TENNESSEE REGULATORY AUTHORITY

460 James Robertson Parkway
Nashville, Tennessee 37243-0505

December 14, 2005

Ron Jones, Chairman
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, TN 37243

Re: Review of Nashville Gas Company's IPA Relating to Asset Management Fees
Docket Number: 05-00165

Dear Chairman Jones,

Please find enclosed for filing in the above-referenced matter *TRA Staff's First Discovery Responses to Nashville Gas Company*. Please call me at extension 203 if you have any questions.

Sincerely,

Aaron Rochelle

Aaron Rochelle
Counsel, Authority Staff

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www.state.tn.us/tra

BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

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

TRA STAFF'S DISCOVERY RESPONSES TO NASHVILLE GAS COMPANY

Pursuant to the Procedural Schedule established at the November 2, 2005 Status Conference in this docket and Tenn. Comp. R. and Reg. 1220-1-2-.11, the staff of the Tennessee Regulatory Authority that is participating in this docket as a party ("TRA Staff") responds to the discovery requests of Nashville Gas Company ("Nashville Gas" or the "company") as follows:

1. *State the TRA Staff's position on the issue of whether asset management fees received by Nashville Gas should be included in Nashville Gas' Incentive Plan Account.*

RESPONSE:

At this time, the TRA Staff has not formulated a position as to whether the asset management fees received by Nashville Gas should be included in Nashville Gas' Incentive Plan Account. The TRA Staff is aware of its continuing obligation pursuant to Tenn. R. Civ. Pro. 26.05 to seasonably supplement this response.

2. *With respect to the position stated in response to the foregoing discovery request:*

(a) *Identify each and every factual basis relied upon by the TRA Staff in reaching such position;*

RESPONSE:

1. Nashville Gas' Incentive Plan tariff does not address, either explicitly or implicitly, the concept of asset management or the treatment of asset management fees.

2. The practice of assigning the management of a public utility's assets to a third party asset manager in exchange for a fee was not contemplated at the time Nashville Gas' Incentive Plan was crafted.

(b) *Identify each and every legal basis relied upon by the TRA Staff in reaching such position;*

RESPONSE:
The language in Nashville Gas' Incentive Plan tariff does not address asset management by a third party asset manager or any sharing mechanism applicable for the asset management fees. Therefore, the TRA Staff has not determined its position.

(c) *Identify each and every witness the TRA Staff intends to call to support such position; and*

RESPONSE:
The witnesses that will testify to support such position have not been determined.

(d) *Identify each and every document relating to, or reviewed or relied upon in reaching such position.*

RESPONSE:
The TRA Staff has reviewed the following document: SERVICE SCHEDULE NO. 316 - Performance Incentive Plan, effective July 1, 1996.

3. *State the TRA Staff's position on what structure or structures for the sharing of savings as between the Company and ratepayers will be proposed by the TRA Staff in this docket for utilization under the Company's Incentive Plan.*

RESPONSE:
The TRA Staff does not have a position concerning a savings sharing structure, but intends to develop a position from this first round of discovery and other fact-finding it may pursue.

4. *With respect to the position stated in response to the foregoing discovery request:*

(a) *Identify each and every factual basis relied upon by the TRA Staff in reaching such position;*

RESPONSE:
See response to Interrogatory # 2 (a).

(b) *Identify each and every legal basis relied upon by the TRA Staff in reaching such position;*

RESPONSE:
See response to Interrogatory # 2 (b).

(c) Identify each and every witness the TRA Staff intends to call to support such position.

RESPONSE:
See response to Interrogatory # 2 (c).

(d) *Identify each and every document relating to, or reviewed or relied upon in reaching such position.*

RESPONSE:
See response to Interrogatory # 2 (d).

5. *Identify each and every change to Nashville Gas' Incentive Plan or Incentive Plan Account which the TRA intends to or will propose in this docket.*

RESPONSE:
The TRA Staff has not determined what, if any, changes to Nashville Gas' IPA to propose at this time.

