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April 27, 1999

Mr. David Waddell
Executive Secretary
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, TN 37243-0505

Re: Application of Nashville Gas Company, a Division of Piedmont Natural Gas Company, for Approval of Negotiated Gas Redelivery Agreement with State Industries
Application of Nashville Gas Company, a Division of Piedmont Natural Gas Company, for Approval of Negotiated Gas Redelivery Agreement with Bridgestone/Firestone
Docket Nos. 98-00338 and 98-00339

Dear Mr. Waddell:

I am enclosing for filing in the above captioned proceedings the original and fourteen copies of the following documents on behalf of Nashville Gas Company:

✓1. Brief of Nashville Gas Company on Inapplicability of Prohibitions on Retroactive Ratemaking in Docket Nos. 98-00338 and 98-00339;

2. Proposed Recommendation and Report of Hearing Officer in Docket Nos. 98-00388 and 98-00339;

3. Motion of Nashville Gas Company to Amend Application in Docket No. 98-00338; and

4. Motion of Nashville Gas Company to Amend Application in Docket No. 98-00339.

I am enclosing an additional copy of each document that I would appreciate your stamping "filed" and returning in the enclosed envelope.

Sincerely,

Jerry W. Amos

JWA:kam
Encl.

BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

IN RE:	)	
	)	
NASHVILLE GAS COMPANY APPLICATION FOR APPROVAL OF NEGOTIATED GAS REDELIVERY AGREEMENT WITH STATE INDUSTRIES	)	**DOCKET NO. 98-00338**
	)	
IN RE:	)	
	)	
NASHVILLE GAS COMPANY APPLICATION FOR APPROVAL OF NEGOTIATED GAS REDELIVERY AGREEMENT WITH BRIDGESTONE/FIRESTONE	)	**DOCKET NO. 98-00339**
	)	

BRIEF OF NASHVILLE GAS COMPANY ON INAPPLICABILITY OF PROHIBITIONS ON RETROACTIVE RATEMAKING

EXECUTIVE SUMMARY

This brief is filed by Nashville Gas Company ("Nashville Gas" or the "Company"). This brief addresses the question whether the Tennessee Regulatory Authority ("TRA") can approve a 90%/10% sharing of margin losses resulting from the negotiated agreements between Nashville Gas and Bridgestone/Firestone and between Nashville Gas and State Industries for the period January 1, 1998 (the effective date of the negotiated rates) to May 12, 1998 (the date when the written contracts were filed with the TRA for approval) without violating prohibitions against retroactive ratemaking. In this brief, we will show that the prohibition against retroactive ratemaking does not apply to the issue presently before the TRA in this consolidated proceeding. In this proceeding, the TRA will determine how margin losses should be shared. Since this sharing will take place at a future date, the TRA's decision will not retroactively adjust any rates. To the contrary, the sharing will be effected through prospective rates.

PROCEDURAL BACKGROUND

Effective January 1, 1998, Nashville Gas entered into oral agreements with State Industries and Bridgestone/Firestone to reduce their rates pending the completion and filing of written agreements with the TRA.[1] The written agreements were completed and filed with the TRA on May 12, 1998. On January 22, 1999, the TRA issued orders (1) approving the two written agreements, (2) ordering that margin losses during the period January 1, 1998 to August 1, 1998 be absorbed 100% by Nashville Gas, and (3) ordering that margin losses for periods subsequent to August 1, 1998 be shared 10% by Nashville Gas and 90% by customers.

On February 5, 1999, Nashville Gas requested a rehearing of the TRA's orders. The TRA granted rehearing by orders dated April 14, 1999. The two proceedings were consolidated for hearing on April 15, 1999. At the hearing, the testimony and exhibits of Nashville Gas witnesses Chuck W. Fleenor and Bill R. Morris were received into evidence.

