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November 4, 2004

VIA HAND DELIVERY
Pat Miller, Chairman
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, Tennessee 37219

Re: Petition of Chattanooga Gas Company for Approval of Adjustment of its Rates and Charges and Revised Tariff
Docket Number 04-00034
Petition for Reconsideration

Dear Chairman Miller,

Enclosed you will find the original and 13 copies of Chattanooga Gas Company's Petition for Reconsideration of the Authority's October 20, 2004 Order in the above referenced docket. The Company respectfully requests that its Petition be granted for the reasons set forth in the Petition.

Sincerely,

D. Billye Sanders

D. Billye Sanders
Attorney for Chattanooga Gas Company

cc: Parties of Record
Steve Lindsey
Archie Hickerson
Elizabeth Wade, Esq.
Jeff Brown, Esq.

1062859 1

BEFORE THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE

IN RE:	)	
	)	
PETITION OF CHATTANOOGA GAS	)	
COMPANY FOR APPROVAL OF	)	DOCKET NO. 04-00034
ADJUSTMENT OF ITS RATE AND	)	
CHARGES AND REVISED TARIFF	)	
	)	
	)	

PETITION FOR RECONSIDERATION

Chattanooga Gas Company ("CGC") respectfully petitions the Tennessee Regulatory Authority ("TRA" or "Authority") for Reconsideration of its October 20, 2004 Order in the above-referenced docket (the "Order"), pursuant to TCA §4-5-317 and TRA Rule 1220-1-2.20 because the Authority's decision regarding the fair rate of return set forth in the Order is: (1) in violation of constitutional and legal provisions; (2) arbitrary and capricious; (3) made upon unlawful procedure; and (4) unsupported by evidence which is both substantial and material in light of the entire record. In support of its Petition for Reconsideration, CGC states the following:

I. INTRODUCTION

The extremely low rate of return adopted in the Order violates the standards set forth by the U.S. Supreme Court in *Bluefield Water Works & Improvement Co. v Public Service Comm'n of West Virginia*, 262 U.S. 679 at 692-93, 43 S.Ct. 675 (1923) and *FPC v. Hope Natural Gas Co.*, 320 U.S. 591 at 605, 64 S.Ct. 281 (1944) in that it fails to provide CGC a just and reasonable return which will enable it "to operate successfully, to maintain its financial integrity, to attract capital, and to compensate investors for the risk assumed." *Federal Power Commission v Hope Natural Gas Co*, at 605. The low rate of return resulted in large part by the derivation of a capital structure for CGC which is inconsistent with the Authority's stated methodology, not supported by the record evidence, in violation of the attrition period, and in violation of due process constitutional provisions. This material error is compounded by the extremely low return on equity selected by the Authority. Accordingly, CGC seeks reconsideration and requests that the Authority modify the capital structure to be, at a minimum, consistent with the methodology stated in the Order. CGC also requests the Authority modify the return on equity to be more reflective of the returns expected for companies comparable to CGC.

II. THE TRA'S STATED METHODOLOGY DOES NOT PRODUCE THE CAPITAL STRUCTURE ADOPTED IN THE ORDER.

During the proceeding, the Company recommended that the Authority adopt a "stand alone" approach which would have utilized CGC's own capital structure. The Authority rejected the use of CGC's capital structure and instead decided to use the capital structure of CGC's parent AGL Resources, Inc. ("AGLR"). In its Order, the TRA states that the capital structure is based on AGLR's capital structure *and* is consistent with a prior CGC case, i.e, TRA Docket No. 97-00982 and other previous decisions of the Tennessee Public Service Commission ("TPSC ")[1]. However, a review of the record and those cases reveal the capital structure adopted in the Order is in fact neither.

A. The Capital Structure is Not AGLR's Capital Structure.

The Order states: "...the panel found that AGLR's capital structure was the appropriate capital structure for the determination of CGC's cost of capital."[2] However, the panel did not

[1] The Order pp 43-45

[2] The Order, page 44

actually adopt AGLR's capital structure. Rather, the Order adopted the following capital structure:

Short-term debt	16.4 %
Long-term debt	37.9 %
Preferred Stock	10.2 %
Common equity	35.5 %
Total Capitalization	100.0 %[3]

Not only is this *not* AGLR's capital structure, it is not even found in the exhibit that is cited in the Order as the source of "AGLR's capital structure." The Order identifies Dr. Steven Brown's Pre-filed Direct Testimony, Exhibit CAPD-SB, Schedule 3, Page 1 of 11 (July 26, 2004) as the source.[4] However, the capital structure set forth above is not reflected anywhere on this exhibit. Rather, Exhibit CAPD-SB, Schedule 3 sets forth AGLR's capital structure at 3 different points in time, i.e., December 31, 2003, December 31, 2002, and December 31, 2001. On none of these three dates is AGLR's capital structure consistent with the capital structure adopted by the Authority, and the Order does not provide any details or support regarding how the numbers were derived.

