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**

POST-HEARING BRIEF OF
ATMOS ENERGY CORPORATION

James M. Fischer, MBN 27543
Larry W. Dority, MBN 25617
Fischer & Dority, P.C.
101 Madison Street, Suite 400
Jefferson City, MO 65101
Telephone: (573) 636-6758
Facsimile: (573) 636-0383
Email: jfischerpc@aol.com
Email: lwdority@sprintmail.com

Douglas C. Walther, MBN 32266
Associate General Counsel
Atmos Energy Corporation
P.O. Box 650205
Dallas, Texas 75265-0205
Telephone: (972) 855-3102
Email: doug.walther@atmosenergy.com

Attorneys for Atmos Energy Corporation

__________ Designates "Highly Confidential" Information.
All Such Information Should Be Treated Confidentially
Pursuant To 4 CSR 240-2.135.

NON-PROPRIETARY VERSION

Table of Contents

Table of Authorities

Cases

Statutes

Rules

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**

POST-HEARING BRIEF OF
<u>ATMOS ENERGY CORPORATION</u>

I. INTRODUCTION

A. Executive Summary

This case involves Atmos Energy Corporation's 2007-2008 ACA audit. The Company filed this case in October 16, 2008, nearly 2 ½ years ago. (Tr. 625) After a year-long audit involving substantial discovery, the Commission Staff ("Staff") filed its recommendation on December 28, 2009, wherein the Staff proposed two disallowances related to Atmos' gas purchasing practices. (Tr. 624-625) Atmos filed its response to Staff's recommendation on January 28, 2010, disagreeing with the Staff's affiliated transaction adjustments and requesting that the Commission schedule a hearing to address this matter. Even Staff's primary witness is not aware of any case in which the Commission has accepted a similar affiliated transaction adjustment as the adjustment that Staff is recommending in this case (Tr. 660), and the Company has been diligent in its continued efforts to present this matter to the Commission for resolution. Regrettably, as fully discussed, *infra*, the Staff position (and an accompanying purported need for additional discovery) has continued to morph over an extended course of time, finally resulting in an eleventh hour additional prudence adjustment that was first contained in

Staff's surrebuttal testimony. As noted during the evidentiary hearing in this case, Atmos is pleased to have the opportunity to finally address and resolve the issues that have been raised by Staff in this proceeding and, as explained below, the Commission should reject the proposed disallowances of Staff related to the purchase of gas by Atmos during the 2007-2008 ACA period.

This case presents the following issues for resolution by the Commission:

1. **Were Atmos Energy Corporation's purchasing practices prudent during this ACA period?**
2. **Whether the Affiliated Transaction Rule requires that a regulated LDC like Atmos lower its gas supply costs in the PGA/ACA process by the same amount as the gross profits of an affiliated gas marketer that provided gas supplies after a formal competitive bidding process?**
3. **Whether Atmos provided a "financial advantage" to its affiliate?**
4. **Whether the Commission should prohibit affiliated transactions between Atmos and its affiliated gas marketer?**
5. **Whether the Commission should make a $308,000 disallowance of gas costs because Atmos asserted its right to object to discovery related to its unregulated affiliate?**
6. **Whether Atmos was imprudent by failing to nominate the maximum amount possible under its contract with AEM during a December 2007 Force Majeure period during the rupture of the natural gas pipeline owned and operated by Panhandle Eastern Pipeline Company?**

For the reasons stated herein, the Commission should find and conclude:

1. **Atmos Energy Corporation's purchasing practices were prudent during this ACA period.**
2. **The Affiliated Transaction Rule does not require that a regulated LDC like Atmos lower its gas supply costs in the PGA/ACA process by the same amount as the gross profits of an affiliated gas marketer that provided gas supplies after a formal competitive bidding process.**
3. **Atmos did not provide a "financial advantage" to its affiliate since it paid AEM less than the fair market price, as established by a competitive bidding process, for its gas supplies.**
4. **The Commission should not prohibit affiliated transactions between Atmos and its affiliated gas marketer in this ACA proceeding.**
5. **The Commission should not adopt the Staff's proposed $308,000 disallowance of gas costs because Atmos asserted its legal right to object to discovery related to its unregulated affiliate.**
6. **Atmos was not imprudent by failing to nominate the maximum amount possible under its contract with AEM during a December 2007 Force Majeure period during the rupture of the natural gas pipeline owned and operated by Panhandle Eastern Pipeline Company.**

B. The Facts of the Case Are Largely Not in Dispute

Atmos used a formal competitive bidding process to solicit bids from numerous unregulated gas marketers for the Company's gas supplies in all of its various service areas in Missouri. This formal, competitive bidding process is fully described in the Direct Testimony of Rebecca Buchanan in this proceeding. (Ex No. 1, Buchanan Direct, pp. 6-14)(Tr. 444) After a careful evaluation of the various bids received throughout its service area, Atmos awarded eight (8) gas supply contracts to six (6) different gas marketers for its Missouri service areas. (*Id*.)

Two out of eight of its gas supply contracts were awarded to Atmos Energy Marketing ("AEM"), an affiliated gas marketer, which submitted the lowest and best bid for those gas supplies for the Hannibal and Butler areas of the Company during the 2007-2008 ACA period. (Ex No. 1, Buchanan Direct, pp. 11-12)

AEM did not win the bid for the other areas of the state which make up about 66% percent of Atmos' load in Missouri. In these areas, the winning bids went to other unregulated gas marketers who submitted lower bids than AEM. AEM has not been a dominant gas supplier for Atmos in Missouri. For the period April 2004 through November 2009, Atmos issued forty-eight (48) Missouri RFPs. Of these 48 RFPs, AEM participated in twenty-four (24) RFPs, and AEM was the winning bidder in only 6. Other suppliers who have won multiple times include: BP Energy Company —8 wins; Tenaska--7 wins; Anadarko—7 wins; Centerpoint--5 wins; Conoco Phillips—5 wins, Shell—2 wins, and OGE—2 wins. (*Id*. at 12.)

In this case, Staff is not proposing any disallowances related to the gas marketers that submitted the lowest and best bid in the Kirksville, Piedmont/Arcadia, Jackson and other Southeast service areas. In other words, Staff is not proposing to disallow any costs associated with AEM's competitors—ConocoPhillips, Centerpoint, BP Energy Company, Anadarko, or Tenaska Marketing.

Staff apparently recognizes that Atmos' competitive bidding process produced contracts in these regions that were prudent and reasonable. In these areas, these contracts represented the lowest and best price that was available to Atmos and its customers.

Even though Atmos used the same competitive bidding process for the Hannibal and Butler areas, Staff proposed disallowances in the Staff Recommendation related to the gas supply contracts with AEM, Atmos' unregulated gas marketing affiliate. During the hearings, however, <u>Staff confirmed that it is not asserting that Atmos was imprudent in accepting the lowest and best bid, even though it was from its affiliate</u>. (Tr. 624)

Staff agrees that Atmos is contractually obligated to pay the full amount included in the AEM contracts that were accepted after the formal, competitive bidding process. (Tr. 692) Staff also agrees that the AEM bids were the lowest and best bids available to Atmos and its customers in these areas. (Tr. 645)

The record reflects that Staff has now abandoned its original position (Tr. 640), and totally eliminated its proposed disallowance related to Butler. (*Id.*)   It has also reduced its proposed disallowance related to the Hannibal area. (Ex No. 28NP, Sommerer Surrebuttal, pp. 18)(Tr. 640)

For the Hannibal area, Staff in this case is proposing to lower the gas costs that are passed through to consumers by the same amount as the gross profits of AEM on these contracts. (Tr. 640-42) In other words, Staff is proposing to disallow from Atmos' gas costs an amount equal to the gross profits earned by AEM on these contracts. Staff's disallowance does not take into account that AEM has administrative overheads—salaries, office costs, and numerous other overheads-- that AEM must recover before it makes any net profit on these transactions. (*Id.*) Staff recognizes that their proposed adjustment does not include the personnel costs, and other administrative overheads of AEM. Yet, Staff totally ignores these additional overhead costs in its adjustment. (Tr. 636-37)

In the Hannibal area, if the supply contract had not been awarded to the lowest cost bidder, which happened to be the affiliate, but instead had been awarded to the second place bidder, the annual costs for the Hannibal area customers would have increased by $140,000—looking at the two RFP processes used during this ACA period. The record indicates that Staff would have had a concern if the Company had accepted a higher bid from an unaffiliated gas marketer and Staff would have wanted to look at that transaction "in great detail." (Tr. 645)

Because Atmos tried to save its customers an additional $140,000 by accepting the lowest and best bids, it is now facing a disallowance proposed by Staff of $308,000 and an expensive "forensic audit." (See Ex. 34HC for an estimate of the cost of litigation of this case). The Commission should ask itself the following questions: Is this the type of perverse incentive that the Commission wants to build into the PGA/ACA process? On its face, does this make good public policy sense?

The only difference between the circumstances in the Hannibal service area and in the rest of the Company's service areas is that AEM happens to be an affiliate of Atmos

Energy Corporation, and AEM won the competitive bidding process in the Hannibal and Butler service areas.

It is important to emphasize that AEM is an unregulated gas supplier in competition with numerous other unregulated gas suppliers seeking to win the business of Atmos Energy Corporation in Missouri. AEM is not an agent of Atmos Energy Corporation seeking to obtain gas supplies for Atmos.

The facts associated with the new prudence adjustment included for the first time in Staff's surrebuttal testimony related to a December 2007 Force Majeure Event[1] on the Panhandle Eastern Pipeline will be addressed in Section VI below.