Following the receipt of evidence, counsel for Nashville Gas proposed that the TRA resolve the various issues raised in Nashville Gas' request for rehearing by approving the two agreements to be effective January 1, 1998 and providing that all margin losses from January 1, 1998 be shared 10% by Nashville Gas and 90% by customers. In return, Nashville Gas would withdraw its objections to all issues. Counsel for Nashville Gas contended that this proposal would be fair to all parties and would avoid the various issues related to the applicability of Rate Schedule 9.

The Hearing Examiner requested counsel for Nashville Gas to file (1) a written motion to amend the previously filed petitions in the consolidated dockets and (2) a brief on the question of whether the TRA could grant the 90%/10% sharing for the period January 1, 1998 to May 12, 1998 without violating prohibitions against retroactive ratemaking.[2]

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[1] Nashville Gas notified the TRA of its intent to charge reduced rates by letter dated December 31, 1997.

[2] The written motion is being filed simultaneously with this brief.

ARGUMENT

The purpose of this brief is to address the retroactive ratemaking issues. In this brief, we will show that the prohibition against retroactive ratemaking is not applicable to the issues before the TRA in these dockets. The rates placed into effect for State Industries and Bridgestone/Firestone in this proceeding have not been questioned by any party. The only issue before the TRA in this proceeding is how the margin losses resulting from the lower rates will be shared between Nashville Gas and its customers. The customers' share of the margin losses will be recorded in Nashville Gas' Actual Cost Adjustment ("ACA") account and be recovered prospectively in future rates.

In American Association of Retired Persons v. Tennessee Public Service Commission, 896 S.W.2d 127 (1994) (Permission to Appeal Denied by Supreme Court, Feb. 27, 1995) ("Retired Persons"), the Tennessee Public Service Commission (TPSC) adopted rules that provided for the sharing of telephone company earnings in excess of a certain range between the telephone company and its customers. On appeal, the appellants contended that the sharing of past earnings resulted in retroactive ratemaking. The Court of Appeals for the Middle District of Tennessee disagreed. The Court held that since the sharing of past excess earnings would be effected through prospective rate reductions, rates would not be retroactively changed and, therefore, the prohibition against retroactive ratemaking was inapplicable.

In the instant case, the TRA is not being requested to effect the 90%/10% sharing of margin losses in a retroactive manner. As was the situation in Retired Persons, the sharing between the company and its customers will be effected in prospective rates. As a result, no rate is being adjusted retroactively. The only distinction between the Retired Persons case and the instant case is that in the first case the sharing was of earnings and in the second case the sharing is of losses. Since earnings and losses are simply the reciprocal of each other and are reported on the same line of the income statement, this is clearly a distinction without a difference.

It should be noted that the Company's share of the margin losses will be recovered through Nashville Gas' ACA. Under the ACA, Nashville Gas is permitted to increase (or decrease) future

rates to adjust for an under- or over-collection of gas costs under its Purchased Gas Adjustment (PGA), to adjust for an under- or over-collection of margin under its Weather Normalization Adjustment (WNA), and to adjust for an under- or over-collection of margin with respect to negotiated rates under Rate Schedule 9. In each of these cases, Nashville Gas recovers its past losses or refunds past gains through future rates. The same is true with respect to the margin losses at issue in this proceeding. Nashville Gas is simply seeking to recover its share of the margin losses resulting from the reduced contract rates with Bridgestone/Firestone and State Industries under the ACA. Many cases have held that recovery of costs under similar mechanisms does not result in unlawful retroactive ratemaking.[3]

Other jurisdictions have held that similar transactions do not constitute retroactive ratemaking. In Blackstone Valley Electric Co. v. Rhode Island Public Utilities Commission, 543 A.2d 253 (1988), the Supreme Court of Rhode Island held that a sharing between the utility and its customers of supplier refunds related to past expenses did not constitute retroactive ratemaking. Quoting from Roberts v. Narragansett Electric Co., 470 A.2d 215, 217 (R.I. 1984), the court noted that "[t]he specter of retroactive ratemaking must not be viewed as a talismanic inhibition against the application of principles based upon equity and common sense."

