BEFORE THE TENNESSEE PUBLIC UTILITY COMMISSION

NASHVILLE, TENNESSEE
February 29, 2024

IN RE:	**)**	
	)	
ATMOS ENERGY CORPORATION NOTICE OF	**)**	**DOCKET NO.**
FILING DEPRECIATION STUDY AND REQUEST	**)**	**23-00050**
FOR APPROVAL OF NEW DEPRECIATION RATES	**)**	

ORDER APPROVING NEW DEPRECIATION RATES

This matter came before Chairman Herbert H. Hilliard, Commissioner Clay R. Good, Commissioner David Crowell, Commissioner Kenneth C. Hill, and Commissioner John Hie of the Tennessee Public Utility Commission (the "Commission" or "TPUC"), the voting panel assigned to this docket, during a regularly scheduled Commission Conference held on December 11, 2023, to consider the *Notice of Filing of Depreciation Study and Request for Approval of New Depreciation Rates* ("*Notice*") filed by Atmos Energy Corporation ("Company," "Atmos," or "Atmos Energy") on June 29, 2023.

NOTICE AND RELEVANT BACKGROUND

As part of the authorization of the Company's Annual Rate Review Mechanism ("ARRM") in Docket No. 14-00146, the Commission approved a settlement agreement between Atmos and the Consumer Advocate Division of the Office of the Tennessee Attorney General ("Consumer Advocate") which authorized the Company to submit depreciation studies to update depreciation rates used in ARRM calculations subject to the scrutiny of the Consumer Advocate through a

contested case.[1] The Company's ARRM Tariff approved in Docket No. 14-00146 provides that if Atmos performs a depreciation study recommending new rates, it must obtain Commission approval prior to using the new rates to compute depreciation expense in its subsequent Annual Rate Review Mechanism ("ARRM") filing.[2] On June 29, 2023, Atmos filed the *Notice* and sought approval of new depreciation rates to be included in the Company's next ARRM filing due on February 1, 2024.

Atmos is a public utility engaged in the business of transporting, distributing, and selling natural gas in areas of Tennessee, as well as certain other states. Depreciation rates should not be confused with utility base rates. In general, the utility industry is capital intensive and involves substantial investments in capital assets; thus, depreciation is typically a large expense component because it is designed to recover the cost of the plant and equipment needed to provide utility services over the useful life of the property. Depreciation is a noncash expense that is recovered dollar-for-dollar from ratepayers and, consequently, can have a material impact on base service rates.

Depreciation rates are based on depreciation conventions and refer to the mathematical percentage at which annual depreciation expense is recognized over the life of a capital asset or group of similar assets. For example, if a service truck is determined to have a useful life of eight years, its depreciation rate is 12.50% (100/8); and if a natural gas line is determined to have a service life of thirty years, its depreciation rate is 3.33% (100/30). Due to the voluminous investments in capital assets, depreciable plant and equipment are gathered into homogenous groups for depreciation purposes; and depreciation rates are generally calculated and applied to

[1] *See In re: Petition of Atmos Energy Corporation for a General Rate Increase Under T.C.A. 65-5-103(a) and Adoption of an Annual Rate Review Mechanism Under T.C.A. 65-5-103(d)(6)*, Docket No. 14-00146, *Order Approving Settlement*, Exh. A, pp. 18-19 (November 4, 2015).
[2] *Notice*, p. 1 (June 29, 2023).

groups of assets based on the average depreciation characteristics of the individual groups, as opposed to applying the rates to specific assets.

In support of its request for new depreciation rates, Atmos filed the testimony of Ned W. Allis, Vice President of Gannett Fleming Valuation and Rate Consultants, LLC ("Gannett Fleming").[3] Atmos hired Gannett Fleming to perform the depreciation studies for its Tennessee Direct Property and Kentucky Mid-States General Office, which are sponsored by Mr. Allis's testimony as Exhibits NWA-1 and NWA-2, respectively. In addition, Mr. Allis sponsored the depreciation study of Atmos's Shared Services Unit ("SSU") conducted by Alliance Consulting Group ("Alliance"), as Exhibit NWA-3. Mr. Allis reviewed the SSU Depreciation Study (SSU Study") performed by Alliance and agrees with its analysis.[4] In total, the Company filed three studies with the *Notice* (Exhibits NWA-1, NWA-2, and NWA-3 together, "Depreciation Studies").