II. THE PRUDENCE STANDARD

A. The Prudence Standard.

The Commission recently reviewed and reaffirmed the prudence standard used in Missouri in its *Report & Order* in Re Kansas City Power & Light Company, Case No. ER-2010-0355 (April 12, 2011) at 74-77. As explained by the Commission in the *Kansas City Power & Light Company* decision, the prudence standard is articulated in the *Associated Natural Gas Case* (which was an PGA/ACA case) as follows:

---

[1] According to the Section 11.2 of the standard NAESB Contract used in the natural gas industry, a *Force Majeure Event* is defined as follows (Ex No. 9):
11.2.Force Majeure shall include, but not be limited to, the following: (i) physical events such as acts of God, landslides, lightning, earthquakes, fires, storms or storm warnings, such as hurricanes, which result in evacuation of the affected area, floods, washouts, explosions, breakage or accident or necessity of repairs to machinery or equipment or tines of pipe; (ii) weather related events affecting an entire geographic region, such as low temperatures which cause *freezing* or failure of wells or lines of pipe; (iii) interruption and/or curtailment of Firm transportation and/or storage by Transporters; (iv) acts of Others such as strikes, lockouts or other industrial disturbances, riots, sabotage, insurrections or wars; and (v) governmental actions such as necessity for compliance with any court order, law, statute, ordinance, regulation, or policy having the effect of law promulgated by a governmental authority having jurisdiction. Seller and Buyer shall make reasonable efforts to avoid the adverse impacts of a Force Majeure and to resolve the event or occurrence once it has occurred in order to resume performance. (*emphasis added*.)

> [A] utility's costs are presumed to be prudently incurred.... However, the presumption does not survive "a showing of inefficiency or improvidence."
>
> ...[W]here some other participant in the proceeding creates a serious doubt as to the prudence of an expenditure, then the applicant has the burden of dispelling these doubts and proving the questioned expenditure to have been prudent. (Citations omitted).
>
> In the [Union Electric] case, the PSC noted that this test of prudence should not be based upon hindsight, but upon a reasonableness standard:
>
> [T]he company's conduct should be judged by asking whether the conduct was reasonable at the time, under all the circumstances, considering that the company had to solve its problem prospectively rather than in reliance on hindsight. In effect, our responsibility is to determine how reasonable people would have performed the tasks that confronted the company.

See State ex rel. Associated Natural Gas v. Public Serv. Comm'n, 954 S.W.2d 520, 528-529 (Mo. App. W.D. 1997).

Furthermore, in order for the Commission to disallow a utility's recovery of costs from its ratepayers, the Commission must apply the following two pronged test: (1) evaluate whether the utility acted imprudently (that is, did not act reasonably at the time under the applicable circumstances); and 2) evaluate whether such imprudence was the ***cause*** of the harm (increased costs) to the utility's ratepayers. *See Associated Natural Gas*, 945 S.W.2d at 529.

B. Burden of Proof

As stated above, under the prudence standard, the Commission presumes that the utility's costs were prudently incurred. *See State ex rel. Associated Natural Gas v. Public Serv. Comm'n,* 954 S.W.2d 520 (Mo. App. W.D. 1997); *State ex rel. GS Technologies Operating Co. Inc. v. Public Serv. Comm'n,* 116 S.W.3d 680 (Mo. App. W.D. 2003) (citations omitted). The legal presumption of prudence also applies to affiliated transactions. *State ex rel. Public Counsel v. Public Service Commission*, 274 S.W.3d

569, 577 (Mo.App. 2009). This means that utilities seeking a rate increase or change in their PGA rates are not required to demonstrate in their cases-in-chief that all expenditures were prudent. *See Union Electric*, 66 P.U.R.4th at 212.

Staff or any other party can challenge the presumption of prudence by creating "a serious doubt" as to the prudence of an expenditure. Once a serious doubt has been raised, then the burden shifts to the public utility to "dispel those doubts" and prove that the questioned expenditure was prudent.

Missouri case law has described the showing necessary to create a serious doubt sufficient to shift the burden back to the utility. In the *Associated Natural Gas* case, the Missouri Court of Appeals held that the Staff must provide evidence that the utility's actions caused higher costs than if prudent decisions had been made. *See Associated Natural Gas*, 945 S.W.2d at 529. Substantive and competent evidence regarding higher costs includes evidence about the particular controversial expenditures and evidence as to the "amount that the expenditures would have been if the [utility] had acted in a prudent manner." *See id.* In other words, Staff or the other parties must satisfy the following two-pronged evidentiary test to support a disallowance: 1) identify the imprudent action based upon industry standards and the circumstances at the time the decision or action was made; and 2) provide proof of the increased costs caused by Atmos' imprudent decisions. To meet this standard, a party must provide substantive, competent evidence establishing a causal connection or "nexus" between the alleged imprudent action and the costs incurred.

III. STAFF'S CHANGING AND EVOLVING POSITIONS

On December 28, 2009, the 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. As a part of the Staff Recommendation, the Staff proposed an affiliated transaction adjustment of ($349,015) for the Hannibal area and an adjustment of ($13,964) for the Butler area related to Atmos' acceptance of the low bids of its affiliate AEM for the Hannibal and Butler service areas. (Staff Recommendation, Appendix A-1, page 5 of 12).

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.

In this case, the Staff has <u>not</u> challenged the prudence of: (1) the Atmos Request For Proposal (RFP) process itself; (2) Atmos' acceptance of the lowest and best bids from unaffiliated gas marketers throughout its service areas in Missouri. (Tr. 624); or (3) Atmos' acceptance of the lowest and best bid from an affiliate, AEM, for the Hannibal and Butler services areas (Tr. 624).

On page 4 of his Direct Testimony, Staff witness Sommerer stated: "The issues in this case have been resolved with the exception of Atmos' transactions with its affiliate marketing company." (Ex. No. 26, Sommerer Direct, p. 4; Tr. 623) <u>He confirmed during the hearings that there are not any issues for the Commission to resolve regarding any of the hedging practices or reliability issues related to Atmos Energy Corporation</u>. (Tr. 624)

However, by the end of the hearings in this case, Staff's position was morphing again into the assertion (coupled with new, unsupported disallowances) that there were "big reliability issues and that northeast Missouri was not getting the gas that the company nominated" (Tr. 608), even though Mr. Sommerer testified at the conclusion of the hearings that there were no reliability issues that needed to be addressed:

Q. I understand that Staff also reviews hedging practices and reliability analysis as a part of the ACA review; is that correct?

A. Yes.

Q. On -- on Page 4 of your direct testimony, you state that, The issues in this case have been resolved with the exception of Staff's proposed disallowance regarding Atmos' transactions with its affiliated – its affiliate marketing company; is that correct?

A. That's correct.

Q. In this case, there are no longer any issues for the Commission to resolve regarding any of the hedging practices or reliability issues related to Atmos Energy Corporation; is that correct?

A. That's my understanding, yes.

Q. And that's notwithstanding all of the testimony we heard in the last day regarding reliability issues; is that right?

A. That's correct. (Tr. 623-24)

Atmos agrees with Mr. Sommerer that there are no reliability issues that need to be addressed in this case. Staff initially seemed to challenge the legality of including in its gas costs a bid from AEM that presumably included a gross profit. However, during the hearing, the Staff witness has recanted this position, clarifying that Staff is no longer suggesting that Atmos can not pass along profits from an unaffiliated or an affiliated gas marketer as a part of the PGA/ACA process. (Tr. 663). Instead, Staff's affiliated transaction adjustment is intended to reduce the gas costs to the "fair market price" or "fair market value." (Tr. 626)

In the Surrebuttal Testimony of David M. Sommerer, Staff abandoned its original affiliated transactions adjustments that were contained in the Staff Recommendation and its case-in-chief by reducing the proposed adjustment for the Hannibal area to $308,733, and totally eliminating the proposed affiliated transactions adjustment for Butler. (Ex No. 28HC, Sommerer Surrebuttal, p. 18 and Ex No. 33HC, Schedule 8(revised))

With regard to the revised $308,000 adjustment related to the Hannibal service area, Staff is also suggesting that the disallowance is appropriate because, from Staff's perspective, there were problems with the discovery process in this case (Tr. 673). Apparently, Staff wants the Commission to adopt the $308,000 affiliated transaction adjustment as a <u>sanction</u> for Atmos' allegedly abusive discovery practices in this case. As explained below, this position is unlawful, unreasonable, not based upon competent and substantial evidence, and would amount to an abuse of discretion if adopted by the Commission.

Finally, at the eleventh hour in surrebuttal testimony, Staff is now asserting that Atmos did not act prudently when it failed to nominate the maximum level of nominations possible under its contract with its affiliate, AEM, during December 2007 when a Force Majeure event had been declared as a result of the rupture of the Panhandle Eastern Pipeline Company pipeline. (Ex No. 28, Sommerer Surrebuttal, pp. 19-20.) As explained below, this disallowance is improper since it is being presented for the first time in surrebuttal testimony and should be stricken from the record, as Atmos requested at the evidentiary hearings. (Tr. 600-10)(*See also* 4 CSR 240-2.130(7)(D).[2] However, the Commission has decided to not to strike this portion of Staff's surrebuttal testimony.[3] While the Company believes this decision should be reconsidered in the final *Report and Order* in this case, Atmos will nevertheless address the merits (or lack thereof) of the Staff's proposed prudence disallowances below.

As explained herein, the Commission should reject the alternative proposed adjustments related to the December 2007 Force Majeure Event since the Staff has failed to raise a "serious doubt" regarding the prudence of Atmos' actions, and in fact, the competent and substantial evidence demonstrates that Atmos personnel (i.e. Mr. Mike Walker) acted prudently during this Force Majeure Event.

IV. AFFILIATED TRANSACTIONS RULES

Initially, Atmos believed that the Commission's Affiliated Transaction Rules, 4 CSR 240-40.015 and -40.016 were at the heart of the dispute with Staff in this case. However, as explained in the hearings, it now appears that the real dispute involves Staff's desire to conduct a "forensic audit"[4] of AEM (Tr. 266), and Staff's dissatisfaction with the answers that it received from AEM and Atmos to three data requests in this case.

[2] 4 CSR 240-2.130(7)(D) states: "Surrebuttal testimony shall be limited to material which is responsive to matters raised in another party's rebuttal testimony." Since the December 2007 Force Majeure Event was not discussed previously anywhere in the record, the portion of the Staff's surrebuttal testimony that proposes disallowances based upon this occurrence should be stricken. (Tr. 600-10)

[3] *Order Denying Atmos' Motion To Strike Testimony*, Case No. GR-2007-0364 (issued April 27, 2010).