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[3] Many courts have held that orders requiring the refund of revenues overcollected through fuel adjustment charges or similar semi-automatic cost recovery mechanisms do not violate the ban against retroactive ratemaking or the filed rate doctrine. See MGTC, Inc. v. Public Service Comm'n of Wyoming, 735 P.2d 103 (Wyo. 1987) (refund of overcharges resulting from erroneous calculation of surcharge component of its gas balancing account held not to violate ban against retroactive ratemaking); Southern Calif. Edison Co. v. Pub. Util. Comm'n., 576 P.2d 945 (Cal.), appeal dismissed, 439 U.S. 905 (1978) (refund of revenues overcollected through fuel cost adjustment clause does not constitute retroactive ratemaking); Pub. Serv. Comm'n v. Delmarva Power & Light, 400 A.2d 1147 (Md. App. 1979) (refund of revenues overcollected through a fuel adjustment clause violated neither the prohibition against retroactive ratemaking nor the filed rate doctrine); Daily Advertiser v. Trans-La, 612 So.2d 7 (La. 1993) (refund of revenues overcollected through manipulation of fuel adjustment clause was not retroactive ratemaking and did not violate the filed rate doctrine).

The above quote is particularly applicable to the instant case. The Company negotiated lower rates in order to avoid the loss of two large industrial customers. In the absence of these negotiations, the customers would have been lost, and rates for other customers would have increased. Under these circumstances, principles of equity and common sense suggest that the Company should not bear the entire margin losses, and the TRA has already found that a sharing is appropriate with respect to the losses that have or will occur on and after August 1, 1998. Nashville Gas respectfully submits that the same principles of equity and common sense that led to the TRA's decision to permit a sharing of margin losses on and after August 1, 1998 apply equally to the margin losses that occurred prior to August 1, 1998, and that "the spector of retroactive ratemaking must not be viewed as a talismanic inhibition against the application" of these principles.

In Connecticut Natural Gas Corporation, 148 PUR 239 (Ct. DPUC, 1993), the Connecticut Department of Public Utility Control held that a requirement to share the cost savings resulting from a past change in property tax accounting procedures did not constitute unlawful retroactive ratemaking.

A sampling of other cases follows:

1. In Popowsky v. Pennsylvania Pub. Util. Comm'n, 695 A.2d 448 (1997), the Commonwealth Court of Pennsylvania held that the Pennsylvania Public Utility Commission did not engage in impermissible retroactive rate making when it permitted a utility to (1) charge current ratepayers for deferred prior period costs associated with a change in post-retirement benefits expense or (2) charge current ratepayers for deferred costs incurred ten years earlier for carrying charges and operation and maintenance expenses associated with a nuclear power plant. The Pennsylvania court found it particularly relevant that the costs at issue had been deferred and that they were extraordinary in nature.[4] The same is true in the instant case. The margin losses have been deferred on the

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[4] Other cases support the proposition that permitting the recovery of expenses/losses that are extraordinary does not constitute retroactive ratemaking. See, Porter v. (continued...)

Company's books, and the margin losses are extraordinary in nature. In fact, to the best of the Company's knowledge, there has been only one other instance in which margin losses were incurred to avoid bypass in the entire history of the Company.

2. In Greeley Gas Company, ___ PUR 4th ____ (CO. PUC, June 8, 1994), the Colorado Public Utilities Commission also held that the current recovery of previously deferred expenses does not constitute unlawful retroactive ratemaking. The Colorado Commission stated:

> "As for the Cities' suggestion that recovery of transition expenses constitutes unlawful retroactive ratemaking, we disagree. These expenses are the result of the change in accounting methodology for OPEBs. We find that current recovery of previously deferred expenses, as a consequence of changing accounting methods, is not the equivalent of recovery of past expenditures in current rates. Therefore, the Cities' contention is erroneous."[5]

3. In Public Advocate v. Maine Public Utilities Commission, 718 A.2d 201 (1998), the Supreme Judicial Court of Maine held that a rule that permitted telephone companies to defer the costs of expanding basic service calling areas for future collection through rates did not constitute unlawful retroactive ratemaking.

