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

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| **IN RE:** | ) | |
| | ) | |
| **PETITION OF ATMOS ENERGY** | ) | |
| **CORPORATION FOR ANNUAL** | ) | **Docket No. 14-00081** |
| **REVIEW OF RATES** | ) | |
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## RESPONSE OF ATMOS ENERGY CORPORATION TO CONSUMER ADVOCATE'S MOTION TO DISMISS OR DENY PETITION FOR FAILURE TO MEET STATUTORY REQUIREMENT

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Last year the legislature undertook to streamline utility ratemaking. With TRA backing, the legislature adopted what is now Tenn. Code Ann. 65-5-103(d), authorizing the Authority to implement alternatives to lengthy litigated rate case proceedings. The Consumer Advocate's position would wholly defeat the purpose behind the new law. Rather than reducing the need for time consuming and expensive traditional rate case proceedings, the Advocate's position would make them a prerequisite. Parties who have heretofore sought to reduce the burden of traditional rate case proceedings by resolving them through settlement would be excluded from participation in at least one of the new statutory alternatives, and thereby punished for their past efforts at cooperation. The Advocate's position is fundamentally wrong as matter of policy and legislative intent.

The Advocate's position is equally wrong as a matter of statutory construction and legal analysis. Subsection (d)(6)(B) of the statute specifies the criteria for a utility to be eligible to opt-into the (d)(6) annual review procedure. To be eligible, a utility must have "engaged in a general rate case . . . within the last five (5) years." The statute does not require that the rate case

have been resolved after a full-blown hearing. It does not require any specific form of final order. And it certainly does not exclude resolution by stipulation or settlement. Of course, that is fully consistent with the statute's overriding purpose – to *reduce* rate case litigation, and *encourage* resolution short of an all-issues rate case hearing on the merits.

The Advocate's position stems from the myopic isolation of a few words from one preliminary finding in the TRA's order approving Atmos Energy's settlement of its most recent rate case. In reality, the Stipulation and Settlement Agreement reached between the Advocate and Atmos Energy was "approved, adopted, and incorporated in this [the TRA's] Order as if fully rewritten herein." And that Stipulation and Settlement Agreement in turn included an agreed series of schedules specifying the manner in which the new rates had been determined. While the Advocate clings to certain exculpatory language in the Agreement, the fact remains that the parties ***did agree*** on the settlement's financial terms, including those schedules. The Agreement was not merely illusory, and its incorporation into an Order makes it binding as to *Atmos Energy*, a separate question from whether it, as a consent order, could ever be cited as Authority *precedent,* pursuant to principles of *stare decisis.*

When viewed more reasonably, it becomes clear that, in calling for the Authority to "order the public utility to make the adjustments to its tariff rates to provide that the public utility earns the authorized return on equity," subsection (d)(6) necessarily calls upon the Authority to exercise its ratemaking judgment. At some level, a decision about how rates should be adjusted to earn a given rate of return must be more than a merely mechanical task. It should be clear that no order resolving a rate case reasonably can be expected to descend to every cell of every spreadsheet. The Authority has broad discretion in setting rates, and there is little question that the statute calls for the exercise of that discretion at some level. The only question then is one of

degree. The Advocate's position begs the fundamental question, if the Atmos Energy case was somehow lacking, then what would be required to satisfy the Advocate's view of the (d)(6) annual mechanism? When *would* a utility have the right to opt-into the new statutory mechanism? It is no answer to say that the mechanism will simply be unavailable. The legislation should not be read so as to render it a nullity.

And even if, for the sake of argument, one were to assume the Advocate's position on subsection (d)(6)(A) of the Statute, the Authority still would have the statutory power to grant Atmos Energy's petition in this matter under the broad grant of power provided by subsection (d)(7).

## I. The Advocate's Position is Fundamentally Wrong as a Matter of Policy and Legislative Intent.

### A. The intent of this statute is to reduce the need for protracted and expensive rate case litigation.

The 2013 legislation expressly authorizes the Authority "to implement alternative regulatory methods to allow for public utility ***rate reviews*** and cost recovery ***in lieu of a general rate case proceeding*** before the authority." Tenn. Code Ann. § 65-5-103(d)(1)(A) (emphasis added). The bill's Senate Sponsor explained the legislation was intended to allow "rate reviews and cost recovery in place of the current process" of traditional rate case litigation, which "from the TRA's perspective and the administration's perspective is litigious and lengthy and costly." April 2, 2013 Senate Finance, Ways and Means, Statement of Sponsor Norris (attached). In his testimony before the same committee, then-Chairman Allison explained:

> The area that seems to have attracted the most attention with the Consumer Advocate's response to it is the alternative ratemaking authority section of the bill. This is something that we at the agency, the staff has examined it very closely. We are comfortable with what this does. It essentially is ***another step in the direction of trying to make the agency as efficient as we possibly can*** and keeping with what this body did last year to

> try ***to streamline our process***, to try to make a more cost effective, and it's one of the pieces that we'll take to try to make sure that we are able to live within the lower budget that we'll have by the fact that we'll reduce our fee substantially.

*Id.,* Statement of TRA Chairman James M. Allison (emphasis added).

There is nothing in the legislative history to suggest a belief that the (d)(6) annual review mechanism would be subject to special requirements, or that it would be available only if a utility had not settled its most recent rate case proceeding. To the contrary, in the same breath that he described the new annual review mechanism, the bill's House sponsor acknowledged that rate cases do get settled:

> Section 5 . . . creates a new section authorizing the implementation of alternative regulatory methods for utility rate reviews and cost recovery and this is in lieu of the current process where they have general rate cases every few years. ***Sometimes they settle them***, sometimes they hire lots of lawyers and spend lots of money and take a lot of time and you read a lot about it in the newspaper and they have very contentious issues. ***Basically what they are wanting to do in this [bill] is to have more of an annual review*** and rather than have those big rate cases . . . hopefully we will have less of them . . .

March 6, 2013, House Business and Utilities Sub Committee, Statement of Gerald McCormick (attached) (emphasis added). Similarly, the Advocate's witness acknowledged that recent rate cases had been settled, including specifically Atmos Energy's most recent rate case, and yet did not suggest that this might disqualify those companies from the new annual rate review mechanism under the terms of the bill. *Id.,* Statement of Vance Broemel ("I know there have been some concerns about some rate cases, expense. We agree that can be a problem. . . . I would point out that we have had three major cases with TN American Water and Atmos and Piedmont in the last few years. We have settled them; there were no hearings."). Mr. Broemel later acknowledged: "the intent of the bill is to avoid or not have rate cases . . ." *Id.*

Chairman Allison's testimony reflected what seemed to be a uniform expectation that the annual review mechanism would, in fact, be utilized: "we're going to be tracking their costs on a

much more frequent basis than we do now, through the annual rate review. If they've opted into that system." April 2, 2013 Senate Finance, Ways and Means, Statement of TRA Chairman James M. Allison.

There was never any suggestion that this new mechanism would be unavailable to those utilities who had resolved their most recent rate cases through an approved settlement with the Advocate. And there certainly was no suggestion that the annual rate review mechanism would require utilities first to file and fully litigate an all-issues rate case. Indeed, the overriding purpose of the legislation was to *reduce* the need for traditional rate case litigation.

**B. Contrary to legislative intent, the Advocate's position would exclude most – if not all – utilities from participation in the (d)(6) annual review mechanism, because most rate cases are resolved by settlement.**

A fully-litigated rate case is rare indeed. Most, if not all, rate cases in recent years have been resolved in whole or in part through an agreed stipulation or a comprehensive settlement between the utility and the Consumer Advocate. Indeed, in testimony before the Senate Finance Committee, the Consumer Advocate touted its recent success "in settling [rate] cases without any undue expense in recent years." April 2, 2013 Senate Finance, Ways and Means, Testimony of Vance Broemel. And those settlements usually – if not always – have the same kind of exculpatory language that the Advocate now contends disqualify them from participation in the (d)(6) annual review mechanism. By way of example:

- Piedmont Natural Gas, Docket No. 11-00144 was resolved by Stipulation and Settlement Agreement Between Piedmont Natural Gas Company, Inc. and the Consumer Advocate and Protection Division (December 21, 2011). Settlement Agreement expressly provides: "None of the signatories hereto shall be deemed to have acquiesced in any ratemaking or procedural principle, including without limitation, any cost of service determination or cost allocation or revenue related methodology and neither Party waives its right to take positions with respect to the matters settled herein in future proceedings before the Authority." Agreement at 7.

- Tennessee American Water, Docket No. 12-00049 was resolved by Stipulation and Settlement Agreement between TAWC and the Consumer Advocate and Protection Division, the City of Chattanooga, the Chattanooga Regional Manufacturers Association, Walden's Ridge Utility District, and the Town of Signal Mountain (October 1, 2012). The Agreement contained the same boilerplate as Piedmont's: "None of the signatories hereto shall be deemed to have acquiesced in any ratemaking or procedural principle, including without limitation, any cost of service determination or cost allocation or revenue-related methodology and neither Party waives its right to take positions with respect to the matters settled herein in future proceedings before the Authority." Agreement at 5-6.

- Atmos Energy Corporation, Docket No. 08-00197 was resolved by Settlement Agreement between Atmos and the Consumer Advocate and Protection Division (March 5, 2009). The Settlement Agreement contains the same boilerplate as the others: "None of the signatories to this Settlement Agreement shall be deemed to have acquiesced in any ratemaking or procedural principle, including without limitation, any cost of service determination or cost allocation or revenue-related methodology."

The Advocate protests that it does not mean to exclude every utility that settled its recent rate case from the (d)(6) annual mechanism. Advocate Mem. At 13. But whether they acknowledge it or not, that would be the effect of their position here, because settlements with the Advocate usually – if not always – include the same type of exculpatory language the Advocate relies upon here. At bottom, however, all rate-case settlement agreements have one thing in common. That is, they do *resolve* the case and result in a final order of the Authority approving a set of rates. In the case of the Atmos Energy settlement at issue here, moreover, the Agreement and Final Order also approved a set of agreed schedules setting forth the basis for the new rates, and as discussed below those same agreed and approved schedules form the basis of the Atmos Energy filing in this docket.

Settlement of any litigation, including rate case litigation, should be encouraged. Litigation is at best a necessary evil. As the 2013 Legislation's Senate sponsor explained, rate case litigation was viewed as "litigious and lengthy and costly." Avoiding the time and expense

of a rate case trial is a good thing. Indeed, in its testimony concerning the 2013 legislation, the Consumer Advocate touted: "we've been very successful in settling [rate] cases." April 2, 2013 Senate Finance, Ways and Means, Testimony of Vance Broemel (attached). When the parties can resolve a case by agreement, they should not be punished for it. But if the Advocate's position is accepted that is exactly what will happen.

Settlements should be encouraged, not punished. Indeed, the Tennessee Administrative Procedures Act explicitly encourages the resolution of contested cases through settlement: "Except to the extent precluded by another provision of law, ***informal settlement of matters that may make unnecessary more elaborate proceedings under this chapter is encouraged.***" Tenn. Code Ann. § 4-5-105 (emphasis added).

Utilities who worked cooperatively and flexibly in conjunction with the Advocate to resolve their rate cases short of a full blown rate case hearing should be rewarded. Through their efforts they have reduced the burden of rate case litigation. But the Advocate's position instead would punish these utilities for working with the Advocate and resolving their cases through settlement, by making them ineligible to participate in a key provision of the new statute.

### C. The Advocate's position would defeat the Statute's fundamental purpose by requiring that utilities engage in a fully litigated rate case and seek a litigated ruling on every issue.

The Advocate's position would force utilities to file new rate cases, and not only that, to litigate every issue to conclusion, insisting on an order expressly "adopting" a "methodology" on every cell of every spreadsheet. That becomes apparent upon examination of the situation presented here. As discussed below, the Authority's Order Approving Settlement Agreement in Atmos Energy's most recent rate case (Docket 12-00064) "approved, adopted, and incorporated" the Stipulation and Settlement Agreement between the Advocate and Atmos Energy. That

Agreement settled upon a series of 14 schedules that were attached to the Agreement as Attachment A. Fundamentally then, in approving, adopting and incorporating by reference the Atmos Energy / Advocate settlement, the Authority at a minimum "adopted" the "methodology" reflected in the 14 schedules of Attachment A. If that is not sufficient, then it would appear that the only course for a utility would be to file a rate case and not to resolve any part of it – to litigate every issue to the bitter end. That is the necessary result of the Advocate's position here that subsection (d)(6)(A) requires a litigated decision from the Authority specifically considering and "adopting" a given "methodology" on every issue and formula used to calculate a utility's rates. The only way to obtain such an order on every issue is to litigate every question. And beyond taking a rate case to trial, the Advocate's position would require the utility to litigate and insist upon a ruling as to every subsidiary question, or risk facing the argument that in seeking annual review of its rates, the Authority had not "adopted" a "methodology" as to any given point.

