BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

October 13, 1999

IN RE:	)
	)
NASHVILLE GAS COMPANY	**) Docket No. 99-00076**
ACTUAL COST ADJUSTMENT (ACA) AUDIT	)

NOTICE OF FILING BY ENERGY AND WATER DIVISION OF THE TENNESSEE REGULATORY AUTHORITY

Pursuant to Tenn. Code Ann. §§ 65-4-104, 65-4-111 and 65-3-108, the Energy and Water Division of the Tennessee Regulatory Authority hereby gives notice of its filing of the Compliance Audit Report of the Actual Cost Adjustment (hereafter "ACA") Component of the Purchased Gas Adjustment Rule for Nashville Gas Company in this docket and would respectfully state as follows:

1. The present docket was opened by the Authority to hear matters arising out of the audit of Nashville Gas Company (the "Company").

2. The Company's ACA filing was received on February 4, 1999, and the Staff completed its audit of same on October 8, 1999.

3. On October 11, 1999, the Energy and Water Division issued its preliminary ACA audit findings to the Company, and on October 12, 1999, the Company responded thereto.

FILE

4. The preliminary ACA audit report was modified to reflect the Company's responses and a final ACA audit report (the "Report") resulted therefrom. The Report is attached hereto as Exhibit A and is fully incorporated herein by this reference. The Report contains the audit findings of the Energy and Water Division, the Company's responses thereto and the recommendations of the Energy and Water Division in connection therewith.

5. The Energy and Water Division hereby files its Report with the Tennessee Regulatory Authority for deposit as a public record and approval of the recommendations and findings contained therein.

Respectfully Submitted:

Pat Murphy
Energy and Water Division of the
Tennessee Regulatory Authority

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CERTIFICATE OF SERVICE

I hereby certify that on this 13th day of October, 1999, a true and exact copy of the foregoing has been either hand-delivered or delivered via U.S. Mail, postage pre-paid, to the following persons:

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

Mr. Bill R. Morris
Director-Rates
Piedmont Natural Gas Company
P.O. Box 33068
Charlotte, NC 28233

Ms. Ann Boggs
Assistant Director - Rates
Piedmont Natural Gas Company
P.O. Box 33068
Charlotte, NC 28233

Pat Murphy
Pat Murphy

COMPLIANCE AUDIT REPORT

OF

<u>NASHVILLE GAS COMPANY</u>

<u>ACTUAL COST ADJUSTMENT</u>

PREPARED BY

<u>TENNESSEE REGULATORY AUTHORITY</u>

ENERGY AND WATER DIVISION

OCTOBER, 1999

EXHIBIT

A

COMPLIANCE AUDIT

NASHVILLE GAS COMPANY

ACTUAL COST ADJUSTMENT

TABLE OF CONTENTS

I. <u>JURISDICTION AND POWER OF THE TENNESSEE REGULATORY AUTHORITY</u>

Tennessee Code Annotated (T.C.A.) §65-4-104 gave jurisdiction and control over public utilities to the Tennessee Public Service Commission. By virtue of Chapter 305 of the Public Acts of 1995, jurisdiction and control over public utilities was transferred from the Tennessee Public Service Commission to the Tennessee Regulatory Authority (the "TRA" or "Authority") on July 01, 1996. T.C.A. §65-4-104 states that:

> The Authority shall have general supervision and regulation of, jurisdiction, and control over, all public utilities...

T.C.A states further in §65-4-111 that the public utilities are to maintain a Uniform System of Accounts:

> The Authority shall have the power after hearing, upon notice, by order in writing to require every public utility... to keep its books, records, and accounts so as to afford an intelligent understanding of the conduct of its business, and to that end to require every public utility of the same class to adopt a uniform system of accounting. Such system shall conform, where applicable to any system adopted or approved by the Interstate Commerce Commission of the United States. And to furnish annually, or at other times as the Authority may require, a detailed report of finances and operations as shown by said system of accounts.

The TRA responded to T.C.A. §65-4-111 by establishing its own rule 1220-4-1-1.11 regarding the uniform system of accounts which public utilities should maintain. The TRA's rule provides:

> The following uniform system of accounting will be followed by utilities and other companies making periodic reports to the Authority:
>
> 1. For Classes A and B gas companies - Uniform System of Accounts as adopted by the National Association of Regulatory Utility Commissioners as revised June 30, 1972, and any amendments or revisions pertaining thereto.

