BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the matter of Atmos Energy Corporation's 2008-2009 Purchased Gas Adjustment and Actual Cost Adjustment	)))	**Case No. GR-2009-0417**

ATMOS ENERGY CORPORATION'S
RESPONSE TO STAFF RECOMMENDATION

COMES NOW Atmos Energy Corporation ("Atmos" or "Company"), and pursuant to 4 CSR 240-2.080 and the Commission's Order Directing Response issued on January 3, 2011 states its response to the Staff's Recommendation filed on December 30, 2010 as follows:

On December 30, 2010 the Commission Staff filed its recommendation following completion of the audit of the 2008-2009 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, 2008 to August 31, 2009 for all areas of served by the Company in Missouri. The Company will respond to various issues identified by Staff in paragraphs corresponding to those sections contained in the Staff Memorandum.

Atmos respectfully prefaces its response by noting that a number of these recommendations are similar to those responded to in GR-2008-0364. Additionally, Company personnel met with Staff via teleconference on October 6, 2010 ("Meeting"). During the Meeting, Atmos addressed a variety of Staff's concerns in this docket at length. Further, the Company performed considerable additional analyses at Staff's request following the Meeting. Although previously addressed, many of the same issues addressed in GR-2008-0364 and discussed with Staff at the Meeting have been included in Staff's recommendations without

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mention or apparent consideration by Staff of the information previously provided or recommendations already implemented by Atmos.

SECTION 1: ATMOS ENERGY CORPORATION, GENERAL

Staff made the following recommendations with regard to the overall Atmos Energy Corporation: "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. Provide to Staff, within 90 days, evaluations/assessments and analyses related: (A) Priority of Atmos Firm Natural Gas Supplies; (B) Supply for Combined Hannibal and Bowling Green Service Areas and (C) Flexibility of Supply Plans.

3. Comply with the School Transportation Imbalance section of this Memorandum.

4. Comply with the Customer Billings section of this Memorandum.

5. For the Staff concerns regarding the supply agreement with Atmos Energy Marketing, an affiliate of Atmos, adjust the gas costs for the Northeast district by $413,165 and by $81,852 for the Butler district as shown in Table 1 (Sections 1-4). Additionally, respond to the RFP issues and recommendations in the Affiliated Transaction section of this Memorandum.

6. Respond to Staff's comments in the Hedging Section.

7. Adjust cash-out amounts for the following: Kirksville area $1,570; SEMO area $8,531; and Northeast area ($6,739). These adjustments are included in the tables located in Table 1 (Sections 1-4).

8. File a written response to the recommendations included herein within 30 days." (Staff Memorandum, pages 8 and 9 of 11.)

ATMOS RESPONSE TO GENERAL RECOMMENDATIONS
RELIABILITY ANALYSIS AND GAS SUPPLY PLAN REVIEW

Regression Analysis

All issues associated with the regression analysis have been previously discussed with Staff. Staff mentions that in its comparison between Company's regression models and load from the prior winter, there was "as much as 79% variation in forecasted versus actual loads." Staff acknowledges that Atmos explained the anomalous data point was the result of a measurement problem specific to the Piedmont Arcadia study. The 79% variation also occurred on a day that fell far outside the range of the top five coldest days. A comparison of the forecasted versus actual loads is most accurate on the coldest days for which the model is designed. Staff chose this outlier to demonstrate that the regression analysis may be unreliable. However, it only demonstrates a measurement problem specific to the Piedmont Arcadia system, not a problem with the overall regression methodology. Staff also complains that the data point was not removed from the analysis. The load study to which Staff refers was prepared during the summer of 2008 in anticipation of the 2008-2009 winter. The measurement problem resulting in the anomalous variation was not uncovered until Spring of 2009, long after the analysis was completed.

Staff also expresses a concern that "with the Company using six years worth of data for the regression analysis, the older data may result in an over-estimate of peak day requirements." (Staff Memorandum, page 2 of 11.) To remedy this, Staff recommends that "the Company consider using a fewer number of years of data. Doing so will allow the Company to capture more recent system load variations due to customer growth (increase or decline), change in customer usage habits, or changes in appliance efficiency or housing construction." (Staff Memorandum, page 3 of 11). This is similar to a recommendation made in GR-2008-0364.

