BEFORE THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE TENNESSEE

IN RE:	)	
	)	
AUDIT OF ATMOS ENERGY	)	
CORPORATION'S INCENTIVE PLAN	)	**Docket No. 11-00195**
ACCOUNT FOR PERIOD OF APRIL 1,	)	
2004 THROUGH MARCH 31, 2007	)	

REPLY TESTIMONY OF REBECCA M. BUCHANAN
ON BEHALF OF ATMOS ENERGY CORPORATION

Q. Will you please state your name and business address?

A. My name is Rebecca M. Buchanan, and my work address is 377 Riverside Drive, Suite 201, Franklin, TN.

Q. Did you pre-file direct testimony in this Docket No. 11-00195?

A. Yes.

Q. Have you reviewed the pre-filed Affidavit of Staff witness Pat Murphy on behalf of the Utilities Division of the Tennessee Regulatory Authority?

A. Yes.

Q. What is the purpose of your reply testimony?

A. My reply testimony addresses and responds to several statements in Staff's brief and affidavit.

Q. What statements do you want to correct in Staff's Affidavit?

A. Ms. Murphy's Affidavit is organized in a series of 24 paragraphs. In my reply testimony that follows, I will explain my concerns for the accuracy and representation of information found in paragraphs 10, 11, 12, 13, 15, 17 and 20 .

Q. What observations do you have regarding paragraph 10?

A. In paragraph 10, Ms. Murphy states that *"Staff became aware of Atmos's AMA for the first time when auditing the ACA."* Typically Staff's ACA audit would commence sometime after the ACA period in question, which according to Staff's affidavit was 7/1/04 – 6/30/05. Atmos has located an email from Company employee Mark Martin to former TRA Staff Member Gary Lamb responding to an inquiry from Staff. The email is dated October 6, 2004. Mr. Martin's email explains that AEM made a payment to Atmos as a result of becoming the utility's agent through the RFP process, that the RFP was for the management of the utility's assets, that AEM provided the best bid for our customers, and in that bid AEM agreed to pay the utility for the opportunity to manager the utility's assets. The October 2004 date of this communication was prior to Staff beginning its audit for the 2004-2005 period, since the Company's ACA period begins July 1 and ends June 30 each year. The Company submitted this ACA filing on September 15, 2005, some eleven months after the exchange between Mr. Martin and Mr. Lamb.

Q. In paragraph 11, Staff suggests that because 100% of the AMA upfront payment is initially flowed through the PGA to the full benefit of customers, that somehow Atmos should be precluded from sharing in the savings that are specifically anticipated in the CMIM tariff language. What is wrong with this inference?

A. Staff fails to explain that all savings covered by the Atmos PBR mechanism, whether the savings are from Commodity Discounts, Capacity Releases, Capacity Management payments, or other, are always initially flowed through the ACA to the full benefit of the customers. It is only through the subsequent Performance Based Ratemaking filing that Atmos is given the opportunity to request a share of the savings that has already been realized by the customers. Upon the Authority's approval, the recovery mechanism is accomplished through the Incentive Plan Account (IPA) via an after-the-fact gas cost rider. There is nothing unique or remarkable about this process, and certainly by initially flowing the full savings through to the Tennessee customers Atmos has in no way waived its right to seek subsequent recovery of a share of those savings, as is provided for in the Company's tariff. In fact, this is exactly the way the PBR mechanism is intended to work. Similarly, Piedmont Natural Gas Company, Inc., d.b.a. Nashville Gas, has the same process of initially crediting 100% of savings to customers and then seeking subsequent recovery of a share of the savings. For example, this can be seen in Piedmont's September 29, 2011 filing in Docket 11-00169, line 52, Asset Management Payment.

Q. In paragraph 12, Staff asserts that a bulk release of capacity in exchange for an upfront payment was not contemplated by the Authority in the terms of the Capacity Release Incentive Mechanism. What is wrong with this assertion?

A. Several things. Staff refers incorrectly to the name of the Company's tariff mechanism, which is not Capacity ***Release*** Incentive Mechanism, but rather, Capacity ***Management*** Incentive Mechanism (*emphasis added*). The tariff language for this mechanism reads "*To the extent the Company is able to release daily transportation or daily storage capacity, the associated savings will be shared by the Company's customers and the Company on a 90/10 basis.*" It is irrelevant that the release of daily capacity is done in bulk, or done piecemeal. Either way, daily capacity is released. And either way, the Company is procuring savings for the customer through effective capacity management, exactly what the tariff is intended to encourage.

