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Issue: Weather Normalization Adjustment
Witness: Gary L.. Smith
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Sponsoring Party: Atmos Energy Corporation
Case No.: GR-2006-0387
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MISSOURI PUBLIC SERVICE COMMISSION

CASE NO. GR-2006-0387

DIRECT TESTIMONY

OF

GARY L. SMITH

ON BEHALF OF

ATMOS ENERGY CORPORATION

March 2006

Atmos Exhibit No. 2
Case No(s). GR-2006-0387
Date 11-30-06 Rptr PF

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Atmos Energy Corporation's Tariff Revision Designed to Consolidate Rates and Implement a General Rate Increase for Natural Gas Service in the Missouri Service Area of the Company.	))))	Case No.

AFFIDAVIT OF GARY L. SMITH

STATE OF Tennessee)
) ss
COUNTY OF Williamson)

Gary L. Smith, being first duly sworn on his oath, states:

1. My name is Gary L. Smith. I work in Owensboro, Kentucky, and I am employed by Atmos Energy Corporation as the Vice President of Marketing and Regulatory Affairs for Atmos' Kentucky Division.

2. Attached hereto and made a part hereof for all purposes is my Direct Testimony on behalf of Atmos Energy Corporation consisting of Fourteen (14) pages and Schedules GLS-1 GLS-2, all of which having been prepared in written form for introduction into evidence in the above-captioned docket.

3. I have knowledge of the matters set forth therein. I hereby swear and affirm that my answers contained in the attached testimony to the questions therein propounded, including any attachments thereto, are true and accurate to the best of my knowledge, information and belief.

Gary L. Smith

Subscribed and sworn before me this 21st day of MARCH, 2006.

Notary Public

PAMELA TODD
STATE OF TENNESSEE NOTARY PUBLIC
DAVIDSON COUNTY, TENN.

My commission expires: May 24, 2008

My Commission Expires 05-24-08

BEFORE THE

MISSOURI PUBLIC SERVICE COMMISSION

CASE NO. _____

PREPARED DIRECT TESTIMONY

OF

GARY L. SMITH

On Behalf of

ATMOS ENERGY CORPORATION

I. POSITION AND QUALIFICATIONS

Q. Please state your name, position and business address.

A. My name is Gary L. Smith. I am Vice President – Marketing and Regulatory Affairs for Atmos Energy Corporation's Kentucky operations. My business address is 2401 New Hartford Road, Owensboro, Kentucky 42303.

Q. Please briefly describe your current responsibilities, and professional and educational background.

A. I am responsible for rates and regulatory affairs as well as directing the marketing plans and strategies for natural gas utility services to residential, commercial, and industrial sales and transportation markets in Kentucky. I am a 1983 graduate of the University of Kentucky, with a Bachelor of Science degree in Civil Engineering. I have been employed by Atmos Energy Corporation ("Atmos Energy" or the "Company") since 1984, initially as Project Engineer. After serving in a variety of technical and supervisory engineering positions, I transferred into the Industrial Marketing department in 1990. I became Director of Large Volume Sales in 1991, was named Vice President – Marketing in 1998,

and named to my current position in 2003. I also serve on numerous corporate-wide committees, including the role of chair of Atmos Energy's Utility Marketing Council, a group responsible for corporate-wide market development policies. I am active in civic and community organizations and associations relating to the natural gas industry. I am chairman of the Utilization Technology Development, NFP Corporation and previously served as chair of the Strategic Marketing Committee for the American Gas Association ("AGA").

Q. Have you ever testified before this Commission?

A. No.

Q. Have you testified on matters before other State regulatory Commissions?

A. Yes, before the Kentucky Public Service Commission ("KPSC"), and before the Georgia Public Service Commission ("GPSC").

Q. Please briefly describe the matters on which you testified.

A. In 2005, I participated in GPSC Docket No. 20298-U as witness regarding the Weather Normalization Adjustment ("WNA") mechanism in a comprehensive rate case for Atmos Energy's Georgia operations.

