BEFORE THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE

'01 JUN 19 PM 1 24

IN RE: PETITION OF UNITED CITIES GAS COMPANY FOR EXPEDITED APPROVAL OF AUTHORITY TO PURCHASE FUTURES CONTRACTS FOR THE WEATHER HEATING SEASON OF 2001-02 ON AN EXPERIMENTAL BASIS	)))))))	DOCKET NO. 01-00510

June 14, 2001 Response to Data Request Dated June 13, 2001
and June 18, 2001 Response to Data Request Dated June 15,2001

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1. **United Cities is requesting that this long-term contract not be included in the Performance Based Ratemaking plan (PBR). Please discuss the risk and reward tradeoffs under the existing gas purchasing procedures compared to the risk and reward tradeoffs of the proposed procedures.**

   Existing gas purchasing procedures:
   The potential risk of continuing gas purchases per the existing gas purchasing procedures at index pricing for the upcoming 2001-02 winter season would expose customers to possible price spikes similar to the winter 2000-01 period.

   The potential reward would be realized by purchasing gas at market prices if those market prices were lower than purchased futures prices.

   Proposed change for winter 2001-02:
   The proposed futures contract would be in place only during November, 2001 through March, 2002 for 50% of anticipated purchases, net of storage.

   The potential risks would be that the contracted futures prices could be actually higher than the actual market indices during the proposed period. (Yet, a reasonable price cap would be established, gas cost would be known previously, and gas costs would be stabilized.)

   The potential reward would be that the contracted futures prices would provide mitigation of price volatility and provide price stability.

2. **Your examples state that you rely on storage to fulfill 42% of your winter gas requirements. Therefore, provide five years (1996 through 2000) of storage data, detailing injection volumes and cost per MCF. What is your normal storage level**

going into the winter season? Explain your future plans for continued storage capacity.

Please see attachments for 1996 through 2000 injection volumes and cost per MCF. The attachment contains confidential and highly proprietary information and is filed under seal. UCG strives to bring storage levels to an operationally full level of approximately 90% to 95% capacity by October 31each year. Filling storage facilities to these levels allows space for injections if needed during warm periods during the shoulder month of November. UCG does not intend to change this practice in the future.

3. **What has been your normal gas purchasing procedures? For example, have there been any long-term gas contracts purchased before? How many purchase contracts are normally executed during the five winter months? Have most gas purchases in the past been spot market gas?**

UCG utilized the Request for Proposal Process and entered into a multi-year requirements contract at market based pricing (exclusive of Nora deliveries).

During the past several years of the current requirements contract, UCG requested bids from qualified suppliers. This process confirmed that the existing requirements contract has continued to be the lowest market price.

With reference to past gas purchases being spot market gas, most gas has been priced at indices published at the first of each month. Should an incremental volume be necessary to meet requirements, these volumes would be purchased at a daily published price.

4. **Provide a schedule detailing your gas purchases (costs) for the summer and winter months. Please list frequency of purchases and costs per MCF. As a corollary to your purchases, provide gas futures costs quoted in July for the following January for the last five years. This will provide a comparison between the futures price of gas (six months prior to actual purchase) and the actual price paid for that purchase. Provide this graphically with futures on one line and actual costs on another line.**

Please see attachments. The attachments contain confidential and highly proprietary information and is filed under seal. Included is a schedule detailing purchases for April, 1997 through March, 2001. Also included is the requested January price graph for 1997 through 1998.

5. **Have you had any affiliate purchasing transactions for any non-regulated company in the past? Do you anticipate any during this experimental year? If so, provide steps to assure the TRA that your ratepayers will receive the lowest prices.**

There have been no affiliate purchasing transactions for a non-regulated company in Tennessee. UCG does not anticipate any such transactions during this experimental year. If UCG's proposal is approved, UCG will purchase futures contracts specific to UCG's Tennessee requirements.

6. **Do historical natural gas prices indicate a seasonal fluctuation in prices? Please provide a chart and table of values showing actual monthly commodity gas prices over the last ten years or similar supporting documentation to support this conclusion.**

Please see attachments. Typically, market prices during the summer are less than the market prices during the winter. However, there is a recent trend, which indicates greater volatility relative to historical prices.

7. **What is the extent of your experience in working with gas futures?**

The Company has some limited experience with futures contracts in other utility service territories.

8. **Have you proposed a similar hedging mechanism in other states? If so, summarize by state, what was proposed, when it was submitted, the status of the proposal and what formal or informal action was taken by each state. Also, provide any orders, rulings or findings issued by the states.**

Please see the attached response to the State of Iowa. It is a good summary of our discussions with other states. Kansas and Kentucky are the only states in which we have received an issued order to date. The Kansas and Kentucky orders are attached.

9. **Currently, the accounting procedures for recording gas costs are as follows. Under the terms of the PGA Rule, gas purchase costs are debited to the deferred gas cost account (Account 191) and the ratepayer reimburses the Company for 100% of these costs. Under the PBR, gas procurement transactions are compared to a predetermined benchmark and the ratepayer reimburses the Company 50% of any net gains and is credited for 50% of any net losses. With respect to the Company's proposal. Please provide a detailed explanation of the accounting procedures (accounting entries) that will be made under the proposed hedging contract.**

Please see attachment.