B. The Capital Structure is Not Consistent with the Attrition Period, CGC's Last Rate Case, or other TRA Orders.

More importantly, based on the TRA's stated methodology, it would be inappropriate to even use Exhibit CAPD-SB. Significantly, none of the capital structures presented on Exhibit CAPD-SB, Schedule 3 reflect AGLR's current capital structure, the capital structure at August 30, 2004 when the panel deliberated the matter and adopted the capital structure as set forth in

[3] The Order, pp 58-59

[4] The Order p 45, footnote 89.

the October 20, 2004 Order, or the capital structure reasonably expected to be in place during the attrition period ended June 30, 2005 as adopted by the Authority.

In CGC's last rate case, TRA Docket No. 97-00982, the TRA adopted a *projected* average capital structure of the parent for the attrition period[5]. If the TRA uses the same methodology used in Docket No. 97-00982, which it stated it intended to do in this case, the resulting projected capital structure, as addressed more fully below in Paragraph Numbers 9 and 10, would be:

Short term debt	4.07%
Long Term debt	40.24%
Preferred stock	9.47%
Common Equity	46.22%
Total Capitalization	100.00%[6]

Consequently, this is the capital structure that is consistent with the panel's decision that CGC's cost of capital should be based on AGLR's capital structure and should be consistent with the methodology adopted by the Authority in CGC's last rate case in Docket No. 97-00982. In addition, in Docket No. U-82-7175, another CGC rate case, the TPSC used "an

[5] *In re Petition of Chattanooga Gas Company to Place into Effect a Revised Natural Gas Tariff* TRA, Docket No. 97-00982, Testimony of Gerald A Hinesley, page 10 (copy attached as Exhibit No Recon-1) and Order in Docket No 97-00982, dated October 7, 1998 pp. 49-50 The TRA refers to the Order in Docket No 97-00982 in the Order in the present Docket. There is a reference to the taking of administrative notice of the '97 docket in the transcript Vol. VI pp 52-53. However, it is unclear from the transcript whether the Authority took administrative notice of the entire record in that Docket or just the order. If the Authority did not take such notice, CGC respectfully, requests that the Authority take official notice of the entire record in Docket No 97-00982 inasmuch as the panel has relied on information in that Docket in its findings in the present Docket

[6] The projected average capital structure for the twelve months ended June 30, 2005 is the average of the actual capital structure of June 30, 2004 and September 30, 2004 and the projected capital structure at December 31, 2004, March 31, 2005 and June 30, 2005

average capital structure for the 12 months ending December 31, 1983.[7] In that proceedıng, the 12 months ending December 31, 1983 was the attrition penod.

Not only would such a capital structure be consistent with the TRA's stated methodology and CGC's last rate case, it would also be consistent with established principles of utility rate makıng law which require adjustments for known and reasonably anticipated changes.[8] In the *South Central Bell* case cıted ın footnote 8, the Tennessee Court of Appeals stated that "...the test period results must be adjusted to take into account known changes that are likely to occur in the immediate future. ...To ignore these expenses and changes reasonably certain to occur fails to follow the basic purpose of rate making; to set rates for the future."[9]

Sımilarly, in the Order issued in Docket Numbers 93-04818, 94-00388 and 94-00389 regarding United Telephone-Southeast Inc., the TPSC used a June 30, 1993 capital structure because it contained short term debt. The staff witness who recommended this capıtal structure testified that it was more representative of the capital structure that the company would have

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[7] *In re Petıtıon of Chattanooga Gas Company to Place ınto Effect a Revısed Natural Gas Tarıff and to Amend Specıal Contract*, Docket No U-82-7175, Order dated December 13, 1982, pp 7-8 At the tıme of thıs case Chattanooga Gas Company was not a subsıdıary. It was a dıvısıon of Jupıter Industrıes, Inc

[8] *South Central Bell Telephone v Tennessee Publıc Servıce Commıssıon*, 579 S.W 2d 429, (TN Ct. App 1979) In TPSC Docket No U-85-7338 the TPSC adopted the capıtal structure of Tennessee-Amerıcan Water Company as of the test perıod, ı e., as of December 31, 1984 The Commıssıon concluded that the December 31, 1984 capıtal structure was approprıate because ıt was based on the latest balance sheet date avaılable *See In re Petıtıon of Tennessee-Amerıcan Water Company to Place ınto effect a Revısed Tarıff*, Docket Number U-85-7338, Order pp. 15-16. CGC does not advocate the use of the test perıod capıtal structure as of one poınt ın time because CGC's capıtal structure changes throughout the year. The use of an average based upon the attrıtıon perıod ıs more reasonable because short-term debt ıs hıgh at the end of the fourth quarter due to short-term borrowıngs durıng the heatıng season. Conversely, short-term debt ıs low durıng other perıods when certaın operatıonal expenses are lower Such cyclıcal fluctuatıons ın short-term debt may not necessarıly apply or be as materıal to a water company, such as Tennessee-Amerıcan as for a natural gas dıstrıbutor

[9] *Id , at p 6*

during the three-year period for which its rates were being set[10]. Consistent with the TRA's Order in CGC's last rate case in Docket No. 97-00982 , the TPSC did not rely strictly on historical information but recognized the need to utilize the capital structure that is reasonably anticipated to be in place during the period in which the rates will be in effect.