The Depreciation Studies were performed using the Company's depreciable property and reserve balances as of the fiscal year ended September 30, 2022.[5] According to Mr. Allis, the depreciation studies use the same methods, procedures, and techniques as used in the past by Atmos, as well as other companies appearing before the Commission.[6] The Depreciation Studies utilized the straight-line method and remaining life technique to compute proposed depreciation rates.[7]

For each study, historical plant data was collected and analyzed to estimate the service life and net salvage characteristics of each depreciable group.[8] Under both the Average Life Group ("ALG") and Equal Life Group ("ELG") procedures, the remaining lives were calculated

[3] Ned W. Allis, Pre-Filed Direct Testimony, p. 2 (June 29, 2023).
[4] *Id.* at. 3.
[5] *Id*. at 4.
[6] *Id*. at 5-6.
[7] *Id.* at 6.
[8] *Id.* at 7-8.

according to group expectancy techniques using the Iowa Survivor Curves ("Iowa Curves").[9] The Iowa Curves are the industry standard system of survivor curves that contain the survivor characteristics experienced by industrial companies, including public utilities.[10] The Company's actual historical data, as well as net salvage estimates for other gas companies, were utilized for estimating the studies' net salvage percentages.[11] Cost of removal studies performed in 2014 and 2016 were considered when estimating net salvage values ("Alliance Studies").[12]

After the service life estimates and salvage characteristics were determined, the annual depreciation rates were computed based on plant in service as of September 30, 2022.[13] For each plant account, the difference between the surviving investment, adjusted for estimated net salvage, and the allocated book depreciation reserve, was divided by the remaining life to yield the annual depreciation expense. The annual depreciation expense divided by the sum of the original plant cost yields the annual depreciation rate.[14]

The Tennessee Direct Property study resulted in a composite depreciation rate for all plant of 2.30% (43.48 years), with proposed depreciation rates by plant account shown on Exhibit NWA-1, Part VI, page 4. The Kentucky Mid-States General Office study computed a composite depreciation rate of 7.55% (13.25 years), with rates by plant account shown on Exhibit NWA-2, Part VI, page 4. The Shared Services Unit study shows a composite rate of 7.46% (13.40 years) with individual plant account rates listed in Exhibit NWA-3, Appendix A. The depreciation rates proposed by Atmos in this case would generate annual depreciation expense of approximately $19.2 million based on the Company's investment in depreciable property as of September 30,

[9] *Id*. at 9-10; Exh. NWA-3, pp. 4-6.
[10] *Id.* at 9.
[11] *Id.* at 11.
[12] *Id.* at 12.
[13] *Id.*
[14] *Id*. at 7-8, 14-16.

2022; and the aggregate effect of all three depreciation studies is an increase in annual depreciation expense of approximately $755,000.[15]

POSITION OF THE CONSUMER ADVOCATE

On August 1, 2023, the Consumer Advocate filed a *Petition to Intervene* seeking to intervene, which was subsequently granted.[16] The Consumer Advocate initially made two broad objections to the proposed depreciation rates. The first objection dealt with the service lives of certain plant accounts. After discussions with the Company, the Consumer Advocate withdrew the objection but did not concede the issue.[17] The remaining objection centered around the calculation and accounting for net salvage values. After the Consumer Advocate withdrew its objections to the service lives of certain plant, both parties requested a hearing on the issues concerning net salvage values.[18]

The Consumer Advocate retained Michael J. Majoros, Jr., President of Snavely King Majoros & Associates, to review Atmos Energy's Depreciation Studies. In pre-filed direct testimony, Mr. Majoros addressed the Company's Tennessee Direct Property study.[19] With respect to cost of removal, Mr. Majoros opined that the Company should only charge the cost of removal associated with final, unreplaced retirements to the cost of removal of the unreplaced asset, and that in cases where a retired asset is being replaced with another asset, replacement cost additions should include the cost of removal of the replaced assets. Additionally, Mr. Majoros contended that the studies performed by Alliance that Atmos used to allocate cost of removal in asset replacement projects are flawed and should not be used because they improperly allocate