In response, the Company notes that it began incorporating a stability test beginning with the 2009-2010 ACA. Staff was given information about this stability test in the response to Staff's recommendations filed in GR-2008-0364 as well as during the Meeting. The stability test is a statistical test called the "Quandt-Andrews Break Point Test" which tests for breakpoints or structural changes in the sample of an equation. These breakpoints simply mean that the data has changed over the sample period. The overall forecast is improved by removing the unstable data and calculating the regression on stable data.

Gas Supply Planning

1. Priority of Atmos Firm Natural Gas Supplies

Staff begins by suggesting that Atmos supplies may be less than reliable or "firm," because Atmos has "no contracted capacity in the Production Area." (Staff Memorandum, page 3 of 11.) This assertion is incorrect. Atmos maintains Panhandle Eastern Pipeline (PEPL) capacity in the Production Area ("Field Zone") throughout the year, and has done so for at least 14 years. Atmos typically uses Field Zone capacity in the winter for storage withdrawals and in the summer for storage injections. Staff recommends that the Company "assess the reliability of deliveries" and "assess whether its own or its supplier's lack of Production Area capacity impacts reliability." (Staff Memorandum, page 3 of 11.) Staff refers to the fact that pipelines could issue force majeure, curtailments, flow orders, or other cuts of natural gas deliveries. These are pipeline events, however, and do not reflect a reliability issue with respect to Atmos or its suppliers. In fact, when a pipeline actually did invoke force majeure during the 2007-2008 ACA period following a pipeline rupture, Atmos customers were not impacted. Atmos simply pulled gas from storage, using its Field Zone capacity as designed. Atmos does not lack capacity and has experienced no reliability issues with its suppliers.

2. Supply For Combined Hannibal and Bowling Green Service Areas

Staff notes that "Atmos received only 2 supply bids for the combined Hannibal and Bowling Green service area for the period of April 2009 through March 2010" and recommends that Company "evaluate the limited response to its RFP." (Staff Memorandum, page 3 of 11.)

Company has already investigated Staff's concern and related its findings to the Staff during the Meeting. According to Company's Panhandle Eastern Pipeline representative, when the Production/Market interface was introduced, suppliers predicted that the Market Zone would have more liquidity than the Field Zone. Over time, the Field Zone has actually become more liquid. Accordingly, suppliers have started shifting their pipeline capacity back to the Field Zone. To put another way, there are simply fewer suppliers holding capacity in the Market Zone. Atmos prepared and provided to Staff[1] a comparative cost analysis of Field receipts versus Market receipts using supplier pricing during the period April 2007-March 2008. The net result of this analysis showed that Atmos saved $.099 per Dth by keeping pipeline receipt capacity in the Market Zone. The gas supply market continues to evolve, and there are now more supply sources available in the Market Zone than in the past, which may ultimately increase the number of bidders. The bottom line is that by following the Staff recommendations, Atmos would forgo the savings the analysis showed by moving its Haven Market Zone receipts to the Field Zone and subsequently incur increased demand charges with no assurance of more supply reliability. This is not something that Atmos is prepared to do unless ordered by the Commission. As the supply situation changes, Atmos will continue to evaluate moving our receipts within the Market Zone and Field Zone to best access the supply in a financially responsible manner.

