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OFFICE OF THE EXECUTIVE SECRETARY

BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

March 19, 2001

IN RE:	)
	)
UNITED CITIES GAS COMPANY	**) Docket No. 00-00801**
ACTUAL COST ADJUSTMENT (ACA) AUDIT	)

NOTICE OF FILING BY ENERGY AND WATER DIVISION OF THE TENNESSEE REGULATORY AUTHORITY

Pursuant to Tenn. Code Ann. §§ 65-4-104, 65-4-111 and 65-3-108, the Energy and Water Division of the Tennessee Regulatory Authority gives notice of its filing of the United Cities Gas Company's ACA Audit Report in this docket and would respectfully state as follows:

1. The present docket was opened by the Authority to hear matters arising out of the audit of United Cities Gas Company (the "Company").

2. The Company's ACA filing was received on September 6, 2000, and the Staff completed its audit of same on February 23, 2001.

3. On March 8, 2001, the Energy and Water Division issued its preliminary ACA audit findings to the Company, and on March 12, 2001, the Company responded thereto.

4. The preliminary ACA audit report was modified to reflect the Company's responses and a final ACA audit report (the "Report") resulted therefrom. The Report is attached hereto as <u>Exhibit A</u> and is fully incorporated herein by this reference. The Report

contains the audit findings of the Energy and Water Division, the Company's responses thereto and the recommendations of the Energy and Water Division in connection therewith.

5. The Energy and Water Division hereby files its Report with the Tennessee Regulatory Authority for deposit as a public record and approval of the recommendations and findings contained therein.

Respectfully Submitted:

David McClanahan
Energy and Water Division of the
Tennessee Regulatory Authority

CERTIFICATE OF SERVICE

I hereby certify that on this 19th day of March, 2001, a true and exact copy of the foregoing has been either hand-delivered or delivered via U.S. Mail, postage pre-paid, to the following persons:

Mr. K. David Waddell
Executive Secretary
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, TN 37243

Mr. Mark G. Thessin
Vice President of Rates and Regulatory Affairs
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810 Crescent Centre Dr., Suite 600
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David McClanahan

David McClanahan

COMPLIANCE AUDIT REPORT

OF

UNITED CITIES GAS COMPANY

ACTUAL COST ADJUSTMENT

DOCKET NO. 00-00801

PREPARED BY

TENNESSEE REGULATORY AUTHORITY

ENERGY AND WATER DIVISION

MARCH 2001

EXHIBIT A

COMPLIANCE AUDIT

UNITED CITIES GAS COMPANY

ACTUAL COST ADJUSTMENT

DOCKET NO. 00-00801

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I. INTRODUCTION

The subject of this audit is United Cities Gas Company's ("Company" or "United Cities") compliance with the Actual Cost Adjustment and Refund Adjustment of the Purchased Gas Adjustment Rule ("PGA Rule") of the Tennessee Regulatory Authority ("TRA" or the "Authority"). The objective of the audit was to determine whether the Purchased Gas Adjustments, which are encompassed by the Actual Cost Adjustment ("ACA") as more fully described in Section V., for the year ended June 30, 2000, were calculated correctly and were supported by appropriate source documentation.

II. AUDIT OPINION

The Staff concludes that, except for the findings detailed in this report, the Purchased Gas Adjustment mechanism as calculated in the Actual Cost Adjustment appears to be working properly and in accordance with the TRA rules for United Cities Gas Company.

The Company made its Actual Cost Adjustment filing for the Union City, Tennessee service area and Tennessee service areas other than Union City on September 6, 2000. This ACA filing showed $67,835,516 in total gas costs, with $70,495,308 being recovered from customers through rates. Adding a beginning balance in the ACA account of $1,748,447 in underrecovered gas costs from the preceding ACA period and interest due from customers for the current period of $141,618 resulted in an ACA balance at June 30, 2000 of $769,727 in overrecovered gas costs. The Company began refunding this amount to its customers on October 1, 2000.