[15] *Id.* at Exhs. NWA-4, NWA-5 & NWA-6.
[16] *Order Granting the Petition to Intervene Filed by the Consumer Advocate*, p. 4 (August 21, 2023).
[17] Michael J. Majoros, Jr., Supplemental Pre-Filed Direct Testimony, pp. 2-3 (October 26, 2023); Ned W. Allis, Supplemental Pre-Filed Direct Testimony, pp. 2-3 (October 26, 2023).
[18] *Id.*
[19] Michael J. Majoros, Jr., Pre-Filed Direct Testimony, p. 13 (September 22, 2023).

replacement costs to cost of removal.[20]

Mr. Majoros testified that increasing the cost of the removal ratio increases the calculated depreciation rate, and that if the cost of removal is not supportable, the depreciation rate is excessive.[21] Mr. Majoros asserted that Mr. Allis's approach is flawed because the Alliance Studies inappropriately compare cost of removal expressed in current dollars to retirements expressed in historic dollars; and more significantly, Mr. Allis did not correct the Company's arbitrary, unnecessary, and inappropriate accounting for replacements.[22]

Mr. Majoros claimed that the cost of removal proposed by the Company is arbitrary because it allocates a percentage of the replacement costs to cost of removal when such costs should be included in the total cost of replacement projects and recorded as new plant additions.[23] To support his position, Mr. Majoros relied on Uniform System of Accounts ("USOA") Definition 32, which states "Replacing or replacement, when not otherwise indicated in the context, means the construction or installation of gas plant in place of property retired, together with the removal of the property retired."[24] According to Mr. Majoros, this definition means that the original cost of a replacement addition is one hundred percent of the total project cost, which includes the cost of removing the existing item. As such, he argued that the Company's accounting for replacements does not comply with this USOA requirement. [25]

Mr. Majoros argued that the Company's allocation of part of the original cost of the replacement project to the cost of removal of the existing asset is unnecessary and arbitrary and concluded that all allocations are arbitrary.[26] According to Mr. Majoros, the allocation is

[20] *Id*. at 2.
[21] *Id.* at 12.
[22] *Id*. at 18.
[23] *Id.*
[24] *Id.* at 19.
[25] *Id*.
[26] *Id.*

unnecessary because under the Federal Energy Regulatory Commission ("FERC") accounting system, rate base remains the same after the allocation is done as it was before the allocation because the remaining life technique keeps the depreciation rate the same before and after the allocation. Thus, Mr. Majoros concluded that the only purpose of the allocation was to feed cost of removal amounts into studies such as Mr. Allis's so that the Company can charge inflated cost of removal ratios to ratepayers.[27]

Mr. Majoros testified that Pennsylvania and New Jersey do not allow utilities to include future net salvage ratios in depreciation rates, and that Maryland requires utilities to discount their future net salvage estimates to their present value.[28] According to Mr. Majoros, these techniques address expressing estimates of future net salvage as percentages of the surviving plant in service, which was done by Mr. Allis.[29] Mr. Majoros asserted that Mr. Allis's reliance on the Alliance Studies enabled Mr. Allis to propose higher cost of removal ratios, and that the intent of the Alliance Studies was to pass more costs of removal into Mr. Allis's net salvage studies.[30] Further, Mr. Majoros stated the Alliance Studies support his assertion that the Company's accounting approach is arbitrary and unnecessary, because the study results are used to allocate removal costs for replacement projects and because the allocation factors are used to charge a portion of overall labor costs to removal costs for various capital replacement activities.[31]

Mr. Majoros relied in part on statements and discovery responses made by Atmos. According to Atmos, if a replacement project is cost of removal eligible, then the install/removal split for contractor labor, contractor services, and Company labor defaults to a 95%/5% split, and

[27] *Id.*
[28] *Id.* at 21.
[29] *Id.* at 20 (internal citations omitted).
[30] *Id*. at 22.
[31] *Id.* at 23 (internal citations omitted).

