BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

October 23, 2009

IN RE:	)	
	)	
CHATTANOOGA GAS COMPANY	)	
PERFORMANCE-BASED RATEMAKING	)	**Docket No. 09-00127**
TARIFF ("INCENTIVE PLAN") 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 Performance-Based Ratemaking Tariff (hereafter "Incentive Plan") for Chattanooga Gas Company ("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 Incentive Plan audit of the Company.

2. The Company's Incentive Plan filing was received on September 1, 2009, and the Audit Staff ("Staff") completed its audit of same on September 30, 2009.

3. Staff detected no material findings during the course of the Incentive Plan audit ("IPA").

4. A final IPA 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 Greene

Paul Greene
Utilities Division of the
Tennessee Regulatory Authority

CERTIFICATE OF SERVICE

I hereby certify that on this 23rd day of October 2009, 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:

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Tennessee Regulatory Authority
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COMPLIANCE AUDIT REPORT
of the
PERFORMANCE-BASED RATEMAKING TARIFF
(hereafter "INCENTIVE PLAN")
for
CHATTANOOGA GAS COMPANY

Docket No. 09-00127

Prepared by:

THE UTILITIES DIVISION
of the
TENNESSEE REGULATORY AUTHORITY

October
2009

EXHIBIT A

COMPLIANCE AUDIT REPORT
of the
PERFORMANCE-BASED RATEMAKING TARIFF
(hereafter "INCENTIVE PLAN")

for
CHATTANOOGA GAS COMPANY
for the Year ended June 30, 2009

Docket No. 09-00127

TABLE OF CONTENTS

I. INTRODUCTION AND AUDIT OPINION

The subject of this compliance audit is the Performance-Based Ratemaking tariff ("PBR" or "Incentive Plan,") of Chattanooga Gas Company ("Chattanooga," "CGC," or the "Company"). The audit objective is to determine whether the Company has complied with the terms and conditions of its PBR tariff as of June 30, 2009. After reviewing the Company's gas[1] purchases activity as reported in the Actual Cost Adjustment Audit ("ACA") filing, along with the applicable benchmark indexes each month, Audit Staff ("Staff") found no material errors. Staff concludes that, during the plan year under review, the Company's gas purchases have met the criteria as specified in its tariff. Section III of this report further describes the actual results of the plan year.

II. BACKGROUND AND DESCRIPTION OF INCENTIVE PLAN

On January 8, 2002, the Tennessee Regulatory Authority ("TRA" or "Authority") issued an Order in Docket Number 01-00619 approving a tariff to establish a performance-based ratemaking mechanism for Chattanooga Gas Company. The specific details of the mechanism are included in Chattanooga Gas' tariff entitled Performance-Based Ratemaking, which was issued on January 25, 2002, made effective on September 11, 2001.[2] The tariff was revised effective February 1, 2006 in Docket No. 04-00402 to include Affiliate Transaction Guidelines, and was further revised effective September 1, 2006 to include RFP Procedures for Selection of Asset Manager and/or Gas Provider. A copy of the current tariff is attached to this report as Attachment 1.

Chattanooga's tariff differs from traditional incentive plans in that the Company does not share in any profits or losses experienced when comparing its actual gas cost purchases against a predetermined benchmark. The "incentive" in Chattanooga Gas's case is a waiver of the prudence audit of gas purchases as required under the TRA's Purchased Gas Adjustment Rule.[3] The terms under which the prudence audit will be waived is found in the section Prudence Determination of the tariff (Second Revised Sheet No. 56A).

> "If Chattanooga's total commodity gas cost for the plan year does not exceed the total benchmark amount by one percentage point (1%) for a plan year ending after June 30, 2000, Chattanooga's gas cost will be deemed prudent and the audit required by Tennessee Regulatory Authority's Administrative Rule 1220-4-7-.05 is waived. If during any month of the plan year, the Company's commodity gas cost exceeds the benchmark amount by greater than two percentage points

[1] Docket # 09-00126.

[2] September 11, 2001 was the date of the Authority Conference during which the Directors voted to approve the Company's tariff petition with certain modifications.

[3] TRA Rule 1220-4-7-.05.

(2%), the Company shall file a report with the Authority fully explaining why the cost exceeded the benchmark."

