

**IN THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE**

IN RE: PETITION TO OPEN AN)	
INVESTIGATION TO DETERMINE)	
WHETHER ATMOS ENERGY CORP.)	
SHOULD BE REQUIRED BY THE TRA)	Docket No. 05-00258
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)	

**BRIEF OF ATMOS ENERGY CORPORATION
AND REQUEST FOR ORAL ARGUMENT**

On November 7, 2006, a Notice of Filing was issued in this docket memorializing the Panel's November 6, 2006 ruling directing the parties to submit briefs discussing the appropriate forum the Authority should employ to take up certain asset management issues. Specifically, the Notice recited that the Panel voted "to require the filing of briefs by the parties regarding whether Docket No. 05-00253 or Docket No. 05-00258 is the appropriate forum to address asset management issues and how resolution of such issues should proceed. These briefs shall take into consideration that Docket No. 05-00253 is a contested case in which parties can seek intervention to address these issues apart from Docket No. 05-0258."¹ Atmos Energy Corporation ("Atmos") submits this brief as required by the Panel.² Atmos also respectfully requests that the parties be permitted to present oral argument to the Panel on these issues.

¹ *Notice of Filing* (November 7, 2006), p. 1.

² Atmos also incorporates by reference the arguments presented in its *Request for Implementation of the Order of the Authority*, filed September 29, 2006 in Docket No. 05-00253.

I. **THE ASSET MANAGEMENT ISSUES SHOULD NOT BE CONSIDERED WITHIN DOCKET NO. 05-00258.**

The asset management issues that have been raised by Staff and the intervenors in this docket are concerned exclusively with Atmos' gas supply procurement activities, specifically the management of the assets Atmos uses to secure gas for its customers. There can be no dispute that Docket No. 05-00258 is a base rate proceeding.³ Since the implementation of the PGA Rule, the Authority has regulated gas supply procurement activities separately from the base rates gas utilities charge its customers. This traditional distinction between the two types of regulation of gas utilities is similar to the two sides of a ledger: on the left-hand side is the regulation of base rates, through rate cases; on the right, the regulation of gas procurement issues, through the PGA rule, the ACA audits, and incentive plan audits, such as Atmos' PBR. The separate and distinct nature of these two sides of the ledger, and the fact that gas supply procurement issues are not relevant in base rate proceedings such as Docket No. 05-00258, is concisely set forth in the June 14, 2006 *Order Resolving Discovery and Protective Order Disputes and Requiring Filings* in this docket:

As a general proposition, information related to the cost of gas, which includes the commodity and transportation costs *offset by any revenues derived from the use of the natural gas assets*, is not relevant to this docket because such costs are not a factor used in calculating a company's rate base, operation and maintenance expenses, net operating income, rate of return, or base rates, all issues in this docket. Instead, gas costs are regulated independent of these items. Such costs are passed directly through to consumers via the PGA. Upon filing, the Authority audits gas cost recovery via the PGA using the ACA audit and assesses a surcharge or credit as necessary to ensure that only actually incurred natural gas costs are recovered from consumers. A second audit, the PBR audit, reviews the allocation of revenues or losses derived from the sale or purchase of natural gas between consumers and stockholders. *Thus,*

³ See *Order Resolving Discovery and Protective Order Disputes and Requiring Filings*, p. 6 (June 14, 2006); *Order Accepting Recommendation of Investigative Staff and Appointing a Hearing Officer*, pp. 4-5 (Aug. 2, 2006).

*information related solely to gas costs is not relevant to the determinations to be made in this docket.*⁴

In addition, the Authority has recognized in at least one previous order the fact that gas supply procurement activities such as asset management, and more specifically, the sharing of revenues derived from the management of gas supply assets, is not a base rate issue to be considered in the context of a rate proceeding.⁵

Quite simply, Docket No. 05-00258 is a base rate proceeding, and the asset management issues that have been raised are not base rate issues to be considered in such a proceeding. Expanding the scope of Docket No. 05-00258 to encompass such issues raises numerous policy and practical concerns. First, in the most recent gas utility rate case, the Authority found such issues beyond the scope of the proceeding.⁶ To find otherwise for Atmos raises concerns of disparate treatment.

In addition, as demonstrated by the agreed Phase II issues list, consideration of these asset management issues will require the Authority to examine numerous complex legal and policy issues, including the balance of incentives in Atmos' PBR mechanism implemented in Docket No. 97-01364, which replaces the requirement that the TRA Staff conduct annual audits of the prudence of Atmos' gas supply procurement activities with an incentive based regulatory scheme.⁷ The Report of Investigative Staff contains no foundational support that would justify expanding

⁴ *Order Resolving Discovery and Protective Order Disputes and Requiring Filings*, June 14, 2006, p. 6 (emphasis added).