6. With respect to each such change identified in response to the foregoing discovery request:

(a) Identify each and every factual basis relied upon by the TRA Staff in reaching such position;

RESPONSE:
See response to Interrogatory # 2 (a).

(b) *Identify each and every legal basis relied upon by the TRA Staff in reaching such position;*

RESPONSE:
See response to Interrogatory # 2 (b).

(c) *Identify each and every witness the TRA Staff intends to call to support such position; and*

RESPONSE:
See response to Interrogatory # 2 (c).

(d) *Identify each and every document relating to, or reviewed or relied upon in reaching such position.*

RESPONSE:
See response to Interrogatory # 2 (d).

7. *To the extent not provided in response to the foregoing questions, identify each and every matter or issue about which the TRA Staff intends to present evidence or argument in this proceeding and the TRA Staff's position thereon. With respect to each such change identified in response to the foregoing discovery request:*

RESPONSE:
See response to Interrogatory # 1, 2, 3, & 5.

8. *With respect to each matter, issue, or position identified in response to the foregoing discovery request:*

(a) *Identify each and every factual basis relied upon by the TRA Staff in reaching such matter, issue, or position;*

RESPONSE:
See response to Interrogatory # 2 (a).

(b) *Identify each and every legal basis relied upon by the TRA Staff in reaching such matter, issue, or position;*

RESPONSE:
See response to Interrogatory # 2 (b).

(c) *Identify each and every witness the TRA Staff intends to call to support such matter, issue, or position;*

RESPONSE:
See response to Interrogatory # 2 (c).

(d) *Identify each and every document relating to, or reviewed or relied upon by the TRA Staff with respect to such matter, issue, or position.*

RESPONSE:
See response to Interrogatory # 2 (d).

9. *With respect to each person you expect to call as a witness, including any expert witness, regarding this matter, state or provide:*

RESPONSE:
The witnesses that will testify to support such position have not been determined. The TRA Staff is aware of its continuing obligation to seasonably supplement this response pursuant to Tenn. R. Civ. Pro. 26.05.

(a) *The witness' full name and work address;*

RESPONSE:

The witnesses that will testify to support such position have not been determined. The TRA Staff is aware of its continuing obligation to seasonably supplement this response pursuant to Tenn. R. Civ. Pro. 26.05.

(b) *The subject matter (or subject matters) about which the witness is expected to testify;*

RESPONSE:

The witnesses that will testify to support such position have not been determined. The TRA Staff is aware of its continuing obligation to seasonably supplement this response pursuant to Tenn. R. Civ. Pro. 26.05.

(c) *The substance of the facts and opinions to which any expert is expected to testify;*

RESPONSE:

The witnesses that will testify to support such position have not been determined. The TRA Staff is aware of its continuing obligation to seasonably supplement this response pursuant to Tenn. R. Civ. Pro. 26.05.

(d) *A summary of the grounds or basis of each opinion to which such witness is expected to testify;*

RESPONSE:

The witnesses that will testify to support such position have not been determined. The TRA Staff is aware of its continuing obligation to seasonably supplement this response pursuant to Tenn. R. Civ. Pro. 26.05.

(e) *Whether or not the expert has prepared a report, letter, or memorandum of his/her findings, conclusions, or opinions;*

RESPONSE:

The witnesses that will testify to support such position have not been determined. The TRA Staff is aware of its continuing obligation to seasonably supplement this response pursuant to Tenn. R. Civ. Pro. 26.05.

(f) The witness's background information, including current employer, education, professional and employment history, and qualifications within the field in which the expert is expected to testify;

RESPONSE:

The witnesses that will testify to support such position have not been determined. The TRA Staff is aware of its continuing obligation to seasonably supplement this response pursuant to Tenn. R. Civ. Pro. 26.05.

(g) An identification of any matter in which the expert has testified by specifying the name, docket number and forum of each such case, and the dates of the prior testimony;

RESPONSE:

The witnesses that will testify to support such position have not been determined. The TRA Staff is aware of its continuing obligation to seasonably supplement this response pursuant to Tenn. R. Civ. Pro. 26.05.