In accordance with the cases discussed above, the capital structure adopted in the Order should reflect known or reasonably anticipated changes to AGLR's capital structure. However, it does not. Specifically, Dr. Brown's Exhibit CAPD-SB, Schedule 3, Page 1 of 11 identifies AGLR's capital structure at December 31, 2001, at December 31, 2002, and at December 31, 2003. As evident from that exhibit, AGLR's equity percentage increased from 31.6% at December 31, 2001 to 41.4% at December 31, 2003. The capital structure adopted in the Order reflects an equity percentage of only 35.5%. Also, as explained in AGLR's 10-Q Report for the quarter ended March 31, 2003 to the Securities and Exchange Commission (which was also filed with the TRA in this Docket in response to the Minimum Filing Guideline #17), in February 2003 AGLR issued 6.4 million shares of common stock resulting in net proceeds of approximately $136.7 million increase in equity. Neither of the capital structures at December 31, 2001 nor at December 31, 2002 as presented on Dr. Brown's Exhibit reflect this known change in equity. Neither of the capital structures presented on the Exhibit reflect more recent changes in equity and debt recorded on AGLR's books.

[10] *In re Earnings Investigation of United Telephone-Southeast, Inc,* Docket No 03-04818, *Petition of United Telephone-Southeast, Inc to Extend for One Year its Participation Under the Existing Regulatory Reform Plan,* Docket No 94-000384, and *Petition of United Telephone-Southeast, Inc for Conditional Election for Alternative Regulation,* Docket No 94-00389, Order dated December 30,1994, p 6. In the United Telephone-Southeast case the rates were set for three years as opposed to one year in the Chattanooga Gas Company cases

III. THE TRA'S FAILURE TO ADOPT A CAPITAL STRUCTURE BASED ON ITS STATED METHODOLOGY OR UPON EVIDENCE IN THE RECORD RESULTS IN LEGAL INFIRMITIES.

As stated above, the capital structure adopted in the Order results in an extremely low rate of return which violates the standards set forth by the U.S. Supreme Court in the *Bluefield* and *Hope* cases cited above. In addition, the TRA's stated methodology does not produce the capital structure adopted in the Order. Moreover, the Order does not explain how the TRA actually derived the capital structure it utilized for AGLR. Thus, the capital structure is unsupported by substantial and material evidence in the record, violates due process principles, is arbitrary and capricious and was made upon unlawful procedure because CGC was deprived of an opportunity to address the reasonableness of the methodology during the proceeding.[11] In *Tennessee American Water Company v. Tennessee Public Service Commission* the Court of Appeals reversed and remanded the decision of the Public Service Commission that provided a rate of return outside the scope of evidence and provided no explanation for the agency's reliance on its own expertise.[12] In the *Tennessee American* case, the Court said:

> An agency acts arbitrarily when it unreasonably rejects evidence such as expert opinion, ... Or when its members act on speculation or disregard uncontradicted testimony without stating a valid reason for doing so.[13]

The Court further stated that:

> The Commission may not, however avoid the duty to explain its decision and to base the decision on substantial evidence in the record by mere assertion of its expertise. .... When an agency

[11] *Tennessee-American Water Company vs Tennessee Public Service Commission*, 1985 Tenn. App LEXIS 2800, Tenn Ct App April 11, 1985

[12] *Id*

[13] *Id* At page 4

exercises its discretion or relies on its expertise, it should provide a clear explanation of its action[14].

Because neither of the capital structures recommended in the record were adopted and the agency has not given an explanation of how the capital structure it adopted was derived, CGC has been deprived of an opportunity to address the reasonableness of the methodology. Moreover, since no party to the proceeding entered testimony that addressed a proposed capital structure that resembled the structure adopted in the Order, CGC had no opportunity to provide rebuttal testimony, cross-examine the proponent of the structure, or otherwise provide evidence relative to the proposal. As a result, CGC has been denied procedural due process with respect to a matter for which no evidence was presented in these proceedings. In *Steele v. Metropolitan Board of Zoning Appeals* the Tennessee Court of Appeals reversed an agency decision because the agency failed to place in the record information that it considered, thus preempting the Court from reviewing evidence considered by the agency in reaching its decision.[15] In the *Steele* case the Court of Appeals said:

> As a general rule, for reasons as fundamental as due process, an agency may not base its decision on evidence or information outside the record.[16]

The Court went on to say that:

> Agencies may, of course, consider facts that were developed in a prior proceeding but only if the information from the prior proceeding is put into evidence at the hearing before the agency

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[14] *Id*

[15] *Steele v Metropolitan Board of Zoning Appeals,* 1986 WL 3985 (Tenn Ct App), at p 3

[16] *Id*

> *and the parties are given a chance for rebuttal.*[17] (emphasis added)

The rule of law in the *Steele* case is codified in T.C.A. § 4-5-313(6) with respect to official notice. T.C.A. § 4-5-313 (6) states in part:

> Parties must be notified before or during the hearing, or before the issuance of any initial or final order that is based in whole or in part on facts or material noticed, of the specific facts or material noticed and the source thereof, *including any staff memoranda and data*, and *be afforded an opportunity to contest and rebut the facts or material so noticed.* (emphasis added)

In *McNiel v Tennessee Board of Medical Examiners*, the Tennessee Court of Appeals overruled the decision of the agency because it was not supported by substantial and material evidence. The Court said the agency failed to put into the record evidence of the special knowledge of the board members upon which the board apparently relied.[18] The Court stated that if the agency takes official notice of facts within its knowledge, it must do so consistent with the standard in the Administrative Procedures Act (APA).[19] The Court said that: "A court obviously cannot review knowledge, however expert, that is only in the minds of one or more members."[20] The Court stated that the agency had not properly complied with the requirements of taking official notice of its own expertise:

> There is no record that petitioners were notified that the members of the Board would consider as evidence those matters of expert information known to them, or as to which they held an opinion; and no record appears that such information or opinion was disclosed at the hearing *with opportunity to cross-examine and*

[17] *Id*

[18] *McNiel v Tennessee Board of Medical Examiners*, 1997 WL 92071 (Tenn Ct App)

[19] *Id* , at pp 6-7

[20] *Id* , p. 6.

> *contradict.* (emphasis added) Under the circumstances, the undisclosed expertise of the Board cannot substitute for lack of evidence.[21]

Therefore, if the Authority does not believe the capital structure is in error, as suggested by CGG, and does not adopt the capital structure that CGG proposes in this Petition as the capital structure of AGLR using the methodology used in Docket No. 97-00982, then CGC respectfully requests an explanation of the methodology used by the TRA in deriving the AGLR capital structure and an opportunity to respond to the methodology adopted by the Authority.

IV. RELIEF SOUGHT TO ADDRESS LEGAL INFIRMITIES OF CAPITAL STRUCTURE

CGC continues to believe that the stand alone capital structure presented in its testimony in this proceeding is the appropriate capital structure and urges its adoption by the Authority. However, if the TRA continues to support the capital structure of the parent AGLR, then the TRA should use the projected average capital structure for the attrition period which is consistent with the stated methodology in the Authority's Order. As stated above, this is the methodology used by the Authority in CGC's last rate case in Docket No. 97-00982. The resulting capital structure utilizing this methodology is shown below and is also shown above in Paragraph 5.

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[21] *Id*, at p 7

Short term debt	4.07%
Long Term debt	40.24%
Preferred stock	9.47%
Common Equity	46.22%
Total Capitalization	100.00 %[22]

Because this methodology was not presented by any party to the proceeding, the data necessary to calculate the average capital structure for the attrition period is not in the record. Therefore, consistent with TRA § 1220-1-2-.20, CGC seeks to present new evidence which would consist of the quarterly capital structures of AGLR during the attrition period and the resulting calculation of the projected average capital structure, a copy of which is provided as Exhibit No. Recon-2. In addition, CGC proposes to present Mr. Mike Morley as a witness to authenticate the exhibit. The lack of an opportunity to address this methodology during the proceeding provides a good cause basis for the introduction of new evidence on reconsideration.

In the alternative, if the Authority does not desire to have new evidence introduced on reconsideration, CGC suggests that the Authority utilize the capital structure as of the midpoint of the attrition period. The midpoint of the attrition period is December 31, 2004 and the projected capital structure for AGLR was provided in response to Data Request Number 6 of the TRA, Econ # 2 set of data requests which is part of the record. The projected capital structure for AGLR as of December 31, 2004 is as follows:

[22] The projected average capital structure for the twelve months ended June 30, 2005 is the average of the actual capital structure of June 30, 2004 and September 30, 2004 and the projected capital structure at December 31, 2004, March 31, 2005 and June 30, 2005.

Short term debt	9.96%
Long Term debt	37.74%
Preferred stock	9.12%
Common Equity	43.18%
Total	100.00%[23]

However, this is not the preferred alternative because utilization of a single point of December 31 of any year gives an inaccurate view of the capital structure of a gas utility. The capital structure at that point in time of any year reflects higher short-term debt due to increased operating costs during the winter heating season.

V. THE RATE OF RETURN ON EQUITY FAILS TO PROVIDE A FAIR RATE OF RETURN AND IS OUT OF LINE WITH RECENT DECISIONS.

The low rate determined by the TRA for return on equity also fails to provide CGC a return which enables it to maintain its financial integrity, attract capital, and compensate its investors for assumed risk. Accordingly, the Order violates the standards set forth in the *Hope* and *Bluefield* cases of the U.S. Supreme Court cited above. In addition, the return on equity of 10.20% adopted in the Order is out of line with the returns on equity adopted this year for gas utilities. As demonstrated in CGC's Supplemental Response to Discovery Request Number 15 of the CAPD which was filed on August 18, 2004, there had been seven (7) gas utility decisions on equity returns prior to the Order. Of the decisions, only one was lower than 10.20% with six (6) of the decisions being higher. Significantly, four (4) of the decisions were between 10.90% and 12.00%, in keeping with the 11.25% return on equity requested by CGC in this proceeding. Accordingly, CGC respectfully requests the Authority reconsider and adopt an 11.25% return on equity.