The Staff's audit showed total gas costs of $ 67,825,391 with $70,495,308 being recovered from customers through rates. Thus, total interest due to the customers for the period is $ 140,934 and the adjusted ACA balance at June 30, 1999 is **$780,536** in overrecovered gas costs. The results of the Staff's audit was a **net overrecovery of $10,809** for the audit period. The effect was to increase the amount of the overrecovered balance by this amount. A detail summary of the ACA account and the Staff's findings is found under ACA Findings on page 5 of this report.

After the Staff's adjustments, the Company's total gas costs incurred for the ACA period under audit totalled $68 million. The **$10,809 overrecovery** calculated by the Staff is less than one percent of the total gas purchases and is not considered material in comparison. United Cities Gas Company customarily makes an adjustment for Staff's findings to the Deferred Gas Cost account in the following audit period. The Staff concurs with this method.

III. BACKGROUND INFORMATION ON COMPANY AND GAS SUPPLIERS

United Cities Gas Company, a Division of Atmos Energy Corporation, located at 810 Crescent Centre Dr., Suite 600, Franklin, Tennessee, is a multistate gas distributor. The Company provides service to customers in twelve cities and surrounding areas in Tennessee. The natural gas used to serve these areas is purchased from four natural gas pipelines in accordance with separate and individual tariffs approved by the Federal Energy Regulatory Commission (FERC). The interstate pipelines are Tennessee Gas Pipeline (TGP), East Tennessee Natural Gas (ETNG), Texas Gas Transmission Corporation (TGTC), and Texas Eastern Transmission Corporation (TETC).

TGP and ETNG provide service to east Tennessee towns, which include Columbia, Shelbyville, Maryville, Morristown, Elizabethton, Greeneville, Johnson City, Kingsport, Bristol and adjacent areas in Maury, Bedford, Moore, Blount, Hamblen, Sullivan, Carter, Washington, and Greene Counties.

TETC provides service to UCG in Murfreesboro and Franklin and adjacent areas in Rutherford and Williamson Counties.

TGTC provides service to UCG in Union City and adjacent areas in Obion County.

IV. JURISDICTION OF THE TENNESSEE REGULATORY AUTHORITY

Tennessee Code Annotated (T.C.A.) gave jurisdiction and control over public utilities to the Tennessee Regulatory Authority. T.C.A. §65-4-104 states that:

> The [A]uthority has general supervisory and regulatory power, jurisdiction, and control over all public utilities, and also over their property, property rights, facilities, and franchises, so far as may be necessary for the purpose of carrying out the provisions of this chapter.

Further, T.C.A. §65-4-105 grants the same power to the Authority with reference to all public utilities within its jurisdiction as chapters 3 and 5 of Title 65 of the T.C.A. have conferred on the Department of Transportation's oversight of the railroads or the Department of Safety's oversight of transportation companies. By virtue of T.C.A. §65-3-108, this power includes the right to audit:

> The department is given full power to examine the books and papers of the companies, and to examine, under oath, the officers, agents, and employees of the companies and any other persons, to procure the necessary information to

> intelligently and justly discharge its duties and carry out the provisions of this chapter and chapter 5 of this title.

The Energy and Water Division of the TRA is responsible for auditing those companies under the Division's jurisdiction to ensure that each company is abiding by Tennessee statute as well as the Rules and Regulations of the Authority. This audit was performed by David McClanahan and Pat Murphy of the Energy and Water Division.

V. DESCRIPTION OF PURCHASED GAS ADJUSTMENT RULE

Actual Cost Adjustment Audits:

The PGA Rule can be found in Chapter 1220-4-7 of the Rules of the Tennessee Regulatory Authority. The PGA Rule permits a gas company to recover, in a timely fashion, the total cost of gas purchased for delivery to its customers and to assure that a company does not over-collect or under-collect gas costs from its customers. The PGA consists of three major components:

1. **The Actual Cost Adjustment (ACA)**
2. **The Gas Charge Adjustment (GCA)**
3. **The Refund Adjustment (RA)**

The ACA is the difference between the revenues billed customers by means of the GCA and the cost of gas invoiced the Company by suppliers plus margin loss (if allowed by order of the TRA in another docket) as reflected in the Deferred Gas Cost account. The ACA then "trues-up" the difference between the actual gas costs and the gas costs recovered from customers through a surcharge or a refund. The RA refunds the "true-up" along with other supplier refunds. For a more complete definition of the GCA and RA, please see the PGA Formula in Appendix A.

