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BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

October 27, 2003

IN RE:	)
	)
NASHVILLE GAS COMPANY	) **Docket No. 03-00317**
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 hereby gives notice of its filing of the Compliance Audit Report of the Actual Cost Adjustment (hereafter "ACA") Component of the Purchased Gas Adjustment Rule for Nashville Gas Company (hereafter the "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 audit of the Company's ACA filing for the period January 2002 through December 2002.

2. The Company's ACA filing was received on May 2, 2003, and the TRA Staff completed its audit of same on October 15, 2003.

3. On October 16, 2003, the Energy and Water Division issued its preliminary ACA audit findings to the Company and on October 23, 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 (the "Report") resulted therefrom. The Report is attached hereto as Exhibit A 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:

Pat Murphy
Pat Murphy
Energy and Water Division of the
Tennessee Regulatory Authority

CERTIFICATE OF SERVICE

I hereby certify that on this 27th day of October, 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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Chairman
Tennessee Regulatory Authority
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EXHIBIT A

COMPLIANCE AUDIT REPORT

OF

<u>Nashville Gas Company</u>

<u>ACTUAL COST ADJUSTMENT</u>

DOCKET NO. 03-00317

PREPARED BY

<u>TENNESSEE REGULATORY AUTHORITY</u>

ENERGY AND WATER DIVISION

October 2003

COMPLIANCE AUDIT

NASHVILLE GAS COMPANY

ACTUAL COST ADJUSTMENT

DOCKET NO. 03-00317

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I. INTRODUCTION

The subject of this audit is Nashville Gas Company's ("Company" or "NGC") 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")[1], for the twelve (12) months ended December 31, 2002, were calculated correctly and were supported by appropriate source documentation.

II. AUDIT OPINION

On May 2, 2003, Staff received NGC's ACA filing supporting the activity in its deferred gas cost account ("ACA account") for the period January 1, 2002 through December 31, 2002. The Company filed a PGA on March 12, 2003, effective April 1, 2003, implementing a rate adjustment to distribute the balance reflected in the ACA account to the various rate classes. This ACA filing showed $77,832,330 in total gas costs, with $80,512,441 being recovered from customers through rates. Adding a beginning balance in the ACA account of $1,948,626 in over-collected gas costs from the preceding ACA period and interest due to customers for the current period of $172,364 resulted in an ACA balance at December 31, 2002 of **$4,801,101 in over-recovered gas costs.**[2] The Company began refunding this amount to its customers on April 1, 2003.

Staff's audit resulted in five (5) findings.[3] The net amount of these findings is **$103,298 in additional unrecovered gas costs**. Therefore, the Company's reported December 31, 2002 balance of $4,801,101 in over-collected gas costs is reduced by this amount. The corrected balance in the ACA account is **$4,697,803 in over-recovered gas costs.** The amount of the Company's errors represent less than one percent of its total gas invoices, and is therefore immaterial by comparison. Therefore, Staff concludes that except for the findings noted in this report, NGC is correctly implementing its Purchased Gas Adjustment Rider as calculated in the Actual Cost Adjustment, in accordance with the TRA rules for Nashville Gas Company.

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[1] The ACA is more fully described in Section V.
[2] A summary of the ACA account can be found in Section VII.
[3] Refer to Section VII for a description of the findings.

III. BACKGROUND INFORMATION ON COMPANY AND GAS SUPPLIERS

Nashville Gas Company, with headquarters at 665 Mainstream Drive, Nashville, Tennessee, is an operating division of Piedmont Natural Gas Company, which has its headquarters at 1915 Rexford Road, Charlotte, North Carolina. NGC is a gas distributor that provides service to several communities in the Middle Tennessee area. The natural gas used to serve these areas is purchased from producers and marketers and transported to Nashville's city gate through the interstate transmission facilities of Tennessee Gas Pipeline (TGP), Columbia Gas Transmission Corporation (CGTC), and Texas Eastern Gas Pipeline (TETCO).

