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BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

May 30, 2008

IN RE:	)	
	)	
CHATTANOOGA GAS COMPANY	)	Docket No. 07-00265
ACTUAL COST ADJUSTMENT AUDIT	)	

**NOTICE OF FILING BY THE UTILITIES DIVISION OF THE TENNESSEE
REGULATORY AUTHORITY**

Pursuant to Tenn. Code Ann. §§65-4-104, 65-4-111 and 65-3-108, the Utilities Division of the Tennessee Regulatory Authority hereby gives notice of its filing of the Compliance Audit Report of the Actual Cost Adjustment (hereafter "ACA") component of the Purchased Gas Adjustment Rule for Chattanooga Gas Company in this docket and would respectfully state as follows:

1. The present docket was opened by the Authority to hear matters arising out of the ACA audit of Chattanooga Gas Company (the "Company").
2. The Company's ACA filing was received on November 29, 2007, and the Audit Staff completed its audit of same on May 27, 2008. The original 180-day deadline for the Staff's completion of the audit was extended to June 9, 2008 and again to June 23, 2008 by mutual consent of Chattanooga Gas Company and the TRA Audit Staff as provided for in

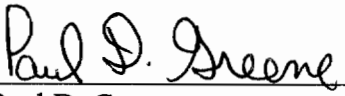
the Purchased Gas Adjustment Rule (1220-4-7-.03 (2)). The extensions were necessary due to a change in the date of the Authority Conference in June.

3. There were six (6) findings during the course of the ACA audit. None of the findings were considered material and therefore there is no need to adjust the ACA factor put into effect January 1, 2008.

4. A final ACA audit report (hereafter the "Report") resulted therefrom. The Report is attached hereto as Exhibit A and is fully incorporated herein by this reference.

5. The Utilities Division hereby files its Report with the Tennessee Regulatory Authority for deposit as a public record.

Respectfully Submitted:



Paul D. Greene
Utilities Division of the
Tennessee Regulatory Authority

CERTIFICATE OF SERVICE

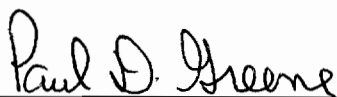
I hereby certify that on this 30th day of May 2008, a true and exact copy of the foregoing has been either hand-delivered or delivered via U.S. Mail, postage pre-paid, to the following persons:

Eddie Roberson
Chairman
Tennessee Regulatory Authority
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Paul D. Greene

**COMPLIANCE AUDIT REPORT
of the
ACTUAL COST ADJUSTMENT COMPONENT
of the
PURCHASED GAS ADJUSTMENT RULE
for
CHATTANOOGA GAS COMPANY**

Docket No. 07-00265

Prepared by:

**THE UTILITIES DIVISION
of the
TENNESSEE REGULATORY AUTHORITY**

May 2008

EXHIBIT A

**COMPLIANCE AUDIT REPORT
of the
ACTUAL COST ADJUSTMENT COMPONENT
of the
PURCHASED GAS ADJUSTMENT RULE
for
CHATTANOOGA GAS COMPANY
for the Year ended June 30, 2007**

Docket No. 07-00265

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I. INTRODUCTION

The subject of this audit is Chattanooga Gas Company's ("Company," "Chattanooga," or "CGC") compliance with the Actual Cost Adjustment and Refund Adjustment of the Purchased Gas Adjustment Rule ("PGA Rule") of the Tennessee Regulatory Authority ("TRA" or the "Authority"). The objective of the audit is to determine whether the purchased gas adjustments, which are encompassed by the Actual Cost Adjustment ("ACA"), as more fully described in section VI., for the year ended June 30, 2007, are calculated correctly in accordance with all TRA rules, orders, and directives applicable to Chattanooga and are supported by appropriate source documentation.