The Company put its asset management contract out for bid following the approved RFP procedures and brought the fully executed contract before the TRA for approval in Docket No. 08-00012. The TRA approved the contract at its February 25, 2008 Authority Conference to become effective April 1, 2008 as requested by the Company.

During the reporting period which is the subject of this audit, Sequent Energy Management[4] ("SEM") was CGC's asset manager. The terms of the asset management agreement provided that SEM would supply CGC's gas requirements and manage its assets. Fifty percent (50%) of the proceeds realized by SEM under the agreement are refunded to the utility's customers via the Interruptible Margin Credit Rider ("IMCR") tariff.[5] Benefits accruing to customers during the audit period are explained more fully in Section III., ACTUAL PLAN YEAR RESULTS.

The Incentive Plan automatically rolls over for an additional plan year on each July 1st, and continues until the Incentive Plan is either (a) terminated at the end of a plan year or by not less than 90 days notice to the TRA by Chattanooga Gas or (b) modified, amended or terminated by the TRA.

III. ACTUAL PLAN YEAR RESULTS

On September 1, 2009, Chattanooga filed an annual report as required by its tariff, showing the actual cost of gas invoiced by its affiliate Sequent Energy Management ("Sequent" or "SEM") and other suppliers and the applicable benchmark index for each purchase during each month of the plan year ending June 30, 2009. The Staff reviewed Sequent invoices and other supplier invoices which were filed as part of the Company's ACA audit, and the indexes used to calculate the benchmark each month.[6] The first table below is a table summarizing the Company's monthly purchases as compared to the calculated monthly benchmarks with their fixed costs included in both benchmarks and the actual purchased cost of the gas. This table is inappropriate to judge actual purchase cost against the Company's benchmark due to a fixed price transaction which was entered into in June of 2008 and affected the cost of the Company's actual gas for the months of August, September, and October.

In June 2008, an off-system customer approached the Company and requested that they supply LNG to its facility over the summer. To provide the quote to the off-system customer for over the summer delivery and lock in the margin from the transaction, the Company entered into a fixed price deal to purchase gas for liquefaction at $11.81

[4] Sequent is the unregulated marketing arm of AGL Resources, Inc., the parent company of Chattanooga Gas and therefore, an affiliate of Chattanooga.

[5] Under the IMCR tariff, the utility does not share in the 50% of proceeds that are refunded to customers.

[6] The table presented on page 3 of this report shows a 9.3% price over benchmark. This could be interpreted to violate the prudency determination show in Attachment 1 sheet 56 A. This is not considered a violation since the Company entered into a fixed price agreement which resulted in financial gain to both Sequent and the customers of CGC equally.

citygate price for delivery in August. The market condition changed in August, and the market price for the SNG zone 0 wellhead price was $9.34. This caused the variance on the Company's PBR filing to be greater than the benchmark by more than 1%. However, the $11.81 purchase price was used to compute the cost of the off-system sales and the resulting profit margin was shared with the ratepayer[7]. The $11.81 purchase price was not used to determine the PGA rate charged to the Company's ratepayers and was not included in the cost of gas sold to the Company's on-system customers. The Company's regulated customers were not adversely affected by the fixed price purchase. The appropriate table to look at to compare the Company's actual purchased cost of gas against benchmarks is the second table, which excludes the fixed-price purchase transaction.

[7] Profits resulting from the fixed price deals executed by Sequent on the behalf of CGC as their asset manager provided equal financial benefit to both Sequent and the customers of CGC, although CGC is not required to share the profit with their customers.

Cost of Gas Including Fixed Price Purchase Transaction			
Month	**Actual Purchase Cost**	**Benchmark Cost**	**Percentage Over/(Under) Benchmark**
July 2008	$12,011,964.15	$12,011,973.26	-0.0001%
August 2008	$6,519,075.67	$5,964,014.18	**9.3068%**
September 2008	$5,035,089.06	$5,043,822.38	-0.1731%
October 2008	$6,255,060.30	$6,256,758.93	-0.0271%
November 2008	$4,842,563.36	$4,810,256.09	0.6716%
December 2008	$4,479,271.30	$4,460,018.14	0.4317%
January 2009	$4,410,740.43	$4,391,093.02	0.4474%
February 2009	$2,435,811.12	$2,416,394.42	0.8035%
March 2009	$1,649,367.19	$1,618,680.63	1.8958%
April 2009	$2,412,590.56	$2,412,594.11	-0.0001%
May 2009	$1,901,539.33	$1,901,520.71	0.0010%
June 2009	$1,570,966.43	$1,570,943.51	0.0015%
Annual Cost	**$53,524,038.90**	**$52,858,069.39**	**1.2600%**