During the period in dispute (2004-2010), the Company's work to secure Asset Management Agreements has saved Tennessee customers nearly $3.8 million in contested up-front Asset Management payments. Additionally over that same period the Company obtained commodity savings for the customers of more than $6 million. That is a combined savings of nearly $10 million for Tennessee customers. It is obvious by these results that the Company is striving for and successfully achieving savings for its customers. This is exactly what the PBR mechanism was intended to encourage.

Q. In paragraph 13, Staff points to the following tariff language as proof that the Authority did not consider Asset Management capacity releases: "*To the extent the Company is able to release daily transportation or daily storage capacity, the associated savings will be shared by the Company's customers and the Company on a 90/10 basis.*" 1st Revised Sheet No, 45.2, <u>Capacity Management Incentive Mechanism</u>. What is wrong with this argument?

A. This argument reflects a misunderstanding of capacity release. On page 8 of my direct testimony in this Docket, I provided a thorough discussion of why a release of daily capacity is not the same as doing a daily release. To my knowledge the Company has never done releases of capacity on the frequency of "daily". Ms. Murphy indicates on page 4 of her affidavit that the capacity releases performed by the Company before and during the hearings in Docket No. 97-01364 were made <u>monthly</u>. It just does not make sense to think the Authority would require the Company to post a capacity release every single day – that would be inefficient and frankly absurd. What does make sense is that the Company releases its <u>daily</u> transportation capacity or its <u>daily</u> storage capacity (just like the tariff indicates, and just like what we have done). The unit of measure for capacity is "daily capacity." Pipeline contracts describe the capacity in terms of MDQ "maximum daily quantity", MDIQ "maximum daily injection quantity", and MDWQ "maximum daily withdraw quantity".

To reiterate my direct testimony, when Atmos performs a capacity release, we are releasing the daily capacity, whether we perform that task once a day, once a month, or once a year, or longer. It is still a release of daily transportation or daily storage capacity regardless of the duration or the frequency of that release. The Tariff does not specify that Atmos must perform the task of releasing every day, but only that we release our daily quantity. And if we are successful, we share in the savings. An AMA involves real capacity releases of daily transportation and daily storage capacity. The releases are done once at the beginning of the contract term. We release our daily capacity to our Asset Manager; this is considered a secondary market release. The value received for the releases comes in the form of the annual up-front payment we receive from the asset manager, pursuant to the terms of the Asset Management Agreement. There is no conflict between the Company's capacity release activity and the Company's tariff language for the Capacity Management Incentive Mechanism.

Q. Did you find any errors in Staff's paragraph 15?

A. Yes. In paragraph 15, Staff stated that during the first year the Asset Management Agreement was in place (2004-2005), total savings under the plan were derived from the Capacity Management Incentive Mechanism and that no savings were reported under the Gas Procurement Incentive Mechanism. This is an inaccurate statement. What Atmos reported in its 2004-2005 filing was that there were no Gas Procurement Savings outside the *deadband.* However, there were in fact Gas Procurement Savings of $327,685 within the deadband. These savings were retained 100% by the Tennessee customers, and Atmos did not share in any of these savings. Perhaps Staff overlooked this because Atmos is the only TN regulated LDC whose savings are subject to a deadband before the Company has an opportunity to share in the savings. In 2004-2005, 47% of total overall savings of $748,557 for that year were the result of the upfront AMA payment. Similarly for the full three year IPA period under review in this Docket, there were Gas Procurement Savings of $1,627,625 within the deadband. These savings are retained 100% by the Tennessee customers. Also during this same three year period, the AMA upfront payment averaged 37% of total overall savings of $2,753,414. In her Affidavit, Ms. Murphy incorrectly stated that the percentage of Atmos capacity release savings were a far cry from the 30-35% experienced during the Incentive Plan hearings. To the contrary, the 37% of savings experienced in subsequent years (i.e. in the years under review here) were within the same range. That Ms. Murphy erred in calculating 83.6% in paragraph 15 dispels her resulting assessment that "this is proof that asset management agreements were not the norm and the Authority had no opportunity to examine these types of arrangements when approving the terms of the current Incentive Plan." Her conclusion is founded upon an erroneous calculation.

