BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

June 30, 2008

IN RE:	)	
	)	**DOCKET NO.**
REVIEW OF NASHVILLE GAS	)	**05-00165**
COMPANY'S INCENTIVE PLAN	)	
ACCOUNT RELATING TO ASSET	)	
MANAGEMENT FEES	)	

DISSENTING OPINION OF DIRECTOR RON JONES TO THE *ORDER APPROVING SETTLEMENT*

The above-styled docket came before a panel of the Tennessee Regulatory Authority during an Authority Conference on October 22, 2007, to consider the *Joint Request for Approval of Proposed Settlement Agreement of Nashville Gas Company, the Office of the Attorney General, Consumer Advocate and Protection Division, and the Audit Staff of the Tennessee Regulatory Authority*. At the October 22, 2007, Authority Conference, a majority of the panel voted to approve the *Proposed Settlement Agreement*. I dissented from this conclusion and offer this opinion in support of my vote.

I. RELEVANT PROCEDURAL HISTORY

On September 1, 2004, in Docket No. 04-00290, the Audit Staff of the Tennessee Regulatory Authority ("Authority") issued a finding in which it concluded that the incentive plan used by Nashville Gas Company ("NGC") did not allow for the inclusion of asset management fees in the calculation of shared savings.[1] On June 13, 2005, the panel voted in Docket No. 04-00290 to open a separate docket to revisit the structure of the shared savings percentages for the

[1] *In re: Nashville Gas Company, a Division of Piedmont Natural Gas Company Incentive Plan Account (IPA) Audit*, Docket No. 04-00290, *Notice of Filing by Utilities Division of the Tennessee Regulatory Authority*, Exhibit A, pp. 6-9 (Mar. 4, 2005).

capacity management incentive mechanism in the incentive plan account and, thereafter, to consider the Authority's future need to engage a consultant.[2]

On June 27, 2005, the panel assigned to Docket No 05-00165, the newly-created docket, convened the docket as a contested case and appointed the Authority's General Counsel or his designee to prepare the docket for hearing by the panel. On March 27, 2006, NGC, the Authority Staff, and the Consumer Advocate and Protection Division of the Office of the Attorney General ("Consumer Advocate") filed an *Agreed Motion to Stay Proceedings*. According to the motion, the parties were engaged in settlement negotiations and all agreed that judicial economy would be promoted by staying further proceedings.[3] On March 27, 2006, the Hearing Officer entered the *Order Granting Agreed Motion to Stay Proceedings*. On October 16, 2006, the parties reported that the negotiations were progressing and that there were a few issues that remained outstanding. At the request of the parties, the Chairman granted them additional time to continue their negotiations.[4] At the March 12, 2007, Authority Conference, the parties reported that the negotiations were progressing and that there were still a few issues that remained outstanding.[5]

On June 5, 2007, the parties filed the *Joint Request for Approval of Proposed Settlement Agreement of Nashville Gas Company, the Office of the Attorney General, Consumer Advocate and Protection Division, and the Audit Staff of the Tennessee Regulatory Authority*. Attached to

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[2] *In re: Nashville Gas Company, a Division of Piedmont Natural Gas Company Incentive Plan Account (IPA) Audit*, Docket No. 04-00290, *Order Adopting Incentive Plan Account Filing of Nashville Gas Company for Year Ended June 30, 2004*, p. 5 (Sept. 6, 2005).
[3] *Agreed Motion to Stay Proceedings*, p. 1 (Mar. 27, 2006).
[4] Transcript of Authority Conference, pp. 16-18 (Oct. 16, 2006).
[5] Transcript of Authority Conference, pp. 29-35 (Mar. 12, 2007).

the filing was the *Proposed Settlement Agreement*, which contained an effective date of July 1, 2006.[6]

During the August 20, 2007, Authority Conference, the panel questioned the parties with regard to the *Proposed Settlement Agreement*. During the October 22, 2007, Authority Conference, a majority of the panel voted to approve the *Proposed Settlement Agreement* with an effective date of July 1, 2006. The majority issued the *Order Approving Settlement* on December 14, 2007.

II. DISCUSSION

In the *Order Approving Settlement*, the majority relies on the following five findings to support their decision to approve the *Proposed Settlement Agreement*.

1. The parties "agree with the *Proposed Settlement Agreement*."
2. The parties "agreed that the Authority has the legal authority to approve the *Proposed Settlement Agreement*."
3. The "*Proposed Settlement Agreement* is in the public interest."
4. "Nashville Gas Company is not harmed by approval of the *Proposed Settlement Agreement*."
5. "[C]onsumers will benefit by approval of the *Proposed Settlement Agreement*."[7]

Because of my disagreement with the second finding, I cannot support approval of the *Proposed Settlement Agreement* as filed.[8]

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[6] *Joint Request for Approval of Proposed Settlement Agreement of Nashville Gas Company, the Office of the Attorney General, Consumer Advocate and Protection Division, and the Audit Staff of the Tennessee Regulatory Authority*, *Proposed Settlement Agreement*, p. 2 (Jun. 5, 2007).