The 2013 Legislation was enacted to ***reduce***, not encourage, rate case litigation. The Advocate's position would do exactly the opposite. And the majority of utilities, who fostered cooperation and resolved their rate cases without a resource-intensive hearing, would be punished for doing so.

## II. The Advocate's Position is Wrong as a Matter of Statutory Construction and Legal Analysis

The Advocate fundamentally misinterprets subsection (d)(6), myopically focusing on a few words read out of context, and ignoring others altogether. The Advocate also errs in its interpretation of the Atmos Energy / Advocate Settlement Agreement and the Authority's Order approving, adopting, and incorporating that Agreement by reference.

### A. Subsection (d)(6)(A) does not require an Authority Order approving a specific "methodology."

The Consumer Advocate commits a fundamental error of statutory construction when it isolates a few words in Tenn. Code Ann. 65-5-103 subsection (d)(6)(A) and reads them out of context. Proper statutory construction requires that one read and apply the statute as a coherent whole. *See, e.g., Lee Med., Inc. v. Beecher*, 312 S.W.3d 515, 527 (Tenn. 2010). Statutory interpretation should not be based "on a single sentence, phrase, or word, but should instead endeavor to give effect to every clause, phrase, or word in the statute" with the goal being "to construe a statute in a way that avoids conflict and facilitates the harmonious operation of the law." *Id.* "It is well established that courts are to construe a statute as a whole and read them in conjunction with their surrounding parts, and view them consistently with the legislative purpose." *E. Tennessee Grading, Inc. v. Bank of Am., N.A.*, 338 S.W.3d 506, 513-14 (Tenn. Ct. App. 2010) (*citing Kradel v. Piper Indus., Inc.*, 60 S.W.3d 744, 750 (Tenn.2001)). As one court explained:

> Impressive authorities have warned judges that they must ascertain meaning from more than the actual language of a statute. Cardozo wrote that "[w]hen things are called by the same name it is easy for the mind to slide into an assumption that the verbal identity is accompanied in all its sequences by identity of meaning." *Lowden v. Northwestern National Bank & Trust Co.*, 298 U.S. 160, 165, 56 S.Ct. 696, 699, 80 L.Ed. 1114 (1936). Holmes told us: "A word is not a crystal, transparent and unchanged, it is the skin of a living thought and may vary greatly in color and content according to the circumstances and the time in which it is used." *Towne v. Eisner*, 245 U.S. 418, 425, 38 S.Ct. 158, 159, 62 L.Ed. 372 (1918). Learned Hand said, "it is one of the surest indexes of a mature and developed jurisprudence not to make a fortress out of the dictionary; but to remember that statutes always have some purpose or object to accomplish, whose sympathetic and imaginative discovery is the surest guide to their meaning." *Cabell v. Markham*, 148 F.2d 737, 739 (2d Cir.), aff'd, 326 U.S. 404, 66 S.Ct. 193, 90 L.Ed. 165 (1945).
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> Ascertaining the legislative intent behind the words of a statute is a task somewhat akin to pinpointing the intent of a testator or the intent of disputing parties to a contract. Proper judicial construction, in the modern view, requires recognition and implementation of the underlying legislative purpose, *Train v. Colorado Pub. Interest Research Group, Inc.*, 426 U.S. 1, 9–10, 96 S.Ct. 1938, 1942, 48 L.Ed.2d 434 (1976), and

> the judge, the theory holds, must accommodate the societal claims and demands reflected in that purpose. To accomplish this task, as Justice Roger J. Traynor put it, we need "literate, not literal" judges, lest a court make a construction within the statute's letter, but beyond its intent. Traynor, Reasoning in a Circle of Law, 56 Va.L.Rev. 739, 749 (1970).

*Bevill, Bresler & Schulman Asset Mgmt. Corp. v. Spencer Sav. & Loan Ass'n*, 878 F.2d 742, 750-51 (3d Cir. 1989).

Reading the statute as a whole, several key points become apparent. First, the Legislature said so explicitly when it meant to require Authority ***approval***. At three places within the statute, the Legislature expressly referred to rates of return "***approved*** by the authority at the public utility's most recent general rate case." *See* Tenn. Code Ann. §§ 65-5-103(d)(2)(B), (d)(3)(B), (d)(5)(C) (emphasis added). Under the accepted canon of statutory construction '*expressio unius est exclusio alterius*,' "the expression of one thing implies the exclusion of others." *Rich v. Tennessee Bd. of Med. Examiners*, 350 S.W.3d 919, 927 (Tenn. 2011). This doctrine recognizes that having addressed the matter specifically elsewhere, if the legislature had intended to require specific authority approval, "it would have included specific language to that effect." *Id.* If subsection (d)(6)(A) were meant to require Authority approval of a specific methodology, as the Advocate contends, then it must be presumed that the Legislature would have used the same terminology it had used elsewhere in the statute – that it would have said "approved by the authority" if it had meant "approved by the authority," as the Advocate now contends.

Second, subsection (d)(6)(A) must be read as a whole: "A public utility may opt to file for an annual review of its rates based upon the methodology adopted in its most recent rate case pursuant to § 65-5-101 and subsection (a), if applicable." The subject of this sentence is a "public utility," which "may opt" for annual review of its rates "based upon the methodology adopted in its most recent rate case." Recognizing that this subsection does not refer to matters

"approved by the authority," as the statute does elsewhere, it is reasonable to read this sentence as a whole as to include the methodology adopted by the public utility in its most recent general rate case. Consistent with this interpretation, the sentence refers generally to the methodology "adopted in" the most recent rate case. It does not make reference to the final order in the case. It does not require that the case have been resolved through litigation rather than settlement. And it certainly does not seek to require any specific form of final order as a prerequisite to the public utility's right to "opt" for annual review of its rates. Read reasonably and in context, the language of section (d)(6)(A) was written to be flexible enough to encompass rates established in settled rate cases as well as litigated ones, and without specifically requiring strict application of detailed formulas explicitly "approved by the authority."

Third, to make this point even more clear, subsection (d)(6)(A) concludes with the qualifier "***if applicable***." Words have meaning and statutory phrases cannot simply be ignored. Rather than simply ignoring this qualifier, as the Advocate has done, the Authority should "endeavor to give effect to every clause, phrase, or word in the statute." *Lee Med., Inc. v. Beecher*, 312 S.W.3d 515, 527 (Tenn. 2010). This qualifier – "if applicable" – could only have been intended to stress that the preceding phrase "methodology adopted in its most recent rate case" was not intended to operate as a strict prerequisite or precondition to application of the annual rate review mechanism. To the contrary, it conveys that the mechanism is available whether or not – or regardless of the degree to which – a "methodology" was "adopted" in the most recent rate case.

### B. Subsection (d)(6)(B) expressly ties eligibility for the annual rate mechanism to having "engaged in" a general rate case within the last five years.

In reading the statute as a whole, one must also read subsection (B), the paragraph where the Legislature expressly defined the only prerequisite to a utility's right to opt-into annual rate

review. That is, a utility must have "engaged in a general rate case" within the past five years. And by the express terms of subsection (B), even that lone prerequisite may be waived or extended by the Authority.

After introducing the statutory annual review mechanism in subsection (A), the Legislature then devoted subsection (B) to defining eligibility for the mechanism, before turning in (C) to the timetable and standard for how rates are to be adjusted each year, and in (D) to how an annual review mechanism can be modified or terminated. Subsection (B) defines eligibility for the annual review mechanism as follows:

> In order for a public utility ***to be eligible*** to make an election ***to opt into an annual rate review***, the public utility must have ***engaged in a general rate ca***se pursuant to § 65-5-101 and subsection (a) ***within the last five (5) years***; provided, however, that ***the authority may waive such requirement*** or increase the eligibility period upon a finding that doing such would be in the public interest.

Tenn. Code Ann. § 65-5-103(d)(6)(B) (emphasis added). In construing a statute, the specific controls over the general. *See, e.g., Wright v. Tennessee Peace Officer Standards & Training Comm'n*, 277 S.W.3d 1, 16 (Tenn. Ct. App. 2008). The Legislature's inclusion of a specific subsection defining the requisites for a public utility "to be eligible" to "opt into an annual rate review" therefore adds to the conclusion that the more general language of subsection (A) should not be read to impose additional eligibility prerequisites, as the Advocate contends.

Eligibility to "opt into" an annual rate review is expressly defined by whether the utility has "engaged in" a general rate case within the last five years. Eligibility does not require that the rate case have been resolved by an order specifically approving a set of rate-setting formulas, as the Advocate now contends. No specific form of order is required. Eligibility does not require a litigated resolution, or exclude resolution of the case by stipulation or settlement. Indeed, the section is drafted so as to be independent of how the rate case was resolved. What is

required is simply that the utility have "engaged in" a general rate case within the past five years. It is beyond dispute that Atmos Energy "engaged in" a general rate case in Docket No. 12-00064, less than five years ago.[1] It is, therefore, "***eligible*** to make an election to ***opt into*** an annual rate review" under the express terms of the statute.

Making it even clearer that the drafters viewed subsection (B) as controlling eligibility to opt into an annual rate review, they included an escape clause expressly providing the Authority with discretion to "waive" the eligibility "requirement" of having "engaged in a rate case" within the last five years. The Authority was, alternatively, authorized to "increase the eligibility period" beyond five years. In subsection (B), the Legislature granted the Authority ultimate power and discretion to extend eligibility "upon a finding that doing such would be in the public interest." Including this discretion to control "eligibility" within subsection (B) would not have made sense if the Legislature had believed, as the Advocate contends, that eligibility was independently controlled by the "methodology adopted" language of subsection (A).

[1] Indeed, Atmos Energy also "engaged in" a general rate case under Docket No. 08-00197, which was finally resolved by an Order Approving Settlement Agreement dated April 7, 2009. That Order did not include the specific phrase the Advocate relies upon here as, depending upon how it is viewed, either the bedrock foundation of its argument, or the fig leaf hiding the reality that the Advocate's position would exclude from the annual rate mechanism any utility whose most recent rate case was resolved in whole or in part by settlement or stipulation – which as discussed above is virtually every rate case in recent years. If the Advocate's position concerning the 12-00064 Atmos docket were accepted, and that case were disqualified by the specific language in the Authority's final order, the statute would authorize the Authority to waive the five year requirement or increase the eligibility period and instead utilize the final order in Docket No. 08-00197 as the basis for the Company's annual rate review. Of course, this result would be far less satisfactory than simply utilizing the Company's most recent rate case as a reasonable interpretation of the statute clearly requires.

**C. In approving Atmos Energy's settlement of its most recent rate case, the Authority "approved, adopted, and incorporated in its order" the Settlement Agreement, including all of its agreed schedules, and in so doing "adopted" the "methodology" agreed to in the Settlement.**

It is important to consider what the Authority's Order approving the Atmos Energy / Advocate settlement of Docket 12-00064 actually said and did. The Order reviewed *and approved* the terms of the settlement agreement, finding they were "within the zone of reasonableness" and promoted the public interest by "balancing the interests of the utility consumers and the provider." Order at 4. The Order rejected a specific provision the Settlement Agreement calling on Atmos Energy to offset the Advocate's accounting witness fees. Order at 5. Having otherwise approved the settlement terms as within the zone of reasonableness and promoting the public interest, the Order then stated: "In addition, the panel found that, in accepting the *Stipulation and Settlement Agreement*, the Authority was not adopting any specific means, models or methodologies ***used to calculate the resulting agreed-upon terms***." Order at 4 (emphasis added). Following these preliminary statements, the Order then proceeded to state specifically what the Authority was Ordering, and included this ordering language:

> The *Stipulation and Settlement Agreement*, a copy of which is attached to this Order as Exhibit A, and as amended by the deletion of the $20,000 accounting witness fee provision I Paragraph 11d agreed to by the Parties, ***is approved, adopted, and incorporated in this Order as if fully rewritten herein***.

