

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

Filed electronically 10/15/08

IN RE:

**PETITION OF ATMOS ENERGY)
CORPORATION FOR APPROVAL OF)
ADJUSTMENT OF ITS RATES AND)
REVISED TARIFF)**

DOCKET NO. 0800197

EARNEST B. NAPIER, P.E.

I. INTRODUCTION OF WITNESS

Q. PLEASE STATE YOUR NAME, POSITION AND BUSINESS ADDRESS.

A. My name is Earnest B. Napier. I am Vice President Technical Services of the KY/Mid-States Division of Atmos Energy Corporation ("Atmos Energy" or "Company"). My business address is 810 Crescent Centre Drive, Suite 600, Franklin, TN 37067-6226.

II. SUMMARY OF TESTIMONY

Q. PLEASE SUMMARIZE THE TESTIMONY YOU INTEND TO GIVE IN THIS MATTER.

A. I will describe Atmos Energy's budgeting process for capital expenses ("Capex"). My testimony will describe how the Company decides upon and prioritizes its capital expenditures.

Specifically, I will discuss the Company's budget for capital expenditures relating to Tennessee for the historic period and as forecast for future years.

1 **III. WITNESS QUALIFICATIONS**

2 **Q. PLEASE DESCRIBE YOUR PROFESSIONAL AND EDUCATIONAL**
3 **BACKGROUND.**

4 A. I received a Bachelor of Science degree in Civil Engineering from The University
5 of Tennessee in 1982. I am a Registered Professional Engineer in the states of
6 Tennessee, Missouri, and Kansas. I have been employed in the utility industry
7 since 1977, predominantly in the natural gas distribution field. I have been
8 employed by Atmos Energy Corporation for over twenty six (26) years.

9 During my time at Atmos, I have held several different positions. I began
10 as a Project Engineer and have held the following positions: Manager-
11 Engineering Design, Division Vice President-Engineering, and Manager-
12 Engineering Services. I was named Vice President of Technical Services for the
13 KY/Mid-States Division in July of 2007.
14

15 **Q. WHAT ARE YOUR RESPONSIBILITIES AS THE VICE PRESIDENT OF**
16 **TECHNICAL SERVICES?**

17 A. I have overall responsibility for decision-making related to technical operations.
18 This includes engineering and system design, safety, compliance, procurement,
19 environmental, measurement, communications, technological infrastructure, and
20 storage operations. I also sponsor Atmos' Compliance Committee, and am a
21 member of the Atmos Utility Operations Council, which sets the Company's
22 standard practices and procedures for construction, maintenance, and service. In
23 addition, I am responsible for developing the Division's (including Tennessee's)
24 annual capital budget, and for monitoring capital budgetary compliance. In this
25 regard, it is my role to ensure that the Company's investment in new plant and
26 equipment in Tennessee is targeted towards meeting the important goals of public
27 safety, system reliability, and efficiency.
28

1 **IV. CAPITAL BUDGETING PROCESS**

2 **Q. WHAT ARE THE OBJECTIVES OF THE COMPANY'S CAPITAL**
3 **BUDGETING PROCESS?**

4 A. The objectives are to:

- 5 (1) Formalize the process of identifying construction needs and prioritizing
6 capital expenditures;
7 (2) Assess the economic feasibility of individual construction projects;
8 (3) Determine overall capital requirements for the planning periods;
9 (4) Reassess long term system maintenance requirements annually; and
10 (5) Review past construction projects and work practices, and apply procedural
11 improvements as appropriate.
12

13 **Q. PLEASE DESCRIBE THE PLANNING AND BUDGET PROCESS FOR**
14 **THE COMPANY'S CAPITAL CONSTRUCTION PROGRAM.**

15 A. The Company plans its capital expenditures over five fiscal years, with a focused
16 emphasis on the first year of that five-year period. We normally begin this
17 process during our third fiscal quarter (April-May) of each year, some 4 to 5
18 months prior to the beginning of the next fiscal year. The process is initiated
19 within the Division by a request from my office for a "bottom-up" submission of
20 projects from our operations supervisors and operations managers in Tennessee.
21 All proposed projects, vehicles, and equipment must be identified at a high level
22 by need and cost, and all budgets are prepared based upon meeting the five
23 objectives described above. The proposed projects, vehicles, and equipment are
24 reviewed by the KY/Mid-States Division's regional vice presidents of operations
25 for collaborative agreements between the regional vice presidents, operations
26 managers, and me.

