COMPLIANCE AUDIT REPORT
of the
ACTUAL COST ADJUSTMENT COMPONENT
of the
PURCHASED GAS ADJUSTMENT RULE
for
CHATTANOOGA GAS COMPANY

Docket No. 01-01010

Prepared by:

THE ENERGY AND WATER DIVISION
of the
TENNESSEE REGULATORY AUTHORITY

April 2002

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I. INTRODUCTION

The subject of this audit is Chattanooga Gas Company's (hereafter the "Company" or "Chattanooga") compliance with the Actual Cost Adjustment and Refund Adjustment of the Purchased Gas Adjustment Rule (hereafter "PGA") of the Tennessee Regulatory Authority (hereafter the "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 (hereafter "ACA") as more fully described in section V., for the year ended June 30, 2001, were calculated correctly and were supported by appropriate source documentation.

II. AUDIT OPINION AND RECOMMENDATION

The Company submitted its ACA filing on October 29, 2001. The Staff appreciates the timely filing of the ACA report this year as opposed to last year. After review of the ACA filing, there were only two findings of significance, an improvement over last year.

The Staff's audit resulted in two (2) exceptions for the current ACA period as detailed in Section VII. The **net under-recovery of $56,995.98** increased the Company's net under-recovered balance in the ACA Account by this amount. **The corrected net balance in the Deferred Gas Cost Account should be $2,639,263.01.** Based on our review, we conclude that for the current ACA filing period the Purchased Gas Adjustment mechanism as calculated in the Actual Cost Adjustment is working properly and in accordance with the TRA's rules.

III. BACKGROUND INFORMATION ON COMPANY

Chattanooga Gas Company, located at 6125 Preservation Drive in Chattanooga, Tennessee, is a wholly owned subsidiary of Atlanta Gas Light Company, which has its main office at 1251 Caroline St. N.E., Atlanta, Georgia. As a local distribution company (hereafter "LDC") Chattanooga Gas provides service to customers in Chattanooga and Cleveland, Tennessee, and environs in Hamilton and Bradley Counties in Tennessee, respectively. The natural gas used to serve these areas is purchased from three natural gas pipelines in accordance with separate and individual tariffs approved by the Federal Energy Regulatory Commission. The three interstate pipelines are Tennessee Gas Pipeline, East Tennessee Natural Gas, and Southern Natural Gas.

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 (hereafter the "Authority" or "TRA"). T.C.A. § 65-4-104 states:

> The Authority shall have 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. has 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 said power includes the right to audit:

> The department is given full power to examine the books and papers of the said companies, and to examine, under oath, the officers, agents, and employees of said companies... to procure the necessary information to intelligently and justly discharge their 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. David McClanahan and Pat Murphy of the Energy and Water Division conducted this audit.

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 the Company to recover, in a timely fashion, the total cost of gas purchased for delivery to its customers and to assure that the 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 (hereafter the "ACA")**
2. **The Gas Charge Adjustment (hereafter the "GCA")**
3. **The Refund Adjustment (hereafter the "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 the customer 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 of this Report.

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 Adjustment Account shall be deemed in compliance with the provisions of this Rule. 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:

At the September 11, 2001 Authority Conference, the Directors voted to approve a Performance-Based Ratemaking Mechanism for Chattanooga. As part of the tariff, the Company established a benchmark to compare its gas purchases against. If it meets the criteria established, the Company is released from having to undergo a prudency review by an independent consultant for that plan year. Chattanooga Gas Company was able to avoid a prudency review during this period because of adherence to the benchmark.

VI. SCOPE OF ACA AUDIT

Background:

The Staff's audit of Chattanooga's Deferred Gas Cost Account for the ACA period July 1, 2000 through June 30, 2001 resulted in two (2) exceptions, the net effect of which increased the under-recovered balance in the account by $56,995.98. The Company is to be commended for its improvement in the calculation of their ACA.

Audit Scope:

The Staff summarized the balance in the Deferred Gas Cost Account (hereafter "ACA Account") at June 30, 2001, as follows:

Beginning Balance @ 6/30/00	$ 2,216,335
Activity during year ended 6/30/01:	
Gas Purchases	79,249,512
Gas Recoveries	(79,063,995)
Interest accrued during year ended 6/30/01	237,411
ENDING BALANCE @ 6/30/01	$ 2,639,263

We performed an in-house audit to ascertain that the Company's calculations of gas costs incurred and recovered were correct. The results of our audit showed an under-recovery in the ACA Account of $56,995.98. Details of the ACA Account and the Staff's findings can be found in Section VII.of this report.

We also audited a sample of customer bills to determine if the proper PGA rates were being applied in the Company's calculation of the customers' bills. Since the Company's billing process is computerized, we tested a sample of 68 bills. These bills were selected to be representative of the residential, commercial, industrial and interruptible customers in the Company's service area. The sample was selected from the twelve-month period of July 1, 2000, through June 30, 2001. After recalculating each sample bill, we determined that the calculation methods utilized by the Company are correct.

VII. ACA FINDINGS

As mentioned in Section II above, the result of the Staff's audit was a **net under-collection of $56,995.98** which had the effect of increasing the Company's under-recovered 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 6/30/00	$ 2,216,335.06	$ 2,216,335.06	$ 0
Plus Gas Costs	79,196,147.62	79,249,511.66	53,364.04
Minus Recoveries	79,063,995.08	79,063,995.08	0
Ending Balance before Interest	2,348,487.60	2,401,851.64	53,364.04
Plus Interest	233,779.43	237,411.37	3,631.94
Ending Balance at 6/30/00	$ 2,582,267.03	$ 2,639,263.01	$ 56,995.98

The above-corrected balance in the ACA Account shows a difference of $56,364.04 under-recovery in the Commodity portion, and $3,631.94 under-recovery of interest.

SUMMARY OF FINDINGS:

FINDING # 1	Pipeline failed to bill CNG for withdrawal Of 17,878 dth in October 2000.	$ 53,364.04	under-recovery
FINDING # 2	Interest recalculation resulting from #1	3,631.94	under-recovery
	Net Result	**$ 56,995.98**	**under-recovery**

FINDING #1:

Exception:

The Staff calculated an **under-recovery of $53,364.04** in invoiced gas costs.

Discussion:

The Pipeline failed to bill Chattanooga Gas Company for the withdrawal of 17,878 dth in October 2000. Please refer to your response to question #3 on our Data Request #2. Therefore, an adjustment (17,878 dth X $2.9849) will need to be made.

Company Response:

The Company is in agreement with this finding.

FINDING #2:

Exception:

The Staff calculated an **under-recovery of $3,631.94** in interest on the above adjustment.

Discussion:

The Staff recalculated interest based on Finding # 1.

Company Response:

The Company is in agreement 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.