[4] Staff counsel explained the "forensic audit" process as follows: "The audit actually looks less like a compliance audit and more like a forensic audit. The audit becomes much more extensive and much more detailed. And the audit must drill down into the transaction of the affiliate with its supplier. It is essentially peeling back the layers of the onion to understand the economics of the transaction that the company conducted essentially with itself. Now, why do we do this? It is Staff's job to scrutinize these transactions, because the affiliate transaction must be transparent." (Tr. 266)

(Tr. 266, 295) It appears that one of the primary reasons that Staff is now proposing the $308,000 disallowance is to teach Atmos and AEM a lesson that Staff is not to be challenged as it conducts its "forensic audit" of unregulated gas marketers' business practices in the future.

Notwithstanding the fact that the Staff has now primarily focused on its <u>need for discovery in ACA cases</u> in which an affiliate wins the competitive bidding process, rather than its original positions regarding the Affiliate Transaction Rules, Atmos will address below the legal issues surrounding the Affiliated Transaction Rules.

A. Atmos Followed the Affiliated Transaction Rule's Requirement To Utilize Competitive Bidding For Its Purchase Of Gas Supplies From Its Affiliate And Its Purchasing Practices Are Presumed To Be Prudent.

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. Both the Affiliated Transactions Rule and the Marketing Affiliate Transaction Rule have the following provision that mandates competitive bidding unless good cause is shown why competitive bidding is not appropriate:

> 4 CSR 240-40-40.15(3)(A) states in part:
>
> When a regulated gas corporation purchases information, assets, goods or services from an affiliated entity, the regulated gas corporation shall <u>either obtain competitive bids for such information, assets, goods or services</u> or demonstrate why competitive bids were neither necessary nor appropriate. (emphasis added)

Atmos followed the preferred competitive bidding process. (Tr. 444-45) Staff and Public Counsel have not challenged the legitimacy of the Atmos RFP process in this case, or raised any "serious doubt" regarding any other gas purchasing practices related to affiliate transactions. In fact, the competent and substantial evidence in the record shows that Atmos gave no preferential treatment to any bidder, 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 prices available in the open, competitive market. (Ex No. 1, Buchanan Direct, pp. 15-16)

It was prudent for the Company to utilize a competitive bidding process to obtain its gas supplies. Atmos has followed the Commission's mandated competitive bidding requirement throughout the ACA period. (Tr. 444-45) Perhaps more importantly, the Company believes that this is the best method for securing a reliable source of gas supplies at a reasonable price.

The Company's robust, 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. Atmos has been successful in obtaining sufficient gas supplies at market prices by using this competitive process that allows the Company to provide its customers with reliable natural gas at just and reasonable rates.

The competitive bidding process is well developed and described within the Manual attached to the Direct Testimony of Rebecca M. Buchanan. (Ex No. 1, Buchanan Direct, Attachment No. 1; Tr. 445) 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. In the case of the Hannibal area, the Company sent out RFP Letters to fifty-six (56) different gas marketers during the April 2008 through March 2009 Bid Process. (Ex No. 14HC, Buchanan Direct, RFP Evaluation, Appendix A)

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)

The following sections of this brief will discuss the details of the RFP evaluations during the ACA periods. However, it is undisputed in this case that Atmos followed the Commission's requirement to use competitive bidding when it obtained its gas supplies during this ACA period, and treated its affiliate AEM like any other unaffiliated gas marketer. By accepting the lowest and best bids, whether from an affiliate or an unaffiliated gas marketer, Atmos conducted itself in a prudent manner. Staff and Public Counsel have not challenged the prudence of accepting the lowest and best bid, even if it comes from an affiliate. (Tr. 624) Since no party has raised a "serious doubt" about its gas purchasing practices during this ACA period, there is nothing in the record to overcome the legal presumption of prudence. Based upon the competent and substantial evidence in the record in this proceeding, the Commission should find that Atmos Energy Corporation's gas purchasing practices were prudent during this ACA period.

B. The Affiliated Transaction Rule Does Not Require that a Regulated LDC like Atmos Lower Its Gas Supply Costs in the PGA/ACA process by the Same Amount as the Gross Profits of an Affiliated Gas Marketer that Provided Gas Supplies After A Formal Competitive Bidding Process.

In Staff's *Position Statement* filed on June 30, 2010, the Staff explained its position in this case as follows:

> It is Staff's position that the rates charged by Atmos in its Butler and Hannibal service areas were NOT just and reasonable because the rates did not merely pass on the cost of the gas but included a profit for Atmos' shareholders.
>
> Atmos acquired the gas in question from AEM, its wholly-owned, captive, unregulated-gas-marketing subsidiary. The profits realized by AEM on the gas sales were the profits of its owner, Atmos, and Atmos' shareholders. The PGA/ACA mechanism, which protects LDCs from the effects of natural gas price volatility by removing regulatory lag to the greatest extent possible by permitting rate changes outside of a general rate case, is legally permissible ONLY if the rate simply passes on to the ratepayers the cost at which the LDC obtained the commodity. Atmos' shareholders cannot be allowed to evade this central principle of the PGA/ACA mechanism by profiting on their own sales of gas to the LDC.

Even though the Staff did not identify the basis for its position in its Staff Recommendation, Staff's pre-filed testimony, or Staff's *Position Statement*, Atmos had presumed that Staff's position was based upon an incorrect interpretation of the Commission's Affiliated Transactions Rules since the Staff Recommendation and pre-filed testimony recommended an "affiliated transaction" adjustment for Hannibal and Butler that included removing the "profits" of AEM from the gas costs passed through the PGA mechanism. However, during the hearings, Staff witness David Sommerer recanted Staff's position that profits of an affiliated gas marketer can not be legally passed through the PGA/ACA mechanism:

Q. Now, as I understand your deposition testimony, as a layman, you don't think that the Commission's affiliated transaction rule necessarily requires that the profits of an affiliate be used to reduce the cost of gas of the – of the regulated utility; is that right?

A. Not by a direct reading of the rule in my layperson's understanding of the rule. (Tr. 632)

Mr. Sommerer is correct on this point. There is nothing in the Commission's Affiliate Transaction Rule, Missouri statutes or case law that prohibits gas costs passed through the PGA/ACA mechanism from including a profit for a gas marketer, whether an unaffiliated gas marketer[5] or an affiliated gas marketer. The Affiliated Transaction Rule itself does not even use the term "profit" anywhere in its provisions.

Commissioner Jarrett succinctly and accurately summarized the relevant questions to be addressed on this issue:

---

[5] Staff has not challenged the inclusion of profits from unaffiliated gas marketers in the gas costs that are passed through the PGA/ACA process for Atmos.

> The relevant question is not whether the non-regulated AEM paid fair market value for the gas it bought. The relevant question is whether the Atmos regulated LDC paid fair market value for the gas it bought from AEM. Staff already has the information to make that determination, as indicated in the position statement it filed in this case on June 30, 2010:
>
>> It is staff's position that the rates charged by Atmos in its Butler and Hannibal service areas were NOT just and reasonable because the rates did not merely pass on the cost of the gas but included profits for Atmos' shareholders.
>
> Position Statement at 1 (emphasis in the original). Further, Staff calculated the profit to be $362,979 in total and asked that that amount be disallowed. *Id*. at 2. By subtracting the profit from the total amount paid to AEM by Atmos' regulated LDC, Staff knows exactly <u>to the dollar</u> the actual price of the gas paid for by the LDC. Staff can easily compare this amount to other information to which it has access in order to determine whether the regulated LDC paid fair market price for the gas. The position of Staff completely ignores the affiliate rules by advocating that Atmos should purchase gas from AEM not at a fair market price, nor at Atmos' fully distributed cost, but at AEM's cost. The fact that AEM may have made a profit on the sale is irrelevant to <u>this</u> inquiry under the affiliate rules. Non-affiliate providers of gas to Atmos' regulated LDC make a profit on their sales, and Staff does not object to that. It is unrealistic for Staff to assert that an affiliate should not make a profit as well.
>
> Staff's real purpose, in my opinion, is to investigate whether there is an improper relationship between the non-regulated affiliate and the regulated entity, and they want the affiliate's records to prove this. To do so, Staff must pierce the "regulatory veil" between the two entities, because they are not authorized to investigate a non-regulated entity. Staff wants the discovery under the auspices of the affiliate rules, but under the limited scope of the affiliate rules, Staff cannot use them to pierce that veil. Since Staff's investigation is not authorized by any law or rule of this Commission, the discovery it seeks is irrelevant.[6]

As discussed below, the Affiliated Transaction Rules seem to prohibit an LDC from paying its affiliated gas marketer more than the "fair market price" for its gas supplies. *See* 4 CSR 240-40.015(2)(A)(1)[7]. However, there is no definition of "fair

[6] *Dissenting Opinion of Commissioner Terry M. Jarrett In The Order Granting Staff's Motion To Compel Atmos To Respond To Data Request* (filed December 22, 2010)

[7] 4 CSR 240-40.015(2)(A)(1) states: "A regulated gas corporation shall not provide a financial advantage to an affiliated entity. For the purposes of this rule, a regulated gas corporation shall be deemed to provide

market price" in the Affiliated Transactions Rules. There is nothing in the Affiliated Transaction Rules that suggests that a "fair market price" may not include a "profit" for the gas marketer.

In Staff's *Prehearing Brief* in Re Laclede Gas Company, Case Nos. GR-2005-0203 and GR-2006-0288, Staff defined "fair market price" as follows: "Fair market price" is the "price that a seller is willing to accept and a buyer is willing to pay on the open market and in an arm's length transaction." (*citing* Black's Law Dictionary 1549 (7th ed. 1999).(Tr. 627) Staff witness Sommerer also agreed with this definition of "fair market price" in the hearing. (*Id*.)