10. **Will all gas purchase transactions be debited to the deferred gas cost account, as they are now? Then, when the Company receives payment for the savings, will the deferred gas cost account be credited? If not, explain how the savings are passed on to the ratepayer.**

Yes, all gas purchase transactions will continue to be debited to the deferred gas cost account. Yes, upon realization of savings/ costs, the deferred gas cost account will be credited/ debited.

11. [NOT USED]

12. **Would UCG be willing to submit to, and pay for, a prudence audit by an outside auditor of the proposed purchase gas futures contracts?**

UCG does not think that a prudence audit by an outside auditor is necessary in regard to the experimental hedging program for the winter season of 2001-02. Instead, UCG suggests that it is more appropriate to supply the TRA with the necessary information in order to review the program and evaluate its effectiveness in consideration of whether additional hedging programs by UCG might be appropriate at sometime in the future. UCG proposes that it provide similar information as required by the Kentucky Public Service Commission in its order approving an experimental hedging program filed on June 15, 2001. A copy of the order has been supplied in response to Data Request No. 8.

For instance, UCG proposes to file with the TRA no later than November 15, 2001, an interim report on any hedging activity in which it engages between now and the November 1, 2001 beginning of the winter heating season. This report will identify each futures contract, the date of the transaction, the cost of the transaction, the futures price reflected in the contract and include the accounting entries made by UCG to record the hedging transactions. The report would also include a brief narrative discussion of the factors that influenced UCG's purchasing decision, including but not limited to: (1) futures prices at the time of the purchasing decision; (2) market price trends at the time of purchasing decisions; (3) market price forecast at the time of the purchasing decision; and (4) UCG's storage levels at the time of purchasing decisions. UCG would also file a final report on its hedging program by no later than April 15, 2002, which would identify any gas cost savings realized under the hedging program and provide the accounting entries made by UCG to record the monthly charges in market prices and the closing of the contracts and net settlement. If UCG desires to renew or extend the hedging program, or propose a new hedging program, it would submit an appropriate request at the time it submits its final report.

With this information, the effectiveness of the hedging program could be easily and thoroughly analyzed without the necessity of a prudence audit by an outside auditor.

13. **UCG's tariff offers a "Budget Bill Plan" to customers. Does UCG allow customers to participate in this plan after the initial sign up period? Will customers that have used other payment options be allowed to participate in the "Budget Bill Plan" if their accounts are not current? Can consumers sign up for the plan anytime during the year?**

The Budget Plan Year begins in June. It is preferred that customers enroll in the summer to build a credit balance before the heating season, however customers can enroll throughout the year. Customers must pay their balance in full to be eligible for budget billing.

14. **Upon request and with some restrictions, UCG offered other payment options to consumers during the last heating season. Could you describe these plans and indicated if these options will be available in the come heating season?**

This past winter season gas prices were at unprecedented levels. Due to the severity of the high pga(s) and cold weather, the Company worked with all customers having problems paying their energy bills. Deferred payment plans were offered for extended periods up to seven months depending upon the customer's balance and ability to pay. If this past winter's prices and weather were to reoccur, the Company would most likely offer the same extended payment options. As a rule, however, deferred payment plans are offered for a three month period.

Respectfully submitted,

BAKER, DONELSON, BEARMAN
& CALDWELL, P.C.

Joe A. Conner by Jennifer L. Cook with permission

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Misty Smith Kelley, TN BPR # 19450
1800 Republic Centre
633 Chestnut Street
Chattanooga, TN 37450-1800

Attorneys for United Cities Gas Company

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing has been mailed, postage prepaid, to the following parties of interest this 19th day of June, 2001.

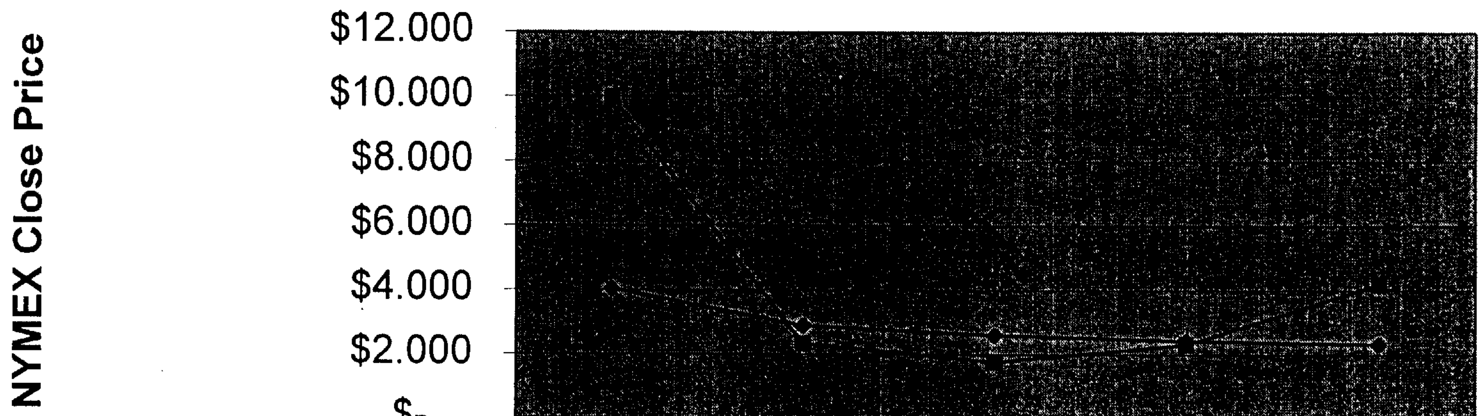
Richard Collier
General Counsel, Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, TN 37243-0505

