BEFORE THE PUBLIC SERVICE COMMISSION OF THE STATE OF MISSOURI

In the matter of PGA / ACA filing of Atmos Energy Corporation for the West Area (Old Butler), West Area (Old Greeley), Southeastern Area (Old SEMO), Southeastern Area (Old Neelyville), Kirksville Area, and in the Northeastern Area	))))))	**Case No. GR-2008-0364**

POSITION STATEMENT OF
ATMOS ENERGY CORPORATION

COMES NOW Atmos Energy Corporation ("Atmos" or "Company"), and pursuant to Missouri Public Service Commission ("Commission") Rule 4 CSR 240-2.080 and the *Order Adopting Procedural Schedule* issued on February 24, 2010, files its Position Statement. In support of its Position Statement, the Company respectfully states as follows:

I. PROCEDURAL HISTORY

On December 28, 2009, the Commission Staff ("Staff") filed its recommendation following completion of the audit of the 2007-2008 Actual Cost Adjustment ("ACA") filing. The Staff's audit consisted of a review and analysis of the billed revenues and actual gas costs for the period of September 1, 2007 to August 31, 2008 for all areas of served by the Company in Missouri.

Atmos filed its response to Staff's recommendation on January 28, 2010. In its Response, the Company disagreed with Staff's affiliated transaction adjustments and requested that the Commission schedule a hearing to deal with the matter.

On January 30, 2010, the Commission scheduled a prehearing conference for February 11, 2010, so that the Commission and the Parties could discuss a procedural schedule. At the prehearing conference, the Regulatory Law Judge requested that the Parties submit a procedural schedule by February 18, 2010. After discussing this matter, the Parties were unable to agree on a joint recommendation regarding the procedural schedule.

On February 24, 2010, the Commission issued its *Order Adopting Procedural Schedule* which required the Parties to submit a Joint List of Issues on June 25, 2010, and a Position Statement on June 30, 2010.

The purpose of this Position Statement is to explain to the Commission the perspective of Atmos Energy Corporation on the issues raised by Staff's Affiliated Transaction adjustments proposed in this case.

II. STATEMENT OF POSITION ON THE ISSUES

1. Were the Company's gas supply costs reasonable and prudent during the 2007-2008 ACA period?

Atmos Position: Yes. Atmos has been successful in obtaining gas supplies during this ACA period that were reasonable and prudent. In every instance, the Company used a fair and arms length competitive bid process to solicit, evaluate and award the contract to the qualified bidder who offered the least cost supply. Atmos gave no preferential treatment to any bidder, incumbent or otherwise, and regardless of affiliate status. All bidders were on an equal playing field. As a result of the competitive bidding process, Atmos was able to obtain gas supplies at the most reasonable price available in the open, competitive market. (Buchanan Direct, pp. 15-16)

2. Was it prudent for Atmos to utilize a competitive bidding process to obtain its gas supplies?

Atmos Position: Yes. It was prudent for the Company to utilize a competitive bidding process to obtain its gas supplies. The Company believes that this is the best method for securing a reliable source of gas supplies at a reasonable price.

The Company's open, competitive bidding process allows the opportunity for the Company to obtain numerous proposals from a variety of gas marketers who are in the very competitive market of providing gas supplies to local distribution companies throughout the country. We have been successful in obtaining sufficient gas supplies at market prices by using this competitive process that allows the Company to provide our customers with reliable natural gas at just and reasonable rates.

The competitive bidding process (i.e. Request for Proposal Process and RFP Flow Process) is well developed and described within the Manual attached to the Direct Testimony of Becky Buchanan.

The processes for maintaining a Supplier List and Qualification Procedure are described on pages 5-7 of the Manual. A "Sample RFP Letter" is contained on pages 8-10 of the Manual. The Bid Evaluation and Documentation Procedure is discussed on pages 11-12 of the Manual.

The **Affiliated Procedures Section** of the Manual states as follows:

"**Purpose:**

The purpose of this policy is to detail the requirements for dealing with affiliate operations.

RFP Process:

The Company's RFP process ensures that no preferential treatment is given to an affiliated company.

General:

The goal is to prevent preferential treatment being given to any marketer, especially an affiliate. It will be each employee's responsibility to treat all marketers the same. A particular marketer may have more experience on a particular pipeline and may be better equipped to ask certain questions. A rule of thumb should be that an employee should feel comfortable giving several marketers the same information. If an employee has concerns over providing certain data to a marketer or to a group of marketers, the employee should go to their Manager. If concern still exists, the employee and the Manager will consult with the Director, Gas Supply and Services.

