MEMORANDUM

TO: Missouri Public Service Commission Official Case File
Case No. GR-2010-0238, Atmos Energy Corporation

FROM: David M. Sommerer, Manager - Procurement Analysis
Phil Lock, Regulatory Auditor - Procurement Analysis
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/s/ David M. Sommerer, 12/21/2011	s/ Lera Shemwell, 12/21/2011
Project Coordinator, Date	Staff Counsel's Office, Date

SUBJECT: Staff's Recommendation in Atmos Energy Corporation's
2009-2010 Actual Cost Adjustment Filing

DATE: December 21, 2011

EXECUTIVE SUMMARY

Procurement Analysis (Staff) has reviewed Atmos Energy Corporation's (Atmos or Company) 2009-2010 Actual Cost Adjustment (ACA) filing. This filing was made on October 15, 2010, for rates to become effective on November 1, 2010, in all areas served in Missouri. This filing was docketed as Case No. GR-2010-0238.

This memorandum is organized into three sections. Each section begins with detailed explanations of Staff's concerns and recommendations. The three sections are:

1. Atmos Energy Corporation – General
2. Northeast area
3. Southeast (SEMO) area

Staff's analysis consisted of:

1. A review and evaluation of the Company's billed revenues and its natural gas costs for the period of September 1, 2009, to August 31, 2010.
2. A comparison of billed revenue recovery with actual costs will yield either an over-recovery or under-recovery of the ACA costs.
3. An examination of Atmos' gas purchasing practices to determine the prudence of the Company's purchasing decisions.
4. A hedging review to determine the reasonableness of the Company's hedging plans for this ACA period.
5. A reliability analysis of the Company's estimated peak day requirements and capacity levels to meet those requirements.

** **Denotes Highly Confidential Information** **

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On August 1, 2011, Atmos Energy and Liberty Energy (Midstates) filed a joint application for authority to sell its regulated natural gas utility assets in Missouri, Illinois and Iowa to Liberty Energy (Midstates) Corporation. (Joint Application of Atmos Energy Corporation and Liberty Energy (Midstates) Corporation – File No. GM-2012-0037). The sale of the properties is contingent upon approval from the three regulatory commissions in Missouri, Illinois and Iowa.

Summary of Recommendations

The Staff recommends that the Commission issue an order requiring Atmos to:

1. Respond to the issues in the Reliability Analysis and Gas Supply Planning section of this memorandum. (There is no financial adjustment related to Reliability or Supply Planning for this ACA review period.)
2. Respond to the RFP and Transaction Confirmation section of this memorandum.
3. Respond to the Storage section for the Piedmont Arcadia (MRT system).
4. Respond to Staff's comments in the Hedging section. (There is no financial adjustment related to Hedging)
5. Respond to the Cash Out section of this memorandum.
6. Respond to the Storage section for the Northeast and SEMO service areas as outlined in Sections 2 and 3.

STAFF TECHNICAL REPORT AND ANALYSIS

SECTION 1 - ATMOS ENERGY CORPORATION – GENERAL

Atmos' Missouri service territory

Atmos serves the following areas: West, Kirksville, Northeast and Southeast.

The West area includes Butler which is served by Panhandle Eastern Pipe Line Co., LP (PEPL) and the former Rich-Hill/Hume service area which is served by Southern Star Central Gas Pipeline, Inc. (SSCGP). The West area is served by an average of 4,000 firm sales customers.

The Kirksville area, served by ANR Pipeline Co. (ANR), has an average of nearly 5,700 firm sales customers.

The Northeast area, served by Panhandle Eastern Pipe Line Co., LP (PEPL), serves an average of 13,360 firm sales customers in Hannibal-Canton, Bowling Green and Palmyra.