Timothy C. Phillips
Office of Attorney General and Reporter
Consumer Advocate Division
P.O. Box 20207
Nashville, TN 37202

Jennifer L. Cook

United Cities Gas Company,
A Division of Atmos Energy Corporation
State of Tennessee
TRA Docket No. 01-00510
<u>Data Request #4</u>
June 14, 2001

Comparison of Summer vs. Actual January NYMEX Price



	1/01	1/00	1/99	1/98	1/97
July's Close for January	$4.048	$2.898	$2.603	$2.428	$2.325
Actual January Close	$9.978	$2.344	$1.765	$2.309	$4.192

July's Close for January — Actual January Close

Publication	Pipeline	Market Area / Region	Yr.	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC
Inside FERC	Tennessee Gas	Louisiana	91	$1.85	$1.34	$1.32	$1.33	$1.30	$1.25	$1.10	$1.13	$1.38	$1.72	$1.73	$1.90
Inside FERC	Tennessee Gas	Louisiana (Zone 1)	92	$1.65	$1.02	$1.19	$1.35	$1.53	$1.65	$1.45	$1.85	$1.91	$2.61	$2.30	$2.18
Inside FERC	Tennessee Gas	La. & OffShore (Zone 1)	93	$1.88	$1.59	$1.84	$2.14	$2.60	$1.86	$1.81	$1.95	$2.27	$1.92	$2.05	$2.33
Inside FERC	Tennessee Gas	La. & OffShore (Zone 1)	94	$1.98	$2.31	$2.32	$1.92	$2.00	$1.73	$1.87	$1.70	$1.40	$1.35	$1.62	$1.64
Inside FERC	Tennessee Gas	La. & OffShore (Zone 1)	95	$1.57	$1.37	$1.42	$1.50	$1.60	$1.64	$1.42	$1.30	$1.50	$1.58	$1.73	$2.24
Inside FERC	Tennessee Gas	La. & OffShore (Zone 1)	96	$3.25	$2.33	$2.81	$2.58	$2.10	$2.28	$2.57	$2.22	$1.72	$1.75	$2.63	$3.73
Inside FERC	Tennessee Gas	La. & OffShore (Zone 1)	97	$3.84	$2.79	$1.66	$1.76	$2.04	$2.24	$2.07	$2.11	$2.46	$3.02	$3.20	$2.45
Inside FERC	Tennessee Gas	La. & OffShore (Zone 1)	98	$2.19	$1.93	$2.19	$2.24	$2.21	$1.96	$2.29	$1.85	$1.53	$1.95	$1.93	$2.05
Inside FERC	Tennessee Gas	La. & OffShore (Zone 1)	99	$1.71	$1.75	$1.57	$1.84	$2.30	$2.16	$2.21	$2.54	$2.83	$2.47	$2.97	$2.07
Inside FERC	Tennessee Gas	La. & OffShore (Zone 1)	0	$2.30	$2.58	$2.56	$2.80	$3.03	$4.32	$4.29	$3.74	$4.52	$5.19	$4.42	$5.92
Inside FERC	Tennessee Gas	La. & OffShore (Zone 1)	1	$9.82	$6.13	$4.91	$5.28	$4.79	$3.62						

United Cities Gas,
A Division of Atmos Energy Corporation

State of Tennessee
TRA Docket No. 01-00510

<u>Data Request #6- Table of 10 Years of Inside FERC Prices for Tennessee Gas Pipeline, Louisiana (Zone 1)</u>

Writer's Direct Dial:
Ph: 972-855-3102
Fax: 972-855-3080

June 8, 2001

Mr. John Harvey
Energy Manager
Iowa Utilities Board
350 Maple Street
Des Moines, IA 50313-0055

Re: United Cities Gas Company Hedging Proposal
2001-2002 Heating Season

Dear Mr. Harvey:

United Cities Gas Company appreciates the opportunity to meet with the Board's Staff and representatives of the Office of Consumer Advocate on May 29 to discuss strategies to stabilize the cost of gas in an effort to mitigate potential price spikes during the upcoming winter. It was helpful to receive the perspective and support of the Board's Staff and the Office of Consumer Advocate on the hedging strategy United Cities is planning to pursue.

