BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

April 4, 2003

IN RE:

CHATTANOOGA GAS COMPANY ACTUAL COST ADJUSTMENT AUDIT	)))Docket No. 02-00929)

NOTICE OF FILING BY THE 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 hereby gives notice of its filing of the Compliance Audit Report of the Actual Cost Adjustment Audit (hereafter "ACA") component of the Purchased Gas Adjustment Rule for Chattanooga Gas Company 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 ACA audit of Chattanooga Gas Company (the "Company").

2. The Company's ACA filing was received on August 30, 2002, and the Staff completed its audit of same on March 21, 2003.

3. On March 28, 2003, the Energy and Water Division issued its preliminary ACA audit findings to the Company, and on April 1, 2003 the Company responded thereto.

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

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:

Pat Murphy

Pat Murphy
Energy and Water Division of the
Tennessee Regulatory Authority

CERTIFICATE OF SERVICE

I hereby certify that on this 4th day of April, 2003, 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:

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

Docket No. 02-00929

Prepared by:

THE ENERGY AND WATER DIVISION
of the
TENNESSEE REGULATORY AUTHORITY

April 2003

EXHIBIT A

COMPLIANCE AUDIT REPORT
of the
ACTUAL COST ADJUSTMENT COMPONENT
of the
PURCHASED GAS ADJUSTMENT RULE
for
CHATTANOOGA GAS COMPANY
for the Year ended June 30, 2002

Docket No. 02-00929

TABLE OF CONTENTS

		Pages
I.	INTRODUCTION	1
II.	AUDIT OPINION	1
III.	SUMMARY OF COMPANY FILING	1
IV.	BACKGROUND INFORMATION ON COMPANY	2
V.	JURISDICTION OF THE TENNESSEE REGULATORY AUTHORITY	2
VI.	DESCRIPTION OF PURCHASED GAS ADJUSTMENT RULE	3
VII.	SCOPE OF ACA AUDIT	4
VIII.	ACA FINDINGS	5

I. INTRODUCTION

The subject of this audit is Chattanooga Gas Company's ("Company," "Chattanooga," or "CGC") 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 VI., for the year ended June 30, 2002, were calculated correctly and were supported by appropriate source documentation.

II. AUDIT OPINION

The Staff concludes that 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 Chattanooga Gas Company. The findings contained herein are not material with respect to the Company's total gas costs.

III. SUMMARY OF COMPANY FILING

The Company made its Actual Cost Adjustment filing for its Tennessee service area on August 30, 2002. This ACA filing showed $44,885,354 in total gas costs, with $38,449,098 being recovered from customers through rates. Adding a beginning balance in the Deferred Gas Cost account ("ACA account") of positive $2,639,263 in under-recovered gas costs from the preceding ACA period and interest due to customers for the current period of $353,580 resulted in an ACA balance at June 30, 2002 of positive $9,429,099 in under-recovered gas costs. The Company's filing is summarized below:

CHATTANOOGA GAS COMPANY
ACA FILING FOR PERIOD JULY 2001-JUNE 2002

Line		
1	Beginning Balance (July 2001)	$ 2,639,263.01
2	Purchased Gas Costs	44,885,353.62
3	Gas Costs recovered through rates	38,449,098.09
4	Interest on monthly balances	353,579.98
5	Ending Balance (June 2002) (Line 1 + Line 2 – Line 3 + Line 4)	$9,429,098.52

The Company began surcharging its customers October 1, 2002, to recover the balance in the ACA account as of June 30, 2002. The Staff's findings resulting from this audit are described in detail in Section VIII of this report.

IV. 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.

V. 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. Pat Murphy and Butch Phillips of the Energy and Water Division conducted this audit.

VI. 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:

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. At its September 11, 2001 Authority Conference, the Directors voted to approve a Performance-Based Ratemaking Mechanism for Chattanooga (Docket No. 01-00619). The mechanism affects all plan years ending after June 30, 2000 and continues each year unless terminated by the Company or the Authority. For each year that the mechanism is in effect, if CGC's total commodity gas purchases are less than 1% above the total annual benchmark, its purchases are deemed prudent and the requirements of Section 1220-4-7-.05 of the PGA Rule is waived.