Affiliate Guidelines:

In the event a state has specific guidelines for affiliated transactions, it is the Gas Supply Specialist's responsibility to know and follow those guidelines." (Affiliated Procedures Section of Manual)

3. Has Atmos provided a "financial advantage" to its affiliated gas marketing company (AEM) under the Affiliated Transactions Rule (4 CSR 240-40.015) by awarding a portion of its gas supply contracts to AEM after utilizing a competitive bidding process?

Atmos Position: No. Atmos has compensated its affiliated gas marketer Atmos Energy Marketing ("AEM") for its gas supplies at the lesser of fair market value or the fully distributed cost to Atmos to provide those gas supplies to itself.

The open, competitive bidding process utilized by Atmos during the ACA period determined the fair market value of the gas supplies provided by AEM. AEM's bid was the lowest and best bid submitted for those gas supplies during this competitive bidding process. Atmos strongly believes that this bidding process is the best way to determine the fair market value for these gas supplies.

Atmos Energy Corporation does not have the in-house capability to provide the gas marketing services that AEM and other gas marketers provide to Atmos. For example, Atmos does not have personnel who are experts in obtaining gas supplies from the producers of natural gas, or dealing with the intricacies of obtaining interstate and/or intrastate transportation services from upstream suppliers.

The Regional Gas Supply Department employs five professionals in the Gas Supply Department. They include Rebecca Buchanan, a Senior Administrative Assistant, a Gas Supply Representative responsible for IL, TN, and VA, as Gas Supply Specialist responsible for GA and KY, and a Gas Supply Specialist responsible for IA and MO. In order to provide these types of services to the Missouri areas of Atmos, the Company would need to hire additional personnel at a substantial cost and develop processes already utilized by gas marketers for securing such gas supplies and transportation services in the interstate market.

It is unlikely that Atmos could provide such specialized services for the sole benefit of the Missouri jurisdiction at a cost less than a supplier/marketer who performs these services routinely on a much larger scale for a multitude of customers. A simple understanding of the concept of "economies of scale" makes this a reasonable assumption. In addition, Atmos would be entitled to include a reasonable profit on these transactions.

Based upon these facts, Atmos believes that the Fully Distributed Cost of providing these gas services in-house would exceed the market price of those gas supplies, as established by the competitive bidding process.

4. Does the Commission's Affiliated Transaction Rule (4 CSR 240-40.015) require Atmos to lower its gas costs in the PGA/ACA process by the same amount as the profits of the affiliated gas marketer that provided a portion of the gas supplies to Atmos after the formal competitive bidding process?

Atmos Position: Absolutely not. The Affiliated Transaction Rules state that:

"When a regulated gas corporation purchases information, assets, goods or services from an affiliated entity, the regulated gas corporation shall <u>either</u> obtain competitive bids for such information, assets, goods or services <u>or</u> demonstrate why competitive bids were neither necessary nor appropriate." (4 CSR 240-40.015(3)(A). (*emphasis added*)

The Company has fully complied with this requirement of the rule by obtaining competitive bids.

The Affiliate Transactions rules state that the utility "shall not provide a financial advantage to an affiliated entity." The rules also state that the utility "shall conduct its business in such a way as not to provide any preferential service, information, or treatment to an affiliated entity over another party at any time."

The Company has also complied with this aspect of the Affiliate Transactions rules. A financial advantage would occur if the utility compensated an affiliate at a rate that is above the lesser of the fair market price or the fully distributed cost ("FDC") to the utility. The rules further specify that the FDC means a methodology that examines all costs of an enterprise in relation to all the goods and services that are produced, including a recognition of all costs incurred directly or indirectly including a general allocation of any costs that could not be directly assigned or indirectly allocated. The Rules do not specify that a profit constitutes a financial advantage.

As explained in the Direct and Rebuttal Testimony of Rebecca Buchanan, Atmos Energy Corporation does not have the in-house capability to provide the gas marketing services that AEM and other gas marketers provide to Atmos. For example, Atmos does not have sufficient personnel with the in-house expertise to perform the gas marketing services that AEM and other marketers provide to Atmos. Atmos does not have personnel experienced in obtaining gas supply from producers of natural gas, trading on the physical and financial markets, or arranging for transportation services from upstream suppliers.

