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BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

November 5, 2004

IN RE:	)
	)
COUNCE NATURAL GAS COMPANY	) **Docket No. 04-00359**
ACTUAL COST ADJUSTMENT (ACA) AUDIT	)

NOTICE OF FILING BY ENERGY AND WATER SECTION OF THE UTILITIES 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 Compliance Staff ("Staff") of the Utilities Division of the Tennessee Regulatory Authority gives notice of its filing of the Counce Natural Gas Company's ACA Audit Report 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 Counce Natural Gas Company (the "Company").

2. The Company's ACA filing was received on October 13, 2004, and the Staff completed its audit of same on November 3, 2004.

3. On November 4, 2004, the Staff issued its preliminary ACA audit findings to the Company, and on November 4, 2004, 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 Staff, the Company's responses thereto and the recommendations of the Staff in connection therewith.

5. The Energy and Water Compliance Staff 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, Manager
Energy and Water Section
of the Utilities Division
Tennessee Regulatory Authority

CERTIFICATE OF SERVICE

I hereby certify that on this 5th day of November 2004, 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:

Pat Miller
Chairman
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, TN 37243

Mr. Mike Horton, President
Counce Natural Gas Company
P.O. Box 285
Burnsville, MS 38833

Pat Murphy

Pat Murphy

<u>EXHIBIT A</u>

COMPLIANCE AUDIT REPORT

OF

<u>COUNCE NATURAL GAS COMPANY</u>

<u>ACTUAL COST ADJUSTMENT</u>

DOCKET #04-00359

PREPARED BY THE

<u>TENNESSEE REGULATORY AUTHORITY</u>

ENERGY AND WATER SECTION

OF THE UTILITIES DIVISION

November 2004

COUNCE NATURAL GAS COMPANY

COMPLIANCE AUDIT REPORT OF ACTUAL COST ADJUSTMENT FILING

DOCKET NO. 04-00359

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I. INTRODUCTION

The subject of this audit is Counce Natural Gas Company's ("Company" or "Counce") 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 September 30, 2003, were calculated correctly and were supported by appropriate source documentation.

II. AUDIT OPINION

On October 13, 2004, Staff received Counce's ACA filing supporting the activity in its deferred gas cost account ("ACA account") for the period October 1, 2003 through September 30, 2004. For the period under audit, this ACA filing showed $143,331.81 in total gas costs, with $138,228.38 being recovered from customers through rates. Adding a beginning balance in the ACA account of **negative** $3,927.17 in over-collected gas costs from the preceding ACA period and interest due from customers for the current period of $100.65 resulted in an ACA balance at September 30, 2003 of **positive $4,562.25 in under-recovered gas costs**. Small gas companies, such as Counce, do not automatically surcharge or refund the balance in the ACA account until the Staff's audit is complete and the surcharge or refund factor is determined by the TRA.

SUMMARY OF THE ACA ACCOUNT:[2]

Line No.		Company (as filed)	Staff (as corrected)	Difference (Findings)
1	Beginning Balance at 10/01/03	$ -3,927.17	$ -3,665.74	$ 261.43
2	**Activity During Current Period:**			
3	Plus Gas Costs	$143,331.81	$143,331.81	$ 0
4	Minus ACA Recoveries	-3,285.34	-3,756.39	-471.05
5	Minus PGA Recoveries	138,228.38	138,165.68	-62.70
6	Ending Balance before Interest (line 1 + line 3 – line 4 – line 5)	$ 4,461.60	$ 5,256.78	$ 795.18
7	Plus Interest	100.65	140.39	39.74
8	**Ending Balance Including Interest at 09/30/04 (line 6 + line 7)**	**$ 4,562.25**	**$ 5,397.17**	**$ 834.92**

[1] The ACA is more fully described in Section V

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

Staff's audit resulted in five (5) findings.[3] The net amount of these findings is a **positive $834.92 in under-recovered gas costs.**[4] Staff's correction of the Company's reported September 30, 2004 balance of positive $4,562.25 produced an ending balance in the ACA account of **positive $5,397.17 in under-recovered gas costs.**[5]

The amount of the Company's errors represents less than one percent of its total gas invoices, and is therefore immaterial by comparison. Also, Findings #1 - #4 associated with the ACA Account were primarily reporting errors and not actual errors in billing its customers. Since the Company does not surcharge (refund) its ACA Account balance until after Staff's audit, the customers were not affected by the reporting errors. Staff, therefore, concludes that except for the findings noted in this report, Counce is correctly implementing its Purchased Gas Adjustment Rider as calculated in the Actual Cost Adjustment, in accordance with the TRA rules for Counce Natural Gas Company.