During the October 20, 2010 oral argument held in this proceeding, Commissioner Davis asked Staff counsel about a similar definition of "fair market value." Commissioner Davis quoted the following definition:

> "It provides the price that a seller is willing to accept and a buyer is willing to pay on the open market and at an arms length transaction; the point at which supply and demand intersect." (Tr. 113; 627-28)

Mr. Sommerer also agreed with this definition of "fair market value" and testified that he considered "fair market price" and "fair market value" to be synonymous in his mind. (Tr. 628)

During the hearings, it became apparent that now Staff is taking the position that in some situations (presumably when Staff doesn't receive "absolute cooperation" from the LDC and the affiliated gas marketer in the discovery process)(Tr. 663), then "fair market price" should be defined differently than explained to Commissioner Davis in the October oral argument. In some situations where the Staff does not have what it

---

a financial advantage to an affiliated entity if—1. It compensates an affiliated entity for goods or services above the lesser of—A. The fair market price; or B. The fully distributed cost to the regulated gas corporation to provide the goods or services for itself;"

considers to be "absolute cooperation" in the discovery process from an unregulated, affiliated gas marketer, then the "fair market price" is defined, according to Staff, as the cost of gas determined in a competitive bidding process <u>minus</u> the "gross profit" of the affiliated gas marketer. (Tr. 635-36; 611-12; 631-33)

Apparently, in this case, Staff did not believe that it would receive "absolute cooperation" from AEM in the discovery process so it recommended its original $363,000 affiliated transaction disallowance when it filed its Staff Recommendation on December 28, 2009, —<u>but Staff took this position before there had been a motion to compel filed or a single discovery dispute in the case</u>! (Tr. 674)

Mr. Sommerer explained the Staff's position as follows:

Q. Let's assume as a hypothetical that Atmos accepted one bid for gas supplies from AEM that included a profit. Would Staff propose an adjustment to remove the profit of AEM from the gas cost passed onto Atmos ratepayers as you've done in this case?

A. It depends upon the facts and circumstances of the case.

Q. Didn't you testify in the deposition, Not necessarily, not as a matter of course. I don't believe it's Staff's goal to identify profits and disallow them from affiliated marketer companies just because those affiliated profits may exist?

A. That's correct.

Q. Didn't you testify in your deposition that with the absolute cooperation from AEM and with contemporaneous records about their gas costs, Staff would not necessarily propose that AEM's profits be removed from Atmos' cost of gas in the PGA process?

A. That's correct.

Q. Assuming that the Staff received the information you wanted from AEM, and I believe you're saying absolute cooperation, if AEM has a profit, is Staff going to take the position that that profit ought to be removed from the PGA process before passing it along to customers?

A. Not as a matter of course, no. (Tr. 662-63)

* * *

Q. Now from your perspective as the head of the procurement analysis staff and not as a lawyer, you've not concluded that the affiliated transaction rule itself would always require that AEM's profits be removed from the gas cost of Atmos. Right?

A. That's correct.

Q. It all depends on whether Atmos is paying more than the fair market price to an affiliate, AEM. Right?

A. That is a primary focus of Staff's adjustment.

Q. And from your perspective, the way to determine whether AEM is paying above the fair market price requires that Staff have access to the books and records of AEM and the details and the types of upstream contracts that AEM has with its upstream contracts that AEM has with its upstream providers, that what you need. Right?

A. That's correct. (Tr. 664-65)(*See also* Tr. 740)

On this fundamental point, Atmos must respectfully disagree with the Staff and Mr. Sommerer. It is unnecessary for Staff to have access to all of the books and records of the affiliated gas marketer—and "absolute cooperation"—to determine the fair market price for gas supplies—whether from an affiliate or an unaffiliated gas marketer. <u>It is the market—not the Staff analyst—that determines the fair market price.</u> "Fair market price" is the price point where the willing buyer and the willing seller agree on a price in an arms-length transaction. As Commissioner Davis noted, it is "the point at which supply and demand intersect." (Tr. 113; 627-28)

This price point is determined by a robust, competitive bidding process used by Atmos—without the need to look at all of the details and communications related to upstream transportation contracts and upstream gas supply arrangements, the business practices of AEM, AEM's awarded gas supply contracts, AEM's own bidding process, AEM's profit and loss calculations, and other matters related to AEM's internal policies, as Staff continues to seek in these ACA cases. (*See* Staff's *Notice of Record Deposition*, <u>Re Atmos Energy Corporation's 2008-2009 PGA/ACA</u>, Case No. GR-2009-0417)(filed April 13, 2011).

Staff seems to recognize that the "fair market price" can be determined without the need for a "forensic audit" when Atmos purchases gas through its competitive bidding process from unaffiliated gas marketers:

Q. How would Staff determine whether Atmos is paying more than the fair market price to unaffiliated gas marketers?

A. You could look at a bidding process, you could look at comparable contracts, you could look at published information with regard to price indices, you could ask about Atmos' process of establishing fair market value. All of those things would be asked in terms of an unaffiliated transaction.

Q. You would inquire into the bidding process. Right?

A. Precisely. (Tr. 667-68)

Since Staff appears to have abandoned its original position that it was somehow legally impermissible for an affiliated gas marketer to include a profit in its gas costs charged to the LDC, Atmos will reserve its remaining arguments until it better understands Staff and Public Counsel's position on this issue.

However, it should be noted that even if there was some requirement to remove the "profits" of an affiliated gas marketer in the PGA/ACA process (which there is not), then the Staff's proposed affiliated transaction adjustment is flawed since it relies upon the removal of the "gross profits" of AEM, totally ignoring the personnel costs and other overheads of AEM that are required to provide the gas supplies to Atmos. (Tr. 636-41) As Mr. Sommerer candidly admitted, gas marketers don't always make money on these transactions. (Tr. 641-42) This is clearly demonstrated by the fact that AEM did not make a profit on its gas sales to the Butler area (Tr. 641), and Staff has now abandoned its proposed affiliated transaction adjustment for the Butler area. (Tr. 638) Even Mr. Sommerer agreed that if the Commission wanted to reflect AEM's personnel costs and overheads in its calculation of the AEM "profits," the Commission would have to lower Staff's $308,000 adjustment to reflect those personnel costs and overheads. (Tr. 642-43).

However, Staff did not seek the personnel costs and administrative overheads necessary to determine the "net profits" of AEM. (Tr. 643)

In summary, the Commission should reject the position of the Staff and Public Counsel that the Affiliated Transaction Rule requires that a regulated LDC like Atmos lower its gas supply costs in the PGA/ACA process by the same amount as the gross profits of an affiliated gas marketer that provided gas supplies after a formal competitive bidding process. There is no basis for this position in the law or in the facts of this case.

C. Atmos Did Not Provide a "Financial Advantage" to Its Affiliate Since It Paid AEM Less Than the Fair Market Price, As Established by a Competitive Bidding Process, For Its Gas Supplies.

One of Staff's arguments is that Atmos provided AEM with a "financial advantage". (Ex No. 26, Sommerer Direct, pp. 6-7) Mr. Sommerer explained the issue as follows:

> In its review of transactions between Atmos, the LDC, and its unregulated affiliate AEM, Staff must consider whether such transactions provided a financial advantage to the affiliated entity, to the detriment of customers of Atmos the LDC. While the Commission's Affiliate Transaction Rule, 4 CSR 240-40.015, Section (2)(A), is not the only basis for determining prudency of transactions, the Commission's rule states that a regulated gas corporation shall <u>not</u> provide a financial advantage to an affiliated entity. It further defines how such transactions are to be priced to prevent giving a financial advantage to an affiliate. This pricing requires the regulated entity to compensate the affiliate for goods or services at the <u>lesser</u> of the fair market price or the fully distributed cost to the regulated gas corporation to provide the goods or services for itself. When the Staff considers Atmos' (the LDC) fair market value for a particular portfolio of supply, it is reasonable and necessary for Staff to question why the LDC's fair market value would be any different than AEM's fair market value.

Again, Staff is incorrect that Atmos provided <u>any</u> advantage, financial or otherwise, to AEM. According to the criteria established in the Commission's Affiliated

Transactions Rule, it is very clear that Atmos did not provide its affiliated gas marketer any "financial advantage," as defined by the Affiliated Transaction Rule.

4 CSR 240-40.015(2)(A) states: "A regulated gas corporation shall not provide a financial advantage to an affiliated entity. For the purposes of this rule, a regulated gas corporation shall be deemed to provide a financial advantage to an affiliate if—

1. It compensates an affiliate for goods or services <u>above</u> the lesser of—
   A. The fair market price; or
   B. The fully distributed cost to provide the goods and services for itself;" (*emphasis added*)

In this case, Staff has stated that it is focusing on the "fair market price" for the gas that AEM has sold Atmos. (Tr. 698-99) Staff has not suggested that the fully distributed cost to Atmos was lower than the fair market price. (Tr. 698; Ex No. 27, Sommerer Rebuttal, p. 11) In fact, the evidence shows that Atmos' Regional Gas Supply Department does not have the in-house expertise to perform the gas marketing services that AEM and other marketers provide to Atmos. (Ex No. 1, Buchanan Direct, pp. 20-21) While Atmos has a talented group of personnel, it does not have personnel experienced in obtaining gas supplies from producers of natural gas, trading on the physical and financial markets, or arranging for interstate and/or intrastate transportation services from upstream suppliers. (*Id.*) In order to perform the services that gas marketers provide, the Company would need to hire or train additional personnel at a substantial cost and develop processes already utilized by gas marketers for securing gas supplies and transportation services in the interstate market. (*Id.* at 21) According to Ms. Buchanan, "[i]t is unlikely that Atmos could perform such specialized services for the sole benefit of the Missouri jurisdiction at a lower cost than a marketer who performs these services routinely for a much broader customer base. A basic understanding of economies of scale makes this a reasonable conclusion." (*Id*.) Staff has not challenged this conclusion. (Tr. 698; Ex No. 27, Sommerer Rebuttal, p. 11)

According to Mr. Sommerer, Staff's focus is in this proceeding is: What is the fair market price of the gas that Atmos purchased from AEM? (Tr. 683) The Company has provided competent and substantial evidence of the fair market price that willing unaffiliated sellers were willing sell the gas supplies for during the ACA period.

Atmos has also presented competent and substantial evidence that it did not pay AEM <u>more</u> than the "fair market price" in order to demonstrate that it did not provide its affiliate with a "financial advantage" as defined by the Affiliated Transaction Rule.