Order at 5 (emphasis added). The Settlement Agreement, having been "approved, adopted and incorporated in [the] Order as if fully rewritten" therein, in turn included an agreed set of schedules defining how the agreed-upon rates would be calculated. The Agreement provided in relevant part: "The Parties agree that the Company's attrition period cost of service should include the components set forth ***on Attachment A hereto, which the Parties agree are fair and reasonable to the Company and its customers*** for the limited purpose of settling this docket . . ."

Settlement Agreement para. 9 (emphasis added). Attachment A to the Agreement consisted of a set of 14 schedules setting-forth the parties' agreed calculations of the Company's costs of service. And it is this agreed and approved "methodology" that Atmos Energy has used to model its filing in this docket.

Stepping back to read the whole Order, therefore, the premise for the Advocate's argument here evaporates. The ordering paragraph of the Order approves, adopts and incorporates by reference the Settlement Agreement, which in turn includes an agreed set of schedules used to calculate the Company's costs of service and resulting rates. This point bears emphasis, and should alone be dispositive. The fundamental premise for the Advocate's position here is simply incorrect. The Order approving the Atmos Energy / Advocate settlement did, in fact, adopt and approve the settlement, and in the process approved the schedules the parties had agreed were a "fair and reasonable" statement of the company's costs of service and resulting rates. There are, in fact, approved rate-making methodologies underlying those schedules. By analyzing the case record in conjunction with the schedules, it is possible to ascertain how the inputs into the schedules were derived, as summarized below in Section V. Those methodologies are embodied in the approved Settlement Agreement and attached schedules, the same way that a "methodology" would be embodied in any other rate case resolved by settlement.

A critical fact bears emphasis: the Settlement Agreement did in fact ***resolve*** the rate case and that resolution was approved by a final order of the Authority. At bottom, the Advocate's position ignores this dispositive reality.

The Order approving the Atmos Energy / Advocate Settlement Agreement is in legal effect a consent order or consent decree. *See, e.g., Third Nat. Bank v. Scribner,* 212 Tenn. 400,

404-05, 370 S.W.2d 482, 484 (1963) (order considered and approved settlement between the parties and, as in this case, "then adjudged that the agreement was ratified and approved and made the order of the court"); *Bacardi v. Tennessee Bd. of Registration in Podiatry*, 124 S.W.3d 553 (Tenn. Ct. App. 2003) (consent order of Board of Registry in Podiatry incorporating podiatrist's voluntary relinquishment of his right to reactivate or reapply for his state license was valid and binding, and noting that 4-5-105 encourages settlement of administrative proceedings). "It is well settled in Tennessee that consent orders are valid and binding." *Bacardi*, 124 S.W.3d at 562. "A consent decree is so binding as to be ***absolutely conclusive upon the consenting parties.***" *Third Nat. Bank*, 212 Tenn. at 409, 370 S.W.2d at 486 (emphasis added). "While a consent judgment and a judgment on the merits are distinguishable, for enforcement purposes they stand on a parity. ***A consent judgment acquires the incidents of, and will be given the same force and effect as, judgments rendered after litigation.***" *Id.* (emphasis added, internal quotations omitted). As the Tennessee Supreme Court has explained: "The conclusiveness of *res judicata* effect of a consent judgment applies even though the court rendering the consent decree has not ascertained the truth of the facts averred, and has not exercised its mind and passed on the matters in controversy, and even though the judgment is erroneous. The fact that without the consent of the parties the court might not have rendered the judgment does not affect its effect as *res judicata*." *Id.*

Fundamentally then, the Order approving the Atmos Energy / Advocate settlement of Docket 12-00064 "approved, adopted, and incorporated" the Settlement Agreement in the Order "as if fully rewritten herein." In legal effect, the Settlement Agreement became the Order of the Authority. And that Agreement included an agreed set of 14 schedules setting-forth the determination of Atmos Energy's cost of service and the determination of its rates. The Order is

legally binding to the same extent as a judgment rendered after litigation. It is conclusive and binding even if it could be said that the Authority might not have reached all of the same conclusions if the matter had been fully litigated and there had been no settlement.

### D. The Advocate confuses *stare decisis* (precedent) with *res judicata* (the binding effect of a consent order), and therefore misreads the Atmos Energy/Advocate Settlement Agreement.

The Advocate's Settlement Agreement with Atmos Energy states in several places that it shall not be cited as ***binding precedent*** in future cases. But the Settlement Agreement is not being used here as ***precedent***, which decides the same legal question in the same way in a second action between ***strangers*** to the first action under the doctrine of *stare decisis*. The doctrine at play here is *res judicata*, or simply the recognition, as discussed above, that the Settlement Agreement did in fact reach a final resolution of the Atmos Energy rate case in Docket No. 12-00064, was approved by the Authority, and has binding effect as a consent order.

The language of the Settlement Agreement distinguishes between citation of the Agreement as ***precedent*** in a future case and use of the Agreement to enforce the final resolution of the rate case between the parties. The Agreement provided specifically: "This Settlement Agreement shall not have any precedential effect in any future proceeding or be binding on any of the Parties in this or any other jurisdiction ***except to the limited extent necessary to implement the provisions hereof.***" Agreement at 6 (emphasis added). Fundamentally, the Agreement resolved the Atmos rate case, set rates, and agreed to the schedules that now form the basis for Atmos Energy's application in this docket. In this case, Atmos simply seeks to enforce or "implement" the terms of the approved Settlement Agreement.

This clause and the others relied upon by the Advocate were meant to prevent the argument that the settlement established ***precedent***, not to render the Agreement unenforceable

or non-binding. The legal term "precedent" invokes the doctrine of *stare decisis*, which is definied as "[t]he doctrine of precedent . . ." Black's Law Dictionary (8th Ed). The Tennessee Supreme Court explained the important distinction between precedent (*stare decisis)* and judgment finality (*res judicata)*:

> *Res judicata* relates to the conclusiveness of prior judicial findings or adjudications, whereas *stare decisis* relates to the binding effect of the legal principles involved; and *res judicata* binds parties and privies, whereas *stare decisis* governs the decision of the same question in the same way in an action between strangers to the record.
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> The doctrine of *stare decisis* relates to legal principles, not to facts. At common law the only thing in a decision binding as authority under the rule of *stare decisis* is the right principle upon which the case was decided—*ratio decidendi*—and not the application of such principle.

*Union Trust Co. v. Williamson Cnty. Bd. of Zoning Appeals*, 500 S.W.2d 608, 615 (Tenn. 1973). "*Res judicata* is based on the conclusiveness of prior judicial findings on the parties, while *stare decisis* relates to the binding effect of the legal principles, including on strangers to that litigation." 21 C.J.S. Courts § 195.

What we have here is not an application of precedent, or *stare decisis*. The Agreement is not being used as *precedent* by another utility arguing that the Atmos Energy/Advocate settlement established a generally applicable legal principle. It is instead a simple application of finality, or *res judicata*. The Atmos Energy Settlement Agreement was a final and binding resolution of the most recent Atmos Energy rate case. In legal effect, it was a consent order, which as discussed above has the same binding effect on the parties as a judgment reached after a fully litigated hearing.

## III. In applying the same new statute, the Advocate has consented to and the Authority has allowed the use of methodologies adopted by stipulation in a prior rate case.

Piedmont Natural Gas recently filed and received Authority approval for an annual infrastructure mechanism under another subsection of the same 2013 statute at issue here. In the Piedmont case, the Authority approved a resolution under which both the Advocate and Piedmont Natural Gas agreed "to use the ***methodologies approved in the most recent rate case*** for accumulated depreciation, depreciation expense, property taxes, pre-tax return and uncollectibles gross-up factor." Stipulation of Piedmont Natural Gas Company [and the Consumer Advocate], Docket No. 13-00118 (November 27, 2013) (emphasis added). *See also* Order Granting Petition, Docket No. 13-00118 (May 13, 2014). Piedmont Natural Gas occupied the same position as Atmos Energy, in that both companies' most recent rate cases were resolved by way of a settlement agreement. *See* Order Approving Settlement Agreement, Docket No. 11-00144 (December 21, 2011). When asked to clarify the approved methodologies that would be utilized for its mechanism, Piedmont explicitly referenced the settlement schedules from its rate case settlement agreement as the source of the methodologies. *See* Piedmont's Response to Date Request, Docket No. 13-00118 (December 12, 2013). The Advocate agreed with and adopted Piedmont's response. *See* CAD's Data Response to the TRA, Docket No. 13-00118 (December 12, 2013). Similar to Atmos Energy, the Piedmont rate case settlement included a provision explicitly stating: "***None of the signatories hereto shall be deemed to have acquiesced in any ratemaking or procedural principle***, including without limitation, any cost of service determination ***or cost allocation or revenue related methodology*** and neither Party waives its right to take positions with respect to the matters settled herein in future proceedings before the Authority." Stipulation and Settlement Agreement Between Piedmont Natural Gas Company, Inc. and the Consumer Advocate and Protection Division, Docket No. 11-00144 at 7

(emphasis added). In addition, the settlement contained the language that "[t]his Stipulation and Settlement Agreement shall not have precedential effect in any future proceeding or be binding on any Party except to the limited extent necessary to implement the provisions hereof." *Id.* At 9. And, just like the Authority's Order approving the Atmos Energy settlement, the operative ordering paragraph of the Authority's Order approving the Piedmont settlement ordered the settlement agreement "approved and accepted and is incorporated into this Order as if fully rewritten herein." Order Approving Settlement Agreement, Docket No. 11-00144, at 7.

If the Consumer Advocate's position here had been accepted in the Piedmont matter, there could not have been any "methodologies approved in the most recent rate case." Piedmont's rate case was resolved by a settlement agreement, not by litigation in which the Authority separately considered and ruled upon the merits of specific "methodologies." And the Piedmont settlement agreement – as do most, if not all, Advocate settlements – included the same type of exculpatory language the Advocate relies on here. Like the Atmos Energy case, the Piedmont settlement was approved by an Order that adopted and incorporated by reference the settlement agreement as part of the Authority's Order. If there was a "methodology approved" in resolving the most recent Piedmont rate case, then equally there was a "methodology adopted" in resolving the most recent Atmos Energy rate case. As discussed above, that is certainly the right answer. As a legal matter, the Authority's order approving and incorporating by reference the settlement agreement was a binding consent order, which has the same conclusive effect as a litigated judgment whether or not the Authority "exercised its mind and passed on" every methodological issue, and even though "without the consent of the parties the [Authority] might not have rendered the [same] judgment." *Third Nat. Bank, supra,* 212 Tenn. at 409, 370 S.W.2d at 486. And as a matter of policy and reality, if the only rate case proceedings that can qualify as

benchmarks for application of the new alternative ratemaking mechanisms are those rate cases that have been resolved through full litigation, without settlement or stipulation, then very few will qualify. And the new statute will not be allowed to operate as intended.

## IV. The statute requires the Authority to exercise its ratemaking discretion in adjusting the utility's tariff rates to provide it the opportunity to earn its authorized return on equity.

The Advocate's myopic focus on the "methodology adopted" language of subsection (d)(6)(A) begs the obvious question, what is a methodology? A "methodology" is not a formula or an algorithm. It is broader than that. Methodology has been defined as: "the processes, techniques or approaches employed in the solution of a problem or in doing something." Webster's Third New International Dictionary of the English Language Unabridged (1986). At least one definition goes further by clarifying that a methodology is "A system of broad principles or rules from which specific methods or procedures may be derived to interpret or solve different problems within the scope of a particular discipline. ***Unlike an algorithm, a methodology is not a formula but a set of practices.***"[2]

And to pose the question more precisely, at what level of abstraction does one determine the "methodology adopted"? At one level, the methodology adopted in the most recent Atmos Energy rate case, and in every other recent Tennessee case, utilized a forward looking test year modeled upon projected revenues, costs of service, and rate base. At a more detailed level, the approved Settlement Agreement established a set of 14 schedules setting forth the agreed basis for the rates being adopted. In any case, however, at some level of particularity there will of necessity be matters that the Authority must resolve in any case in order to set rates. The (d)(6) annual rate review mechanism ultimately requires the Authority to "make adjustments" to the

[2] See http://www.businessdictionary.com/definition/methodology.html (emphasis added).

utility's rates "to provide that the public utility earns the authorized return on equity established in the public utility's most recent general rate case . . ." Tenn. Code Ann. § 65-5-103(d)(6)(C). And at some level, that of necessity will require the Authority to exercise its inherent ratemaking judgment to set rates that in its view are reasonably expected to achieve the mandated return on equity.