[23] Exhibit No Recon-3 sets forth the supporting calculations of the protected capital structure as of December 31, 2004 for AGLR based on information provided in CGC's response to Data Request Number 6 of the TRA, Econ #2 set of data requests

VI. CONCLUSION

For the foregoing reasons, CGC respectfully requests that the TRA grant this Petition for Reconsideration and reconsider the capital structure and return on equity previously adopted in this proceeding. CGC respectfully requests that the Commission modify and amend the Order to correct and eliminate the errors described in this Petition by providing CGC the relief set forth herein and by providing CGC such further and other relief as the Authority may deem proper.

Respectfully submitted,

Chattanooga Gas Company

By: D. Billye Sanders

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Attorney for Chattanooga Gas Company

CERTIFICATE OF SERVICE

I, hereby certify that on this 4th day of November, 2004, a true and correct copy of the foregoing was delivered by hand delivery, or U.S. mail postage prepaid and email to the other Counsel of Record listed below.

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D. Billye Sanders, Esq.

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Exhibit No. Recon.-1

BEFORE THE

TENNESSEE REGULATORY AUTHORITY

DIRECT

TESTIMONY

OF

GERALD A. HINESLEY

IN RE:

CHATTANOOGA GAS COMPANY

DOCKET NO. 97-00982

Direct Testimony of Gerald A. Hinesley

Q. Please state your name and occupation.

A. I am Gerald A. Hinesley, Vice President and Controller of AGL Resources Service Company.

Q. What are your principal responsibilities as Vice President and Controller?

A. I have overall responsibility for the accounting functions of AGL Resources Inc. (AGLR), and all of its subsidiaries including Atlanta Gas Light Company and Chattanooga Gas Company hereinafter referred to as the Company or Chattanooga.

Q. Please outline your educational and professional training and experience.

A. I received a B.B.A. from the University of Georgia in 1981 with a major in accounting. I have been associated with AGL Resources Inc. and its predecessor company, Atlanta Gas Light Company, continuously since December 1978 in various capacities, primarily in the Accounting Department. I have been successively, Staff Accountant, Assistant Manager-Financial Accounting, Director-Financial and Accounting Services and Director-Corporate Accounting. I was named Controller in 1996 and Vice President and Controller in 1997. I am a Certified Public Accountant in Georgia.

Q. Have you previously submitted testimony for Chattanooga to this Authority?

A. No, I have not.

Q. What is the subject of your testimony?

A. I will present various financial and accounting data in support of Chattanooga's filing in this proceeding.

Q. Have you prepared an exhibit which shows these data?

A. Yes, I am sponsoring Exhibit No. 5 which contains various schedules. This exhibit was prepared under my supervision and direction.

Q. What is the purpose of Exhibit No. 5?

A. The primary purpose of Exhibit No. 5 is to present and support Chattanooga's additional revenue requirement based upon the forward-looking test year ending September 30, 1998.

Q. Please describe the content of Exhibit No. 5.

A. Schedules 1 through 3 of the Exhibit contain the Balance Sheet, Statement of Income and Detail of Operating and Maintenance Expenses for the twelve-month period ended September 30, 1996. Schedules 4 through 10 of the Exhibit are based upon forecasts of the various financial data.

Q. What is the basis of the forecasts used for the test year ending September 30, 1998?

A. The forecasts of customer growth and volumes of gas sold for the general service and interruptible customers is covered in Mr. Fred Carillo's testimony. The forecast of the related operating revenues for customer classes is covered in Ms. Lisa Howard Wooten's testimony. The Company's most recent Construction Forecast is the source of the construction expenditure forecast for the test year. The construction forecast is updated each year for planning purposes based upon a thorough review of all capital expenditure plans. The forecast of Operating and Maintenance Expenses consists of three parts, payroll expenses, expenses other than payroll and shared services expenses allocated to Chattanooga. To derive payroll costs for the test year, Chattanooga must project test year employment levels and then apply expected salary increases through the end of the test year to current wage levels. The test year forecast includes 100 employees. This is the minimum level of employees we feel is needed to maintain service at adequate levels.

Q. What level of salary increases were used to arrive at the forecast of total expenses for the test year?

A. The Company has forecast salary increases ranging from 2.5%-3.5% for non-exempt, non-bargaining unit employees and 4.5% for exempt employees. These increases are based upon the most current market forecasts of comparable rates available to us. The overall increase forecast for the test year is 3.3% compared with the average increase of 3.5% in the survey of market data.

Q. Why were exempt employees' pay increased by 4.5%?

A. The market data indicates that employees within this group are paid below the market for these positions. A 4.5% increase, which is slightly above the market average increase of 3.8% for this group of employees, will begin to move these employees closer to the market average pay for these positions.