[7] *Order Approving Settlement Agreement*, pp. 4-5 (Dec. 14, 2007).

[8] Although I do not specifically address the majority's findings other than the second finding, I note that during the deliberations I offered the following findings in support of the *Proposed Settlement Agreement.*

1. The *Proposed Settlement Agreement* addresses the structure of shared savings percentages of the capacity management incentive mechanism as was the purpose of this docket.
2. The *Proposed Settlement Agreement* simplifies the incentive plan mechanism.
3. The *Proposed Settlement Agreement* increases the ratepayers' sharing percentage in certain instances.
4. The *Proposed Settlement Agreement* provides for a request for proposal procedure and triennial review process.
5. The *Proposed Settlement Agreement* has benefits.

Transcript of Authority Conference, pp. 21-22 (Oct. 22, 2007).

The majority's second finding, in my opinion, speaks directly to the issue raised during the August 20, 2007, Authority Conference of whether the retroactive effective date of July 1, 2006, is violative of Tennessee Code Annotated section 65-5-103(b)(2).[9] In other words, the question is whether making the revisions contained in the *Proposed Settlement Agreement* effective July 1, 2006, results in an illegal refund. According to the majority, the parties agreed that such was not the case. However, I cannot and will not rely on the agreement of the parties when it comes to the resolution of a legal issue. It is incumbent upon me to review the legal authorities available and to make an independent assessment of the legal issue. Having done so in this case, I have determined that approving the proposed retroactive effective date does, in fact, result in the approval of an illegal refund. Therefore, I must reject the parties' agreement to the contrary.

The Consumer Advocate took the lead when the Chairman asked the parties about the issue of whether the retroactive effective date violates Tennessee Code Annotated section 65-5-103 or retroactive ratemaking generally. The Consumer Advocate did not assert that the effective date of the *Proposed Settlement Agreement* resulted in retroactive ratemaking, but argued that in the event that it did, it was permissible because "parties can agree to an order that otherwise would be retroactive ratemaking."[10] In support of its position, the Consumer Advocate relied on a single case - *South Central Bell Telephone Company v. Tennessee Public Service*

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[9] Tennessee Code Annotated section 65-5-103(b)(2) provides, in part:

> (2) Where increased rates or charges are thus made effective, the interested utility shall maintain its records in such a manner as will enable it, or the authority, to determine the amounts to be refunded and to whom due, in the event a refund is subsequently ordered by the authority as provided in this subdivision (b)(2). Upon completion of the hearing and decision, the authority may order the utility to refund, to the persons in whose behalf such amounts were paid, such portion of such increase, change or alteration as shall have been collected under bond and subsequently disallowed by the authority. . . .

Tenn. Code Ann. § 65-5-103(b)(2) (2004 Repl.).

[10] Transcript of Authority Conference, p. 53 (Aug. 20, 2007).

Commission.[11] While I generally agree with the Consumer Advocate's characterization of the facts of *South Central Bell Telephone Company v. Tennessee Public Service Commission,*[12] I cannot agree with the conclusion the Consumer Advocate gleaned from those facts.

In *South Central Bell Telephone Company v. Tennessee Public Service Commission*, the Tennessee Court of Appeals recognized that the Tennessee Public Service Commission ("Commission"), the predecessor of the Authority, did not have retroactive ratemaking authority. Specifically, the Court determined that the Commission was without authority to issue refunds except as provided for in Tennessee Code Annotated section 65-5-103.[13] In this case, South Central Bell Telephone Company ("SCB") had proposed to place into effect a rate increase based on an anticipated increase of depreciation expenses by the Federal Communications Commission ("FCC"). SCB further agreed that it would obtain a bond so that in the event that the FCC did not act as expected, SCB would refund any overcollected sums to ratepayers. SCB's agreement was offered in exchange for the Commission allowing SCB to place the rates into effect in advance of the FCC's action. Thereafter, the Commission, as a result of changes to FCC regulations, ordered SCB to refund approximately 6.4 million dollars to its customers. On review, the Chancery Court held that the refund was invalid. The Court of Appeals next heard the case, and, as earlier mentioned recognized at the outset that the Commission cannot issue a refund except as provided for in Tennessee Code Annotated section 65-5-103.[14] Specifically, the Court determined that the Commission may not "reserve the right to change rates retroactively thereby requiring a refund."[15] Thus, the Court concluded that had the Commission entered the

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[11] 675 S.W.2d 718 (Tenn. Ct. App. 1984).
[12] Transcript of Authority Conference, pp. 52-53 (Aug. 20, 2007).
[13] *South Cent. Bell Tel. Co. v. Tennessee Pub. Serv. Comm'n*, 675 S.W.2d 718, 719 (Tenn. Ct. App. 1984) (referencing the earlier codification of the statute at 65-5-203).
[14] *Id.*
[15] *Id.* at 720.