(h) The identity of all documents shown to, delivered to, received from, relied upon, or prepared by any expert witness related to the witness' expected testimony in this case.

RESPONSE:

The witnesses that will testify to support such position have not been determined. The TRA Staff is aware of its continuing obligation to seasonably supplement this response pursuant to Tenn. R. Civ. Pro. 26.05.

10. Identify each and every member of the TRA Staff designated to participate as a party in this proceeding.

RESPONSE:
Pat Murphy, Utilities Division
Paul Greene, Utilities Division
Gary Lamb, Utilities Division
Butch Phillips, Utilities Division
Jerry Kettles, Competitive Markets & Policy Division
Gary Hotvedt, Legal Division

11. Identify each and every member of the TRA Staff, and each and every current or former member of the Advisory Staff who previously participated in formulating the Staff's recommendations in Docket Nos. 03-00489 and 04-00290, or who advocated or advised the TRA in those proceedings regarding the establishment of a contested case relating to the matters at issue in this docket.

RESPONSE:
The TRA Staff does not have sufficient information to identify members of the Advisory Staff, but avers that no member listed in the Response to Interrogatory # 10 has served in the Advisory Staff concerning Dockets # 03-00489 and 04-00290.

12. Identify each and every communication with the Consumer Advocate regarding the matters set for hearing in this proceeding and with respect to each:

RESPONSE:
Staff objects to question 12 (a-c) because of the protections by the attorney-client privilege and attorney work product doctrine.

(a) *State the subject and substance thereof;*

RESPONSE:
Staff objects to question 12 (a-c) because of the protections by the attorney-client privilege and attorney work product doctrine.

(b) *Identify the date and means thereof; and*

RESPONSE:
Staff objects to question 12 (a-c) because of the protections by the attorney-client privilege and attorney work product doctrine.

(c) Identify each and every document in the possession, custody, or control of the Consumer Advocate evidencing, relating or referring thereto.

RESPONSE:
Staff objects to question 12 (a-c) because of the protections by the attorney-client privilege and attorney work product doctrine.

13. Identify all exhibits which the TRA Staff intends to introduce into evidence in this proceeding.

RESPONSE:
SERVICE SCHEDULE NO. 316 - Performance Incentive Plan, effective July 1, 1996. The TRA Staff is aware of its continuing obligation to seasonably supplement this response pursuant to Tenn. R. Civ. Pro. 26.05.

14. Produce a copy of all documents identified in response to the foregoing discovery requests.

RESPONSE:
SERVICE SCHEDULE NO. 316 - Performance Incentive Plan, effective July 1, 1996.

15. *Identify each and every person who provided information or participated in the preparation of the responses to these discovery requests and indicate which responses each such person worked on or provided information for.*

RESPONSE:
Pat Murphy, Utilities Division

Respectfully submitted,

Aaron Rochelle

Aaron Rochelle, Counsel
Tennessee Regulatory Authority
460 James Robertson Pkwy.
Nashville, Tennessee 37243-0505
(615)741-3191
Dated: November 14, 2005

CERTIFICATE OF SERVICE

I, Aaron Rochelle, hereby certify that I have served a copy of the foregoing Discovery Requests on the following persons by hand delivery or by depositing a copy of the same in the United States Mail, postage prepaid, addressed to them at the addresses shown below, this 14th day of December, 2005.

R. Dales Grimes, Esq.
Bass, Berry & Sims, PLC
AmSouth Center
315 Deaderick Street, Suite 2700
Nashville, Tennessee 37238-3001

James H. Jeffries IV, Esq.
Nelson, Mullins, Riley & Scarborough, L.L.P.
Bank of America Corporate Center, Suite 2400
100 North Tryon Street
Charlotte, North Carolina 28202-4003

Stephen Butler & Joe Shirley, Esq.
Consumer Advocate and Protection Division of the Office of the Attorney General
Post Office Box 20207
Nashville, Tennessee 37202

