our strategies to reduce tax payments;
- the effects of litigation and regulatory investigations, proceedings, including our rate cases, or inquiries;
- changes in accounting standards and corporate governance;
- our ability to attract and retain talented management and directors;
- the results of financing efforts, including our ability to obtain financing on favorable terms, which can be affected by various factors, including our credit ratings and general economic conditions;

declines in the market prices of debt and equity securities and resulting funding requirements for our defined benefit pension plans;

the ability to successfully complete merger, acquisition or divestiture plans, regulatory or other limitations imposed as a result of a merger, acquisition or divestiture, and the success of the business following a merger, acquisition or divestiture;

the final resolutions or outcomes with respect to our contingent and other corporate liabilities related to the natural gas distribution business and any related actions for indemnification made pursuant to the Separation and Distribution Agreement with ONEOK;

our ability to operate effectively as a separate, publicly traded company; and

- the costs associated with increased regulation and enhanced disclosure and corporate governance requirements pursuant to the Dodd-Frank Wall Street Reform and the Consumer Protection Act of 2010.

These factors are not necessarily all of the important factors that could cause actual results to differ materially from those expressed in any of our forward-looking statements. Other factors could also have material adverse effects on our future results. These and other risks are described in greater detail in Item 1A, Risk Factors, in our Annual Report. All forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by these factors. Other than as required under securities laws, we undertake no obligation to update publicly any forward-looking statement whether as a result of new information, subsequent events or change in circumstances, expectations or otherwise.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our quantitative and qualitative disclosures about market risk are consistent with those discussed in Part II, Item 7A, Quantitative and Qualitative Disclosures About Market Risk, in our Annual Report.

Commodity Price Risk

Our commodity price risk, driven primarily by fluctuations in the price of natural gas, is mitigated by our purchased-gas cost adjustment mechanisms. Additionally, we inject natural gas into storage during the summer months and withdraw the natural gas during the winter heating season. Pursuant to programs that are approved by the state commissions, we use derivative instruments to mitigate the volatility of natural gas prices for anticipated natural gas purchases during the winter heating months. Premiums paid and any cash settlements received associated with these derivative instruments are included in, and recoverable through our purchased-gas cost adjustment mechanisms.

Interest-Rate Risk

We would be exposed to interest-rate risk with any new debt financing. We are able to manage interest-rate risk through the use of fixed-rate debt, floating-rate debt and, at times, interest-rate swaps. Fixed-rate swaps may be used to reduce our risk of increased interest costs during periods of rising interest rates. Floating-rate swaps may be used to convert the fixed rates of long-term borrowings into short-term variable rates.

Counterparty Credit Risk

We assess the creditworthiness of our customers. Those customers who do not meet minimum standards are required to provide security, including deposits and other forms of collateral, when appropriate. With more than 2 million customers across three states, we are not exposed materially to a concentration of credit risk. We maintain a provision for doubtful accounts based upon factors surrounding the credit risk of customers, historical trends, consideration of the current credit environment and other information. In most jurisdictions, we are able to recover the natural gas cost component of our uncollectible accounts through our purchased-gas cost mechanisms.

ITEM 4. CONTROLS AND PROCEDURES

Quarterly Evaluation of Disclosure Controls and Procedures - Our Chief Executive Officer (Principal Executive Officer) and Chief Financial Officer (Principal Financial Officer) have concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report based on the evaluation of the controls and procedures required by Rules 13(a)-15(b) of the Exchange Act.

Changes in Internal Control Over Financial Reporting - In the three months ended September 30, 2015, we implemented a new work management and field enablement system that enhances the capturing of additions and

retirements to our property records. We believe the internal controls over financial reporting remained substantially unchanged and do not believe these related internal control changes have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Other than described above, there have been no other changes in our internal control over financial reporting during the three months ended September 30, 2015.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are a party to various litigation matters and claims that have arisen in the normal course of our operations. While the results of litigation and claims cannot be predicted with certainty, we believe the reasonably possible losses from such matters, individually and in the aggregate, are not material. Additionally, we believe the probable final outcome of such matters will not have a material adverse effect on our results of operations, financial position or cash flows.

ITEM 1A. RISK FACTORS

Our investors should consider the risks set forth in Part I, Item 1A, Risk Factors, of our Annual Report that could affect us and our business. Although we have tried to discuss key factors, our investors need to be aware that other risks may prove to be important in the future. New risks may emerge at any time, and we cannot predict such risks or estimate the extent to which they may affect our financial performance. Investors should carefully consider the discussion of risks and the other information included or incorporated by reference in this Quarterly Report, including “Forward-Looking Statements,” which are included in Part I, Item 2, Management’s Discussion and Analysis of Financial Condition and Results of Operations.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Not Applicable.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not Applicable.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

Not applicable.

ITEM 6. EXHIBITS

Readers of this report should not rely on or assume the accuracy of any representation or warranty or the validity of any opinion contained in any agreement filed as an exhibit to this Quarterly Report, because such representation, warranty or opinion may be subject to exceptions and qualifications contained in separate disclosure schedules, may represent an allocation of risk between parties in the particular transaction, may be qualified by materiality standards that differ from what may be viewed as material for securities law purposes, or may no longer continue to be true as of any given date. All exhibits attached to this Quarterly Report are included for the purpose of complying with requirements of the SEC. Other than the certifications made by our officers pursuant to the Sarbanes-Oxley Act of 2002 included as exhibits to this Quarterly Report, all exhibits are included only to provide information to investors regarding their respective terms and should not be relied upon as constituting or providing any factual disclosures about us, any other persons, any state of affairs or other matters.

The following exhibits are filed as part of this Quarterly Report:

Exhibit No.	Exhibit Description
31.1	Certification of Pierce H. Norton II pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Curtis L. Dinan pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Pierce H. Norton II pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished only pursuant to Rule 13a-14(b)).
32.2	Certification of Curtis L. Dinan pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished only pursuant to Rule 13a-14(b)).
101.INS	XBRL Instance Document.
101.SCH	XBRL Schema Document.
101.CAL	XBRL Calculation Linkbase Document.
101.LAB	XBRL Label Linkbase Document.
101. PRE	XBRL Presentation Linkbase Document.
101.DEF	XBRL Extension Definition Linkbase Document.

Attached as Exhibit 101 to this Quarterly Report are the following XBRL-related documents: (i) Document and Entity Information; (ii) Statements of Income for the three and nine months ended September 30, 2015 and 2014; (iii) Statements of Comprehensive Income for the three and nine months ended September 30, 2015 and 2014; (iv) Balance Sheets at September 30, 2015 and December 31, 2014; (v) Statements of Cash Flows for the nine months ended September 30, 2015 and 2014; (vi) Statement of Equity for the nine months ended September 30, 2015; and (vii) Notes to Financial Statements.

We also make available on our website the Interactive Data Files submitted as Exhibit 101 to this Quarterly Report.

SIGNATURE

Pursuant to the requirements of the Exchange Act, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: October 29, 2015

ONE Gas, Inc.
Registrant

By: /s/ Curtis L. Dinan
Curtis L. Dinan
Senior Vice President,
Chief Financial Officer and Treasurer
(Principal Financial Officer)