The "establishment of just and reasonable rates is a value judgment to be made by the [Authority] in the exercise of its sound regulatory judgment and discretion." *Powell Tel. Co. v. Tennessee Pub. Serv. Comm'n*, 660 S.W.2d 44, 46 (Tenn. 1983) (quoting *CF Indus. v. Tennessee Pub. Serv. Comm'n,* 599 S.W.2d 536, 542 (Tenn.1980)). The Authority generally is afforded broad discretion in ratemaking decisions, and courts play a "limited role" in reviewing its actions. *CF Industries,* 599 S.W.2d at 542 (citing *Southern Bell Telephone & Telegraph Co. v. Tennessee Public Service Com'n.,* 304 S.W.2d 640 (1957)). The Authority may utilize its "experience, technical competence, and specialized knowledge" and at bottom is charged with determining what is "just and reasonable":

> Thus, the Public Service Commission in rate making and design cases is not solely governed by the proof although, of course, there must be an adequate evidentiary predicate. The Commission, however, is not hamstrung by the naked record. It may consider all relevant circumstances shown by the record, all recognized technical and scientific facts pertinent to the issue under consideration and may superimpose upon the entire transaction its own expertise, technical competence and specialized knowledge. Thus focusing upon the issues, the Commission decides that which is just and reasonable. This is the litmus test nothing more, nothing less.

*Id. at 543.*

"[R]ates are set for the future and [] the estimated effect of reasonably expected increases in expenses and investment should be taken into consideration in the establishment of a rate structure." *Am. Ass'n of Retired Persons v. Tennessee Pub. Serv. Comm'n*, 896 S.W.2d 127, 133

(Tenn. Ct. App. 1994) (citing *South Central Bell Telephone Co. v. Tennessee Public Service Commission,* 579 S.W.2d 429 (Tenn.App.1979); *Tennessee Cable TV v. PSC,* 844 S.W.2d 151 (Tenn.App.1992)).

At bottom, the (d)(6) annual review mechanism calls on the Authority to exercise its inherent ratemaking discretion to set rates so as to achieve a previously-determined return on equity. This exercise of discretion is both proper and inevitable. Setting rates is not a mechanical exercise. The upshot of the Advocate's position here is that the (d)(6) mechanism would be available only if the previous rate case had approved something akin to a fixed set of formulas from which rates could be calculated mechanically. Of course, that has rarely if ever occurred. The Legislature enacted the (d)(6) mechanism so that it could be used. Adopting the Advocate's position would make that practically impossible.

## V. Atmos Energy has in good faith modeled its filing in this case upon the methodology adopted in the Company's most recent Tennessee rate case.

At the most basic level, the methodology employed in Atmos Energy's Tennessee rate cases has always used a forward looking test year (or "attrition year"). The primary data source for the Company's forward looking test year for both investment (rate base) and operating expenses – in this case and in past cases – has utilized the Company's most recently completed operating budget. *See, e.g.,* Atmos Response to Staff Data Request No. 1. As explained in the testimony of Gregory Waller, that method, utilizing the Company's actual, vetted operating budget to forecast operating expenses for the forward-looking attrition period has been used consistently in the Company's Tennessee rate cases and has worked well.

As in previous cases, including Docket No. 12-00064, the Company's filing in this case relies on its most recently completed budget to the extent it was available at the time the filing was prepared. For months in the forward looking test year for which no budget had yet been

completed, the Company relies on forecast methodologies consistent with those used in Docket No. 12-00064. The Company allocates costs from the same Division General Office and Shared Services entities as it has for years. The allocation percentages are calculated the same way they were in Docket No. 12-00064. For rate base and operating expenses, the Company presents a Base Period which is made up of actual per books data for the purpose of comparison to its forward looking test year.

The Schedules attached to the Company's petition, as well as the calculations, data sources and methodologies contained within and underlying them, are consistent with those in Docket No. 12-00064. Schedules 1-10 are consistent in format, sources, and underlying methodologies with Schedules 1-10 that were attached to the testimony of Company witness Thomas Petersen in Docket No. 12-00064. Schedule 11 is consistent with Exhibits 1-5 attached to the testimony of Company witness Joshua Densman in Docket No. 12-00064. Some of the work papers supporting Schedules 1-10 were included as exhibits or work papers of other witnesses in Docket No. 12-00064 or developed for this proposal to ensure that the resulting revenue requirement calculations are consistent with the methodologies adopted in Docket No. 12-00064.

Each component of O&M has been built in the same way as it was in Docket No. 12-00064. The development and application of inflation factors is consistent with the methodologies used in Docket No. 12-00064. In this filing they are only needed for the last three months of the Forward Looking Test Year because the Company has a recently completed budget covering all but the final three months of the Forward Looking Test Year. The selection of the June ending Historic Base Period and September 1 Annual Filing Date ensures that the first nine months of the Forward Looking Test Year can rely on the Company's recently

completed budget without the need to forecast using inflation factors. Pension expense is handled per the Stipulation and Settlement Agreement in Docket No. 12-00064, where the methodology is specified on page 4. The required treatment of pension costs affects O&M, depreciation and amortization expense, and rate base. One other O&M adjustment is made in recognition of the fact that the Final Order in Docket No. 12-00064 approves and incorporates by reference a settlement among the parties. In the settlement, the parties agreed to a specific level of O&M expense. Accordingly, in order to remain true to the outcome of Docket No. 12-00064, the Company, in this and subsequent annual filings, has and will model the level of O&M in the Forward Looking Test Year to include the reduction to O&M that was agreed upon in the parties' settlement and approved and incorporated by reference in the Authority's Final Order. Because the Company's Forward Looking Test Year O&M is forecasted in the same manner that it was in Docket No 12-00064 and prior cases, it is a valid starting point from which to apply the approved settlement.

Atmos Energy has used the most recently approved depreciation rates to calculate depreciation expense and accumulated depreciation. The Company made the various adjustments related to intercompany leased storage assets and intercompany leased operational work centers that have been required of the Company in each of its rate cases subsequent to the purchase by United Cities Gas Company of Barnsley storage in 1989 (and including Docket No 12-00064). These adjustments affect cost of gas, O&M, depreciation expense, other taxes and rate base and have been made consistently since their inception.

Each component of rate base is calculated as it was in Docket No. 12-00064. The Final Order in Docket No. 12-00064 approves and incorporates by reference the Atmos Energy / Advocate Stipulation and Settlement Agreement. A review of Schedule 3 of the Settlement

Exhibit attached to the Final Order in Docket No. 12-00064 reveals only two components of rate base where the stipulated rate base differs from the Company's filed rate base. The first is cash working capital. The differences for cash working capital are "flow-through" differences, which means they result from other adjustments made throughout the filing to O&M and revenues. The other difference on Schedule 3 is a line labeled "Misc. Rate Base Adjustment - Settlement". The amount is $6,582,062. In order to remain true to the outcome of Docket No. 12-00064, the Company, in this and subsequent annual filings, has and will model the level of rate base in the Forward Looking Test Year to include the adjustment that was agreed upon in the parties' settlement and approved and incorporated by reference in the Authority's Final Order.

Consistent with Docket No. 12-00064, Capital structure is the Company's average capital structure over the last 3 years, as of the last day of the Historic Base Period. The costs of short term and long term debt are calculated consistently with those in Docket No. 12-00064. The 10.1% return on equity is the ROE specified in the Final Order of Docket No. 12-00064.

Forward looking billing determinants were developed using the methodology reflected in the Atmos Energy/Advocate settlement of Docket No. 12-00064, which was in fact the model employed by the Advocate's consultant. The same is true for customer growth adjustments, again using the Advocate's consultant's methodology, as reflected in the approved Stipulation and Settlement Agreement. Weather normalization was done using the same weather stations reflected in the Atmos Energy / Advocate settlement, and an updated 30 year normal was calculated through June 30 using the same methodology (used by both Atmos Energy and the Advocate's consultant) in Docket No. 12-00064.

At bottom, Atmos Energy has in good faith modeled its filing in this case on the resolution of Docket No. 12-00064. At the most basic level, it has used the same "methodology"

it has long used in Tennessee, a forward looking attrition period developed using the Company's approved and vetted budget for that period. Descending to a more specific level, the Company has faithfully modeled this filing upon the Stipulation and Settlement Agreement in Docket No. 12-00064, which was approved and incorporated by reference as an Order, and as a consent judgment has the same *res judicata* effect as a judgment reached after a full blown hearing. The Stipulation and Settlement Agreement does, in fact, specify specific agreed upon components of cost of service both within the body of its text and in the 14 schedules attached thereto. By analyzing the case record (testimony, discovery, exhibits, supporting workpapers, etc.) in conjunction with the text and schedules, it is possible to ascertain how the inputs into the 14 schedules were derived. It is then possible, in turn, to substantiate the Company's claim that it has in good faith constructed those inputs consistent with the methodologies used in Docket No. 12-00064.

## VI. Even if one were to adopt the Advocate's incorrect interpretation of subsection (b)(6), the Authority could (and should) approve the Company's proposed Annual Review Mechanism tariff under subsection (b)(7).

Even if one were to ignore all of the foregoing and assume, for the sake of argument only, all of the Advocate's arguments concerning section (b)(6), the Authority still would have the statutory power to implement an annual review mechanism as proposed by Atmos in this matter. That is true because subsections (d)(1) and (d)(7) of the statute expressly grant the Authority power to consider and implement other alternative regulatory methods, in addition to those specifically set-forth in subsections (2) through (6). Subsection (d)(1)(A) grants the Authority a general authorization "to implement alternative regulatory methods to allow for public utility rate reviews and cost recovery in lieu of a general rate case proceeding before the authority." Tenn. Code Ann. § 65-5-103(d)(1)(A). And subsection (7) specifically authorizes

the adoption of other alternative ratemaking mechanisms beyond the limits of sections (2) through (6):

> (7) ***In addition to the alternative regulatory methods described in this subsection (d)***, a public utility may opt to file for other alternative regulatory methods. Upon a filing by a public utility for an alternative method not prescribed, the authority is empowered to adopt policies or procedures, that would permit ***a more timely review and revisions of the rates***, tolls, fares, charges, schedules, classifications or rate structures of public utilities, and that would further ***streamline the regulatory process and reduce the cost and time associated with the ratemaking processes in § 65-5-101 and subsection (a).***

Tenn. Code Ann. § 65-5-103(d)(7) (emphasis added). The annual review mechanism tariff proposed by Atmos in this case certainly will promote "a more timely review and revision of [] rates" and will "streamline the regulatory process" and "reduce cost and time" as compared to traditional rate case litigation. These are the overriding goals of the statute as a whole, and specifically of this catchall provision. This provision clearly authorizes the Authority to grant the relief requested here, without regard to how one resolves the Advocate's incorrect arguments concerning subsection (d)(6).

## CONCLUSION

For these reasons, the Advocate's Motion should be denied.

Respectfully submitted,

**NEAL & HARWELL, PLC**

By: _____

A. Scott Ross, #15634
2000 One Nashville Place
150 Fourth Avenue, North
Nashville, TN 37219-2498
(615) 244-1713 – Telephone
(615) 726-0573 – Facsimile

*Counsel for Atmos Energy Corporation*

**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 1st day of October, 2014.

| | |
|---|---|
| ( ) Hand | Wayne Irvin, Esq. |
| ( ) Mail | Vance Broemel, Esq. |
| ( ) Fax | Consumer Advocate and Protection Division |
| ( ) Fed. Ex. | P. O. Box 20207 |
| (X) E-Mail | Nashville, TN 37202-0207 |

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**TENNESSEE GENERAL ASSEMBLY**

**House Business and Utilities Sub Committee, March 6, 2013**

**Chairman Pat Marsh:** House Bill No. 191 - Leader McCormick you are recognized…..

**Representative Gerald McCormick:** Thank you Mr. Chairman and I thought I would come up here because we will probably need to call on a couple of folks to come up here and give their opinions on the bill of course with the permission of the Committee. This is the TRA bill that's brought really jointly by the administration and the TRA and it does several things and if I could I will go over the basic outline of it and focus in on one section that I think we will have the most discussion on but I think this is the place to have the discussion. There are basically five sections that make changes. Section 1 would say that the TRA Directors are eligible for state employee health insurance benefits and those types of things, that was the original intention. This makes that more clear. The second section also clarifies that there is some actually some ambiguity relative to the conflict of interests prohibitions for the directors, this is going to make it easier and it just makes it clearer what they can and can't do and its clean up language. Section three talks about implementing optional cost based services at the request of the utilities and cover the cost for doing so, again that is not a huge change. Section 4 will realign the fee structure to basically reflect who is being regulated and let them pay the fees rather than have companies that are not being regulated any or not very much and reduce their fees, this will also result in a savings of a little over a million dollars a year in the budget which the TRA has worked very hard to make sure they can meet that and hopefully save rate payers over a million dollars a year in the process. Section 5 is the section that I'm sure our folks here will want to focus in on. What this does is it creates a new section authorizing the implementation of alternative regulatory methods for utility rate reviews and cost recovery and this is in lieu of the current process where they have general rate cases every few years. Sometime they settle them, sometimes they hire a lot of lawyers and spend lots of money and take a lot of time and you read a lot about it in the newspaper and they have very contentious issues. Basically what they are wanting to do in this is to have more of an annual review and rather than have those big rate cases now it won't keep us from having rate cases we can still have them, but hopefully we will have less of them and in my opinion I think a good way to say it is we are bringing in CPAs to review it more regularly and probably not using lawyers as much that have been rate review cases.