Q. Of what significance or relevance is the percentage of total savings generated by the Asset Management upfront payment?

A. In this proceeding, none. There is no language in the Atmos tariff to indicate a certain percentage of the savings must come from any one of the categories of savings. Staff's argument in this regard is a red herring. It is important to keep in mind that the Company has negotiated contracts that create savings for the customers. The IPA provides for shared savings from the discounted commodity cost of gas (via the Gas Procurement Incentive Mechanism), from the release of daily transportation or daily storage capacity (via the Capacity Management Incentive Mechanism) and from Financial Instruments or Other Private Contracts. It does not matter if savings come from one category or from all categories, the Company is subject to a cap on overall incentive savings or costs on both mechanisms of $1.25 million annually. For the three year period in review in this Docket, the uncontested Atmos share of savings is $9,698 on total savings of $2,753,414, less than one half of one percent. For the three year period in review in this Docket, the contested Atmos share of savings totals $102,881, which is less than 4% of total savings. This shared savings is a mere fraction of the $1.25 million annual cap on Atmos shared savings. It is perplexing that Staff has taken such an adamant position against the Company's small shared savings when the Company has obtained millions of dollars in savings for the benefit of Tennessee customers.

Q. In paragraph 15, Ms. Murphy states that in 2004, asset management agreements were not the norm and the authority had no opportunity to examine these types of arrangements when approving the terms of the current Incentive Plan. Do you agree?

A. No. There is evidence in publically filed Compliance Audit Reports of Nashville Gas Company from as far back as the 1999-2000 period that there have been lump sum Asset Management payments. For example, in Docket No. 00-00759, Compliance Audit Report of Nashville Gas Company's Incentive Plan Account, prepared by the TRA's Energy and Water Division, for the year ended June 30, 2000, on page 3, Section III of Staff's report indicates:

> "The Capacity Management Mechanism generated a total of $1,950,692 in savings, of which $300,692 was due to off system sales and $1,650,000 was due to capacity release. ... The $1,650,000 savings for this year was the result of

Nashville Gas assigning its pipeline capacity to an "asset manager". The Company provided the following summary of its Gas Asset Management Agreement to the TRA Staff.

"Under the Gas Asset Management agreement, Nashville Gas assigns its firm pipeline transportation (capacity), storage (excluding local LNG) and supply rights to the "Asset Manager." In return for this assignment, Nashville Gas receives a lump-sum payment from the asset manager for the assignment of these rights.

Nashville Gas retains the right to call on supply from the asset manager for its city gate needs consistent with its rights as they existed prior to their assignment to the asset manager. The asset manager's lump-sum payment is for the value acquired for utilization of the released assets when they are not needed by Nashville Gas. The lump-sum payment is considered a capacity release transaction and, as such is accounted for in the Performance Incentive Plan under the Capacity Management Incentive mechanism.

In essence, Nashville Gas and its ratepayers are "guaranteed" the up-front lump-sum payment by the asset manager, as opposed to Nashville Gas releasing capacity and entering into off-system sales transactions with third parties…."

For each of the next seven years, Staff's Compliance Audit Reports of Nashville Gas Company's Incentive Plan Account contained the following footnote in Section III: "*Under the Gas Asset Management agreement, Nashville Gas assigns its firm pipeline transportation (capacity), storage (excluding local LNG) and supply rights to the "Asset Manager." In return for this assignment, Nashville Gas receives a lump-sum payment from the asset manager for the assignment of these rights.*" This is proof that the Authority and Staff had ample opportunity during the five years preceding the Atmos 2004 Asset Management Agreement to examine these types of arrangements.

The fact that Asset Management Agreements and the use of asset managers has been in industry practice since well before 2004 is supported by the response of Nashville Gas Company to Interrogatory No. 13 in Docket No. 05-0165 (Review of Nashville Gas

Company's IPA, Relating to Asset Management Fees, Audit Staff First Discovery Requests, dated November 14, 2005):

***"Interrogatory No. 13**:*

Explain in detail the extent to which regulated natural gas utilities use outside asset managers. In your answer, describe such usage as of April, 1996 and describe the evolution of such usage through the present.