VII. SCOPE OF ACA AUDIT

The ACA audit is a limited compliance audit of the Company's ACA account. The audit goal was to verify that the Company's calculations of gas costs incurred and recovered were materially correct,[1] and that the Company is following all Authority orders and directives with respect to its calculation of the ACA account balance. Also included in this audit is the Company's PGA filing implementing a customer surcharge of the ACA account balance, effective October 1, 2002. Refer to the ACA Account detail provided in Section III, Summary of Company Filing.

To accomplish the audit goal, Staff reviewed gas supply invoices, as well as supplemental schedules and other source documentation provided by Chattanooga. Where appropriate, Staff requested additional information to clarify the filing. Staff 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 twelve month audit period. Since the Company's billing process is computerized, a sample of 68 bills was tested. These bills were selected to be representative of the residential, commercial, industrial and interruptible customers. After recalculating each sample bill, Staff determined that the Company's calculation methods are correct.

[1] The audit goal is not to guarantee that the Company's results are 100% correct. Where it is appropriate, Staff utilizes sampling techniques to determine whether the Company's calculations are materially correct. Material discrepancies would dictate a broadening of the scope of Staff's review.

VIII. ACA FINDINGS

Staff's audit resulted in findings totaling a **net under-recovery of $5,564.77.** This amount is the net total of three (3) findings and represents an additional under-recovered amount, which when added to the Company's calculated balance, results in an ending balance in the ACA account of a **positive $9,434,663.28 in under-recovered gas costs**. A summary of the ACA account as filed by the Company and as adjusted by the Staff is shown below, followed by a description of each finding.

SUMMARY OF THE ACA ACCOUNT:

	Company	Staff	Difference (Findings)
Beginning Balance at 6/30/01	$ 2,639,263.01	$ 2,639,263.01	$ 0.00
Plus Gas Costs	44,885,353.62	44,890,765.31	5,411.69
Minus Recoveries	38,449,098.09	38,449,098.09	0.00
Ending Balance before Interest	$ 9,075,518.54	$ 9,080,930.23	$ 5,411.69
Plus Interest	353,579.98	353,733.06	153.08
Ending Balance at 6/30/02	$ 9,429,098.52	$ 9,434,663.28	$ 5,564.77

The above corrected balance in the ACA Account shows a difference of $5,411.69 under-recovery in the Commodity portion, and $153.08 under-recovery of interest.

SUMMARY OF FINDINGS:

FINDING #1	Inventory Injections/Withdrawals	$5,519.15	Under-collection
FINDING #2	Commodity purchases	107.46	Over-collection
FINDING #3	Interest on account - commodity	153.08	Under-collection
	TOTAL	**$$5,564.77**	**Under-collection**

FINDING #1:

Exception:

The Staff calculated an **under-recovery of $5,519.15** in the cost of inventory injections and withdrawals.

Discussion:

In calculating its cost of inventory injections and withdrawals for December 2001 and inventory injections for February and March 2002, the Company failed to net the volumes injected or withdrawn with the fuel loss volumes for one inventory account. The result was a net under-collection of $5,519.15.

Company Response:

Chattanooga Gas Company concurs and will make the necessary adjustments to the Deferred Gas Cost Account.

FINDING #2:

Exception:

The Staff calculated an **over-recovery of $107.46** in commodity purchases.

Discussion:

In matching the injection and withdrawal volumes on the inventory schedules with the appropriate pipeline invoices, Staff noted some variances. In two (2) instances, these variances were related to pipeline invoice volumes that applied to Sequent Energy Management[2] activity and not CGC activity. Therefore, the injection and withdrawal charges charged by the pipeline regarding these volumes should not be charged to Chattanooga customers. The net of these charges is an over-collection of $107.46.

Company Response:

Chattanooga Gas Company concurs and will make the necessary adjustments to the Deferred Gas Cost Account.

[2] Sequent Energy Management is an affiliate of Atlanta Gas Light Company. Sequent purchases gas on behalf of Chattanooga Gas.

FINDING #3:

Exception:

The Staff calculated an **under-recovery of $153.08** in the interest due from customers on the monthly account balance.

Discussion:

Staff recalculated the interest on account after making the corrections detailed in Findings #1 and #2.

Company Response:

Chattanooga Gas Company concurs and will make the necessary adjustments to the Deferred Gas Cost Account.

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.