the Alliance Studies support the use of the 95%/5% split.[32] However, Mr. Majoros noted the Company's actual replacement split was 78% in FY22 and 74% in FY 23.[33] Mr. Majoros testified that Mr. Allis's net salvage costs are inflated because Mr. Allis applied a removal ratio of 100%, rather than a figure in the range of 74% to 78%.[34] Mr. Majoros used the 76% average of the FY22 and FY23 replacement plant percentages to limit the amount of future net salvage included in deprecation rates to the portion of the plant that will not be replaced (*i.e.,* retirements without replacements). Mr. Majoros then applied the Alliance Studies' 5% allocation ratio for removals to the 24% of future retirements that he contends are cost of removal eligible. Based on these assumptions, Mr. Majoros calculated a cost of removal ratio for eligible plant retirements of 1.2%.[35] Mr. Majoros then used the computed net cost of removal ratio to recommend the Consumer Advocate's proposed alternative depreciation rates.[36]

ATMOS ENERGY REBUTTAL TESTIMONY

Mr. Allis filed rebuttal testimony on behalf of Atmos on October 11, 2023. According to Mr. Allis, asset retirements may occur with replacements (meaning that a new asset is added to replace the retiring one) or without replacement (meaning no new asset is added to replace the retiring one). In either case, the net salvage value should be included in the depreciation study.[37]

Mr. Allis testified that including net salvage in depreciation is consistent with general principles of accounting. In particular, the matching principle is satisfied by matching the cost of capital assets, including net salvage, with the periods over which the assets generate revenues. Thus, the full cost of the assets, including their end-of-life costs associated with retirements, may

[32] *Id.* at 24.
[33] *Id*. at 24.
[34] *Id.* at 25.
[35] *Id.*
[36] *Id.* at 26.
[37] Ned W. Allis, Pre-Filed Rebuttal Testimony, p. 3 (October 11, 2023).

be recovered over their service lives. In support of his testimony, Mr. Allis referenced page 157 of the National Association of Regulatory Utility Commissioners' publication *Public Utility Depreciation Practices* (1996), which discusses this matching principle concept and states in part that "[h]istorically, most regulatory commissions have required that both gross salvage and cost of removal be reflected in depreciation rates."[38]

Mr. Allis testified that including net salvage values in depreciation is a ratemaking principle that accomplishes the goal of intergenerational equity because each generation of customers pays their fair share of the costs to provide service. Mr. Allis testified that not recognizing costs of removal through deprecation rates over the lives of the related assets, would cause customers to pay these costs after the assets are retired and create intergenerational inequity.[39] Further, Mr. Allis claimed that Mr. Majoros's argument to decrease depreciation expense in the short-run fails to recognize the impacts to ratepayers. Lower depreciation today not only means higher depreciation in the future, but it also has the effect of computing a higher rate base and associated higher rate of return requirement. Thus, according to Mr. Allis, lower depreciation expense can lead to higher customer rates because the higher rate base eventually exceeds the impact of lower depreciation expense.[40]

Mr. Allis asserted that Mr. Majoros's proposed accounting for net salvage value is inconsistent with the USOA and industry practices.[41] Mr. Allis cited USOA Plant Instruction 10(B)(2) which he testified provides that retirements of depreciable gas plant shall be charged to accumulated depreciation for such plant and that "[t]he cost of removal and the salvage shall be

[38] *Id*. at 4.
[39] *Id.* at 4-5.
[40] *Id.* at 5.
[41] *Id*. at 6.

charged or credited, as appropriate, to such depreciation account."[42] Additionally, Mr. Allis cited in his testimony that the USOA's description of Account 108, Accumulated Provision for Depreciation of Gas Plant, states "[a]t the time of retirement of depreciable gas utility plant, this account shall be charged with the book cost of the property retired and the cost of removal and shall be credited with the salvage value and any other amounts recovered, such as insurance."[43] Mr. Allis concluded that the USOA is clear that whether or not a retirement occurs due to a replacement, the cost of removal and gross salvage shall be charged or credited to accumulated depreciation; and that recording cost of removal as part of a plant addition as suggested by Mr. Majoros would not comply with the USOA.[44]

