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TRA. SECRET ROOM

August 11, 2006

## VIA HAND DELIVERY

Chairman Sara Kyle  
Tennessee Regulatory Authority  
460 James Robertson Parkway  
Nashville, Tennessee 37243-00505

Re: Docket 04-00402 Summary of the Transactions in Chattanooga Gas Company's  
Deferred Gas Cost Account for the Twelve Months Ended June 30, 2004 and the  
Computation of the ACA Factor Effective January 1, 2005

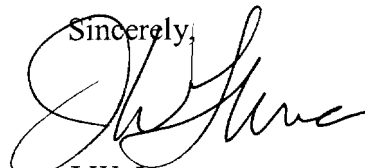
Docket 04-00403 Chattanooga Gas Company's Report of Actual Gas Costs and  
the Applicable Index Cost for Each Month of the Plan Year Ended June 30, 2004

Dear Chairman Kyle:

The Staff has asked Chattanooga Gas Company to re-file its proposed revision to its  
Tariff, which adds RFP Procedures for Selection of Asset Manager and/or Gas Provider, so that  
the filing complies with the TRA's new format for designating changes and additions in tariff  
filings. Accordingly, I have attached an original and thirteen (13) copies.

If you have any questions, please call me at 254-9146 or Archie Hickerson at 757-616-  
7510.

Sincerely,



J.W. Luna

Enclosure

cc: Elizabeth Wade, Esq.  
Archie Hickerson  
Steve Lindsey

**PERFORMANCE-BASED RATEMAKING**

**APPLICABILITY**

This Performance-Based Ratemaking Mechanism (PBRM) is designed to encourage the utility to maximize its gas purchasing activities at minimum cost consistent with efficient operations and service reliability. Each plan year will begin July 1. The annual provision and filings herein will apply to this annual period. The PBRM will continue until it is either (a) terminated at the end of a plan year or by not less than 90 days notice by the Company to the Authority or (b) modified, amended or terminated by the Authority.

**OVERVIEW OF STRUCTURE**

The Performance-Based Ratemaking Mechanism establishes predefined monthly benchmark indexes to which the Company's commodity cost is compared.

**BENCHMARK INDEX**

Each month, Chattanooga Gas Company (Company / Chattanooga) will compare its actual commodity cost of gas to the appropriate benchmark amount. The benchmark gas cost will be computed by multiplying actual purchase quantities for the month, including quantities purchased for injection into storage, by the appropriate benchmark price index.

**Spot Market Purchases:**

The monthly spot market benchmark is the "Index" price published in the first issue of the delivery month of *Inside FERC's Gas Market Report* in the table titled "Price of Spot Gas Delivered to Pipelines," denoted in the column labeled "Index" and the row for the applicable "Pricing Point."

**Swing Purchases**

For swing purchases, the benchmark "Index" price for gas delivered on any day upon which *Gas Daily* is published, is equal to the Gas Daily-Midpoint price for the immediately following day under the heading "Daily Price Survey." For gas delivered on Saturday, Sunday, or any other day upon which *Gas Daily* is not published, the price index is equal to the Daily-Midpoint for the nearest subsequent day published by *Gas Daily*.

**Long-term purchases**

For long term purchases, i.e., a term more than one month, the "Index" price published in the first issue of the delivery month of *Inside FERC's Gas Market Report* in the table titled "Price of Spot Gas Delivered to Pipelines" denoted in the column labeled "Index" and the row for the applicable "Pricing Point" will be adjusted for the Company's rolling three-year average premium paid to ensure long-term supply availability during peak periods.

**City Gate Purchases**

For city gate purchases where gas is delivered by the supplier to the local distribution company, the indexes will be adjusted for the avoided transportation costs that would have been paid if the upstream capacity were purchased versus the demand charges actually paid to the supplier.

**PERFORMANCE-BASED RATEMAKING (Continued)**

**PRUDENCE DETERMINATION**

If Chattanooga's total commodity gas cost for the plan year does not exceed the total benchmark amount by one percentage point (1%) for a plan year ending after June 30, 2000, Chattanooga's gas cost will be deemed prudent and the audit required by Tennessee Regulatory Authority's Administrative Rule 1220-4-7-. 05 is waived. If during any month of the plan year, the Company's commodity gas cost exceeds the benchmark amount by greater than two percentage points (2%), the Company shall file a report with the Authority fully explaining why the cost exceeded the benchmark.

**FILING WITH THE AUTHORITY**

The Company will file an annual report not later than 60 days following the end of each plan year identifying the actual cost of gas purchased and the applicable index for each month of the plan year.

Unless the Authority provides written notification to the Company within 180 days of such reports, the annual filing shall be deemed in compliance with the provisions of this Service Schedule.

**PERIODIC INDEX REVISIONS**

Because of changes in the natural gas marketplace, the price indices used by Chattanooga and the composition of Chattanooga's purchased gas portfolio may change. The Company shall, within 30 days of identifying a change to a significant component of the mechanism, provide notice of such change to the Authority. Unless the Authority provides written notice to Chattanooga within 30 days of the Company's notice to the Authority, the price indices shall be deemed approved as proposed by the Company.