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 energy and water utilities under the Authority'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 David McClanahan 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 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 Adjustment 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 96-00805, Nashville Gas was authorized to operate under a Performance-Based Ratemaking Mechanism ("PBR"), beginning July 1, 1998, 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 ACA audit is a limited compliance audit of NGC's ACA account. The audit goal was to verify that the Company's calculations of gas costs incurred and recovered were materially correct,[4] 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 refund of the ACA account balance at December 31, 2002, effective April 1, 2003. Refer to the ACA Account detail provided in Section VII Summary of ACA Account.

To accomplish the audit goal, Staff reviewed gas supply invoices, as well as supplemental schedules and other source documentation provided by the Company. Where appropriate, Staff requested additional information to clarify the filing.

The Company submitted its ACA filing on May 2, 2003. On October 3, 2003, the TRA Staff requested an extension of the 180 days notification period to November 10, 2003 and the Company agreed. An extension was needed in order that the Staff would have sufficient time to complete the audit.

[4] 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.

VII. ACA AUDIT FINDINGS

The result of the Staff's audit was a **net under-recovery of $103,298,** which had the effect of decreasing the Company's over-recovery balance in the ACA account by this amount. A summary of the 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:[5]

	Company	Staff	Difference (Findings)
Beginning Balance at 01/01/02	$ -1,948,626	$ -1,948,626	$ 0
Plus Gas Costs	77,832,330	77,930,936	98,606
Minus Recoveries	80,512,441	80,512,527	86
Ending Balance before Interest	$ -4,628,737	$ -4,530,217	$ 98,520
Plus Interest	-172,364	-167,586	4,778
Ending Balance at 12/31/02	$ -4,801,101	$ -4,697,803	$ 103,298

SUMMARY OF FINDINGS:

				See page
FINDING #1	Columbia Inventory Withdrawals	$ 267	Under-recovery	6
FINDING #2	CNG Inventory Withdrawals	285	Under-recovery	7
FINDING #3	Bear Creek Inventory Withdrawals	98,054	Under-recovery	8
FINDING #4	ACA Surcharges/Refunds	-86	Over-recovery	9
FINDING #5	Interest on the above findings	4,778	Under-recovery	10
	Net Result	**$103,298**	**Under-recovery**	

[5] A negative number represents an over-recovery (or over-collection) of gas costs.

FINDING #1:

Exception

Columbia-WS/FSS Inventory withdrawals for January 2002 were understated by $267.

Discussion

The December 2001 withdrawal rate of $4.1377 was applied to the January withdrawal volumes in error. The correct January 2002 rate should have been $4.1406. This calculation error resulted in a $267 under-recovery in the Commodity portion of the ACA.

Company Response

The Company agrees with this finding.

FINDING #2:

Exception

CNG-GSS Inventory withdrawals for January 2002 were understated by $285.

Discussion

The December 2001 withdrawal rate of $4.4329 was applied to the January withdrawal volumes in error. The correct January 2002 rate should have been $4.4373. This calculation error resulted in a $285 under-recovery in the Commodity portion of the ACA.

Company Response

The Company agrees with this finding.

FINDING #3:

Exception

Bear Creek Inventory withdrawals for January 2002 were understated by $98,054.

Discussion

In calculating the January 2002 withdrawals, the Company made two errors. The first error involved applying the withdrawal rate to the net withdrawal volumes instead of the gross withdrawal volumes, which resulted in a $56,560 understatement. The second error pertained to the withdrawal rate used. The withdrawal rate used in the calculation had not been updated for the effect of the January injections, which resulted in a $41,494 understatement.

Company Response

The Company agrees with this finding.

FINDING #4:

Exception

The ACA refunds were overstated in January 2002 and February 2002.

Discussion

The volumes billed to customers in the rate schedules 331, 341, 371, 372 did not tie to the Company provided billing information for these customers. The refund volumes were overstated, which led to an over-recovery of $44 in January and $42 in February.

Company Response

The Company agrees with this finding.

FINDING #5:

Exception

The Staff calculated additional interest due from customers of $4,778 based on the above findings.

Discussion

The Company used the correct interest rates; however, based on the above findings, interest was recalculated in the period in which the errors occurred.

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.