II. AUDIT OPINION

Audit Staff's ("Staff") audit resulted in six (6) findings.¹ The net amount of these findings is **\$102,363.84 in over-recovered gas costs**. The Company's reported June 30, 2007 balance of **\$2,883,756.83 in over-collected** gas costs is increased by the \$102,363.84 over-collected gas costs determined in this audit. The corrected balance in the ACA account at June 30, 2007 is **\$2,986,120.67 in over-recovered gas costs**. The amount of the Company's errors represent less than one percent of its total gas invoices, and is therefore immaterial by comparison.

Staff concludes that, except for the findings noted in this report, the Purchased Gas Adjustment mechanism, as calculated in the Actual Cost Adjustment, appears to be working properly and in accordance with the TRA rules for Chattanooga Gas Company.

III. SUMMARY OF COMPANY FILING

The Company made its Actual Cost Adjustment filing for its Tennessee service area on November 29, 2007. This ACA filing showed \$72,188,957.09 in total gas costs, with \$71,833,585.55 being recovered from customers through rates. Adding a beginning balance in the Deferred Gas Cost account ("ACA account") of negative \$2,934,398.37 in over-recovered gas costs from the preceding ACA period and interest owed to customers for the current period of negative \$304,730.00 resulted in an ACA balance at June 30, 2007 of **negative \$2,883,756.83 in over-recovered** gas costs. The Company's filing is summarized on the following page.

¹ Refer to Section VIII for a description of the findings.

**CHATTANOOGA GAS COMPANY
ACA FILING FOR PERIOD JULY 2006-JUNE 2007**

Line

1 Beginning Balance (July 2006)	\$ (2,934,398.37)
2 Purchased Gas Costs (July 2006 – June 2007)	72,188,957.09
3 Gas Costs recovered through rates (July 2006 – June 2007)	71,833,585.55
4 Interest on monthly ACA Account balances	<u>(304,730.00)</u>
5 Ending Balance (June 2007) (Line 1 + Line 2 – Line 3 + Line 4)	<u>\$ (2,883,756.83)</u>

A () around a number indicates a negative or credit balance in the ACA Account, which represents an over-recovery of gas costs. Over-recoveries result in a refund due to customers.

The Company filed a tariff, effective January 1, 2008, to begin refunding the balance in the ACA account as of June 30, 2007.

IV. BACKGROUND INFORMATION ON COMPANY

Chattanooga Gas Company, located at 6125 Preservation Drive in Chattanooga, Tennessee, is a wholly owned subsidiary of AGL Resources, Inc., a holding company formed in 2000 in response to the Public Utility Holding Company Act (PUCHA) of 1935. AGL Resources, Inc. is located at Ten Peachtree Place, Atlanta, Georgia. As a local distribution company (“LDC”), Chattanooga Gas provides service to customers in Chattanooga and Cleveland, Tennessee, and environs in Hamilton and Bradley Counties in Tennessee, respectively. The natural gas used to serve these areas is purchased from various suppliers and transported via three natural gas pipelines in accordance with separate and individual tariffs approved by the Federal Energy Regulatory Commission (FERC). The three interstate pipelines are Tennessee Gas Pipeline (TGP), East Tennessee Natural Gas (ETNG), and Southern Natural Gas (SNG).

V. JURISDICTION OF THE TENNESSEE REGULATORY AUTHORITY

Tennessee law provides broad jurisdiction and control over public utilities to the Tennessee Regulatory Authority (hereafter the “Authority” or “TRA”). Tenn. Code Ann. § 65-4-104 states:

The authority has general supervisory and regulatory power, jurisdiction, and control over all public utilities, and also over their property, property rights, facilities, and franchises, so far as may be necessary for the purpose of carrying out the provisions of this chapter.