**AFFILIATE TRANSACTION GUIDELINES**

Terms used in these affiliate transaction guidelines have the following meanings:

1. Affiliate, when used in reference to any person in this standard, means another entity who controls, is controlled by, or is under common control with, the first entity.
2. Control (including the terms "controlling", "controlled by", and "under common control with") as used in the affiliate transaction guidelines, includes, but is not limited to, the possession, directly or indirectly and whether acting alone or in conjunction with others, of the authority to direct or cause the direction of the management or policies of an entity. Under all circumstances, beneficial ownership of more than ten percent (10%) of voting securities or partnership interest of an entity shall be deemed to confer control for purposes of these affiliate transaction guidelines.
3. Gas supplier is any person who sells or otherwise provides gas to the Company. It does not include customers who transport their gas and as a result of an imbalance in the amount consumed and the amount delivered to the city gate sell gas to the Company in compliance with the Company's approved tariff provisions.

**PERFORMANCE-BASED RATEMAKING (Continued)**

The Company must conduct its business to conform to the following standards:

1. All purchases from an affiliated gas supplier of gas for system supply or storage shall be at the price and in accordance with the terms provided in a fully executed contract between the Company and the affiliated gas supplier.
2. The Company and the affiliated gas supplier shall maintain records to show that such purchases are not at a price greater than the market price at the time of the transaction.
3. All sales of gas by the Company to an affiliated gas supplier shall be in accordance with the provisions of the Company's approved tariff or at the price and in accordance with the terms provided in a fully executed contract between the Company and the affiliated gas supplier. Any sale of gas to an affiliate not in accordance with an approved tariff provision shall be at a price that is not less than the greater of the cost as recorded on the Company's books or the market price at the time of the transaction.
4. The Company shall maintain records to show that sales to an affiliated supplier are in accordance with the applicable tariff provision or, if not provided under an approved tariff provision, the price is not less than the greater of the cost as recorded on the Company's books or market price at the time of the transaction.
5. An affiliated gas supplier shall not make sales to any customer's premise that is connected to the Company's distribution facilities.
6. The Company shall not disclose to any affiliated gas supplier any information that the Company receives from a non-affiliated gas supplier that the non-affiliated gas supplier has identified as confidential unless the prior consent of the parties to which the information relates has been voluntarily given.
7. To the maximum extent practicable, the Company's operating employees and the operating employees of an affiliated gas supplier must function independently of each other.
8. The Company must maintain its books of accounts and records separately from those of an affiliated gas supplier.
9. The Company shall maintain sufficiently detailed records of all transactions with any affiliated gas supplier.

**RFP PROCEDURES FOR SELECTION OF ASSET MANAGER AND/OR GAS PROVIDER**

1. In each instance in which Chattanooga Gas Company (Company) intends to engage the services of an asset manager to provide system gas supply requirements and/or manage its assets regulated by the Tennessee Regulatory Authority (TRA), the Company shall develop a written request for proposal (RFP) defining the Company's assets to be managed and detailing the Company's minimum service requirements. The RFP shall also describe the content requirements of the bid proposals and shall include procedures for submission and evaluation of the bid proposals. N
2. The RFP shall be advertised for a minimum period of thirty (30) days through a systematic notification process that includes, at a minimum, contacting potential asset managers, including past bidders and other approved asset managers, and publication in trade journals as reasonably available. This thirty (30)-day minimum period may be shortened with the written consent of the TRA Staff to a period of not less than fifteen (15) days. N
3. The procedures for submission of bid proposals shall require all initial and follow-up bid proposals to be submitted in writing on or before a designated proposal deadline. The Company shall not accept initial or follow-up bid proposals that are not written, or that are submitted after the designated proposal deadline. N

**PERFORMANCE-BASED RATEMAKING (Continued)**

Following receipt of initial bid proposals, and on a non-discriminatory basis, the Company may solicit follow-up bid proposals from those submitting initial bid proposals in an effort to obtain the most overall value for the transaction.

4. All initial and follow-up bid proposals shall be evaluated as they are received. The criteria for choosing the winning bid proposal shall include, at a minimum, the following: (a) the total value of the bid proposal; (b) the bidder's ability to perform the RFP requirements; (c) the bidder's asset management qualifications and experience; and (d) the bidder's financial stability and strength. The winning bid proposal shall be the one with the best combination of attributes based on the evaluation criteria. If, however, the winning bid proposal is lower in amount than any other initial or follow-up bid proposal(s), the Company shall explain in writing to the TRA why it rejected each higher bid proposal in favor of the lower winning bid proposal. The Company shall maintain records demonstrating its compliance with the evaluation and selection procedures. N
5. An incumbent asset manager shall not be granted an automatic right to match a winning bid proposal. If the incumbent asset manager desires to continue its asset management relationship with the Company after expiration of its asset management agreement, it shall submit a written bid proposal in accordance with the Company's RFP procedures. The bid proposal shall be evaluated pursuant to the procedures set forth in paragraph 4 above. N
6. The Company may develop additional procedures for asset management selection as it deems necessary and appropriate so long as such procedures are consistent with the agreed-upon procedures described herein. N
7. The Company shall retain all RFP documents and records for at least four (4) years and such documents and records shall be subject to the review and examination of the TRA Staff. The Asset Manager shall maintain documents and records of all transaction that utilize the Company's gas supply assets. All documents and records of such transactions shall be retained for two years after termination of the agreement and shall be subject to review and examination by the Company and the TRA Staff. N