

**BEFORE THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE**

August 7, 2006

*In re: Petition to Open an Investigation to)
Determine Whether Atmos Energy Corp. Should be)
Required by the TRA to Appear and Show Cause)
That Atmos Energy Corp. is Not Overearning in)
Violation of Tennessee Law and That it is Charging)
Rates That are Just and Reasonable)*

Docket No. 05-00258

**TRA INVESTIGATIVE STAFF RESPONSES TO DISCOVERY REQUEST OF THE
CONSUMER ADVOCATE AND PROTECTION DIVISION**

The TRA Investigative Staff ("Staff") responds to the Consumer Advocate and Protection Division's Discovery Request as follows.

QUESTION 1. Please produce copies of all hearing exhibits that you will introduce, use, or reference during the Phase One Hearing.

RESPONSE: No determination has been made concerning exhibits to be presented at hearing at this time.

QUESTION 2. Please produce copies of all documents – including, without limitation, workpapers, spreadsheets, summaries, charts, notes, exhibits, articles, journals, treatises, periodicals, publications, reports, records, statements, Internet web pages, or financial information – that support the factual assertions, conclusions, or opinions of Mr. Jerry Kettles in this matter.

RESPONSE: See response to Question 4, below.

QUESTION 3. Please produce copies of all documents – including, without limitation, workpapers, spreadsheets, summaries, charts, notes, exhibits, articles, journals, treatises, periodicals, publications, reports, records, statements, Internet web pages, or financial information – that relied the factual assertions, conclusions, or opinions of Mr. Jerry Kettles in this matter.

RESPONSE: See response to Question 4, below.

QUESTION 4. Please produce copies of all documents – including, without limitation, workpapers, spreadsheets, summaries, charts, notes, and exhibits – created by or for or prepared by or for Mr. Jerry Kettles in evaluating, reaching conclusions, or formulating an opinion in this matter.

RESPONSE: During preparation of testimony, I viewed information from the Wall Street Journal, Yahoo! Finance, Value Line, Standard and Poor's and other outlets for information on the gas industry and other economic variables. No attempt was made to track or record the information viewed and such tracking would not occur as part of normal work.

I relied on both print and electronic information within the MFR responses provided by the company. I also consulted Ibbotson Associates 2004 Yearbook and 2002 Valuation Guide as found in the Nashville Public library. Both texts are reference materials that cannot be removed from the library. Photocopies of pages containing data used in my analysis are provided, however. See documents Bates numbered 2485-3464.

QUESTION 5. Please state whether the TRA Investigative Staff will take a position regarding the cost of capital and/or capital structure of Atmos Energy Corporation proposed during Phase One of this docket by the Consumer Advocate and Atmos Energy Corporation.

RESPONSE: TRA Investigative Staff has not yet determined if it will take a position on the CAPD's testimony on the capital structure and cost of capital of Atmos.

QUESTION 6. Please state in detail and provide all supporting grounds for any position taken by the TRA Investigative Staff regarding the cost of capital and/or capital structure of Atmos Energy Corporation proposed during Phase One of this docket by the Consumer Advocate and Atmos Energy Corporation.

RESPONSE: TRA Investigative Staff has not yet determined if it will take a position on the CAPD's testimony on the capital structure and cost of capital of Atmos.

QUESTION 7. Mr. Jerry Kettles testified: "Ultimately consumers are harmed by the inability of the firm to attract sufficient capital to finance facility improvements, safety upgrades, and expand service to new areas." Kettles Direct at 3.

- a. If Mr. Kettles is aware of any facility improvements in Tennessee made by Atmos, identify for each: when the improvement was made, where the improvement was made, the cost of the improvement, and the method of financing Atmos used to finance the improvements (e.g., internal funds, short-term borrowings, long-term borrowings, etc.).
- b. Explain how the term "new" is defined as used on page 3, line 14 and identify the "new areas" in Tennessee that Atmos is serving.
- c. If Mr. Kettles is aware of any safety upgrades in Tennessee made by Atmos, identify the safety upgrade, as well as where it was made and when it was made.
- d. How far into the future is "ultimately" as used on page 3, line 14 (e.g. a month, a year, a decade, etc.).

RESPONSE: For each item in CAPD Request No. 7, I make no representation that the quoted passages apply specifically to Atmos or that I have any specific knowledge of ongoing capital projects such as

improvements, safety upgrades or expansion of territory in Tennessee by Atmos. The statement simply notes the relationship between financial health of a regulated utility to its ability to provide quality service. Specific responses follow:

- a. I am unaware of any facility improvements made by Atmos in Tennessee.
- b. I am unaware of any new service areas or expansion of current service areas by Atmos in Tennessee.
- c. I am unaware of any specific safety upgrades being made in Tennessee by Atmos.
- d. Ultimately does not refer to a specific time as referenced on page 3, line 14.

QUESTION 8. **Regarding Mr. Kettles' testimony at page 5 lines 5-6 that "given Atmos' history with respect to short-term debt, it is appropriate to exclude short-term debt from the company's capital structure," identify the duration of the "history" Mr. Kettles considered (e.g. was this "history" based on six months, one year, two years or more of information).**

RESPONSE: Two years of monthly information.

QUESTION 9. **Regarding Mr. Kettles' testimony on page 11, lines 8-9 that there is a "prevailing market return of 12.5%," provide copies of the source, copies of the data, and show the calculations which lead to the 12.5%.**

RESPONSE: I used the Ibbotson's 2004 Stock, Bond, Bills and Inflation Yearbook. Data through 2003 are included in the 2004 Yearbook calculations. The 2004 Yearbook was the most recent edition available to the analyst. The 12.5% return statistic is derived by looking at the central tendency several long term measures of market returns. All data are provided in the attached sheets from the Ibbotson's publication referenced above. First, I looked at arithmetic mean of large company stock returns for 1926 to 2003. This return is reported as 12.4%.