Q. What increases were forecast for bargaining unit employees?

A. The Company has forecast no increases for the bargaining unit employees. Instead, lump sum payments of $500 paid to each bargaining unit employee is included in the forecast consistent with the bargaining unit agreement signed in 1996.

Q. How were non-payroll costs forecast?

A. The forecast of most non-payroll costs was accomplished by applying a growth and inflation factor to the September 30, 1996 balances, excluding payroll, in each expense account. It is, however, necessary to forecast separately certain accounts that are known to be affected by more or less than the general changes in the growth and inflation factors.

Q. What was the basis used for the growth and inflation factors?

A. The growth factor was based upon the net customer additions forecast from September 1996 through the test year ending September 30, 1998. The growth factor used was 8.95%. The inflation factor used was based upon the forecasted increase in the average Consumer Price Index (CPI) for the year ended 1996 through 1998. The increase in the average CPI forecast for this period is 6.67% based upon information provided by the College of Business Administration, Economic Forecasting Center of Georgia State University.

Q. Please describe the estimates of operation and maintenance expenses which were not forecast using the growth and inflation factors.

A. The experience rate for the twelve months ended February 1997 (the most recent twelve-month period) for uncollectible accounts was applied to test year residential and commercial revenues to forecast the test year uncollectible accounts expense. Property and Liability insurance costs were forecast using data obtained from the Company's insurance brokers. Pension expense was forecast by the Plan Actuary for the test period. Employee health insurance costs were forecast using a projected trended rate of 10% based on information from A. Foster Higgins and Company, Inc.. Postretirement Benefits Other Than Pensions (required by FAS 106) were forecast by the Plan Actuary. Postemployment Benefits costs (required by FAS 112), were forecast using information provided by John Hancock Mutual Life Insurance Company for the cost of benefits entitled to employees for Long Term Disability.

Q. Has the Company filed a detail of the test year operation and maintenance expenses?

A. Yes. A detail of all accounts and adjustments is provided in the Company workpapers.

Q. Please explain the calculation of shared services expenses allocated to Chattanooga and the reason for the increase from the levels historically allocated.

A. The methodology used to allocate shared services is covered in Mr. Jim Kissel's testimony. As explained in Mr. Harry Thompson's testimony, Atlanta Gas Light Company has recently undergone significant changes which have had a direct impact on Chattanooga. These changes have resulted in the consolidation of several of Chattanooga's departments and functions with those of AGLR or its subsidiaries including Atlanta Gas Light Company. These functions include information systems, accounting, engineering, customer service, rates and dispatch. The consolidation of these areas means that the associated costs are now being allocated to Chattanooga rather than being directly charged.

Q. Are there other changes that have had an impact on the allocation?

A. Yes. As a result of the shared services study, we determined that there were several areas of the company that were performing services for Chattanooga for which no expenses were being allocated. These areas included such things as treasury, accounts payable, mail center, gas control, human resources and others. In effect, Chattanooga had been receiving the benefit of these services "free of charge". As a result of the consolidation of functions and the findings from the shared services study, the allocation of expenses has increased from $1,259,082 in fiscal 1996 to $5,226,872 requested in this case.

Q. How were Taxes Other Than Income forecast?

A. In most cases, current or projected rates are applied to projected tax basis balances to forecast the tax expenses. For example, current payroll tax rates are applied to projected payroll to arrive at payroll tax expense for the test year. The actual ad valorem tax rates are applied to projected assessment balances for each taxing district to arrive at ad valorem tax expense for the test year. The Tennessee Franchise Tax is forecast in the same manner.

Q. What rate was used to calculate Federal Income Tax expense for the test year?

A. A thirty five (35) percent rate was used.

Q. What depreciation rates were used to arrive at test year depreciation expense?

A. As discussed in the testimony of Mr. Don Roff, a depreciation study completed in March 1997 reveals a slight overall decrease in the composite depreciation rate for Chattanooga. The new rates developed in the study are used in the test year forecast of depreciation expense. It should be noted that the methodology is consistent with the methodology allowed by the Authority in Docket No. 91-03765.

Q. How much did the rates decrease?

A. Based on depreciable plant balances at September 30, 1996, the overall composite rate decreased from 3.66% to 3.61%.

Q. Why have you included the Acquisition Adjustment in this filing?

A. As discussed in Mr. Royse's testimony, the customers of Chattanooga Gas Company have enjoyed several benefits since the acquisition. These benefits have included cost savings, improved service quality, greater system reliability and enhanced operational efficiencies.

Q. What is the impact of the inclusion of the Acquisition Adjustment on this case?

A. The Company is seeking cost of service recovery of approximately $411,000 for the annual amortization expense and the inclusion of approximately $9.6 million in rate base for the unamortized portion of the Acquisition Adjustment.

Q. Will you please explain schedules 1 through 3 of your Exhibit?

A. Schedules 1 through 3 are the Balance Sheet, Statement of Income and Detail of Operating and Maintenance Expenses for the twelve-month period ended September 30, 1996. These schedules reflect actual data for the twelve month period, which is used as the starting point for this filing.