**Chairman Pat Marsh:** We have a motion on the bill, do I hear a second? We have a motion and second and we do have an amendment on it and you want to talk about it….?

**Representative Gerald McCormick:** I believe that is what I just explained what the advantages are…

**Chairman Pat Marsh:** Alright do we have a motion on the amendment – we have a motion and second on the amendment and we will ah. . . Anybody have any questions on the amendment? Representative Pody?

**Representative Mark Pody:** Yes, I've got one. Where it says it that will empower the TRA to make these rules, are these rules that have to come before Gov Ops? Who oversees the rules that they are making to make sure, who checks them?

**Representative Gerald McCormick:** I think all rules have to come through Gov Op at some point for review.

**Representative Mark Pody:** So . . . these rules will come .....?

**Representative Gerald McCormick:** Yes, yes, they will come through and I will let them, if that is not correct, they will get a chance in a second, that is correct, and Mr. Chairman I think it's only fair we have had some objections to the bill, especially for that last section from the Attorney General's office and with your permission, I would like to have them come up and state their case and then hopefully have the TRA directors come up and state theirs.

**Chairman Pat Marsh:** We will go ahead, do we have any more questions on the amendment? If not, I think we are going to go ahead and vote the amendment if, without objection we will go ahead and vote on the amendment. All in favor please say I, oppose and that is amendment number 3640. The amendment passes, now we are back on the bill and I think if it's ok with you Leader, we will go out of the recess and hear from whoever you want to bring up or however you want to work it, we want to hear from the Attorney General's office. Is there anybody here from the Attorney General's office? Would you all like to come up and ah, let us hear from you please? If you wouldn't mind stating your name and your position and then we will hear your testimony. Turn your microphone on please, Sir.

**Vance Broemel:** My name is Vance Broemel. I'm with the Consumer Advocacy Protection Division of the Office of the Attorney General and with me here today is Ryan McGehee who is also from the Consumer Advocate Protection Division and under the statute that created us we have the duty and authority to have cases at the Tennessee Regulatory Authority and also to participate in legislative and judicial proceedings and that's why we are here today, here on this House Bill 191 and in particular Section 5 as Leader McCormick pointed out there are numerous sections here. We are not speaking on the inspection fee portion of the bill which has to do with fees paid by regulated companies they are going down for some and up for others but we are not speaking on that. We simply note that those fees, whatever they are can be recovered by the companies from rate payers. We are here today to speak on Section 5 which changes greatly the

way rates will be set in Tennessee if it's passed. What this does, in our opinion, is make it more likely that rates will increase for businesses and households who are customers of regulated companies and the reason for this is that this bill greatly reduces the risk that the regulated companies utilities gas and water in particular will have as businesses because they will be allowed to recover virtually immediately their expenses and capital investments. Now heretofore, as was pointed out by Leader McCormick, we had rate cases and in that you have a general hearing you consider all the expenses all the capital investments of a company and then you project going forward what they think their expenses will be for the coming year and a rate is set on that with the addition that any investment that the company has made, they get to recover a rate of return on that and this is similar to any business if you have a start-up company and its difficult to attract capital you would want a high rate of return similarly, if you had a safe investment in bonds or a CD the rate of return would be less and what the TRA does is look at the company and decide what level of risk does it have and then that is expressed as a percentage usually, just take a round figure, you get a rate of return of 10% that means on all their investments if they have $50 million dollars of investments, they get their projected expenses plus a rate of return of 10% of that $50 million and each side presents testimony, our group has accountants that we have now they are contract accountants and they present testimony to TRA hearing and decides the case, sets the rate. What this bill does is it takes the last rate case and that's still in effect, the rates are still there, but in addition it allows companies to come in and say we want recovery for this expense, we've had some new project or whatever. Well, in the traditional rate case all those things are supposed to have been figured into their projected rates and covered in the rates, here what we are afraid of is that the risk, since the companies are recovering these expenses virtually immediately the risks should go down but there is nothing in the bill to reflect that decline in risk therefore we think rates will be unnecessarily high for consumers. We would point out that the TRA has full authority to do this without this bill. They have set what we will call alternative rate making mechanisms in the past, they could do this today and we think it would be better to do that because then you would have input from concerned persons – you would have more flexibility and it wouldn't necessarily be the legislators framework it would be the TRA who, that's their responsibility to set rates and they have expertise to say how this should be done and we think it would be better in that kind of hearing. We would also point out that, I know this is fairly complicated this office did send a letter with a memo attached and we hope you all have it, and if not we are glad to get it to you and the idea is that we are concerned about this potential increase in rates and we would also point out that by and large the utilities of TN particularly the larger ones are doing very well financially if you look at their stock prices from 2008 to the present in some cases it has virtually doubled and so they are not under financial stress, there is no idea in the bill that this is the reason why this is being done and another one of our major concerns is not only will this likely increase rates, but the way rate cases work once this rate is set and you have a rate of return on it if the company can become more efficient they get the benefits of the savings, in other words if you set a rate and the customer is charged say $50 a month and the company gets real efficient

and can do things for you know it cost them less than they projected, they get that savings under this system where they just simply submit a bill and say we want reimbursement we think they will lose that efficiency. So, um in summary that is our concern that this is really a big shift in the way rates are set. I know there have been some concerns about some rate cases, expense. We agree that that can be a problem. We think that could be addressed at the TRA. I would point out that we have had three major cases with TN American Water and Atmos and Piedmont in the last few years. We have settled them, there were no hearings. Expenses were rather minimal. The expenses come when there is problems and discovery as we call it, kind of a legal term trying to get information from the company, but we are very aware of that and very conscious of it and we do try to hold the expenses down. So, if there are any questions we will be glad to entertain them, either myself or Mr. McGehee, do you think, that's concludes our remarks.

**Chairman Pat Marsh:** Mr. Broemel, in your testimony I think you, I thought you just said that they can currently do this now,

**Vance Broemel:** Yes....

**Chairman Pat Marsh:** If they can currently do it now, why do you object to them doing it in the bill?

**Vance Broemel:** Well because we think it would be more input from more concerned parties and there could be more flexibility in the bill itself, it states that they can develop rules and procedures we think it would be better to do that all at the same time and in the past there was a bill here about something called the Coupling, where the idea was if consumers conserved there was concern that companies would not be making their projected rate of return, the Legislature made a general policy statement about the TRA should hear cases where the companies can present this concern with conservation and then they will make a determination and they did that and they developed a system to cover those cases and so in other words until you really have a full case with all the implications we think it is not a wise idea to set this kind of frame work as it were in a vacuum. It would be better to have them do it when there is much more to consider.

**Ryan McGehee:** And if I may, if you lock in the specific mechanisms here and that you have now with guaranteeing the return on equity along those and the procedures that encompass that, it makes it difficult for the TRA and our office to present safeguards for consumers to prevent over earning to adjust the return on equity because the risk is being shifted to the customers. Here you are locking them in under the old system when they are slightly more riskier, here we will move into a system where you are shifting the risk and there should be an adjustment there with a return on equity to actually have a company on record agree with us in a past case that these things do shift risk, but this bill does not address that and does not allow for that flexibility.

Another aspect of this bill is that it does not have a rate cap, which previous legislation in 2009 legislation in this Committee, the Commerce Committee chose to put forward a study there was a rate cap in there but there is not one here. So there are some things that are locked in and are going to limit flexibility in the future.

**Chairman Pat Marsh:** I think we have a question from Representative Curtiss?

**Representative Charles Curtiss:** Thank you Mr. Chairman. Toward the end of your statement you made I believe I heard this correctly but, estimating what the expenses will be they could end up over estimating what the expense is going to be and if they were to conserve even and have a savings they would retain that as profit?

**Ryan McGehee:** Right

**Representative Charles Curtiss:** I understood that correctly?

**Vance Broemel:** Yes.

**Representative Charles Curtiss:** So is there anything that you can think of that were given through the rule making authority that TRA is going to have to go through rule making procedures is there anything in this statute that's been proposed that would prevent them from rule making to recapture that money?

**Vance Broemel:** Uh, its um, I suppose they could try it but it, there is nothing in the statute that allows them to do that and we just don't know how that would work.

**Representative Charles Curtiss:** I'll ask that question. Thank you Sir.

**Chairman Pat Marsh:** Leader McCormick?

**Representative Gerald McCormick:** Thank you Mr. Chairman and I've got a couple of questions, did you all say that the TRA could do this without legislation, they could basically implement this program right now, or just that section?

**Vance Broemel:** Section 5, in the past they have done extensive regulation and I believe it was in the early 90s with the phone companies going through what we call an alternative form of rate making where they allowed them to have a projected rate of return and if there were over earnings then they would have a review of that and have a recapture – they did that all without legislation, yes.

**Representative Gerald McCormick:** Ok....

**Ryan McGehee:** There are a number of items they have already done as well like the commodity cost of gas is passed on to consumers, rates are adjusted annually for natural gas companies based on the weather, if you have a mild winter the rates go up, if you have a very cold winter the rates can go down, there are already a number of pass-throughs in effect and that's all without legislature authority.

**Representative Gerald McCormick:** I'll ask the same question with the TRA folks get up, but if they can go ahead and implement this without legislation I would rather get three votes than 50 so we'll see what the TRA folks say about that. Now, I want to go in Section C of 5, the very last sentence it says talking about "recovering operational expenses, capital costs or both associated with the investment and other programs including the rate of return approved by the authority at the public utilities most recent general rate case" - now could I take that to mean if lets say the water companies electric rates go up because TBA raises them and the power board raises them in return, they have to pay an extra $10,000 in their bill next year, are you saying that they will be able to charge $11,000 if they get a 10% rate of return on a simple bill, simple expense like that or is it just things that have to do with capital improvements?

**Vance Broemel:** I think it would be capital improvements and they would get a recovery of that increase perhaps, depending on you know the circumstances and that's one of our concerns when you have a rate case you take into consideration all expenses. Here they are singling out one that went up, they may have gotten more efficient with their labor costs and that's gone down but there is no provision in this bill to look at what went down its only what goes up and that's our concern. On a rate case you look at all expenses, some go up, some go down, you come to a global understanding, but here that's a good example if the electric went up they could come up with a higher electric bill and say we need to raise rates but they wouldn't be telling you that they have a new computer system or smart meters that read meters more efficiently and they don't need as many people doing that and there is no offset so that's the very kind of thing we are concerned with about just looking at what goes up.

**Representative Gerald McCormick:** But would the TRA not be able to take that into account or would they be legally prohibited from taking that into account?

**Vance Broemel:** Well there is nothing in the bill that – it just talks about your authorized to get this expense and in fact it just says you will get a rate of the last rate case. There is nothing about other expenses and that's another concern when you quoted the last rate case we all know that the capital markets can change. Some of these companies haven't been in for years and years they might have a rate of return of say 12% and the TRA is prohibited from adjusting that. And so you need, this bill says you look at what happens as of the last rate case and as we all

know with the economy you need much more current financial data and that's another concern of ours.

**Representative Gerald McCormick:** So you are saying that if a company had a good rate case five or six years ago they might never want a rate case….

**Vance Broemel:** Right….

**Representative Gerald McCormick:** But I suppose you guys could initiate a rate case, couldn't you?

**Vance Broemel:** We have in the past, I mean its getting into kind of history I supposed, we did it once with Atmos and it was expensive and very contentious if I can use that word in the sense that they were over-earning by some $5 or $6 million dollars a year. We did do that and brought it in and reduced their rates so we do have that power at the current time, but with this annual rate review with these trackers its to me very unclear whether we will be able to do that in the future.

