BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

October 30, 2006

IN RE:	)	
	)	
NASHVILLE GAS COMPANY,	)	**DOCKET NO.**
A DIVISION OF PIEDMONT NATURAL GAS	)	**06-00017**
COMPANY, INC. PGA FILING	)	
	)	
	)	

ORDER WAIVING PGA FORMULA APPROACH AND 30-DAY-NOTICE REQUIREMENT

This matter came before Chairman Ron Jones, Director Pat Miller and Director Sara Kyle, of the Tennessee Regulatory Authority (the "Authority" or "TRA"), the voting panel assigned to this docket, at a regularly scheduled Authority Conference held on January 23, 2006 for consideration of the Purchased Gas Adjustment filing ("PGA") submitted on behalf of Nashville Gas Company ("Nashville Gas") on January 18, 2006 by its parent company, Piedmont Natural Gas ("Piedmont").

The PGA

On January 18, 2006, Piedmont filed its PGA requesting that the Authority waive the *formula approach* dictated in the PGA rule to enable Nashville Gas to lower the commodity portion of its PGA calculation to $7.00 per dekatherm, which was at the time $4.00 below its commodity PGA and approximately $2.00 below market price. In addition, Piedmont requested any necessary waivers of the PGA rule to allow this PGA to take effect February 1, 2006.

Background

The Gas Cost Adjustment ("GCA") formula is found in TRA Rule 1220-4-7-.03(1).[1] The GCA is a billing adjustment factor calculated by dividing the estimated total annual gas costs by the

[1] This rule defines the components of the PGA: (1) Gas Cost Adjustment (GCA), (2) Refund Adjustment (RA) and (3) Actual Cost Adjustment (ACA).

total estimated annual gas sales. Demand and commodity costs reflected in this formula are based on supplier rates that are "effective, known or reasonably anticipated at the time the PGA is filed with the Authority..."[2] Demand rates are set by contract between gas companies and interstate pipelines. These contracts are usually long term contracts and therefore do not change often. Nevertheless, commodity prices have become highly volatile and can change dramatically during a month. As a result, gas companies must try to "anticipate" their gas costs based on a moving target. The New York Mercantile Exchange ("NYMEX") futures are generally accepted in the industry, as a reasonable predictor of gas prices.

The GCA formula also allows for an adjustment to the estimated cost of gas based on the balance in a gas company's deferred gas cost account or "ACA" account.[3] Each month, gas companies debit their gas costs based on actual invoices received and paid to this account. They also credit revenues[4] billed for the month to this account. If revenues billed exceed the invoiced gas costs for the month, then an over-recovery (over-collection) of gas costs has occurred. Likewise, if revenues billed are less than invoiced gas costs, then an under-recovery (under-collection) of gas costs has occurred. A running balance is maintained in this account and at any point in time, the balance[5] is known. A positive (debit) balance represents gas costs that have not yet been recovered (collected) from customers. A negative (credit) balance represents the amount recovered (collected) from customers in excess of the gas company's actual gas costs. The Actual Cost Adjustment ("ACA") is a true-up of the actual invoiced gas costs compared to the actual amount of gas costs recovered (collected) from the customers. The TRA audit staff audits the balance in the ACA Account annually at a specific point in time to ensure that the gas company has not over-collected or under-collected their gas costs.

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[2] TRA Rule 1220-4-7-.03(1)(a)3.(i) and (iii).
[3] See TRA Rule 1220-4-7-.04 which describes the accounting procedure.
[4] Revenues are the rates billed to customers for the recovery (collection or reimbursement) of gas costs multiplied by the volumes billed. The rates are established by the GCA in effect for a particular month.
[5] The balance reflects total gas costs incurred (netted) with total gas costs recovered (collected) through customer rates.

The GCA formula can address significant[6] under-recoveries or over-recoveries in a PGA filing prior to the true-up audit process. If gas costs are significantly under-recovered, the balance is added to the total gas costs, which in turn increases the total gas costs that are billed volumetrically to customers based on usage. Conversely, if gas costs are significantly over-recovered, the balance is subtracted from the total gas costs, which lowers the total gas costs to be collected and in turn lowers the GCA factor billed to customers. If the GCA is lower, the revenues billed to customers will be lower, resulting in a reduction of the negative ACA account balance. While the mismatch of gas costs incurred and gas costs recovered is trued up annually, a "correction" during the intervening year may be necessary to avoid an overly large rate impact at the time of audit.

In the current PGA, Piedmont is requesting permission to deviate from the above described *formula approach* and use a commodity price of $7.00 per dekatherm in the calculation of its total commodity costs, rather than the market price of gas, as determined by NYMEX. Other costs, such as transportation, fixed storage costs, etc., are calculated using Federal Energy Regulatory Commission ("FERC") approved pipeline tariff rates. While the commodity cost of gas decreased significantly over the period in question, using the NYMEX futures as a benchmark would have resulted in a commodity price of approximately $9.00. If this was the only factor Piedmont took into account at the time of this PGA, the adjustment to the GCA could have been accomplished within the formula and no modification would be needed. Piedmont determined that taking other factors into consideration, such as: the management of its ACA account, the weather forecast, and the price of its gas in storage, would allow Nashville Gas to reduce the commodity price even further to a level of $7.00.