In Kentucky, I have served as witness in a number of Cases in recent years, including an extension of the Company's performance based ratemaking ("PBR") tariff (KPSC Case No. 2005-00321), an extension of the Company's WNA mechanism (KPSC Case No. 2005-00268), an extension of a demand-side management ("DSM") program (KPSC Case No. 2005-00515), an annual hedging plan (KPSC Case No. 2005-00175), and an extension of the margin loss recovery mechanism (KPSC Case No. 2003-00305).

In the Kentucky division's most recent comprehensive rate case (KPSC Case Number 1999-070), I served as witness responsible for revenues and rate design. In 1997, I participated as a witness in a hearing on the matter of "Petitions of Western Kentucky Gas Company for Approval and Confidential Treatment of a Special Contract Submitted to the Kentucky Public Service Commission", KPSC Case Numbers 1996-096, 1996-113, 1996-185, 1996-278, 1996-295 and 1996-424.

II. PURPOSE OF TESTIMONY

Q. What is the purpose of your testimony in this proceeding?

A. The purpose of my testimony is to support the Company's proposal to incorporate a Weather Normalization Adjustment ("WNA") Rider in its tariffs. This mechanism is included in the filing with the proposed tariffs on SHEETS 50-51.

Q. Are you sponsoring any Schedules with your testimony?

A. Yes. I am sponsoring Schedule GLS-1, which depicts Missouri residential volumes and Schedule GLS-2, which depicts applicable weather reporting stations.

III. WEATHER NORMALIZATION ADJUSTMENT

Q. Please describe the purpose of the Weather Normalization Adjustment ("WNA") Rider proposed by Atmos Energy.

A. The purpose of a WNA is to eliminate the effects of abnormal weather on customer bills and the Company's earnings.

During the process of rate design, a utility's authorized revenue requirement is distributed to a fixed monthly customer charge component and a volumetric-

dependent distribution component for each customer class. The vast predominance of non-gas costs borne by a utility, and correspondingly its revenue requirements, are fixed and are basically unaffected by the volumes sold or transported. Thus, as annual volumes rise above the weather-normalized rate case volumes upon which the revenue requirements were divided, the utility over-recovers it authorized non-gas cost revenues. Alternatively, lower annual volumes lead to non-gas revenues below the established revenue requirement. WNA mechanisms address the affects of volume variances relating to weather. Since the Commission designs rates based on normal weather and the Company has no control over weather, a WNA is a logical extension of that methodology. The benefit of a WNA is that neither the customer nor the Company bears an advantage or disadvantage as a result of abnormal weather variations during any heating season.