Mr. Allis asserted that Mr. Majoros's reliance on USOA Definition 32 regarding plant replacements is erroneous. Definition 32 provides that a plant replacement "when not otherwise indicated in context, means the construction or installation of gas plant in place of property retired, together with removal of the property retired."[45] According to Mr. Allis, the definition is not explaining that cost of removal should be a cost of the new plant addition, but is merely explaining what a replacement is. Mr. Allis testified that the additional sections of the USOA that he cites confirm that Mr. Majoros's interpretation of Definition 32 is incorrect.[46]

Based on his review of the depreciation studies for Piedmont Natural Gas Company submitted in Docket No. 20-00086 and Chattanooga Gas Company submitted in Docket No. 18-00017, Mr. Allis noted that both companies included net salvage estimates in depreciation rates and that both recorded the cost of removal to accumulated depreciation for replacement projects.[47]

[42] *Id*. at 9.
[43] *Id.* at 10.
[44] *Id*. at 9-10.
[45] *Id.* at 8 (internal citations omitted).
[46] *Id.*
[47] *Id.* at 7.

Of the hundreds of depreciation studies that he has worked on, Mr. Allis testified that he could not recall any utility being required to account for cost of removal in the way Mr. Majoros suggested.[48] Mr. Allis contended that if Mr. Majoros was correct, virtually every utility in the country would be violating the USOA.[49]

With respect to determining the cost of removal for plant retirements that are associated with replacement projects, Mr. Allis testified that there are two primary methods by which these types of costs may be recorded in plant in service or removal. First, is the incremental method, in which only costs associated with retirement that are incremental to the project (i.e., that occur in addition to the cost of placing the new asset in service) are recorded as cost of removal. The second is the common cost sharing method in which costs common to both tasks are allocated between plant in service and cost of removal in proportion to the directly assigned costs (primarily labor) associated with each task. Mr. Allis testified, that the method implemented by Atmos Energy follows the incremental method recommended by the Alliance Studies.[50]

Mr. Allis asserted that using the incremental method results in less cost of removal being allocated for replacement projects than the common cost sharing method. Since the Company's implementation of the incremental method in late 2015 and late 2016, the Company's recorded cost of removal has decreased, which can be seen in the three-year moving averages for Account 380.00, Services, which had exceeded -20% in prior years but declined to the -10% to -15% range after adoption of the incremental method.[51]

Mr. Allis disputed Mr. Majoros's claim that there are substantial increases in cost of removal after the Alliance Studies were implemented. While the dollar levels of cost of removal

[48] *Id.* at 6.
[49] *Id.* at 7.
[50] *Id.* at 11.
[51] *Id*. at 12.

have increased, the reason for the increase is the volume and cost of the work performed. In other words, due to capital improvements and replacements, the Company is retiring more assets and, therefore, the cost of removal has increased overall. According to Mr. Allis, a comparison of the percentage of cost of removal, as expressed in relation to capital expenditures, shows that cost of removal has declined, rather than increased.[52] Mr. Allis testified that Mr. Majoros's claim that the intent of the Alliance Studies was to pass more cost of removal into the net salvage studies is inflammatory and reflected Mr. Majoros's misunderstanding of the Alliance Studies, since they had the opposite effect than what Mr. Majoros implied.[53]

Mr. Allis testified that the percentage of capital replacement costs assigned to cost of removal is based on a detailed study of the tasks involved for replacement projects and a sample of specific projects and the associated costs and tasks.[54] Mr. Allis disputed Mr. Majoros's contention that the allocation is arbitrary, contending that the cost of removal allocations based on the studies are thorough and reasonable.[55] Further, Mr. Allis claimed that Mr. Majoros's calculations are incorrect because (1) his assumed 5% allocation factor understates costs of removal since it is applied to the original cost of the asset and (2) because the 5% allocation is based on the incremental method that excludes common costs and, therefore, understates costs of removal for retirement-only assets (retirements without replacements).[56]

Finally, Mr. Allis claimed that the alternatives Mr. Majoros proposes – such as excluding net salvage from depreciation rates and instead recovering those costs when expended, and discounting future net salvage costs to present value – are not widely accepted. Mr. Allis asserted

[52] *Id.* at 12-13.
[53] *Id.* at 13.
[54] *Id.* at 14.
[55] *Id.*
[56] *Id*. at 14-15.