The Southeast area (SEMO) includes Jackson, served by Natural Gas Pipeline Co. of America (NGPL), Piedmont, served by Mississippi River Transmission Corp. (MRT), and the Southeast Missouri Integrated system, served by Texas Eastern Transmission, LP (TETCO) and Ozark Gas Transmission, LLC. The Southeast area also includes the former Neelyville service area which is served by NGPL and TETCO. Together they served an average of 33,168 firm sales customers.

Reliability Analysis and Gas Supply Plan Review

One purpose of the ACA process is to examine the reliability of the Local Distribution Company's (LDC) gas supply, transportation, and storage capabilities. As a gas corporation providing natural gas service to Missouri customers, the Company is responsible for conducting reasonable long-range supply planning and for the decisions resulting from that planning. For this analysis, Staff reviews the LDC's plans and decisions regarding estimated peak day requirements and the capacity levels to meet those requirements, peak day reserve margin and the rationale for this reserve margin, and natural gas supply plans for various weather conditions.

Staff's review of the status of the reliability for the Atmos service areas produced the following comments and concerns:

A. Reserve Margins and Future Growth/Decline

Effective November 1, 2009, the Company reduced its pipeline capacity to the Kirksville system (on ANR pipeline) after an updated review revealed the company had more capacity than necessary to meet its peak day requirements. The reduction in capacity changed the reserve margin from 32% (2008/2009 ACA) to 10% (2009/2010 ACA), which saves ratepayers in this district approximately $11.20 per customer per year. Staff encourages the Company to continue to monitor the reserve margins for all of its districts.

B. Supply Planning

1. Supply For Combined Hannibal and Bowling Green Service Areas

Combined, the peak days for Hannibal and Bowling Green areas for the 2009/2010 ACA are 20,395 dth. Atmos purchases a single supply contract to serve both areas. Staff evaluated the amount of gas supply needed to reliably serve these areas. Based on the table shown below, Staff believes that the Company has excess supply contracted for the two areas.

Supply – Consolidated	Winter Dth/ Day	Comments
Hannibal/Canton/Palmyra (HCP)	18,591	Atmos Estimated peak day for 2009/2010 Winter
Bowling Green	1,804	Atmos Estimated peak day for 2009/2010 Winter
Sub-total	20,395	Atmos Combined peak days for BG and HCP
Bowling Green storage contract	(520)	IOS storage MDWQ
Hannibal storage contracts	(11,886)	IOS, WS, and FS storage MDWQ is 12,200. Staff reduced this to 11,886 because of ratchets on storage.
Subtotal	7,989	Requirements for flowing supply (Peak Day less supply provided by storage withdrawals rights)
	(3,300)	Propane air mixture
Subtotal	4,689	Net flowing requirements
	(10,645)	Amount of baseload and swing supply under contract
Subtotal	(5,956)	Net flowing requirements (negative number indicates more supply than required for a peak day)

In reviewing the invoices for baseload nominations this ACA period, in November Atmos nominated 2,250 dth/day, while December and January nominations were 3,500 dth/day, February was 1,800 dth/day, and March was 3,000 dth/day. The highest daily Swing volume nominated for Swing gas was 5,300 dth/day, which occurred in February. However, this was without the use of propane and February was nominated at 1,800 dth/day. The maximum combined baseload and swing supply nominated occurred in January at 7,885 dth. This means that, in the winter months, the amount of gas flowing was 7,885 dth or less each day. Atmos' summer nominations were 4,100 dth /day or less. Total demand charges for the 2009/2010 winter were approximately $17,700. Staff considered Atmos' cold weather plans and the plan shows that flowing requirements of 8,000 dth/day would meet their needs. However, this does not consider the propane withdrawal of 3,300 dth/day. When the propane withdrawal is considered, the flowing requirements become 4,700 dth/day. This leads to Staff's conclusion Atmos could have reduced its 10,645 dth/day (baseload and swing contracted) nominations. If Atmos had done so, it would have reduced reservation charges in the 2009/2010 ACA, with no loss in reliability. No adjustment is proposed for this ACA, because the amount is immaterial, when viewed on a per customer basis. However, Atmos gas supply planning personnel should consider the level of demand charge costs associated with a full requirements contract, when customer demand can be met using storage withdrawals.