3. Flexibility and Cost of Atmos Supply Plans

a. <u>Cost of Supply</u>

Staff uses an incorrect figure in their recommendations that overstates the excess supply held by Atmos in the Hannibal and Bowling Green areas. During the Meeting, Atmos explained to Staff that the figure of 26,394Dths is not accurate. In this total volume, Staff incorrectly

[1] GR-2009-0417 Data Request 10.1

includes In/Out Storage (IOS) volumes that are already included as part of the Enhanced Firm Transportation (EFT) and Small Customer Transportation (SCT) capacities. The correct capacity should be only 24,264 Dths [8,045 EFT (Hannibal) + 1,052 Winter Storage (Hannibal) + 9,267 Flexible Storage (Hannibal) + 3,300 Propane (Hannibal) + 2600 SCT (Bowling Green)]. Additionally, Atmos explained that it is improper to combine Hannibal and Bowling Green because the Company only pays for what is actually used of the 2,600 available on Bowling Green's SCT. Staff's assertion that the Company's contracted supply and storage exceeds peak day requirements by 22.8% is misleading.

Finally, Staff undertakes an analysis of two different scenarios to determine the potential impact of any excess supply. Atmos is unaware of the assumptions or methodology underlying Staff's analyses and cannot verify the accuracy of the results. Staff concludes that under either circumstance, however, the resulting impact of any excess supply is "not material." (Staff Memorandum, page 4 of 11.)

b. Flexibility of Supply Plans

As explained to Staff during the Meeting, the Company's supply plans are based on normal weather requirements and are provided to the suppliers for informational purposes only. The actual nominations are given before each upcoming month. The plans provide for 20% warmer and 20% colder scenarios, demonstrating what purchases might be if conditions are not normal. If warmer weather occurs, Atmos would purchase less first-of-month (FOM) gas to accommodate planned storage withdrawals. If the FOM nomination is already in place, Atmos has the option to sell excess FOM volumes back to the supplier.

Staff notes that "Atmos does not provide an analysis of how its supply plans could be varied to address warm weather requirements for the winter months of November through

March.” (Staff Memorandum, page 4 of 11.) The Company does not agree that there is need for further analysis. Atmos has already explained to Staff, at length, how Atmos prepares and monitors the daily forecast requirements and deals with changing system requirements through the use of storage injections and withdrawals, swing purchases, and supplier buybacks.

School Transportation Imbalances

Staff recommends that all future billings for school transportation customers include the pipeline’s maximum firm transportation commodity rate and fuel charges in its monthly-cash out calculation. (Staff Memorandum, page 4 of 11.)

According to PGA tariff sheet 63.3b, monthly cash-out rates for school transportation customers will be calculated using the "applicable pipeline's maximum firm transportation commodity rate and fuel charges to the pipeline's applicable cash-out rate as published at the end of each month." These charges were not applied to the cash-out rates for school transportation customers on the MRT, NGPL, TETCO, ANR and PEPL pipeline systems. The revised cash-out rates resulting from this change were immaterial during this ACA period so no adjustment was made.

The Company will ensure that all future billings for school transportation service will be done in compliance with the approved tariff.

Customer Billings

Staff recommends that Atmos follow language included on Sheet No. 40 of the Company’s PGA tariffs limiting applicability of new rates only to those bills where all service is taken after the effective date of the new rates. Rate Administration has implemented a one month lag in billing newly effective rates in order to remain in compliance with the tariff language. For example, a new PGA rate effective on February 1st will be billed with the first

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cycle in March. This will ensure all gas consumed in January will be billed with the rate that was effective in January.

Request for Proposals (RFPs)

Staff recommends that "the supply bid process and the resulting supply contracts must contain sufficient terms and conditions to assure firm supply." (Staff Memorandum, page 5 of 11.) The Company's RFPs and gas supply contracts clearly require firm supply. Beginning with the 2011-2012 RFPs, Atmos has also included language in its RFPs specifying that the "asset manager's rights to storage and associated transportation are secondary to Atmos' rights" and "the asset manager selected is responsible for any penalties or incremental costs associated with non-compliance with any rule, regulation tariff provision of any Federal, State, or local governing entities including asset manager's election to deviate from the company provided planned flowing and storage gas injections and/or withdrawal requirements."

Staff further recommends that RFPs should provide a "detailed explanation of penalties and consequences of failure to perform." (Staff Memorandum, page 5 of 11.) Atmos disagrees. Penalties and consequences are a matter of contract and cannot properly be addressed in the RFP, which is a document describing the supply requirements of the LDC. If penalties were separately listed in the RFP which were inconsistent with the industry standard base NAESB provisions, Atmos could further limit the pool of interested bidders.