The TRA received its authority to examine the books and records of public utilities from T.C.A. §65-4-105 which states that the TRA would possess all the other powers conferred on the TRA. T.C.A. §65-3-108 gives the TRA:

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

II. PURPOSE OF COMPLIANCE AUDITS

The two basic reasons for compliance audits are to assure compliance with the Uniform System of Accounts (USOA) and to assure that the utility is following all rules, regulations and directives adopted by the TRA.

Compliance audits provide the foundation of assurance underlying the basic objective of regulatory accounting, which is to provide a uniform method of recording transactions among similar companies. This uniform record keeping is accomplished through the adoption of the USOA and insures the integrity, reliability, and comparability of the financial data contained in financial reports filed with the TRA, which provides the TRA with one of its most useful regulatory tools for establishing just and reasonable rates.

III. DESCRIPTION OF PURCHASED GAS ADJUSTMENT (PGA) RULE

The Tennessee Regulatory Authority issued an Order in Docket No. G-86-1, which adopted a new PGA rule beginning July 1, 1992. The PGA Rider is intended to permit the Company to recover, in a timely fashion, the total cost of gas purchased for delivery to its customers and to assure that the Company does not overcollect or undercollect gas costs from its customers. This PGA consists of three major components:

1) **The Actual Cost Adjustment (ACA)**
2: **The Gas Charge Adjustment (GCA)**
3) **The Refund Adjustment (RA)**

The ACA is the difference between the revenues billed customers by means of the GCA and the cost of gas invoiced the Company by suppliers plus margin loss (if allowed by order of the TRA in another docket) as reflected in the Deferred Gas Cost account. The ACA then "trues-up" the difference between the actual gas costs and the gas costs recovered from the customer through a surcharge or a refund. The RA refunds the "true-up" along with other supplier refunds.

For a more complete definition of the GCA and RA, please see the PGA Formula in Appendix A.

IV. AUDIT TEAM

The TRA's Energy and Water Division is responsible for conducting ACA audits. This audit was conducted by Pat Murphy of the Energy and Water Division.

V. OBJECTIVE AND SCOPE OF AUDIT

The order for Docket G-86-1 required that the Company

> each year...shall file with the Authority an annual report reflecting the transactions in the Deferred Gas Cost Account. Unless the Authority provides written notification to the Company within one hundred eighty (180) days from the date of filing the report, the Deferred Gas Cost Adjustment Account shall be deemed in compliance with the provisions of this Rule...

The objective of this audit was to determine that Purchased Gas Adjustments, which are encompassed by the ACA and were described earlier, approved by the TRA during the period from January 1, 1998, to December 31, 1998, had been calculated correctly and were supported by appropriate source documentation.

To accomplish this task, the Staff conducted in-house audit work during which the Company's calculations of gas costs incurred and gas costs recovered were tested.

The Staff also audited a sample of customer bills to determine if the proper PGA rates were being applied in the Company's calculation of the customers' bills. Since the Company's billing process is computerized, the Staff decided to test a sample of 68 bills. These bills were selected to be representative of the residential, commercial, industrial and interruptible customers in each of the Company's service areas. The sample was selected from all twelve months of the audit period. After recalculating each sample bill, the Staff was in agreement with the Company's calculations in deriving the amount on each bill. Therefore, the Staff contends that, as a result of this sample, the Company is correctly calculating its bills to all customers.

The Staff's last ACA audit of Nashville Gas Company was conducted in 1998 covering the period from January 1, 1997, to December 31, 1997.

VI. BACKGROUND INFORMATION ON COMPANY AND GAS SUPPLIERS

Nashville Gas Company (NGC or Company), with headquarters at 665 Mainstream Drive, Nashville, Tennessee, is a division of Piedmont Natural Gas Company, which has its headquarters at 1915 Rexford Road, Charlotte, North Carolina. NGC is a gas distributor which provides service to several communities in the Middle Tennessee area. The natural gas used to serve these areas is purchased from three natural gas pipelines in accordance with separate and individual tariffs approved by the Federal Energy Regulatory Commission (FERC). The three interstate pipelines are Tennessee Gas Pipeline (TGP), Columbia Gas Transmission Corporation (CGTC), and Texas Eastern Gas Pipeline (TETCO).