The "fair market price" is established by a willing buyer and a willing seller agreeing to on a price for the good or service after an arms length negotiations process. In *Carter v. Matthey Laundry & Dry Cleaning Co*., 350 S.W.2d 786, 794 (Mo. 1961), the Missouri Supreme Court defined "fair market value" as: "The term 'fair market value means the price which property will bring when it is offered for sale by an owner who is willing but under no compulsion to sell and is bought by a buyer who is willing or desires to purchase but is not compelled to do so" citing *Metropolitan St. Ry. Co. v. Walsh, 197 Mo. 392, 94 S.W. 860, 861*.

In *St. Joseph Minerals Corp. v. State Tax Commission*, 854 S.W.2d 526 (Mo.App. 1993), the Court held that for purposes of determining tax assessment for real property, "Fair market value typically is defined as the price which the property would bring when offered for sale by a willing seller who is not obligated to sell, and purchased by a willing buyer who is not compelled to buy." *See also State ex rel. State Highway Commission of Missouri v. Pfizer, Inc.*, 659 S.W.2d 537, 540 (Mo.App.1983).

For the Hannibal service area, there were two competitive RFP processes that overlapped during this ACA period. AEM had the lowest bid in each of the RFP processes. In the first RFP process for the period of April 1, 2007 to March 31, 2008, there were six <u>unaffiliated</u> bidders that established the fair market price for the gas. In the second RFP process for the period of April 1, 2008 to March 31, 2009, there were three <u>unaffiliated</u> bidders that established the fair market price for the gas. Staff witness Sommerer also recognized that a competitive bidding process among unaffiliated gas marketers can be used to establish the fair market price for gas supplies. (Tr. 674, 667-68, 670-71)

Mr. Sommerer also recognized that it would be a game-changer if he saw evidence that Atmos paid AEM less than the true fair market price for its gas supplies:

Q. Well, assuming that we could show you that we paid less than the fair market price—Atmos I'm saying—would you recommend to the Staff that they –they withdraw their affiliated transaction adjustment in this case?

A. I would want the opportunity to consult with my superiors and legal counsel before I made that – that determination. As I sit here today, if there was evidence that the Company had paid less than the true fair market value and the evidence was compelling, I would not disregard that recommendation. I would think about that discussion and possibly make it.

Q. So you would consider suggesting that that affiliated transaction adjustment be withdrawn?

A. That's correct. (Tr. 630)

The evidence that Atmos paid AEM less than the fair market price for its gas supplies is compelling, and should not be disregarded by Staff or the Commission. In the first RPF Process, there were six unaffiliated bidders that offered to provide gas to Atmos. (See Ex No. 24HC, Appendix A, p. 7) During the hearings, these six unaffiliated bids were discussed without identifying the names of the specific bidders to avoid public disclosure of the highly confidential information. The following were the bid amounts received during the first RFP process:

AEM Low Bid—$13,947,511

Unaffiliated Bidders:

Bidder 2—$14,049,424

Bidder 3—$14,064,796

Bidder 4—$14,244,297 Mean Bid Unaffiliated Bidders=$14,299,764

Bidder 5—$14,425,783

Bidder 6—$14,472,350

Bidder 7—$14,541,937

The bid prices among unaffiliated bidders ranged from $14.0 Million to $14.5 Million. These bids established the fair market price for the gas supplies, or the "price that a seller is willing to accept and a buyer is willing to pay on the open market and in an arm's length transaction." Based upon the bidding process among these unaffiliated companies, it is clear that the fair market price for the gas supplies was in the $14.0 to

$14.5 Million range at the time of the bidding process. However, AEM's bid was less than the fair market price established by these unaffiliated bids. In fact, the AEM bid was at least $102,000 less than the fair market price for the gas established by these unaffiliated bidders. Ultimately, Atmos actually paid less than the AEM bid since it did not need as much gas as assumed in the bid. (Tr. 654-55)

During cross-examination, Staff witness Sommerer candidly admitted that the fair market price for this period would be in the range of $14.0 million to $14.5 million (Tr. 685), and that the AEM bid of $13,947,297 was less than the fair market value. (Tr. 686):

Q. Now just looking at the bids for the unaffiliated marketers, the second through the seventh, the range is about $500,000 for those unaffiliated – or the spread, I guess is a better word, would be about $500,000 among the unaffiliated gas marketers?

A. That's correct.

Q. And based upon these unaffiliated gas marketer bids, would you agree that the fair market price for the gas during this period to Hannibal would be somewhere between 14 million and 14 and a half million dollars, that's the range?

A. Well, again, assuming what we've already discussed about volumes and estimated prices and then the prudence would still be applicable, that's— <u>that's the fair market value</u>.

Q. And I believe <u>you agree that the AEM bid was for $13,947,297, which was less than the fair market price established by these unaffiliated gas marketer bids</u>. Right?

A. <u>That's correct</u>. (*emphasis added*)(Tr.685-86)

In the second RFP process conducted later in the ACA period, there were similar results (See Ex No. 24HC, Appendix A, p. 3)(Tr. 647-51):

AEM Low Bid—$14,723,472

<u>Unaffiliated bids:</u>

Bidder 2—$14,761,471

Bidder 3—$14,958,757 Mean Bid of Unaffiliated Bidders=$14,929,984

Bidder 4—$15,069,726

In the second RFP bidding process, the bid prices among <u>unaffiliated</u> bidders ranged from $14.8 Million to $15.1 Million. (Tr. 653-54) These unaffiliated bidders established the "price that a seller is willing to accept and a buyer is willing to pay on the open market and in an arm's length transaction." Atmos believes that this competitive bidding process among these unaffiliated companies established that the fair market price for the gas was in the $14.8 Million to $15.1 Million range at the time of the bidding process. However, AEM's bid was <u>less</u> than the fair market price established by these unaffiliated bids. In fact, the AEM bid was at least $38,000 less than the fair market price for the gas established by these unaffiliated bidders.

During his deposition, Staff witness Sommerer candidly admitted that the fair market price for this period would be in the range of $14.7 million to $15.1 million (Tr. 653-54), and that the AEM bid was less than the fair market value. (Tr. 686):

Q. Let's look up at the top of the page . . . [page 46 of Sommerer Deposition] where I ask you, If you looked at those bids, <u>wouldn't you agree that the fair market price would be considered to be in that range of 14.7 to 15.1 on a million dollar basis</u>? And then you – would you read into the record your answer?

A. Again, using these numbers as establishing the fair market value under the assumption that the volumes ended up being what the hypothetical volumes were in the analysis, then <u>those dollars would represent fair market value</u>.

Q. Okay. <u>Now I believe you agreed that the AEM bid was less than that range; is that right</u>?

A. <u>That's correct</u>. (Tr. 653-54)(*emphasis added*)

Based upon the competent and substantial evidence in the record, the Commission should find that Atmos did not provide a "financial advantage" to its affiliate since it paid AEM less than the fair market price for its gas supplies. As a result, the Commission should reject Staff's proposed affiliated transactions adjustment of $308,000 for this ACA period.

D. The Commission Should Not Prohibit Affiliated Transactions Between Atmos and its Affiliated Gas Marketer in this ACA Proceeding.

In Staff's *Position Statement*, the Chief Staff Counsel has recommended that the Commission effectively repeal the Affiliated Transactions Rules by prohibiting LDCs from engaging in gas supply transactions with unregulated affiliates and subsidiaries:

> Staff further states that Atmos has waged an unrelenting campaign of discovery obstruction during the course of this case in order to prevent Staff from determining whether Atmos unlawfully provided financial and other advantages to AEM, wholly-owned, captive, unregulated-gas-marketing subsidiary, in any number of subtle ways. Further, Staff points out that Atmos' behavior in this regard is common among Missouri LDCs, with the result that Staff now urges the Commission to prohibit LDCs from engaging in gas supply transactions with unregulated affiliates and subsidiaries. (*emphasis added*)

While Atmos strongly denies that it "has waged an unrelenting campaign of discovery obstruction during the course of this case," Staff's recommendation must be rejected for a more fundamental reason. Staff's recommendation is simply unlawful. The Missouri Supreme Court in *Greenbriar Hills Country Club v. Department of Revenue*, 47 S.W.3d 346, 357 (Mo. Banc 2001) has held, as Commissioner Davis referenced in questioning in this proceeding (Tr. 262), that a repeal of a rule in a contested case constitutes an improper rulemaking by adjudication. In *Greenbriar*, the Court held:

> Agency rulemaking occurs with the formulation, or repeal, of a "statement of general applicability that implements, interprets or prescribes law or policy, or that describes the organization, procedure, or practice requirements of any agency." [FN33] Agencies cannot promulgate, or repeal, a rule by an adjudicated order.[FN34] To repeal a rule, an agency must comply with the notice, publication, and public comment method prescribed in section 536.021 of Missouri's Administrative Procedures Act. Pursuing a major change in Missouri's long-term tax regulations in a quasi-legislative forum inappropriately allowed the Director to bypass the more stringent and lengthy process of rulemaking as required under section 536.021. (*footnotes omitted*)

Since the Commission's Affiliated Transactions Rules, including the Gas Marketing Affiliated Transaction Rule, 4 CSR 240-40.016, specifically authorize and prescribe the rules regarding how LDCs may engage in gas supply transactions with unregulated affiliates and subsidiaries, the adoption of Staff's recommendation to prohibit such transactions in this adjudicatory proceeding would be unlawful under the Court's holding in *Greenbriar*.

Staff's own witness Mr. Sommerer did not agree with this Staff recommendation to prohibit such affiliated transactions. (Tr. 692-93). In fact, Mr. Sommerer testified that such a prohibition could harm the interests of consumers since affiliated gas marketers, as in this case, may be able to provide gas supplies at the lowest cost to consumers. (Tr. 681):

> Q. If the Commission prohibited affiliated transactions between LDCs and affiliated gas marketers, do you believe that it would necessarily benefit consumers?
>
> A. Not necessarily.
>
> Q. In some cases, affiliated gas marketers may be able to provide gas supplies at the lowest price to consumers. Right?
>
> A. That is a possibility.