III. BACKGROUND INFORMATION ON COMPANY AND GAS SUPPLIERS

Counce Natural Gas Company, with its headquarters in Burnsville, MS, is a wholly owned subsidiary of Tumlinson Engineering, Inc., and was formed in 1995 for the purpose of acquiring the operating authority of Hardin County Gas Company and providing natural gas service to customers in Hardin County, Tennessee. Hardin County Gas Company's certificate of convenience and necessity ("CCN") was transferred to Counce on December 22, 1995, per Docket #95-03379. In October 2000, ownership of Tumlinson Engineering, Inc. was transferred from Ted Tumlinson to Mike Horton.

The natural gas used to serve this area is purchased from Enbridge Marketing (U.S.), L.P. The gas purchases are made in accordance with separate and individual tariffs approved by the Federal Energy Regulatory Commission, while the gas transported is purchased under contract or on the spot market.

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.

[3] Refer to Section VII for a description of the findings

[4] Refer to Chart, page 1

[5] Company's positive $4,562 25 balance increased by Staff findings of $834 92

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 of the Energy and Water Division conducted this audit.

V. DESCRIPTION OF PURCHASED GAS ADJUSTMENT RULE

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 to 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 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].

VI. SCOPE OF ACTUAL COST ADJUSTMENT AUDIT

The ACA audit is a limited compliance audit of Counce's ACA account. The audit goal was to verify that the Company's calculations of gas costs incurred and recovered were materially correct,[6] and that the Company is following all Authority orders and directives with respect to its calculation of the ACA account balance. Refer to the ACA Account detail provided in Section II, 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. Staff also audited a sample of customer bills to determine if the proper tariff rates, as well as PGA and ACA rates were applied in the Company's calculation of customer bills during the twelve month audit period. After recalculating each sample bill, Staff determined that the Company's calculation methods are correct. However, an error occurred in the July 2004 billing that is described in Staff Finding #5.

[6] 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 $834.92,** which had the net effect of increasing the Company's under-recovery (positive) balance in the ACA account by this amount. A summary of the ACA account was presented in Section II. See a summary of Staff's findings below, followed by a detailed description of each finding.

SUMMARY OF FINDINGS:

FINDING #1	Beginning Balance	$261.43	Under-recovery
FINDING #2	Gas Cost Recovered	62.70	Under-recovery
FINDING #3	ACA Refunds	471.05	Under-recovery
FINDING #4	Interest on Account	39.74	Under-recovery
FINDING #5	Billing Error	N/A	
	Net Results	**$834.92**	**Under-recovery**

FINDING #1:

Exception

Counce used an incorrect beginning balance in its calculation of the September 30, 2004 balance in the ACA Account.

Discussion

According to Staff's audit results in Docket 03-00613, the ending balance in the ACA Account should have been a negative $3,665.74, representing over-recovered gas costs. The Company used a negative $3,927.17 as its beginning balance in this filing. The difference of **$261.43** between the Staff's calculation and the Company's calculation represents an additional **under-recovery** of Counce's gas costs.

Company Response

Company made a mistake typing wrong amount. We will proof read better to prevent future errors from occurring.

FINDING #2:

<u>Exception</u>

Counce over-stated its gas cost recoveries for the months of October 2003 and January 2004.

<u>Discussion</u>

When reviewing the amount of sales each month, Staff discovered that the volumes reported in the filing for October 2003 and January 2004 did not tie to the Company's Billing Summary Report for those months. Gas sales were over-stated; therefore, the gas costs recovered for these months were also over-stated. The **$62.70** difference between Staff's calculation and the Company's calculation represents a net **under-recovery** of Counce's gas costs.

<u>Company Response</u>

There was a computer error.

FINDING #3:

Exception

The Company under-stated the amount refunded to its customers for the Actual Cost Adjustment (ACA) during the audit period.

Discussion

This finding is the result of two errors. One, Counce reported the wrong ACA refund factor for the month of October 2003. Counce reported a negative $0.1653, which is the factor calculated in the last audit to become effective November 2003. When Staff audited a sample of customer bills, however, it discovered that the Company billed the correct ACA factor of negative $0.8200 for October. This was a reporting error and did not affect the actual amount billed. The second error was that the Company did not bill a refund factor to its customers for the months of July, August and September 2004.

The combination of these errors was a net under-statement of the amount of ACA refunds for the audit period. The **$471.05** difference between Staff's calculation and the Company's calculation represents an **under-recovery** of Counce's gas costs.

Company Response

There was a clerical error made. We will proof check next time to prevent future errors.