4. In Re Cambridge Electric Light Company, 164 PUR 4th 69 (MA. DPU, 1995), the Massachusetts Department of Public Utilities held that the recovery of stranded costs through a customer transition charge did not constitute unlawful retroactive ratemaking.

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[4] (...continued)
South Carolina Public Service Commission, 493 S.E.2d 92 (S.C. 1997) (recovery of unamortized portion of previously-approved rate case expense is unanticipated and non-recurring and qualifies as an extraordinary expense, and, therefore, does not constitute retroactive ratemaking); MCI Telecommunications Corp. v. Public Service Commission, (Utah 1992) (rule against retroactive ratemaking does not bar an adjustment in utility rates to take into account extraordinary earnings or overearnings).

[5] The holding of the Colorado Commission is particularly applicable to the instant case, since the costs in question in the instant case, like the costs in the Colorado case, have been previously deferred awaiting a decision by the appropriate regulatory authority.

5. In U.S. West Communications, Inc., ___ PUR 4th ___ (OR. PUC, May 3, 1996), the Oregon Public Utility Commission held that adopting depreciation rates to be effective at a past date did not amount to retroactive ratemaking because no adjustments to customer rates (related to the depreciation rates) would be made until a future date.

Nashville Gas respectfully submits that it was always the intent of all parties that Nashville Gas set its industrial rates as high as reasonably appropriate with the expectation that Nashville Gas may have to negotiate lower rates (either under Rate Schedule 9 or in special contracts) to avoid losing these customers. It was also recognized that this procedure would cause Nashville Gas' shareholders to earn less than their allowed return unless Nashville Gas was permitted to recover these margin losses. Under such circumstances, permitting Nashville Gas to recover 90% of these margin losses in accordance with these previously established policies does not violate prohibitions against retroactive ratemaking and is fair to all parties.

CONCLUSION

When the TRA established rates for Nashville Gas in its last general rate case, it was assumed that Nashville Gas would recover 100% of the margin earned on deliveries to Bridgestone/Firestone and State Industries. As a result, rates to Nashville Gas' captive residential customers and Nashville Gas' earnings from these customers were lower than they otherwise would have been. During the period January 1, 1998 through July 31, 1998, these two customers purchased 8,076,315 therms of gas. If billed at full margin, Nashville Gas would have collected $308,348.32. Under the negotiated rates, Nashville Gas collected only $192,815.02 – a margin loss of $115,533.30. Under Nashville Gas' settlement proposal, Nashville Gas' shareholders will absorb $11,223.33 of this loss. Although the remainder will be collected from Nashville Gas' other customers, those customers will still pay rates that are $204,038.35 ($308,348.32 margin contribution less $104,309.97 of margin loss recovery) lower than they would have paid had Nashville Gas not negotiated lower rates. In addition, Nashville Gas' shareholders will continue to absorb 10% of the margin losses on a prospective basis until Nashville Gas' next general rate case.

If Nashville Gas were not permitted to recover any portion of the margin losses for the period January 1, 1998 through May 11, 1998, Nashville Gas' shareholders would absorb $115,533.30 of margin losses through July 31, 1998 and 10% of all prospective margin losses until Nashville Gas' next general rate case. Nashville Gas respectfully submits that such a result would clearly be unfair and unjust, and, to quote the Supreme Court of Rhode Island, "the spector of retroactive ratemaking must not be viewed as a talismanic inhibition against the application principles based upon equity and common sense."

For the reasons set forth above, Nashville Gas respectfully submits that the TRA can permit Nashville Gas to recover 90% of its margin losses for the period January 1, 1998 through May 11, 1998 without violating the prohibition against retroactive ratemaking. Nashville Gas respectfully submits that approval of the proposed settlement will result in fair and reasonable rates to all concerned.

Respectfully submitted, this the 27th day of April, 1999.

Nashville Gas Company, a Division
Of Piedmont Natural Gas Company, Inc.

By: _____
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