Staff's overzealous desire to perform forensic audits on unregulated, affiliated gas marketers is not a sufficient reason for the Commission to violate the terms of the Administrative Procedures Act. *See Section 536.021*; and *Greenbriar.* Quite simply, this Staff Recommendation is just another indication of Staff's desire to delve into the books and records of affiliated gas marketers at virtually any cost, or alternatively, seek the "death penalty" for such transactions if "absolute cooperation" from unregulated entities is not forthcoming. The Commission should reject Staff's attempt to repeal this State's long-standing policy to allow, and even encourage, such transactions when they are in the best interests of consumers. Unfortunately, the Commission should also recognize that Staff's distaste for affiliated transactions has colored the issues in this entire case. At the end of his redirect testimony, Mr. Sommerer testified that even Staff now does not want the Commission to prohibit affiliate transactions (Tr. 741-42), notwithstanding the fact that Staff has never amended its Position Statement filed in this case. (Tr. 707)

E. The Commission Should Not Adopt the Staff's Proposed $308,000 Disallowance of Gas Costs as a Penalty or Sanction Because Atmos Asserted Its Legal Right to Object to Discovery Related to Its Unregulated Affiliate.

During the hearings, it became apparent that the primary reason that Staff is proposing the $308,000 affiliated transaction adjustment is its dissatisfaction with the discovery process in this case, and (more likely) in another LDC's case. (Tr. 676-77) In fact, Staff anticipated such discovery problems when it originally filed its Staff Recommendation on December 28, 2009, months before there had even been a single discovery issue raised in this case. (Tr. 676-77) However, an objective observer of the discovery process in this case would conclude that Atmos did not abuse the discovery process or otherwise exhibit behavior that would justify a $308,000 penalty—a penalty that is not authorized by statute or case law.

On December 28, 2009, Staff filed its Staff Recommendation with a $362,979 affiliated transaction adjustment for Hannibal ($349,015) and Butler ($13,964) <u>at the end</u>

of a year long ACA audit—but stated it needed to conduct further discovery of AEM. (Staff Recommendation, Appendix A-1, Memorandum, pp. 4-5):

> The Staff requested underlying supporting documentation for these transactions. AEM provided some, but not all of the requested information. Because further information regarding how AEM used upstream supplies to meet its obligations under these agreements was withheld, the Staff has based a disallowance of affiliated costs based upon the information that was made available. As this case proceeds the Staff may pursue additional AEM data.

On March 12, 2010, Staff filed its Staff direct case with $362,979 affiliated transaction adjustment—but stated it needed to conduct further discovery of AEM. (Ex No. 26NP, Sommerer Direct, p. 7)

On June 14, 2010, Staff filed its Rebuttal Testimony which continued to propose the original affiliated transaction adjustment—but "Staff was unable to make a fully informed recommendation" without more discovery. (Ex No. 27NP, Sommerer Rebuttal, p. 5)

On May 3, 2010, nearly five months after it completed its ACA audit and alleged that the Company was charging rates that were unjust and unreasonable, Staff issued DR No. 117 which requested more information about AEM's business practices.

On May 24, 2010, Atmos answered DR No.117, within the time prescribed by the Commission's rules. The Company also supplemented the response on June 3, 2010.

On June 11, 2010, Staff filed its *Motion To Suspend Procedural Schedule* on the ground that it could not file its rebuttal testimony without the additional discovery of AEM. *See Staff's Motion To Suspend Procedural Schedule* (filed on June 3, 2010). Of course, this was now more than 5 months after it originally alleged that Atmos' rates were "unjust and unreasonable" and made its original affiliated transactions adjustment to reduce Atmos' gas costs by the amount of the gross profit included in AEM's cost of gas supplies. Even though the Staff did not receive the requested information until later, the Staff filed its rebuttal testimony on June 14, 2010. Staff filed its *Motion And Waiver Request Concerning Discovery* on June 14, 2010 which, *inter alia*, sought an indefinite suspension of the procedural schedule and sanctions against Atmos for its failure to answer DR No. 117. (*See Motion And Waiver Request Concerning Discovery* (filed June 14, 2010)

On July 2, 2010, the Commission granted in part Staff's request and suspended procedural schedule until Atmos and AEM provided Staff with additional information related to the unregulated activities of AEM. The requested information was provided to Staff on July 29, 2010, as directed.

On August 27, 2010, Staff issued follow-up data requests asking Atmos for more details about the business practices of AEM. Atmos objected, and the Staff filed a *Motion To Compel Atmos' Response to Staff Data Requests 117.1 and 131.1* on September 14, 2010. The Commission granted this motion, and the Commission directed Atmos to answer these 2 Data Requests by November 22—which it did. The Commission also reestablished the procedural schedule in that order and <u>ordered that discovery end by December 23, 2010</u>. *See Order Granting Staff's Motion To Compel Atmos To Respond To Data Requests and Reestablishing Procedural Schedule*. (issued on November 10, 2010) Over two years had passed since the case was initiated, but Staff still claimed that it needed more discovery to support its case.

On December 23, 2010, Staff filed its Surrebuttal Testimony of David M. Sommerer which proposed for the first time two new, alternative disallowances related to a Force Majeure Event that resulted from a pipeline rupture on the Panhandle Eastern Pipeline system. In surrebuttal testimony, Staff is now proposing a new prudence adjustment of $52,572 or $85,775 related to Atmos' willingness work with its supplier when a pipeline rupture occurred, and there was a Force Majeure Event declared. (Ex No. 28NP, Sommerer Surrebuttal, pp. 19-20)

As a result of the pipeline rupture, Atmos' supplier AEM could not deliver the maximum amount that Atmos could have nominated under its contract. Atmos agreed to nominate a lesser amount than the maximum. Staff is apparently alleging that this action was imprudent. Atmos does not believe that there is a legal basis for Staff's proposed adjustment.

On February 10, 2011, Staff subpoenaed Becky Buchanan and Mike Walker for depositions and more discovery, notwithstanding the Commission's directive that discovery should end by December 23, 2010, more than one year after the Staff filed its Staff Recommendation alleging that Atmos' rates were "unjust and unreasonable". *See Request for Subpoenas Duces Tecum* (filed February 14, 2011) Apparently, Staff still needed "more discovery" to support its new prudence adjustment.

Atmos decided to cooperate with the Staff's new round of discovery with the hope that it could more quickly have the substantive issues presented to the Commission and finally resolved.

On February 28, 2010, the Staff conducted the discovery depositions of Becky Buchanan and Mike Walker. *See Notice of Deposition* (filed February 16, 2011) Atmos also conducted the deposition of Mr. David M. Sommerer the next day. *See Notice of Deposition* (filed February 22, 2011)

On March 2, 2011, Staff subpoenaed Mike Walker as a witness for the hearing (even though Mr. Walker had not pre-filed testimony in this case) and requested that he again produce documents which the Company had already provided to Staff in the extensive discovery process. *See Request For Subpoenas Duces Tecum* (filed March 3, 2011) On March 8, 2011, Atmos filed its *Motion For Protective Order Of Atmos Energy Corporation To Quash Hearing Subpoena*.

On March 16, 2011, the Commission issued its *Order Denying In Part and Granting In Part Atmos' Motion To Quash Subpoena* which directed that Mike Walker appear at the hearing, but granted Atmos' request that Mr. Walker not be required to bring documents that had already been provided to Staff.

Based upon this procedural history, Atmos does not believe that the record reflects that it has in any way abused the discovery process, or otherwise been uncooperative in providing Staff necessary and relevant information during its "forensic audit." Atmos objected to two or three data requests which it believed were inappropriate and irrelevant. (Tr. 693) When the Commission ruled in favor of the Staff, Atmos and AEM timely complied and provided the requested information.

Yet, from the beginning of this case, Staff anticipated a discovery battle and decided to propose an affiliated transaction adjustment and allege that Atmos' rates were "unjust and unreasonable" to force Atmos to defend its gas purchasing practices and allow Staff an additional year for discovery. (Tr. 676-78) Even after an additional year of discovery, Staff has been unable to present competent and substantial evidence that raised a "serious doubt" regarding the prudence of its gas purchasing practices during this ACA period.

From the Company's perspective, the Staff's proposed Affiliated Transaction adjustment is more about the opportunity to delve into the business practices of AEM, than it is about the prudence of Atmos accepting the lowest bid from an affiliate, or Atmos passing along through the PGA/ACA process the actual gas supply costs, including a profit, from its affiliate.

It would be totally inappropriate and an abuse of discretion for the Commission to adopt Staff's affiliated transactions adjustment as a sanction for Atmos and AEM raising objections to discovery requests which they believed were not relevant or appropriate in this proceeding. *See State ex rel. Arkansas Power & Light Company v. Public Service Commission*, 736 S.W.2d 457, 461 (Mo. App. 1987). The Commission should decline to adopt Staff's adjustment in this case as a punitive measure for Atmos raising two or three objections regarding Staff's fishing expedition into the business practices of AEM. Atmos and AEM complied with the Commission's discovery orders, and it would be an abuse of discretion for the Commission to adopt Staff's proposed $308,000 disallowance merely because the Company voiced an objection to the discovery to obtain a determination from the Commission whether the data requests were relevant and appropriate.

V. PERVERSE INCENTIVES AND PUBLIC POLICY

In this proceeding, Atmos tried to save its customers an additional $140,000 by accepting the lowest and best bids from its affiliate rather than paying the fair market price established by the competitive bidding process with unaffiliated gas marketers. As a result, Atmos is now facing a disallowance proposed by Staff of $308,000 that was initially based upon the theory that it was legally impermissible to pass through profits through the PGA/ACA mechanism, and now is premised upon the argument that Atmos should be sanctioned for its discovery behavior. In addition, Atmos has had to participate in an expensive, and unnecessary forensic audit to demonstrate that it did not provide a "financial advantage" to its affiliated gas marketer when it accepted the lowest and best bid.

If the Commission decides that Staff's original interpretation of the Affiliated Transaction Rule is appropriate, it will provide a huge disincentive for regulated gas corporations to transact business with an affiliated gas marketer, even if that affiliated 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.