Q. Doesn't the effect of abnormal weather average out over time so that neither customers nor the Company is harmed?

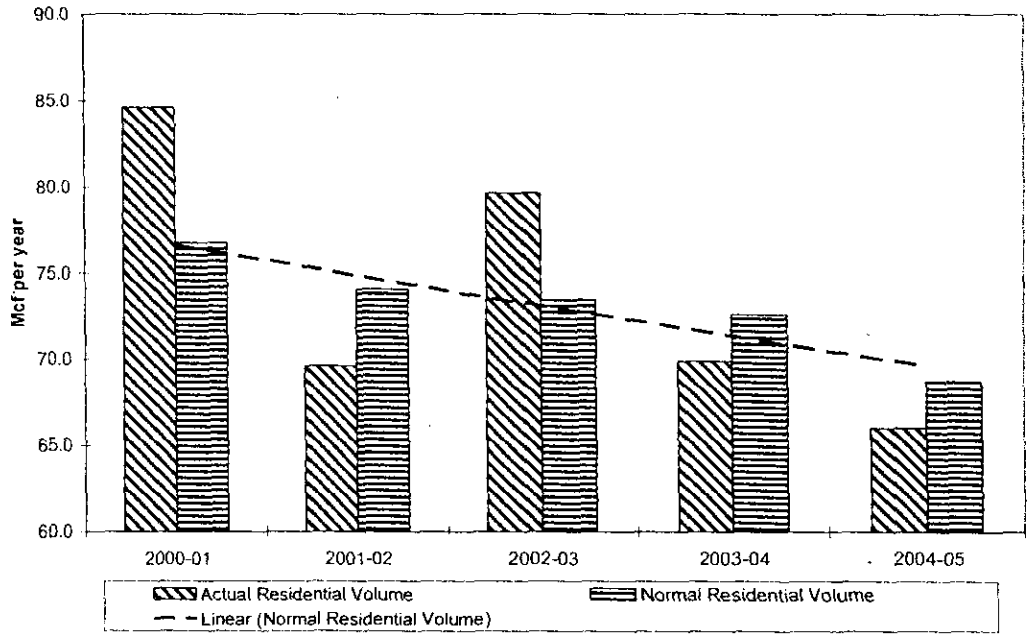
A. That may be the theory, but during a given abnormal heating season either the customer or the Company may be harmed. Moreover, during consecutive heating seasons of abnormally cold weather, customers may be harmed for a prolonged number of years. Conversely, during consecutive warm heating seasons, the Company may be harmed by abnormal weather for a prolonged number of years. Either we collect substantially more revenue from customers than intended by the Commission or we substantially under-collect as a result of volume variances

attributable to weather. Neither situation is equitable; this issue can be addressed by implementing a WNA mechanism.

Schedule GLS-1, below, plots the actual average residential consumption each year for the past five years. Residential volumes during the period range from 84.6 Mcf in 2000-01 down to 66.0 Mcf in 2004-05. Within this timeframe, weather was 12.5% colder than normal in 2000-01, thus residential volumes relating to space heating were higher than normal and the Company benefited from higher distribution charges applied to those volumes. Conversely, in 2004-05, weather was 7% warmer than normal, so the Company received less through its volumetric distribution charges.

On Schedule GLS-1, the corresponding weather-normalized residential volume is shown for comparative purposes. In effect, the proposed WNA mechanism will adjust the distribution rate per Ccf to compensate for weather-driven volume variances from that which would have occurred with normal weather.

Schedule GLS - 1
Residential Volumes - Missouri



Q. Are there factors affecting customer usage patterns other than weather?

A. Yes. In Schedule GLS-1, above, I have added a trend line for weather normalized residential volumes in Missouri. As is evident in the chart, residential gas consumption is declining at a rate of approximately 1.8 Mcf per year due to factors other than weather. This trend is not unique to Missouri. In fact, the trend of declining usage is rather pervasive throughout Atmos Energy's 12-state service area and throughout most regions of the United States.

Q. What is the impact of the trend of declining, weather normalized, consumption patterns?

A. The impact of declining weather-normalized consumption creates significant financial challenges to gas utilities operating under traditional rate making models. Again, in traditional rate making processes, the Company's revenue requirements are determined, based upon reasonable operating costs, which are

predominately fixed or unaffected by varying sales volumes, and a fair return. A portion of the authorized revenue requirement is spread over a base period volume, normalized for weather, to calculate volumetric distribution rates. Those base period volumes must be sustained for the Company to have a reasonable opportunity to achieve the authorized revenues on an ongoing basis. Clearly, the trend of declining volume per customer undermines the Company's "reasonable" opportunity.