Staff states that "when an LDC deals with its affiliate, the LDC must have clear assurances that its affiliate provides the same high level of service as is expected from non-affiliates. (Staff Memorandum, page 5 of 11.) The Company's affiliate is and always has been held to the same standards as non-affiliate suppliers. Further, there is no evidence that the affiliate's service has been anything less than reliable. Atmos' affiliate has consistently provided reliable service over the many years supplying Atmos.

Staff goes on to opine that the "LDC must take appropriate action in the event of an affiliate's non-performance, including seeking of penalties that would hold captive ratepayers harmless." Affiliate non-performance has never been an issue for Atmos. It is the Company's position, however, that any penalties for non-performance are more properly placed in the contract rather than the RFP. This is true for any supplier. It should be noted that there is nothing in the RFP that limits the ability of the LDC to seek contract damages against any breaching supplier, affiliated or non-affiliated.

Staff states that this is of heightened concern because of the "potential for supply cuts to firm service" such as those experienced during the 2007-2008 ACA period. (Staff Memorandum, page 5 of 11.) The referenced supply cuts were made as the result of a force majeure pipeline event and had nothing to do with supplier reliability. The Company's supply plan worked as intended, gas was withdrawn from storage, and no customers were impacted. Atmos has explained this situation to Staff on more than one occasion, during the Meeting and in a Data Request.[2] To mention this as a reason for concern about the RFP process is not only inaccurate and misleading, but also demonstrates a lack of fundamental understanding of gas supply.

Finally, Staff requests that Company provide the current status of all Company actions regarding Staff's past RFP recommendations for the 2006-2007 and 2007-2008 ACA cases. Atmos found no any recommendations regarding the RFP process in Staff's memorandum in the 2007-2008 case. The status of the recommendations made pursuant to the 2006-2007 case are as follows:

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[2] GR-2008-0364 DR 132.2

- Starting with the 2009-2010 Hannibal RFP, Atmos added the statement "Field Zone bids in lieu of Haven bids will not be accepted and considered non-conforming" in response to Staff's recommendation that the Company clarify language regarding the Market receipt point and the treatment of Field transport charges to the receipt point.
- In response to Staff's recommendation to clarify all future gas supply RFP language to indicate whether Atmos is using a flat charge for fuel and L&U or whether the bidder is to include the cost of fuel and L&U in its bid. As part of our RFP bid analysis, if there is any uncertainty over fuel or other variable prices, Atmos clarifies with the bidders and the appropriate pricing is included in the RFP analysis. Atmos will add language to the RFPs asking bidders to specify whether fuel is to be added or is included in their bid price.
- Starting with the 2008-2009 RFPs, language was included under the Asset Management section to clarify language regarding the gains from capacity releases and storage arbitrage, reliability standards, and real and virtual storage.

Affiliated Transactions

Atmos has serious disagreements with Staff over the Affiliated Transaction Adjustments proposed in this case related to the Asset Management Agreements and gas supply contracts with AEM. For the reasons explained herein, the Staff should reconsider its proposed Affiliated Transactions Adjustments in this proceeding. Staff's recommendation reads "If AEM is allowed to cut supplies, its service is not comparable to other bidders." (Staff Memorandum, page 6 of 11.) To be clear, Atmos does not allow any supplier, affiliate or otherwise, to cut supplies. In a Force Majeure event, it is the pipeline, not suppliers, that restricts firm capacity which can result in cuts

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to supply. Staff states that Company's incentive compensation can reward LDC employees for the financial success of the affiliate, but does not present any supporting information showing that any contracts have been improperly awarded to the affiliate. Staff claims that Company's "continued use of a secondary receipt point in this period, coupled with AEM's lack of providing certain supplies in the 2007-2008 period" are cause for concern. (Staff Memorandum, page 6 of 11.) Neither of these claims provides a legitimate basis for a disallowance. AEM has never failed to provide adequate supply. The Company has explained to Staff that the PEPL supplies were cut by the pipeline as the result of a pipeline force majeure event. If anything, the force majeure served as a demonstration of the reliability of Atmos and its gas supply plan, since no customers were impacted. The Company's use of secondary receipt points on PEPL was considered "firm and in-path" by pipeline and resulted in lower fuel costs since the receipt points were further downstream and closer to Company's delivery points.