Section 1220-4-7-.03(2) of the PGA Rule requires:

> Each year, the Company shall file with the [Authority] an annual report reflecting the transactions in the Deferred Gas Cost Account. Unless the [Authority] provides written notification to the Company within one hundred eighty (180) days from the date of filing the report, the Deferred Gas Cost Adjusment Account shall be deemed in compliance with the provisions of these Rules. This 180 day notification period may be extended by mutual consent of the Company and the [Authority] Staff or by order of the [Authority].

Prudence Audit of Gas Purchases:

Section 1220-4-7-.05 of the PGA Rule requires, unless otherwise ordered by the Authority, an "Audit of Prudence of Gas Purchases" by a qualified consultant. This specialized audit evaluates and reports annually on the prudence of any gas costs included in the PGA. In Docket 97-01364, United Cities was authorized to operate under a Performance-Based Ratemaking Mechanism ("PBR"), beginning April 1, 1999, and continuing each year unless terminated by the Company or the Authority. For each year that the mechanism is in effect, the requirements of Section 1220-4-7-.05 of the PGA Rule is waived.

VI. SCOPE OF ACTUAL COST ADJUSTMENT AUDIT

The Company submitted its ACA filing on September 6, 2000. On January 17, 2001, the TRA Staff requested an extension of the 180 days notification period to April 1, 2001 and the Company agreed. On February 22, 2001, the Staff requested a further extension to April 17, 2001. An additional extension was needed in order that the Company would have sufficient time to respond to the Staff's findings and the Staff would have sufficient time to incorporate those responses into the final audit report.

We performed this audit to verify that the Company's calculations of gas costs incurred and recovered were correct. A detail of the ACA account is provided in Section VII (ACA Findings). Also included in this audit was the Company's PGA filing implementing a surcharge of the ACA account balance at June 30, 2000, effective October 1, 2000.

We also audited a sample of customer bills to determine if the proper PGA rates were applied in the Company's calculation of customer bills during the audit period. Since the Company's billing process is computerized, a sample of 245 bills was tested. These bills were selected to be representative of the residential, commercial, industrial and interruptible customers in each of the Company's service areas. The sample was selected from the twelve month period July 1999 through June 2000. After recalculating each sample bill, we determined that the calculation methods utilized by the Company are correct.

VII. ACA FINDINGS

As outlined above, the result of the Staff's audit was a **net overrecovery of $10,809**, which had the effect of increasing the Company's overrecovery balance in the ACA account by this amount. A summary of the ACA account as filed by the Company and as adjusted by the Staff is shown below, followed by a detail of each finding.

SUMMARY OF THE ACA ACCOUNT:

	Company	Staff	Difference (Findings)
Beginning Balance at June 30, 1999	$ 1,748,447	$ 1,748,447	$ 0
Plus Gas Costs	67,835,516	67,825,391	-10,125
Minus Recoveries	70,495,308	70,495,308	0
Ending Balance before Interest	$ -911,345	$ -921,470	$ -10,125
Plus Interest	141,618	140,934	-684
Ending Balance at June 30, 2000	$ -769,727	$ -780,536	$ -10,809

SUMMARY OF FINDINGS:

				See page
FINDING #1	Union City - Commodity	$ 15,893.28	Overrecovery	6
FINDING #2	All Other Towns - Commodity	5,962.13	Underrecovery	7
FINDING #3	All Other Towns-Commodity	194.25	Overrecovery	8
FINDING #4	Interest Recalculations	684.36	Overrecovery	9
	Net Result	**$ 10,809.76**	**Overrecovery**	

FINDING #1:

Exception

The Staff calculated an **overrecovery of $15,893.28** in the commodity costs for the Union City filing.

Discussion

The commodity cost of gas was affected by incorrectly recording the cost of inventory in Union City. There were mathematical errors in recording the injection costs into storage for the months of October 1999 (9,582.19), November 1999 (2,591.43), and December 1999 (3,719.66). This resulted in incorrect costs being recorded in storage inventory.

Company Response

The Company agrees with this finding.