Further, Tenn. Code Ann. § 65-4-105 grants the same power to the Authority with reference to all public utilities within its jurisdiction as Tenn. Code Ann., Title 65. Chapters 3 and 5 confer oversight of the railroads to the Department of Transportation or oversight of transportation companies to the Department of Safety. By virtue of Tenn. Code Ann. § 65-3-108, said power includes the right to audit:

The department of transportation is given full power to examine the books and papers of the companies, and to examine, under oath, the officers, agents, and employees of the companies... to procure the necessary information to intelligently and justly discharge its duties and carry out the provisions of this chapter and chapter 5 of this title.

The Utilities Division of the TRA is responsible for auditing those companies under the Authority's jurisdiction to ensure that each company is abiding by Tennessee statutes as well as the Rules and Regulations of the Authority. Paul Greene, Ron Graham and Helen Trimble-Anthony of the Utilities Division conducted this audit.

VI. DESCRIPTION OF PURCHASED GAS ADJUSTMENT RULE

Actual Cost Adjustment Audits:

The PGA Rule can be found in Chapter 1220-4-7 of the Rules of the Tennessee Regulatory Authority. The PGA Rule permits the Company to recover, in a timely fashion, the total cost of gas purchased for delivery to its customers and to assure that the Company does not over-collect or under-collect gas costs from its customers.

The PGA consists of three major components:

- 1. The Actual Cost Adjustment (hereafter the "ACA")**
- 2. The Gas Charge Adjustment (hereafter the "GCA")**
- 3. The Refund Adjustment (hereafter the "RA")**

The ACA is the difference between the revenues billed customers by means of the GCA and the cost of gas invoiced the Company by suppliers plus margin loss (if allowed by order of the TRA in another docket) as reflected in the Deferred Gas Cost account. The ACA then "true-up" the difference between the actual gas costs and the gas costs recovered from customers through a surcharge or a refund. The RA refunds the "true-up" along with other supplier refunds. For a more complete definition of the GCA and RA, please see the PGA Formula in Appendix A of this Report.

Section 1220-4-7-.03 (2) of the PGA rule requires:

Each year, the Company shall file with the Authority an annual report reflecting the transactions in the Deferred Gas Cost Account. Unless the Authority provides written notification to the Company within one hundred eighty (180) days from the date of filing the report, the Deferred Gas Cost Adjustment Account shall be deemed in compliance

with the provisions of these Rules. This 180-day notification period may be extended by mutual consent of the Company and the Authority Staff or by order of the Authority.

Prudence Audit of Gas Purchases:

Section 1220-4-7-.05 of the PGA Rule requires, unless otherwise ordered by the Authority, an audit of Prudence of Gas Purchases by a qualified consultant. This specialized audit evaluates and reports annually on the prudence of any gas costs included in the PGA. At its September 11, 2001, Authority Conference, the Directors voted to approve a Performance-Based Ratemaking Mechanism for Chattanooga (Docket No. 01-00619). The mechanism affects all plan years ending after June 30, 2000, and continues each year unless terminated by the Company or the Authority. For each year that the mechanism is in effect, if CGC's total commodity gas purchases are less than 1% above the total annual benchmark, its purchases are deemed prudent and the requirements of Section 1220-4-7-.05 of the PGA Rule are waived. Staff reviewed these gas purchases as part of the Compliance Audit in Docket No. 07-00266. Staff's Audit revealed that the Company met the requirements of its tariff and recommended that the Company be released from the prudence audit.

VII. SCOPE OF ACA AUDIT

The ACA audit is a compliance audit of the Company's ACA account. The audit goal is to verify that the Company's calculations of gas costs incurred and recovered are materially correct,² and that the Company is following all Authority rules, orders and directives with respect to its calculation of the ACA Account balance. Also included in this audit is the Company's PGA filing implementing a customer refund of the ACA Account balance, effective January 1, 2008. Refer to the ACA Account detail provided in Section III, Summary of Company Filing.

To accomplish the audit goal, Staff reviewed gas supply invoices, as well as supplemental schedules and other source documentation provided by Chattanooga. Where appropriate, Staff requested additional information to clarify the filing.