***Response**: Nashville Gas Company is unable to answer this question inasmuch as it is not familiar with the practices of other regulated natural gas utilities in this regard. Notwithstanding this fact, it is Nashville Gas' belief, based on anecdotal evidence, that asset management arrangements have become more common since April of 1996."*

Q. Please comment on the two subparts of Ms. Murphy's Affidavit paragraph 17.

A. The Company disagrees with subpart a. The Atmos 2004 Asset Management Agreement is essentially a capacity release transaction, similar in nature to the capacity releases reported from 1999 to 2004, and especially similar to the Asset Management Agreements reported by Nashville Gas from 1999 forward. In paragraph 17 subpart b., Staff has again made an erroneous assertion that the payments under Atmos' 2004 asset management arrangement constitutes a much larger percentage of savings than when the Authority approved the IPA. This has already been discussed and rebutted in the discussion of paragraph 15 above. The Company disagrees that at the time the Authority considered whether to approve an Incentive Plan for Atmos that the savings from asset management arrangements were much less than the savings experienced in 2004. In particular, the historic percentage of savings from Nashville Gas Company's Asset Management fees are set forth in the following table:

Nashville Gas Company

Docket No.	Year	AMA fee as % of Capacity Mgt Savings / AMA fee as % of Total Incentive Savings
00-00759	1999-2000	85% / 74%
02-00933	2001-2002	83% / 96%
03-00489	2002-2003	72% / 46%
04-00290	2003-2004	84% / 57%
05-00268	2004-2005	72% / 46%

This table illustrates that savings from Asset Management fees were a significant portion of Nashville Gas Company's IPAs for several years prior to Atmos' 2004 Asset Management Agreement, and they have been allowed to retained a share of the savings from these arrangements.

Q. Do you have any comments regarding paragraph 20?

A. Yes. In paragraph 20, Ms. Murphy indicates that Staff clearly stated to the Company its position on the inclusion of asset management fees, and that Staff advised Atmos that Asset Management Agreement upfront payments are not eligible for sharing between customers and Atmos under the terms of the current Incentive Plan. The Company disagrees with Staff's position; Atmos' tariff encourages the Company to enter into capacity management transactions. The purpose of using an asset manager is to extract the most value from unutilized assets for the benefit of Tennessee customers and the Company, whose interests are aligned under the Incentive Plan.

Q. With regards to Staff's repeated statements that the Company is required to obtain prior approval of contracts, do you wish to respond?

A. Yes. On page 5 of Staff's brief, Staff cites that the Company's failure to notify the TRA is in violation of the PGA Rules (footnote 24). Staff states that the PGA Rule 1220-4-7-.03(5)(iii) empowers the TRA to review and determine the prudency of payments and purchases made to or from an affiliate. The Company has read that Section of the PGA Rule (statute) and the words "or from" is not within the Rule. The PGA rule addresses all costs incurred by the Company and subjects the Company to a prudency review of those costs. Payments to the utility from an Asset Manager, which are not costs to the utility, are not addressed in the PGA Rule. The credit by Atmos of the Asset Manager upfront fee to the ACA filing is made because it is required under the Performance Based Ratemaking Mechanism.

The TRA issued its order in Docket 05-00253 on December 7, 2006. The Authority voted to adopt Staff's recommendations with the exception of Recommendations 1 through 2(c). Recommendation 3 states: "The Authority should direct the Company to file all future proposed asset management and gas procurement agreements or renewal of the current contract with the TRA for prior approval of the Authority." On January 30, 2007, the TRA approved Staff's clarification (Exhibit I) to the above language states "To clarify the recommendation with respect to the gas procurement agreement, Staff is asking the Authority to require the Company to timely file its executed gas procurement agreements with the Authority Staff, so that they are available to Staff for its review and acceptance during the audits of the ACA and any future filings under the Company's Performance Based Ratemaking Mechanism Rider included in the Company's tariff."

As a practical matter, all executed Atmos' contracts for Asset Management have been submitted to the Tennessee Regulatory Authority for approval. It is Atmos' practice to include regulatory out language in the event the Authority does not approve the agreement, and the Authority has accepted this practice.