that these methods lead to higher base rates than the traditional methods employed by the Company and would in turn lead to higher rates for customers in the long run.[57] Mr. Allis testified that the majority of regulatory jurisdictions utilize the traditional method, and that only three states (Maryland, New Jersey, and Pennsylvania) use Mr. Majoros's proposed alternative methods for net salvage value.[58] Finally, Mr. Allis maintained that the FERC also recently rejected the alternative approaches recommended by Mr. Majoros.[59]

THE HEARING

The hearing in this matter was noticed by the Commission on October 26, 2023, and held during the regularly scheduled Commission Conference on November 6, 2023. Appearances were made by the following:

> Atmos Energy Corporation. – Erik C. Lybeck Esq., 3322 West End Ave., Suite 200 Nashville, Tennessee 37203.
>
> Consumer Advocate Division – Vance Broemel, Esq., Consumer Advocate Division of the Office of the Tennessee Attorney General and Reporter, Post Office Box 20207, Nashville, Tennessee, 37219.

Mr. Allis presented testimony on behalf of the Company and Mr. Majoros testified on behalf of the Consumer Advocate. Prior to the hearing, the parties were authorized to submit post hearing briefs on November 22, 2023, in lieu of giving closing arguments at the hearing, and the parties anticipated the Commission would deliberate this matter in December of 2023.[60] During the hearing, members of the public were given an opportunity to offer comments, but no one sought recognition to do so.

[57] *Id.* at 15.
[58] *Id.*
[59] *Id.* at 16.
[60] *Pre-Hearing Order*, p. 3 (November 3, 2023).

POST-HEARING BRIEF OF THE CONSUMER ADVOCATE

In its Post-Hearing Brief, the Consumer Advocate contended that the Commission's authority allows it to consider, follow, or depart from accounting principles established by other entities. The Commission, therefore, has the same broad powers and discretion in this case to adopt a simplified method of accounting for cost of removal and is not bound by any self-imposed limitation on its ratemaking authority in general or in depreciation cases. The Commission may consider alternative methods or accounting principles that may result in just and reasonable rates.[61]

According to the Consumer Advocate, the recommendation to adopt Mr. Majoros's method of accounting for cost of removal does not require the Commission to depart from prior ratemaking policy or the USOA, and it does not require the Commission to disregard Commission Rule 1220-04-01-.11 that requires utilities to follow a uniform system of accounts. The Consumer Advocate asserted that while the rule requires the Company to keep its books in a certain manner, it does not bind the Commission in determining how depreciation rates should be computed to arrive at just and reasonable rates.[62]

The Consumer Advocate argued that its recommendation on the accounting for cost of removal comports with a more holistic reading of the USOA. The Consumer Advocate relied upon Definition 32.A, which states that replacements include "the construction and installation of gas plant in place of property retired, together with the removal of the property retired."[63] According to the Consumer Advocate, the Company's allocation of a percentage of costs associated with retirement-replacement assets to cost of removal is at odds with the USOA's definition of replacements.[64]

[61] Consumer Advocate Post-Hearing Brief, pp. 3-4 (November 22, 2023).
[62] *Id.* at 4-5.
[63] *Id.* at 7.
[64] *Id*. at 6-7.

The Consumer Advocate asserted it was in agreement with the Company that USOA Gas Plant Instruction 10.B.(2) is controlling but argued that the Company has misapplied the USOA in this case. Gas Plant Instruction 10.B.(2) states that when "a retirement is retired from gas plant, with or without replacement, the book cost thereof shall be credited to the gas plant account in which it is included …. The cost of removal and the salvage shall be charged or credited, as appropriate, to such depreciation account."[65] The Consumer Advocate argued that the phrase "as appropriate" denotes that there are projects where cost of removal should not be booked to the depreciation account. Thus, according to the Consumer Advocate, when Gas Plant Instruction 10.B.(2) is read in conjunction with Definition 32.A, the USOA supports its contention that it is not appropriate to place the cost of removal into the depreciation account for replacement assets, but that such costs should already be included with the cost of the replacement project.[66]