2. Storage Balance for Piedmont/Arcadia (MRT system).

Staff is concerned that, for this area, Atmos plans are to have storage filled at the end of October, which does not allow the Company to put any excess gas supply into storage during the first half of November when the weather could still be warm. Staff recommends Atmos evaluate its planned storage balances for October and November to allow it to make injections should it experience warm or extremely warm weather in these months. The Company's gas storage plan for the Piedmont system shows Atmos has planned for storage balances to be at 100% at the end of October. By adhering to its plan, the Company was unable to inject excess gas supplies into storage during November of this ACA period. Specifically, Atmos nominated 340 dth/day for the period of November 1st through November 30th. However, about mid-way through the month, the Company realized it did not need this much gas. This led to the Company selling excess gas back to its supplier from November 18th through the 30th. As a result, Atmos bought 4,420 dth at a first of month index price of ** _________ ** and sold back to the supplier at a Gas Daily average (per agreement) price of ** ___________. ** The net loss for the sale was approximately ** _________ ** or $3,991, an immaterial amount for the Piedmont area, but this sale would not have occurred had the Company only filled its Piedmont storage to 95%, as it does in other areas. The Company also sold back 900 dths in January, resulting in an immaterial loss of $527 and resulting in a total of 5,320 dth being sold back to the supplier during this winter season.

<u>Request for Proposals (RFPs) and Transaction Confirmations</u>

The Company received ** ______________________ ** for the period of April 1, 2009, through March 31, 2010, for the Hannibal/Bowling Green area and November 1, 2009 through March 31, 2011 for the Piedmont/Arcadia area. The Company should review its plans to increase vendor participation in response to the low number of bid responses to RFPs.

The supply contract for the Rich Hill and Hume service area (WEMO district) covers the period of April 1, 2009 through March 31, 2011. The Company re-bid its contract for the period of June 1, 2011 to March 31, 2012 and received ** _____________________. ** Since the current contract is included in the 2010-2011 and 2011-2012 ACA's, Staff will provide further comments regarding the separation from the larger Kansas system and the contractual split in the context of those ACA reviews.

<u>Transaction Confirmations</u> - Staff recommends the Company evaluate the requirements it must have in each final transaction confirmation. Atmos should carefully review the confirmations to ensure that they reflect the terms of the gas being purchased.

Affiliated Transactions

For the 2009-2010 ACA period ending August 2010, Atmos had the following affiliated supply and Asset Management Arrangement (AMA).

- The Rich-Hill/Hume AMA effective 4-1-07 to 3-31-09 and 4-1-09 to 3-31-11. The Rich-Hill/Hume AMA was effective during the entire ACA period.

This agreement was executed between Atmos Energy Corporation (AEC) and Atmos Energy Marketing (AEM). Staff does not propose any adjustment related to this AMA agreement.

The Commission issued its Report and Order in Case No. GR-2008-0364 on November 9, 2011.

Hedging

Atmos implemented a hedging plan using the Company's Regulated Utility Operations Risk Management Control Guidelines. The Risk Management activities may include both physical transactions and financial transactions. The Company's hedging plan, based on expected requirements for Missouri for the 2009-2010 winter, included storage and financial hedging instruments. For financial hedging, the Company used swap agreements, over-the-counter instruments that allowed the Company to fix a price in exchange of cash flows. This method, combined with storage, was consistent with the Company's hedging purpose to stabilize the volatility of natural gas prices, not necessarily achieving the lowest possible cost. ** ** The financial hedging instruments and storage combined to cover 71% of the volumes actually delivered to customers for November 2009 through March 2010. This is equivalent of hedging 67% of normal winter requirements with storage and the financial instruments. The financial hedging purchases for November 2009 through March 2010 were ratably made between early April 2009 and late October 2009. The Company's hedging term is for two winter seasons (November through March) and its implementation period is from April through October. However, Staff was notified in June 2008 that Atmos would be temporarily curtailing its hedging transactions for the winter of 2009-2010, in its 2-year hedging program, due to escalating natural gas prices. The Company ultimately started hedging for the 2009-2010 ACA period in 2009 as the prices declined from the highs.