27 After review, additional information is requested for projects that are
28 determined to be the most eligible for funding, and more detailed documentation
29 is requested from the operations and technical services managers on those
30 particular projects. The process is largely complete by late June when projects are

1 entered into the Atmos Energy capital budget system (PlanIt), although
2 finalization of capital expenditures is not completed until late July. During this
3 time, the agreed-to projects have been further substantiated to ensure they meet
4 the appropriate financial criteria and the stated objectives.

5 The final proposed budget must be reviewed by the Division's senior
6 management, including the Division President. Additional reviews are performed
7 by corporate executive operations management and their staff. High level reviews
8 of the division budgets are also performed by the Company's senior executives
9 who are presiding members of the Company's Management Committee. The
10 Capex budget for Tennessee is not officially approved until it, as part of the
11 Company's total Capex budget, is presented to the Company's Board of Directors
12 in September of each year. Upon this approval, all approved projects are
13 transferred into the Atmos Energy capital tracking system (POWERPLANT) and
14 are ready for appropriation.

15
16 **Q. HOW DOES ATMOS PRIORITIZE ITS CAPITAL EXPENDITURES?**

17 A. Our priorities for capital expenditure, listed in order of importance, are:

- 18 1. Public Safety;
- 19 2. System Capacity and Reliability;
- 20 3. Customer Growth;
- 21 4. Facilities Maintenance;
- 22 5. Public Works; and
- 23 6. Support of Long Term Technological Programs.

24
25 **Q. WHAT FINANCIAL CRITERIA ARE THE MOST SIGNIFICANT IN**
26 **APPROVING A PROJECT DURING THE CAPITAL BUDGETING**
27 **PROCESS?**

28 A. We begin work with an overall capital spending goal, which we try to work
29 within, although variations are permitted if justified. We also use key investment
30 criteria to evaluate projects. Any expenditure above targeted levels must be

1 justified. Individual projects, and our construction program as a whole, are
2 assessed on the basis of their return on investment, return on equity, cost of
3 capital, cash flow, new business forecasts, and various capital overheads such as
4 labor, benefits, and inflation.
5

6 **Q. MUST ALL PROJECTS MEET THE SAME FINANCIAL CRITERIA?**

7 A. No. We separate projects into growth and non-growth capital expenditures.
8 Growth projects are revenue-producing investments for which we can identify a
9 stream of revenues, cash flow, return, payback and other standard investment
10 criteria. Non-growth capital expenditures involve system integrity, equipment,
11 structures, pipeline integrity, system maintenance and reliability projects which
12 are evaluated on a cost/benefit basis. We endeavor to keep our annual non-
13 growth capital expenditures below the level of depreciation. Since these
14 expenditures do not have an associated stream of revenues, our goal is to fund
15 these expenditures through internal financial cash flow. Obviously, there are
16 certain non-growth expenditures that do not impact public safety that can be
17 scheduled into our five-year investment program to ensure that we properly
18 maintain our system while still operating within overall cash flow constraints.
19 Expenditures that impact public safety always have had and will continue to have
20 the highest priority. To help manage and prioritize our System Integrity pipeline
21 replacements projects, we use our Atmos Risk Management Model ("ARMM").
22 ARMM is computer software that was developed to identify and prioritize
23 pipeline replacements, primarily our bare steel pipelines. In accordance with the
24 2007 settlement agreement in Docket Number 07-00105, Atmos is replacing at
25 least 45,000 feet of bare steel main on an annual basis until all bare steel main in
26 the State of Tennessee is retired. We take our obligation to build and operate a
27 safe and reliable gas system very seriously. Finally, there are also a number of
28 projects we must fund over which we have little control as to timing, such as
29 public works projects and highway relocations.
30