As we explained at the meeting, United Cities has considered a number of hedging strategies for the upcoming heating season including call options and futures contracts. After evaluating the various options available, United Cities has decided that the best course of action is to purchase natural gas futures contracts in the range of 40% to 60% of the supply required, net of storage, to serve its Iowa customers for the 2001-2002 heating season. We believe that this will result in stabilization of gas costs for our customers and provide them with adequate protection from price spikes that may occur this winter. It is United Cities understanding that while it may not receive an order from the Board providing formal approval of its hedging plan, the Staff and Office of Consumer Advocate are supportive of the plan as long as United Cities can document what it is doing as well as any deviations from the plan.

United Cities and the other Atmos operating divisions have been discussing potential hedging strategies in each of the other ten states in which Atmos operates. The support by Atmos' regulators for some type and level of hedging has been positive throughout our service territory. Pursuant to your request, a summary of the course of action Atmos is planning to pursue in each of these states is contained below:

Kentucky, Tennessee, Georgia

Atmos has Performance Based Rates (PBR's) approved in these three states which contain benchmarks for gas costs. Atmos is seeking approval from the Commission's in these states to move the costs and benefits that result from gas price hedging directly to gas costs. If this approval is obtained, the gas purchased pursuant to the hedging strategy would not be compared to the benchmark. Therefore, the customer would receive all costs and benefits resulting from the hedging activities in the same manner as they would in states without PBR's.

Atmos has made a filing in Kentucky requesting approval to purchase natural gas futures contracts for approximately 50% of its purchase requirements, net of storage, for the November 2001 to March 2002 time frame. An order approving the request is pending.

An Application is being prepared in Tennessee similar to the one that was filed in Kentucky.

In Georgia, discussions are ongoing with the Staff of the Public Service Commission. Georgia is unique from Kentucky and Tennessee in that it requires an annual gas supply plan hearing for approval of gas purchase contracts. To date, no filing has been made.

Louisiana

Atmos has filed an application requesting approval to purchase natural gas futures contracts for 75% to 100% of its purchase requirements, net of storage, for the 2001-2002 heating season. Atmos is awaiting an order from the Commission addressing its request.

Illinois, Missouri, Virginia

No formal filings requesting approval of Atmos' hedging strategy will be made in these states. Atmos has met with the Commission Staff in each of these states and they have all expressed support for hedging and indicated that continuing to purchase 100% of gas supply at market prices may not be advisable. In addition, they have stated that a well-documented reasonable hedging plan would not be second-guessed. Atmos currently plans to purchase natural gas futures contracts in the range of 40% to 60% of its total purchases, net of storage, in these states.

Kansas

Atmos has received approval from the Kansas Corporation Commission of a hedging budget to provide price caps during December and January with the ability to utilize budget funds for November and February if conditions change during implementation of the hedging program.

Colorado

The Commission Staff and Office of Consumer Counsel support price stabilization but are leaning toward fixing the physical supply contracts. Therefore, Atmos will likely pursue fixing physical contracts for 40% to 60% of its requirements for the upcoming heating season.

Texas

Atmos plans to fix a price through physical supply contracts. In addition, because of the unique regulatory framework in Texas, which involves individual municipalities in the ratemaking and gas supply process, Atmos is evaluating additional financial hedging. Atmos is currently considering utilizing hedging tools for 40% to 60% of its requirements, net of storage, in Texas.

I hope this information is helpful to you in your consideration of this issue. If you have any questions or require further information regarding this matter, please do not hesitate to contact me at (972) 855-3102.

Sincerely,

Douglas C. Walther
Senior Attorney

cc: Cecil Wright
Ben Stead

THE STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS

Post-it® Fax Note 7671 | Date 6-14 | # of pages ▶
To Joe Conner | From John Hack
Co./Dept. | Co.
Phone # | Phone #
Fax # 423-752-9527 | Fax #

Before Commissioners: John Wine, Chair
Cynthia L. Claus
Brian J. Moline

In the Matter of the Application of Greeley Gas Company, a division of Atmos Energy Corporation, for Approval of an Accounting Order to Permit Greeley Gas Company to Recover Amounts Necessary to Expend in Order to Establish and Maintain a Gas Ceiling Price for the 2001-2002 Heating Season; and for Approval of Greeley Gas Company's "Gas Hedge Program" Tariff.) Docket No. 01-GRLG-886-PGA

ORDER GRANTING JOINT MOTION
GRANTING INTERVENTION
AND
APPROVING STIPULATION AND AGREEMENT

NOW, the above-captioned matter comes before the State Corporation Commission of the State of Kansas ("Commission") on the Joint Motion for an Order Approving the Stipulation and Agreement filed by the Commission Staff ("Staff"), Greeley Gas Company, a division of Atmos Energy Corporation ("Greeley"), and the Citizens' Utility Ratepayers Board ("CURB"). Having examined its files and records, and being duly advised in the premises, the Commission finds as follows:

BACKGROUND

1. On April 18, 2001, Greeley filed its Application with the Commission in this docket seeking approval of an accounting order to permit Greeley to recover amounts necessary to expend in order to establish and maintain a gas ceiling price for the 2001-2002 heating season and for approval of Greeley's "Gas Hedge Program" tariff. Greeley contends that the creation of a ceiling price for certain quantities of natural gas purchased by Greeley for the 2001-2002 heating season will provide the possibility of avoiding the sort of price volatility experienced during the 2000-2001 winter. On April 19, 2001, CURB filed a petition seeking intervention. On April 26, 2001, The Commission entered a Suspension Order,

suspending operation of the proposed Application for 240 days, until December 14, 2001, pursuant to K.S.A. 66-117.