TGP and CGTC provide service to the city of Nashville, and the towns of White House, Greenbrier, and Fairview, and the surrounding areas. TETCO provides service to the Hartsville, Tennessee area.

VII. ACA FINDINGS

The Company submitted its annual ACA filing on February 4, 1999. The filing reflected an **overcollection** of gas costs from Tennessee customers of **$7,090,698**. The Company began refunding this overcollection to its customers on March 1, 1999.

The Staff's audit resulted in a **net reduction of this overcollection** in the ACA account of **$356,727**. A list of the exceptions noted is summarized below.

SUMMARY:

FINDING #1	Bear Creek Inventory		no effect
FINDING #2	Bear Creek Inventory	$ 1,037.25	underrecovery
FINDING #3	Bear Creek Inventory	90.00	overrecovery
FINDING #4	Negotiated Loss	31,065.34	overrecovery
FINDING #5	Negotiated Loss	24,645.37	overrecovery
FINDING #6	Negotiated Gain	2,908.27	overrecovery
FINDING #7	ACA Surcharges	100.84	overrecovery
FINDING #8	Commodity Recovery	105.45	overrecovery
FINDING #9	Demand Recovery	417,207.91	underrecovery
FINDING #10	Interest Expense – Commodity	4,080.10	overrecovery
FINDING #11	Interest Expense - Demand	1,477.61	underrecovery
	Net Result	**$356,727.40**	**underrecovery**

FINDING #1:

Exception

On the Bear Creek inventory schedule, the withdrawal charge was understated for December 1998.

Discussion

The Company understated the withdrawal charge by $20 on its inventory schedule. The withdrawal charge is used in the calculation of the withdrawal rate, but has **no effect** on the ACA account.

Company Response

The Company agrees with this finding.

FINDING #2:

Exception

The Staff calculated a **$1,037.25 underrecovery** in the April 1998 Bear Creek inventory injections.

Discussion

The injection volumes for April, 1998 were overstated. The Company used 125,940 DKT, instead of 125,490 DKT as shown on the supplier invoice. The Company states this was a transposition error in data entry. The difference of 450 dekatherms times the injection rate of $2.3050 produces an underrecovery of $1,037.25 in the ACA account.

Company Response

The Company agrees with this finding.

FINDING #3:

Exception

The Staff calculated an **overrecovery of $90.00** in the June 1998 Bear Creek inventory injections.

Discussion

The Company incorrectly posted the June, 1998 injections to the ACA account. $114,324.28 in injections was recorded as $114,234.283. This transposition error led to the $90.00 overrecovery.

Company Response

The Company agrees with this finding.

FINDING #4:

Exception

The Staff calculated an **overrecovery of $31,065.34** in the negotiated loss activity for the Bridgestone Tire special contract.

Discussion

Effective January 1, 1998, Nashville Gas began offering reduced rates to Bridgestone Tire under its Rate Schedule 9. On May 12, 1998, Nashville Gas filed a petition with the TRA requesting approval of a special contract, to become effective on the first day of the month following approval of the contract by the TRA. The Company requested permission to recover 100% of any lost margin related to the agreement from January 1, 1998.

In its January 22, 1999 Order, the TRA approved the contract effective August 1, 1998. All margin losses incurred from January 1, 1998 to July 31, 1998 were to be absorbed by Nashville Gas; and, all margin losses after August 1, 1998 would be shared by the ratepayers (90%) and the Company (10%).

On February 5, 1999, Nashville Gas requested a rehearing. A rehearing was granted on April 6, 1999 and was heard on April 15, 1999. The Hearing Officer's decision was memorialized in his July 6, 1999 Initial Order. That Order permitted the Company to recover 90% of its margin losses from May 12, 1998 to July 31, 1998. It also reaffirmed the January 22, 1999 order with respect to margin losses after August 1, 1998. The Chairman filed a motion for review of the Initial Order. The motion was denied at the Authority's July 13, 1999 Directors Conference.

Based upon the July 6, 1999 Order referred to above, Staff has recalculated the margin losses that were charged to the ACA account for the audit period January through December, 1998. The Company correctly booked 90% of its losses for the months July through December. However, the Staff made adjustments to the amounts booked for January through June.