FINDING #4:

Exception

The Company under-stated the amount of interest on account balance owed by its customers for the audit period.

Discussion

Based on the audit findings, Staff recalculated the amount of interest on account balance for each month of the audit period. The **$39.74** difference between the Staff's calculation and the Company's calculation represents **an under-collection** of Counce's gas costs.

Company Response

Agree with your finding. We will proof check next time to prevent future errors.

FINDING #5:

Exception

The Company did not bill its base rate of $2.13 per MCF to its customers for the month of July 2004.

Discussion

As part of its compliance audit, Staff audited a sample of customer bills for each month of the audit period. For July 2004, Staff found that the Company billed only the current PGA adjustment (for recovery of gas costs) volumetrically to its customers. There were no charges billed for the Company's recovery of its cost of service and margin allowed in its last rate case. At the time, Counce was involved in a rate proceeding to increase its base rates. The increase became effective with the August 2004 billing and was billed appropriately by the Company. Based on the sales volumes reported for July, the Staff estimates that the Company under-billed by a total of $1,122.74 for the month.

This finding does not affect the balance in the deferred gas cost account, but is an observation made by Staff during its audit of customer bills.

Company Response

We agree with your finding. In August 2004 company billed the customers the rate base of gas used in July 2004.

Staff Response

Staff called the Company representative on November 5 to clarify the above response. The Company discovered post July billing that due to oversight, it had failed to bill its base rate that month. Therefore, the Company did not bill its ACA refund factor to customers in August and September, in an attempt to recoup the lost revenue. Prior to talking to Staff, the Company believed that by not refunding during those two months, they accomplished that goal. However, we explained to the Company that any adjustment made to the ACA refund was automatically trued-up in the audit process, so the refund was accomplished in the newly calculated ACA factor going forward. As a result, the Company did not collect the approximately $1,122.74 in base revenues as it thought The only way to collect those revenues would be to recalculate the customers' bills for July and make a bill adjustment to each specific customer bill in November for the difference.

VIII. CONCLUSIONS AND RECOMMENDATIONS

The corrected balance in the ACA account as of September 30, 2004 is a **positive $5,397.17 in under-recovered (under-collected) gas costs**. Staff's calculation of this balance is shown in **the Summary of the ACA Account in Section II**. The balance is the sum of $62.70[7] in under-collected gas costs for the period, $471.05[8] difference in ACA refunds made, $39.74[9] in additional interest due from customers, and $261.43[10] difference in the over-collected beginning balance at October 1, 2003. Spreading the positive $5,397.17 balance over the 12 month-to-date September 2004 sales of 19,866 MCF produces an **ACA adjustment factor of a positive $0.27 (surcharge) per MCF.**[11] Therefore, Counce's **new billing rate is $12.27 per MCF for residential, commercial, and industrial customers.** It is composed of $2.95 base rate plus the currently approved $9.05 purchased gas adjustment plus the new positive $0.27 ACA adjustment. Staff recommends that the new ACA rate be effective with the Company's November 2004 billing, and continue until the completion of the Staff's next audit.

As stated in Finding #5, Staff recommends that the Company make a billing adjustment in November to correct the July 2004 billing. The Company cannot afford to absorb that amount of loss. Individual bills should be recalculated and actual adjustments be surcharged to the specific customers.[12] Customers should be notified, perhaps by a bill insert, what the adjustment is for.

[7] Finding #2
[8] Finding #3
[9] Finding #4
[10] Finding #1
[11] See Attachment 1 for detail of calculation of the ACA factor.
[12] The average adjustment for a residential customer would be $1 31 (0 613 MCF avg usage times $2 13 base rate)

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.

Attachment 1

Counce Natural Gas Corporation

Calculation of the ACA factor

Docket No. 04-00359

Line No.	Factor to be applied to residential, commercial and industrial customers:	
1	Invoiced Gas Costs (10/1/03 - 9/30/04)	143,331 81
2	Gas Cost Recovered (10/1/03 - 9/30/04)	138,165.68
3	Under/(Over) Recovery (line 1 minus line 2)	5,166.13
4	Interest on Average Monthly Balances	140 39
5	ACA Surcharges/(Refunds) (10/1/03 - 9/30/04)	(3,756.39)
6	Beginning Balance at 10/01/03	(3,665.74)
7	**ACA BALANCE INCLUDING INTEREST at 9/30/04** **(line 3 + line 4 - line 5 + line 6)**	**5,397.17** **Under-Recovery**
8	Sales Volumes (Actual MCF for 12 month ended 9/30/04)	19,866
9	ACA Factor per MCF (line 7 divided by line 8)	**0.2717**