Finally, the Consumer Advocate argued that its recommendation to account for cost of removal as plant additions for replacement assets is more objective and, therefore, just and reasonable. According to the Consumer Advocate, the 5% allocation of replacement costs as incremental cost of removal is not an exact figure, but rather is based on estimates contained in the Alliance Studies. The Consumer Advocate claimed these Studies are opinions that may be well-informed and detailed, but which are nonetheless opinions that involve examination of many variable elements with opportunities for excessive allowances present.[67] Rather than using estimated cost of removal, the Consumer Advocate recommended waiting until the end of the life of the asset, when the cost to remove is known and objectively measurable, and book that cost of removal wholly to the new plant account. The Consumer Advocate contended that this simplified

[65] *Id.* at 7-8.
[66] *Id.*
[67] *Id.* at 8-9.

method is both more objective in the present when determining actual cost of removal, and in the future because looking at actual cost at the time of removal negates the risk of over or under depreciation of any particular asset group. The Consumer Advocate concluded that the Commission should not credit subjective opinions when an alternative method of employing objective standards is available and recommended.[68]

POST-HEARING BRIEF OF ATMOS

The Company asserted that it is conceptually appropriate to include cost of removal for replacement projects as part of depreciation expense; and it points out that the Consumer Advocate did not object to including cost of removal in depreciation as a general matter.[69] The Consumer Advocate objected only when cost of removal is incurred as part of retiring an asset that is being replaced with a new asset. Even when replacing an asset, however, there are still certain steps and associated costs that are only required to remove the existing asset from service. It is these "incremental costs" only incurred in connection with removing the old asset from service that would need to be incurred whether it is a retirement-only or a replacement project. Atmos argued there is no conceptual justification for treating incremental costs of removal for replacement projects any differently than the same costs incurred with a retirement-only project, as the Consumer Advocate proposes.[70]

According to Atmos, including cost of removal for replacement projects in depreciation is supported by the USOA, which the Company is required to follow under Commission Rule 1220-04-01-.11. Most significantly, the USOA's Gas Plant Instruction 10.B.(2) states:

> When a retirement unit is retired from gas plant, with or without replacement, the book cost thereof shall be credited to the gas plant account in which it is included, determined in the manner set forth in paragraph D, below. If the retirement unit is

[68] *Id.* at 9-10.
[69] Atmos Energy Corporation's Post-Hearing Brief, p. 2 (November 22, 2023).
[70] *Id.* at 3-4.

> of a depreciable class, the book cost of the unit retired and credited to gas plant shall be charged to the accumulated provision for depreciation applicable to such property. The cost of removal and salvage shall be charged or credited, as appropriate, to such depreciation account.

The Company argued that Gas Plant Instruction 10.B.(2) is clear that cost of removal should be included in depreciation, and there is no indication from the instruction that it does not apply to replacement projects. The instruction expressly states that this step is appropriate when a retirement occurs with or without replacement. The Company asserted that the Consumer Advocate's proposal is directly contrary to the express terms of the USOA.[71]

Atmos stated that inclusion of cost of removal for replacement projects in depreciation is consistent with the precedent of the Commission. The prior depreciation studies approved by the Commission for Atmos, as well as other companies, have included cost of removal for replacement projects. Atmos cited its previous depreciation study approved in Docket No. 15-00089, as well as the last depreciation studies of Piedmont Natural Gas Company in Docket No. 20-00086 and Chattanooga Gas Company in Docket No. 18-00017, as including cost of removal allocations in both replacement and retirement-only projects.[72] By contrast, the Consumer Advocate, according to the Company, has cited no precedents in support of its proposal, and instead relies only on USOA Definition 32.A and "common sense."[73]

Atmos contended, with respect to the Consumer Advocate's reliance on Definition 32.A, that the definition itself defines replacement as "when not otherwise indicated in context, means the construction or installation of gas plant in place of property retired, together with the removal of the property retired."[74] The Company argued that the separate listing of the (i) construction of

[71] *Id.* at 4-5.
[72] *Id.* at 6.
[73] *Id.* at 6-7.
[74] *Id.* at 7.