Aaron Rochelle
Aaron Rochelle

SERVICE SCHEDULE NO. 316
Performance Incentive Plan

APPLICABILITY

The Performance Incentive Plan (the plan) replaces the reasonableness or prudence review of Nashville Gas Company's (Nashville or Company) gas purchasing activities overseen by the Tennessee Regulatory Authority (Authority). The plan is designed to provide incentives to Nashville in a manner that will produce rewards for its customers and its shareholders and improvements in Nashville's gas procurement activities. Each plan year will begin July 1. The annual provisions and filings herein would apply to this annual period. The Plan will continue until the Plan is either (a) terminated at the end of a plan year by not less than 90 days notice by Nashville to the Authority or (b) the Plan is modified, amended or terminated by the Authority.

OVERVIEW OF STRUCTURE

Nashville's Performance Incentive Plan is comprised of two interrelated components.

- Gas Procurement Incentive Mechanism
- Capacity Management Incentive Mechanism

The Gas Procurement Incentive Mechanism establishes a predefined benchmark index to which Nashville's commodity cost of gas is compared. It also addresses the recovery of gas supply reservation fees, the treatment of off-system sales and wholesale interstate sale for resale transactions, and the use of financial or private contracts in managing gas costs. The net incentive benefits or costs will be shared between the Company's customers and the Company on a 50% / 50% basis.

The Capacity Management Incentive Mechanism is designed to encourage Nashville to actively market off-peak unutilized transportation and storage capacity on upstream pipelines in the secondary market. The net incentive benefits or costs will be shared between the Company's customers and the Company utilizing a graduated sharing formula, with sharing percentages for Nashville ranging between zero and fifty percent.

The Company is subject to a cap on overall incentive gains or losses of $1.6 million annually. In connection with the Performance Incentive Plan, Nashville shall file with the Authority Staff, and update each year a Three Year Supply Plan. Nashville will obtain additional firm capacity and/or gas supply pursuant to such plan.

GAS PROCUREMENT INCENTIVE MECHANISM

The Gas Procurement Incentive Mechanism addresses the following areas:

- Commodity Costs
- Gas Supply Reservation Fees
- Off-System Sales and Sale for Resale Transactions
- Use of Financial Instruments or Other Private Contracts

COMMODITY COSTS

Each month Nashville will compare its *total city gate commodity cost of gas*[1] to a benchmark dollar amount. The benchmark gas cost will be computed by multiplying total actual purchase quantities for the month by a price index. The monthly price index is defined as

$$I = F_f(P_0K_0+P_1K_1+P_cK_c+\ldots P_\infty K_\infty)+F_oO+F_dD;\text{ where}$$

$$F_f+F_o+F_d= 1;\text{ and}$$

I = the monthly city gate commodity gas cost index.

F_f = the fraction of gas supplies purchased in the first-of-the-month market which are transported to the city gate under Nashville's FT service agreements.

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1 Gas purchases under Nashville's existing supply contract on the Tetco system are excluded from the incentive mechanism. Nashville will continue to recover 100 percent of these costs through its PGA with no profit or loss potential. Extension or replacement of such contract shall be subject to the same competitive bidding procedures that will apply to other firm gas supply agreements. In addition, Nashville's gas procurement incentive mechanism will measure storage gas supplies against the benchmark index during the months such quantities are purchased for injection. For purposes of comparing such gas purchase costs against the monthly city gate index price, Nashville will exclude any commodity costs incurred downstream of the city gate to storage so that Nashville's actual costs and the benchmark index are calculated on the same basis.

P = the *Inside FERC Gas Market Report* price index for the first-of-the-month edition for a geographic pricing region, where subscript 0 denotes Tennessee Gas Pipeline (TGP) Rate Zone 0; subscript 1 denotes TGP Rate Zone 1; subscript C denotes Columbia Gas Transmission (CGT), Louisiana, plus applicable transportation and fuel charges in CGT's FT tariff to Rayne, and subscript $\propto$ denotes new incremental firm services to which Nashville may subscribe in the future.[2] The commodity index prices will be adjusted to include the appropriate pipeline maximum firm transportation (FT) commodity transportation charges and fuel retention to the city gate under Nashville's FT service agreements.