Staff's interpretation of the Affiliated Transaction Rule is likely to cause the regulated natural gas corporations in Missouri to forego dealing with affiliated gas marketers, even though the affiliated gas marketers are offering to provide gas supplies at a lower price than all other bidders for those same gas supplies. As a result, ratepayers will not receive the lowest and best price for their natural gas supplies.

As the public policy maker for the State of Missouri, the Commission should ask itself the following question:

Is this the kind of perverse incentive that the Commission wants to encourage in the PGA/ACA process?

Under Staff's view of the regulatory regime, if an LDC accepts the lowest and best bid from an affiliate, then it will face a substantial disallowance based upon Staff's analysis of the affiliate's gross profits, and face the cost of an expensive forensic audit of its affiliate's business practices. If it doesn't accept the lowest and best bid from its affiliate, then it will likely face a prudence disallowance proposed by Staff for its failure to accept the lowest and best bid for gas supplies (Tr. 644)—Isn't this an example of "Damned if you do; damned if you don't" Regulation?

Under this type of regulatory regime, isn't the incentive for the LDC and its affiliate to make independent decisions not to do business with one another? There is no legal compulsion for an unregulated affiliate to provide services to its affiliated public utility when it knows it and its affiliate will be subjected to an expensive "forensic audit" if it would be lucky enough to win the bidding process.[8] Similarly, there is no incentive for the LDC to seek bids from its affiliate if it knows that the LDC would have to absorb some level of imputed "gross profits" in the regulatory process if its affiliated gas marketer happens to make the lowest and best bid.

Even Staff witness Sommerer recognized that the adoption of Staff's proposed disallowance in this case could be a disincentive for Atmos to do business in the future with its affiliate (Tr. 706):

> Q. Would you agree that if the Commission adopts the Staff's affiliated adjustment in this case, it would be a disincentive for Atmos and AEM to do business together in the future?
>
> A. That could very well be the result.

[8] *See Report & Order*, Re Union Electric Company, Case No. ER-2007-0002, pp. 54 ("The Commission's [affiliate transaction] rule does not, and cannot require an unregulated affiliate to provide service to its regulated utility affiliate . . . ").

Q. Is it the goal of Staff in this proceeding to provide a disincentive for Atmos to do business with its affiliated gas marketer in the future?

* * *

A. No.

Based upon the competent and substantial evidence in the record, the Commission should carefully consider the public policy implications of the adoption of Staff's unprecedented adjustment in this case. (Tr. 660). It would be unfortunate if the Commission adopted Staff's view of the "proper" regulatory regime, and created a major disincentive for LDCs and their affiliated gas marketers to do business with one another in the future—and the primary losers in the process would be the LDC's consumers.

VI. FORCE MAJEURE ADJUSTMENTS

For the first time in surrebuttal testimony, Staff proposed a new prudence adjustment (i.e. $52,572 or alternatively, $85,775) related to a Force Majeure Event that occurred in December 2007. Staff has argued in its very limited surrebuttal testimony on the subject that Atmos did not act in a reasonable and prudent manner during the supply disruption that occurred when a Force Majeure Event was declared by Panhandle Eastern Pipeline when a pipeline rupture occurred in December, 2007. (Ex No. 28HC, Sommerer Surrebuttal, p. 2, 19-20). However, the facts do not support Staff's position, and the Commission should consider the tardiness of Staff's new allegation as it considers the merits of the proposed prudence adjustment. As explained below, Staff's position is not persuasive and lacks credibility.

The Staff's prudence adjustment was not included in the Staff Recommendation, Staff's direct testimony, or Staff's rebuttal testimony. It was not mentioned in the Staff's

List of Issues, or Position Statement. Nor did the Company witness address anything in her pre-filed testimony related to the Force Majeure Event in December 2007. (Tr. 602-05). In fact, Mr. Sommerer did not quibble with the fact that this prudence adjustment had never been discussed anywhere in the record until Staff filed its surrebuttal testimony on December 23, 2010. (Tr. 602) The Staff witness testified that this adjustment was not even developed until after the filing of the rebuttal testimony in this case in June, 2010.

As noted in the Commission's *Order Denying Atmos' Motion To Strike* issued on April 27, 2011, Staff justified its failure to include the proposed disallowances in its direct testimony by arguing "Atmos had concealed the circumstances surrounding the December 2007 baseload nominations from Staff until after Staff had filed its rebuttal testimony and for that reason, Staff could not present the new disallowance until it filed its surrebuttal testimony." (*Order* p. 2) However, the record is not consistent with this expression of surprise by Staff.

Staff witness Sommerer testified at the hearings in answer to questions from Judge Woodruff that he knew about the Force Majeure Event at the time it occurred and even discussed the incident with Atmos personnel at that time of the general supply disruption. (Tr. 701)—It was certainly no surprise to Staff!

> Q. Okay. Another thing I want to be clear about. The –the December 2007 disruption on the pipeline that resulted on the force majeure, was Staff aware of . . . the fact that there had been a disruption?
>
> A. Yes. (Tr. 711-12)

Just as importantly, it is indisputable that the Force Majeure Event and Atmos' alleged "imprudence" had occurred more than three (3) years before Staff ever decided to allege imprudence related to this incident. (Tr. 604) Mr. Sommerer also had contemporaneous discussions about the pipeline rupture with Jackie Butler, a Panhandle Eastern Pipeline representative, and Staff does not dispute that a Force Majeure Event was declared by the pipeline due to the rupture. (Tr. 702)

Based upon evidence in the record, it would be reasonable and appropriate for the Commission to strike the portion of Staff's surrebuttal testimony that addresses this adjustment, as requested by Atmos at the evidentiary hearing, since it is in the nature of direct testimony that should have been filed on March 12, 2010. (See Tr. 605-09)(*See 4 CSR 240-2.130(7))*, and Atmos respectfully requests that the Commission reconsider its decision to admit this portion of the surrebuttal testimony.

A. Staff Has Failed to Raise a "Serious Doubt" Regarding Atmos' Purchasing Practices During November and December, 2007.

Notwithstanding the untimeliness of Staff's proposed adjustment, more importantly, Staff has failed to raise a "serious doubt" regarding the prudence of Atmos' purchasing practices during November and December of 2007. Staff's rationale for its proposed prudence adjustment related to the Force Majeure Event in December 2007 is contained in about a dozen lines of Mr. Sommerer's Surrebuttal Testimony at pages 1-2:

**

> ____
> ____
> ____** This could have been avoided had AEC taken reasonable and prudent precautions to ensure reliability and continuity of its gas supplies.

(Ex No. 28HC, Sommerer Surrebuttal, pp. 1-2)

On its face, this limited testimony does not raise a serious doubt regarding the prudence of Atmos' actions as required by *State ex rel. Associated Natural Gas v. Public Serv. Comm'n*, 954 S.W.2d 520, 528-529 (Mo. App. W.D. 1997).

At the conclusion of Mr. Sommerer's Surrebuttal Testimony, he includes what he characterizes as "Staff's calculation of damages." (*Id*. at 19) He suggests that "[t]he Staff's calculation of damages reflects the fact that the Company could have reasonably avoided the **____ ______________________.** (*Id*. at 19) However, Mr. Sommerer does not explain in his testimony how he calculated these "damages" and fails to include any workpapers that would support his calculations. Recognizing this flaw in Staff's evidence, Staff counsel on redirect of Mr. Sommerer attempted to improperly introduce Mr. Sommerer's workpapers to supplement a record that is clearly lacking in the necessary competent and substantial evidence to support Staff's eleventh hour adjustment. (Tr. 716-19)

Although Atmos witnesses Rebecca Buchanan and Mike Walker did not have the opportunity to address Staff's allegations of "imprudence" in pre-filed testimony since Staff failed to raise the allegations until surrebuttal testimony, they have nonetheless fully explained the events surrounding the Force Majeure Event and Atmos' response to those events in their live testimony at the hearing. Based upon this competent and substantial testimony, the Commission should find that Atmos (and particularly Mr. Mike Walker, Atmos' gas purchaser) acted prudently during this period when the pipeline had been ruptured due to an Act of God.

B. Facts Surrounding the Force Majeure Event and Atmos' Nominations

Ms. Buchanan and Mr. Walker each explained the events surrounding the gas supply disruption that occurred in 2007 and Atmos' actions in response. (Tr. 448-65; 569-78) As Ms. Buchanan explained, Mr. Walker made his first-of-the month nominations on Tuesday, November 20th which was a day before he typically would do so. (Tr. 448; See also Tr. 569-70) However, since it was Thanksgiving Week, Mr. Walker was going on vacation on Wednesday, November 21, and he was permitted by Company policy to make his nominations on that day. (Tr. 448; 569) Ms. Buchanan testified that his action to nominate on that day was reasonable and prudent. (Tr. 448) He made his First-of-the Month ("FOM") nomination using his best judgment about the trends of the year, and where his storage levels would end up based upon those trends. (Tr. 570-71)

On Wednesday, November 21 at about 10:00 P.M. (the day before Thanksgiving), Atmos received a notice from Panhandle Eastern Pipeline that said that the pipeline would reduce its mainline capacity, but that there was no anticipated impact on shippers expected. (Tr. 449; 570) Even if Mr. Walker had not chosen to take a vacation day on Wednesday, November 21, he still would not have been in the office at that late hour to receive that first notice from Panhandle Eastern Pipeline.

Mr. Walker returned to the office on Monday, November 26th, following the Thanksgiving holiday. As Ms. Buchanan explained, the deadline for changing any FOM nominations was 9 AM on Monday. According to Ms. Buchanan's testimony, Mr. Walker would not have expected any problems to shippers based upon the notice that Atmos received on Wednesday evening. (Tr. 449; 569)   In fact, Ms. Buchanan testified that there were no adverse impacts upon Atmos customers as a result of the Force Majeure Event:

> We served all of our customers throughout that entire force majeure event. Our customers received the gas that they needed. There was no curtailment of our customers; no impact.
>
> They probably didn't even realize anything was going on, because we have ways to deal with the situation. For example, storage gas;   we were able to pull out of storage some more and work with our supplier to make sure that we got the gas to our customers. (Tr. 450)

Staff counsel also confirmed this fact in answer to Commissioner Davis' questions regarding whether Atmos ever failed to deliver gas to its customers: "The regulated customers in northeast Missouri did receive gas supplies. There was on outage, if that's what you're referring to." (Tr. 311)

On Monday, November 26th, a second pipeline notice came to Atmos during the morning. (Tr. 450)   This notice indicated that nominations through the Haven receipt point would be limited. (Tr. 450) Later that day, a third pipeline notice was received that declared a Force Majeure Event. (Tr. 450-51; 570) Each of these notices arrived after the 9 AM deadline for changing FOM nominations.