Q. Are there any rate mechanisms to compensate for the trend of declining consumption patterns?

A. Yes, a number of mechanisms address the financial impact of declining consumption patterns which impact the utility under traditional rate making processes. Through participation in industry specific seminars, Atmos Energy's relationship with the AGA, and research of gas utility company filings before other state commissions, the Company has examined several different ways that gas utilities have addressed non-weather related volume changes. They include:

1. Higher Fixed Monthly Customer Charges
2. 100% Fixed Rate Monthly Customer Charge
3. Declining Block Commodity Rates
4. Decoupling Mechanisms

Q. How recent or new are these various rate mechanisms?

A. The history and impact of moving toward higher monthly customer charges is difficult to track for other gas utility companies, but the Company has requested and received higher customer charges in all of its rate cases in the past several

years in an effort to address these concerns. Atlanta Gas Light ("AGL") is the only gas utility of which Atmos Energy is aware that has 100% fixed rate monthly customer charge. AGL received this rate design in connection with its unbundling election in Georgia in 2001. California, prior to its 1996 deregulation, encouraged decoupling tariffs in both gas and electric utilities. Decoupling refers to rate mechanisms that break the link between the volume of gas sold and the utility's opportunity to achieve its authorized revenue requirements. Since deregulation, Southwest Gas, in California, has received approval (2004) to decouple its rates. Baltimore Gas and Electric (1999), in Maryland, Northwest Natural Gas, in Oregon, (2002), and Piedmont (2005), in North Carolina, have also recently decoupled rates.

Q. Do decoupling mechanisms deprive customers of the benefit of their conservation efforts?

A. No. Decoupling mechanisms apply only to the non-gas portion of the customer's bill, applying only to the distribution charges retained by the utility for its costs of distribution service and operations. The customer realizes the most significant portion of the avoided, or conserved, Ccf - the gas charge. For this reason, many groups, including the National Association of Regulatory Utility Commissioners ("NARUC") endorse decoupling rate mechanisms so that utilities interests can fully align with customers in regard to conservation efforts.

Q. Is Atmos Energy proposing a rate mechanism to address the impact of these non-weather related volume changes in this Case?

A. No, not at this time. Despite Atmos Energy's interest in and endorsement of decoupling mechanisms, we are not proposing such a rate design in Missouri in this case.

Instead, Atmos Energy is proposing a traditional, real-time, WNA mechanism in this case; a mechanism mirroring a process we already employ in several states already with a proven record of performing well. We are, however, very willing to work with the Commission to refine this mechanism as is deemed appropriate. We believe that the ultimate goal should be to eliminate the variable currently introduced by weather for both the customer and the Company.

Q. Would the Atmos Energy's proposed WNA apply to the Gas Cost Adjustment ("GCA") or Gas Charge?

A. No, the WNA would only apply to the Company's margin tied to volumetric sales, or its' Distribution Commodity Rate. The GCA, through which the Company recovers its gas costs, would be unaffected by the WNA.

Q. How would the proposed WNA benefit customers?

A. The proposed WNA would stabilize customer bills, thereby making them more predictable during the heating season.

In winter periods that are colder than normal, customer consumption generally increases and their gas charges increase with each Ccf purchased. During such winters, when customer bills are increasing due to greater gas commodity charges, the WNA would lower the company's per unit distribution charge and lower the total bill compared to the same service absent the WNA Rider. Conversely, in warmer than normal winter months, although the WNA Rider

would increase the company's per unit distribution charge, the customer would still avoid the much higher cost gas component for volumes avoided due to warmer weather.

Q. How would the proposed WNA benefit the Company?

A. The Company would benefit from revenue stability, making its revenues more predictable during the heating season and from year to year. Although the Company would no longer benefit from an over-recovery of authorized revenue requirements during colder than normal winters, the Company would also no longer suffer from lower distribution charge revenues as a result of warmer than normal weather.

Q. Does a WNA reduce the Company's risk?

A. No. WNA reduces a downside risk only if actual weather is warmer than normal. However, it also removes an upside opportunity when weather is colder than normal.

Q. How does the proposed WNA eliminate the effects of abnormal weather?

A. The WNA is an adjustment mechanism that computes the marginal change in fixed cost revenue associated with abnormal weather and spreads that revenue over actual sales.