² The audit goal is not to guarantee that the Company's results are 100% correct. Where it is appropriate, Staff utilizes sampling techniques to determine whether the Company's calculations are materially correct. Material discrepancies would dictate a broadening of the scope of Staff's review.

VIII. ACA FINDINGS

The result of the Staff's audit was a **net over-recovery of \$102,363.84** which has the effect of increasing the Company's over-recovered balance at June 30, 2007 by this amount. A summary of the account as filed by the Company and as adjusted by the Staff is shown below, followed by a detailed description of each finding.

SUMMARY OF THE ACA ACCOUNT:

	Company	Staff	Difference (Findings)
Commodity Balance at 6/30/06	\$ -3,501,441.84	\$ -3,501,441.84	\$ 0.00
Plus Gas Costs	60,916,035.32	60,938,708.59	22,673.27
Minus Recoveries	<u>60,441,869.83</u>	<u>60,453,902.83</u>	<u>12,033.00</u>
Ending Balance before Interest	\$ -3,027,276.35	\$ -3,016,636.08	\$ 10,640.27
Plus Interest	<u>-337,185.00</u>	<u>-338,883.00</u>	<u>-1,698.00</u>
Commodity Balance at 6/30/07	<u>\$ -3,364,461.35</u>	<u>\$ -3,355,519.08</u>	<u>\$ 8,942.27</u>
Demand Balance at 6/30/06	\$ 567,043.47	\$ 567,043.47	\$ 0.00
Plus Gas Costs	11,272,921.77	11,253,355.66	-19,566.11
Minus Recoveries	<u>11,391,715.72</u>	<u>11,481,794.72</u>	<u>27,950.00</u>
Ending Balance before Interest	\$ 448,249.52	\$ 338,604.41	\$ -47,516.11
Plus Interest	<u>32,455.00</u>	<u>30,794.00</u>	<u>-1,661.00</u>
Demand Balance at 6/30/07	<u>\$ 480,704.52</u>	<u>\$ 369,398.41</u>	<u>\$ -49,177.11</u>
Total ACA Ending Balance at 6/30/07	<u>\$ -2,883,756.83</u>	<u>\$ -2,986,120.67</u>	<u>\$ -102,363.84³</u>

Note: A negative number indicates an over-recovery of gas costs.

³ The differences appearing in the "Difference" column calculate to \$40,234.84 in total findings. However, the Staff discovered formula errors in the Company's calculation of the ACA balance. The remaining \$62,129 is the result of these errors. See Finding #5.

SUMMARY OF FINDINGS:See page

FINDING #1	Gas Cost Adjustment	\$ 0.00	Interest Effect Only	7
FINDING #2	Gas Cost Adjustment	0.00	Interest Effect Only	8
FINDING #3	Gas Cost Recovery Adjustment.	(39,983.00)	Over-recovery	9
FINDING #4	Gas Cost Adjustment	3,107.16	Under-recovery	10
FINDING #5	Calculation Error	(62,129.00)	Over-recovery	11
FINDING #6	Interest Adjustment	<u>(3,359.00)</u>	Over-recovery	12
	Net Result	\$ <u>(102,363.84)</u>	Over-recovery	

FINDING #1:

Exception

The Company incorrectly recorded an East Tennessee Natural Gas Pipeline December 2006 credit and related reversal, a January 2007 Commodity cost and a January 2007 prior period Commodity cost.

Discussion

The Company recorded a Commodity credit of \$11,174.50 twice in December 2006. The Company then reversed the duplicate credit in January 2007; however, it was reversed as a Demand cost instead of a Commodity cost. To correct the entries, Staff increased December 2006 Commodity costs by \$11,174.50 to eliminate the duplicate credit and eliminated the \$11,174.50 inappropriately adjusted to Demand costs in January 2007. The result of Staff's adjustments is a reclassification of the adjustment from January 2007 to December 2006 and from Demand cost to Commodity cost. The only dollar effect of Staff's adjustments was to interest expense between Commodity and Demand, due to reclassification and timing differences.