Cost of Gas Excluding Fixed Price Purchase Transaction			
Month	**Actual Purchase Cost**	**Benchmark Cost**	**Percentage Over/(Under) Benchmark**
July 2008	$12,011,964.15	$12,011,973.26	-0.0001%
August 2008	3,669,609	3,669,685	-0.0021%
September 2008	4,886,378	4,886,370	0.0002%
October 2008	6,114,871	6,114,979	-0.0018%
November 2008	$4,842,563.36	$4,810,256.09	0.6716%
December 2008	$4,479,271.30	$4,460,018.14	0.4317%
January 2009	$4,410,740.43	$4,391,093.02	0.4474%
February 2009	$2,435,811.12	$2,416,394.42	0.8035%
March 2009	$1,649,367.19	$1,618,680.63	1.8958%
April 2009	$2,412,590.56	$2,412,594.11	-0.0001%
May 2009	$1,901,539.33	$1,901,520.71	0.0010%
June 2009	$1,570,966.43	$1,570,943.51	0.0015%
Annual Cost	**$50,385,671.93**	**$50,264,508.22**	**0.2411%**

In four (4) months, amounts invoiced by Sequent and other suppliers were below the calculated benchmark for the month. In the eight (8) remaining months, amounts invoiced by Sequent and other suppliers were above the calculated benchmark, but within the 2% monthly upper limit of the tariff. The total gas costs invoiced for the year were 0.2411% above the annual benchmark amount which is below the 1% plan year upper limit. Therefore, Staff opines that Chattanooga Gas has satisfied the criteria as set forth in its tariff and is released from the prudence audit for the plan year ended June 30, 2009.

On May 27, 2009, Chattanooga filed a tariff to refund the customers' share of profits accruing under the Interruptible Margin Credit Rider ("IMCR"). At March 31, 2009, the customers' share of net profits including interest and residual from the prior year totaled $4,146,960. Effective July 1, 2009, the Company began refunding this amount to its customers.

IV. JURISDICTION OF THE TENNESSEE REGULATORY AUTHORITY

Tennessee Code Annotated (hereafter "T.C.A.") gave jurisdiction and control over public utilities to the Tennessee Regulatory Authority. T.C.A. § 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, T.C.A. § 65-4-105 grants the same power to the Authority with reference to all public utilities within its jurisdiction as chapters 3 and 5 of Title 65 of the T.C.A. has conferred on the Department of Transportation's oversight of the railroads or the Department of Safety's oversight of transportation companies. By virtue of T.C.A. § 65-3-108, said power includes the right to audit:

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

The Authority's Utilities Division is responsible for auditing those companies under the Division's jurisdiction to insure that each company is abiding by the rules and regulations of the TRA. This audit was performed by Paul Greene and Tiffany Underwood of the Utilities Division.

V. IPA FINDINGS

After reviewing the Company's filing, the Staff concludes that there are no material findings.[8]

[8] 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.

VI. CONCLUSIONS AND RECOMMENDATIONS

After reviewing the Company's gas purchases activity as reported in the ACA filing, along with the applicable benchmark indexes each month, Staff found no material errors. Staff concludes that, during the plan year under review, the Company's gas purchases have met the criteria as specified in its tariff. Therefore, for the plan year ended June 30, 2009, Staff recommends that the Company be released from the prudence audit requirements encompassed in the Purchased Gas Adjustment Rule ("PGA Rule") 1220-4-7-.05.

The Company tariff requires:

> FILING WITH THE AUTHORITY
>
> The Company will file an annual report not later than 60 days following the end of each plan year identifying the actual cost of gas purchased and the applicable index for each month of the plan year.[9]

Staff recommends that the Authority direct the Company to comply with the filing deadline cited above.

Audit Staff recognizes and appreciates the cooperation of the Company personnel during this audit.

[9] Second Revised Tariff Sheet No. 56A.