Given the nature of the hedging strategy adopted by the Company, potentially using various financial instruments in order to assist in achieving a diversified hedging program, the Staff recommends the Company continue to monitor the market movements diligently, employ

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disciplined as well as discretionary approaches in its hedging practices, and consider the possibility of expanding its gas portfolio to include physical as well as financial hedges, in addition to storage, that more closely track physical price risk. There should be a strong relationship between the physical price risk and the hedges used to mitigate that price risk. In addition, the Company should carefully consider looking at longer term time horizons for establishing hedges.

	Hedged % of Normal
Kirksville	** ____ **
Butler	** ____ **
SEMO	** ____ **
Consolidated (Hannibal/ Bowling Green)	** ____ **

Cash out Provisions

Under its Missouri tariffs, Atmos tracks its transportation customers' monthly imbalances for gas the customer nominated versus the gas it actually used. These imbalances are then cashed out on a monthly basis. When pricing out monthly imbalances for transportation customers on ANR, MRT, NGPL and PEPL (June 2010 – August 2010) the Company relied on high or low published index prices from the beginning to the end of each month (without regard to weekly index prices). According to the Company's tariff sheet No. 52 for Natural Gas Transportation Service, monthly imbalance volumes are applied to the high or low index prices for any week beginning in the calendar month as published in Natural Gas Week. For TETCO, the same cash out indexes were retrieved from Spectra Energy instead of Natural Gas Weekly, also creating a difference in pricing. Going forward, the Company agreed to price out monthly imbalances using the Natural Gas Week published index price for any week beginning in the calendar month. Because the tariffs were not followed for the transactions mentioned above, there were some differences in Staff's cash-out calculations. In total, the differences were small so Staff did not propose any cash out adjustments in this ACA.

RECOMMENDATION – ATMOS ENERGY CORPORATION, GENERAL

The Staff recommends that the Commission issue an order requiring Atmos to:

1. Respond to the issues in the Reliability Analysis and Gas Supply Planning section of this memorandum. (There is no financial adjustment related to Reliability or Supply Planning for this ACA review period.)
2. Respond to the RFP and Transaction Confirmation section of this memorandum.
3. Respond to the Storage section for the Piedmont Arcadia (MRT system).
4. Respond to Staff's comments in the Hedging section.
5. Respond to the Cash Out section of this memorandum.

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SECTION 2 – NORTHEAST AREA

Staff's review found storage rate discrepancies on PEPL, TETCO and NGPL. The discrepancies are small so Staff did not make any adjustments. Staff recommends, however, that the Company evaluate the storage discrepancies for PEPL, TETCO and NGPL as described below and keep Staff informed of all changes.

PEPL Storage

During the months of July and August 2010 Atmos improperly calculated its gas costs for storage injections on PEPL. The Company acknowledged, in its response to Data Request No. 105, that an incorrect invoice amount was used to determine the injection rates for July and August 2010. Atmos further indicated that the storage injection rates should have been calculated using the current months' gas supply costs. Using the proper rate changes, the storage injection rate in July 2010 would be ** ______ ** instead of ** ______ ** as filed and the August 2010 storage injection rate would be ** ______ ** instead of ** ______ ** as filed. Staff recommends that the Company evaluate the storage injection costs on PEPL for July and August 2010.

SECTION 3 – SOUTHEAST (SEMO) AREA

TETCO Storage

During August 2010, the storage injection amount for TETCO was misstated. Atmos inadvertently added $22,309 to the Anadarko invoice amount (to calculate storage injection costs) when it should have subtracted that amount. The Company agrees with this change.