The Company incorrectly reported the commodity portion of the January 2007 invoice (\$2,728.84) as a demand cost. Also, the Company incorrectly reported a prior period Commodity cost (\$5,662.77) in January 2007 as a Demand cost. Staff reduced Demand costs by \$8,391.61 and increased Commodity costs by \$8,391.61. The reclassification resulted in a shift of interest expense between Commodity and Demand.

Company Response

Chattanooga Gas Company concurs.

FINDING #2:**Exception**

The Company overstated Commodity costs in December 2006 and understated Commodity costs in April 2007 due to double payment of a Tennessee Gas Pipeline invoice.

Discussion

The Company paid a December 2006 invoice amount of \$77,466.76 twice for a total payment of \$154,933.52. The April 2007 pipeline invoice was in the amount of \$41,344.44. The Company recorded a negative \$36,122.32 in the ACA after reversing the overpayment made in December 2006 (\$41,344.44 minus \$77,466.76).

Invoiced amounts should be reflected in the ACA in the month billed. Staff subtracted the \$77,466.76 duplicate payment amount from December 2006 Commodity costs and added \$77,466.76 to April 2007 Commodity costs (reversed the negative \$36,122.32 and added \$41,344.44 for the April 2007 invoice).

The effect of this finding is interest only due to timing difference.

Company Response

Chattanooga Gas Company concurs.

FINDING #3:

Exception

The Company used an incorrect PGA factor in the calculation of gas cost recoveries.

Discussion

The Company used incorrect PGA factors for the months of January 2007 – March 2007. As a result, the calculated recovery amounts for both Commodity and Demand costs were understated. This finding results in an **over-recovery of Commodity costs in the amount of \$12,033** and an **over-recovery of Demand costs in the amount of \$27,950**.

Company Response

Chattanooga Gas Company concurs that as a result of the use of incorrect PGA factors on the spread sheet the balance as of June 30, 2007 was reported incorrectly. The correct PGA factors were used for customer billing.

FINDING #4:

Exception

The Company understated its Commodity invoiced gas cost for April, May and June 2007.

Discussion

Due to revised Sequent invoices, the Company failed to properly state its Commodity gas costs for the months of April, May and June 2007. Staff increased Commodity gas costs by \$941.56 in April 2007, \$1,193.70 in May 2007 and \$971.90 in June 2007. The result is a **\$3,107.16 under-recovery** of gas costs.

Company Response

Chattanooga Gas Company concurs.

FINDING #5:

Exception

In its ACA filing, the Company made formula errors in the calculation of the ACA balance at June 30, 2007. The errors resulted in an overstatement of the under-recovered balance in the Demand portion of the ACA and consequently an understatement of the over-recovered total balance in the ACA Account.

Discussion

The total balance reported in the ACA Account as of June 30, 2007 in this filing was a negative \$2,883,756.83, which represents an over-recovery of this amount from customers. By letter dated November 26, 2007, the Company filed a tariff to begin refunding this amount effective January 1, 2008.

During the course of this audit, Staff determined that formula errors occurred in the spreadsheet used to calculate the ACA balance. Staff corrected the formulas and recalculated the balance to be a negative \$2,986,120.67 in over-recovered gas costs. The difference is a **negative \$102,363.84 over-recovery**. \$40,234.84 of this difference is explained by Findings #3, #4 and #6. The balance of \$62,129 is the result of the formula errors.

Company Response

Chattanooga Gas Company concurs with the finding that due to a formula an error in the spreadsheet \$62,129 in recovered gas cost was not included in the computation of the June 30, 2007 balance or included in the computation of the ACA effective December 31, 2007.

FINDING #6:

Exception

Commodity and Demand interest amounts were restated due audit findings.