⁵ TRA Docket No. 04-0034, *Order*, p. 28 (Oct. 20, 2004)

⁶ *Id.*

⁷ See, e.g., *Order Adopting Phase Two Issues and Modifying Procedural Schedule*, at Attachment A, Issue No. 7 (Oct. 6, 2006), which states the following as one of the issues to be addressed in Phase Two:

Should Atmos Energy Corporation share in the lump sum fee it receives from Atmos Energy Marketing under the asset management contract through its existing Performance Based Ratemaking ("PBR") plan? If so, how would such a change affect the balance of incentives in the current PBR plan? If the Tennessee Regulatory Authority orders that all or a portion of Atmos Energy Marketing profits be imputed to Atmos Energy Corporation, how would the balance of incentives in the current PBR be affected? Would such action render the PBR plan ineffective or invalid? Would such action require reversal of the Authority's orders in the PBR dockets?

For ease of reference, a complete copy of the Phase II issues list is attached to this Brief as Exhibit A.

the scope of this docket to include such issues. Expanding the scope of Docket No. 05-00258 beyond the foundation provided by the Staff Investigative Report raises serious due process concerns. *See Williams v. Pittard*, 604 S.W.2d 845, 849-50 (Tenn. 1980).

Finally, consideration of the asset management issues within the context of Docket No. 05-00258 sets a precedent for requiring a “Phase Two” in every rate case to provide a ready-made contested case-type forum for discovery and hearings on an unlimited range of complex issues. Not only would such a procedure unduly complicate the process of rate cases, making them more expensive and time consuming for both the agency and the utilities, but it would also reduce the flexibility the Authority currently has to select more informal and efficient means of resolving issues and addressing concerns, such as talks between the parties, mediation, workshops, task forces, rulemakings, etc. The Authority should be able to explore such informal means of dispute resolution before committing the resources of the agency to a fully litigated contested case.

Docket No. 05-00258 is a base rate proceeding. The asset management issues that have been raised are not base rate issues, and are beyond the scope of Docket No. 05-00258. Therefore, the Authority should not take up consideration of the asset management issues within Docket No. 05-0258.

II. THE AUTHORITY HAS ALREADY DETERMINED, IN DOCKET NO. 05-00253, HOW RESOLUTION OF THE ASSET MANAGEMENT ISSUES SHOULD PROCEED.

There is no dispute that the asset management issues in this docket are the precise same issues first raised by Authority Audit Staff in Atmos’ most recent ACA audit, Docket No. 05-00253.⁸ Atmos filed a written response to the Audit Staff Report on May 10, 2006 specifically

⁸ *See Recommendation of the Hearing Officer Regarding the Dismissal of Phase Two and the Need for a Rulemaking*, p. 15 (Oct. 6, 2006) (stating, in reference to the Phase 2 issues, that “[t]hese listed topics certainly concern the same subject matter as the audit recommendation in Docket No. 05-00253); *see also*, *Phase 2 Issues List From Atmos Intervention Group*, TRA Docket No. 02-00258 (Sept. 12, 2006), p. 1 (noting that Phase II will include several issues,

responding to Audit Staff's recommendations concerning the Company's asset management. In addition to noting several factual inaccuracies in the Audit Report,⁹ Atmos argued, *inter alia*, that a determination adopting Audit Staff's recommendations would represent new policy for the Authority that would impact all three regulated natural gas companies in Tennessee. Therefore, Atmos asserted that such a determination should be resolved through a rulemaking.¹⁰ *See Tennessee Cable Assoc. v. Tennessee Pub. Serv. Comm'n*, 844 S.W.2d 151, 161-62 (Tenn. Ct. App. 1992). Thus, the question of the manner in which these asset management issues should be considered by the Authority was an issue that was squarely before the Panel in Docket No. 05-00253.

The presiding Panel took up the issue of how to deal with the asset management issues at the Authority's May 15, 2006 Agenda Conference. The Panel rejected all of Audit Staff's asset management recommendations except Recommendation 3 (that future asset management contracts be submitted for prior approval by the Authority) and 2D (proposed revision of affiliate rules "to provide additional guidance to the Company in the selection of an asset manager").¹¹ As to the other issues, the Panel ordered Audit Staff and Company to meet and, stated that only after considering the report of those meetings would "this Panel may then consider whether to convene a contested case on those issues or take some other actions."¹²

including "issues raised arising from Atmos' asset management practices and affiliate relationships **as pointed out by TRA Staff in its most recent ACA audit report on Atmos.**" (emphasis added); TRA Docket No. 05-00258, Transc. of Proceedings, Sept. 26, 2006. at pp. 8-9 (statements indicating the parties' agreement as to the issues implicated in Phase II).