K = the fraction (relative to total maximum daily contract entitlement) of Nashville's total firm transportation capacity under contract in a geographic pricing region, where the subscripts are as above.[3]

F_o = the fraction of gas supplies purchased in the first-of-the-month spot market which are delivered to Nashville's system using transportation arrangements other than Nashville's FT contracts.

O = the weighted average of *Inside FERC Gas Market Report* first-of-the-month price indices, plus applicable maximum IT rates and fuel retention, from the source of the gas to the city gate, where the weights are computed based on actual purchases of gas supplies purchased by Nashville and delivered to Nashville's system using transportation arrangements other than Nashville's FT contracts.

F_d = the fraction of gas supplies purchased in the daily spot market.

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2 To the extent that Nashville renegotiates existing reservation fee supply contracts or executes new reservation fee supply contracts with commodity pricing provisions at a discount to the first-of-the-month price index, Nashville shall modify the monthly commodity price index to reflect such discount.

3 Because the aggregate maximum daily contract quantities in Nashville's FT contract portfolio vary by month over the course of the year, the weights will be recalculated each month to reflect actual contract demand quantities for such month. The contract weights, and potentially the price indices used, will also vary as Nashville renegotiates existing or adds new FT contracts. As new contracts are negotiated, Nashville shall modify the index to reflect actual contract demand quantities and the commodity price indices appropriate for the supply regions reached by such FT agreements.

D = the weighted average of daily average index commodity prices taken from *Gas Daily* for the appropriate geographic pricing regions, where the weights are computed based on actual purchases made during the month. The commodity index prices will be adjusted to include the appropriate maximum transportation commodity charges and fuel retention to the city gate.

If the actual total commodity gas purchase cost in a month is within one percent of the benchmark dollar amount, there will be no incentive gains or losses. If the actual total commodity gas purchase cost varies from the benchmark dollar allowance by more than one percent, the variance in excess of the one percent threshold shall be deemed incentive gains or losses under the plan. Such gains or losses will be shared 50/50 between the Company and the ratepayers.

<u>Gas Supply Reservation Fees</u>

Nashville will continue to recover 100% of gas supply reservation fee costs through its PGA with no profit or loss potential. For new contracts and/or contracts subject to renegotiation during the Plan year, Nashville will solicit bids for gas supply contracts containing a reservation fee.

<u>Off-System Sales And Sale For Resale Transactions</u>

Margin on off-system sales and wholesale sale-for-resale transactions using Nashville's firm transportation and capacity entitlements (the costs of which are recovered from Nashville's ratepayers) shall be credited to the commodity gas cost component of the Gas Procurement Incentive Mechanism and will be shared with ratepayers. Margin on such sales will be defined as the difference between the sales proceeds and the total variable costs incurred by Nashville in connection with the transaction, including transportation and gas costs, taxes, fuel, or other costs. For purposes of gas costs, Nashville will impute such costs for its related supply purchases at the benchmark first-of-the-month or daily index, as appropriate, on the pipeline and in the zone in which the sale takes place. The difference between Nashville's actual costs and such index price is taken into account under the Gas Procurement Incentive Mechanism. As to transportation costs, Nashville will impute such costs up to the transporting pipeline's maximum interruptible transportation (IT) rate. The difference between the maximum IT rate and Nashville's actual transportation commodity costs will be treated as capacity release margin under the Capacity Management Incentive Mechanism. After deducting the total transaction costs from the sales proceeds, any remaining margin will be credited to commodity gas costs and shared on a 50/50 basis with ratepayers.

<u>Use Of Financial Instruments Or Other Private Contracts</u>

To the extent Nashville uses futures contracts, financial derivative products, storage swap arrangements, or other private agreements to hedge, manage or reduce gas costs, any gains or losses will flow through the commodity cost component of the Gas Procurement Incentive Mechanism.