STAFF'S PROPOSED AFFILIATED TRANSACTIONS ADJUSTMENTS

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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.

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The Missouri Court of Appeals reviewed a similar situation involving the issue of whether an unregulated affiliate of an electric company was required to sell its services to a regulated affiliate company at its cost without incurring a profit. The Court held that such a requirement to sell to the affiliated regulated company at cost "would have resulted in the [the unregulated affiliated company] board's violating its fiduciary duty . . . to manage the corporate business solely in accord with the corporation's interest." *State ex rel. Public Counsel v. Public Service Commission*, WD 69259 (consolidated with WD 69270 and WD 69297)(Slip Opinion, p. 18)(Filed on January 13, 2009).

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Cash-Out Provisions

Atmos agrees with the scheduling fee adjustments proposed by Staff for the respective pipelines.

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SECTION 2: SOUTHEAST AREA

Atmos agrees with Staff's findings and has recorded adjusting entries accordingly.

SECTION 3: WEST AREA

Atmos agrees with Staff's findings and has recorded adjusting entries accordingly.

SECTION 4: KIRKSVILLE AREA

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Sections 1-4

Staff's recommendations listed below are acceptable to the Company, with the exception of the highlighted items.

"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 Recommended" column of the following table:

TABLE 1 (SECTIONS 1-4)

ALL AREAS	**Filed Balances for 2008-2009 (Ending 8-31-09)**	**Staff Adjustments**	**Staff Recommended Ending Balances for 2008-2009**
Southeast Area: Demand ACA	($634,905) (1)	$0	($634,905)
Commodity ACA	($3,762,136) (2)	$1,387 (A) $8,53 1(B)	($3,752,218)
Kirksville Area: Demand ACA	$22,071	$0	$22,071
Commodity ACA	($896,044)	$0 (A) $1,570(B)	($894,474)
West Area: Demand ACA	$44,403 (3)	$0	$44,403
Commodity ACA	($718,360) (4)	($13,964) (A) ($81,852) (C)	($814,176)
Northeast Area: Demand ACA	$33,803	$0	$33,803
Commodity ACA	($2,549,115)	($349,015) (A) $2,725 (B) ($9,464) (B) ($413,165) (C)	($3,318,034)

Notes to Staff Adjustments:

1) Combined Semo and Neelyville Demand ACA balances - ($644,221) + $9,316
2) Combined Semo and Neelyville Commodity ACA balances - ($3,681,082) + ($81,054)
3) Combined Butler and Rich-Hill/Hume Demand ACA balances - $60,266 + ($16,791) +$928
4) Combined Butler and Rich-Hill/Hume Commodity ACA balances - ($760,682) + $48,371 + ($6,049)

A) ACA beginning balances August 31, 2008 adjusted to prior year ending balances (Exhibit A)
B) Cash-out - Scheduling Fee & General Mills
C) Affiliated transaction

2. File a written response to the recommendations included herein within 30 days." (Staff Memorandum, page 10 of 11.)

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SUMMARY

In summary, the Company agrees with most of the adjustments proposed by Staff, with the exception of the Affiliated Transactions Adjustments. The Company, however, strongly disagrees with the Affiliated Transaction Adjustments, as explained more fully herein.

WHEREFORE, the Company respectfully recommends that the Commission schedule a Prehearing Conference for the parties to discuss their differences on the Affiliated Transactions issues discussed herein and propose a procedural schedule for resolving this case.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I do hereby certify that a true and correct copy of this document has been hand-delivered, emailed or mailed, First Class, postage prepaid, this 2nd day of February, 2011, to:

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/s/ James M. Fischer

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