In order to provide these types of services to the Missouri areas of Atmos, the Company would need to incur substantial cost and develop many processes already utilized by gas marketers for securing such gas supplies and transportation services in the interstate market. Further, Atmos would be entitled to include these additional expenses in its cost of service upon which its rates are based and earn a reasonable return on any capital investment related to these services.

Based upon these facts, Atmos has determined that the Fully Distributed Cost of providing these gas services to itself would exceed the market price of those gas supplies. Therefore, Atmos believes it is prudent to solicit proposals from gas marketers through a competitive bidding process to provide these necessary services in the most cost-effective manner.

Unfortunately, Staff makes the flawed assumption in the Direct Testimony of David M. Sommerer that if AEM is able to procure gas supply at a certain price, then the regulated utility must also have similar access to gas supply at that same price without any additional overhead. Thus, he concludes, the utility could provide its own gas supply at a lesser rate without contracting with the affiliate.

Mr. Sommerer's assertion overlooks two crucial facts. First, he ignores the additional costs that the utility would incur in terms of personnel and processes necessary to provide gas marketing services that AEM and other marketers provide to Atmos. Second, Mr. Sommerer overlooks the fact that gas marketers, both affiliated and non-affiliated, have greater purchasing power than regulated utilities by virtue of the fact that they may bundle their purchases into a comprehensive portfolio of business that can include non-utility customers. The utility does not have the ability to take advantage of similar efficiencies of scale. The fair market value that a public utility can obtain in the natural gas markets is simply not the same as the fair market value that AEM can obtain in the natural gas market.

While Mr. Sommerer correctly notes that gas costs are passed through to ratepayers with no markup, he does not take into account the fact that additional Company personnel and resources would be necessary to provide such gas supply. The additional expenses would be included in the Company's cost of service, and the utility is permitted to recover prudent expenses and earn a reasonable return on any capital costs associated with these services.

5. Should Staff's proposed affiliated transaction adjustments be adopted?

Atmos Position: No. Staff has proposed to lower Atmos' gas supply costs by an amount equal to Staff's calculation of the profits of AEM on transactions in the Hannibal/Canton and Butler areas of the Company. In effect, Staff is proposing to impute the profits of AEM to Atmos, and thereby lower the gas supply costs to the customers in these areas. In effect, $349,015 of Atmos' gas costs will be disallowed in the Northeast rate division (the Consolidated system of Hannibal, Canton, Palmyra and Bowling Green), and by $13,964 disallowed in the West rate division (the Butler system), even though the AEM bid was the lowest and best bid in these areas. Atmos was committed contractually to pay the amount of the bid that was accepted. However, Staff's proposed adjustment will require Atmos shareholders to absorb $362,979 [$349,015 + $13,964] of prudently incurred costs.

The Staff's proposed affiliated transactions adjustment is inappropriate and unreasonable because Atmos' gas costs are prudent, and the Company has complied with the Commission's Affiliated Transaction Rule by competitively bidding for its gas supplies. Atmos has treated its affiliated gas supplier in the same manner as it has the other gas suppliers that participate in the RFP process.

It would be unreasonable to expect Atmos to lower its gas costs by some amount of imputed profits of one of its gas marketers when it is contractually obligated to pay the bid price of the lowest and best bid accepted from the affiliated gas marketer. Atmos must respectfully disagree with Staff's concerns related to the fact that Atmos has utilized the services of AEM, an affiliate of Atmos, for some of its underlying gas supply services.

Staff's concerns and proposed adjustments are misplaced, and should be rejected by the Commission. As explained herein, Atmos utilized a formal Request For Proposal (RFP) process, as required by 4 CSR 240-40.016(4)(A), to determine that AEM's proposals for gas supplies were the least expensive, and best proposal for Atmos and its ratepayers. Such competitive bidding is required by 4 CSR 240-40.016, unless the regulated company can demonstrate why competitive bids were neither necessary nor appropriate.

4 CSR 240-40.016(4)(A) states as follows:

> "When a regulated gas corporation purchases. . . goods or services from an affiliated entity, the regulated gas corporation shall either obtain competitive bids for such . . . goods or services or demonstrate why competitive bids were neither necessary nor appropriate."