2. On May 14, 2001, Staff, Greeley and CURB entered into and filed a Stipulation and Agreement, together with their Joint Motion for an Order Approving Stipulation and Agreement. No hearing has been held on this matter.

3. In Docket No. 98-KGSG-475-CON, the Commission recently approved a Stipulation and Agreement per Kansas Gas Service Company's ("KGS") Gas Hedge Program and issued an accompanying Accounting Order. Staff, Greeley and CURB believe that the Gas Hedge Program described in the proposed Stipulation and Agreement in this docket is nearly identical to the program which the Commission recently approved for KGS. The Joint Movants state that ". . .the only differences between the two hedge programs are described in Paragraph 6 of the proposed Stipulation and Agreement."

4. Furthermore, to possibly take advantage of favorable market conditions that are time sensitive, whether there is a hearing or not, Greeley requests the proposed Stipulation and Agreement be approved on an expedited basis.

DISCUSSION

5. The parties stipulate and agree that the Gas Hedge Program and Accounting Order for Greeley shall be as follows:

A. The initial program budget for the 2001-2002 program year shall not exceed $1.4 million. The $1.4 million budget for Greeley is equivalent to the $7.3 million budget provided to Kansas Gas Service Company in terms of average monthly cost to each sales customer, i.e., $1.00 per month per sales customer, for the program year.

B. At this time, Greeley's preferred risk management strategy for the 2001-2002 program year shall be the purchase of straight call options for the purpose of establishing a "price cap". Alternative risk management strategies, such as call spreads, "call collars" (such as the purchase of a call and the sale of a put for the same time period), or similar financial strategies, are to be utilized for the 2001-2002 program only if market conditions develop in which the implementation of such risk management strategies appears to be more reasonable than the currently preferred method of establishing price protection for Greeley's customers. However, Greeley, Staff and CURB agree that Greeley management shall have discretion in selecting among the various risk management strategies that are available.

C. For the 2001-2002 program year, Greeley shall concentrate on managing the price risk for the months of December and January. However, depending on how market conditions develop, Greeley may extend price risk management to the months of November and February. As a preliminary objective, Greeley will attempt protecting sixty-five percent (65%) or more of the budgeted December and January flowing gas volumes before attempting to protect November and February flowing gas volumes.

D. Greeley shall recover the program costs for the 2001-2002 Gas Hedge Program from all of its sales customers through the PGA on a volumetric basis during the months of June 2001 through October 2001, and April 2002 through May 2002. Thus, for bill smoothing purposes, the cost of Greeley's Gas Hedge Program shall be recovered during the non-winter months. No carrying costs shall be allowed. Any over or under recovery, and any of the budget amount not used by Greeley, shall be reflected in Greeley's ACA filing in 2002. Greeley will itemize the volumetric charge attributable to its Gas Hedge Program on its customers' monthly bills.

E. Greeley shall file a monthly report, in a format agreed to by Staff, for the purpose of detailing the current and cumulative status of the program. Greeley shall meet with Staff and CURB each month either by phone or in person, or as otherwise requested, to discuss any program implementation issues. In these meetings, Greeley shall provide an explanation of its program implementation decisions, but particularly those decisions that pertain to the timing of purchases and/or sales of financial derivatives.

F. Greeley shall work with Staff and CURB during the 2001-2002 program year to develop a method by which to gauge customer acceptance for the Gas Hedge Program. In particular, Greeley shall work to develop a clearer understanding of its customers' willingness and ability to pay for the sort of risk management services that can be provided through the Gas Hedge Program. Greeley will also work with Staff and CURB to develop an appropriate program description for use in customer surveys or focus groups and for use in the general media.

FINDINGS AND CONCLUSIONS

6. Greeley is a certified public utility authorized to transact the business of a natural gas public utility within the state of Kansas. The proposed program and this application affect existing practices; therefore, the Commission has jurisdiction over this matter pursuant to K.S.A. 66-117, K.S.A. 66-1,200 *et seq.* and K.S.A. 66-104.

7. There is a strong policy in the law that settlements are to be encouraged. *Bright v. LSI Corp.*, 254 Kan. 853, 858, 869 P.2d 686 (1994). However, the Commission must make an independent judgment concerning whether the settlement is in the public interest and should be approved. In making this determination, the Commission takes into consideration the immediate and future impact upon consumers.

8. The requested Program and Tariff, as conditioned by the Stipulation and Agreement, is designed to and may likely act to mitigate against winter price volatility. Price volatility exposes consumers to unpredictable or extremely high gas bills, such as the price spikes experienced during the 2000-2001 winter heating season. The Commission anticipates the current price volatility in the natural gas market may still exist in the foreseeable future.