1 **Q. HOW CAN THE COMPANY JUSTIFY ADDITIONAL EXPENDITURES**
2 **BEYOND ITS REGULAR CAPITAL BUDGET PROJECTIONS?**

3 A. The KY/Mid-States Division can secure additional funding through Atmos
4 Energy if we can demonstrate that we have potential investments that compare
5 more favorably to competing expenditures in other Atmos business units and are,
6 therefore, more worthy of immediate funding from a purely financial standpoint.
7 Unbudgeted expenditures that impact public safety, system capacity, or reliability,
8 along with compliance projects, have the highest priority, and are considered
9 mandatory capital projects. Unbudgeted expenditures greater than twenty-five
10 thousand dollars must be reviewed by the Division's senior management,
11 including the Division President. If applicable, high-level reviews of unbudgeted
12 expenditures also are performed by the Company's senior executives, who are
13 presiding members of the Company's Management Committee.
14

15 **V. CONTROL & MONITORING OF CAPITAL EXPENDITURES**

16 **Q. WHAT ARE THE GOALS OF THE COMPANY'S PROCESS OF**
17 **CONTROLLING AND MONITORING CAPITAL EXPENDITURE**
18 **VARIANCES?**

19 A. Variances from budgeted amounts are inherent in the process of making capital
20 expenditures. Our variance monitoring process exists to institute financial quality
21 control by formalizing the analysis of variances by responsibility center in a
22 process that identifies year-to-date spending variances by project. These reports
23 are received and reviewed every month at the business unit level and on a
24 quarterly basis at the corporate level. The goal is to keep all levels of
25 management informed of spending by category or project relative to budgeted
26 levels and to ensure that corrective action is initiated on a timely basis. This
27 supports decision-making related to the cost and appropriate management of
28 current and future capital projects.
29

1 **Q. PLEASE DESCRIBE THE COMPANY'S PROCESS FOR**
2 **CONTROLLING AND MONITORING CAPITAL EXPENDITURE**
3 **VARIANCES.**

4 A. The Company's capital budgeting system maintains projects in two broad
5 categories – Blanket Functionals and Specific Projects. The Blanket Functionals
6 include total capital authorizations of a similar type such as new services, leak
7 repair, short main replacements, small integrity/reliability projects, etc. Specific
8 projects are uniquely identified, such as a specific highway relocation project,
9 replacement of work equipment, or some larger significant integrity/reliability
10 project.

11 Once a project has been entered in the capital budget system an
12 appropriation Purpose and Necessity (P&N) may be submitted for authorization.
13 Projects are then monitored to ensure they stay within budgeted levels. If during
14 the course of a project, field management identifies that the costs of the project
15 will exceed approved amounts, a request for supplemental funding may be
16 submitted. All expenditures above authorized appropriation, and all expenditures
17 for unbudgeted projects or variances on budgeted and approved projects, must be
18 approved at the appropriate levels within the Company.

19 Each month, various project variance reports are published. Each budget
20 center manager is responsible and held accountable for managing his overall
21 approved capital budget.

22
23 **Q. DISCUSS CAPITAL SPENDING DURING THE HISTORIC PERIOD.**

24 A. During the historic period, July 1, 2007 through June 30, 2008, the Company's
25 actual capital expenditures in Tennessee were \$21.7 million, resulting in a
26 variance of 19% or \$3.5 million over the historic period budget. This variance
27 was largely due to an unbudgeted system fortification project of over eight miles
28 of 10" and 6" coated steel pipe in Williamson County to support and ensure
29 reliable gas service to the existing and future customer base in the Franklin,
30 Spring Hill and Thompson Station communities..