**Ryan McGehee:** Leader McCormick, another big concern here is that not every company can decide to do annual rate review. They can cherry pick with a specific tracker and the rest of their rates would not be looked at – it would just be those expenses that flow under that tracker and the return that is guaranteed on that.

**Representative Gerald McCormick**: But you could still initiate a review, but you are saying it would be very expensive and …..

**Vance Broemel:** And it would really be a cross purpose with this bill, I think the companies would complain that they have chosen an annual rate review and these trackers and they don't need to have a rate case and I you know, I hate to it would just be up on the air as to what would happen. We would probably ask for one, but if we would get… I would point out that with the Atmos case our initial request that those rates be reduced was dismissed and we had to come back again and so if anybody knows the law you can make an argument but whether the agency will accept it I don't know.

**Representative Gerald McCormick:** And I would certainly want to have the legislative intent be such that a company couldn't take advantage, well for instance we've had a long period low interest rates and cheap capital and that kind of thing and somebody is hanging onto 14% returns from 10 years ago, that is not something we would have to guard against if that is the legislative intent if this were to pass …that we would want to do that…

**Representative Gerald McCormick:** One other question, is the rate cap you are talking about, what would be a reasonable rate cap as far as annual increases go, again put into the law.

**Ryan McGehee:** I would like to see or would like to discuss this with General Cooper specifically rate cap not only on the annual rate review, but also on the trackers themselves and I would think that just off the top of my head a 3% cap would be good.

**Representative Gerald McCormick:** You aren't old enough to remember the 70s, but if you had done that in 1974 you could have wiped out some of these being monopolies, you could have wiped them out basically.

**Ryan McGehee:** I know a lot of people speculate we are heading back that way, but we are not in that kind of inflationary period just yet....

**Representative Gerald McCormick:** Thank you Mr. Chairman.

**Chairman Pat Marsh**: Representative Mr. Pody.

**Representative Mark Pody:** Thank you Mr. Chairman. I want to go back to the TRA, I thought that if somebody came back for a rate increase, TRA had a right to look at their entire budget and their entire loss, they are not going to just look at one section so I'm not following where this would happen. If they had a profit in one area because they recoup that money, the next time they came for a rate increase that would be taken into account, is that not correct?

**Vance Broemel:** That is correct under the current situation, under a rate case but this bill changes that entirely. For two or three pages it goes on and on about all you, you can recover for a singled out expense it will not look at their total expense, no.

**Representative Mark Pody:** So if this goes through TRA will not have that authority?

**Vance Broemel:** No, I mean under this bill they wouldn't. We were speaking to Leader McCormick like I supposed we could ask for an entirely not rate case but the intent of this bill is to avoid or not have rate cases which means that you would not be looking at their entire expenses.

**Ryan McGehee:** And there are several mechanisms under the bill not just saying a rate review that would allow the companies to cherry pick several issues where you don't look at the operations and revenue.

**Vance Broemel:** I would like point out that this office is very concerned about investments in TN and to the best of my recollection we have never opposed a capital project to put in pipes, valves, whatever, particularly with the water company in Chattanooga. So its not that we want to cut down on recovery of capital expenses, we just want to do it in a way that we think is fair to all parties.

**Chairman Pat Marsh:** Alright, any other questions? If not, we will let you all go back and ask the other side to come up and to give their side, if that going to be you Mr. Allison? If you wouldn't mind please state your name and who you are with and we will hear your testimony.

**Jim Allison:** I'm Jim Allison, I'm the Chairman of the TN Regulatory Authority and with me today are Jean Stone our general counsel and Earl Taylor our Executive Director. I will make some comments and we will do our best to answer any questions you may have. This bill basically does two things. The first thing it does is reduce the regulatory burden on the utility companies in the State of TN by about $1.1 million dollars a year. By reducing our regulatory fees. The second primary piece of the bill is what was just discussed this alternative regulation. I want to make it clear to the Committee that this is not new stuff. Georgia, South Carolina, Mississippi, Alabama, Virginia and a whole host of other states across this country have already done a number of these things. Its procedural in nature, it does not substantively change that the TRA can do or cannot do. Now the Attorney General's office has focused in a very narrow sense on what the bill says on the rate of return. What they have missed is that before the regulatory authority will allow a company to enter into one of these alternative rate making processes is that we have to go through a process to establish and conclude that going into one of these alternative methods is in the public interests and in doing that we will look at a whole variety of things including the rate of return. Now there is another piece of the alternative bill that will permit companies, and its all permissive, none of the companies have to do any of this and the TRA does not have to accept any of this, we have to agree that its in the public interest before we enter into any of these alternative methods, but another piece of the bill requires, would require if a company opts into it an annual rate file by making an annual rate filing it will keep us more up to date on the cost, the returns, the expenses of all these companies so when we are dealing with the rate of return of issue that was brought up earlier we are not going to be in a position of not having looked at it for five, six or eight years, as a matter of fact the law requires them to have a general rate case within the last five years to enter into this annual rate review. So we will be looking at their rates every year if they opt into this annual rate review. If the rate of return gets out of kilter with the current market conditions, the authority can and in the past we have brought proceedings to open up the entire rate spectrum and we can do that here even if they go into this. As far as the trackers are concerned, again these are in wide use around the country, it's an effort to streamline the regulatory process, the example that was used here earlier was a good one if a water company that uses a lot of power to pump their water has a major rate increase from TBA, why open up every piece of their rates just to look at that. Now again we

would have to certify that its in the public interests before we do that, why not have a proceeding that would allow you to just look at that one piece. You may have just had a general rate case last year, again we can stay on top of that on a regular basis by this annual review and we will look at that. We've got a staff that will be looking at them on a regular basis. If the rate of return gets out of kilter, we can open a rate case to look at the rate of return. There is nothing in here that prohibits us from doing that and we will continue to do that just like we have done in the past. I'm going to kind of shut up and try and answer any questions you have, but the bottom line is that the authority has looked at this, we are very comfortable that we can continue to carry out our responsibilities with this bill as its written, again its permissive both on the part of the utility system to opt into it and it is permissive on our part to allow them to opt into it because we have then certify it in public interest.

**Chairman Pat Marsh**: Thank you very much. I have a question. I have heard about some of the parts of this bill I understood that this change should help do away with a lot of legal expenses on both sides of bringing up a host of lawyers to argue and all that savings the way I understand it is that it will go back to the rate payers? Is that correct?

**Jim Allison:** That's correct. The intent of this bill is to make the process more accounting driven and more analyst driven than it is attorney driven. And I know there are a lot of attorneys in the legislature so I don't want to say too much bad about attorneys, but I've been on both sides of rat cases now. I've spent my career working in the utility industry and I have testified before regulatory agencies in six states, I know how frustrating it is to have to write those million dollar checks to the law firms and I also know how frustrating it is on the part of a regulator for us to have to say ok, its ok for you to go recover that million dollar check that you wrote to the law firm from your rate payers. What we are interested in doing is trying to make Government more efficient, more streamlined and we are prepared to do everything we can at the TN Regulatory Authority to make that happen. We think this bill moves in that direction.

**Chairman Pat Marsh:** I have one other question that might be a little off – I've been asked to ask this by the Fuel and Convenience Store Association is it the intent of this legislation to permit regulated natural gas companies to subsidize their retail or wholesale alternative motor vehicle transportation fuel operations with rate payer funds?

**Jim Allison:** The answer to that is no. The bill is procedural in nature, there is no substantive change policy in the state of TN other than the fact that it will hopefully streamline the regulatory process.

**Chairman Pat Marsh:** Leader McCormick

**Representative Gerald McCormick:** Thank you Mr. Chairman and I need to ask some questions, I'm the sponsor of the bill and I support the bill but I also have an obligation not only to the rate payers of my area but to the members of my caucus and the general assembly, I want to first ask a couple of questions along those lines. You talked about a minute ago about lets say Chattanooga, the water company had a bigger electric bill and it went up and you could look at the item and see where it went up would that be considered an operational expense?

**Jim Allison:** That is an operational expense, yes sir.

**Representative Gerald McCormick:** Well the law says that any operational expenses can be recovered plus the rate of return so if they are going to make a 10% or 12% profit on paying their water bill? That's what I'm reading here....

**Jim Allison:** No sir, the rate of return is on invested capital. It is intended to cover the cost of the capital is the way we apply it to the rate case. So if there is a capital component to that, I don't know specifically what section you are looking at but it involves operating expenses as well as capital expenditure, the rate of return is on the capital expenses, not operating expenses.

**Representative Gerald McCormick:** I better read it to you then, it's in section 5C and it says: "the authority shall grant recovery and shall authorize separate recovery mechanism or adjust rates to recover operational expenses capital costs or both associated with the investment and other programs" so maybe that's how you get out of just paying the bill, but certainly if I was the company I would say that my light bill is associated with investment and other programs including the rate of return approved by the authority at the public utilities most recent general rate case. Maybe we need to get anybody from the industry to come up here and say if your light bill goes up about $10,000 are you going to give us a bill for $11,000 and let our rate payers pay for it. That's the real question.

**Jim Allison:** If you want industry to address it you are welcome, its well settled in rate cases methodology that rate of return is applied only to capital expenditures and it involves both debt as well as equity returns. So you have both elements of the return in there.

**Representative Gerald McCormick:** Maybe we'll settle but we are changing it with this right here from the way I'm reading it, but I'm not a lawyer, but we may have to go to the Senate and find some lawyers to come over here, but that's what it says, so we probably need to find out if it says what it means or if it means something else, but it specifically says recover operational expenses including the rate of return approved by the authority of public utilities most recent general rate case so I'll ask some of the people who are with some of these companies maybe after the meeting if they can give me some feedback on that.

**Jim Allison:** Our attorney is here with us and she can address it in more detail if you wish to, but the rate of return in there is intended to apply to the capital cost piece of that paragraph. It says to recover operational expenses, capital costs or both including the rate of return approved by the authority of the public utilities most recent general rate case pursuant to that rate of return would apply only to the capital investment, not the operating expenses.

**Chairman Pat Marsh:** Thank you very much. Representative Curtiss?

**Representative Charles Curtiss:** Thank you Mr. Chairman. You heard the question I asked the Attorney General's office we made the comment that an entity before the TRA on a regular year or case they would say they were going to do some capital expenditures and they were going to be X amount of dollars and the rate was based upon that but through efficiencies, they are way under the budget you would have the ability to still look at that if they calculated that incorrectly? I mean because without that ability the incentive would be to always over estimate your expenditures to have a higher rate and reap the profit.

**Jim Allison:** Not only will we have the opportunity, we will have an enhanced opportunity with the annual rate filing. Otherwise, in the current situation, we may look at it every three, four five, six years. All of our utilities except one have been within a fairly recent period of time for a general rate case so we don't have anybody out there that's gone 20 years without a general rate case or anything like that. This bill would give us an enhanced opportunity to look at those expenses.

**Representative Charles Curtiss** Right, and the other thing that occurred to me while we are testifying – you are not preventing the Attorney General's office to ask questions about rate savings, they are still going to have the ability to bring something to your attention, is that correct?

**Jim Allison:** That's correct and if at any time we focused some earlier comments about the rate of turn, anytime they feel like a company's rate of return is excessive they are certainly permitted by statute to file a petition requesting us to look at that and we have historically always accepted those.

**Representative Charles Curtiss:** Thank you sir. I think that the facts of this – seems a little bit like its vague in the bill in some places but the fact that you are going to have rule making authority that is not preventing you from being able to address all these areas that are not spelled out.

**Jim Allison:** That's correct.

**Representative Charles Curtiss:** Thank you.

**Chairman Pat Marsh:** Representative Hill?

**Representative Hill:** Thank you Mr. Chairman and of course Mr. Chairman thank you so much for being here and I appreciate the intent of the legislation, just a couple of quick questions. You said earlier in your statement, you said that this is really conforming into what other states are doing and that I think some of the questions on Section 5 of the legislation – do other states do that as well, as it sits?

**Jim Allison:** Yes, there are and I don't have the exact number but it's a long list of states that have entered into some of these alternative and rate making and the Attorney General quoted our last audit report in there is with some comments that if you read the entire paragraph it will say in there that this is clearly a national trend to move in this direction.