Company Response

The adjustment calculations made are based on an Order of the Authority issued in August 1999. The Company had made adjustments based on the Orders issued during 1999 to ACA period totaling $42,939.39. We agree with the calculations made based on the final Order and will record the difference ($15,699.59) in the ACA account.

FINDING #5:

Exception

The Staff calculated an **overrecovery of $24,645.37** in the negotiated loss activity for the State Industries special contract.

Discussion

Effective January 1, 1998, Nashville Gas began offering reduced rates to State Industries under its Rate Schedule 9. On May 12, 1998, Nashville Gas filed a petition with the TRA requesting approval of a special contract, to become effective on the first day of the month following approval of the contract by the TRA. The Company stated it had been recovering its lost margin and requested it be allowed to continue to recover the margin loss associated with the contract.

In its January 22, 1999 Order, the TRA approved the contract effective August 1, 1998. All margin losses incurred from January 1, 1998 to July 31, 1998 were to be borne by Nashville Gas; and, all margin losses after August 1, 1998 would be shared by the ratepayers (90%) and the Company (10%).

On February 5, 1999, Nashville Gas requested a rehearing. A rehearing was granted on April 6, 1999 and was heard on April 15, 1999. The Hearing Officer's decision was memorialized in his July 6, 1999 Initial Order. That Order permitted the Company to recover 90% of its margin losses from May 12, 1998 to July 31, 1998. It also reaffirmed the January 22, 1999 Order with respect to margin losses after August 1, 1998. The Chairman filed a motion for review of the Initial Order. The motion was denied at the Authority's July 13, 1999 Directors Conference.

Based upon the July 6, 1999 Order referred to above, Staff has recalculated the margin losses that were charged to the ACA account for the audit period January through December, 1998. The Company correctly booked 90% of its losses for the months July through December. However, the Staff made adjustments to the amounts booked for January through June.

Company Response

The adjustment calculations made are based on an Order of the Authority issued in August 1999. The Company had made adjustments based on the Orders issued during 1999 to ACA period totaling $42,939.39. We agree with the calculations made based on the final Order and will record the difference ($15,699.59) in the ACA account.

FINDING #6:

Exception

The Staff calculated an **overrecovery of $2,908.27** in the negotiated gain activity for the Ford Motor Company special contract.

Discussion

On February 26, 1998, Nashville Gas Company petitioned the TRA for approval of a negotiated gas redelivery agreement with Ford Motor Company. Nashville Gas had been providing transportation services for Ford under a five-year agreement that was to expire on February 28, 1998. The request was for approval of an "extension" agreement for an additional period to begin March 1, 1998 and end October 31, 2000.

New terms related to the "extension" agreement provided for rates that are higher than the current rates that were approved for Ford in Nashville Gas' most recent rate case. The TRA Order dated March 12, 1999 ordered that the terms of the "extension" agreement were approved and that "Nashville Gas will credit its ratepayers with one hundred percent (100%) of the difference between the Ford rates as negotiated in the Extension Agreement and the current tariff rates approved by the Authority".

Based upon the March 12, 1999 Order referred to above, Staff has recalculated the negotiated gain amounts that were credited to the ACA account for the audit period January through December, 1998. The Company correctly credited 100% of the gains for the months March through June. However, the Company credited 90% of the gains for July through December. The Staff made adjustments to the ACA account to credit the 10% additional amount.

Company Response

The adjustment calculations made are based on an Order of the Authority issued in August 1999. The Company had made adjustments based on the Orders issued during 1999 to ACA period totaling $42,939.39. We agree with the calculations made based on the final Order and will record the difference ($15,699.59) in the ACA account.

FINDING #7:

Exception

The Staff calculated an **overrecovery of $100.84** in the October, 1998 commodity ACA surcharge.

Discussion

The ACA surcharge amounts for rate class 4 and the Town of Smyrna were understated. For rate class 4, sales volumes were understated by 400 therms. For the Town of Smyrna, the Company used an incorrect surcharge rate.

Company Response

The Company agrees with this finding.

FINDING #8:

Exception

The Staff calculated a **$105.45 overrecovery** in the commodity gas cost recoveries for October 1998.

Discussion

The recoveries for rate class 4 were understated. The sales volumes were understated by 400 therms.

Company Response

The Company agrees with this finding.

FINDING #9:

Exception

The Staff calculated a **$417,207.91 underrecovery** in the demand recoveries for December 1998.

Discussion

The Company included Order 636 transition costs in the demand recoveries for December.