I reviewed the returns for holding investments 20 years as detailed in Table 2.11. Over the most recent time period reported, 1984 to 2003, large company stocks grew 12.99 percent. Over the same time frame, small company stocks grew 12.35%. Averaging the two returns provides a broader measure of long term growth across both large and small companies which should be indicative of the growth in the market as a whole. The average return of large and small company stocks held over the twenty year period 1984 to 2003 yields a 12.67% return. I adjusted the long term (1926 – 2003) large company stock return upwards by simply averaging the 12.4% large stock return with the 12.67% return figure described above. The resulting figure of 12.53% was rounded downward to 12.5% for use in the analysis.

While long-term growth rates are relatively stable and do not vary substantially from year to year, I reserve the right to incorporate more recent data on market returns in my analysis. See documents Bates numbered 3461-3464.

QUESTION 10. **Regarding Mr. Kettles’ testimony at page 10 lines 14-15 that he used “[beta] calculations from Value Line ... they have been used by several witnesses,” identify Mr. Kettles efforts to make his own independent assessment of Value Line’s betas and provide a copy of that effort, if it resulted in an analysis.**

RESPONSE: I did not attempt to manually calculate or recreate the Value Line Beta estimates. I am aware of technique Value Line uses to calculate its betas as report in the Ibbotson Associates Valuation Edition.

QUESTION 11. **Regarding Mr. Kettles’ testimony at page 13 lines 3-4 that he used “long-term forecasts of growth in earnings per share and dividends per share in my calculations,” identify Mr. Kettles’ efforts to make his own independent assessment of those forecasts and provide a copy of that effort, if it resulted in an analysis.**

RESPONSE: With respect to earnings per, I calculated various term compound growth rates assuming \$0.02 annual dividend growth.

QUESTION 12. Regarding Mr. Kettles' testimony at page 2 lines 2-4 that his "testimony is a recommendation on the fair rate of return ...based on .. prevailing economic conditions," identify and explain all "prevailing economic conditions" affecting Mr. Kettles' recommendation of a "fair rate of return," and explain if there are differences, if any, between "prevailing economic conditions" and forecasted economic conditions.

RESPONSE: As a normal part of my job, I monitor the aggregate U.S. economy with respect to data commonly reported in the Wall Street Journal and similar publications. Such items included, but are not limited to, interest rates, inflation, wage growth, employment statistics, and output measures. In my testimony, the prevailing conditions are levels of variables used in the analysis that exist at a period of time that is close to the filing of the testimony. As an example, data on interest rates and 52-week stock prices represent data reflective of prevailing conditions in the economy. Forecasted values, such as the risk free return used in my CAPM analysis are forecast values derived from prevailing conditions.

QUESTION 13. Regarding Mr. Kettles' testimony at page 9, line 34 that he "removed [certain companies] because they have an inconsistent history of dividend payments," provide an explanation of what Mr. Kettles considers as inconsistent dividend payments.

RESPONSE: Per the Value Line data used in my analysis, each company had suspended dividend payments. Semco Energy suspended dividend payments as of June 2004 and had not resumed payments as of June 2006. Southern Union paid a 5% common stock dividend until the end of 2005. Cash dividend payments for

Southern Union were paid in mid-April 2006. Companies with inconsistent dividend payments are those who have failed to pay cash dividends in the recent past.

QUESTION 14. **Regarding Mr. Kettles' Schedule JLK-6, if Mr. Kettles performed an analysis to examine the consistency of earnings per share history for the companies displayed, provide a copy of that analysis.**

RESPONSE: I reviewed the historical earnings per share data provided by Value Line but did not independently attempt to recreate their forecast values.

QUESTION 15. **Refer to Mr. Kettles' Schedule JLK-3 and either admit or deny the following:**

- a. Notes with GS6M interest are more risky than notes with a GS20 interest rate.**
- b. The risk of a note with a GS6M interest is equal to the risk of a note with a GS20 interest rate.**
- c. The interest rate applied to a note is not related to the risk of the note.**

RESPONSE: Each response below refers to the default risk of the respective government security.

- a. Deny.
- b. Admit.
- c. Admit.

Respectfully submitted,

By: 

Gary R. Hotvedt (#16468)
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, Tennessee 37243
(615) 741-3191 x. 212

Counsel for TRA Investigative Staff

CERTIFICATE OF SERVICE

I hereby certify that a true and exact copy of the foregoing has been forwarded by electronic mail to the following parties on the 7th day of August, 2006.

Timothy Phillips, Senior Counsel
Vance L. Broemel, Assistant Attorney General
Joe Shirley, Assistant Attorney General
Office of the Attorney General
Consumer Advocate and Protection Division
P.O. Box 20207
Nashville, TN 37202

Misty Smith Kelley, Esq.
Baker, Donelson, Bearman & Caldwell
1800 Republic Centre
633 Chestnut Street
Chattanooga, TN 37450

Henry Walker, Esq.
Boult, Cummings, Conners & Berry
1600 Division Street, Suite 700
P.O. Box 340025
Nashville, TN 37203

J.W. Luna, Esq.
Jennifer Brundige, Esq.
Farmer & Luna
333 Union Street, Suite 300
Nashville, TN 37201

Melvin J. Malone, Esq.
Miller & Martin
2300 One Nashville Place
150 4th Avenue North
Nashville, TN 37219



Gary R. Hotvedt

Electronically filed with the TRA Docket Room on August 7, 2006.