9. A Gas Hedge Program can afford consumers some measure of protection against such price volatility. The Commission concludes that such a Program, if properly operated and designed, may provide a reasonable means of protecting consumers against price spikes.

10. Under the Stipulation and Agreement in this docket, the gas purchasing practices of Greeley can be more effectively monitored by Staff, through more reporting and meetings between Staff, Greeley and CURB. Such additional reporting and information sharing will help Staff keep the Commission apprised of all program developments and the potential need for corrective action.

11. For these reasons, the Commission finds that the Stipulation and Agreement is reasonable and in the public interest. The Commission therefore approves and adopts the Stipulation and Agreement, which is attached hereto as Attachment A, and is hereby incorporated and made part of this Order by reference, and in accordance with the terms of that Stipulation and Agreement, hereby grants the Applicant's request for approval of an accounting order permitting Greeley gas to implement this program and recover such funds as may be necessary to establish and maintain it.

12. The general criteria governing intervention is set by statute and in the Commission's rules and regulations, specifically K.S.A. 77-521 and K.A.R. 82-1-225. These authorities provide the Commission great discretion regarding intervention, essentially allowing the Commission to grant intervention if it is determined that the request was made in the interest of justice and will not delay the orderly and prompt conduct of the proceeding. Further, K.S.A. 77-521 and K.A.R. 82-1-225 provide that: a) the intervenor's participation may be limited to designated issues in which the intervenor has a particular interest; b) the intervenor's use of discovery, cross-examination and other procedures may be limited so as to promote the orderly and prompt conduct of the proceedings; and c) two or more intervenors may be required to combine their presentations of evidence and argument, cross-examination, discovery and other participation in the proceedings.

14. The Commission finds that CURB properly filed its Petition to intervene and stated facts

demonstrating that its legal interests may be substantially affected by this proceeding. Therefore, the Commission grants full intervention to CURB, which is reminded that the Commission may, at any time, limit its participation in this proceeding, including the use of discovery, cross-examination and other procedures so as to promote the orderly and prompt conduct of this proceeding.

IT IS THEREFORE, BY THE COMMISSION ORDERED:

A. The Parties' Joint Motion is hereby granted and the Stipulation and Agreement is hereby approved and incorporated in this Order by reference.

B. Greeley Gas Company's Application for approval of an accounting order and Gas Hedge Program tariff is hereby approved, as conditioned by the terms of the Stipulation and Agreement

C. The petition to intervene filed by CURB is hereby granted pursuant to K.S.A. 77-521 and K.A.R. 82-1-225.

D. A party may file a petition for reconsideration of this order within 15 days of service. If the order is served by mail, three (3) days are added to the above time period.

E. The Commission retains jurisdiction of the subject matter and parties for the purpose of entering such further order or orders as it may deem necessary.

BY THE COMMISSION IT IS SO ORDERED.

Dated: MAY 23 2001

Wine, Chair; Claus, Com.; Moline, Com.

ORDER MAILED

Jeffrey Wagaman
EXECUTIVE DIRECTOR MAY 24 2001

Jeffrey S. Wagaman Executive Director

TMN

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

MODIFICATION TO WESTERN KENTUCKY GAS COMPANY, A DIVISION OF ATMOS ENERGY CORPORATION, GAS COST ADJUSTMENT TO INCORPORATE AN EXPERIMENTAL PERFORMANCE-BASED RATEMAKING MECHANISM	)	CASE NO. 1997-513

ORDER

On April 2, 2001, Western Kentucky Gas Company ("Western") filed a motion requesting approval to extend its experimental gas procurement Performance-Based Ratemaking mechanism ("PBR") for nine months, through March 31, 2002, and approval of an experimental gas procurement financial hedging program that would involve purchasing call options to cover approximately 25 percent of its gas supply requirements for the months of November 2001 through March 2002. Representatives of Western, the Attorney General ("AG") and Commission Staff ("Staff") met in two informal conferences to discuss the motion and related issues. Western also provided written responses to data requests made by the AG and Staff at the conferences.

On May 8, 2001, the AG filed comments on Western's motion indicating he had no objection to the extension of the PBR but that he did object to the proposed hedging program. The AG based his objection to the hedging program on his opposition to Western's proposal that ratepayers would bear 100 percent of the costs of the hedging program even though there was no assurance that ratepayers would realize any savings under the program. Western filed reply comments on May 14, 2001, wherein it proposed to eliminate the "shared savings" provision of its original proposal, meaning ratepayers would receive 100 percent of the program's savings as well as bear 100 percent of the program's costs.

On May 25, 2001, Western modified its proposal making futures contracts rather than call options the preferred hedging instrument. The AG filed comments on the modified proposal on May 30, 2001, restating his objections to ratepayers bearing 100 percent of the costs of the program and requesting that the matter be submitted to the Commission. Western supplied further information on June 5, 2001 in response to a May 31, 2001 information request from Commission Staff. No additional comments have been received from the AG.