CAPACITY MANAGEMENT INCENTIVE MECHANISM

To the extent Nashville is able to release transportation or storage capacity, or generate transportation or storage margin associated with off-system or wholesale sales-for-resale, the associated cost savings shall be shared by Nashville and customers according to the following sharing formula:

Capacity Management Incentive cost savings as a percent of Nashville's annual transportation and storage demand costs.	Sharing percentages Nashville/Customers. (Percent)
Less than or equal to 1 percent	0/100
Greater than 1 percent but less than or equal to 2 percent	10/90
Greater than 2 percent but less than or equal to 3 percent	25/75
Greater than 3 percent	50/50

The sharing percentages shall be determined based on the actual demand costs incurred by Nashville (exclusive of credits for capacity release) for transportation and storage capacity during the plan year, as such costs may be adjusted due to refunds or surcharges from pipeline and storage suppliers. Any incentive gains or losses resulting from adjustments to the sharing percentages caused by refunds or surcharges shall be recorded in the current Incentive Plan Account (IPA).

DETERMINATION OF SHARED SAVINGS

Each month during the term of plan, Nashville will compute any gains or losses in accordance with the plan. If Nashville earns a gain, a separate Incentive Plan Account (IPA) will be debited with such gain. If Nashville incurs a loss, that same IPA will be credited with such loss. During a plan year, Nashville will be limited to overall gains or losses totaling $1.6 million. Interest shall be computed on balances in the IPA using the same interest rate and methods as used in Nashville's Actual Cost Adjustment (ACA) account. The offsetting entries to IPA gains or losses will be recorded to income or expense, as appropriate. At its option, however, Nashville may temporarily record any monthly gains in a non-regulatory deferred credit balance sheet account until results for the entire plan year are available.

Gains or losses accruing to the Company under the Plan will form the basis for a rate increment or decrement to be filed and placed into effect separate from any other rate adjustments to recover or refund such amount over a prospective twelve-month period.

Each year, effective November 1, the rates for all customers, excluding interruptible transportation customers who receive no direct benefit from any gas cost reductions resulting from the plan, will be increased or decreased by a separate rate increment or decrement designed to amortize the collection or refund of the June 30 IPA balance over, the succeeding twelve month period. The increment or decrement will be established by dividing the June 30 IPA balance by the appropriate volumetric billing determinants for the twelve months ended June 30. During the twelve month amortization period, the amount collected or refunded each month will be computed by multiplying the billed volumetric determinants for such month by the increment or decrement, as applicable. The product will be credited or debited to the IPA, as appropriate. The balance in the IPA will be tracked as a separate collection mechanism.

FILING WITH THE AUTHORITY

The Company will file calculations of shared savings and shared costs quarterly with the Authority not later than 60 days after the end of each interim fiscal quarter and will file an annual report not later than 60 days following the end of each plan year. Unless the Authority provides written notification to the Company within 180 days of such reports, the Incentive Plan Account 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 utilized by the Company, and the composition of the Company'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 justification to the Company within 30 days of such notice, the price indices shall be deemed approved as proposed by the Company.

GAS SUPPLY INCENTIVE COMPENSATION PROGRAM

The Company has in place a Gas Supply Incentive Compensation Program (the Program) designed to provide incentive compensation to selected Gas Supply non-executive employees involved in the implementation of the Nashville Incentive Plan and Secondary Marketing Programs in a manner consistent with the benefits achieved for customers and shareholders through improvements in gas procurement and secondary marketing activities. Participants in the program receive incentive compensation as recognition for their contribution to the customers and shareholders of the Company through lower gas costs and gains related thereto. Performance measures are established for the Program each year.

During the time this tariff is in effect, the Company will continue to have in place the Gas Supply Incentive Compensation Program, as detailed to the Authority, as it relates to the Nashville Incentive Plan. The Company will advise the Authority in writing of any changes to the Program, and unless the Company is advised within 60 days, said changes will become effective. No filing for prior approval is required for changes in the performance measures.