Q. Please explain Schedule 4 the Projected Statement of Income.

A. Schedule 4 is a presentation of actual Utility Operating Income for the twelve months ended September 30, 1996. These actual numbers are presented in Column (b). The projected Test Year Adjustments, Column (c) are then applied to Column (b) to arrive at the Projected Test Year results. Column (e) shows the Company's estimated Utility Operating Income without a rate increase. The additional revenue requirement and related pro-forma adjustments in Column (f) were applied to the Test Year results to arrive at Utility Operating Income on a pro-forma Test Year basis. Column (h) shows the income statement effects of the requested rate increase in the amount of $4,422,610. Column (h) is a pro-forma income statement for the Test Year that reflects all of the adjustments shown on the schedule. It shows the Company's Operating Revenues would be $36,608,313 and Operating Income applicable to Rate Base would be $9,742,473.

Q. Please explain Schedule 5, Revenue Deficiency.

A. Schedule 5 presents the calculations of the revenue deficiency if the Company's rates remain at present levels. The fair rate of return of 9.61% is applied to the projected Net Rate Base of $101,378,492 to arrive at the required Operating Income of $9,742,473. Operating Income at present rates of $7,027,287 is subtracted from the Required Operating Income to arrive at the Operating Income Deficiency of $2,715,186. The gross revenue conversion factor, calculated in

Schedule 6, of 1.628842 is applied to the Operating Income Deficiency to arrive at a total Revenue Deficiency of $4,422,610.

Q. What is the purpose of the calculations in Schedule 6, Revenue Conversion Factor?

A. This factor is derived for the purpose of grossing up operating revenues to cover the additional taxes, forfeited discounts and uncollectible accounts that result from the additional revenues. This factor reflects experience rates and tax rates projected to be in effect during the test period.

Q. Please explain the computation of Federal Income Taxes and Tennessee Excise Taxes contained in Schedule 7.

A. This schedule is in support of the Tennessee Excise and Federal Income Tax amounts reflected on schedule 4. The statutory rate of 6% is applied to the pre-tax book income at present and proposed rates to arrive at $303,810 and $570,440, respectively, for Tennessee Excise Tax. The excise tax amounts are subtracted from the pre-tax book income to arrive at the Federal Taxable Income amounts for the present and proposed rates. The Federal Income Tax rate of 35% is applied to the amounts to arrive at the Federal Income Tax expense of $1,665,893 and $3,127,915 respectively.

Q. Please explain your Computation of Average Rate Base as reflected on Schedule 8.

A. The components of Rate Base for the forward-looking test year are based upon the Rate Base as it existed at September 30, 1996, adjusted for known and projected changes to arrive at the Average Rate Base for the test year. Average Utility Plant In Service including construction-work-in-progress increased $14,032,268, which includes projected gross additions of $8,407,640 for 1997 and $7,722,585 for 1998. Projected utility plant retirements of $781,323 and $772,235 for 1997 and

1998, respectively, are deducted to arrive at the test-year average utility plant balance of $140,014,935. As discussed previously in my testimony, the company is seeking recovery of the acquisition adjustment. The gross acquisition adjustment balance added to rate base is $13,355,565. Working Capital, as calculated on Schedule 8, pages 2 through 4, is added to Utility Plant to arrive at a total Average Gross Rate Base of $159,569,226.

Q. How is Working Capital calculated?

A. The calculation of Working Capital of $6,198,726 is shown on pages 2 through 4 of Schedule 8. Line 1 of Schedule 8, page 2 of 4, represents the average daily cash balance of $2,373,422 for the period of October 1, 1995, through September 30, 1996. Lines 2 though 7 are twelve month average balances of Materials and Supplies of $453,221, Gas Inventories-LNG of $1,539,858, Gas Inventories-Underground Storage of $3,879,286, Deferred Rate Case Expense of $200,668, Prepayments of $1,189,348, Other Accounts Receivable of $92,027, and Lead Lag Study results of $1,736,716. The results of the Lead Lag are covered in more detail in the testimony of Mr. Greg Aliff. The total of the items listed above is $11,464,545. From this total the projected twelve month average balances of Reserve for Uncollectibles of $278,723, Other Reserves of $549,562, Customer Deposits of $3,766,190 and Accrued Interest on Customer Deposits of $671,344 are deducted to arrive at the Working Capital amount of $6,198,726. The total of Utility Plant in Service of $140,014,935 added to the Unamortized Acquisition Adjustment of $13,355,565 plus the Working Capital of $6,198,726 requirement results in a total Average Gross Rate Base of $159,569,226.

Q. Please continue with your explanation of how Rate Base was derived.

A. From this Average Gross Rate Base of $159,569,226 is deducted Accumulated Depreciation of $46,569,377; Contributions in Aid of Construction of $1,908,645; Customer Advances for Construction of $384,855; and Accumulated Deferred Income Taxes of $5,131,816. The Average Accumulated Depreciation increased $7,390,964 and includes depreciation provisions of $4,607,476 for 1997 and $4,877,899 for 1998. Net plant retirements of $1,653,128 including cost of removal less salvage, for the two periods are deducted to arrive at test year average reserve for depreciation of $46,569,377. The test-year Average Net Rate Base totals $101,378,492 after deducting the above items.