**Representative** Hill: Ok, alright, thank you so much.

**Chairman Pat Marsh:** Representative Pody?

**Representative Mark Pody:** Two questions. One what would you say is a good rate of return right now that would be approved?

**Jim Allison:** The overall rate of return will reflect both the cost of debt as well as the cost of equity. The debt costs right now are fairly low. We've seen some rate cases and I'm going to look to staff to correct me if I misspeak here but the overall rate of return is 6-7% but the debt component of that is on the low end of that, the equity numbers are on the higher end of that. Its set on an individual case depending on the riskiness of it, we've got some utilities that are well established with relatively low equity numbers, return numbers, we've got others that are fairly risky proposition, we've got one that just bought a company out of bankruptcy and it would be a risky proposition and it would have a higher rate of return than the others.

**Representative Mark Pody:** And my last question you said that most of the utilities are fairly current and you have monitored them and such, now what's the one that is oldest, what is the oldest one out there?

**Jim Allison:** Again, I'm going to refer to staff if I misspeak but I believe it is Kingsport Power the electric utility we regulate up in upper east TN and I believe they are somewhere around 8-9 years.

**Jean Stone:** I believe they are more like 18-19 years at this point, but their rates are extremely low, in comparison with other electric rates in that area.

**Chairman Pat Marsh:** Do we have any other questions while we are out of session? Leader McCormick?

**Representative Gerald McCormick:** Thank you Mr. Chairman and one more you may have answered this and I was in a side bar conversation but my question is in Section 5 can the TRA, do you have the authority to do this without a vote of the legislature to make these changes?

**Jim Allison:** We have instituted some trackers and some fairly limited situations and again I will defer to our attorney to comment on the legalities of it, but we feel like its prudent to clarify the nature of these and to get legislative authorization before we go further with it and that's the reason we are supporting the bill. We think it clarifies it and resolves any question about whether or not instituting some of these trackers is appropriate or not but I would invite Ms. Stone to comment on the legalities of it.

**Jean Stone:** I think that is absolutely correct and I will just add that rate setting is traditionally a legislative function and so it is entirely appropriate in my opinion to come to the legislature to ask you all to set the policy and the perimeters for rate setting including alternative methods.

**Chairman Pat Marsh:** Thank you. Do we have any other questions while we are out of session? If not we will go back in session. Thank you all for coming up. Representative Towns we are proud to see you come in today, welcome. We are back on the bill do we have any other discussions on the bill? If not, are we ready to vote on the bill? All in favor please say I, oppose, I's have it. This bill moves out to the Finance Ways and Means.

Thank you Mr. Chairman and members of the Committee.

**TENNESSEE GENERAL ASSEMBLY**

**Senate – Finance, Ways and Means Committee – April 2, 2013**

**Senator Mark Norris - Senate Bill 0197**

**Chairman Randy McNally:** Senator Norris on Senate Bill 197. Inaudible – Go ahead.

**Senator Mark Norris**: Thank you, Mr. Chairman. I'll move the bill to get it before us. This is the latest in TRA regulatory amendments. If there's a second, I'll present it. I think the amendment traveled with the bill from commerce.

**Chairman Randy McNally:** Senator Norris moves Senate Bill 197, seconded by the Chair, the amendment is from the Commerce Committee 3640 and travels with the bill and I believe Senator Kyle, was this the one you had the witness on?

**Senator Mark Norris**: Mr. Chairman, I had asked and Senator Kyle and I have been ships passing in the night, I had asked, of course, Senator Jim Allison's here and Earl Taylor, the director of TRA are here, and they've been stalwarts. They've been here a lot waiting for this moment. But I've also corresponded with the Attorney General's Office with Bob Cooper, and I think the Consumer Advocate's counsel, who I can't see, but I asked them to come and I think Senator Kyle did as well on this because the bill essentially does 5 things, only one of which has really drawn a lot of attention and that is the section that authorizes implementation of alternative regulatory authority methods, the so called trackers that we've heard about, that is where the Consumer Advocate's Division has concerns and we have, I think we all probably have received correspondence not only from the Consumer Advocate's Division but also from Mr. Allison addressing some of those concerns. As I always do, I declare Rule 13 when the TRA is involved and I'll do that again. But I'm at the will of the Committee, Mr. Chairman, if you'd like to stand and recess to hear from whomever, if you'd like me to explain more about the contents of the other provisions of the bill.

**Chairman Randy McNally:** Senator Norris, it's up to you. Do you want to proceed with the explanation and then hear from the witnesses?

**Senator Mark Norris**: Thank you. Yes, sir. The things that apparently have not drawn much question or concern are as follows. There's a provision in the bill relative to the State Employee Group Insurance Plan. This will make it clear that TRA directors are eligible for that. There's another section in the bill that attempts to clarify any ambiguities that may exist relative to conflicts of interest. It provides clarifying language deleting a phrase that currently says "or who

has any interest personally in any way or manner in such business or entity" substituting that with clearer language. Section 3 of the bill permits the agency to implement some optional cost based services at the request of one or more utilities and covered the cost for doing so. Section 4 of the bill re-aligns the fee structure to reflect today's regulatory environment resulting in a reduction of about I think it's $1.1 Million in fees paid to the agency to the benefit of consumers and utilities. It's section, I think it's Section 5 of the bill that deals with the manner in which the TRA reviews and approves rates proposed by utilities which from the TRA's perspective and the administration's perspective is litigious and lengthy and costly. And so by, this section authorizes the implementation of trackers an alternative regulatory method for utility rate reviews and cost recovery in place of the current process of the general rate case which involves such litigation. From the administration's point of view it expands the agency's tool kit for how rates are determined again maintaining the public interest and you'll hear about some of these, the different methods, safety and reliability cost recovery, economic development and annual review. As this was presented to me, it has remained, from my understanding and I think that Chairman Allison has pointed out in his correspondence, if not elsewhere, that third parties, whether it's the Consumer Advocate or others, are still able to intervene and participate in these proceedings, and I think that's key. But because of the concerns that have been raised, I wanted to have an opportunity for the Committee to hear from them on both sides of the issue.

**Chairman Randy McNally:** Without objection we will stand and recess and hear from Chairman Allison and Senator Kyle.

**Senator Jim Kyle:** Mr. Chairman, I appreciate Senator Norris's inviting the Consumer Advocate. I just want to give the Committee a brief history lesson as to the office of the Consumer Advocate. In 1994 my wife ran for the Public Service Commission and whether or not we would create a Consumer Advocate was the dominant issue of that particular political campaign. And subsequent to her election and her support of that particular area, previously the Public Service Commission took the position that there was no need for a public advocate because as public service commissioners they were public advocates. And, but there was a desire upon the legislature, ultimately, that there should be someone who would be monitoring the actions of the agency and through that the decision was made that we would have the office of the Consumer Advocate which is housed in the Attorney General's office and I know there are two representatives who, I don't know if this is all they do or what they do, but that's why they are here as members of the Consumer Advocate. I had read comments that they had made publicly and the testimony before the House and felt that it was worthy that we at least hear their view and view point at least of the office and where they're coming from. I think it is only appropriate that the agency make its presentation and those who would have rebuttal. As they come forward, Mr. Chairman, and as I mentioned to you some of those in the Government Operations Committee I think an issue that we have to, that I think we need to be comfortable with before this is all over is how you can remove this much revenue from the agency and then

still be able to do their task. I'm not saying we shouldn't remove the revenue, but you can only go far as a tank of gas will take you. And so I think that's something relevant to see where we are.

**Chairman Randy McNally:** Without objection, we will stand in recess.

**Jim Allison:** Thank you Mr. Chairman. I'm Jim Allison. I'm the Chairman of the Tennessee Regulatory Authority and appreciate the opportunity to visit with the Committee today. With me today are Earl Taylor, Executive Director, and Laura Forman, our Financial Director at the Authority. The bill before you essentially does two things. There are a few minor things it does, but basically it reduces the regulatory burden on the organizations that the TRA regulates by about $1.1 Million a year. In response to the leader's questions about the Authority's ability to absorb that kind of reduction, the Authority's been preparing that for some time. As the Committee is likely well aware, the TRA was substantially restructured last year. That resulted in very substantial cost savings to the consumers of the State of Tennessee. A big chunk of those cost savings are part of that $1.1 Million. We have some vacancies that we have held open as we became aware that this bill was going to be offered and we're sitting on some open positions that if the bill passes we will not fill. We will absorb the costs in that regard. Another big piece of the savings that we expect to absorb this year is a move from our current facility, moving into smaller facilities as part of the State project that is underway in that regard. It will save us a substantial amount of rent. Those are the three largest pieces of the cost savings that we'll experience to absorb the reduction to the citizens of Tennessee of about $1.1 Million.

The area that seems to have attracted the most attention with the Consumer Advocate's response to it is the alternative ratemaking authority section of the bill. This is something that we at the agency, the staff has examined very closely. We are very comfortable with what this does. It essentially is another step in the direction of trying to make the agency as efficient as we possibly can and keeping with what this body did last year to try to streamline our process, to try to make a more cost effective, and it's one of the pieces that we'll take to try to make sure that we are able to live within the lower budget that we'll have by the fact that we'll reduce our fee substantially. These are not necessarily new steps. They've been undertaken in several states around the country, including most of our neighboring states that have adopted various methods of alternative ratemaking. They have been to some limited degree adopted by the TRA already. For example, we have trackers with our major utility systems that we do now for fuel and things of that nature that are major relatively non-discretionary type of costs that have to passed on that are major cost expenses. We've looked at it very closely and we feel comfortable that we'll be able to continue to operate. The Consumer Advocate's concern about the bill seems to stem primarily from the provisions in the proposed bill that assure the ability to pass costs through on and recover at the currently authorized rate of return and we feel like that will be addressed in the proceeding up front whereas the sponsor pointed out, the Consumer Advocate is able to

intervene and if there is an issue with the rate of return that's on the books for that facility, that can be dealt with at that time, because we have to go through that process to establish it's in the public interest before we enter into one of these alternative ratemaking authorities. I'll be happy to try to answer any other questions you have if you have any for me.

**Chairman Randy McNally:** Questions by members of the Committee? Well thank you. Appreciate your testimony. Senator Kyle, did you have . . .

**Senator Mark Norris**: Well, thank you Mr. Chairman. Senator Norris deferred, yielded to me to do so. I think that we have, I see them now, we have Vance Broemel, and Bryan McGee, I think. Forgive me if I've got you wrong, but thank you for coming over and thank you, you've probably been here several times just as Chairman Allison had after I e-mailed General Cooper several weeks ago for all hands on deck. But thank you for coming over and thank you for expressing your concerns about the bill.

**Vance Broemel:** Yes. And thank you. We appreciate the opportunity to be here and the opportunity to have spoken with the TRA. Oh, excuse me. Vance Broemel with the Consumer Advocate Division of the Attorney General and Senator Kyle spoke a little about our office. We are a separate division within the office created by statute to represent households and businesses who are consumers of public utilities. Public utilities meaning for profit utilities, and some of you are undoubtedly familiar with these in your district. In Nashville it would be Piedmont, Williamson County, Rutherford County, Atmos Gas, Chattanooga you would have Chattanooga Gas and Tennessee American Water. And Kingsport has Kingsport Power. These are regulated by the TRA and it's been stated, our concern is with one section of the bill and that is the alternative ratemaking. And what this is, heretofore rates were set in what is known as a rate case and that's when a company who wanted to raise its rates would come before the TRA and present all its financial data. And I'm sure listening to some of the budget discussions I can see that this Committee is used to dealing with the big picture like that. And what this is is, you look at all the expenses, labor, chemicals, pensions, and if they need an increase you give them, the company is allowed to recover expenses and then they get the profit called the rate of return on their investment. And some expenses may go up or done in the coming years but as long as they are earning the rate of return, they are in good financial shape. What this bill does is allow a company to come in under an alternative ratemaking mechanism and pick one expense and ask the TRA to allow them to increase rates to recover that one expense. So, in other words, if you had an increase, as we all know in gasoline, they could say their fuel costs have gone up that year and they need to raise rates to recover that. But if you don't know that their labor costs have gone down in a way that would offset that fuel expense, there would be no need for a rate increase. Under this bill as proposed, you're looking at what's called the tracker, which means you track one expense. And we feel that the better picture is to look at the whole picture of the company and have what we call a rate case and in the past year we've had three major rate cases.