⁹ For example, Audit Staff misstated the amount of the annual lump sum fee, and wrongly assumed Atmos' contract with AEM was a bundled arrangement for asset management and gas procurement, similar to the contracts in place for Chattanooga Gas and Nashville Gas. *See* TRA Docket No. 05-00253, *Memo. To File from Audit Staff* (June 14, 2006) (acknowledging the incorrect statements concerning the lump sum fee) and *Atmos Resp. to Audit Staff Report* (May 10, 2006) (discussing factual inaccuracies in Audit Report).

¹⁰ *Atmos Resp. to Audit Staff Rep.*, TRA Docket No. 05-00253 (May 10, 2006), pp. 4-6.

¹¹ TRA Docket No. 05-00253, Transcript of Agenda Conference (May 15, 2006), at p. 3, ll. 4-7.

¹² *Id.* at p. 3, ll. 15-17.

The Panel's decision on how to deal with the asset management issues is clear: under the Panel's own order in Docket No. 05-00253, it is only after meetings between Atmos and Audit Staff and a joint report will the Panel make a determination as to whether a contested case or other action, such as a rulemaking, is necessary.

This ruling is consistent with the Authority's treatment of Nashville Gas and Chattanooga Gas, both of whom were ordered to meet with Staff to attempt to resolve the same asset management issues Audit Staff has raised with regard to Atmos before the Authority decided whether additional proceedings were needed.¹³ Although Atmos continues to maintain that an industry-wide rulemaking is the most appropriate way for the Authority to develop policy to regulate asset management, the Panel has indicated it would like Atmos to meet with Audit Staff to attempt to resolve the issues informally before making a determination as to whether a rulemaking or contested case is necessary.

The Panel's approach is certainly reasonable. The Authority has consistently exercised its discretion to order the gas companies to work with Authority Staff to informally resolve asset management issues before convening a contested case or other proceeding to address the issues. This approach has been successful, both in Tennessee and in other jurisdictions. Through informal talks, Chattanooga Gas was able to reach a mutual resolution with Staff addressing Staff's concerns about its asset management. At the October 16, 2006 Agenda Conference, the parties reported that settlement talks with regard to Nashville Gas' asset management issues were progressing towards a mutual resolution. Atmos has been successful in other jurisdictions addressing similar concerns as those raised by Audit Staff through informal meetings with Commission Staff members. Atmos is eager to meet with Audit Staff to discuss the asset

¹³ See TRA Docket No. 05-00253, *Atmos Energy Corporation's Request for Implementation of the Order of the Authority*, p. 5 (Sept. 29, 2006) (containing a chart comparing the Authority's treatment of asset management issues for Chattanooga Gas, Nashville Gas, and Atmos).

management issues, and the Company is optimistic that such talks can resolve many, if not all, of Staff's concerns.

Permitting the talks required by the Authority's order in Docket No. 05-00253 is consistent with the Authority's treatment of asset management issues for Chattanooga Gas and Nashville Gas, and, consistent with the basic concerns of fairness, will ensure that Atmos is afforded the same procedural and substantive considerations as the other regulated gas companies in the state. *See Tennessee Cable v. Tennessee Public Serv. Comm'n*, 844 S.W.2d 151, 162 (Tenn. Ct. App. 1992) (holding that the agency's substantial discretion in choosing the forum to resolve disputes "does not immunize an agency's decision from considerations of fairness"); *see also Tennessee Consumer Advocate v. Tennessee Reg. Auth.*, 1997 WL 92079, *4 (Tenn. App. Ct. Mar. 5, 1997). The results of such talks may eliminate the need for a rulemaking or contested case. Even if a resolution cannot be reached on all issues, the talks may very well narrow the issues remaining for resolution by rulemaking or contested case. The talks will also permit the Company the opportunity to share information with Staff to correct the misunderstandings concerning its asset management arrangement, and permit Staff to make the legal and policy analysis necessary to take positions and advise in further proceedings, whether they be in the form of a rulemaking or a contested case.