Q. If the Authority is persuaded by Staff's position that the Asset Management upfront payments are not to be considered within Atmos' Capacity Management Incentive Mechanism, what alternative treatment may be afforded these savings?

A. There are three other possible treatments that may be afforded Asset Management upfront payments. The first alternative, as was explained in my direct testimony in this Docket on page five and in Exhibit A, is that the Asset Management contract is covered under the Atmos tariff provision for a Capacity Assignment Credit Rider (1^{st} Revised Sheet No. 45). This provision allows the Company to enter into contractual agreements with others to temporarily assign or release capacity held by the Company. Revenues related to any fixed demand costs, related surcharges and any additional administrative charges shall be shared on a 90/10 basis. A second alternative is that the 2004 asset management contract, also known as the "Gas Exchange and Optimization Services Agreement", be considered an "Other Private Contract." Atmos' tariff 1st Revised Sheet No. 45.2 addresses Financial Instruments or Other Private Contracts within the context of the Performance Based Ratemaking Mechanism Rider. "To the extent the Company uses … other private agreements to … manage or reduce gas costs, any savings or costs will flow through the commodity cost component of the Gas Procurement Incentive Mechanism." This treatment would afford sharing on a 50/50 basis. And lastly, as I mentioned in my Direct testimony page 18, if the up-front AMA payments are not considered to be payments for capacity release, then there would be no requirement to credit them against the Company's gas costs. The net effect would be that the Company would retain 100% of the up-front AMA payments. Indeed, if these up-front AMA payments are deemed not to be capacity release payments, the Company will have the right to go back and adjust its ACA filings for these prior years by removing these AMA up-front payments from the gas cost calculations, pursuant to TRA Rule 1220-4-7-.03(1)(c)(3).

Q. Please comment on the agreement between United Cities and Woodward Marketing that was discussed in the Authority's Final Order On Phase Two, Docket Nos. 95-01134, and 97-01364 (August 16, 1999)?

A. From the discussion in that Order, it is clear that United Cities entered into an all requirements gas supply agreement with its affiliate Woodward Marketing, LLC. The contract with Woodward was a bundled asset management and gas supply agreement. Among other things, this contract gave Woodward the right to manage all of United Cities' upstream capacity. Testimony established and the Authority found that Woodward Marketing was providing United Cities with very favorable rates for gas supply. Importantly, testimony also established that the *reason* Woodward could provide such good gas supply prices was that the contract allowed Woodward to serve as an asset manager and try to earn a profit by releasing unused capacity on the secondary market.

As the Order notes, "Mr. Woodward testified that WMLLC [Woodward Marketing] could not afford to offer such a guaranteed low price to United Cities if it could not use United Cities' capacity to generate a profit." The Authority ultimately approved of this arrangement between United Cities and Woodward Marketing and held that Woodward had been billing United Cities appropriately pursuant to the contract. The significance of this was that the resultant savings on the gas cost side would be included within the Company's incentive plan account.

As mentioned, the United Cities / Woodward agreement described in this Order was a bundled gas supply / asset management agreement. In exchange for the right to manage UCG's pipeline assets and make a profit from them, Woodward agreed to provide UCG with below-market gas prices. In other words, instead of providing an up-front cash payment for the right to manage UCG's assets, Woodward made this payment in the form of lower gas prices. Woodward and UCG could have structured this deal as a separate supply agreement and asset management agreement, and Woodward could have agreed to pay UCG a fixed up-front fee – i.e. the type of Asset Management Agreement up-front payment that Staff have challenged in this case. The economic effect would have been the same. The Woodward / UCG agreement was, in reality, an asset management agreement.

Q. Does this conclude your testimony?

A. Yes.

Rebecca M. Buchanan

Rebecca M. Buchanan

STATE OF TENNESSEE)
)
COUNTY OF Williamson)

SWORN to and subscribed before me
this 14 day of March, 2012.

Deborah G. Sparkman

Notary Public

My Commission Expires: **My Commission Expires: September 16, 2012**

DEBORAH G. SPARKMAN
STATE OF TENNESSEE NOTARY PUBLIC
RUTHERFORD COUNTY

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing has been served, via the method(s) indicated below, on the following counsel of record, this the 14th day of March, 2012.

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