a new asset and (ii) the removal of the old asset in the definition supports different accounting treatments, rather than the same treatment as argued by the Consumer Advocate. Atmos also claimed the Consumer Advocate's reliance on the definitions section of the USOA rather than the instructions section does not provide any useful guidance. While the definitions section merely defines certain terms, it does not provide guidance on what to do with those terms. Rather, the guidance on how to apply the terms comes from the instructions section of the USOA. Those instructions, according to Atmos, direct utilities to record cost of removal to depreciation for all retirement projects, with or without replacement. The Company urged rejection of the Consumer Advocate's attempt to create a wholly novel approach to cost of removal accounting based on an implausible interpretation of a single definition, read in isolation of the rest of the USOA.[75]

Atmos claimed that the Consumer Advocate's contention that overall cost of removal has increased due to the Alliance Studies is incorrect. While the dollar amount of cost of removal has increased because of more money being spent on replacement activity, the incremental methodology adopted as a result of the Studies has decreased cost of removal as compared to what the costs would have been absent the Studies.[76] Although the 5% cost of removal ratio was criticized by the Consumer Advocate for being based on the estimates, the Consumer Advocate did not dispute that the estimates were based on the results of a detailed study, nor did the Consumer Advocate raise any objections to the methods used in the Depreciation Studies and Alliance Studies. Further, Mr. Majoros used the 5% figure in his own model.[77]

Finally, the Company asserted that the Consumer Advocate's proposed alternative is not workable because under its model, the cost of removal would only be recorded for retirement only

[75] *Id*. at 7-8.
[76] *Id.* at 9.
[77] *Id*. at 9-10.

projects and would result in an artificially low cost of removal. Thus, according to the Company, the Consumer Advocate's proposal should be rejected, even if the Commission disagrees with the Company's approach.[78]

FINDINGS & CONCLUSIONS

Based on the presentations of the parties, the arguments in the post-hearing briefs, and the evidentiary record in its entirety, the hearing panel voted unanimously to approve the annual depreciation rates proposed in the Depreciation Studies attached as exhibits to the Direct Testimony of Ned W. Allis and found such depreciation rates just and reasonable. Based on the evidence in this docket, the cost of removal for retirements of all depreciable assets, including retirements associated with asset replacements, should be accounted for as a charge to the accumulated depreciation reserve of the retired asset and should be incorporated into the calculation of depreciation rates in accordance with the methodologies proposed by Atmos in its Depreciation Studies. The hearing panel found that accounting for retirements in this manner is reasonable, complies with the definitions and requirements of the USOA, reflects previous Commission decisions, and does not infringe upon the matching principle of ratemaking or impose undue costs on future generations of ratepayers. Moreover, Atmos's treatment of retirements does not require the Commission to adopt a novel approach to depreciation for which there is little compelling precedent in other state jurisdictions.

Therefore, the hearing panel voted unanimously to adopt the proposed annual depreciation rates for Tennessee Direct Property set forth in Exhibit NWA-1, Part VI, page 4; approved the annual depreciation rates for Kentucky Mid-States General Office set forth in Exhibit NWA-2, Part VI, page 4; and approved the annual depreciation rates for Shared Services Unit set forth in

[78] *Id*. at 11.

Exhibit NWA-3, Appendix A. The Company was further directed to calculate depreciation expense using the newly approved rates in its subsequent Annual Rate Review Mechanism filings.

IT IS THEREFORE ORDERED THAT:

1. The *Notice of Filing of Depreciation Study and Request for Approval of New Depreciation Rates* filed by Atmos Energy Corporation on June 29, 2023, is APPROVED.

2. Any party aggrieved by the Commission's decision in this matter may file a Petition for Reconsideration with the Commission within fifteen (15) days from the date of this Order.

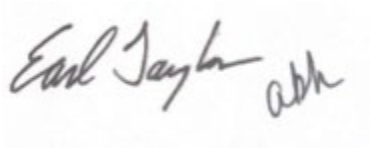
3. Any party aggrieved by the Commission's decision in this matter has the right to judicial review by filing a Petition for Review in the Tennessee Court of Appeals, Middle Section, within sixty (60) days from the date of this Order.

FOR THE TENNESSEE PUBLIC UTILITY COMMISSION:

Chairman Herbert H. Hilliard,
Commissioner Clay R. Good,
Commissioner David Crowell,
Commissioner Kenneth C. Hill, and
Commissioner John Hie concurring.

None dissenting.

ATTEST:



Earl R. Taylor, Executive Director