The warmer than normal weather experienced during the past heating season, and the anticipated continuance of warmer weather in the near future, leads to a decrease in sales, which

[6] It is not unusual for the ACA account balance to be in the millions of dollars. There is a regulatory lag inherent in the gas cost recovery mechanism; in that "estimated" gas costs are netted against actual billed revenues that are based on rates previously established in a PGA tariff filing. The actual gas costs are not known until gas purchasing takes place after the fact.

affects storage withdrawals, which in turn affects market prices: warmer weather slows the depletion of gas supplies. With more supplies and less demand, the market reacted with a decreasing NYMEX futures price.

The warmer than usual weather also allowed Piedmont to retain stored gas inventories rather than deplete them. Further, Piedmont stated that it has gas in storage available if needed that would prevent Nashville Gas from having to purchase gas at spot market prices. The price of its gas in storage is lower than the current market price of gas at spot market prices.

As of this PGA filing Nashville Gas had a commodity ACA account balance of approximately *negative* $5.6 million in over-recovered gas costs. Piedmont took this fact into consideration in making its decision to lower the commodity price below market price.

Piedmont proposed to effectively begin the refund of the over-collection rather than wait until the annual audit which commenced approximately April 1, 2006. In addition, Piedmont requested an effective date of February 1, 2006 which is less than the thirty (30) days notice required by the PGA Rule.

January 23 Authority Conference

TRA Rule 1220-4-7-.03(4) allows formulas to be modified from time to time to carry out the intent of these PGA Rules. Furthermore, TRA Rule 1220-4-7-.02(3) provides:

> To the extent, practicable, any revision in the PGA shall be filed with the Authority no less than thirty (30) days in advance of the proposed effective date and shall be accompanied by the computations and information required by these Rules. It is recognized, however, that in many instances the Company receives less than thirty (30) days notice from its suppliers and that other conditions may exist which prevent the Company from providing thirty (30) days advance notice. Therefore, should circumstances occur where information necessary for the determination of an adjustment under these Rules is not available to the Company so that the thirty (30) days requirement can be met, the Authority may permit the Company to place rates into effect with shorter advance notice, upon good cause shown.

At the January 23, 2006 Authority conference, a majority of the Panel found that Tenn. Comp. R. & Regs. 1220-4-7-.03(4) and 1220-4-7-.02(3) apply to this transaction. The majority determined that lowering the GCA and reducing the amount of revenues billed to customers would accelerate the refund of this over-recovery to Nashville Gas customers, in keeping with the intent of these PGA rules. A majority of the Panel also determined that providing a reduction in gas prices to consumers in less than thirty (30) days constitutes good cause for the Authority to reduce the thirty (30) day notice requirement for the effectiveness of Piedmont's PGA. The Panel voted unanimously to grant approval of the application.

IT IS THEREFORE ORDERED THAT:

The Purchased Gas Adjustment Tariff filed by Piedmont Natural Gas Company, Inc. on behalf of Nashville Gas Company is approved as filed, thereby modifying the Gas Cost Adjustment formula pursuant to Tenn. Comp. R. & Regs. 1220-4-7-.03(4) and reducing the thirty (30) day filing requirement pursuant to Tenn. Comp. R. & Regs. 1220-4-7-.02(3).

Ron Jones, Chairman[7]

Pat Miller, Director

Sara Kyle, Director

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[7] Director Jones agreed that the tariff should be approved and the thirty (30) day time period shortened; however, he provided an alternative analysis than that described in this Order. During the conference, Director Jones found that Nashville Gas is seeking to first apply the GCA formula, and then to reduce the $9.51 GCA formula rate to $7.00 per decatherm. Director Jones noted that Nashville Gas relies on its $5.6 million negative balance in its ACA account and the availability of low-cost stored gas to support its rate proposal. Director Jones determined that the TRA rules are silent as to this factual scenario. Director Jones further determined that the PGA rules generally results in a rate that is reasonable and in harmony with Tenn. Code Ann. § 65-5-104. In this instance, however, at a time when consumers have been forced to bear the burden of record high gas costs, Director Jones noted that adhering to a strict application of the PGA rules results in a rate that is unreasonable in violation of Tenn. Code Ann. § 65-5-104. Thus, Director Jones concluded that because the requirements of Tenn. Code Ann. § 65-5-104 trump our administrative rules, Nashville Gas should be permitted to reduce the rate below that calculated using only the GCA formula.

As to the thirty (30) day time period, Director Jones noted that Authority Rule 1220-4-7-.02(3) allows for shorter notice when the requisite information is not available to a company. Based on the facts of this case, Director Jones determined that the NYMEX information necessary to justify the rate reduction to $9.51 was not available thirty (30) days in advance of the effective date of the proposed rate. Thus, Director Jones concluded that Nashville Gas should be permitted to place its proposed rate into effect with less than thirty (30) days notice.