Ms. Buchanan testified that Force Majeure Events are rare (this was the only one Atmos knew of during the year)(Tr. 571), and it is difficult to know for a few days what is the likely impact of the event. (Tr. 451; 571) However, on November 27th, there was a small pipeline cut at the Hannibal receipt location due to the pipeline rupture. Later in December there were further cuts in Hannibal. (Tr. 451-52)

On December 4th, a fourth pipeline notice came out that discussed reductions in capacity, lower operating pressure and the pipeline assessed the seriousness of the rupture. (Tr. 452) Initially, Atmos personnel believed that there may not be any impact upon them or their customers since AEM (Atmos' supplier) was using the Pony Express Receipt Point downstream of the actual rupture. (Tr. 452) Ms. Buchanan testified that it was reasonable, from Atmos' perspective, that AEM would use the Pony Express Receipt Point, under these circumstances. (Tr. 452-53)

After the Force Majeure Event was declared by the pipeline, the area experienced some colder weather which required that Mr. Walker order swing gas. Due to a clerical error on the part of AEM, AEM did not deliver the additional swing gas for three days over the weekend (i.e. Saturday, Sunday and Monday).(Tr. 453) On Monday, when Mr. Walker returned to the office, he discussed the situation with AEM, and AEM fixed the problem. (Tr. 453) AEM also explained that the supply coming through the Pony Express Receipt Point was limited, and AEM told Mr. Walker how much gas they believed he could get without getting cut by the pipeline. Mr. Walker accepted AEM's representations and did not nominate the maximum under the contract. According to Ms. Buchanan, it was reasonable for him to do so since AEM had been a very reliable supplier in the past. (Tr. 454) Mr. Walker also confirmed the basic facts surrounding this Force Majeure Event and his actions in November and December, 2007. (Tr. 568-78)

C. Mr. Walker's Actions to Cooperate With the Supplier during the Force Majeure Event Were Reasonable and Prudent.

Staff alleges that Mr. Walker failed to nominate sufficient baseload gas supplies for the month of December, 2007 since he voluntarily cooperated with AEM during the events surrounding the pipeline rupture, and he did not nominate the maximum amount possible. Staff is incorrect in its criticism of Mr. Walker's actions. Ms. Buchanan testified that as Mr. Walker's supervisor, she <u>expected</u> Mr. Walker to cooperate with the industry when a Force Majeure Event is declared:

> Q. As the manager of the gas supply group at Atmos, do you expect your gas specialist to work with the industry when a force majeure is declared?
>
> A. It's a requirement. Yes. He needed to do that. He needed to work with the supplier and with the pipeline to make sure all parties try to get the gas they need, or at least as much as they can. (Tr. 454)

On this fundamental point, even the Staff witness Sommerer agreed with Ms. Buchanan that it was reasonable for Atmos personnel to work with the industry during a Force Majeure Event to mitigate adverse consequences to the entire pipeline:

> Q. Wouldn't you expect the LDCs to cooperate with their suppliers to mitigate such adverse consequences to the entire pipeline system whether or not those suppliers are affiliated or unaffiliated companies?
>
> A. To the extent that it does not have a negative impact, that it doesn't have a negative impact, I would say that's a reasonable course of action. (Tr. 700)

Notwithstanding Staff's expectation that LDCs work with the industry during a Force Majeure Event, Staff tried to Monday-Morning Quarterback Mr. Walker's actions by suggesting (with 20/20 hindsight) what Mr. Sommerer believed he should have done. Tr. 621) According to Mr. Sommerer (who has no actual experience as a gas purchaser), what Mr. Walker should have done on that first Monday morning after Thanksgiving was to "up" his nomination before the 9 AM deadline (Tr. 621), even though the pipeline notice did not indicate that there would be any adverse impact upon shippers. (Tr. 570) Then throughout the month of December, Mr. Sommerer "would have been pushing AEM to provide me with an explanation on why the supplies weren't available." (Tr. 622) But he immediately followed up this criticism with the candid admission that "Mr. Walker did this through one of his emails where he said where are my supplies." (Tr. 622) But according to Mr. Sommerer, "I would not have accepted the answer that came back from . . . AEM." (Tr. 622)

After-the-fact, both Mr. Sommerer and Mr. Walker now know that a Force Majeure Event was declared later in the month of December 2007 (Tr. 592; 712-13), but at the time the decisions were being made in late November regarding FOM nominations, Mr. Walker had no way to know that there would be additional cuts later in December. Staff's analysis is simply an example of the prohibited use of hindsight in evaluating the prudence of decisions that were being made with the best information available at the time. *See Report & Order* in Re Kansas City Power & Light Company, Case No. ER-2010-0355 (April 12, 0355) at 74-77; *State ex rel. Associated Natural Gas v. Public Serv. Comm'n*, 954 S.W.2d 520, 528-529 (Mo. App. W.D. 1997).

Ms. Buchanan who has more than twenty years experience in the natural gas industry and more than five years experience as the Manager of Gas Supply, evaluated Mr. Walker's actions related to the Force Majeure Event as follows:

Q. Did you find anything imprudent about what he did?

A. I thought he did a really good job handling the -- handling the event. You know, if our supplier had been unreliable in the past, I could see why Mr. Walker might question what they're suggesting him to do to address this event. But AEM had -- has been very reliable for many years, and has -- has not caused us any concern. So I'm fine with Mr. Walker working with our supplier. And if they said, I cannot get more than this gas to serve you, I'm okay with him listening to them and trying to work with them through this -- through this event. We did have sufficient storage balances, and we were able to pull gas out of storage and flow it to our customers. (Tr. 454-55)

Mr. Walker also testified, that contrary to the implications of Staff's allegations in this case, he did not have any agreement or any conspiracy with any AEM representative to reduce his nominations during that Force Majeure Event to help AEM's bottom line. (Tr. 575)

Based upon all the competent and substantial evidence in the record, the Commission should find and conclude that Atmos' actions surrounding the Force Majeure Event in December 2007 were reasonable and prudent, given the information and circumstances that were known at the time the gas nominations were being made.

The Commission should therefore reject the Staff's prudence adjustment contained in its surrebuttal testimony.

D. Staff Has Failed to Supply the Required "Nexus" Between The Alleged Imprudence and Any Harm to Consumers.

Even if the Commission found something about Mr. Walker's actions to be less than prudent, the Staff has failed to show the "nexus" between his actions and any harm to consumers. *See Associated Natural Gas*, 945 S.W.2d at 529. As Ms. Buchanan testified, there were other reasons besides the Force Majeure Event that would require that in January, February and March, there might be larger purchases of gas. (Tr. 455) The reasons included: a propane peaking plant in Hannibal experienced an outage in mid-December requiring additional purchases, storage contract ratchets require additional purchases to ensure deliverability on a peak day, and the need to purchase gas supplies for unusually cold days. (Tr. 456) As a result, Staff has not demonstrated that any specific actions by Mr. Walker caused any harm to consumers. As previously noted, no consumer was affected or probably even aware of the pipeline rupture during this rare Force Majeure Event. (Tr. 540)

VII. CONCLUSION

In conclusion, the Commission should reject the Staff's proposed $308,000 Affiliated Transaction Adjustment, and the prudence adjustment associated with the Force Majeure Event in December 2007. Staff simply failed to raise a serious doubt regarding the prudence of Atmos' gas purchasing practices during the ACA period. Even if a "serious doubt" had been raised (which it has not), the competent and substantial evidence in the record presented by the Atmos witnesses demonstrates that Atmos was prudent in its gas purchasing activities during the 2007-2008 ACA period.

For the reasons stated herein, the Commission should find and conclude:

1. Atmos Energy Corporation's purchasing practices were prudent during this ACA period.

2. The Affiliated Transaction Rule does not require that a regulated LDC like Atmos lower its gas supply costs in the PGA/ACA process by the same amount as the gross profits of an affiliated gas marketer that provided gas supplies after a formal competitive bidding process.

3. Atmos did not provide a "financial advantage" to its affiliate since it paid AEM less than the fair market price, as established by a competitive bidding process, for its gas supplies.

4. The Commission should not prohibit affiliated transactions between Atmos and its affiliated gas marketer in this ACA proceeding.

5. The Commission should not adopt the Staff's proposed $308,000 disallowance of gas costs because Atmos asserted its legal right to object to discovery related to its unregulated affiliate.

6. Atmos was not imprudent by failing to nominate the maximum amount possible under its contract with AEM during a December 2007 Force Majeure period during the rupture of the natural gas pipeline owned and operated by Panhandle Eastern Pipeline Company.

Respectfully submitted,

/s/ James M. Fischer

James M. Fischer, MBN 27543
email: jfischerpc@aol.com
Larry W. Dority, MBN 25617
email: lwdority@sprintmail.com
Fischer & Dority, P.C.
101 Madison Street, Suite 400
Jefferson City, MO 65101
Telephone: (573) 636-6758
Facsimile: (573) 636-0383

Douglas C. Walther, MBN 32266
Associate General Counsel
Atmos Energy Corporation
P.O. Box 650205
Dallas, Texas 75265-0205
Email: doug.walther @atmosenergy.com
Telephone: (972) 855-3102

Attorneys for Atmos Energy Corporation

CERTIFICATE OF SERVICE

I do hereby certify that a true and correct copy of the foregoing document has been hand-delivered, emailed or mailed, First Class mail, postage prepaid, this 29th day of April, 2011, to all counsel of record in this matter.

/s/ James M. Fischer

James M. Fischer