Company Response

The adjustment of the $417,207.91 out of the ACA as of December 1998 is correct and we agree with the Staff's removal. The recovery was posted to the 186.56 transition cost account to calculate the point of recovery and removal of those amounts from the billing factors in August 1999 and the transfer of the balance into the ACA.

FINDING #10:

Exception

The Staff calculated an **overrecovery of $4,080.10** in the interest expense for the commodity portion of the ACA.

Discussion

The Staff recalculated the interest expense based upon Findings #2 through #8 above.

Company Response

The Company agrees with this finding.

FINDING #11:

Exception

The Staff calculated an **underrecovery of $1,477.61** in the interest expense for the demand portion of the ACA.

Discussion

The Staff recalculated the interest expense based upon Finding #9 above.

Company Response

The Company agrees with this finding.

VIII. CONCLUSIONS AND RECOMMENDATIONS

The Company incurred approximately $62.4 million in total gas costs for the ACA period under audit. The audit exceptions totaled $419,722.77 in underrecoveries and $62,995.37 in overrecoveries for a net underrecovery of $356,727.40. The **net $356,727 underrecovery** calculated by the Staff is less than one percent (1%) of the total gas purchases and is not considered material in comparison. Except for the above findings, the Purchased Gas Adjustment mechanism as calculated in the Actual Cost Adjustment appears to be working properly and in accordance with the TRA rules. Ordinarily the Staff recommends that any over or underrecovery be placed in the Refund Due Customers account. Nashville Gas Company customarily adjusts the Deferred Gas account in the subsequent audit period. The Staff concurs with this method.

APPENDIX A

PGA FORMULA

The computation of the GCA can be broken down into the following formulas:

$$\text{Firm GCA} = \frac{D + DACA}{SF} - DB + \frac{P + T + SR + CACA}{ST} - CB$$

$$\text{Non-Firm GCA} = \frac{P + T + SR\ CACA}{ST} - CB$$

where

GCA	=	The Gas Charge Adjustment in dollars per Ccf/Therm, rounded to no more than five decimal places.
D	=	The sum of all fixed Gas Costs.
DACA	=	The demand portion of the ACA.
P	=	The sum of all commodity/gas charges.
T	=	The sum of all transportation charges.
SR	=	The sum of all FERC approved surcharges.
CACA	=	The commodity portion of the ACA.
DB	=	The per unit rate of demand costs or other fixed charges included in base rates in the most recently completed general rate case (which may be zero if the Company so elects and the Commission so approves).
CB	=	The per unit rate of variable gas costs included in base rates in the most recently completed general rate case (which may be zero if the Company so elects and the Commission so approves).
SF	=	Firm Sales.
ST	=	Total Sales.

The computation of the RA can be computed using the following formulas:

$$\text{Firm RA} = \frac{DR1 - DR2}{SFR} + \frac{CR1 - CR2 + CR3 + i}{STR}$$

$$\text{Non-Firm RA} = \frac{CR1 - CR2 + CR3 + i}{STR}$$

where

RA	=	The Refund Adjustment in dollars per Ccf/Therm, rounded to no more than five decimal places.
DR1	=	Demand refund not included in a currently effective Refund Adjustment, and received from suppliers by check, wire transfer, or credit memo.
DR2	=	A demand surcharge from a supplier not includable in the GCA, and not included in a currently effective Refund Adjustment.
CR1	=	Commodity refund not included in a currently effective Refund Adjustment, and received from suppliers by check, wire transfer, or credit memo.
CR2	=	A commodity surcharge from a supplier not includable in the GCA, and not included in a currently effective Refund Adjustment.
CR3	=	The residual balance of an expired Refund Adjustment.

i = Interest on the "Refund Due Customers" account, using the average monthly balances based on the beginning and ending monthly balances. The interest rates for each calendar quarter used to compute such interest shall be the arithmetic mean (to the nearest one-hundredth of one percent) of the prime rate value published in the "Federal Reserve Bulletin" or in the Federal Reserve's "Selected Interest Rates" for the 4th, 3rd, and 2nd months preceding the 1st month of the calendar quarter.

SFR = Firm sales as defined in the GCA computation, less sales under a transportation or negotiated rate schedule.

STR = Total sales as defined in the GCA computation, less sales under a transportation or negotiated rate schedule.