PROPOSAL

Under its original proposal Western would have used call options exclusively as the hedging instrument for 25 percent of its normal winter supply requirements for the period from November 2001 through March 2002. Western also proposed that, through its PBR, it would share 50/50 in any net savings realized under the program. Western estimated transaction and premium costs for its call option proposal to be $4.9 million, or approximately one dollar per Mcf, based on purchasing options to cover 25 percent of its winter supply requirements. Western also requested approval to extend its experimental PBR beyond the scheduled June 30, 2001 termination date through March 2002. Western requested that the extension coincide with the end of the proposed hedging program. It also desired to postpone any negotiations with natural gas suppliers until after the upcoming heating season and to continue the pilot PBR during the time it will be under review by the Commission, such review to begin in September 2001, upon the filing by Western of its report on the 3-year PBR pilot.[1]

Western modified its proposed hedging program to use futures contracts as the preferred hedging instrument, with the estimated transaction costs being approximately $236,000, or 5 cents per Mcf. Western indicated that the switch from options to futures contracts was driven by recent price decreases in the wholesale natural gas market and the knowledge that futures prices have recently been less volatile than they were at the time it filed its original hedging proposal. Under the modified proposal ratepayers would bear 100 percent of the costs and receive 100 percent of any net savings.

Western indicated that the transactions envisioned under its modified hedging program would qualify as cash flow hedges in that it will protect against the risk of increasing natural gas prices.[2] In addition, Western stated that the contemplated contracts would meet the accounting requirements in the Financial Accounting Standards Board's Statement of Financial Accounting 133 ("SFAS 133"), Accounting for Derivative Instruments and Hedging Activities.[3] It identified the accounts it would use to record the transactions related to the hedging program and provided examples of the

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[1] During the term of its experimental PBR Western's gas procurement function has been contracted to an outside party, initially, Reliant Energy, and currently, Woodward Marketing, LLC ("Woodward") under the terms of a contract that runs for the length of the PBR pilot. Western also indicated it would use Woodward as the broker to purchase futures contracts.

[2] June 5, 2001 Response to Commission Staff's Data Request dated May 31, 2001, Item 8.

[3] <u>Id.</u>, Item 7.

accounting entries it would make at the inception of the transactions, at monthly intervals to reflect market price changes, and at closing when net settlement occurs.[4]

DISCUSSION

Western's proposal raises fundamental policy issues for the Commission's consideration. In Administrative Case No. 297[5] the Commission addressed numerous issues associated with its regulation of retail natural gas utility service and found that local distribution companies ("LDCs"), such as Western, should have the objective of acquiring gas at "market clearing prices." We note that Western has engaged in gas procurement strategies specifically for the purpose of accomplishing that objective. This policy worked well when prices were relatively stable. However, the experiences of this past winter and the resulting increases in wholesale natural gas prices have led utility commissions and LDCs across the country to examine current policies and procedures in order to ensure that regulatory oversight continues to be responsive to the current marketplace and to the LDCs' abilities to adequately manage their natural gas portfolios.

One aspect of an LDC's natural gas portfolio is the development of price mitigation strategies. These strategies are becoming increasingly important in minimizing the potential for price spikes similar to this past December and January when prices approached, and then exceeded, $10.00 per MMBTU. It is this experience, viewed in light of last summer's price forecasts for this past winter and the current price

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[4] Id., Item 6.

[5] Administrative Case No. 297, An Investigation of the Impact of Federal Policy on Natural Gas to Kentucky Consumers and Suppliers, Order dated May 29, 1987.

level prices will actually reach this winter.[7] Summer weather, with its impact on the demand for gas-fired electric generation, price fluctuations in other fuel markets, notably the international crude oil market, and late autumn and early winter temperatures that might influence temperature expectations for the primary heating season months, are three uncontrollable factors that influence natural gas prices. While expectations for the future are uncertain, recent experience can be useful for the purpose of analyzing possible future scenarios. We recognize there is no certainty that last winter's prices will be repeated this winter; however, the Commission takes notice of the fact that, had Western's modified "futures contracts" program been in place this past heating season, savings of several million dollars in gas costs would have been realized in exchange for less than $250,000 in transactions costs to implement the program.[8]

A hedging program can be viewed in a manner similar to an automobile liability insurance policy. The costs incurred in conjunction with a hedging program are somewhat comparable to premiums paid for an insurance policy. The premium is paid for the insurance policy in order to mitigate the exposure to financial risk in the event of an accident. In a hedging program, costs are incurred in order to mitigate exposure to the risk that wholesale natural gas prices might increase to exorbitant levels. Since an LDC cannot exert control over market prices, it can expect to recover the cost incurred for natural gas purchases so long as those costs reflect market clearing prices.

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[7] We note that in June of 2000 there were no predictions that prices would reach the levels of $9.00 and $10.00 per MMBTU that were reached in the 2000-2001 winter.

[8] Under the Gas Cost Adjustment mechanism contained in Western's tariffs, 100 percent of those reduced gas costs would have been passed on to ratepayers.

consistent with the Commission's finding in Administrative Case No. 297. If the LDC is able to recover 100 percent of the cost of gas acquired at market clearing prices, then ratepayers are bearing 100 percent of the risk attendant to allowing the LDC such cost recovery. Likewise, ratepayers, not the LDC, should be the beneficiaries of the hedging program, since the risk that is mitigated is risk otherwise borne by the ratepayers. Inasmuch as ratepayers will be the beneficiaries of the proposed hedging program, it is entirely appropriate and reasonable that they bear the full amount of the costs of the program.