1

2 **VI. ATTRITION PERIOD CAPITAL BUDGET**

3 **Q. WHAT IS THE ATTRITION PERIOD USED IN THIS RATE**
4 **APPLICATION?**

5 A. The attrition period is April 1, 2009 through March 31, 2010. This represents six
6 months of Tennessee's fiscal year 2009 (FY2009) and six months of Tennessee's
7 fiscal year 2010 (FY2010).
8

9 **Q. WHAT IS TENNESSEE'S ATTRITION PERIOD CAPITAL BUDGET?**

10 A. Tennessee's attrition period capital budget is \$17.7 million. Tennessee's capital
11 budget is comprised of three components: (1) the capital spending for Tennessee
12 for the forecasted period; (2) the amount allocated to Tennessee resulting from
13 capital spending by the KY/Mid-States Division's general office; and (3) the
14 amount allocated to Tennessee resulting from capital spending by the Company's
15 Shared Services (SSU) during the forecasted attrition period. The budgeting
16 process for SSU Capex is described in the direct testimony of Company witness
17 Mr. Waller, and the amounts projected to be closed to plant and comprising
18 additions to SSU rate base are sponsored by Company witness Mr. Petersen. The
19 methodology for allocating SSU and the Division general office rate base
20 amounts to Tennessee is described in the testimony of Company witness Mr.
21 Meziere.
22

23 **Q. HOW WAS TENNESSEE'S CAPITAL BUDGET FOR THE ATTRITION**
24 **PERIOD DEVELOPED?**

25 A. We relied upon the FY2009 capital budget as a baseline for projecting FY2009
26 through FY2010 capital expenditures for purposes of the attrition period in this
27 rate application.
28

29 **Q. WHAT IS TENNESSEE'S FY 2009 DIRECT CAPITAL BUDGET?**

30 A. The original approved FY2009 direct capital budget for Tennessee was \$16.4

1 million.

2
3 **Q. WHAT IS TENNESSEE'S FY2010 DIRECT CAPITAL BUDGET AS**
4 **PROJECTED IN THIS CASE?**

5 A. Tennessee's FY2010 direct capital budget is projected at \$17.2 million.
6

7 **Q. HOW DID YOU ADJUST TENNESSEE'S FY2009 CAPITAL BUDGET IN**
8 **ORDER TO PREPARE THE FY2010 CAPITAL BUDGET?**

9 The projected cost of budgeted projects planned for FY2009, before the
10 application of overheads, was used as a baseline. Five percent was added to
11 FY2009 capital budget to develop the FY2010 capital budget.
12

13 **Q. HOW WAS THE DIVISION'S GENERAL OFFICE CAPITAL BUDGET**
14 **DEVELOPED?**

15 A. The capital budget for the KY/Mid-States Division general office was developed
16 in conjunction with Tennessee's capital budget as well as the capital budgets for
17 all other rate jurisdictions within the Division, as part of the Division's total
18 capital budget. The budgeting processes I have described herein applied to all
19 rate division capital budgets that roll up into the Division's total capital budget,
20 including Tennessee and the Division general office.
21

22 **Q. WHAT IS THE PORTION OF THE DIVISION'S FY2009 CAPITAL**
23 **BUDGET ALLOCATED TO TENNESSEE?**

24 A. The portion of the approved FY2009 Division's general office capital budget
25 allocated to Tennessee is \$12,000.
26

27 **Q. WHAT ABOUT SUBSEQUENT FISCAL YEARS?**

28 A. Those forecasted amounts are \$12,600 for FY2010 and \$13,300 for FY2011.
29

1 **Q. HOW WAS THE SHARED SERVICES ATTRITION PERIOD CAPITAL**
2 **BUDGET DEVELOPED?**

3 A. The development of the Shared Service capital budget for the forecasted attrition
4 period is described in Company witness Mr. Waller direct testimony.
5