Q. What is the basis for the Cost of Capital of 9.61% as reflected on Schedule 9?

A. Schedule 9 reflects the projected average capitalization of the Company for the test year ending September 30, 1998. The projected September 30, 1998, capital structure of Atlanta Gas Light Company is used as a basis for projecting the September 30, 1998, capital structure and cost of debt of Chattanooga Gas Company.

Q. Why was the capital structure projected in this manner?

A. Chattanooga has only common equity and short term debt in its capital structure. Chattanooga has no long term debt and its short term debt is arranged through its parent, AGLR. There are no plans for Chattanooga to issue debt in its own name in the foreseeable future. Since AGLR owns all of the common stock of Chattanooga including common stock equity and retained earnings, Chattanooga is completely dependent on AGLR for all of its financing needs. The source of all of Chattanooga's financing is AGLR, therefore the appropriate capital structure would be that of AGLR. In the Company's last two general rate case filings in Docket No. 93-06946 and 95-02116, based upon the findings of the Commission

Staff, the Commission approved the use of AGLR's capital structure as being appropriate for that of Chattanooga.

Q. How is the cost of common equity derived?

A. The basis for the Test-Year cost of common equity of 12.25% is explained in testimony presented by Dr. Victor L. Andrews.

Q. What is the purpose of Schedule 10.

A. Schedule 10 consists of two pages that summarize test-year and pro forma adjustments. The adjustments contained on Schedule 10 are assigned an adjustment number for easy cross-referencing to Schedule 4. A brief explanation is given for each adjustment. The total effect of these test-year and pro forma adjustments can be cross-referenced to Columns (d) and (f) of Schedule 4.

Q. Does this filing contain full and adequate support, with complete explanation of the adjustments relating to Exhibit No. 5 referred to, in your testimony?

A. Yes. Exhibit No. 5 along with the Schedules reflecting each adjustment and the Company's workpapers, fully support and explain the adjustments outlined in my testimony.

Q. Mr. Hinesley, does this complete your testimony in this rate proceeding?

A. Yes.

AFFIDAVIT

State of Tennessee)
)
County of Hamilton)

Personally, appeared before the undersigned authority, Gerald A. Hinesley, who after being duly sworn states on oath that he is the same Gerald A. Hinesley whose prepared testimony and exhibits accompany this Affidavit; that he is authorized to make this Affidavit; that he is familiar with the contents of the foregoing testimony on behalf of Chattanooga Gas Company to the Tennessee Regulatory Authority; and that the facts stated therein are true to the best of his knowledge, information and belief.

Gerald A. Hinesley
Gerald A. Hinesley

Sworn to and subscribed before me this

28th day of April, 1997.

Loreen C. Morris
Notary Public

My Commission Expires:

4/30/97
(NOTARY SEAL)

Chattanooga Gas Company
TRA Docket 04-00034

Exhibit No. Recon-2

AGL Resources Average Capital Structure Twelve Months Ended June 30, 2005
Percent of Total

Class of Capital	6/30/2004	9/30/2004	12/31/2004	3/31/2005	6/30/2005	Twelve Months Ended June 30, 2005 Average
Short Term Debt	7 31%	2 17%	5 95%	1 21%	3 72%	4 07%
Total Long Term Debt	34 85%	43 26%	40 43%	41 91%	40 78%	40 24%
Preferred Stock	10 09%	9 44%	9 13%	9 46%	9 21%	9 47%
Common Equity	47 75%	45 13%	44 49%	47 42%	46 29%	46 22%
	100 0%	100 0%	100 0%	100 0%	100 0%	100 0%

	Qtr Ended 6/30/2004	Qtr Ended 9/30/2004	Qtr Ended 12/31/2004	Qtr Ended 3/30/2005	Qtr Ended 6/30/2005
Short Term Debt	$ 161 0	$ 51 0	$ 144 7	$ 28 3	$ 89 6
Total Long Term Debt	767	1,017	983	983	983
Preferred Stock	222	222	222	222	222
Common Equity a/	1,051	1,061	1,082	1,112	1,116
Total	$ 2,201 0	$ 2,109 0	$ 2,323 5	$ 2,137 5	$ 2,202 3

a/ Amounts have been adjusted to exclude "other comprehensive income" related to AGLR's consolidated accrued pension liability and other items not yet recognized as expense

Exhibit No. Recon-3

Chattanooga Gas Company
TRA Docket 04-00034
AGL Resources Projected Capital Structure as of December 31, 2004

Class of Capital		**(A) Amount**	**(B) Percent**
Short Term Debt	$	243,700	9 96%
Total Long Term Debt		922,936	37 74%
Preferred Stock		222,913	9 12%
Common Equity		1,056,000	43 18%
Total Capitalization	$	2,445,549	100 00%

(A) Data provided in response to TRA Data Request ECON #2, Question 6, Schedule 6-1, Part A

(B) Calculated capital structure based on data provided in **(A)**