The WNA, as reflected in the proposed tariffs, would be computed using the following formula:

$$WNAi = Ri \times \frac{HSFi \times (NDD - ADD)}{BLi + (HSFi \times ADD)}$$

Where,

i = any rate schedule or billing classification within a rate schedule that contains more than one billing classification

WNAi = Weather Normalization Adjustment factor for the ith rate schedule or classification expressed as a rate per Ccf

Ri = base rate of temperature sensitive sales for the ith schedule or classification

HSFi = heat sensitive factor for the ith schedule or classification

NDD = normal billing cycle heating degree days, as used in normalizing test year sales. Normal is defined using a 15-year average of daily heating degree days ending June 30, 2005.

ADD = actual billing cycle heating degree days

BLi = base load for the ith schedule or classification

Customer base loads and heating sensitive factors will be determined by class, by rate schedule, and updated annually. The calculation of these factors, for purposes of the Company's revenue deficiency calculation, is set forth in workpaper WP 2-2 to Schedule RMB-2 attached to Company witness Rebecca Buchanan's testimony and explained in the testimony of Company witness James Cagle. These same factors would also apply whether the WNA mechanism is applied to the rate or to consumption.

Q. Does Atmos Energy's proposed WNA mechanism constitute a change in those rates approved by the Commission?

A. No, the WNA factor would simply apply a Commission-approved adjustment process to the existing Commission authorized rates. If the Commission would prefer a mechanism that did not adjust the rate component, the Company could propose an equivalent mechanism which adjusts the volume component of the bill as an alternative.

Q. How does Atmos Energy propose to administer its WNA?

A. The WNA mechanism proposed for Missouri mirrors processes already in place for Atmos Energy's operations in the states of Georgia, Tennessee, Kentucky, Kansas, and portions of Texas. The same administrative processes in use and functioning well for Atmos Energy's customers in those jurisdictions would be applied to the Missouri WNA mechanism. No new computer programs or data collection systems would have to be developed and the same Atmos Energy shared services accounting and billing personnel who successfully administer existing WNA mechanisms would administer the Missouri WNA. This should ensure a smooth transition, a minimum of problems and virtually no start-up or incremental costs to be incurred for Missouri customers.

The WNA calculation would include the "R" factors specific to each Rate Division in Missouri. Also, the calculation would incorporate the "BL" and "HSF" factors corresponding to weather areas as grouped for normalizing volumes in this Case. Each weather area corresponds to a specific weather reporting station which is used as a reference for normal and actual heating degree days ("NDD's" and "ADD's" respectively) in the WNA formula, as noted in Schedule GLS-2 below:

SCHEDULE GLS-2

Tariff Areas	Weather Station Name	Coop ID
Southern	Quincy Regional AP	117072
Western	Kansas City Intl AP	234358
Northern	Paducah	156110

Q. How long has Atmos Energy had the WNA in the other States mentioned above?

A. Atmos Energy's first jurisdiction to utilize a WNA was Georgia in 1990. Atmos Energy has since received approval for WNA mechanisms in Tennessee (1991), Kentucky (1999), Kansas (2003), and portions of its Texas operating area (2003 & 2004).

Q. To which classes of service, and when will the WNA apply?

A. The WNA will apply to all residential firm service and small firm general service bills under Firm Sales Service rate schedules, based on meters read during the heating season months of October through May. The WNA will not be billed to reflect meters read during the months of June through September.

Q. When would Atmos Energy propose to put its WNA into effect for Missouri operations?

A. After approval by the Commission, Atmos Energy proposes to put its WNA in effect at the beginning of the first complete heating season. That date would be October 1, 2007.

Q. Does Atmos Energy propose to submit any reports regarding the results of its WNA to the Commission?

A. Yes, Atmos Energy proposes to submit an annual report to the Commission summarizing the effect of its WNA on customer bills by month for each customer class as well as the corresponding actual and normal heating degree days for each month. Such a proposed annual report would in a format comparable to that provided to its other regulatory commissions in states where Atmos already has WNA.

Q. Does that conclude your pre-filed direct testimony?

A. Yes