The Commission will grant Western's request to extend its experimental PBR for 9 months beyond the 3-year pilot period scheduled to end June 30, 2001.[9] Western indicated its desire to maintain the same type of certainty regarding the manner in which its gas procurement activities will be evaluated during the time its proposed hedging program will be in effect. As stated previously, Western has relied on an outside party to manage its gas procurement functions during the term of its experimental PBR and has indicated it will use the current outside party, Woodward, as its broker for purchasing futures contracts under its proposed hedging program. The Commission also desires certainty regarding the continuation of Western's PBR in conjunction with its hedging program and does not desire that Western's gas procurement be performed any differently during the PBR extension than it was during the 3-year PBR pilot. This certainty is also a matter of particular interest in regard to the requirements of SFAS 133 and the potential repercussions if there were any question about the nature of the

[9] The AG did not object to Western's requested extension of its experimental PBR.

hedging instruments Western intends to utilize. Therefore, we will condition approval of the pilot hedging program and the PBR extension on the requirement that Western obtain an extension of its existing gas supply arrangement with Woodward that will run concurrently with the PBR extension and the hedging program.

This, the first hedging program approved by the Commission, is a pilot program and it will serve to further assist the Commission in its efforts to ensure its policies and procedures are adequate for current regulatory and market environments. As such, we find that certain information will be necessary in order for the Commission to review the program and evaluate its effectiveness in consideration of whether additional hedging programs by Western, or other LDCs, might be appropriate at some time in the future. Therefore, we will require that Western file with the Commission, by no later than November 15, 2001, an interim report on any hedging activity in which it engages between now and the November 1, 2001 beginning of the upcoming heating season. This report should identify each futures contract, the date of the transaction, the cost of the transaction, the futures price reflected in the contract and include the accounting entries made by Western to record the hedging transactions. The report should also include a brief narrative discussion of the factors that influenced Western's purchasing decisions, including, but not limited to: (1) futures prices at the time of purchasing decisions; (2) market price trends at the time of purchasing decisions; (3) market price forecasts at the time of purchasing decisions; and (4) nationwide storage levels, and Western's own on-system storage levels, at the time of purchasing decisions. We will also require that Western file a final report on its hedging program by no later than April 15, 2002, which identifies any gas cost savings realized under the hedging program and

IT IS THEREFORE ORDERED that:

1. Western's experimental PBR is extended through March 31, 2002 on the condition that Western extend its contract with Woodward for the same time period.

2. Western's revised pilot hedging program for the 2001-2002 heating season is approved.

3. Western shall file an interim hedging report as described herein no later than November 15, 2001.

4. Western shall file a final hedging report as described herein no later than April 15, 2002.

Done at Frankfort, Kentucky, this 15th day of June, 2001.

By the Commission

ATTEST:

Executive Director

United Cities Gas Company,
A Division of Atmos Energy Corporation

State of Tennessee

TRA Docket No. 01-00510
Data Request #9

Basic Accounting for Hedge Program

All costs associated with the Hedge Program would be deferred in a separate account within the Balance Sheet 1910-29000, until such time as the final determination of the hedge is completed. Any gain or loss from the Hedge program would then be closed out to 1910-14088 Over(Under) Gas Recoveries.

Based on Example B—High Price Scenario:

Financial Hedge for 970,000 at Futures Contract Price of $5.00, cost of $.05 per MMBtu.

DR 1910-29000 Deferred Hedge Costs 48,500

CR 1310-10409 Cash
48,500

Record cost of the Future Contracts-carrying cost

Record Gas Purchases 1,933,000 @ market $7.00

DR 1910-14088 Over(Under) Gas Recoveries 13,531,000
CR 2320-21001 AP Trade 13,531,000

Record PBR

DR 1910-14087 PBR 155,000
CR 4210-30607 Misc Income_PBR 155,000

Record Hedge Gain

DR 2320-21001 AP Trade 1,940,000
CR 1910-29000 Deferred Hedge Costs
1,940,000

Close Out Hedge

DR 1910-29000 Deferred Hedge Costs 1,891,500

CR	1910-14088	Over(Under) Gas Recoveries	1,891,500

The same basic JE's would be required if their was a loss on the Hedge program, the only difference being the amounts closed out from the Deferred Hedge account into Over(Under) Gas Recoveries.

BEFORE THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE

IN RE: PETITION OF UNITED CITIES GAS COMPANY FOR EXPEDITED APPROVAL OF AUTHORITY TO PURCHASE FUTURES CONTRACTS FOR THE WEATHER HEATING SEASON OF 2001-02 ON AN EXPERIMENTAL BASIS	)	DOCKET NO. 01-00510

June 14, 2001 Response to Data Request Dated June 13, 2001
and June 18, 2001 Response to Data Request Dated June 15,2001

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