Discussion

Based upon Findings #1 - #5, Staff recalculated interest. Commodity interest due to customers increased from \$337,185 to \$338,883, which increases the over-recovered Commodity balance at 6/30/07 by \$1,698. Demand interest due from customers decreased from \$32,455 to \$30,794, which decreases the under-recovered Demand balance at 6/30/07 by \$1,661.

The result is a **\$3,359 over-recovery** of gas costs.

Company Response

Chattanooga Gas Company concurs.

IX. STAFF AUDIT CONCLUSIONS AND RECOMMENDATIONS

As reported in the body of this report, Staff concludes that the Purchased Gas Adjustment mechanism, as calculated in the Actual Cost Adjustment, appears to be working properly and in accordance with the TRA rules for Chattanooga Gas Company. Staff's audit procedures revealed six (6) findings for the audit period under review.

Going forward, Staff would like to gain greater assurance that the injections and withdrawals reported in the inventory accounts for all companies be properly documented by supplier invoices. **To that end, Staff recommends that the Company provide detailed explanations of selected transactions as was provided during this audit.**

Staff acknowledges and greatly appreciates the corporation and assistance provided by the Company Staff during this audit.

APPENDIX A

PGA FORMULA

The computation of the GCA can be broken down into the following formulas:

$$\text{Firm GCA} = \frac{D + \text{DACA}}{\text{SF}} - \text{DB} + \frac{P + T + \text{SR} + \text{CACA}}{\text{ST}} - \text{CB}$$

$$\text{Non-Firm GCA} = \frac{P + T + \text{SR} + \text{CACA}}{\text{ST}} - \text{CB}$$

where

GCA = The Gas Charge Adjustment in dollars per Ccf/Therm, rounded to no more than five decimal places.

D = The sum of all fixed Gas Costs.

DACA = The demand portion of the ACA.

P = The sum of all commodity/gas charges.

T = The sum of all transportation charges.

SR = The sum of all FERC approved surcharges.

CACA = The commodity portion of the ACA.

DB = The per unit rate of demand costs or other fixed charges included in base rates in the most recently completed general rate case (which may be zero if the Company so elects and the Commission so approves).

CB = The per unit rate of variable gas costs included in base rates in the most recently completed general rate case (which may be zero if the Company so elects and the Commission so approves).

SF = Firm Sales.

ST = Total Sales.

The computation of the RA can be computed using the following formulas:

$$\text{Firm RA} = \frac{\text{DR1} - \text{DR2}}{\text{SFR}} + \frac{\text{CR1} - \text{CR2} + \text{CR3} + i}{\text{STR}}$$

$$\text{Non-Firm RA} = \frac{\text{CR1} - \text{CR2} + \text{CR3} + i}{\text{STR}}$$

where

RA =	The Refund Adjustment in dollars per Ccf/Therm, rounded to no more than five decimal places.
DR1 =	Demand refund not included in a currently effective Refund Adjustment, and received from suppliers by check, wire transfer, or credit memo.
DR2 =	A demand surcharge from a supplier not includable in the GCA, and not included in a currently effective Refund Adjustment.
CR1 =	Commodity refund not included in a currently effective Refund Adjustment, and received from suppliers by check, wire transfer, or credit memo.
CR2 =	A commodity surcharge from a supplier not includable in the GCA, and not included in a currently effective Refund Adjustment.
CR3 =	The residual balance of an expired Refund Adjustment.
i =	Interest on the "Refund Due Customers" account, using the average monthly balances based on the beginning and ending monthly balances. The interest rates for each calendar quarter used to compute such interest shall be the arithmetic mean (to the nearest one-hundredth of one percent) of the prime rate value published in the "Federal Reserve Bulletin" or in the Federal Reserve's "Selected Interest Rates" for the 4th, 3rd, and 2nd months preceding the 1st month of the calendar quarter.

SFR = Firm sales as defined in the GCA computation, less sales under a transportation or negotiated rate schedule.

STR = Total sales as defined in the GCA computation, less sales under a transportation or negotiated rate schedule.