6 **Q. WHAT IS THE SHARED SERVICES FY2009 CAPITAL BUDGET**
7 **ATTRIBUTABLE TO TENNESSEE?**

8 A. The portion of the approved FY2009 Shared Services capital budget allocated to
9 Tennessee is \$0.8 million.
10

11 **Q. WHAT ABOUT SUBSEQUENT FISCAL YEARS?**

12 A. Those forecasted amounts are \$0.8 million for FY2010 and \$0.9 million for
13 FY2011.
14

15 **Q. PLEASE DISCUSS TENNESSEE'S OVERALL FORECASTED**
16 **CONSTRUCTION PROGRAM.**

17 A. Tennessee's capital budget was developed by the following major categories:

- 18 1. Equipment;
19 2. Growth;
20 3. Information Technology (IT);
21 4. Pipeline Integrity;
22 5. Public Improvements;
23 6. Structures;
24 7. System Improvements;
25 8. System Integrity; and
26 9. Vehicles.
27

28 **Q. WHAT KEY NEEDS ARE MET THROUGH THIS PARTICULAR**
29 **BUDGET?**

1 A. System improvement, pipeline integrity, and system integrity investments focus
2 on customer safety and system reliability, and are the highest priorities for capital
3 budgeting. Next are public improvements and state and local public works
4 projects such as highway relocations followed by customer growth. Atmos
5 Energy continues to build good working relationships with developers, economic
6 development boards, and growing communities to meet the needs of the customer
7 and to accommodate customer growth on its system. Next in order of priority, a
8 modern fleet of vehicles and equipment (backhoes, safety equipment, ditchers,
9 first responder equipment, air compressors, welding machines, etc.) allows us to
10 maintain our system and continue to provide a reliable level of service to our
11 customers. To enhance the level of customer service provided in the field, we
12 also continue to make investments in new technology. Technology is a strategic
13 investment that will enable us to continue improving our business processes, hold
14 down operating costs, and meet the changing expectations of our customers.

15

16 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

17 A. Yes.

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

IN RE:

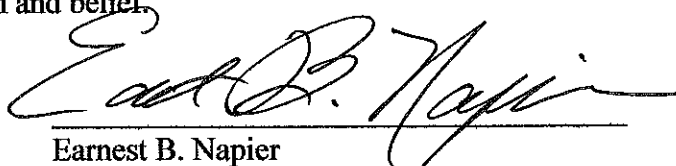
**PETITION OF ATMOS ENERGY
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VERIFICATION

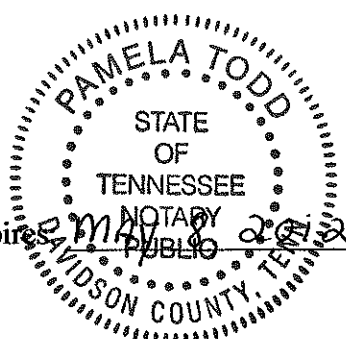
STATE OF TENNESSEE)
)
COUNTY OF WILLIAMSON)

I, Earnest B. Napier, being first duly sworn, state that I am the Vice President of Technical Services for the Kentucky/Mid-States Division of Atmos Energy Corporation, that I am authorized to testify on behalf of Atmos Energy Corporation in the above referenced docket, that the Testimony of Earnest B. Napier in Support of Atmos Energy Corporation's Petition and the Exhibits thereto pre-filed in this docket on the date of filing of this Petition are true and correct to the best of my knowledge, information and belief.

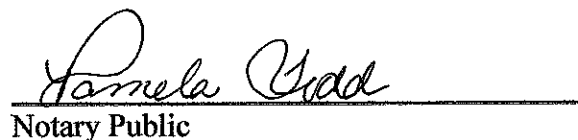

Earnest B. Napier

Sworn and subscribed before me this 24th day of September, 2008.

My Commission Expires



My Commission Expires MAY 8, 2012


Notary Public