The Panel's determination to delay any decision on whether to convene a rulemaking, contested case, or other proceeding to resolve the asset management issues until Atmos has had the opportunity to meet with Audit Staff and attempt to resolve Staff's concerns informally is a sound and valid decision, and should not be reversed. The decision does not prejudice the Consumer Advocate, the Intervention Group, or any other party. Under the Panel's Order in Docket No. 05-00253, no decision with regard to the convening of a rulemaking or contested case

will be made until Atmos and Audit Staff report to the Panel with the results of their meetings concerning the asset management issues. The Consumer Advocate and the Intervention Group are free to submit petitions to intervene to the Panel requesting that the issues be resolved through contested case, a rulemaking convened, or seeking any other relief the parties would like to request. The Panel will consider those petitions, together with the report from the meetings between Atmos and Audit Staff, and will then be able to make an informed decision as to whether a contested case or rulemaking is necessary, or whether it should take any additional actions. The Panel's decision in Docket No. 05-0258 to forego consideration of the asset management issues until after conclusion of the base rate proceedings in no way bars the Authority from upholding its previous order in Docket No. 05-00253.¹⁴

III. CONCLUSION.

The Panel has already concluded that it is premature to decide whether to convene a contested case, rulemaking, or other proceeding to resolve the asset management issues, until after Authority Staff and Atmos have had the opportunity to meet to attempt to resolve Staff's concerns informally. The Panel's previous decision is sound. The decision is consistent with the Authority's determinations with regard to Chattanooga Gas and Nashville Gas, and will ensure that Atmos is treated the same as similarly situated utilities. The asset management issues are gas procurement issues, not base rate issues, and therefore do not belong in Docket No. 05-00258. The Authority's decision in Docket No. 05-00253 to delay any ruling on whether to convene a contested case, rulemaking or other proceeding pending the results of meetings between Atmos and Staff is reasonable, valid, and will not prejudice any party. As such, the Authority's previous order in Docket No. 05-00253 should be upheld.

¹⁴ As with Chattanooga Gas and Nashville Gas, any concerns of ex parte communication can also be addressed by the Authority's action.

Atmos believes that oral argument would be helpful to the Panel in this case, and therefore requests that the Panel permit the parties to present oral argument on these issues.

BAKER, DONELSON, BEARMAN
CALDWELL, & BERKOWITZ, P.C.

By: 

Misty Smith Kelley, TN BPR # 19450
Clinton P. Sanko, TN BPR # 023354
1800 Republic Centre
633 Chestnut Street
Chattanooga, TN 37450-1800
(423) 209-4148
(423) 752-9549 (Facsimile)
mkelley@bakerdonelson.com
Attorneys for Atmos Energy Corporation

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing has been hand-delivered, e-mailed or faxed to the following parties of interest this 20th day of November, 2006.

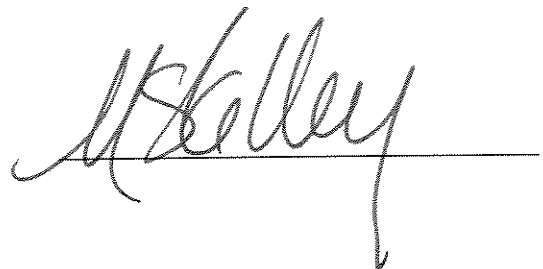
Vance L. Broemel
Joe Shirley
Cynthia Kinser
Office of Attorney General
Consumer Advocate and Protection Division
P.O. Box 20207
Nashville, TN 37202

Gary Hotvedt
General Counsel
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, TN 37243-0505

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

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

Melvin Malone
Miller & Martin
2300 One Nashville Place
150 4th Avenue North
Nashville, TN 37219-2433

A handwritten signature in dark ink, appearing to read "M. Kelley", is written over a horizontal line.