order approving the tariff and SCB challenged the validity of the order in a timely manner, then the Commission's order would have been reversed and vacated as *ultra vires*.[16] Next, the Court recognized that "the acceptance and retention of benefits may estop an attack upon the validity of an administrative order."[17] The Court next found that SCB had not timely challenged the Commission's order approving the rates and had benefited from the order and SCB's subsequent act of placing the rates into effect and collecting the additional revenue. Based on these findings, the Court concluded that SCB is "estopped to deny the validity of the action it sought and from which it has benefited."[18] Thus, contrary to the Consumer Advocate's argument, the Court of Appeals did not hold that parties can agree to an otherwise illegal refund or retroactive ratemaking. Instead, the Court firmly held that retroactive ratemaking is illegal, but also determined that the doctrine of estoppel prohibited SCB from contesting the validity of the action from which it did not timely appeal and from which it benefited.

The Court of Appeals has recognized the prohibition against retroactive ratemaking in other appellate decisions. In 1994, the Tennessee Court of Appeals recognized that the Commission "has no statutory authority to fix rates retroactively or to order refunds except in very limited circumstances."[19] In this case, the court addressed a plan of regulatory reform through which the Commission would order refunds to consumers and require excess revenues to be used to modernize the telecommunications infrastructure in Tennessee.[20] The Court found

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[16] *Id.*
[17] *Id.*
[18] *Id.*
[19] *American Assoc. of Retired Persons v. Tennessee Pub. Serv. Comm'n*, 896 S.W.2d 127, 134 (Tenn. Ct. App. 1994).
[20] *Id.* at 130-131 (referencing Authority Rule 1220-4-2-.55).

that the plan did not involve refunds or retroactive ratemaking because the rule at issue provided for prospective rate adjustments and service improvements.[21]

Similarly, in 1996, the Court of Appeals recognized its consistently held position that the Commission "does not have the authority to approve temporary or tentative rates subject to refund" except as expressly provided for in Tennessee Code Annotated section 65-5-103.[22] In this case, the Court reviewed an order of the Commission that allowed Kentucky Power Company to pass through its purchased power costs to consumers without a ratemaking proceeding. The Court noted that the conditions described in Tennessee Code Annotated section 65-5-103 were not present, but also distinguished the facts before it from those before the Court in *South Central Bell Telephone Company v. Tennessee Public Service Commission.*[23] The point of distinction noted by the Court was that in this case the refund provision of the Commission's order was "necessary to complete the obvious intent of the federal scheme to refund to the class that ultimately has had to pay it."[24]

The Court of Appeals again addressed retroactive ratemaking in 2000. In this case, the Consumer Advocate challenged the decision of the Authority to approve BellSouth Telecommunications, Inc.'s price regulation plan with a retroactive effective date.[25] The Court explained that the Authority's order resulted only in prospective rate changes and avoided the essence of retroactive ratemaking, that is, requiring future ratepayers to pay for past use.[26]

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[21] *Id.* at 134.
[22] *Consumer Advocate Div. v. Bissell*, 1996 WL 482970, *3 (Tenn. Ct. App. Aug. 28, 1996) (referencing the earlier codification of the statute at 65-5-203) (citing *South Cent. Bell Tel. Co. v. Tennessee Pub. Serv. Comm'n*, 675 S.W.2d 718, 719 (Tenn. Ct. App. 1984)).
[23] *Id.*
[24] *Id.*
[25] *Consumer Advocate Div. v. Tennessee Regulatory Auth.*, 2000 WL 13794, *3 (Tenn. Ct. App. Jan. 10, 2000).
[26] *Id.* (citing *Porter v. South Carolina Pub. Serv. Comm'n*, 493 S.E.2d 92 (S.C. 1997)).

Having reviewed the cited appellate decisions, it is my opinion that approving the *Proposed Settlement Agreement* with a July 1, 2006, effective date results in retroactive ratemaking, specifically an illegal refund. According to the case law, the Authority is limited in its ability to order a refund to those instances when the facts permit a refund pursuant to Tennessee Code Annotated section 65-5-103 or when the refund is necessary to complete the intent of a federal scheme. Neither of these exceptions is present here. The result of approving the *Proposed Settlement Agreement* with the July1, 2006, effective date is to provide ratepayers a one-time refund of a portion of the gas costs already paid. The Authority is prohibited from taking such an action.

It is socially and politically appealing to approve a refund to consumers. Moreover, in this instance with all the parties agreeing to the refund there will be no opportunity for the Court of Appeals to review the majority's decision. Despite these favorable circumstances, I am constrained by the law from approving the *Proposed Settlement Agreement* as filed and will not take an action that, in my opinion, sets a dangerous precedent. Based on the foregoing, it is my conclusion that the *Proposed Settlement Agreement* should be denied.

Ron Jones, Director