They've all settled. And we recognize the litigiousness, as it's called, in increasing expenses of having rate cases as an issue but we feel this can be dealt with in a way other than this alternative ratemaking, and we would point out that we've been very successful in settling cases without any undue expense in recent years. So those are our concerns we think the TRA has the ability to do this with its own rules if it wants to rather than legislation where it could be done with more participation from interested parties and we would also point out that at this point the companies that I referred to, Tennessee American, Piedmont, Atmos, Chattanooga Gas, all are very healthy financially. There's no testimony, evidence or implication that this is driven at all by a need to allow companies to survive financially. They are all doing very well. So that is our position. As I said, we are only looking at this one section of the bill and we would be glad to answer any questions you might have.

**Chairman Randy McNally:** Chairman Henry.

**Senator Douglas Henry:** Thank you, Mr. Chairman. Mr. Broemel, did you say they could single out these items without this bill?

**Vance Broemel:** You mean currently? Well, the TRA could have rulemaking that would allow this or have a case. In fact, that was done several years ago. Chattanooga Gas wanted what we call the Tracker and they came in on proof and then they could make a case for it, for an individual case, and then we could all participate. So they do have the authority to do this at the present, in our opinion, and we would rather see it done at the TRA level than legislation.

**Senator Douglas Henry:** TRA, by action of the TRA could do what the bill would let them do by statute. Is that correct?

**Vance Broemel:** Correct. Yes, sir.

**Senator Douglas Henry:** Then the bill would have no effect . . . not harm, correct?

**Vance Broemel:** It allows it to be done on a very broad level that we don't think, it would be much better if they had either a rulemaking to do it for, with participation of all parties, and a more, you know, you could have more participation testimony, that kind of thing, or you could do it on a case by case. In other words, Atmos could come in and say we need a fuel tracker and then you could explain, they could explain why they wanted it rather than just giving them carte blanch authority to do it at this point.

**Senator Douglas Henry:** So if TRA internally, they would not have to, if the TRA did this by rule, we'll say, they would not have to incorporate as much information into a particular case as well they could.

**Vance Broemel:** They could. Yes, they could. Yes. They could do as much as they feel would be necessary and it would be tailored to an individual utility rather than this legislation.

**Senator Douglas Henry:** But the statute, what did the statute do? The statute with regard to the trackers. Does the statute, the statute lets them single out a single expense like gasoline, I think you said.

**Vance Broemel:** Yes.

**Senator Douglas Henry:** It allows them to single out gasoline and raise their rates with regard because of the gasoline expense without having to look at the whole picture. Is that right?

**Vance Broemel:** That's our position. Now, I will agree that as Chairman Allison said there is a provision that talks about looking at the public interest, but we don't feel that that's precise enough and that's why we prefer a rate case where you would look at a number of expenses.

**Senator Douglas Henry:** Suppose they did what you just described and they looked at the single item and they said, yes we've observed it. We've looked at the public interest too. Do you have standing to take them into court and disagree with that?

**Vance Broemel:** Well, the bill does not refer to us being able to participate, which is not to say that we can't. We've just heard that we can, but it will be a new procedure and I think everyone would agree that there's a lot of established practice for rate cases but this is a brand new area and we don't know, for instance, if there'll be testimony, if it will be called, what's technically called a contested case, any number of items like that which, you know, we'll be, if the bill passes we'll be learning soon enough and then of course, our office, let me assure everyone that we're prepared to act for consumers under any regime of law. We've gone from fulltime directors to part time directors, so we're not disputing that we're going to represent consumers to the best of our ability. We're just pointing out that . . .

**Senator Douglas Henry:** If they do this, if they use a tracker of just a single expense and you don't think they would serve the public interest you have standing to take them to court, is that right?

**Vance Broemel:** Oh, yes. Yes. We would have a hearing and then, I think under the law, I think it would still be in effect, it could be appealed, yes.

**Ryan McGehee:** So they could appeal it, the Court of Appeals, the Tennessee Supreme Court in the past have invested a lot of discretion into what the TRA, the decisions the TRA makes.

Because, frankly, I don't think the Courts want to get too involved into the accounting part of the cases.

**Senator Douglas Henry:** You have broad appeal but to show, you have de novo or passion, prejudice or caprice.

**Vance Broemel:** Yes. That's correct.

**Senator Douglas Henry:** Which way? De novo or passion, prejudice or caprice? What would you have to show?

**Vance Broemel:** It would be abuse of discretion. Basically, the way the law reads no support in fact and generally speaking abuse of discretion. It's an administrative procedures act appeal. Because the cases are contested cases.

**Senator Douglas Henry:** Alright. So you'd take them before one of the Secretary of State judges?

**Vance Broemel:** No. It would go directly to the Court of Appeals.

**Senator Douglas Henry:** You go to the Court of Appeals and you would allege that the public interest was not taken into account. Now, would you be allowed to put on proof to that effect, or would you have to go on the record made below?

**Vance Broemel:** It would be the record made below. Yes.

**Senator Douglas Henry:** You wouldn't have to show some certiorari type reason to be there, right?

**Vance Broemel:** Yes. And we, our staff, while we don't currently have them on staff, but we contract with accountants and economists and they would testify most likely and that would be in the record.

**Senator Douglas Henry:** . . . seriously. I'd like to ask the Majority Leader on that point. I think that's important.

**Chairman Randy McNally**: Do we have other questions? Senator Kyle? And if we could, Mr. Broemel, the other attorney's name for the record?

**Vance Broemel:** Ryan McGehee. He's also with the Consumer Advocate Division. We're both attorney generals there.

**Chairman Randy McNally:** Senator Kyle?

**Senator Jim Kyle:** Yes, sir. I guess it begs the question if you're no longer having rate cases and you no longer have rate cases in the telecommunications area, what's there left for ya'll to do? I mean, if we have, essentially this nebulous phrase "in the public interest" I mean. I'm not trying to be flippant or anything but I'm just curious as, how would the Consumer Advocate advocate if there isn't a forum for the Consumer Advocate to advocate in? Because it appears to me from my reading of the bill and I'd be curious what the TRA thinks, if this is all going to be managed administratively within the agency and unless there is some gross abuse of discretion, whatever they say they're going to do they're going to do. Am I over simplifying the situation?

**Vance Broemel:** Well, it will be different. And again we're not, the bill does not specify the way that hearings will be held. We would prefer what we call pre-filed testimony. That's what you do in a rate case, where an expert will write out questions and answers in very detailed form going into a lot of accounting or economics, and then the company, both the company and the Consumer Advocate file this kind of testimony. We would hope that there would be that here but we're not certain and, you know we would hope, we expect to still have a function for sure. Whatever, if we can only file a brief we'll do that or affidavits, we'll do that.

**Senator Jim Kyle:** But from a dollar standpoint from the Attorney General's budget, I mean all due respect, we're not having hearings, I mean, just, I'm just, I raise that question from a financial side to the Committee that if we're funding a watch dog program that there's nothing to watch because, you're not put in a posture, I do think Mr. Chairman, it would be, what I hear the gentleman saying, correct me if I'm wrong, that if you were say a water company you would pick out the cost that you could justify, in other words the cost that had gone up and you would ignore the cost that would equal it off and then, is that not correct? And therefore you justify your rate increase even though you have a counter . . .and you're not, you will not be giving an ability to counterbalance that with additional information will you?

**Vance Broemel:** Well again, it's not specified in the bill. We would hope there would be discovery and we would do our best to bring out the other costs. But again, it is a new scenario and it's not like a rate case so, and that's in fact why we're concerned because these things just track one expense.

**Senator Jim Kyle:** Well then, I guess it would be interesting to the sponsor, I would be curious what the agency thinks all this means and say you're essentially in the driver's seat and these facts are in the rumble seat.

**Senator Mark Norris**: Mr. Chairman. I think that would be fine. I think they should be heard on this point because the way this bill is crafted it adds to the provisions of Title 65-5-103. It's not deleting. This is an alternative for them. As I understand it they may for some reason, decide they still want to have a rate case per se. There are alternatives they may use. And as you have correctly pointed out, they could probably have done this through rulemaking but the administration thought it was better to bring it here so we could have an open discussion about it, but I see Mr. Allison is prepared to answer those questions specifically if I haven't done it generally.

**Vance Broemel:** Yes. Let me assure you that is correct. It does not eliminate rate cases and there may, there will still be need for one. It could be ordered, we could request it, that kind of thing, yes.

**Chairman Randy McNally:** Mr. Allison. You wish to comment?

**Jim Allison:** I think it's important to understand that all the alternative ratemaking arrangements are permissive, they are not required. It requires the company to ask for the alternative ratemaking treatment and then the Authority enters into a deliberation as to whether or not agreeing to that alternative arrangement is in the public interest. Now the Consumer Advocate Division will have full and ample opportunity to participate in that hearing. The example I've used before some of the other committees. Let's take for example a water company that spends a considerable amount of money on electricity to run their pumps, to keep the pressure up in their water system. If TVA has a large rate increase, they have little opportunity but to pay their bill. And is there any need at that point in time to open the whole set of books and look at all their costs as opposed to just go through an expedited proceeding and allow those costs to pass on. Now having said that, if there is a concern about other costs, because we're going to be tracking their costs on a much more frequent basis than we do now through the annual rate review. If they've opted into that system. And if there are concerns about other costs, pension cost, or their rate of return, or whatever it is, then you can enter a proceeding for a rate case. We're not doing away with full rate cases. These are just alternatives that are available on a permissive basis. But if the Consumer Advocate or any other allowable party has a concern about other costs, they can come to the Authority and say we need to look at the whole ball of costs and if the Authority agrees with that, we will go the full rate case route as opposed to the alternative ratemaking.

**Chairman Randy McNally:** Leader Kyle?

**Senator Jim Kyle:** But you pretty much have carte blanch, don't you sir, in whether you decide you want to do it or not. I mean, there's not like five factors and you've got to review the five factors and see whether you hit the mark or whether there's three factors. I mean it's just what

ya'll decide to do. Whether you want to do it or not. I mean, wouldn't that, ya'll have a great deal of discretion in this matter wouldn't you say?

**Jim Allison:** We would have a great deal of discretion, just as we do now in general rate cases. It's a procedural change. The way you go about doing things. But we have to, our overall objective is to balance the interest of the consumers with the companies that are operating in those environments.

**Senator Jim Kyle:** And how will ya'll be reporting your decision making to the General Assembly?

**Jim Allison:** We issue official orders of everything that we do that are public record and available. As far as reporting to the General Assembly, I know we file an annual report. Beyond that, I'd probably have to get some help from the staff to answer that question any more specifically.

**Senator Jim Kyle:** Would the Agency have a problem, and I ask this to the sponsor, would the Agency have a problem if the annual report of the Agency indicated to the General Assembly we had these petitions and we ruled this way. Therefore, because I don't think we get that data today. I'm just asking you, a water company says we need, TVA raised our rates. Power, electric power, Piedmont comes to you and says we've had some bit of flood in our community and we had this or that. I'm just saying to you the various and ya'll determined, ya'll made a decision because in the public interest, you know I went through a process yesterday that was allegedly in the public interest. I disagreed at the end. But I would just say to you, I mean that's wide open and I do think if these people at the Consumer Advocate, the whole idea that the General Assembly when the Consumer Advocate was created was to not to be having to monitor what was going on at the Public Service Commission because there were concerns that things, they had so much discretion they were discressing the wrong way, contrary to the public interest. That, at least that was the street talk. And therefore, we had to have a professional group to be sitting at the table or be sitting in the courtroom and therefore if there was a problem, they would come up here and tell us there was going to be a problem. Now since these folks have such a more limited role, it just seems to me, and I just take it to you and to Mr. Taylor who is running the show at this time that there ought to be some mechanism where a legislator from Chattanooga, Kingsport, Nashville, Williamson County, or whatever, could look and see that well they tried, they did this and they ruled this way and might say I want a little more, know a little more about that because I do think that legislators do get calls when rates change, as you can imagine, and I don't think they're going to find you, Mr. Allison, but they'll sure find us before it's all over, and so I'd ask for the sponsor to consider that we make clear that the annual report is going to have a summary of matters brought, the decision we're not doing a rate case,

we do that like this, and therefore people could look and see whether or not, if they agreed that what you were doing was in the public interest.

**Jim Allison:** We would be happy to do that, sir. We're a creature of this body and we will provide whatever information, everything we have is public information, and we will make a point in our next annual report to provide some additional information on petitions of this nature that we get and what we deal with them.

**Chairman Randy McNally:** Other questions? Thank you gentlemen. Appreciate your testimony.