NGPL Storage

During July 2010, Atmos misstated the total purchased gas cost for NGPL storage injections. The Company acknowledged that the proper amount should have been $191,154, not $181,154.

The Company also applied a hard-coded fuel factor of $0.0434 for all NGPL storage injection calculations. The fuel factor normally changes on a monthly basis based upon the deliveries for each month. The Company acknowledged that the fuel factor should have been a formula that divides the fuel loss on each NGPL invoice by the total delivered amount. Staff recommends that all fuel factors be calculated by formula.

RECOMMENDATION – ATMOS ENERGY CORPORATION

The Staff recommends that the Commission issue an order requiring Atmos to:

1. Adjust the ACA account balances in its next ACA filing to reflect the following Staff adjustments and to reflect the (over)/under-recovered ACA balances in the "Staff Balances" column of the following table:

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TABLE 1 (SECTIONS 1-3)

ALL AREAS	Filed Balances for 2009-2010 (Ending 8-31-10)	Staff Adjustments	Staff Balances for 2009-2010 (Ending 8-31-10)
Southeast Area: Demand ACA	($235,952)	$0	($235,952)
Commodity ACA	($1,094,543)	$9,918 (A)(A1)	($1,084,625)
Kirksville Area: Demand ACA	($58,469)	$0	($58,469)
Commodity ACA	($418,449)	$1,570 (A)(A2)	($416,879)
West Area: Demand ACA	$39,369	$0	$39,369
Commodity ACA	($94,548)	$0	($94,548)
Northeast Area: Demand ACA	($22,826)	$0	($22,826)
Commodity ACA	($394,555)	($334,501)(A)(A3)	($729,056)

Notes to Staff Adjustments:
A) ACA beginning balances August 31, 2009 adjusted to prior year ending balances
A1) $1,387 Supply allocation (2006-07 ACA) + $8,531 cash-out (scheduling fees 2008-09 ACA)
A2) $1,570 Cash-out (scheduling fees 2008-09 ACA)
A3) ($337,226) Affiliated transaction for Hannibal/Canton/Palmyra/Bowling Green and Butler service areas during the 2008-09 ACA (Staff Brief) + $2,725 Cash-Out (2008-09 ACA)

2. Respond to the Storage section for the Northeast and SEMO service areas as outlined in Sections 2 and 3.

3. File a written response to the recommendations included herein within 30 days.

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter In the Matter of Atmos Energy Corporation's Purchased Gas Adjustment Tariff Filing	))))	File No. GR-2010-0238

AFFIDAVIT OF DAVID M. SOMMERER

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

David M. Sommerer, being of lawful age, on his oath states: that as a Utility Regulatory Manager in the Procurement Analysis Unit of the Utility Services Department, he has participated in the preparation of the foregoing report, consisting of 9 pages to be presented in the above case; that he has verified that the following Staff Memorandum was prepared by himself and Staff of the Commission that have knowledge of the matters set forth as described below; that he has verified with each of the Staff members listed below that the matters set forth in the Staff Memorandum are true and correct to the best of his knowledge and belief,

Phil Lock, Utility Regulatory Auditor III: Billed Revenues and Actual Gas Costs
Derick Miles, PE, Utility Regulatory Engineer I: Reliability Analysis and Gas Supply Planning
Kwang Choe, PhD, Regulatory Economist II: Hedging

that he has knowledge of the matters set forth in such report and that such matters are true to the best of his knowledge and belief.

David M. Sommerer

David M. Sommerer

Subscribed and sworn to before me this 21st day of December, 2011.

D. SUZIE MANKIN
Notary Public - Notary Seal
State of Missouri
Commissioned for Cole County
My Commission Expires: December 08, 2012
Commission Number: 08412071

D. Suzie Mankin

Notary Public