Docket No. 05-00258 – Phase Two Issues List

1. How is Atmos Energy Corporation compensated for the sale, lease, or release of capacity and is that compensation fair to consumers?
 - a. What is the bidding process for the sale, lease, or release of capacity?
 - b. What asset management arrangements or contracts are or have been in place with regard to capacity?
 - c. How are FERC-mandated payments handled?
2. What exactly is the amount of total capacity and what amount of capacity is available for the sale, lease, or release to third parties or affiliates or divisions of Atmos Energy Corporation?
 - a. What is the appropriate level of capacity?
 - b. What has been the record of capacity planning in the past?
 - c. What are the future plans?
3. What is the relation between Atmos Energy Corporation and Atmos Energy Marketing and any other affiliate or division of Atmos Energy Corporation?
 - a. the appropriate relation between parent and affiliate or division
 - b. communications between parent and affiliate or division
 - c. the number of overlapping employees
 - d. the record keeping of the parent and affiliate or division
4. Are consumers receiving fair compensation for the assets related to the sale, lease, or release of capacity for which they have paid?
5. Does the Tennessee Regulatory Authority have the authority to impute to Atmos Energy Corporation all or a portion of the profits Atmos Energy Corporation's separate, non-regulated affiliate corporation, Atmos Energy Marketing, generates through its management of Atmos Energy Corporation's idle gas supply assets?
 - a. If yes, may the Tennessee Regulatory Authority impute those profits to lower Atmos Energy Corporation's revenue requirement for base rates even though the assets are part of Atmos Energy Corporation's gas supply procurement activities, which under established Tennessee Regulatory Authority policy are separately regulated through the Purchased Gas Adjustment mechanism, and not through base rates?
 - b. If the Tennessee Regulatory Authority imputes Atmos Energy Marketing asset management profits to lower Atmos Energy Corporation's revenue requirement for base rates, must the Tennessee Regulatory Authority treat other similarly situated gas companies in a like manner? Can such imputation be accomplished in a contested case, or is a rulemaking required?
 - c. Does the Tennessee Regulatory Authority have the authority to impute Atmos Energy Marketing's asset management profits to Atmos Energy Corporation even though there is no requirement for gas companies to engage in asset management?
 - d. If the Tennessee Regulatory Authority's decision in Phase Two of this docket results in a decision by Atmos Energy Marketing to exercise its right to terminate its asset management contract with Atmos Energy Corporation, can the Tennessee Regulatory Authority order Atmos Energy Corporation to engage in asset management itself? If so, how will the Tennessee Regulatory Authority provide for Atmos Energy Corporation to recover the costs of engaging in those activities,

- and how will the Tennessee Regulatory Authority monitor Atmos Energy Corporation's compliance? Would prudency audits be required?
- e. If the Tennessee Regulatory Authority orders that a portion of the Atmos Energy Marketing asset management profits be imputed to Atmos Energy Corporation, how will the agency determine what percentage of Atmos Energy Marketing revenues are derived from the Atmos Energy Corporation regulated Tennessee assets, versus what percentage are derived from Atmos Energy Corporation regulated assets in other states, or from Atmos Energy Marketing's own separately owned assets?
 - f. If the Tennessee Regulatory Authority orders that a portion of the Atmos Energy Marketing asset management profits be imputed to Atmos Energy Corporation, how will the agency determine the portion of Atmos Energy Marketing revenues that constitute profit and what portion Atmos Energy Marketing must use to meet the costs it incurs?
 - g. What constitutes retroactive ratemaking?
 - h. If the Tennessee Regulatory Authority orders that a portion of the Atmos Energy Marketing asset management profits be imputed to Atmos Energy Corporation, how will the Tennessee Regulatory Authority determine this amount consistent with the prohibition against retroactive ratemaking? Would the Tennessee Regulatory Authority have to reach a determination as to the amount of profit Atmos Energy Marketing will make in a particular future time period? If the Tennessee Regulatory Authority orders that a percentage of the Atmos Energy Marketing profits be imputed to Atmos Energy Corporation, how will the Tennessee Regulatory Authority monitor compliance? Would it require regular audits from Tennessee Regulatory Authority Staff? Does the Tennessee Regulatory Authority have the authority to audit non-regulated affiliates such as Atmos Energy Marketing?
6. Did Atmos Energy Corporation comply with the Guidelines for Affiliate Transactions entering into the existing asset management contract with Atmos Energy Marketing? If so, does the Tennessee Regulatory Authority have the Authority to invalidate the existing contract or change the terms of the existing contract? If the contract is invalidated, is Atmos Energy Marketing entitled to a refund of all or a portion of the annual lump sum fee it pays under the contract for the right to manage Atmos Energy Corporation's assets that is currently flowed through 100% to consumers?
 7. Should Atmos Energy Corporation share in the lump sum fee it receives from Atmos Energy Marketing under the terms under the asset management contract through its existing Performance Based Ratemaking ("PBR") plan? If so, how would such a change affect the balance of incentives in the current PBR plan? If the Tennessee Regulatory Authority orders that all or a portion of Atmos Energy Marketing asset management profits be imputed to Atmos Energy Corporation, how would the balance of the incentives in the current PBR be affected? Would such action render the PBR plan ineffective or invalid? Would such action require reversal of the Authority's orders in the PBR dockets?
 8. Whether Atmos Energy Corporation has oversubscribed to storage and capacity assets to handle the Company's jurisdictional requirements?
 9. Whether Atmos Energy Corporation is currently utilizing its gas storage assets to maximize benefits to ratepayers?