In this case, Atmos utilized the preferred competitive bidding process to obtain its gas supplies. Staff does not dispute this fact and identifies no fault with the bidding process itself. Staff does not dispute that AEM was the least cost bid. Despite this, Staff seems to have an underlying and unfounded distrust of the contractual arrangements solely because they involve an affiliated company. This Staff distrust is completely misplaced.

Since AEM provided the lowest and best bid for the PEPL gas supplies, the regulatory concerns related to the affiliated transaction should be satisfied. If Atmos had entered into a transaction with its affiliate that was not the least expensive and best bid, then Staff would have a legitimate concern about the prudence of gas costs incurred. However, those are not the facts in this case.

Staff attempts to impute the profits from AEM to Atmos, suggesting that it is somehow imprudent for Atmos to accept the low cost bids of AEM. Staff suggests that AEM's bid should be even lower (even though the analysis of other bids already shows AEM to be the lowest of all bids received). In essence, Staff does not afford AEM the same opportunity to make a profit as the other suppliers. Beyond the scope of the rules' requirement that Atmos not provide a financial advantage to its affiliate, it appears that Staff is intent on making AEM provide a non-profit gas supply service to the Missouri customers. This adjustment is improper and should be rejected by the Commission.

Atmos also has a fundamental disagreement with Staff regarding the appropriateness of any adjustment to Atmos' gas costs related to the AEM contracts for gas supplies. The Staff has not demonstrated the imprudence of Atmos entering into the contracts with AEM that provide the lowest cost gas supplies for Atmos and its ratepayers. However, the Staff has proposed a disallowance for these costs apparently for the sole reason that the gas supply contracts were provided by an affiliate. Atmos does not believe that Staff has provided a reasonable or lawful basis for its proposed affiliated transactions disallowances.

In responses to Staff data request DR 0079 in the current case, Atmos provided its RFP evaluations. These evaluations clearly show that in every instance Atmos awarded the contract to the supplier who submitted the least cost and best bid. Had Atmos failed to award the contracts in question to AEM, Missouri customers would have been subject to higher gas costs.

> If the Commission decides that Staff's interpretation of the Affiliated Transaction Rule is appropriate, it will provide a huge disincentive for regulated gas corporations to deal with an affiliated gas marketer, even if that gas marketer could provide the lowest and best bid for natural gas supplies. In effect, the regulated natural gas corporation will have to lower its gas costs by an amount equal to some imputed profit level of the affiliated gas marketer, even though the natural gas company will be required by contract to pay the affiliated gas marketer the bid price that includes that profit level for the natural gas supplies.
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> Staff's interpretation of the Affiliated Transaction Rule will cause the regulated natural gas corporations in Missouri to forego dealing with an affiliated gas marketer, even though the affiliated gas marketer is offering to provide gas supplies at a lower price than all other bidders for those gas supplies. As a result, ratepayers will not receive the lowest and best price for their natural gas supplies.
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> Even if the Commission adopted Staff erroneous interpretation of the Affiliated Transactions rules, it should reject Staff's proposed adjustments in this case. Staff's proposed adjustment imputes the "gross profits" of AEM to the Company. However, Staff apparently ignores the fact that AEM also has overhead that must be recovered before AEM can make a "profit".
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> Mr. Sommerer's calculation only takes into account the price of gas purchased by AEM against the price of gas sold to the utility. When making his recommendation for disallowance, Mr. Sommerer has failed to consider any of AEM's administrative and general costs to provide gas marketing services to the utility. Even if the Commission can accept his argument that a utility should be compelled to reduce its recoverable gas costs by any profit made by its affiliate, the schedule Staff provides to support the disallowance does not accurately state the level of net income earned by AEM on the gas supply deals under review because it is missing an important piece of the calculation.
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> The Company respectfully suggests that there is no legitimate or lawful basis for the Staff proposed affiliated transaction adjustments in this case.

WHEREFORE, Atmos Energy Corporation hereby requests that the Commission reject the proposed Affiliated Transactions adjustments proposed by the Staff in this proceeding.

Respectfully submitted,

*/s/ James M. Fischer*_________________

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CERTIFICATE OF SERVICE

I do hereby certify that a true and correct copy of the foregoing document has been hand delivered, emailed or mailed, postage prepaid, this 30th day of June, 2010, to all counsel of record.

/s/ *James M. Fischer*
James M. Fischer