FINDING #2:

Exception

The Staff calculated an **underrecovery of $5,962.13** in the commodity costs for All Tennessee Towns Other Than Union City filing.

Discussion

The Company made an error in December 1999 in calculating the allocation factor used to allocate gas cost between Tennessee and Virginia. This factor as calculated by the company was 65.02%. The correct factor as calculated by the staff was 65.20%. Therefore, more gas costs should have been allocated to Tennessee in the amount of $5,962.13. This created errors in December 1999 ($6,147.55) as well as in the months of January 2000 ($8.21), March 2000 ($-230.19), and May 2000 ($36.56) when revised December 1999 invoice amounts were recorded.

Company Response

The Company agrees with this finding.

FINDING #3:

Exception

The Staff calculated an **overrecovery of $194.25** in gas cost from propane

Discussion

The Company was unable to find a invoice in July 1999 for propane for this amount.

Company Response

The Company agrees with this finding.

FINDING #4

Exception

The Staff recalculated an **overrecovery** of interest as a result of the above findings in the amount of **$684.37**.

Discussion

The interest recalculation breakdown is as follows:

All Other Towns		$273.76	Underrecovery (1)
Union City		70.03	Overrecovery (2)
Union City		888.09	Overrecovery (3)
	Total	$684.37	Overrecovery

(1) Due to Findings #2 and #3.
(2) The Company used an incorrect interest rate for the 4th quarter.
(3) Due to Finding #1.

Company Response

The Company agrees with this finding.

APPENDIX A

PGA FORMULA

The computation of the GCA can be broken down into the following formulas:

$$\text{Firm GCA} = \frac{D + DACA}{SF} - DB + \frac{P + T + SR + CACA}{ST} - CB$$

$$\text{Non-Firm GCA} = \frac{P + T + SR \;\; CACA}{ST} - CB$$

where

GCA	=	The Gas Charge Adjustment in dollars per Ccf/Therm, rounded to no more than five decimal places.
D	=	The sum of all fixed Gas Costs.
DACA	=	The demand portion of the ACA.
P	=	The sum of all commodity/gas charges.
T	=	The sum of all transportation charges.
SR	=	The sum of all FERC approved surcharges.
CACA	=	The commodity portion of the ACA.
DB	=	The per unit rate of demand costs or other fixed charges included in base rates in the most recently completed general rate case (which may be zero if the Company so elects and the Commission so approves).
CB	=	The per unit rate of variable gas costs included in base rates in the most recently completed general rate case (which may be zero if the Company so elects and the Commission so approves).
SF	=	Firm Sales.

ST = Total Sales.

The computation of the RA can be computed using the following formulas:

$$\text{Firm RA} = \frac{DR1 - DR2}{SFR} + \frac{CR1 - CR2 + CR3 + i}{STR}$$

$$\text{Non-Firm RA} = \frac{CR1 - CR2 + CR3 + i}{STR}$$

where

RA =	The Refund Adjustment in dollars per Ccf/Therm, rounded to no more than five decimal places.
DR1 =	Demand refund not included in a currently effective Refund Adjustment, and received from suppliers by check, wire transfer, or credit memo.
DR2 =	A demand surcharge from a supplier not includable in the GCA, and not included in a currently effective Refund Adjustment.
CR1 =	Commodity refund not included in a currently effective Refund Adjustment, and received from suppliers by check, wire transfer, or credit memo.
CR2 =	A commodity surcharge from a supplier not includable in the GCA, and not included in a currently effective Refund Adjustment.
CR3 =	The residual balance of an expired Refund Adjustment.

i	=	Interest on the "Refund Due Customers" account, using the average monthly balances based on the beginning and ending monthly balances. The interest rates for each calendar quarter used to compute such interest shall be the arithmetic mean (to the nearest one-hundredth of one percent) of the prime rate value published in the "Federal Reserve Bulletin" or in the Federal Reserve's "Selected Interest Rates" for the 4th, 3rd, and 2nd months preceding the 1st month of the calendar quarter.
SFR	=	Firm sales as defined in the GCA computation, less sales under a transportation or negotiated rate schedule.
STR	=	Total sales as defined in the GCA computation, less sales under a transportation or negotiated rate schedule.